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Financial Crisis: Where Stand The Insurance Regulators?

The financial crisis, with its recent bloodbath in stock markets around the world, has drawn vigorous debate on whether the Great Depression 2 is upon us. There is a caucus building for some form of sustained consistent global action to help the world cope with the crisis though businesses are weary of economics being made a matter of politics. The recession seems confirmed, and more than US$6 trillion has been drained out of the economy. Where does insurance stand in this move for action, bearing in mind banking regulators have been held out until recently as role models in risk management. Can IAIS play a positive role in this exercise to restore confidence in the insurance industry both at the domestic level and at the international level?

In the AIG saga, it was repeatedly emphasised that it was the stability of the insurance business that led the US government to lead the bail out. In the words of Mr Eric Dinallo, New York Insurance Superintendent: "The Federal Reserve's rescue offer would likely not have been made if it were not for the core value of AIG's insurance subsidiaries, which exists due to sound solvency regulation and oversight provided by IAIS members worldwide." The losses had come from the non-insurance activities of the financial giant which, for better or worse, had become the icon of the insurance industry to the man in the street for all this while.

Stepping Up Co-ordination

In the wake of the crisis, IAIS was quick to step up its supervisory co-ordination efforts. In September, just days after the crisis broke loose, key insurance supervisors from around the globe were actively updated on matters relating to AIG and agreed to hold regular conference calls to monitor solutions to supervisory issues.

Burning Questions

Beyond this, what can the IAIS do? What can insurance regulators do especially vis-à-vis huge conglomerates and big groups whose operations are extensive and truly international and beyond the full supervision of any one regulator? Can rating agencies help, bearing in mind that many argue that their credibility has also been affected, given the fact that they were not quick enough to foretell the problems? Some blame the rapidity with which rating bodies move in to downgrade ratings as another factor accelerating the crisis.

Increased Exposures

More light needs to be shed on the intricacies of the linkages and the full extent of these links. While the insurance operations might be fully scrutinised and catered for, the insurance companies might face a double whammy on the

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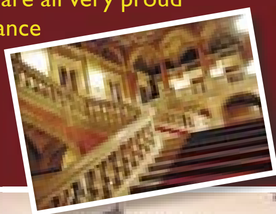
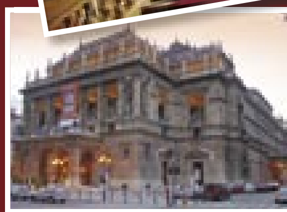
A Warm Welcome to Budapest!

As the very first representative of Hungary, one of the founding members of the IAIS and representative of the region in the Executive Committee for several terms, it is my pleasure and special honour to welcome you to Budapest.

For our region, for Hungary and especially for the hosting Hungarian Financial Supervisory Authority (HFSA), it is a unique opportunity for us to introduce ourselves. We are all very proud of the development of our countries and insurance industries during the past two decades and we would like to show you the results of our longstanding efforts.





Budapest Opera House

A Three-Year Preparation

The HFSA has been preparing – in a friendly co-operation with the whole Hungarian insurance industry and with MABISZ, its representative association – for almost three years now for the 15th Annual Conference of the IAIS. All arrangements made by our colleagues are based on the strong wish to make this conference memorable for all of you. You will learn that Hungary is a wonderful, challenging and colourful geographical area that abounds with intellectual, cultural and social values. We are confident that you will make the best of and enjoy your stay in Budapest, in the magnificent Opera House, in the Museum of Fine Arts with its unique exhibitions and at the different social programmes and excursions.

The representatives of the Hungarian insurance industry and the HFSA, its integrated supervisory authority have the common view that we can envisage high quality financial activity, level of services and regulation, as well as supervision in all "transition countries" of our region. We strive to show the distinguished representatives of the insurance industry and supervisory world the lessons learnt, positive and negative experience gained by our countries while they have emerged

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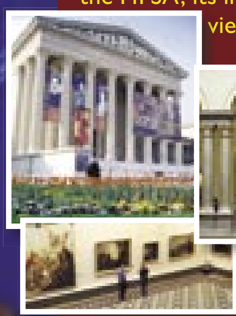
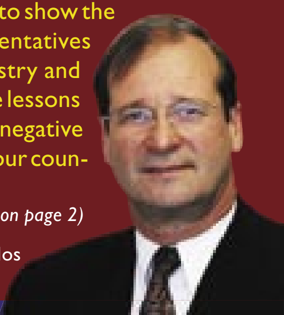


Museum of Fine Arts



Mr László Asztalos

Financial Crisis *(continued)*

investment front as some of the "bluest of the blue" chips have gone south too. So the dilemma and drama continue, with no respite. And worse, no one is seen as holding the magic wand anymore.

