



Group-wide Supervision



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2nd International Insurance Supervision Seminar on
Core Supervisory Issues

9 August 2006



Agenda

- I. What is group wide supervision?**
- II. Insurance Core Principles and other IAIS documents
- III. Other international forums
- IV. Elements of group wide supervision
- V. Supervisory cooperation



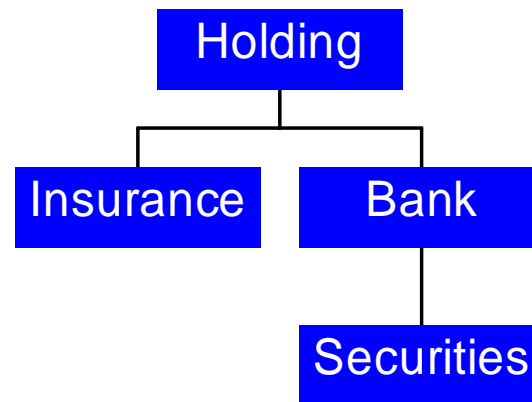
I. What is group wide supervision?

- Definitions
 - Group wide supervision
 - A supervisory approach to a financial group which considers the group structure, the constituent licensed entities and all the interrelationships within that financial group



I. What is group wide supervision?

- Definitions
 - Financial group (financial conglomerate)
 - Any group of companies under common control whose exclusive or predominant activities consist of providing significant services in at least two different financial sectors (insurance, banking, securities)
 - Example



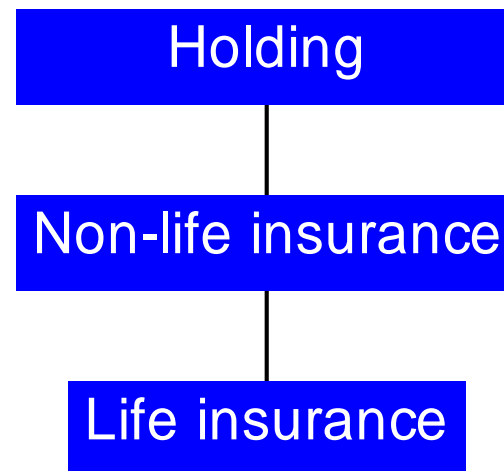


I. What is group wide supervision?

- Definitions

- Insurance group

- A financial group that consists of two or more insurers (and possibly other non-licensed entities)
 - Example



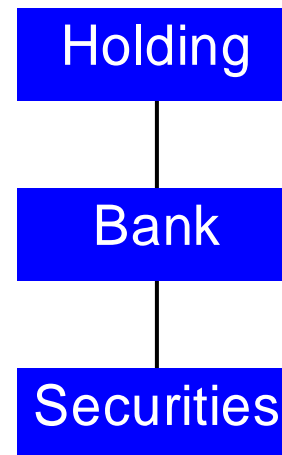


I. What is group wide supervision?

- Definitions

- Banking group

- A financial group that consists of two or more banks (or securities firms) (and possibly other non-licensed entities)
 - Example





I. What is group wide supervision?

- Methods applied in group wide supervision
 - Solo-plus supervision
 - A supervisory group approach that combines the solo supervision applied to all licensed financial entities with a mainly qualitative assessment of the group as a whole, by considering all group relations that could have an impact on the financial position of the individual entities, with special attention to capital adequacy, risk concentration, intra-group transactions and exposures etc.



I. What is group wide supervision?

- Methods applied in group-wide supervision
 - Consolidated supervision
 - A supervisory group approach that focuses on the total of individual (licensed or not) entities of the entire group, consolidated at the level of the top holding (or regulated) company. In this case the solvency requirements and other supervisory requirements are applied to the group as a whole.
 - The group is seen as one economic entity.



I. What is group wide supervision?

Group risks

- Risks to regulated entities belonging to a group - originating from the group - in addition to the risk inherent in being an insurer, a bank or a securities firm
- The fact that regulated entities are part of a group alters, often considerably, their risk profile, the financial position, the role of their management, and their business strategy



I. What is group wide supervision?

- **Double gearing**
 - Occurs whenever one entity holds regulatory capital issued by another entity within the same group and the issuer is allowed to count the capital in its own balance sheet
- **Capital leverage**
 - Occurs when the parent issues debt and downstreams the proceeds to a dependent in the form of equity or other elements of regulatory capital



I. What is group wide supervision?

- Conflicts of interest
 - Occur when the Board of Directors and the Management of individual group entities do not have sufficient autonomy and authority
 - Firewalls, Chinese walls?
- Contagion
 - Occurs when problems in one part of the group spread to other parts of the group
 - Reputation risk
 - Example: cross default clauses



