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Global Groups – A Globalized Regulatory Approach?

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- Global bundling and cross-spreading of risk in groups
- Regulatory approaches to groups to date
- Experience with group supervision in Switzerland
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Global bundling and cross-spreading of risk in groups (1)

Recent financial turmoil demonstrates

- Bundling of various activities in one part of a group of companies may lead to cross-sectoral (financial) stress in other parts of that group
  - Example: Insurance/reinsurance combined with (investment) banking or other capital markets activities

- Financial exposures of a group in one market can in effect be "transported" to other markets where the group is active
  - Example: Capital/legal entity holding structure and intragroup financing can touch on several jurisdictions

Global bundling and cross-spreading of risk in groups (2)

The complexity resulting from the bundling and "transport" role of groups has a considerable potential for either

- Bringing benefits to their customers or impacting them adversely
- Rendering the markets more efficient or increasing the dependencies and vulnerabilities of markets
- Creating value for other markets in which the group is active or bringing to those markets risks originating elsewhere

An appropriate regulatory response should allow groups to enjoy the economic benefits of bundling while avoiding its potential of adverse effects

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Concept and current practice (1)

Concept 1

Traditionally, insurance regulation has mainly dealt with the supervision of a single legal entity only (solo approach)

- **Current practice**

  Many countries still today lack a legal basis or do not yet practice group supervision

Concept and current practice (2)

Concept 2

Group effects are considered for particular companies located in the relevant jurisdiction, but mainly on a unilateral basis, with a varying degree of exchange with regulators of other jurisdictions

- **Current practice**

  Group information received early consideration by the Holding Company Acts of U.S. states

  Exchange of information based on bilateral or multilateral Memoranda of Understanding

Concept and current practice (3)

Concept 3

Extending the reach of the unilateral approach to the group as a whole, with increasing information exchange

- **Current practice**
  - EU Insurance Group and Conglomerates Directive
    - Coordination Committee Meetings under the chair of a mutually agreed Lead Coordinator
  - New Swiss Insurance Supervisory Law (2006)

Concept and current practice (4)

Concept 4

Group supervision achieved through multinational recognition of foreign supervisory activities based on an allocation of responsibilities among the group supervisor and supervisors of subsidiaries in other countries

- **Current practice**

  Project existing in the EU with the Draft Solvency II Directive (still unilateral approach vis-à-vis third countries)

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Groups and conglomerates in Switzerland

- Addressed by art. 64 et seq. of the new Insurance Supervisory Act (2006) and by the respective Ordinance and Directives
- Today nine insurance “groups” (at least one insurance undertaking) and “conglomerates” (at least one insurance undertaking as well as substantial banking or securities dealer activities) are directed from Switzerland and are under group supervision in Switzerland
- There are also subsidiaries of major foreign groups active in Switzerland

Swiss Integrated Insurance Supervision (1)

Based on the Swiss experience, an integrated approach is key for supervising groups (we call it “Swiss Integrated Insurance Supervision”, also applicable to legal entities). This necessitates first an assessment of the group context.

- Assessment of the group context
  - Mapping the group organization, structure and activities and its governance
  - Understanding the strategy of the group

Swiss Integrated Insurance Supervision (2)

