



Other relevant regulatory matters

20 September 2010

 **ERNST & YOUNG**
Quality In Everything We Do

Agenda

- ▶ Fund solvency concept
- ▶ Management of participating fund
- ▶ Restrictions on use of derivatives for investment of insurance fund assets
- ▶ Risk management guidelines
- ▶ Market conduct
- ▶ Prevention of money laundering/countering the financing of terrorism
- ▶ Product development and pricing
- ▶ Valuation of policy liabilities of life business
- ▶ Appointment of Principal Officers and Directors –
“Fit and proper person” rules
- ▶ Financial reinsurance
- ▶ Other relevant MAS directives, notices, guidelines and consultation papers
- ▶ IFRS developments

Fund solvency concept



Fund solvency concept

- ▶ Solvency requirements of Singapore insurers are governed by the Singapore Insurance Act (Cap.142) and its subsidiary legislation, Insurance (Valuation and Capital) Regulations

- ▶ Two levels of solvency
 - ▶ Fund level
 - ▶ Company level

Fund solvency requirement (FSR)

At all times,

- ▶ **Financial resources** (FR) of the insurance fund are not less than the **total risk requirement** (TRR) of the fund
i.e., $FR \geq TRR$ at all times

Definition of financial resources – for an insurance fund

Participating fund

- ▶ Balance in the surplus account

Plus

- ▶ Allowance for provision for non-guaranteed benefits

Less

- ▶ Reinsurance adjustment
- ▶ Financial resource adjustment

Other insurance fund

- ▶ Surplus of assets of fund over its liabilities

Less

- ▶ Reinsurance adjustment
- ▶ Financial resource adjustment

Total risk requirement (TRR)

- ▶ Sum of
 - ▶ C1 insurance risks; liability risk component
 - ▶ C2 investment risks; asset and mismatching risk component
 - ▶ C3 concentration risks

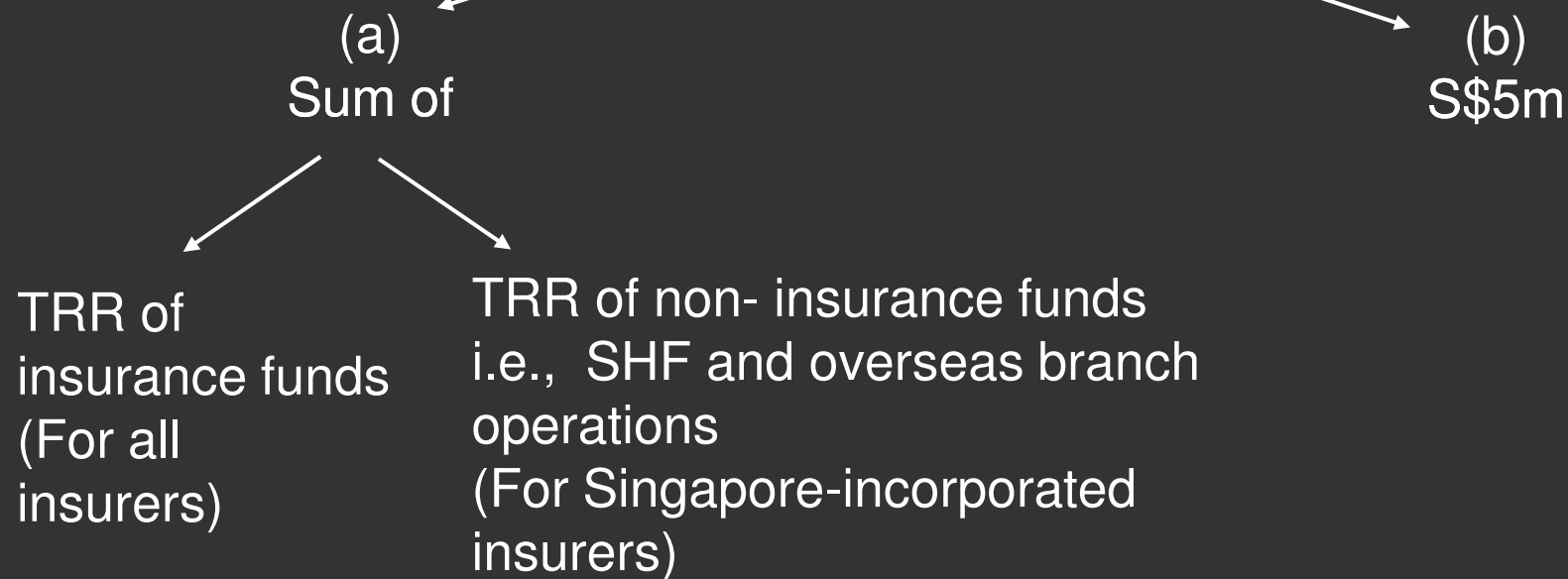
- ▶ Excludes
 - ▶ Unit reserves of the investment-linked fund
 - ▶ For reinsurers incorporated outside Singapore, offshore funds
 - ▶ For Singapore-incorporated reinsurers, C2 and C3 requirements arising from:
 - ▶ Offshore funds
 - ▶ Assets and liabilities of branches outside Singapore

