



Global  
Federation  
of Insurance  
Associations  
Annual Report  
2015–2016



# Annual Report 2015–2016



The Global Federation of Insurance Associations (GFIA), established in October 2012, represents through its 41 member associations the interests of insurers and reinsurers in 60 countries. These companies account for 87% of total insurance premiums worldwide, amounting to more than \$4 trillion. GFIA is incorporated in Switzerland and its secretariat is based in Brussels.

## Glossary

EC	European Commission	IAIS	International Association of Insurance Supervisors
EU	European Union	IMF	International Monetary Fund
FSB	Financial Stability Board	OECD	Organisation for Economic Co-operation & Development
G7	Group of Seven industrialised nations	UN	United Nations
G20	Group of Twenty major economies	WTO	World Trade Organization
GAAP	generally accepted accounting principles		
GDP	gross domestic product		

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GFIA president  
**Governor Dirk Kempthorne**  
President & CEO  
*American Council of Life Insurers*

## Foreword

GFIA is celebrating its fourth anniversary this year. It is astonishing that before 2012 the world's national and regional insurance associations did not have one global federation to represent their collective interests. The appetite for such a body in 2012 was clear, with 32 associations signing on as founding members. That appetite has only grown, as currently we have 41 members.

We are living in a time of rapidly increasing globalization, We are also witnessing immense political and economic shifts in markets large and small — for better or for worse. A global federation that can represent the broad-based, cross-cutting spectrum of the insurance industry in talks with the G20, the OECD, the IAIS, the FSB and other international bodies is, I would argue, absolutely essential.

The leaders of the G20 jurisdictions continue to send strong signals through their policy recommendations about the role of the insurance sector in supporting growth and investment. GFIA has established firm links not only with the G20 but also with its B20 business advisory group.

In 2016, the Chinese government held the G20 presidency. Members of GFIA's executive committee met representatives of the Chinese government in April 2016 and discussed how the goals of insurers align with those of the G20. In particular, we focused on how insurers can contribute to growth, investment, trade and financial inclusion.

GFIA's executives had a productive discussion with the Chinese Ministry of Foreign Affairs, which led the G20 secretariat. Talks focused on how our industry supports the G20 objectives of invigorating investment and global trade, improving connectivity and infrastructure, and promoting inclusive economies. The Chinese Insurance Regulatory Commission (CIRC) confirmed that insurance is fundamental to policymakers, in China and worldwide, who are working towards addressing the retirement gap, stimulating GDP growth and increasing institutional investment.

GFIA also engaged with the B20 and subsequently welcomed several of its 2016 Policy Recommendations. For example, the B20 recommends reassessing the impact of recent and planned financial rules and conducting an independent cost/benefit analysis of new global and liquidity standards for insurance.

Meanwhile, the global regulatory landscape for insurers continues to evolve, most visibly in the ongoing work of the IAIS. In recent years, we have engaged in several IAIS workstreams related to systemic risk. This year, the IAIS updated its work on systemic risk measures. However, the viability of the implementation of these policy proposals remains in question. In addition, its project to develop a global risk-based insurance capital standard (ICS) passed another major milestone in October with the completion of its second consultation. GFIA is following this ambitious project very closely, especially the challenging issues of comparability and implementation. Our coverage of the ICS and the IAIS's related ComFrame project starts on p7.

May 2016: Dirk Kempthorne with guest speaker Victoria Saporta, chair of the executive committee of the IAIS, at GFIA's General Assembly in Dublin, Ireland.



This Annual Report is being published as GFIA gathers for its General Assembly in Asunción, Paraguay. The IAIS is holding its Annual Conference at the same time and GFIA welcomes the reopening of the Conference to stakeholders, which will facilitate greater understanding between supervisors and the industry.

Building strong relationships with policymakers around the globe remains a top GFIA priority and we have invited some of those policymakers — and others — to contribute opinion pieces to this Annual Report. The other articles fall into two categories: reports on GFIA's activities and positions, and views from individual GFIA members.

As we look to 2017 and beyond, our industry must remain open and forward-looking and stay mindful of our core business: protection. No matter what the future brings, families will still need protection, businesses will still need financial security, individuals will still need dignity in old age and communities will still need help to recover from natural or man-made disasters. Insurers and reinsurers provide protection that is critically needed around the world.

It has become clear to me that one of our industry's biggest strengths is that we have one foot secured in the traditions of the past and the other striding toward the promises of the future. Technological advances are enabling consumers and businesses to obtain insurance coverage in ways that have never been seen before. As the world becomes more digital, insurers will continue to evolve, shaping their products and services to reflect the constantly changing needs of consumers. GFIA's newest working groups — examining cyber risks, ageing societies and disruptive technologies — mirror that forward-looking mindset.

Insurers have been helping people for centuries. And at GFIA we will contribute to ensuring that insurers have an appropriate regulatory environment so that they can continue to provide essential protection and peace of mind for citizens worldwide.

Governor Dirk Kempthorne

President





**Olivier Guersent**  
 Director general, financial stability, financial services  
 & capital markets union (DG FISMA)  
 European Commission

## Capital compromises

The challenges of aligning divergent systems to create an international capital standard for insurers

In 2013, the IAIS received a mandate from the FSB to work on an insurance capital standard (ICS) for internationally active insurance groups. This ICS is also planned to function as a basis on top of which a capital add-on for global systemically important insurers (known as higher loss absorbency or HLA) can be added<sup>1</sup>.

### Pros and cons

The rationale, benefits and challenges of developing an ICS on a global scale reflect to some extent those involved in the development of the Solvency II regulatory regime in the EU, which took over 15 years from first conception to final application.

**“... the ICS project cannot succeed unless all jurisdictions are willing to envisage changing some aspects of their systems ...”**

There would be cost savings for internationally-active insurers from no longer applying multiple regulatory systems, and cooperation between supervisors of such firms would be facilitated. On the other hand, the starting point is that widely different regulatory systems currently exist in different jurisdictions and there will be transitional costs of moving to a new system for both supervisors and insurers.