Global Forum

OECD Secretary-General Angel Gurría has stepped up calls for a global forum, offering the OECD as a vehicle to start discussions to chart a way forward out of the current financial crisis. The starting point is a review of the main regulatory and market failures that have emerged in recent months. Noting that a "piecemeal approach will not work", he said the long-term solutions must include a new drive to strengthen the rules and regulations, and raise corporate governance standards to reinforce market integrity.

Being Coherent Globally

IMF First Deputy Managing Director John Lipsky said: "The key challenges to restoring the financial system to full functionality are to insure adequate liquidity provision, to restore damaged balance sheets, and to rebuild capital where needed." Noting that the financial sector in many markets have become "outsized", he said there must be consolidation and "not all institutions can or should be saved".

Globalisation means that policy interventions – including the longer-term issues of regulatory and supervisory reforms – need to be globally coherent and consistent in order to be effective. One of the issues to be tackled is to "prevent excessive risk-taking in the future, without stifling the powerfully positive potential of effective financial markets."

Reminder Not to Close Borders

World Trade Organization's Director General Pacsal Lamy, has repeated his call that the most important lesson of the Great Depression is that "protectionism and economic isolationism do not work".

Any Takers or Leaders on the Insurance Front?

Ms Michaela Koller, Director General of the CEA said: "If Europe's insurers are to be encouraged to develop internationally, European regulatory and supervisory approaches cannot lag behind."

IAIS Chairman Michel Flamée said: "Since the financial community is so interlinked, financial supervisors must continue to co-operate closely in order to protect policyholders around the world."

With this rush for global solutions, at the least, IAIS must ensure that the voice of insurance is heard and not left out in the cold as a poor third cousin in the financial services sector in the global economy.

A Warm Welcome to Budapest! *(continued)*

and caught up with the more sophisticated countries of other parts of the world.

Doing Something New

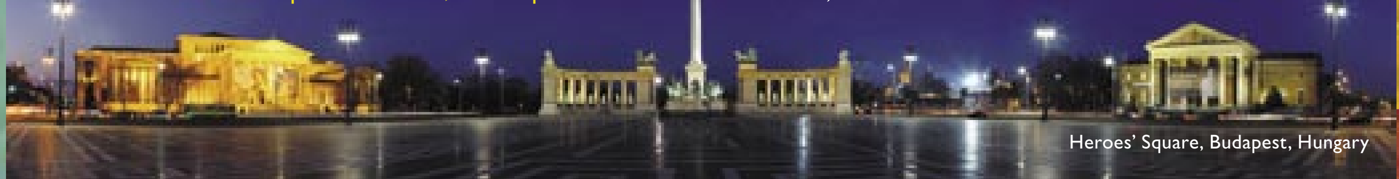
However, the 15th Annual Conference is not planned for dealing with what have already been done. It will be a special forum for the supervisors and the supervised to think together on how to meet the challenges they face individually in their countries and also together regionally or globally.

The "convergence" of financial services – and the options and problems of its regulation and supervision – is today an undisputed fact. We are confident that the main challenges of our globalised world will be identified, discussed and answered with practical lessons for all of us. For Hungary and for all other Central and Eastern European countries, it is of particular importance to acquaint ourselves with the experience of more advanced countries, of other "catch-up" or emerging markets both in the field of "geographical convergence" and in that of "cross-financial convergence".

A Warm Welcome

The organisers of this event at the HFSA all welcome you warmly to Budapest. I strongly believe on their behalf that you will enjoy your stay in Hungary. Thank you for joining us and we do hope you will return to visit us in future.

Mr László Asztalos
Member of the Board,
Hungarian Financial Supervisory Authority, &
Member, IAIS ExCo



Heroes' Square, Budapest, Hungary

What Global Group CEOs say to Regulators

To provide a meaningful feedback to regulators at this forum, we threw the gauntlet at several global Groups to give a quick response to these tricky questions on: "What are the key challenges you face in complying with insurance regulations? What is your view of the ideal insurance regulations? Is there a particular market whose regulations come close to an ideal? What are the current problems you have with domestic insurance regulations? How can the IAIS contribute to globalisation of insurance? Can there ever be such a thing as a global insurance regulator?" Here, we bring you the response of three brave and wise men in the global market, who despite the very busy challenges of the past three weeks, did find time to submit their most useful inputs. We salute them!