Capital adequacy requirement

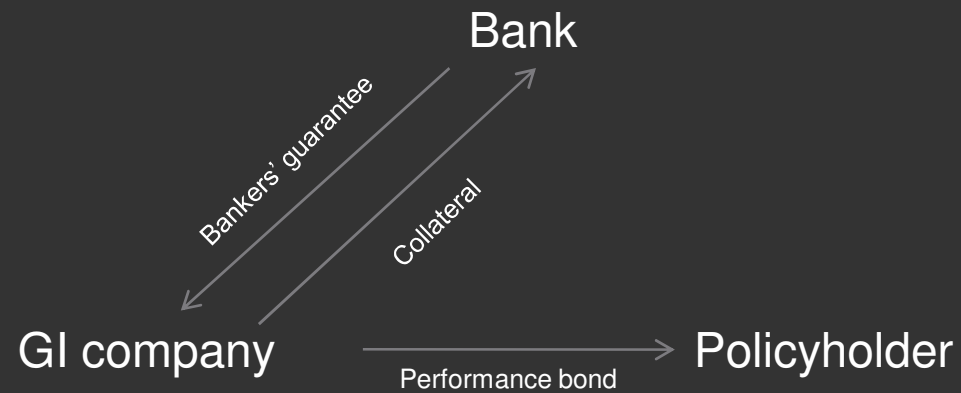
Capital adequacy requirement (CAR) of registered insurer

At company level

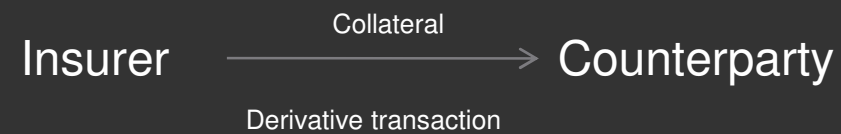
FR \geq
the higher of



Slide 11 – FRA clarification



Slide 12 – FRA clarification



Regulatory update – Clarification on Financial resource adjustment (FRA) *(ID17/09)*

- ▶ Key changes w.e.f 1 April 2010 – FRA should include:
 - ▶ All deposits placed with a related corporation or head office (e.g., unsecured demand, fixed, savings and other deposits regardless of currency)
 - ▶ Exception: Deposits with related entities that are banks licensed in Singapore will only be included in FRA after the expiry of the deposit guarantee provided by the government (i.e., 31 December 2010)
 - ▶ Unsecured loans or guarantees granted by the insurer to a related corporation or head office
 - ▶ Holdings by an insurer of unsecured bonds issued by a related corporation or head office
 - ▶ Amounts due and owing from uncollateralized derivative contracts, where the counterparty is a related company or head office

Regulatory update – Clarification on financial resource adjustment (FRA) *(ID17/09)*

- ▶ Key changes when revised regulations came into effect (second half of 2010) – FRA should include:
 - ▶ Equity investment held by insurer in a related corporation
 - ▶ Only the amount of charged asset that is equivalent to the amount of the credit facility that has been drawn down
 - ▶ E.g., charged asset = S\$1,000; drawn down credit facility = S\$700.
Therefore, FRA = S\$700
 - ▶ Any asset lodged by the insurer with a third party, for which the insurer cannot use for any other purpose
 - ▶ E.g., rental deposit

Regulatory update – Clarification on financial resource adjustment (FRA) *(ID17/09)*

- ▶ Key changes when revised regulations came into effect (second half of 2010) (continued) – FRA should include:
 - ▶ Charged asset to secure banker's guarantee facility, which facilitates the insurer to write certain insurance business. FRA only includes the amount of charged asset equivalent to the amount of policy liabilities incurred as a result of the insurance contract written
 - ▶ Note: Policy liabilities determined at gross of any reinsurance
 - ▶ E.g., An insurer underwrites a performance bond policy
Insurer sought banker's guarantee facility by placing S\$1,000 of charged asset. Gross claims reported to-date on that policy is estimated to be S\$400
Therefore, FRA = S\$400

Regulatory update – Clarification on financial resource adjustment (FRA) *(ID17/09)*

- ▶ Key changes when revised regulations came into effect (second half of 2010) (continued) – FRA should include:
 - ▶ Collateral in respect of a derivative transaction, regardless of whether the insurer has calculated a derivative counterparty risk requirement. FRA only includes the amount of charged asset equivalent to the amount of the financial liability incurred as a result of the derivative transaction.
 - ▶ E.g., An insurer enters into a derivative contract with a counterparty
 - ▶ To mitigate its exposure to the insurer's credit risk, the counterparty demanded a charge over the insurer's asset amounting to S\$1,000. At reporting date, the market value of the derivative contract (measured in the insurer's books) is – S\$750 (i.e., recognized as a derivative liability)
Therefore, FRA = S\$750