Differences between jurisdictions include the valuation approach used to build the prudential balance sheet, with the main approaches being adjusted local GAAP and a market-value based approach for assets and liabilities. The capital requirement can be set by a factor-based formula or a risk-

<sup>1</sup> HLA is scheduled to apply from 2019 to global systemically important insurers, of which there are currently nine. It is currently being reported by them but not required by supervisors, and has a provisional calculation basis known as BCR, until the ICS is available to be the permanent basis.

based total balance sheet approach (that of Solvency II). There can be one solvency threshold, whose breach triggers supervisory action, or two or several. Internal models may or may not be allowed (they are a key part of Solvency II). Some jurisdictions do not yet apply any group-level capital standard to all of their internationally active insurance groups.

Two IAIS public consultations on the ICS have been carried out, one in 2015, and the second from July to mid-October 2016. Early in 2016, the IAIS decided — in light of the challenges involved — to develop the ICS in two phases, with an “ICS 1.0” (a broad-brush ICS) to be developed by 2017 and a finalised “ICS 2.0” to be completed by 2019.

### Compromise required

The European Commission, European Insurance and Occupational Pensions Authority (EIOPA) and EU national insurance supervisors are deeply involved in IAIS work on the ICS in good faith, as indeed are many supervisors worldwide. While compatibility with Solvency II is an objective of the EU participants, it is also understood by all involved that the ICS project cannot succeed unless all jurisdictions are willing to envisage changing some aspects of their systems in order to enforce the ICS, at least as far as internationally active firms are concerned. While the ICS cannot correspond to any one existing system, an ICS that allows current diverging practices, such as valuation bases, to coexist would not be a global standard in any meaningful sense.

The application of an ICS in the EU, following its adoption by the IAIS and endorsement by the FSB and the G20, would require a change to the Solvency II Directive. The EU’s democratic co-legislators, the European Parliament and Council, would have the final say on any changes, based on a proposal by the Commission. ➤



Chair, GFIA capital working group  
**Hugh Savill**  
*Association of British Insurers*

## Abbreviations don't lessen the workload

NTNI becomes SRIPF but still needs work, and ICS too has a long way to go

The work of the Federation's capital working group this year falls neatly into two halves. In the first half of the year we agreed a response to the IAIS consultation on non-traditional, non-insurance (NTNI) activities and products. Since July 2016 our work has been dominated by the consultation on the global insurance capital standard (ICS).

The consultation on NTNI was not vintage IAIS output. GFIA members have always had doubts about the validity of the NTNI concept, and to be frank this consultation did little to dispel them. We raised strong concerns that, once agreed, the NTNI concept would be used by regulators for a wider purpose than that for which it was designed, and that this could have an adverse impact on savings.

The process the IAIS proposed for the identification of NTNI activities and products was both complex and arbitrary. At a very basic level, it is not clear from the document which body should be responsible for making the assessment that would lead to the potential identification of NTNI activities and products. To be fair, this is not easy; the expertise of local regulators/supervisors is required for an accurate understanding of the products in question. Likewise, we expect regulators to work together to produce a consistent approach and to prevent scope creep.

We wondered whether some of the flaws in the IAIS thinking were due to its focus on the specifics of contracts and little else. Such an approach leads to an assessment of the delays that some products impose before a policyholder can surrender their policy — and in fact relies excessively on the length of the delay. In reality, the insurer's ability to manage liquidity risk is a more significant factor. Emphasis on the contract also leads to a narrow focus on exit penalties as a disincentive to surrender. In practice there are many other

factors that act as brakes on the temptation to surrender, including tax considerations, loss of guarantees, switching cost and difficulties in finding an adequate replacement product.

We were also deeply confused by the IAIS identification of "ancillary factors" to an NTNI assessment, which were presented by the IAIS as relevant to systemic risk, but somehow not determinative for the NTNI identification. While some of the ancillary factors mentioned are relevant to an NTNI assessment (even when admittedly difficult to quantify), we encouraged the IAIS to investigate the issue further.

### Systemic risk overstated

However, the substantive problem with the NTNI proposal was that it hopelessly overstated the systemic risk associated with NTNI activities and products. The IAIS rightly drew a distinction between vulnerabilities and transmission channels, but failed to follow through with the logic of this distinction. While the vulnerabilities mentioned by the IAIS are indeed a source of risk to the insurer, that is a matter for microprudential regulation, rather than a macroprudential/systemic risk focus.

By definition, these vulnerabilities can only lead to systemic risk if they are transmitted from the insurer that is engaged in NTNI to the financial system and to the wider economy. In fact, the IAIS analysis understates the ways in which the potential transmission of systemic risk can be limited and even completely prevented by management actions at company level, or through supervisory action.

GFIA also objected strongly to the treatment of derivatives. The frailties of the derivatives market were exposed during the financial crisis, but a great deal of action has been taken

since then to strengthen the market — at great expense to users of derivatives, such as insurers. So we went through the G20 derivatives reform precisely aiming to address systemic risk, and now the IAIS is saying that derivatives can be a source of systemic risk for insurers.

Such analysis translated into a clear disincentive for insurers to use derivatives, although these are often key for optimising risk and portfolio management. Unfortunately, by ruling out any contribution that derivatives might make to delivering a policy's benefits, the IAIS is effectively saying that the policyholder is no better off than if they relied on the insurer's balance sheet alone. This has to be nonsense.

**“The ICS consultation does little to address the design flaws and uncertainty of purpose that GFIA has consistently outlined.”**

The IAIS produced a refreshed look at NTNI in June 2016, unveiling a new name for the concept: “systemic risk from insurance product features” (SRIPF). I fear that this name will not be winning any branding awards either, though I at least appreciate the tribute to the late Prince in the reference to a concept “previously known as NTNI”. The concept will be refined further over time, but this document revises significantly the approach to liquidity risk and macro-economic exposure. The IAIS has also removed double-counting between derivatives and minimum guarantees. These are improvements but, as the IAIS acknowledges, there is more detailed work to be done.

#### **A long journey**

As Chairman of GFIA's working group I have done my duty and occupied plane cabins for long periods of time. A visit to Singapore in March 2016 for the IAIS capital-related stakeholder meeting revealed that the IAIS secretariat had

more progress with the field testers than was publicly admitted in developing the ICS. I now also know that Singapore has a Starbucks and an airport. In June in Budapest I sat on a panel for the IAIS Global Seminar. Luckily I saw rather more of the fine city of Budapest.