I. What is group wide supervision?

- Risk concentration
 - An exposure with the potential to produce losses large enough to threaten a financial institution's or a group's health or ability to maintain its core operations
- Intra-group transactions and exposures
 - The risk that capital or income is transferred from one group company to another group company through the pricing of transactions (terms and conditions)



Agenda

- I. What is group wide supervision?
- II. Insurance Core Principles and other IAIS documents**
- III. Other international forums
- IV. Elements of group wide supervision
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II. Insurance Core Principles and other IAIS documents

- Insurance Core Principle 17
 - “The supervisory authority supervises its insurers on a solo and a group-wide basis to avoid the consequences of double gearing and to assess the risk profile of the whole group”



II. Insurance Core Principles and other IAIS documents

- Group wide supervision includes
 - Group structure and interrelationships
 - Capital adequacy
 - Risk concentration
 - Intra-group transactions and exposures
 - Internal control mechanisms and risk management
 - Fit and proper testing



II. Insurance Core Principles and other IAIS documents

- Supervisors should
 - Define what constitutes an insurance group and a financial conglomerate
 - Ensure effective and efficient group-wide supervision
 - Ensure appropriate co-operation and co-ordination



II. Insurance Core Principles and other IAIS documents

- Supervisors should
 - Monitor
 - Group structure and interrelationships
 - Reinsurance and risk concentration
 - Intra-group transactions and exposures
 - Capital adequacy
 - Internal control mechanisms and risk management
 - Fit and proper testing
 - Adequate reporting systems
- Supervisors may deny or withdraw the license when the group structure hinders effective supervision



II. Insurance Core Principles and other IAIS documents

- Other relevant Insurance Core Principles
 - ICP 5: Supervisory Co-operation and information Sharing
 - ICP 8: Changes in Control and Portfolio Transfers



II. Insurance Core Principles and other IAIS documents

- Principles Applicable to the Supervision of International Insurers and Insurance Groups and their Cross-Border Business Operations (Insurance Concordat)
 - Focuses on principles for cooperation between supervisors in the supervision of foreign business operations of international insurers and insurance groups
 - Covers co-operation between home and host supervisors



II. Insurance Core Principles and other IAIS documents

- Supervisory Standard on Group Coordination
 - Supervisory Standard No. 5, adopted in October 2000
 - Addresses prudential issues arising from the activities of international financial groups
 - Is intended to facilitate the development of coordination and information sharing



II. Insurance Core Principles and other IAIS documents

- Issues Paper: Assessing the IAIS's Requirements on Cross-Border and Cross-Sector Cooperation and Information Exchange, May 2005
- Compilation of Insurance core principles, standards and guidance on cross-border and cross-sector cooperation and information exchange, October 2005



II. Insurance Core Principles and other IAIS documents

- Current activities within the IAIS
 - Multilateral Memorandum of Understanding
 - Will facilitate co-operation and information exchange among supervisors
 - Participation voluntary
 - Confidentiality and professional secrecy ensured
 - To be adopted in 2007
 - A survey on the definition of “Group” and “Financial Conglomerate”
 - Purpose: First step in drafting a standard on group supervision



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III. Other international forums

The Joint forum

- Recent publications from the Joint Forum
 - *The management of liquidity risk in financial groups, 2006*
 - *Regulatory and market differences: issues and observations, 2006*
- Current work in progress
 - Risk concentrations
 - Conduct of business/customer suitability
 - Stocktaking on supervisors' implementation of the Joint Forum Principles for the supervision of financial conglomerates
 - www.bis.org/bcbs/jointforum.htm



III. Other international forums

- The European Union
 - The Insurance Groups Directive (98/78/EC)
 - The Helsinki Protocol
 - CEIOPS Insurance Groups Supervision Committee
 - The Financial Conglomerates Directive (2002/87/CE)
 - Co-ordination committees (for each conglomerate)
 - Solvency II



III. Other international forums

- Links to the European Union and CEIOPS
 - http://ec.europa.eu/internal_market/insurance/groups_en.htm
 - http://www.ceiops.org/media/files/publications/protocols/nl194_helsinki_gbfi.pdf
 - http://ec.europa.eu/internal_market/financial-conglomerates/supervision_en.htm
 - <http://www.ceiops.org/content/view/14/18/>



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IV. Elements of group wide supervision