Regulatory update – Clarification on financial resource adjustment (FRA) *(ID17/09)*

- ▶ Proposed amendments – FRA should include:
 - ▶ Unsecured amounts owed > 30 days by a related party and arising from an insurance contract:
 - ▶ Outstanding premiums (net of gross policy liabilities)
 - ▶ Gross policy liabilities = premium liabilities + claims liabilities, gross of reinsurance
 - ▶ Reinsurance recoverables on paid claims
 - ▶ All other amounts not included in FRA will continue to be subjected to the same risk charges as those unsecured amounts owed by an unrelated party

Management of participating fund



Management of participating fund

- ▶ Regulatory requirements: MAS 320 *Management of participating life insurance business*
 - ▶ An insurer which has established or will be establishing a participating fund shall put in place an internal governance policy on the management of its participating life insurance business
 - ▶ The insurer shall ensure that:
 - ▶ The internal governance policy is approved by its Board of Directors
 - ▶ The internal governance policy is reviewed annually by its Board of Directors to ensure that the internal governance policy remains appropriate
 - ▶ The participating fund is managed according to the rules and guiding principles set out in the internal governance policy

Management of participating fund

- ▶ Regulatory requirements: MAS 320 *Management of participating life insurance business (continued)*
 - ▶ Information to be contained in the internal governance policy
 - ▶ Introduction
 - ▶ Bonus determination
 - ▶ Investment of participating fund assets
 - ▶ Risk management
 - ▶ Charges and expenses
 - ▶ Circumstances under which to cease taking new business
 - ▶ Shareholders' profits and responsibilities
 - ▶ Disclosure requirements

Restrictions on use of derivatives for investment of insurance fund assets



Restrictions on use of derivatives for investment of insurance fund assets

- ▶ Regulatory requirements: MAS 104 *Use of derivatives for investment of insurance fund assets*
 - ▶ Prudent management oversight
 - ▶ Implement adequate controls in respect of derivative transactions
 - ▶ Implement and maintain adequate risk management systems
 - ▶ Permitted derivatives activities
 - ▶ Hedging
 - ▶ Efficient portfolio management
 - ▶ Contravention of any requirement imposed under this Notice shall be an offence and shall attract the penalty

Risk management guidelines



Risk management guidelines

- ▶ MAS guidelines on risk management practices
 - ▶ Objective and scope
 - ▶ Aim to provide financial institutions supervised by MAS with guidance on sound risk management practices
 - ▶ Covers credit risk, market risk, internal controls and the role of an institution's Board of Directors and senior management

Risk management guidelines

- ▶ MAS guidelines on risk management practices (continued)
 - ▶ Four cornerstones of effective risk management and sound internal controls
 - ▶ The role of the Board in its oversight of risk management policies and their implementation
 - ▶ The role of senior management in ensuring that sound policies, effective procedures and robust systems are in place
 - ▶ The presence of sound risk management processes and operating procedures that integrate prudent risk limits with appropriate risk measurement, monitoring and reporting
 - ▶ The presence of competent personnel in the risk management, control and audit functions

Risk management guidelines

- ▶ MAS guidelines on risk management practices (continued)
 - ▶ Related guidelines on operational risks
 - ▶ Business continuity management guidelines
 - ▶ Guidelines on outsourcing
 - ▶ Guidelines for insurance business core activities
 - ▶ Guidelines on insurance fraud risk

Market conduct



Market conduct

- ▶ Regulatory requirements: *MAS 318 Market conduct standards for direct life insurers as a product provider*
 - ▶ Disclosure
 - ▶ Comply with the applicable standards stated in the Insurance Act and its Notices and the Notice on Product Disclosure & Information to Clients issued under the Financial Advisers Act of 2001
 - ▶ Prepare a Product Summary and Benefit Illustration for each of its life insurance policies, as required by the industry standards issued by the Life Insurance Association of Singapore (LIA)
 - ▶ Should not market any product with policy contract that is not in plain language

Market conduct

- ▶ Regulatory requirements: MAS 318 *Market conduct standards for direct life insurers as a product provider (continued)*
 - ▶ Sales process
 - ▶ Should not proceed to issue any policy contract until it receives a copy of the documentation signed by the client
 - ▶ Replacement of life policies
 - ▶ Shall warn prospective policyholders at proposal stage on the disadvantages of replacing an existing policy
 - ▶ Loans and advances
 - ▶ Shall not extend any loans or advances to any financial advisors out of the life insurance funds unless these transactions are based on commercial terms and at arm's length