The Seminar was a huge improvement on the previous Global Seminar in Macau, and it was good to see that the IAIS recognised the contribution that GFIA has made. My favourite moment came at the back-end of the Seminar, when I slipped in a question to a panel of distinguished former IAIS luminaries to ask whether they had at any time considered the cost of their proposals. The bemusement that greeted this question gave its own answer, as Al Iuppa of Zurich gracefully acknowledged.

In July 2016 the IAIS finally released its second consultation on the first version of the ICS. This is a highly technical consultation, with 235 detailed questions. GFIA submitted its response to the consultation by the mid-October deadline. The consultation concentrates on technical issues and does little to address the design flaws and uncertainty of purpose that GFIA has consistently outlined in its comments on the ICS. I am not impressed by the suggestion that these issues will be easier to address when more is known about the technical detail.

The IAIS also makes little attempt to reconcile the fact that this is a minimum standard — allowing local supervisors to adopt more stringent rules if they wish — with their ultimate goal of complete comparability. Finally, the relationship between the ICS and local prudential regimes remains murky. The suggestion that a group standard should have no effect on legal entity requirements goes only so far; the two systems inevitably have to be reconciled. ➤



**Olav Jones**  
Deputy director general  
*Insurance Europe*



**Stef Zielezienski**  
Senior vice-president  
& general counsel  
*American Insurance Association*

## Out of focus?

The IAIS should be focusing on ComFrame's original aims

The ComFrame project was launched by the IAIS in 2010, largely triggered by the financial crisis. Although the insurance industry fared well during the crisis, the need to rescue US insurance group AIG stood out as a significant international incident. It was generally recognised that AIG's problems did not emanate from its insurance activities. Nevertheless, the AIG case naturally triggered questions over whether a regulatory response was needed and, if so, what it should be.

The project to develop a common framework for supervising international groups, or ComFrame, arose as the supervisory response and was initially designed with the key aim of addressing the weaknesses in the regulation of internationally active insurance groups by helping national insurance supervisors to cooperate and coordinate more efficiently and effectively.

### Industry support

There was significant support from the industry for the overarching aim of ComFrame to ensure that all large, internationally active insurance groups (IAIGs) have high-quality governance and risk management covering all their group-wide activities. ComFrame's focus on guaranteeing that all groups have a lead, group-wide supervisor — and a well-functioning college of regulators/supervisors ensuring appropriate oversight for all group-wide activities — was also welcomed.

GFIA closely follows the IAIS work on ComFrame in a working group under the chairmanship of Stef Zielezienski. This article is written in a personal capacity.

Supervisory cooperation is seen by the insurance industry as a vital element of ComFrame. It has to ensure that there are no gaps in the oversight of international groups. Equally importantly, supervisory cooperation needs to ensure coordinated responses and address the growing burden that international groups have been experiencing due to multiple uncoordinated requests from different regulators for similar group information.

### A shift in focus

The initial ambitions of ComFrame have changed over recent years, with a new focus placed on developing a quantitative global insurance group capital standard that would provide consistent and comparable solvency measurement across the world.

Interestingly, the idea of a global capital standard was not triggered by the need to fulfil the aims and objectives of ComFrame, but by the need to address challenges and gaps in another parallel workstream of the IAIS; namely the discussions on systemic risk and whether “too big to fail” applies to the insurance sector (see p13).

A capital add-on, such as that already developed by the Basel Committee on Banking Supervision, was defined as one of the measures that would need to apply to a global systemically important insurer (G-SII). However — unlike in banking — in insurance there is no standard capital basis to which this add-on can be applied in all global jurisdictions. This gap led to the development of a basic capital requirement (BCR), designed to be used as a foundation for a capital add-on called higher loss absorbency (HLA).

The BCR was developed over the course of nine short months, making it an extremely rough measure with very

little risk-sensitivity and one that ignores some of the core elements of risk mitigation and diversification fundamental to an insurer's business model. The IAIS recognised its weaknesses and decided to address them by replacing the BCR with a global insurance capital standard (ICS) to be included as part of ComFrame.

### Insurance is not banking

The explicit intention for the ICS appears to be largely linked to the initial objectives of the Basel Accords for regulating banking; namely to have a “measure of capital adequacy” and for “minimum standards to be achieved”. The starting point of this work in insurance, however, differs significantly from that in banking.

Discussions on the first Basel Accord began in the 1970s and came at a time when local supervisory authorities had only done a comparatively small amount of work in building up their own regulatory frameworks. Progress was then incremental, with jurisdictions implementing changes and rules in parallel over many years, making it more straightforward for an international standard to be adopted by different jurisdictions at the same time.

Work on an international capital standard for insurance, on the other hand, was only announced in 2013. By then some jurisdictions — including the two largest markets, the US and the EU — had already gone through a revision of their local solvency regimes. Jurisdictions are now faced with high-level, principle-based discussions on how a risk-based capital system should be designed and how comparability across jurisdictions could be achieved.

### Rushed and over-ambitious

Based on the experience in Europe, where the Solvency II

project has taken more than 15 years to develop, the IAIS's current timetable and aims for the ICS are particularly ambitious.

Developing effective regulation, while navigating the different approaches to accounting and solvency regulation that an international insurance group encounters, requires effort and engagement from both regulators and the industry. They need to design and test a risk-based system that aims to capture the true risk profile of the insurance business, while minimising unintended consequences that could arise from approaches that focus more on simplicity and less on measurement of real risk. The industry is therefore sceptical about whether the current plans and timeline for the ICS are realistic.

**“The industry is sceptical about whether the current plans and timeline for the ICS are realistic.”**

So, is ComFrame achieving its initial aims? This remains an open question, on which we have seen little reporting by the IAIS recently.

Indeed, the shift in focus to developing an international capital standard has slowed down progress in the areas the insurance industry believes are most important for preventing future problems.

The industry strongly supports high-quality group risk management and fully coordinated supervisory coverage through lead supervision and coordinated supervisory colleges. If policymakers truly want to establish a group supervisory framework that can detect and avoid the types of problems that led to the last crisis from arising again, then this is where they should be focusing their attention. ➤



**Tim Adams**  
President & CEO  
*Institute of International Finance (IIF)*

## Flexibility is key

ComFrame will only succeed if it is not too prescriptive, says the IIF

In 2010, the IAIS embarked on developing a comprehensive common framework (ComFrame) of tools for the supervision of the world's largest and most internationally active insurance groups. Around 50 firms' global operations would be regulated on a consolidated group-wide basis. ComFrame naturally includes both qualitative and quantitative components — the latter represented by the global insurance capital standard.