Dr Helmut Perlet, CFO and Member of the Allianz SE Holding Board

The key challenges today are that there is only a minimum degree of harmonisation of insurance regulation across Europe, including the usage of national options. This leads to different reporting requirements, different rules/interpretations and, in the end, more work for the insurance companies because of double reporting and checks. The current system also shows its limits when coming to the necessity of having a group-wide view, analysis of risks and comparison across countries.

Harmonisation Still at a Minimum

Currently there are no limits for supervisory arbitrage as, for example, a comparison of eligible elements of capital, asset limits, etc, which vary a lot from country to country, shows.

Solvency II goes in the right direction in terms of pushing harmonisation as well as group supervision based on market consistent and risk-based principles. A more interactive exchange and close co-operation between the different local supervisors, EEA (European Economic Area) and non-EEA, might help a lot in the future for having a better overview of the interdependencies between financial institutions as well as within large groups.

Accounting Comparability Must Be Improved

There is an urgent need for an international accounting standard for insurance contracts in order to improve comparability of the financial reporting of insurance companies worldwide. Even though the IASB is discussing this project now for more than 10 years and has issued its preliminary views in 2007, a final IFRS is not expected before 2011. In our view, the proposals should be linked closer with Solvency II proposals while giving appropriate reflection of performance reporting principles that recognise the long-term business model of the insurer.

Being Consistent

The IAIS, as global standard setter, can help a lot in the direction of having a closer system of insurance regulation as well as application. The intensive dialogue between the global regulators and the further development of recommendations on global accounting standards, taking developments like Solvency II into account, has to be further intensified with the aim of having a "consistent" approach in the end.

Mr Jacques Aigrain, Chief Executive Officer, Swiss Re

A short tour around the world of insurance regulation reveals that considerable change is underway. With the proposed Solvency II Framework Directive, Europe has the great opportunity to take the lead in regulating capital requirements. In the US, where insurance supervision is very fragmented, the industry is pushing hard to modernise the overall regulatory framework. In Asia, market liberalisation is a dominant issue, and insurance regulation remains often focused on price and product regulation.

Europe to Take the Lead

When Solvency II comes into force in or after 2012, the European Union will operate with the most modern (re)insurance regulatory standards in the world. This new supervisory system is based on economic principles, and will bring a better understanding of the actual risks an insurance company is facing. For the first time, all risks will be consistently quantifiable, providing an overview and the ability to assess dependencies and diversification effects.

Beware Particular Interest Groups

It remains to be hoped that the spirit of the framework will not be sacrificed in the interest of particular interests in the political debate or the current turbulence in the financial markets. The subprime crisis has raised some criticism about market valuation and risk models in banks. Even though internal risk and capital models are a key component of Solvency II, insurance differs greatly from banking and has also proven to be more resilient to financial crises. First indicative results of QIS 4, the fourth quantitative impact study on Solvency II carried out earlier this year, demonstrates that it is a sound framework for the insurance industry – one that will hold even under extreme scenarios.

There is no doubt about the direction of future insurance capital regulation: its key characteristics include valuation based on economic principles, an all-risks approach based on internal models, the recognition of risk mitigation practices and increased transparency.

Views on Risk and Capital

The IAIS plays an important role in promoting greater harmonisation of regulators' views on risk and capital across the globe. This will lead to a more efficient allocation of risk and capital and to reduced costs of compliance. Ultimately, policyholders will benefit from better protection and shareholders from greater transparency.

Mr Michael Wilkins, Managing Director and Chief Executive Officer, Insurance Australia Group

A growing number of insurers, including Insurance Australia Group, are operating across multiple international jurisdictions, in line with the increasing liberalisation of global trade and capital markets.

While operating cross-border provides significant diversification benefits, it also brings a number of challenges, including the obligation to comply with multiple regulatory regimes in each market. This is further complicated by the need to compete with foreign companies, both at home and abroad, which operate under different regulations.

Harmonisation of both prudential and accounting standards across various international jurisdictions would significantly improve the efficiency of operating cross-border. It would reduce unnecessary compliance costs, provide greater consistency for managing operations in multiple markets, and would ensure a more level playing field for global competitors.

The Domestic Problems

Australian general insurers must adhere to an extensive range of regulatory requirements, many of which entail costly and inefficient compliance duplication and overlap.

Insurers are bound by a variety of Federal, State and Territory regulations which cover prudential supervision, market conduct rules, consumer protection and various statutory insurance schemes. Most insurers must also adhere to the corporate regulatory regime that applies to all Australian incorporated businesses.

There is no doubt regulation is essential to provide consumer protection. However, further balance is required to ensure the burden on insurers is not so great as to undermine efficiency and international competitiveness.

