



Interview

“ Economic Development will encourage the insurance culture in emerging markets ”

Manuel Aguilera-Verduzco

President of the International Association of Insurance Supervisors (IAIS) and President of the National Committee for Insurance and Securities (CNSF: Comisión Nacional de Seguros y Fianzas) of Mexico.

It is not an easy task to discover the role played by insurance in the world, nor is it within the power of everybody to do so.

In the course of this interview, the President of the International Association of Insurance Supervisors (IAIS) reveals the key points about this organisation, which is dedicated to contributing towards international financial stability by the introduction of standards for regulation and supervision of insurance throughout the world. Its influence in promoting and controlling the insurance business is decisive.

The IAIS, together with the Basle Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO), is one of the three pillars of the Coordinating Group for Financial Supervision and is committed to the Financial Sector Assessment Program (FSAP), which various multilateral agencies support.



Manuel Aguilera-Verduzco was born on 26 November 1960 in the city of San Luis Potosí, Mexico. He received his degree in economics from Veracruzana University, a diploma in Economic Planning from the Central School of Planning and Statistics in Warsaw, Poland, and one also from the Alta Dirección de Entidades Públicas (Senior Management of Public Institutions), at the Instituto Nacional de Administración Pública (National Institute for Public Administration) in Mexico.

He is President of the National Committee for Insurance and Securities (CNSF: Comisión Nacional de Seguros y Fianzas) of Mexico, in which he began to work in 1993 before becoming its head in 1998. As executive responsible for supervising the Mexican insurance and guarantee market, he has ample experience in the regulation of solvency. Amongst the duties that he performs as head of CNSF, he has participated and continues to take an active part in the implementation of reforms aimed at modernising the regulatory framework that governs the Mexican insurance and guarantee market.

Since 2001 he has been President of the Executive Committee of the International Association of Insurance Supervisors (IAIS). He is also an active participant in the Association of Insurance Superintendents in Latin America (ASSAL: Asociación de Superintendentes de Seguros de América Latina), where he is in charge of the Grupo de Estándares de Solvencia (Solvency Standards Group). He is also a member of the Advisory Group of the “Centro Internacional de Liderazgo de Toronto para la Supervisión del Sector Financiero” (Toronto International Leadership Centre for the Supervision of the Financial Sector).



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What does insurance contribute to the market economies?

In general terms through its systems for providing protection and indemnity, insurance supplies stability for the functioning of the economy and security to economic agents against possible harm occasioned by different factors.

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Furthermore, in their role as institutional investors, insurance companies constitute an effective means of channelling medium and long term savings towards financing productive economic activity in different spheres.

What are the new focal points of supervision?

In the last decade regulation and supervision of financial activities have been altered in line with international liberalisation and deregulation procedures. Modern practice demands that the supervising body establishes prudent rules in connection with fundamental aspects of the insurance industry, with the focus based on risk analysis and its impact on corporate solvency, in accordance with an environment of free competition. Under this system the supervisor relies on the collaboration of independent third parties, such as external auditors and actuaries, and on good corporate management practices and internal controls established by the insurance companies themselves.

What are the origins of the IAIS and what role does it play?

The International Association of Insurance Supervisors celebrates its tenth anniversary in 2004. It was set up in 1994 to promote cooperation between insurance sector supervisors internationally, and to create institutional links with supervisors of other financial sectors. In its early years the Association was made up of a small group of authorities who were entrusted with the supervision and regulation of insurance and its purpose was restricted to the exchange of information and experience. Those early endeavours have been extended today to the coordination of tasks that contribute to the development of supervision of the insurance industry internationally.

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These tasks concentrate on establishing and implementing standards that reflect the accepted international best practice for achieving greater effectiveness of supervision systems. In the IAIS, insurance supervisors and regulators from more than 100 jurisdictions participate with a total of 131 members. Furthermore, since 1999 more than 70 bodies have joined as observers. These representatives come from the insurance industry, professional associations, insurance and reinsurance companies, consultants and international financial organisations, who benefit the Association by offering their views.