ComFrame builds on the IAIS's Insurance Core Principles, but aims also to deliver measures to apply to globally active firms and their supervisors. Chief among them is an effort to enhance coordination among supervisors, which would benefit both them and firms. Supervisors would benefit from a more comprehensive view of risks across a financial group and across jurisdictions; insurers would benefit from greater operational efficiency and lower compliance costs; and the financial system would benefit from enhanced insurer oversight, risk diversification and increased growth of safe, domestic and global financial markets.

### Three principles

The IIF therefore agrees with the strategic direction of ComFrame. As the IAIS currently focuses on the development of ComFrame's capital component, it is important to consider three fundamental principles. ComFrame should:

- maintain a level competitive playing field for all companies and promote the growth of private insurance markets
- promote more efficient and effective supervision that is free of material gaps, avoiding the unnecessary layering of duplicative requirements
- improve policyholder protection

Within international finance, the insurance business model is unique for its heterogeneity of corporate structures, mix of products, asset portfolios and geographic reach. Those

differences are most notable when looking at products; for example, while fixed-income products may prevail in one country, in another, variable annuities are most popular.

This wide variety logically calls for an appropriately flexible and pragmatic approach under ComFrame. It should be a principle-based framework focused on achieving similar outcomes and able to be implemented in the current policy and political environment. Domestic supervisors should not be overly constrained as to how the standards are met, and ComFrame should not be so prescriptive that it conflicts with, and requires unnecessary changes to, current and developing local frameworks that otherwise satisfy the fundamental principles. To measure the consistency of implementation, the IMF, in coordination with the IAIS and FSB, would need to apply an appropriate process to assess national regimes against the standards, identify non-compliant jurisdictions and facilitate implementation of effective measures.

The differences between regulatory regimes are not likely to narrow significantly by 2020, which is when the IAIS hopes to have ComFrame embedded in supervisory practices. In EU member states, Solvency II has entered into force; in the US, both the state regulators and the Federal Reserve Board have begun work on consolidated group capital measures; and Japan is considering significant revisions to its solvency regime. These systems are based on divergent fundamentals, including different valuation regimes, calibrations of capital adequacy and governance frameworks. Nevertheless, we remain committed to cooperating with the IAIS on the process for developing, over sufficient time, a comprehensive framework for supervising international groups that promotes effective supervisory cooperation, takes appropriate account of a diverse industry and is flexible enough for effective implementation in diverse jurisdictions. ➤



Chair, GFIA systemic risk working group  
**Nicolas Jeanmart**  
*Insurance Europe*

## In the right direction

The IAIS, FSB and IMF need to do further work to accurately reflect the insurance business model

The work of the IAIS and the FSB on the issue of systemic risk in insurance has continued in 2015 and 2016, with a particular focus on global systemically important insurers (G-SIIs). The two organisations continue working under a mandate from the G20 to ensure that no financial institution is “too big to fail”.

The GFIA systemic risk working group contributed to the work of the FSB on effective resolution strategies for G-SIIs and to that of the IAIS on a revised G-SII assessment methodology.

### Positive on resolution

Regarding resolution strategies for G-SIIs, GFIA is of the opinion that, in general, the proposed FSB guidance is appropriate. Identifying institution-specific objectives for resolution is a sensible approach, as long as those objectives are clear to the institutions in question.

The proposed guidance also seems flexible enough to account for the different types of business undertaken by G-SIIs. In particular, GFIA welcomed the flexibility granted to the relevant supervisory authorities regarding the point of entry into resolution, as this reflects the wide range of organisational structures in the insurance industry, as well as the diversity of national insurance regulatory regimes.

GFIA also welcomed the significant improvements made to the identification of critical functions. Particularly positive was the revised definition of critical functions as those that would be likely to have a material impact on the financial system and the real economy if they failed. GFIA agrees that services that do not have a significant impact on economic and financial stability, or that can be easily substituted, should not be considered critical.

On the other hand, GFIA believes that the ability to intervene

rapidly is not necessary in insurance resolution because any failure of an insurer occurs over an extended period of time, given the nature of their liabilities. Therefore, authorities choose resolution tools that are effective and appropriate while avoiding unnecessary value destruction, without regard to whether or not these tools allow for rapid intervention. GFIA also maintains that a lack of substitutability is rarely an issue in the insurance industry because portfolio transfers are common, and capital and expertise (the two key elements of insurance capacity) have in practice proved easy to replace.

### Less positive on assessment

In relation to the revision by the IAIS of its G-SII assessment methodology, GFIA believes that, while a number of concerns have been addressed by the IAIS, several improvements still need to be made in order to achieve an appropriate methodology that accurately reflects the insurance business model.

Specifically, a move to absolute reference values for certain indicators and away from the relative ranking system of the current G-SII assessment methodology would greatly improve the process in the future because — instead of a relative ranking of companies against each other — it would more accurately reflect a company’s potential exposure to or transmission of systemic risk to the financial system. Absolute values would also further increase transparency and certainty. The use of absolute reference values would need to be combined with an absolute threshold for the level of activity, below which insurers should be excluded from the assessment score as the activity would not be a source of systemic risk.

In addition, it remains unclear why the IAIS has suggested having a reinsurance supplemental assessment, given that the IAIS has looked at reinsurance in detail and has concluded that

“traditional reinsurance is unlikely to cause, or amplify, systemic risk”. GFIA maintains its view that no case has yet been made for considering reinsurance as giving rise to systemic risk. Therefore, GFIA argues that reinsurance should not be included in the list of indicators. In fact, reinsurance should be incentivised as a stabilising factor in the financial system rather than penalised.

Finally, GFIA disagrees with the suggestion that insurers use derivatives for speculative purposes. In most jurisdictions, insurers are prohibited from speculative derivative trading and these are instead used for hedging and risk management purposes.

In general, the work of both the IAIS and the FSB shows that the dialogue between industry and the supervisory community has resulted in a better understanding of the insurance business model, and in particular of the potential sources of systemic risk in the sector. This has resulted in improved guidelines for G-SII designation and resolution, but additional work is needed to ensure that supervisors focus their efforts on the limited circumstances that could give rise to systemic risk concerns.

