INTERNATIONAL INSURANCE FOUNDATION
1233 Twentieth Street, NW Suite 202 Washington, DC 20036
Phone: 202-296-2424 Fax: 202-296-4437

Quarterly Report

Winter 2000

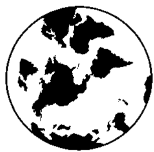
Together with its various partners, the International Insurance Foundation continues to work toward a more efficient global insurance market. Most noteworthy are the contributions of the International Association of Insurance Supervisors (IAIS) to global financial stability. As mandated by the International Monetary Fund, the IAIS is articulating the core principles of insurance supervision. IAIS principles and standards guide supervisors in emerging markets toward transparent and efficient insurance systems capable of gaining consumer confidence.

IAIS Licensing Textbook in Preparation

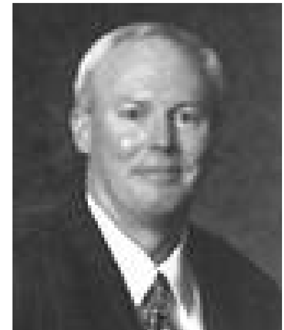
As the IAIS develops the core principles of insurance supervision, successful implementation in emerging markets requires a major educational effort. In addition to sponsoring education conferences, the IIF is assisting the IAIS in the preparation of educational materials. The first project is a textbook that explicates the IAIS Supervisory Standard on Licensing. German Supervisor **Helmut Müller** and his staff drafted the explanatory materials, the IAIS Education Subcommittee reviewed them, and the IIF staff its contributed editorial talents to the project. Eventually the textbook will be available not only in conventional format, but also as an interactive computer learning program accessible on the Internet.

Calendar

Month	Dates	Event
March	**27-29**	**IAIS Latin American Regional Seminar**, ***Lima, Peru***
April		**IIF Executive Committee**, ***Washington***
June		**IAIS African Regional Seminar**, ***Pretoria, South Africa***
July	**8-13**	**IAIS Eastern European Regional Seminar**, ***Cracow, Poland***
September	**11-23**	**FUNENSEG Seminar**, ***New York & Princeton***
		IAIS/OECD Latin American Seminar, ***Mexico City***
October	**10-12**	**IAIS Annual Conference**, ***Capetown, South Africa***
November	**9-10**	**Annual IIF Board Meeting**, ***Washington***

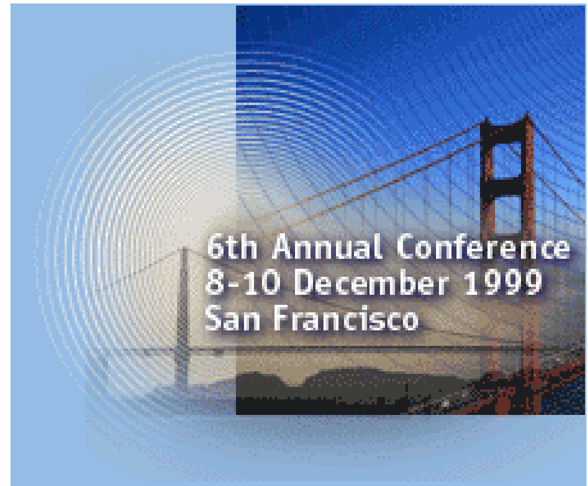


New Founding Member



The International Insurance Foundation welcomes **AEGIS Insurance Services, Inc.**, as a founding member. AEGIS is an excess and surplus lines insurance company owned by its members, more than 300 public utility policyholders. As those utilities have expanded their operations into the global energy industry throughout the world, AEGIS has added products and services to provide solutions for international risk management needs. Its nominee to the IIF Board of Directors is **Alan J. Maguire**, Chairman and CEO.

IAIS Annual Conference



The Sixth Annual Conference of the International Association of Insurance Supervisors met in San Francisco from December 8-10, 1999. The conference included the annual business and committee meetings and panel discussions. Since the 1998 meeting held in Cancun, Mexico, the IAIS has welcomed 11 new members and now represents more than 100 jurisdictions. West Virginia Insurance Commissioner **Hanley Clark** serves as chairman of the IAIS.