After holding the 10th annual conference of the IAIS in Singapore, which topics concern the insurance supervisors and what were the conclusions reached at the meeting?

The IAIS's annual conferences are an ideal opportunity to report on the work done by the Association's different committees and working parties, and they also allow us to hear the views of members present, to identify new topics and consider their significance.

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The 10th annual conference held last October was attended by about 400 insurance supervisors and professionals and on this occasion the general Meeting adopted the Basic Principles of Insurance and its methodology. The review of the Basic Principles of Insurance was the result of collaboration by various jurisdictions throughout the world, from both developed and emerging economies. Furthermore, this new edition of the Basic Principles of Insurance also incorporates the views of the World Bank and the International Monetary Fund, who have adopted this document in their assessments of the financial sector. The General Meeting established a standard for supervision of reinsurance, which seeks to strengthen the framework of supervision at international level. Another important matter for the IAIS is to make common cause with the approach to assessment of adequate capital and solvency; the Meeting approved four documents which aim to take this matter further:



▶ Quantification and assessment of insurance liabilities.

▶ The role of actuaries as part of the supervising model.

▶ Levels of solvency control.

▶ Stress tests for insurers.

With regard to the development of standards, IAIS restated its priorities for the coming years: accounting, capital requirements and solvency, reinsurance, electronic trading and combating money laundering and financing terrorist activities.

What are the objectives of supervision?

Basically these consist of the development of stable and efficient markets for the benefit and protection of insured parties. The IAIS's Basic Principles of Insurance states that an insurer must obtain authorisation before being allowed to operate in any given jurisdiction. The requirements for obtaining authorisation are clear and objective. Insuring bodies that participate in the financial markets are expected to show their ability to operate on a sound basis that protects the interests of the insured. A further basic principle refers to the suitability of those engaged in running a given company, who are expected to display integrity, competence and proven experience in addition to being adequately qualified. It is important for insurance companies to have efficient corporate governance mechanisms so as to promote transparency and reliability in management and encourage confidence, stability and integrity in financial markets. A fundamental aspect amongst the objectives for protecting the interests of insured parties is the solvency of the insurance companies; in

How is insurance developing in Mexico?

The level of penetration of the insurance sector reached 2% of GDP at the end of 2002. Growth in the sector has been maintained in recent years; in 1996 it was only 1.2% of GDP and in 2001 it stood at 1.7% of GDP.

The sector looks set for a high level of growth in forthcoming years because the foundations have been laid. A regulatory framework that is both stable and clear, and whose amendments began in 1993 and terminated with others undertaken in 2002, have contributed to this situation. The arrival of new foreign players has led to a less concentrated and more competitive market.

The increase in competition has encouraged the introduction of new technology and more complex products that seek to adapt themselves to clients' characteristics and financial situations. Life assurance easily represents the greatest contribution to growth in recent years.

The future of substantial insurance business in Mexico will be tied up with products that combine life assurance with medium and long term savings components. Insurance sold by banks in the last three years has been very active in Mexico, with some insurance companies relying solely on this distribution channel.

Furthermore, the low commission on this sales method allows companies to reach persons from lower income brackets by selling 'packaged' products that include life assurance and asset protection cover.

Finally, in an overall analysis of the Mexican insurance sector in recent years, it was seen as a consolidated market that is experiencing rapid growth. Premium growth is in excess of that for the economy in general, and the sector has become one of the most dynamic in the country and indeed in Latin America.



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other words their financial ability to honour the obligations arising from the contracts they underwrite. Supervision must demand that insurance companies hold resources which allow them to cover potential departures from both their technical and financial assumptions and must also require them to provide the necessary information to customers both before and after signing the contract. This highlights the need to develop prudent regulation and supervision procedures that counteract the conflicts of interest of the parties involved in the insurance industry. The international tendency to include auditors with supervisory powers on the board of directors, in addition to the expansion of the role of actuaries, constitutes a good example of external control mechanisms. International progress in the incorporation of accounting standards and the exchange of information on reinsurance are also becoming apparent. The new edition of Basic Principles of Insurance has underlined the need for supervisors to intervene in the prevention of illicit activities such as fraud, money laundering, and the financing of terrorism; not only are they harmful to society, they also undermine confidence in the entire financial system.