#### IMF involvement

In addition to the work done by the IAIS and FSB, the IMF included in its April 2016 Global Financial Stability Report (GFSR) an entire chapter dedicated to the systemic importance of insurers.

The IMF describes major insurance sector developments over the past decade and assesses changes in the systemic importance of insurers. The chapter shows that across advanced economies “the contribution of life insurers to systemic risk has increased in recent years, although it clearly remains below that of banks”. The IMF states that this increase

is largely due to growing common exposures to aggregate risk, caused partly by a rise in insurers’ interest-rate sensitivity.

The IMF concludes that supervisors and regulators should place a greater emphasis on macroprudential policies, so as to better address the systemic risk arising from common exposures. To complement this, the IMF suggests the use of countercyclical capital buffers. The IMF also recommends closer scrutiny of small insurers. In the IMF’s view, even if such insurers are less systemic individually, they may become “too many to fail” if they act similarly. The IMF also calls for an international capital standard for insurance companies to mitigate systemic risk and protect against cross-sectoral and regional spillovers.

The IMF’s interest in insurance and the potential sources of systemic risk in the sector is positive and the dedicated GFSR chapter represents a valuable contribution to the general understanding of the insurance industry’s unique business model. In general, the IMF’s conclusions and policy recommendations seem to move away from the G-SII-centric approach that has been taken until now. While GFIA views this change of perspective favourably, it disagrees with some of the concrete recommendations, notably with the suggestion that using countercyclical capital buffers would mitigate systemic risk concerns. Given that insurance capital is needed exclusively to absorb losses that technical provisions cannot cover and that insurers do not engage in money creation and maturity transformation, such buffers would not have the expected macroprudential effect.

Finally, the IMF discusses a number of challenges faced by our sector that are not only relevant to G-SIIs. GFIA looks forward to opportunities to discuss with the IMF how these challenges can best be overcome. ➤



**Daniel Hofmann**  
Senior advisor, financial stability & insurance economics  
*The Geneva Association*

## Investigating procyclicality

New study finds negligible evidence for systemic risk from procyclical behaviour in insurance investments

The systemic relevance of the whole insurance industry is now firmly on the radar screen of supervisors and bodies charged with macroprudential surveillance. In a recent report, the Bank of England found evidence of so-called procyclical investment behaviour for the time following the dotcom crash, and to a lesser degree during the recent global financial crisis. Similar findings were published by the European Systemic Risk Board as well as by academics and central bank researchers.

This marks a remarkable shift in perspective. In the response to the global financial crisis, supervisors focused on identifying individual insurers of systemic importance. This bottom-up perspective has now been supplemented by a top-down view, broadening the reach of systemic regulation to include the whole sector rather than individual firms. In fact, the IMF recently called for an extension of the policy toolkit developed for global systemically important insurers (G-SIIs) to other large groups.

**“By virtue of their long-dated, mostly illiquid liabilities, insurers are not susceptible to sudden cash drains that would require large asset sales.”**

Of course, there are a number of reasons why insurers could display common, procyclical investment behaviour, including, potentially, new regulation itself. But based on the insurance business model, we question whether such behaviour could assume systemic proportions. By virtue of their long-dated, mostly illiquid liabilities, insurers are not susceptible to sudden cash drains that would require large asset sales. Absent binding regulatory solvency constraints, they should rather be able to “look through the cycle” and ride out financial turbulence. Thus, one would expect the asset allocation of

insurers to be less volatile than that of other large institutional investors. Consequently, the price impact of industry-wide investment decisions should be small.

### What data and stress tests are telling us

The Geneva Association has examined the material impact of the alleged procyclicality and its potential systemic impact<sup>1</sup>. We looked both at the historical record (a period spanning 2001 to 2015) and, recognising that past behaviour cannot be indicative of future performance, at a range of possible market outcomes under hypothetical stress situations in which insurers are forced to sell large quantities of assets.

The procyclicality suspicion is based on the large investment portfolios held in particular by life insurers. While insurers rank among the world’s largest institutional investors, we found that specific asset classes held by insurers comprise smaller portions of the market than those held by other large investors. It suggests that even large asset sales by insurers are unlikely to impact markets as much as large asset sales by other institutional investors.

A similar finding holds for the variation in asset allocations over time. Compared to banks, mutual funds and pension funds, the asset allocations of US life insurers were less volatile before, during and after the crisis. The results summarised in the figure on p16 show that life insurers in fact have the lowest values for the standard deviation of quarterly changes in asset allocation across all asset classes with the exception of equity securities.

Thus, the analysis does not contradict our presumption that the business model of insurers is unlikely to cause procyclical

<sup>1</sup> “Insurance sector investments and their impact on financial stability: An empirical study”, Geneva Association, 2016, [https://www.genevaassociation.org/media/948960/060716\\_investment-behavior\\_complete\\_digital.pdf](https://www.genevaassociation.org/media/948960/060716_investment-behavior_complete_digital.pdf)

behaviour. Assets held by insurers displayed lower volatility over extended periods, and this was also true during the financial crisis. Moreover, our findings seem to support the claim that the investment behaviour of insurers contributed to financial market stability even at times of severe market distress.

**Tested in adverse scenarios**

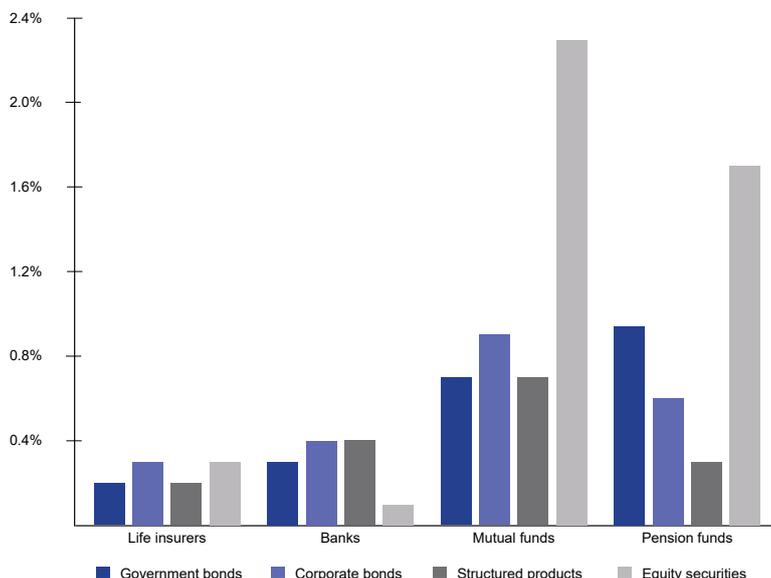
To investigate the range of market outcomes under hypothetical stress scenarios we subjected the portfolios of life insurers to severe shocks, examining the impacts of (i) credit de-risking, (ii) de-risking of equity securities and (iii) forced assets sales caused by large surrenders. To some degree, these shocks have been observed in the past. The

**“The investment behaviour of insurers contributed to financial market stability even at times of severe market distress.”**

equity de-risking of European life insurers after the dotcom bubble burst was thought by many to have added to the stock market volatility observed in the years 2001/02.