During the business meeting, the IAIS adopted three important papers developed by the Technical Committee during the past year. *Principles for the Conduct of Insurance Business* specifies standards of business conduct expected of both insurance companies and intermediaries, including integrity, diligence, prudence, disclosure, customer focus, openness, and management efficiency. *Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations* is a revision of the previously adopted Insurance Concordat, which provides for the cooperation of supervisors in regulating cross border business. *The Supervisory Standards on Asset Management by Insurance Companies* provides guidelines for supervisors to assess how insurers should control the risks associated with their investment activities. With these additions the IAIS has now adopted three principles, four standards, and two guidance papers.

In addition to adopting these new principles and standards, IAIS members voted to create observer membership in the organization. This change will allow private sector representatives to attend and participate in more of the sessions during the annual meetings, bringing greater openness and transparency to IAIS activities.

Hot topics discussed at the IAIS meeting included insurance accounting, privatization, problems of emerging market regulators, and supervisory structures. Insurance accounting is a critical issue for regulators, and they are not completely comfortable with the effort of the International Accounting Standards Committee to develop uniform insurance accounting standards. Satisfying the information needs of policyholders, investors, regulators, and management in multiple jurisdictions is not an easy task, and further developments on this topic deserve close attention.

Supervisors agreed that in the long run, privatization of the insurance market will enhance the national GDP, create higher quality jobs, increase technology spill-over, encourage private savings, and advance capital formation. Despite these evident advantages, governments must convince the population of the benefits arising from privatization. Dissolving a government monopoly eliminates jobs, and consumers may lack confidence in private insurers, whether they are domestic or foreign. Nevertheless, these immediate drawbacks can be alleviated through proper management of the privatization process.

Several supervisors detailed the obstacles encountered during the liberalization process. Since many new IAIS members represent economies in transition, the discussion was particularly relevant. Liberalization of insurance markets often results from the need to converge regulations with economic and trade agreements. In Spain, for example, European integration was a major factor, and in Mexico, the NAFTA negotiations set the process in motion. Liberalization of the Hungarian insurance market occurred as part of the overall economic and political restructuring after the demise of communism. Negotiations over accession to the European Union introduce further pressures for liberalization in Central and Eastern Europe, and regional trade agreements in the Americas, southern Africa, and Southeast Asia are likely to have similar effects. As liberalization opens these markets to greater competition, sound and effective prudential supervision becomes increasingly urgent.

Another trend, the integration of financial services, presents still another challenge to supervisors. On the next page Ian Webb summarizes the divergent views presented in San Francisco on the structure of supervisory authorities.

Essay:

Integrated Financial Regulation

by Ian Webb

The panel on "Pressures for Changes in Supervisory Structures" at the Annual IAIS meeting re-kindled a current debate concerning the optimal structure of financial services supervision. Panelists Martin Roberts and Tom Karp explained why the move to consolidated banking, insurance, and securities market supervision made sense in their respective financial service markets, while Helmut Müller and Jean-Louis Bellando described several potential pitfalls from such consolidation.[1]

Underlying pressures on regulatory systems have been attracting the attention of regulators and international policymakers for some time. Widespread financial integration and consolidation have greatly changed the nature of financial services markets during the last 15 years. This integration has affected ownership structures as well as the development and marketing of financial products. Parallel to the blurring of financial service markets has been the impact of new technology on banks, insurers, and securities firms' operations.

These pressures present new challenges to regulators, who are trying to protect consumers and maintain systemic stability while not dampening innovation and competition. One challenge is the increasing difficulty of monitoring the solvency and marketing practices of financial conglomerates. Separate regulatory agencies monitoring various entities within a financial conglomerate may overlook the risks faced by the group as a whole. For this reason international authorities advocate increased coordination between banking, insurance, and other financial services regulators. The Joint Forum on Financial Conglomerates (Joint Forum) was established in early 1996 to study, among other things, procedures and guidelines that might facilitate the management of risks arising from financial conglomerates. The establishment of this forum represents a concerted international effort among regulators to keep up to date with the risks of an increasingly consolidated and integrated financial services marketplace.

