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Quarterly Report

Winter 2001

As the world's financial markets become increasingly integrated, the International Insurance Foundation continues to play a constructive role in the evolution of global standards for insurance supervision. The Foundation studies the major issues, facilitates educational seminars, and refines the concepts and materials that present best practices. Insurers and consumers alike stand to benefit from the trend toward global standards as insurance markets become more efficient and more reliable.

Progress on IAIS Educational Materials

In addition to formulating global standards of insurance supervision, the International Association of Insurance Supervisors assists emerging market supervisors in implementing those standards. A crucial part of this educational effort is the development of textbooks that explain the IAIS Supervisory Standards. The Education Subcommittee of the IAIS Emerging Markets Committee coordinates this activity, and the International Insurance Foundation contributes as requested.

INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS

IAIS

LICENSING TEXTBOOK

October 2000

One of the IAIS Standards deals with the licensing of insurers. The German Insurance Supervisor, **Dr. Helmut Müller**, who also chairs the IAIS Education Subcommittee, wrote the textbook for the licensing standard. After extensive review by the subcommittee and other insurance supervisors, IIF Executive Director **Robert Gibbons** provided editorial suggestions and additional material incorporated into the final version, which was distributed at the IAIS Annual Conference in October.

The Education Subcommittee is now working on a textbook for the IAIS Supervisory Standard on On-site Inspections, as well as a basic training manual on the Core Principles of Insurance Supervision. Textbooks for the other supervisory standards will follow.

In addition to reviewing and editing these textbooks, the International Insurance Foundation is also assisting the educational effort by developing computer versions of the textbooks. These computer programs present the same content as the textbooks in a self-paced, interactive format that supervisory staff can use in their offices anywhere and anytime. Using this technology, ultimately the education of insurance supervisors can be delivered over the Internet. At that point all insurance supervisors around the world will have access to the same information, making prudential supervision stronger, easier, and more effective.

Malaysia Hosts Conferences for Insurance Industry and Supervisors

Back-to-back conferences in Kuala Lumpur, Malaysia, brought more than two hundred insurance experts from around the world to consider the implications of globalization. The International Insurance Foundation joined several other organizations in sponsoring these conferences.

The Malaysian Insurance Institute organized the Second International Conference for the Emerging Insurance Markets in a Globalized Economy, held January 15-16. Under the theme “Towards Achieving Competitive Advantage” this conference addressed the new economy and insurance markets, the General Agreement on Trade and Services, breaching the technology gap, and the challenges and opportunities facing insurance enterprise and governments in emerging markets. IIF Research Director **Ian Webb** provided a presentation for the program on “Asset-Liability Management in a Volatile Economic Environment.”

The OECD/IAIS Conference on Insurance Regulation and Supervision in Asia on January 17-18 provided an opportunity for policy dialogue among insurance regulators and supervisors as well as industry experts on the theme “Asian Insurance Systems in the New Century.” Approximately 120 participants from 41 countries around the world attended the conference, hosted by Bank Negara Malaysia. They represented both major developed economies and Asian emerging-market economies, as well as international organizations such as the International Monetary Fund, World Bank, International Actuarial Association, and the International Insurance Foundation in addition to the OECD and the IAIS.

Following opening remarks by **Ms. Helena Conruyt-Angenent**, Chairperson of the OECD Insurance Committee, **Mr. Hanley Clark**, Chairperson of the IAIS Executive Committee, and **Dr. Zeti Akhtar Aziz**, Governor of Bank Negara Malaysia, Ms. Conruyt and **Dr. Awang Adek Hussin**, Assistant Governor, Bank Negara Malaysia and IAIS member, chaired six sessions covering important current issues for Asian insurance markets, including market stability, globalization, and risk assessment. The major findings were as follows:

- The economic crisis in the late 1990s, while affecting the insurance industry in the Asian region to a lesser extent than would have been expected, has also generated a momentum for regulatory and supervisory reforms, and provided a basis for further development.
- The insurance sector, as an important part of the whole financial picture, can influence overall financial stability. In order to strengthen domestic financial systems, the Financial Sector Assessment Program, jointly managed by the IMF and the World Bank, assesses observance of the IAIS Core Principles and other financial sector standards. Observance of these standards will contribute to financial stability.
- On a global scale, insurance markets have become increasingly integrated. The next round of World Trade Organization negotiations will encourage further market liberalization. In order to reap the benefits of globalization, however, efforts are needed to ensure that it is successful, especially by establishing adequate prudential regulation for insurance.
- Insurance companies are exposed to various risks. Risk management, involving assessment, measurement and active management of risks, must primarily be the responsibility of the company. Supervision aims to ensure the company’s compliance with relevant regulations.
- Solvency supervision should be comprehensive, including assessment of not only solvency ratio and balance sheet soundness but also operating environment and conditions.
- Private pensions, in which insurance companies play an important role, have recently appeared as a key issue for the future in both OECD countries and emerging economies. The International Network of Pension Regulators and Supervisors, created in April 2000, promotes international exchange of views and experience on private pensions regulation and relevant best practices.
- Private health insurance is also receiving increased attention in the OECD countries, reflecting an ageing of society as well as reforms in health care. Sooner or later emerging economies will face similar issues. Private health insurance can supplement public health care systems to give a better quality of health care provision, but posing new challenges for insurance regulators.

Risk, Freedom, and Development in India by Robert Gibbons

The Republic of India celebrates August 15, the anniversary of independence from Britain in 1947, as Independence Day, but future generations of Indians should celebrate October 23 as well. As of that day one billion people have a new kind of freedom: a choice in providers of insurance products. While this freedom may seem less important than the freedom to choose their own government, it too promises a better life for the people of India.


बीमा विनियामक और विकास प्राधिकरण
INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY

23rd OCTOBER, 2000. New Delhi

SUB : REGISTRATION OF NEW INSURERS BY INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY.

At the meeting of the Insurance Regulatory and Development Authority today, the Authority decided to grant registration under section 3 of the Insurance Act, 1938 to the following companies newly set up:

Since 1972 in the case of general insurance, and 1956 in the case of life insurance, they could buy insurance only from the state-owned companies. That monopoly ended on October 23 when the Insurance Regulatory and Development Authority authorized six new insurance ventures in India. The number of authorized insurers now exceeds 12, and it continues to grow.

Since insurance constitutes only a tiny fraction of the economy, the overall significance of this one reform might seem slight. That assessment, however, misses a profound truth. Advances in economic development should not be measured according to what is, but according to what can be.

India is a land of enormous potential. Of the nations of the world, it ranks second in population, seventh in land mass, and at its current growth rate it will soon rank in the top ten in GDP. It is also a leader in information processing and technology.

Possibilities are one thing; reality is another. India's gap between the two is staggering. India is the world's pre-eminent example of a developing country. Its successes and failures in seeking a better life for its citizens send messages around the globe. Economists of many generations have recommended policies to promote development and alleviate poverty in India. They have at various times advocated centralized economic planning, import substitution, increased food production, meeting basic human needs, better education, family planning, improvements in the status of women, and a host of other measures. Only recently, however, have they come to understand development as an integrated process.

According to Amartya Sen, the 1998 Nobel laureate in economics, poverty cannot be adequately measured merely as insufficient income. Poverty is the deprivation of freedom. More important than how much money people have is what they can do with it. People are impoverished when they cannot do what they might wish. As they gain capabilities, their lives necessarily become better. Thus Sen describes development "as a process of expanding substantive freedoms that people have."

This focus on freedom facilitates an integrated view of development. In Sen's words:

> A variety of social institutions—related to the operation of markets, administrations, legislatures, political parties, nongovernmental organizations, the judiciary, the media and the community in general—contribute to the process of development through their effects on enhancing and sustaining individual freedoms....Values and ... social ethics are also part of the process of development..., along with the working of markets and other institutions.[1]

The new freedom in the insurance sector provides a clear illustration. People buy insurance to protect their families and assets from accidental losses. More than a hundred insurers operated in British India, but the overwhelming majority of the people could not buy insurance and perhaps did not even know of its existence. After independence the

[1]Amartya Sen, *Development as Freedom* (New York, 1999), p. 297.

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government nationalized the insurance industry to channel its services toward the entire population. The state companies effectively organized to serve the whole country, but only with a limited array of products offered at arbitrary prices. Now begins a new era, in which people will have the capability of managing their risks in a variety of ways.