We looked at Europe and the US separately and considered financial assets held by life insurers only in their general account. Readers are referred to our full report for the methodology to calculate the market price reactions of asset sales and for the links between policy surrenders and asset sales.

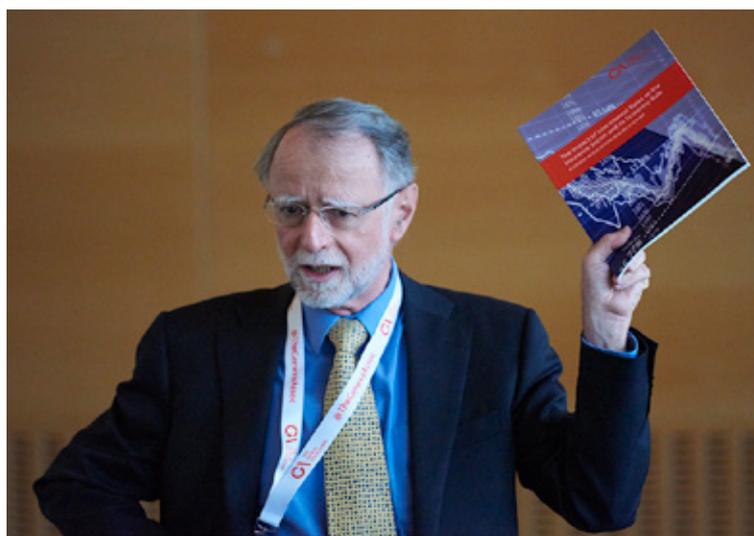
**Standard deviation of quarterly changes of asset allocation — percentage points by asset class, US, Q1/98–Q3/15**



Sources: US Federal Reserve, Oliver Wyman analysis

The summary estimates in the table on p17 are based on observed price and trading volumes and they include a deliberate bias towards adverse price impacts. To determine whether price reactions are systemic, we calibrated them against market circuit breakers developed after the October 1997 US stock-market crash, suggesting that only price declines of more than 20% should be considered systemic.

We recognise that the industry may display some degree of procyclicality. After all, insurers are part of the financial system; they cannot escape certain market trends and they seek to meet their regulatory requirements at all times. We found, however, the price reactions of large asset sales in Europe and the US to be small and unlikely to cause systemically relevant distortions. The only result that came close to systemic proportions was a hypothetical 100% equity de-risking in our



worst-case scenario. It builds on the severe financial market distress experienced during the global financial crisis, when observed price and volume changes of financial assets reached extreme values.

**Policy implications**

In light of these findings, we offer four broad conclusions:

- Absent regulatory requirements, the business model of insurers should not give rise to procyclical investment behaviour with systemic proportions. Thus, there is no need for specific regulation, and in particular for additional capital buffers, to address potential procyclical behaviour.
- Policymakers should avoid creating incentives that

weaken the ability of the insurance sector to absorb financial market distress. During the global financial crisis insurers functioned as shock absorbers and contributed to financial stability at a time of severe distress.

- There is a need for further research into the implications of prudential regulatory regimes based on market-adjusted valuations and whether they may influence or cause procyclical behaviour.
- Theoretical considerations and empirical evidence point to the irony that procyclical behaviour, which has been the proposed rationale for macroprudential regulation, can be triggered, and possibly exacerbated, by microprudential regulation. Thus, policymakers should make an effort to mitigate the unintended consequences of regulation.

**Summary of scenario-based results**

Price impact of large-scale asset sales under various scenarios

	Europe		USA	
	Best market environment	Challenged environment	Best market environment	Challenged environment
<b>Credit de-risking</b>	-0.2%	-0.6%	-0.2%	-0.8%
<b>Equity de-risking</b>	-1.0%	-4.0%	-0.1%	-0.2%
<b>Large surrenders</b>				
Equity securities		-0.1%		-0.05%
Corporate bonds		-0.03%		-0.03%
Agency bonds		n.a.		-0.01%
Government bonds		-0.03%		-0.25%
Municipal securities		n.a.		-0.25%
Structured products		n.a.		-0.11%
<b>Worst-case scenario (global financial crisis)</b>				
Credit de-risking	-7.1%		-8.0%	
Equity de-risking	-19.2%		-1.1%	

Note: "Best market environment" figures are based on the 75th percentile of the historic price/volume distribution; "challenged environment" on the 95th percentile



Chair, GFIA cyber risks working group  
**Leigh Ann Pusey**  
*American Insurance Association*

## Risks without borders

GFIA creates a global group to tackle a global issue

As technology becomes more sophisticated, digitalisation is increasingly integrated into our daily lives. This new reality comes with a whole new landscape of risks that need to be mitigated and managed. Data theft, systems failure, sabotage, or any number of other calamities can strike individuals and businesses.

Insurers are increasingly learning to assess, quantify and indemnify these cyber risks. Currently led by the US, the global cyber risk insurance market is expected to grow exponentially in the next few years (see chart on p19).

Cyber risks and insurance are so new and rapidly evolving that it is inevitable that there will be ongoing debates about what constitutes appropriate regulation and best practices, and what can reasonably be codified into law. Together, regulators, insurers and technology experts will need to determine the way forward.

### International discussions

To be part of this conversation, GFIA set up a cyber risks working group in November 2015. Cyber risk is inherently an international issue, so it follows that there will be discussions about global best practices and standards. The working group intends to share information and develop public policy positions in this area.