The complexity inherent in corporate and managerial structures of financial conglomerates, however, makes coordinated supervision and recognition of all the group's risks a difficult task. There is a complexity inherent in financial conglomerates that often diminishes transparency.[2] It remains to be seen, consequently, whether such coordination can be effectively achieved within separate regulatory agencies.

Systemic risk posed by conglomerates is only one of many concerns that drives the debate on optimal financial services supervisory structure. Another concern is the demand for regulatory transparency and fairness created by financial products which cross traditional boundaries between banking, insurance, and securities. The convergence of financial services means that previously distinct institutions now increasingly compete in offering similar products. Regulatory requirements imposed upon different institutions should arguably create level playing fields in the interests of promoting healthy competition and innovation. Whether this regulatory transparency and fairness can be achieved in the absence of a unified regulatory apparatus remains to be seen.

Another concern is efficient allocation of supervisory resources in the face of increasingly complicated institutional and product issues. The rapid pace of innovation in products and sophisticated asset-liability management techniques presents supervisors with products and practices which require very specialized knowledge.

[1]Martin Roberts is the Director, Insurance Directorate, Financial Supervisory Authority, United Kingdom. Tom Karp is the Executive General Manager of the Australian Prudential Regulation Authority. Helmut Müller is President, Bundesaufsichtsamt für das Versicherungswesen, Germany. Jean-Louis Bellando is Secrétaire Générale, Commission de Contrôle des Assurances, France.

[2]Scott, David, "Regulation and Supervision of Financial Conglomerates", *Private Sector*, The World Bank, FPD Note No. 36, March 1995.

Ian Webb is Research Director of the International Insurance Foundation.

Integrated Regulators

Australia, Canada, Denmark, Japan, Korea, Norway, Singapore, Sweden, and the UK have moved over the last 15 years toward a consolidated supervisory structure. While the UK Financial Services Authority (FSA) emerged only in the last year, Canada has been integrating its regulatory authorities since 1988, and Denmark, Norway, and Sweden since the mid -1980's. At the time of this writing, other countries, representing the majority of financial services trade, still retain largely autonomous regulatory agencies.

What exactly is an integrated regulator? Most of the countries in the "integrated supervisors" club have regulatory frameworks with some or all of the following characteristics:

- a single regulatory body oversees banks and insurance companies, banks and securities dealers, or all financial service activities;
- a single regulatory body applies similar supervisory practices to each industry segment;
- a supervisor works within a similar set of legislation and regulations for each industry segment;
- a supervisor attempts to maintain a level, competitive playing field for different types of financial institutions offering similar products and services.

Supporters of consolidated supervisory structures expect them to provide the needed efficiencies in staff resources to meet new challenges.

To sum up, proponents of consolidation argue that it improves conglomerate supervision, helps establish regulatory transparency and more level playing fields across financial service sectors, and enhances supervisory resources by allowing for the specialization of staff in complex risk areas while sharing staff on common risk areas.

Skeptics of consolidation suggest that an integrated agency may become an inflexible, bureaucratic system. Smaller, separated regulatory agencies, they argue, will be more able to react quickly and specifically to problems that arise in their respective markets than one large agency. In a sense, this is a "niche" argument that equates singly-focused, separated regulatory agencies with better focus and service.

Along these lines is a parallel argument that fundamentally different priorities and concerns are attached to the workings of banks, insurers, and securities firms. For example, banking supervision is said to be more concerned with system risk, insurance supervision with soundness of individual institutions and fair treatment of policyholders, and securities supervision with the efficiency of markets and disclosure to investors.[3] These different supervisory approaches supposedly reflect the differences in consumer expectations and behavior related to specific types of financial service products. Securities, for example, allow consumers to take on risks while insurance promises to take away risks. Establishing one agency for the joint supervision of these three types of institutions, the skeptics conclude, would be a mistake.