Market conduct

- ▶ Regulatory requirements: MAS 318 *Market conduct standards for direct life insurers as a product provider (continued)*
 - ▶ Cessation of business with financial advisors
 - ▶ Should inform the affected policyholders whose financial advisor ceases to operate or ceases to continue to arrange its life policies
 - ▶ Have in place an internal process to recover its properties on the cessation of business of a financial advisor

Market conduct

- ▶ Regulatory requirements: MAS 318 *Market conduct standards for direct life insurers as a product provider (continued)*
 - ▶ Reports to MAS
 - ▶ Shall lodge, in printed form, by 21 April of each calendar year:
 - ▶ Information on distribution costs relating to the preceding calendar year
 - ▶ Information on source of business relating to the preceding calendar year
 - ▶ Information on fact-find options relating to the preceding calendar year
 - ▶ Information on complaints relating to the preceding calendar year

Prevention of money laundering/countering the financing of terrorism (AML/CFT)



Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers*
 - ▶ Underlying principles
 - ▶ Exercise due diligence when dealing with customers, persons appointed to act on the customer's behalf and beneficial owners
 - ▶ Conduct business in conformity with high ethical standards, and guard against undertaking any transaction that is or may be connected with or may facilitate money laundering or terrorist financing
 - ▶ Whenever possible and to the fullest extent possible, assist and cooperate with the relevant law enforcement authorities in Singapore in preventing money laundering and terrorist financing

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Customer due diligence (CDD)
 - ▶ No life insurer shall deal with any person on an anonymous basis or any person using a fictitious name
 - ▶ Shall perform CDD measures in accordance with this Notice
 - ▶ Put in place policies and procedures to address any specific risks associated with non-face-to-face business relationships or transactions

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Reliance on identification and verification already performed
 - ▶ When a life insurer (acquiring life insurer) acquires, either in whole or in part, the business of another financial institution (whether in Singapore or elsewhere), the acquiring life insurer shall perform CDD measures on the customers acquired with the business at the time of acquisition
 - ▶ There are exceptions

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ CDD measures for non-policyholders
 - ▶ A life insurer that undertakes any transaction of a value exceeding S\$20,000 for any customer who does not otherwise have business relations with the life insurer
 - ▶ Timing of verification
 - ▶ Before the life insurer establishes business relations
 - ▶ Before the life insurer undertakes any transaction for a customer, where the customer does not have business relations with the life insurer
 - ▶ There are exceptions

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Where CDD measures are not completed
 - ▶ A life insurer shall terminate the business relationship and consider if the circumstances are suspicious so as to warrant the filling of a suspicious transaction report (STR)
 - ▶ Existing customers
 - ▶ Shall perform such CDD measures as may be appropriate to its existing customers having regard to its own assessment of materiality and risk

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Simplified CDD
 - ▶ When satisfied that the risks of money laundering and terrorist financing are low (e.g., when dealing with a customer that is a financial institution supervised by MAS)
 - ▶ Shall document the details of risk assessment and nature of simplified CDD measures
 - ▶ Enhanced CDD
 - ▶ On high-risk categories

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Performance of CDD measures by intermediaries
 - ▶ A life insurer may rely on an intermediary to perform the CDD measures
 - ▶ No life insurer shall rely on an intermediary to conduct ongoing monitoring of customers
 - ▶ Notwithstanding the reliance upon an intermediary, the life insurer shall remain responsible for its AML/CFT obligations in this Notice

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Record-keeping
 - ▶ Prepare, maintain and retain documentation on all its business relations and transactions with its customers
 - ▶ Suspicious transaction reporting
 - ▶ Shall submit reports on suspicious transactions (including attempted transactions) to Suspicious Transactions Reporting Office, Commercial Affairs Department of the Singapore Police Force (STRO), and extend a copy to the MAS for information

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Internal policies, compliance, audit and training
 - ▶ A life insurer shall develop and implement internal policies, procedures and controls to help prevent money laundering and terrorist financing and communicate these to its employees and agents
 - ▶ A life insurer that is incorporated in Singapore shall develop a group policy on AML/CFT and extend this to all of its branches and subsidiaries outside Singapore
 - ▶ A life insurer shall develop appropriate compliance management arrangements, including at least, the appointment of a management level officer as the AML/CFT compliance officer

Prevention of AML/CFT

- ▶ Regulatory requirements: MAS 314 *Prevention of money laundering and countering the financing of terrorism – life insurers* (continued)
 - ▶ Internal policies, compliance, audit and training (continued)
 - ▶ A life insurer shall maintain an audit function that is adequately resourced and independent
 - ▶ A life insurer shall have in place screening procedures to ensure high standards when hiring employees and agents
 - ▶ A life insurer shall take all appropriate steps to ensure that its staff and agents (whether in Singapore or overseas) are regularly trained