**“Cyber risk is inherently an international issue, so it follows that there will be discussions about global best practices and standards.”**

The group will look at cybersecurity from two angles. First, government efforts to address data security, and specifically how those efforts affect an insurer’s corporate security

practices. Second, public policy issues related to the evolution of the cyber insurance market and challenges to its growth.

The group first carried out a member-wide survey in order to more clearly understand the global regulatory and market environment. The survey sought information at national level on information-sharing initiatives, legislative requirements, government involvement and implementation of national cyber-security strategies. The survey also served to gather information on the current state of the cyber insurance markets in different jurisdictions in terms of product offer and development.

### Policy points identified

The survey enabled the working group to identify issues on which to develop public policy statements. Key points to emerge from the survey include the importance of a flexible and cost-effective, risk-based approach to regulation. In addition, global coordination can help to avoid the headache of multiple, inconsistent regulations for international companies.

Information-sharing is another key issue for companies, but here it is important to distinguish between the importance of sharing cyber-threat information to protect corporate assets and the caution required for competitive reasons over sharing loss and claims data to help grow the cyber insurance market.

The challenges for the cyber insurance market are those of any new and emerging insurance market, such as a lack of actuarial data and a need for robust modelling and more standardisation. The nature of cyber risks makes potential aggregation issues a particular problem, along with how to increase underwriting expertise and how to raise risk awareness among businesses and individuals.

Ultimately, all these challenges underpin the overarching message that emerged from the survey and working group discussions; the market must be allowed to develop organically without regulatory impediments that could stifle growth and innovation.

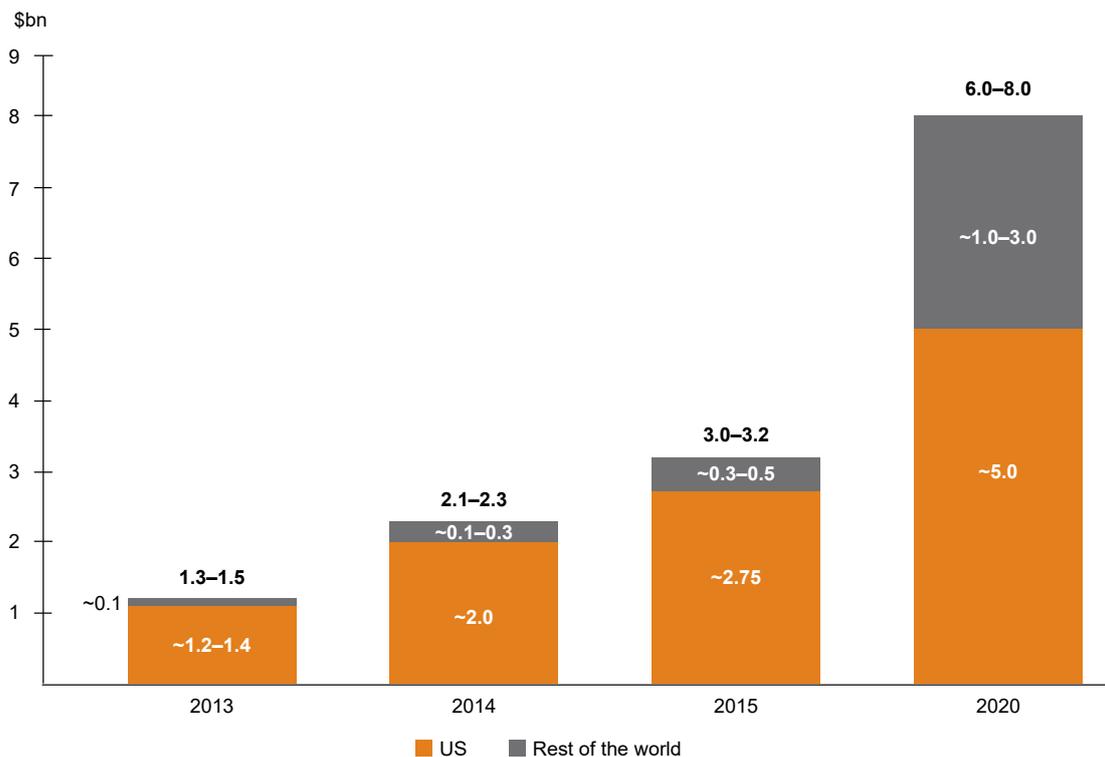
**Response to OECD survey**

GFIA made all these points when, in July 2016, it responded to an OECD questionnaire on cyber risk insurance. It particularly

stressed the importance of governments supporting the development of the cyber insurance market through natural evolution, allowing the market to respond appropriately to the challenges of a unique and ever-evolving risk landscape.

The OECD survey is intended to feed into three reports that it plans to produce on cyber risk insurance; risk awareness, mitigation and prevention; and regulatory and policy issues. These it intends to discuss at an event in 2017. ➔

**Estimated primary cyber insurance market — 2013–2015 & 2020 (\$bn)**



Source: Munich Re, November 2015 (based on various external sources)



Chair, GFIA ad-hoc disruptive technology working group  
**Don Forgeron**  
 Insurance Bureau of Canada

## Opportunities and risks

GFIA has set up a group to look at the implications of disruptive innovations

Around the world, innovations are disrupting established industries and the insurance sector is not immune. In every jurisdiction, insurers are considering the question: what are the disruptions that could target our industry?

To insurers, technological innovation represents an opportunity and a risk. To better understand both, GFIA this year established a group to examine the implications of disruptive innovations and the role that associations can play in responding to them. It provides a forum for participants to share experiences and identify insurance-related public policy considerations. With the intention of promoting a regulatory environment that allows insurers to innovate and provide new products and services, the group is focusing on the implications of disruptive technology for life, health and property and casualty insurance.

### Direct and indirect disruption

Insurance can be disrupted either directly or indirectly. With direct disruption, the industry faces competition from innovative models, such as peer-to-peer risk-sharing platforms, that harness technology and social media to offer consumers customised products at lower premiums. Indirect disruption occurs through a larger reorganisation of the economy. Innovators are not just attempting to replace existing businesses, but to create whole new sectors that transcend traditional industry boundaries.

The regulatory environment in most countries makes direct disruption difficult. But regulations are also a double-edged sword; while they have insulated the industry in the past, they have also inhibited its ability to innovate. The technology-based innovations of today make existing insurers vulnerable to new entrants' business models that circumvent current regulations.