Whether consolidated financial services regulation and supervision is appropriate, however, depends to a large extent on financial market pressures and existing legal, regulatory, and institutional environments within a particular jurisdiction If financial services integration and technological innovation continue on their current course, there may be a convergence of pressures and conducive environments in many jurisdictions that make the benefits of consolidation greater than its potential costs. The need to level playing fields and adopt effective cross-institution supervision moreover, cannot be ignored for long.

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[3]Vaughan, Terri M., Panel on Financial Services Reform: Basic Components, Position, and Prognosis for the Future," Conference on Insurance and Financial Services Regulation, Hartford, CT, October18, 1999.

World Bank Launches Disaster Mitigation Initiative

In February the World Bank launched an international partnership designed to reduce the human and economic costs of natural disasters in the developing world. Executive Director **Robert Gibbons** represented the International Insurance Foundation at the ProVention Consortium, an international coalition of governments, international organizations, private insurance companies, universities, and non-governmental organizations.

The ProVention Consortium strives to give developing countries the means to cope with natural disasters such as earthquakes, hurricanes and floods, and reduce the loss of life and destruction they cause.

In 1998, natural disasters killed more than 50,000 people and destroyed $65 billion worth of property and infrastructure. The World Bank has lent more than $19 billion for post-disaster reconstruction over the last 20 years, often more than once to the same country after successive disasters.

"For too long, the international community has picked up the pieces after disaster has struck. The ProVention Consortium will help poor countries anticipate natural catastrophes so that when they do strike, as they inevitably will, there will be less suffering, destruction and disruption," said Bank President **James D. Wolfensohn**. "Today, the poor in many developing countries are far too vulnerable to natural disasters, as watersheds are deforested, buildings are substandard, and settlements established at unsafe locations. The Consortium seeks to reverse this trend."

The consortium will promote safety by helping governments and communities devise effective preventive measures. It will support public policies that reduce the risk of natural and technological disasters in developing countries by, for example, the integration of prevention and mitigation mechanisms in development plans, the adoption of improved building codes, and more effective management of both land use and emergency response agencies. Finally the consotium will develop governments' ability to anticipate, and respond effectively, to disasters when they strike through the use of early warning systems and civil defense.

"The consortium marks a shift from fatalism to prevention, from response to preparation, from relief to a strategy of risk reduction and risk transfer," said **Alcira Kreimer**, Manager of the World Bank's Disaster Management Facility and principal architect of the consortium. "Disasters will still occur but if prevention and mitigation are taken seriously the massive human and economic costs we have seen in recent years are not inevitable."

The consortium will promote examples of "best practice" such as the measures to update and enforce building codes incorporated into the World Bank $505 million reconstruction loan to Turkey following last August's earthquake. The reconstruction program will introduce better planning for land-use, and requires compulsory insurance for housing. Emergency response management will also be upgraded.

Such efforts of vulnerable countries to reduce their exposure to risk create opportunities for the private sector. The ProVention Consortium seeks the active engagement of the insurance industry in order to seize these opportunities to manage disaster-related risks more effectively. The International Insurance Foundation supports the Consortium not only because its disaster mitigation projects are useful individually, but also because in the long run they will encourage developing countries to adopt policies that facilitate more efficient distribution of all types of risk.

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World Bank in disaster strategy initiative

By Stephen Fidler
In Washington

The World Bank yesterday launched a partnership between private and public organisations aimed at helping poor countries cope with natural disasters.

The so-called ProVention Consortium brings together governments, international organisations, private insurance companies, non-governmental organisations and universities.

Natural disasters killed more than 50,000 people, most in poor countries, and destroyed $65bn of property in 1998. The World Bank says it has lent $19bn for post-disaster reconstruction over the past 20 years.