- Group wide supervision relevant
 - At the time of licensing
 - At the time of approval of change of control
 - Ongoing off-site
 - On-site



IV. Elements of group wide supervision

- As part of the process of licensing an insurer the supervisor should evaluate:
 - Group capital adequacy
 - Intra-group transactions and exposures
 - Group structure
 - License should be refused (or revoked) if the group structure hinders effective supervision
 - Risk concentrations
 - Fitness and propriety of Management, Board and important owners of parent and other group companies
- ... and consult with other supervisors



IV. Elements of group wide supervision

- As part of the process of approval of change of control the supervisor should evaluate:
 - Group capital adequacy
 - Intra-group transactions and exposures
 - Group structure
 - Risk concentrations
 - Fitness and propriety of Management, Board and important owners of parent and other group companies
- ... and consult with other supervisors



IV. Elements of group wide supervision

- As part of the ongoing off-site supervision the supervisor should evaluate:
 - Group capital adequacy
 - Intra-group transactions and exposures
 - Group structure
 - Risk concentrations
 - Fitness and propriety of Management, Board and important owners of parent and other group companies
- ... and consult with other supervisors



IV. Elements of group wide supervision

- As part of an on-site inspection the supervisor should evaluate:
 - Group capital adequacy
 - Intra-group transactions and exposures
 - Any conflicts of interests
 - Risk management, control and reporting
- Before conducting an inspection the supervisor may consult with other supervisors
- Any material findings may be communicated to other supervisors



IV. Elements of group wide supervision

- Capital adequacy
 - Assessing the capital adequacy of the group in order to:
 - Detect and provide for situations of double gearing
 - Detect and provide for situations where parent issues debt and downstreams it in the form of capital
 - Consider double gearing and capital leverage through unregulated holding companies as well
 - Address risks in unregulated entities
 - Treat of minority interests and majority interests in a sound manner



IV. Elements of group wide supervision

- Methods to assess capital adequacy
 - Measurement techniques
 - Building-block approach
 - Risk based aggregation approach
 - Risk-based deduction approach
 - Total deduction
 - Other prudent techniques may be developed in the future
 - Other relevant factors
 - The definition of regulatory capital
 - Accounting principles
 - Unregulated entities
 - Minority and majority interests



IV. Elements of group wide supervision

- Intra-group transactions and exposures
 - Can facilitate synergies
 - Represent avenues of contagion
 - Can complicate resolution of failures
 - Can result in capital or income being inappropriately transferred from the regulated entity
 - Can adversely affect solvency, liquidity and profitability of regulated entities
 - May be used for supervisory arbitrage



IV. Elements of group wide supervision

- Intra-group transactions and exposures
 - Origin of intra-group transactions and exposures
 - Cross shareholdings
 - Trading operations
 - Management of short term liquidity
 - Guarantees, loans and commitments
 - Service arrangements
 - Exposures to major shareholders
 - Placement of client assets
 - Purchases or sales of assets
 - Reinsurance



IV. Elements of group wide supervision

- Intra-group transactions and exposures
 - Example of supervisory measures
 - Board to set general guidelines
 - Management to set procedures
 - Management information and reporting
 - Transactions to be conducted at arm's length terms and conditions, and documented in writing
 - Limits to be set to intra-group exposures
 - The auditor to review intra-group transactions and exposures, and certify that they have caused no threat to regulated entities
 - Disclosure of material intra-group transactions and exposures
 - Supervisor to focus on risk profile and interconnectedness



IV. Elements of group wide supervision

- Risk concentrations
 - Forms of risk concentrations: Exposures to
 - Individual counterparties
 - Groups of counterparties or related entities
 - Industry sectors
 - Specific products
 - Service providers
 - Natural disasters or catastrophes



IV. Elements of group wide supervision

- Risk concentrations
 - Regulation
 - Reporting
 - Limits
 - Prior approval
 - Require appropriate risk management and control
 - Policies and procedures, and management information systems
 - Identify, measure, monitor, and control
 - Stress and scenario testing - where appropriate
 - Disclosure
 - Auditors to evaluate
 - The appropriateness of policies and procedures
 - Material risk concentrations that have a detrimental effect



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V. Supervisory cooperation

- Co-ordination and co-operation with supervisors of other group companies
 - Formal agreements and co-ordination committees
 - MoU
 - Other co-operation agreements
 - Co-ordinator/lead supervisor
 - Home/host supervisor
 - Ongoing and in crisis situations
 - Ad hoc
 - Confidentiality



International Association of Insurance Supervisors (IAIS)

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Group wide supervision

- Any questions?