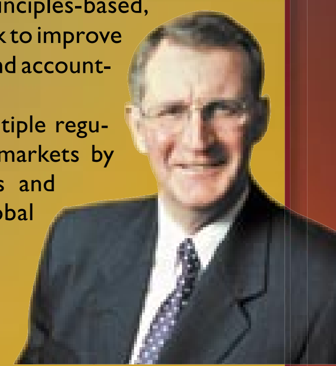
Ideally, the next step would be the introduction of a national regulatory framework which emphasises competitive neutrality, cost effectiveness, transparency, flexibility and accountability.

For example, prudential regulation could be rationalised, with APRA becoming the sole, national prudential regulator thereby removing the duplicate State and Territory statutory requirements in some classes of insurance.

The IAIS to the Rescue

Establishing a global insurance regulator is highly unlikely. However, an opportunity exists to introduce a principles-based, rather than rules-based, global framework to improve efficiency and consistency in prudential and accounting standards across jurisdictions.

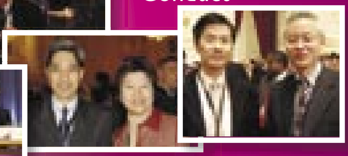
This would limit the potential for multiple regulatory regimes to impact adversely on markets by reducing unnecessary compliance costs and creating a more level competitive global playing field.



Past IAIS Annual Confernces – A PICTORIAL

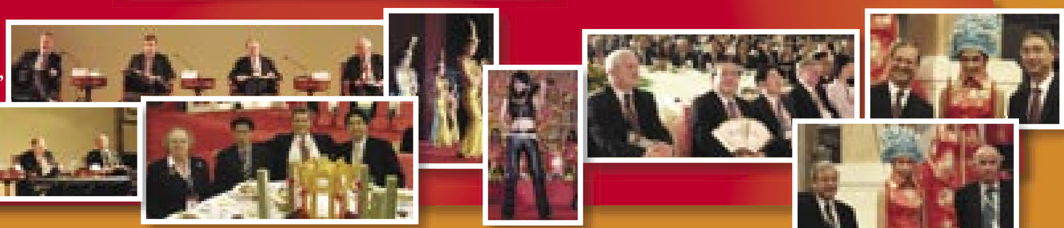
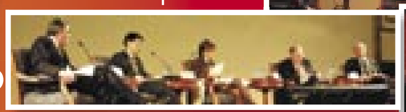
2004
AMMAN JORDAN
Theme: "Globalized Insurance Markets – Challenges & Opportunities"

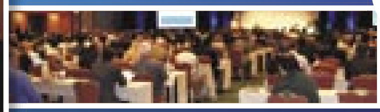




Theme: "Solvency, Governance and Market Conduct"
VIENNA AUSTRIA
2005

BEIJING CHINA
Theme: "Fostering Development and Managing Risk: Challenges for Insurance Supervision"
2006

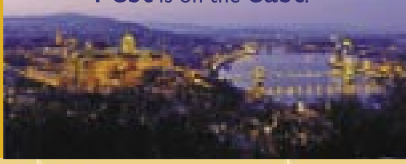
Theme: "A Global Climate for Change: The Future of Insurance Regulation"
2007
FORT LAUDERDALE USA

HUNGARY BY THE NUMBERS

In 2007, Hungary's **total premium** volume was **US$4.9** billion, up 31% y-o-y, of which **life** premium amounted to **US$2.8** billion, while **non-life** premium was **US$2.2** billion.

Hungary had a **0.12%** share of the world market.

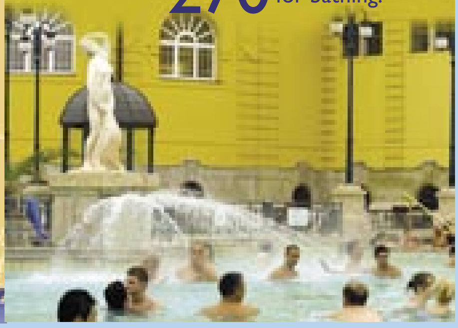
Budapest occupies the **2** banks of the Danube River: **Buda** is on the **west** bank, while **Pest** is on the **east**.



Germany is Hungary's **number 1** economic partner

Hungary has the **5th** largest supply of thermal water in the world.

It has **1,300** thermal springs, **270** of which are used for bathing.



The **population** of Hungary is about **10** million.

Hungary borders **7** countries: Austria, Croatia, Romania, Serbia, Slovakia, Slovenia, and Ukraine

Hungary is made up of **19** counties, **23** urban counties, and **1** capital city.

Sources: CIA The World Factbook – Hungary, Hungary Tourism promotional brochures

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