Product development and pricing



Product development and pricing

- ▶ Regulatory requirements: MAS 302 *Product development and pricing – Mandatory requirements*
 - ▶ Prudent management oversight
 - ▶ Maintain adequate controls
 - ▶ Ensure that the board of directors approves the policies and procedures in respect of the development and pricing of insurance products and investment-linked sub-funds
 - ▶ Approval of new products
 - ▶ Shall obtain written approval from the MAS before offering any product
 - ▶ Request for approval shall be made in writing and submitted to the MAS no later than one month before the proposed official launch date of the product

Product development and pricing

- ▶ Regulatory requirements: MAS 302 *Product development and pricing* (continued)
 - ▶ Approval of new products (continued)
 - ▶ Request for approval shall be accompanied by relevant information and product documents
 - ▶ Approval exemptions
 - ▶ Short-term accident and health policy
 - ▶ Term policy having a duration of five years or less
- ▶ Contravention of any requirement imposed under the mandatory requirements of this Notice shall be an offence and shall attract penalty

Product development and pricing

- ▶ Regulatory requirements: MAS 302 *Product development and pricing – Guidelines*
 - ▶ Notify the MAS in writing of any product launched by the insurer that does not require the approval of the MAS (e.g., addition to existing portfolio of products) within seven working days after the official launch date of the product

Valuation of policy liabilities of life business



Overview of valuation: Life policy liabilities

Governed by:

- ▶ Insurance (Valuation and Capital) Regulations
- ▶ MAS 319 *Valuation of policy liabilities of life business*
 - ▶ Covers valuation of :
 - 1) Non-par policy liabilities
 - 2) Investment-linked policy liabilities
 - 3) Par policy liabilities

Overview of valuation: Life policy liabilities

- ▶ Follow Part V of Regulations for liabilities of the:
 - ▶ Insurance funds
 - ▶ Shareholders fund
 - ▶ Overseas (branch) operations

- ▶ If not specified, follow Singapore financial reporting standards and sound actuarial principles

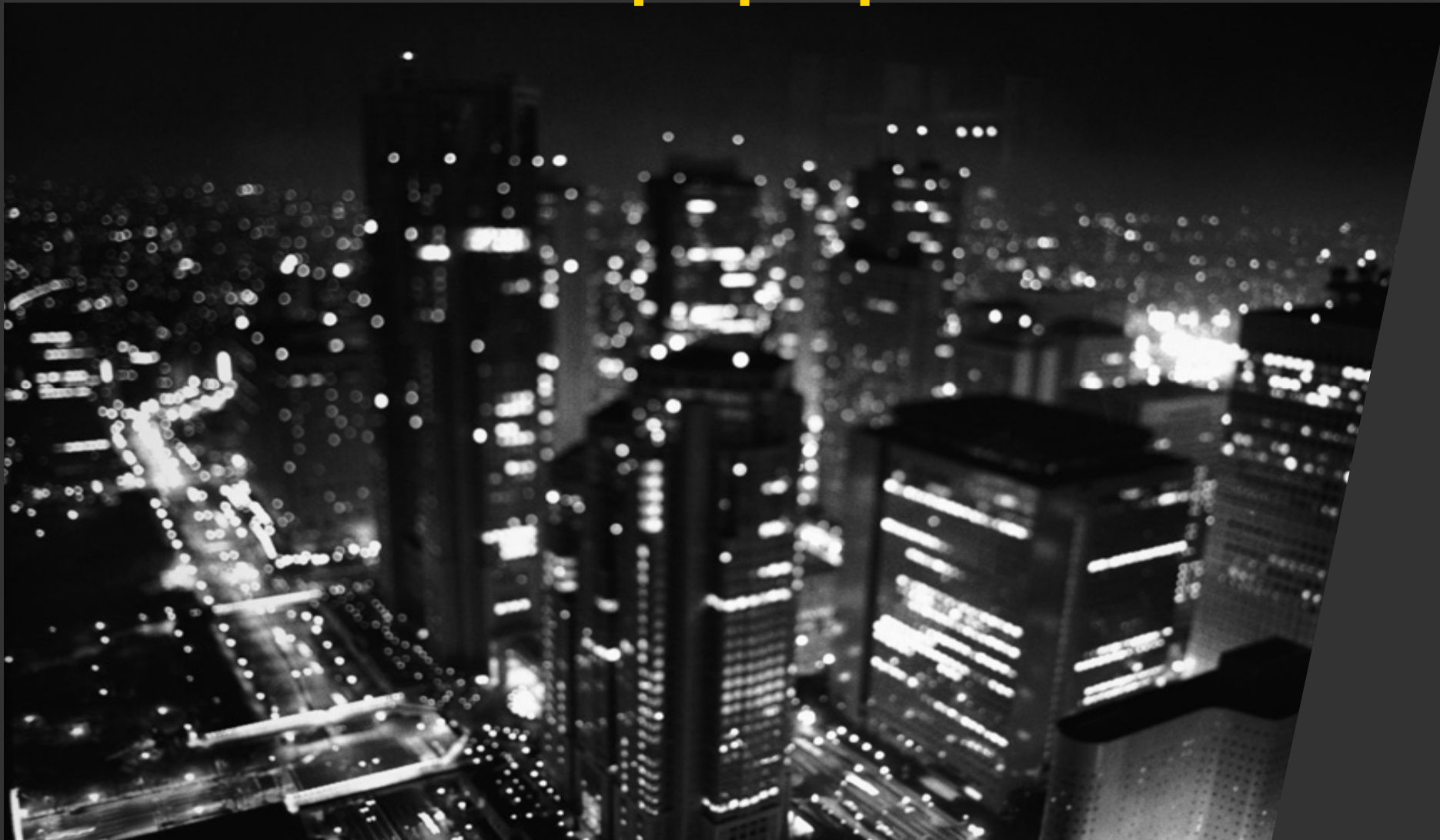
Overview of valuation: Life policy liabilities