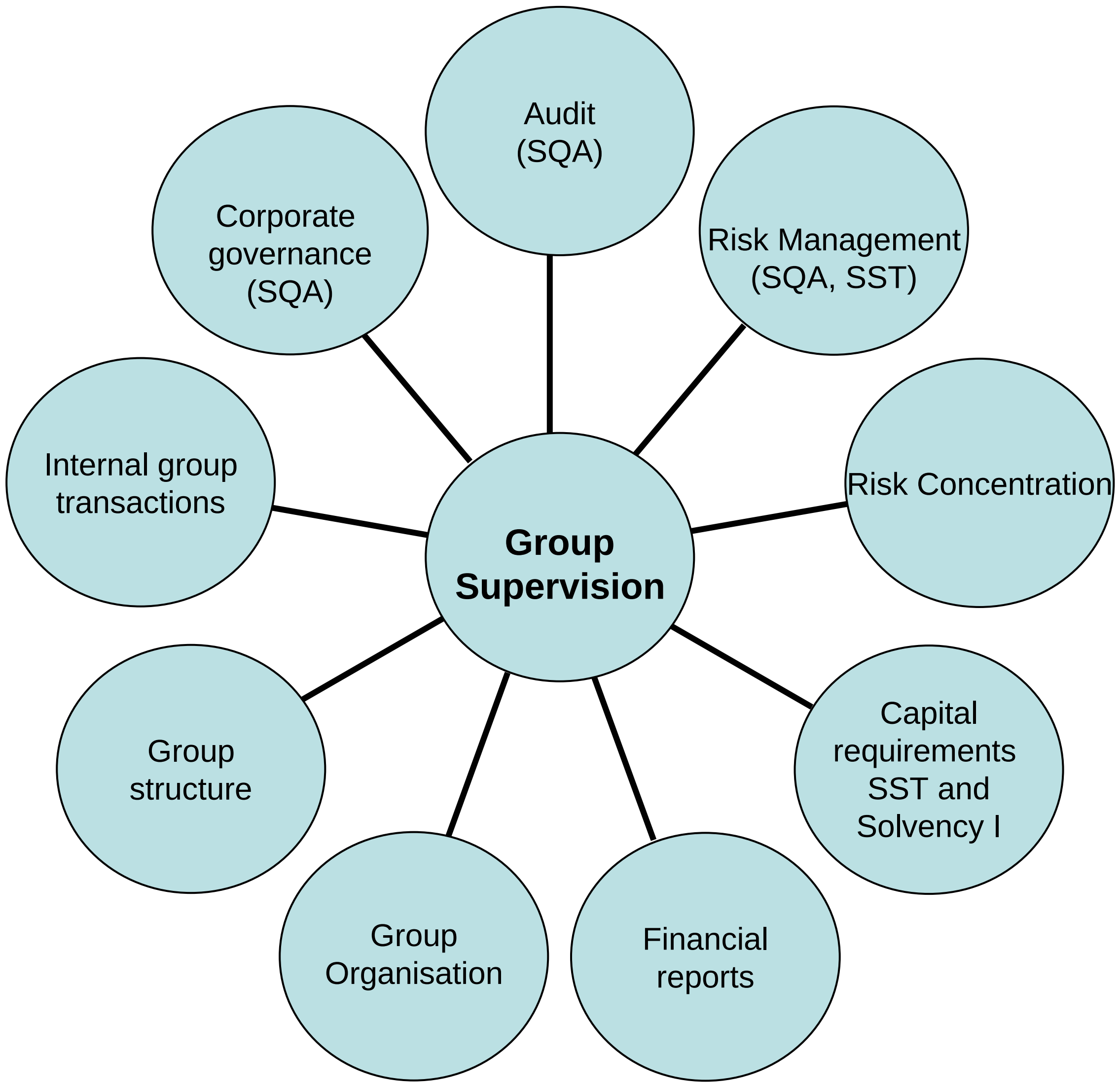
- Implementation of Swiss Integrated Insurance Supervision
  - *Quantitative supervision*
    - Assessment of capital adequacy on an economic basis (Swiss Solvency Test)
    - Financial performance
    - Risk distribution and cumulation
    - Intragroup transactions etc.

Swiss Integrated Insurance Supervision (3)

- *Qualitative supervision*
  - Corporate governance and risk management/internal controls through Swiss Quality Assessments
  - Fitness and properness of corporate bodies
  - Requirements on external and internal audit, actuary, etc.

- *Traditional tools of supervision*
  - Reporting
  - Technical reserves
  - Tied assets
  - Solvency I etc.

Swiss Integrated Insurance Supervision (4)



Organizational focus of Swiss group supervision (1)

- *Integrated and multidisciplinary approach within the supervisory authority*
  - Close cooperation between group supervision and other functions
  - Involvement of all specialist functions
- *Intensive and regular interaction with the groups under supervision*
  - Key account management on senior level to interact with Board of Directors and senior management of the group
  - Written reporting on all key matters
  - Onsite reviews
  - Ad hoc information from the group
  - Regular meetings and calls

Organizational focus of Swiss group supervision (2)

- *International cooperation*

  - Supervisory colleges to be expanded
    - Definition of information flow
    - Allocation of tasks among group and subsidiary regulators to take place over time
    - Crisis management

  - Information exchange (MoUs in existence, MMoU in preparation)

  - Active contribution in international fora

Essence of Swiss experience

Switzerland currently practising a Concept 3 group supervision

Strong focus on a multidisciplinary integrated approach

Development and implementation of Concept 4 that is recognisable in as many jurisdictions as possible is desirable

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Thoughts on the design of a way forward (1)

- Establishing a multilateral approach is under intensive discussion within the European Union.
- However, the Solvency II model would still show vis-à-vis third countries the characteristics of a unilateral approach where the equivalency of the regulation of another country would require prior assessment.
- Thus, developing a group supervisory regime on a truly international basis that can be recognised in as many countries as possible still remains to be explored.

Thoughts on the design of a way forward (2)

- Such a truly international supervisory regime could be composed of blocks of minimum standards regarding either

  - *Quantitative supervision*
    Solvency standards on an economic basis

  - *Qualitative supervision* regarding
    - Corporate governance standards
    - Risk management standards
    - Internal controls
    - Auditing etc.

  - *Traditional supervision*
    - Reporting requirements etc.

Thoughts on the design of a way forward (3)

- The national regulator would have the choice to adopt
  - one, several or all the blocks
  - the regime as the only one applicable to all supervised entities or as an internationally recognizable regime to accompany a national regime
  - additional requirements to enrich the minimum standards
- Those countries which adopt the internationally recognizable minimum standards would be able to rely on defined regulatory actions by regulators in other adopting countries

Thoughts on the design of a way forward (4)

- In the absence of local adoption of the minimum standards groups themselves could submit voluntarily to these standards. This could help
  - facilitate recognition in those countries that have adopted the standards
  - stimulate interest in other countries to adopt the standards

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Conclusions

Groups could have considerable beneficial or potentially adverse effects on national economies and thus require an adequate regulatory response.

A solid minimum regulatory approach that is recognisable in as many jurisdictions as possible may serve as a basis for such a response.

Development agents are needed!