The partnership includes organisations such as the UN Development Programme, the International Federation of the Red Cross and Red Crescent Societies, the Inter-American, Asian, and African Development Banks, the US Federal Emergency Management Agency, the Organisation of American States, and the Ministry of Construction of Japan. The governments of Norway, St Lucia, Mexico and Turkey are also taking part, along with reinsurance companies Munich Re and Swiss Re.

World Bank officials said the private companies would be able to share details of their databases to identify regions of the world vulnerable to natural disasters.

They drew a contrast between the co-ordinated international efforts and spending that regularly take place after a disaster and the lack of advance preparation to reduce the costs when disaster strikes.

"Rather than be reactive, our effort is to try to build more resilient systems and see how we can reduce the losses," said Alcira Kreimer, manager of the World Bank's Disaster Management Facility.

World Bank Workshop on Financial Institutions

The importance of non-bank financial institutions (NBFI) to economic development and financial market stability is becoming increasingly apparent in this global economy. The World Bank hosted a workshop in February to engage experts on NBFIs contribution to encouraging economic growth, consumer protection, and other critical issues in the regulation of NBFIs. The conference, titled "Non-Bank Financial Institutions: Development and Regulations," brought together specialists from a variety of related fields to discuss the issue. **Harold Skipper,** Professor at Georgia State University and IIF Academic Advisor, examined the importance of insurance worldwide. He discussed the role insurance has in economic development, the factors affecting insurance demand and supply, and the challenges facing governments to promote competitive and sound insurance markets in their jurisdictions. During the liberalization process in emerging markets regulatory agencies face several challenges, and **Patrick Goergen** from the insurance unit of the United Nations Conference on Trade and Development (UNCTAD) enumerated the pitfalls of various regulatory approaches. Drawing from the Canadian experience, **Lawrie Savage**, Savage and Associates, described the advantages of consolidated supervision and the greater reliance on boards of directors as a path to better self-regulation by the industry. **Kim Staking,** Financial Economist, Inter-American Development Bank, spoke on the IDB paper, "Financial Risk Management: A practical approach for emerging markets." The paper explained the importance of financial risk management for NBFI's in emerging markets stressing that some of the tools and concepts used by financial risk managers can be of benefit to managers of all types of non-bank financial institutions.

New Senior Advisor

Impressed by the Foundation's goal of a global, private insurance industry characterized by the highest levels of knowledge, technology, professionalism, and business ethics, **D.S. Narain** has accepted the role of IIF Senior Advisor. Mr. Narain recently completed a three-year term as a "whole-time member" of the Insurance Regulatory Authority of India. Prior to joining the IRA, Mr. Narain was the "Senior most Executive" of the LIC and was the Zonal Manager of the South Zone, overseeing the business in Kerala, Tamil Nadu, and the Pondicherry. As General Manager of the Life Insurance Company (LIC) International EC Bahrai, his responsibilities included product innovation, acceptance of risks, handling of investment of companies funds, and development of the intermediary systems. Running the operations of this Middle Eastern joint venture required extensive travel throughout the region. Another noteworthy assignment was to head the Management Development Centre (MDC), Bombay, which addressed the training needs of senior managers of the LIC. During his three year tenure at the IRA, Mr. Narain was closely associated with the drafting of the insurance legislation and the drafting of notification for the "Ombudsman" scheme for insurance consumers. As IIF Senior Advisor Mr. Narain will lend his 35 years of experience in the Indian insurance industry to future IIF training programs and research projects.

IIF Website Links World

What is the IIF? Who are its Founding Members? When is the next seminar in . . . ? Quick answers to these and many other questions are now available at www.iifdc.org. IIF Program Coordinator **Sally Steel** is also IIF Webmaster Sally Steel. Working with Next Wave Consulting, Sally brought the IIF information base into the 21st century. The IIF website now includes program descriptions, staff biographies, IIF Quarterly Reports, and IIF Occasional Papers, as well as links to partner organizations and IIF Founding Members. Eventually it will provide interactive learning to the staff of insurance supervisory offices around the world.