- ▶ Discount rate:
 - ▶ Risk-free discount rate shall be used in determining:
 - ▶ Non-par policy liability
 - ▶ Non-unit reserve of investment-linked policy (ILP)
 - ▶ Minimum condition liability of par fund
 - ▶ Best estimate investment returns shall be used in determining par policy liability based on expected investment returns of assets backing the policy liabilities of the par fund
- ▶ MAS 319 *Notice on valuation of policy liabilities of life business* comprises both mandatory requirements and guidelines on the valuation of policy liabilities in respect of life business, as well as the reporting of such valuation

Overview of valuation: Life policy liabilities

- ▶ MAS 319 key requirements:
 - ▶ Valuation requirements: discount rates and non-guaranteed benefits
 - ▶ Guidelines on data and valuation system
 - ▶ Guidelines on valuation methodology
 - ▶ Guidelines on valuation assumptions
 - ▶ Guidelines on the preparation of the actuarial investigation report
 - ▶ Determination of the risk-free discount rate

Appointment of Principal Officers and Directors – “Fit and proper person” rules



Appointment of Principal Officers and Directors – “Fit and proper person” rules

- ▶ Regulatory requirements: MAS 106 *Appointment of Principal Officers and Directors*
 - ▶ Every insurer is required to seek the prior approval of the MAS in the appointment of its Principal Officer
 - ▶ Every insurer is required to exercise due care in the appointment of its Principal Officer
 - ▶ An insurer shall ensure that the person so appointed is a fit and proper person possessing the relevant qualifications and experience
 - ▶ Have the authority and responsibility to conduct the insurer's business professionally
 - ▶ Capable of ensuring compliance with the insurance law and regulations

Appointment of Principal Officers and Directors – “Fit and proper person” rules

- ▶ Regulatory requirements: MAS 106 *Appointment of Principal Officers and Directors* (continued)
 - ▶ Every insurer incorporated in Singapore is required to seek the prior approval of the MAS in the appointment of its Directors

Financial reinsurance



Financial reinsurance

- ▶ Regulatory requirements: MAS 316 *Notice on financial reinsurance – Mandatory requirements*
 - ▶ Prudent management and oversight and implement adequate controls
 - ▶ In the formulation of financial reinsurance contracts, there shall be clear documentation on the considerations relating to:
 - ▶ The selection of counterparty
 - ▶ The protection of policyholders' interest
 - ▶ The evaluation of the benefits to be derived under the financial reinsurance contract
 - ▶ Prior to its entry into any financial reinsurance contracts, an insurer shall develop and implement a reinsurance management strategy approved by its Board of Directors

Financial reinsurance

- ▶ Regulatory requirements: MAS 316 *Notice on financial reinsurance – Mandatory requirements* (continued)
 - ▶ Prudent management and oversight and implement adequate controls (continued)
 - ▶ Shall ensure that its entry into any financial reinsurance contract is consistent with its reinsurance management strategy
 - ▶ Approval
 - ▶ Shall obtain written approval from the MAS before entering into a financial reinsurance contract
 - ▶ Accounting treatment
 - ▶ A financial reinsurance contract that satisfies the condition of significant risk transfer shall be accounted for as a contract of insurance

Financial reinsurance

- ▶ Regulatory requirements: MAS 316 *Notice on financial reinsurance – Guidelines*
 - ▶ An insurer is advised to use financial reinsurance contracts that involve elements of insurance risk transfer
 - ▶ A significant insurance risk transfer is deemed to have taken place under a financial reinsurance contract when the following conditions are satisfied:
 - ▶ It is reasonably possible that the assuming insurer may realize a significant loss from the contract
 - ▶ It is reasonably possible to have a significant range of outcomes under the contract