We are part of a global world, in which many problems and solutions are common and may be shared. If we look at the planet by regions, what are the principal concerns with regard to insurance?

Market globalisation and liberalisation of the economies have characterised

economic policy in the last two decades. In the emerging economies this has meant important changes in the structure of the markets, which have been stimulated by new products, technology and commercial practices. It has also been necessary to adjust the legislative and supervisory frameworks to make them more efficient. Generally, in emerging markets insurance has a relatively low level of penetration, which is due to the fact that the insurance culture has yet to develop. There is much to do, both from the viewpoint of developing insurance and attending to social and economic problems. In the developed countries industry's concerns focus on other matters, such as the impact of low interest rates or the fall in the stock markets, which exert pressure on insurance companies to obtain resources to be able to comply with their obligations, especially with regard to investment-linked products and guaranteed stocks.

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The topic of retirement pensions as a mechanism for financing social security systems continues to be of great importance in many markets. Perhaps, however, the most important amongst the entire range of matters that take up the attention of the industry and supervisors throughout the world, is that day-by-day

there is a stronger international view that all the solutions to any of these topics must be taken into account in order to maintain the health and stability of the markets.

Has not the lack of confidence shown by the rating agencies towards the leading figures in the industry been somewhat exaggerated?

This is an interesting subject. As insurance supervisors we have not reached a consensus on the role played by the ratings assigned by the agencies, and this is also the case with regard to the part played by the formal supervisory systems. For example in some jurisdictions, from the solvency point of view, ratings given to reinsurance companies are taken into account, because they represent an instrument for measuring the credit risk of insurers that they supervise when they cede business to the reinsurer. It is true that the effects of 11 September 2001 in the United States have taken their toll on the principal reinsurers. It is also true that both the losses from terrorist attacks and the fact that many reinsurance companies are not subject to regulation and supervision, have been important factors in the way the markets view the financial strength of these institutions. In spite of the foregoing, I believe it is important to point out that the rating agencies do not do the work of supervisors, however they can complement it because an independent opinion will always prove useful.



With regard to the European Union and the guidelines of the Basle Committee, which when applied to insurance is called Solvency II, is everything leading the companies towards single capital and solvency standards?

Unlike what occurs in the regulation of banking activities, in which there are established standards for capital requirements, in the insurance industry there are several models of capitalisation that are used internationally. All of them, however, consider in one way or another, the risks faced by an insurance company. One of the IAIS's medium-term projects relates to establishing a model for capital requests which, possibly, may be universally adopted. The four documents approved at the Association's General Meeting in Singapore represent progress in this respect.

The new International Accounting Standard (IAS), which will soon come into effect in the European Union, aim to draw closer to the accounting procedures that exist in North America. What effect and what repercussions will they have on insurance?

The IAIS has played an active part in the project to establish the new IAS in the insurance sector. It is a project that is also included within the framework of the financial supervisors' concern for developing the foundations of international financial stability.

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In view of the ageing of the world population, what role are pension plans likely to play?

One of the greatest challenges of any society, especially in the case of developing countries, is to prepare for the changes and consequences of an ageing population in the forthcoming decade, through development of systems that can support a greater number of retired persons without pushing the economy into debt or exceeding tax resources. In this connection pension plans and the development of products relating to the needs of the market and the population become important. Furthermore, this

type of insurance has become a leading participant in long-term savings, given that these schemes have long-term liabilities and hence are converted into institutional investors who seek to guarantee their return for the longest possible term. In this fashion the companies can finance long-term projects and gradually they are succeeding in creating a market in debt investment with a view to the financial build-up of resources.