To understand the importance of this new freedom, one should compare the risk management practices of other countries. Risk management is a structured process of rational decision making through a sequence of steps: identifying exposures to accidental loss, evaluating alternative techniques for treating each loss exposure, choosing the best alternative, implementing it, and monitoring the results to refine or improve the program. For most businesses, and even some individuals, it is standard procedure. The risk management process enables them to weigh the costs and benefits of higher insurance deductibles, sprinklers, safety training, or any imaginable combination of loss prevention and loss financing techniques. The freedom to allocate their resources to the most efficient ways of mitigating risk allows them to capture more of their potential.

One reason that economies fall short of their potential is the inevitable, but random occurrence of natural disasters, such as the Gujarat earthquake on January 26, 2001. Property losses exceeded $4 billion, but only about 5 percent were insured. The other 95 percent must now be financed with resources originally intended for other purposes, undermining the country's economic plan. Had insurance been more widespread in India, the earthquake would have caused less disruption of the economy.

The benefit of loss financing is, however, only half of the story. For developing countries in particular, loss prevention effects can be still greater, especially as the benefits compound over time. Investments in better buildings, for example, might have prevented a substantial portion of the earthquake damage. A vibrant insurance market provides information regarding costs and benefits that helps property owners calculate which prevention techniques are worthwhile. In the absence of such price signals from the insurance market, they resist making investments for the sake of unknown benefits. The resulting loss is unseen and too often forgotten: it is the cost of the damage that could have been prevented.

Under India's insurance monopoly, earthquake insurance could be added to a standard fire policy offered by one of the state companies. The additional premium for property valued at one lakh [100,000 rupees] is 10, 20, 50, or 100 rupees, depending on the zone in which the property is located. There is little data by which to judge whether these prices are appropriate, but since the state companies are cautious about the risks they assume, both the rates and the zones probably allow them some margin. As a result, many potential insureds forgo earthquake cover because they perceive it to be too expensive.

In a competitive market, one insurer or another will discover that it can profitably accept risks from some portions of the highest-rated zone for 60 or 70 rupees per lakh, inducing more people to purchase this protection against future earthquake losses. Some will be rejected, however, because they have not properly reinforced their structures or have not complied with building codes. Thus the competitive insurance market will also encourage more investment in loss prevention measures that will minimize losses—and save lives—in future earthquakes. Moreover, the accumulation of data used to support these decisions will enable greater precision as time goes by. Systematic risk management, supported by a flexible and efficient insurance market, focuses on what can be rather than what is. The freedom to make efficient decisions about risk will carry India a long way toward achieving its potential.

Full enjoyment of this opportunity, however, will depend on other capabilities. The Insurance Regulatory and Development Authority will need resources to supervise the solvency and performance of insurers effectively. Insurers will need competent and dedicated employees to meet rising consumer expectations. An increasingly educated populace must learn to manage risks efficiently, and they will require greater transparency to obtain the relevant decision-making information. These interdependent capabilities will reinforce each other, bringing new freedoms.

The possibilities exceed any one person's imagination. Suffice it to say that a free India can be a safe India, and a model of development for all.

IAIS Committee Meetings

During the January IAIS committee meetings in Kuala Lumpur, **Manuel Aguilera-Verduzco**, President of Mexico's National Commission of Insurance and Surety, was elected Chairman of the IAIS Executive Committee, succeeding Hanley Clark. The Education Subcommittee approved an extensive agenda for training emerging market supervisors, reflected in the calendar on the back page. The technical committee continued drafting principles on capital adequacy and solvency of insurers and released a draft standard on the evaluation of the reinsurance cover of primary insurers and the security of their reinsurers.

IIF Explores Solvency Supervision and Training with EU Commission

On January 29 and 30, IIF Program Coordinator **Sally Steel** and Research Director **Ian Webb** explored insurance regulatory and training issues with experts from the European Union Commission. They are shown here unfurling the EU flag held by **Michael Thom**. Revisions to the EU solvency margin requirements highlighted the discussions with Michael Thom and **José Manuel de Frutos Gomez** from the insurance unit from the European Commission. Additional discussions included **Dr. Peter Troberg** and **Johan Løvengreen** of the European Financial Expertise Network and **Aristide Forfolis** and **Piet Blonde** from the Technical Assistance and Information Exchange offices. These offices work to assist accession countries with meeting the convergence requirements for the financial services sector prior to accessing the European Union. Since the IIF works with the insurance supervisors of these same countries in IAIS educational seminars, coordination with the EU is essential.