Reinsurance – other matters

- ▶ MAS 114 Reinsurance management strategy
 - ▶ Responsibility and control of reinsurance arrangements, where a portion of the risks assumed by an insurer is ceded to another insurer
 - ▶ Primary responsibility for the sound and prudent management of an insurer rests with the Board of Directors and senior management
 - ▶ The Board of Directors and senior management should develop, implement and maintain a reinsurance management strategy appropriate to the operations of the insurer to ensure that the insurer has sufficient capacity to meet obligations as they fall due
 - ▶ Role of the Board of Directors
 - ▶ Role of senior management
 - ▶ Provides reference checklist for internal use and reference

Other relevant MAS directives, notices, guidelines and consultation papers



Other relevant MAS directives, notices, guidelines and consultation papers

▶ Source: MAS website

▶ http://www.mas.gov.sg/legislation_guidelines/insurance/Insurance.html

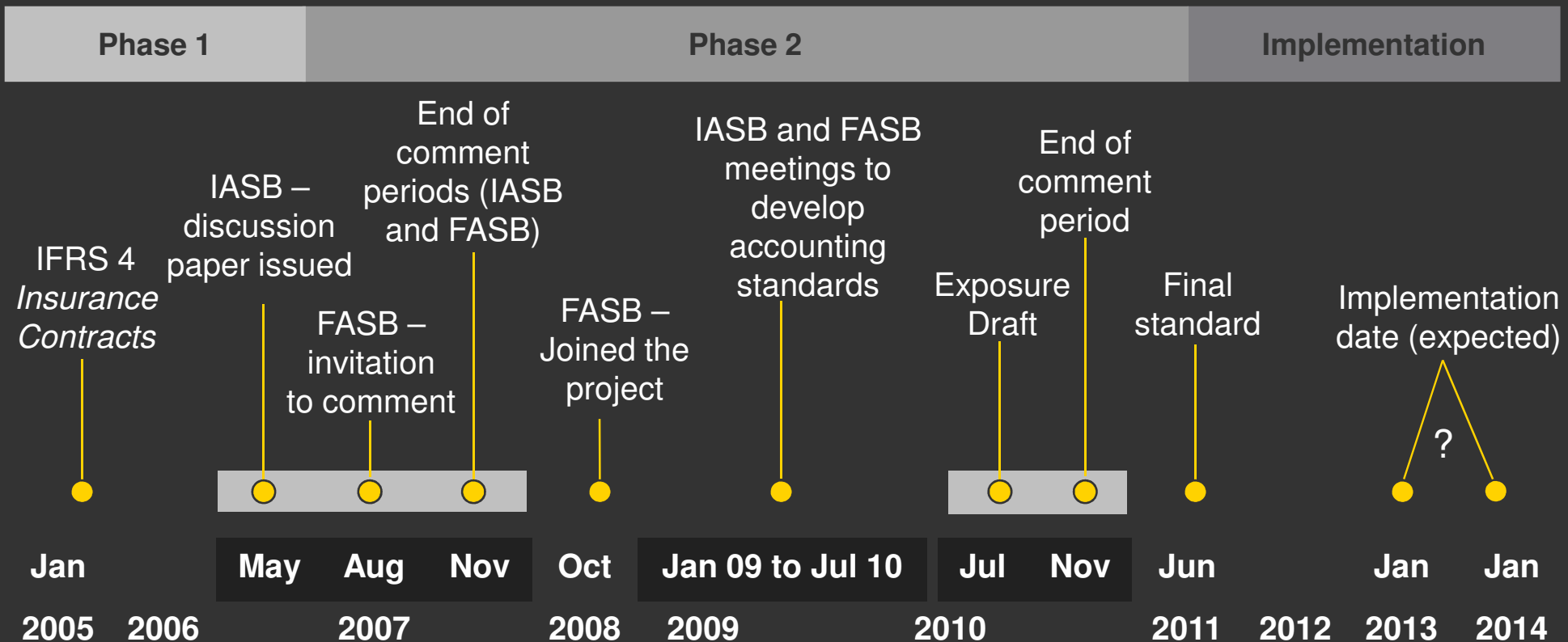
IFRS developments



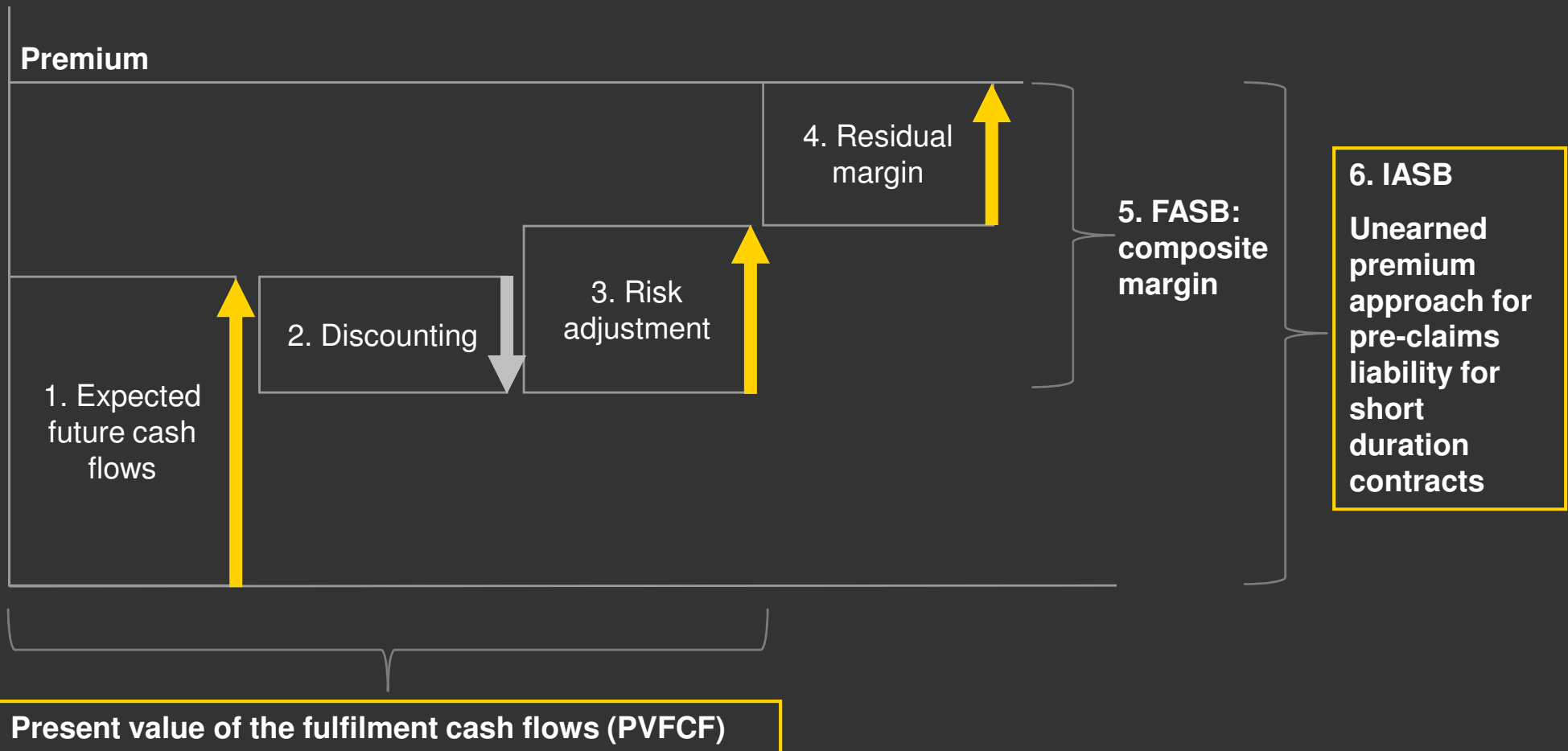
IFRS developments

- ▶ Exposure Draft *Insurance Contracts*
 - ▶ Introduction and timelines
 - ▶ Measurement model
 - ▶ Presentation and disclosure
 - ▶ Implications of the proposals
 - ▶ Next steps and concluding remarks

IFRS developments: Project timeline



Insurance contract accounting building blocks of the insurance liability



IFRS developments: Presentation model

	Year 1	Year 2
Summarized margin		
Risk adjustment *		
Residual margin *		
*(FASB – one composite margin)		
Insurance margin		
Experience adjustment		
Changes in estimates		
Investment income		
Interest on insurance liability		