With regard to reinsurance, what is your view of the ever more frequent use of Alternative Risk Transfer (ART)?

The reinsurance business is one the reasons that helps explain the dynamic nature and innovation of the insurance sector throughout the world. Rapid development of the financial markets has led to the search for new methods to transfer and spread the risks more efficiently.

In recent years, financial reinsurance and more generally the so-called “alternative risk transfer” has led to the design and execution of new systems, that are not only innovative as regards the traditional transfer of insurance risks, but also for the purpose of carrying this out between different types of financial intermediaries. While these activities provide greater flexibility for risk transfer, especially between financial intermediaries, it is also necessary for regulators and supervisors to pay special attention to ensure that the main attraction for using this method is not the possibility of inappropriate arbitrage operations.

Regulation and supervision

How does the IAIS organise itself to fulfil its duties?

The General Meeting has delegated to the executive committee the task of coordinating the Association. Different world regions are represented on this committee. In addition to the executive committee, the Assembly is supported by a technical committee which is in charge of developing standards, an emerging markets committee and a budget committee. The IAIS has a permanent secretariat, whose head office is in Basle, Switzerland.

The duties of the IAIS consist of developing international standards in connection with the regulation and supervision of insurance; implementation of these insurance standards is also carried out through training and the organisation also makes a notable contribution towards international efforts to create the basis for lasting financial stability. The IAIS has strengthened cooperation mechanisms with regulators of other financial sectors where there is interaction with insurance. Last year it presided over the "Grupo de Coordinación para la Supervisión Financiera" (Coordination Group for Financial Supervision), which is made up of the presidents and secretary generals of the international associations of supervisors of the three financial sectors: the Basle Committee on Banking Supervision (BCBS); the International Organisation of Security Committees (IOSCO); and the International Association of Insurance Supervisors (IAIS); as well as by those in the Joint Forum. The Association also participates in the Forum for Financial Stability.

What are the basic principles of insurance that the IAIS defends?

If we start from the premise that its principal task is to contribute to international financial stability by implementing regulatory and supervisory standards for insurance throughout the world, then Basic Principles of Insurance can claim to provide the framework for action. The first Principles were adopted at the General Meeting in October 2000. These have been used by the International Monetary Fund and the World Bank as guidelines for improving international practice in the Financial Sector Assessment Program (FSAP) that both international financial organisations commenced that year. With effect from that date, however, there have been important changes.

Greater opening-up of the markets, together with the phenomenon of financial convergence, made it necessary to update the entire supervision framework. Consequently, from mid-2002 the Association undertook the revision of Basic Principles of Insurance and its methodology, for the purpose of strengthening them and so that they would continue to provide an appropriate framework in order to achieve effective supervision. The new version of Basic Principles of Insurance was adopted by the General Assembly of the Association in October 2003 and it includes 28 principles covering all aspects of supervision, from authorisation of insurance companies to their departure and withdrawal from the market. These principles cover six areas:

I. Conditions for effective insurance supervision.

II. System of supervision.

III. The supervised entity.

IV. Supervision in progress.

V. Prudential requirements.

VI. Market and consumers.

Detailed information on each of the above, as well as on the standards approved by the Association, is available in several languages on our website: www.iaisweb.org

How are IAIS's relationships with other international institutions?

The standards established by the IAIS aim to provide the supervisor with a basic set of principles that are applicable internationally on insurance matters; they are not, however compulsory. The Association helps to assess the level of compliance of its members with regard to insurance supervision standards, and this is done in strict collaboration with the International Monetary Fund and the World Bank, which are the bodies charged with carrying out the assessments within the framework of the Financial Sector Assessment Programme (FSAP) in the different countries. The Association has a list of insurance experts who work in the preparation of these assessments. One of their aims is to establish international compliance guidelines, which facilitates the comparison of a national supervision system with the level of compliance with standards in other jurisdictions. ■



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