Expanding Industry Partnerships

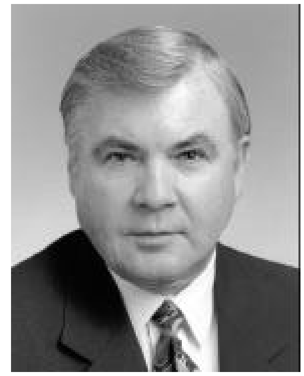
While in Brussels, **Sally Steel** also explored opportunities for cooperation with two important insurance industry organizations, the Comité Européen des Assurances (CEA) and the World Federation of Insurance Intermediaries (WFII). The CEA represents national insurance associations of the EU member countries, internationally and at the European level. It also assists the European Commission with training programs with regulators from EU accession countries, especially in Eastern Europe and Russia. **Jacques Léglu**, Interim Secretary General, and **Ivonka Trojanowska-Phillips**, CEA TTF Project Manager, spoke for the CEA in these discussions.

The WIIF is an umbrella organization coordinating the efforts of national intermediary organizations representing insurance intermediaries. As developing economies privatize state monopoly insurers and open their markets to competition, intermediaries will play a critical role in helping consumers manage their risks efficiently. Thus professional conduct and regulation of intermediaries is critical to the development of the insurance industry. The discussions with **Nic De Maesschalck**, Director of the WFII, identified several areas of future cooperation in IIF educational programs for emerging markets.

Planning for Technical Assistance in India Continues

In January IIF Research Director **Ian Webb** traveled to Mumbai and New Delhi for discussions with the Insurance Institute of India and the Insurance Regulatory and Development Authority. The Foundation is analyzing educational needs for a robust private insurance industry in India. The possibilities include technical training for the IRDA staff on a number of specific issues and cooperative programs to reinforce the capacity of insurance related educational bodies in India.

CIGNA International Renews as IIF Founding Member



When the International Insurance Foundation was established in 1996, CIGNA International was a Founding Member. Despite the sale of its property-casualty operations, CIGNA has reaffirmed its support for the Foundation. The President of CIGNA International, **Terry L. Kendall**, has accepted nomination to the IIF Board of Directors. In announcing this decision he said, "We look forward to actively contributing to the excellent efforts and programs of your organization to promote information exchanges among insurance supervisors and raise the global standards for sound insurance markets around the world."

Today CIGNA International offers health, life, pensions, and expatriate insurance products. CIGNA's private health insurance products, including managed health care and dental programs and indemnity coverages for groups and individuals, are customized to accommodate distinct government regulations and business requirements. The company offers an array of group and individual life and accident and health insurance products. CIGNA's pensions plans provide retirement and investment savings alternatives for employers and employees in companies of all sizes, in major markets such as Brazil and Japan. Expatriate programs include life, accidental death & dismemberment, medical, dental, vision, short- and long-term disability coverages for multinational employer groups, as well as primary medical benefits for international business travelers.

Calendar

March	**7-9**	**IIC Latin American Roundtable,** ***Miami***
March	**12-13**	**World Bank Disaster Risk Management Workshop,** ***San Pedro Sula, Honduras***
April	**17-20**	**IAIS Committee Meetings,** ***Basle, Switzerland***
April-May		**Insurance Institute of India Annual Conference,** ***Mumbai, India***
May	**2**	**IIC International Insurance Day Luncheon,** ***New York***
May	**22-23**	**IAIS Central and Eastern Europe Regional Seminar,** ***Budapest, Hungary***
June	**5-8**	**IAIS Latin American Executive Regional Seminar,** ***Buenos Aires, Argentina***
June	**27-29**	**Central and Eastern Europe Regional Seminar,** ***Gdansk, Poland***
July	**17-19**	**IAIS African Regional Seminar,** ***Pretoria, South Africa***
September	**18-20**	**IAIS Annual Conference,** ***Bonn, Germany***
October	**7-18**	**IIF - FUNENSEG Seminar,** ***Washington & Princeton***
November	**5-9**	**IAIS/ASSAL Latin American Executive Regional Seminar,** ***Lima, Peru***
November	**15-16**	**Annual IIF Board Meeting,** ***Washington***