Net interest and investment		
Profit		

Premiums, claims, claim handling costs, and incremental acquisition costs included in measurement of insurance liability not shown in Statement of Comprehensive Income. Treated as deposit receipt / repayment

Major implications of the Exposure Draft

- ▶ Life insurers
 - ▶ Account driven contracts will require unbundling
 - ▶ Premiums, claims and expenses deposit accounted
 - ▶ Limited allowance for acquisition costs likely to be more restrictive than in many measurement models today
 - ▶ Inconsistencies between measurement of investment contracts and insurance contracts
 - ▶ Risk-free discount rate incorporates liquidity adjustment but not non-performance risk

Major implications of the Exposure Draft

▶ Likely issues

- ▶ Transition proposals – in force does not include residual margin which leads to inconsistency with treatment of new business
- ▶ Financial guarantee contracts issued by financial institutions will be in scope of the new standard
- ▶ Format of the Statement of Comprehensive Income

Major implications of the Exposure Draft

▶ Operational implications

- ▶ Similarities and differences with measurement of liabilities under Solvency II and Embedded Value methods.
- ▶ Significant additional disclosures – especially for those not currently reporting under IFRS. Also detailed reconciliation requirements and information needed by portfolio of insurance contracts.
- ▶ Understanding initial impacts require modelling of existing and new business separately.
- ▶ Unlocked reserves and introduction of IFRS 9 may lead to changes in the way the business is managed.

Thank you



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