At the same time, existing regulations can prevent insurers

from responding quickly to a competitor that circumvents the rules. In some countries, these regulations have hampered the industry's most rudimentary innovations, such as conducting consumer transactions online or collecting certain consumer information that would inform underwriting and rating decisions.

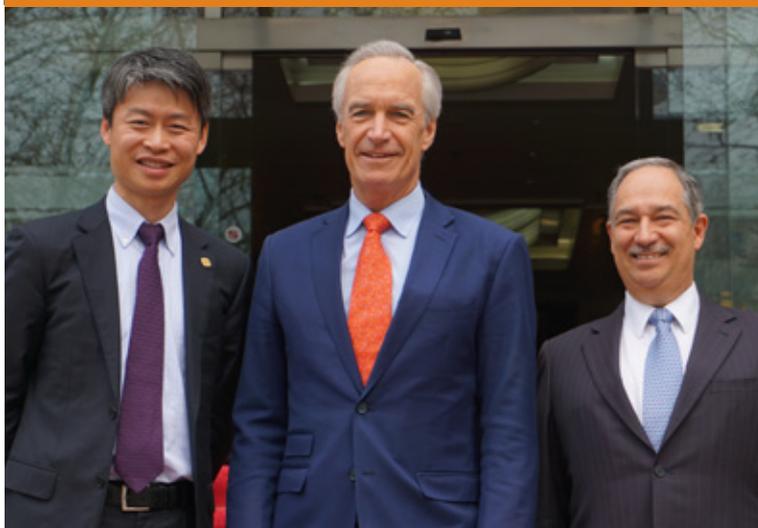
### Societal shifts

Disruptive innovations are not a sectoral phenomenon; they have economy-wide reach. They are creating economic activity and new markets where none existed before. If the nature of personal and/or business risks changes, the demand for specific types of products and the buying patterns of consumers will change accordingly. The sharing economy, telematics, big data and automated vehicles, for example, are affecting or will affect the business of insurance, from product development to underwriting and rating practices to claims management. Creating products for these emerging sectors will be a challenge for insurers.

To be able to respond quickly to both direct and indirect disruption, insurers need to work with their governments to identify obsolete regulations and then modernise them so that insurers are equipped to innovate and provide the market with products and services for the new types of risk.

In August 2016, the working group held its first meeting. As a first step, members agreed to develop and distribute a questionnaire within the group to gather information on disruptive activities, trends in their jurisdiction and regulations that hamper the industry's ability to innovate. The group will share a full report with GFIA members in 2017.

Disruption from technological innovations is inevitable. By taking proactive measures today, the industry is working to ensure that it maintains its primary role in mitigating risk. ➤





**Soo-Chang Lee**  
Chairman & CEO  
*Korea Life Insurance Association*

## Tackling the pension challenge

Insurers are part of the solution to making pension provision fit for the future

People are living longer than ever before. In many countries, including Korea, advances in medicine and technology mean that new generations can expect a longer lifespan than those that came before them. At the same time, as people in many countries become more prosperous, they are choosing to have fewer children.

These pressures have resulted in an unprecedented demographic shift; as the volume of retired people increases, the number of workers that support their retirement is declining — and sharply in many countries. For instance, in Korea people over 65 accounted for around 12% of the population in 2013. However, due to several factors, this figure is set to drastically increase in coming decades, with some estimates hovering around 30% for 2040.

This demographic shift will inevitably put downward pressure on economic growth, and will make it even more difficult to provide the financial means to provide retirement income, both in the wider economy and from governments' budgets.

It is clear that there will be far-reaching economic and social consequences for old-age support systems around the world. The insurance sector has its part to play in the solutions.

### The time to act

Unless policymakers take the right actions, it will be difficult to maintain an adequate standard of living for retirees without putting an unacceptable burden on workers. A growing number of governments have therefore already enacted reforms that reduce the future benefits of state retirement income provision.

Yet, even if those reforms are successfully implemented and more citizens are brought into state pension schemes,

In the last year GFIA has set up an ageing society working group under the leadership of Brad Smith of the American Council of Life Insurers.

increased longevity will still create costs that are historically unprecedented. If not recognised and addressed in sufficient time, these factors have the potential to seriously affect not just national but also international prosperity.

There are several additional issues that policymakers must consider. One is the high level of public indebtedness, which limits how governments can deal with rising retirement and ageing costs. Many of the world's most advanced economies struggle with this. Similarly, these large economies are also dealing with exceptionally low interest rates, which make it more difficult to finance private pensions.

This combination of factors — rapidly ageing populations, high public-debt burdens and record-low interest rates — is totally without precedent.

### Other challenges

These factors are also having an impact on the way that some pensions are designed. In some countries, companies are finding it harder to offer defined benefit (DB) pension schemes. As a result, there has been a steep decline in DB schemes in favour of defined contribution (DC) schemes, which may result in lower pension pot values in the future.

Another important issue is that a lack of understanding among consumers over which pension products best suit their needs — such as annuities versus drawdowns — is also contributing to the challenges to achieving adequacy and sustainability in retirement funding.

The declining generosity of state retirement income provision would be less of a concern if people were saving enough for retirement or had access to a workplace/occupational pension. Unfortunately, research suggests that this is not the case. Rising life expectancy puts people at a growing risk of outliving whatever personal retirement savings they do have.

#### How to respond

For countries to ensure financial security for their retired citizens, while also fairly sharing the costs of ageing between generations, governments must:

- build strong multi-pillar pension systems that complement state-backed retirement provisions
- incentivise people to increase their own long-term retirement savings

#### Multi-pillar pension systems

To tackle the pension challenge, governments should develop a well-designed pension system that consists of different components or “pillars”. Such a system mitigates risk, because the factors affecting the different pillars tend not to be fully correlated. As a result, the system is not too exposed to any single external risk, with the different elements allowing several goals to be achieved simultaneously, including poverty reduction, sustainable income replacement, flexibility, affordability and long-term savings.

In many countries, there is currently an over-reliance on pillar one, state-run pensions, but their sustainability depends on a high ratio of taxpaying or contributing workers to retired beneficiaries. Over-reliance on this pillar makes a society vulnerable to poor labour ratios and ageing demographics. Therefore, work-based and private sector pensions (pillars two and three) should be used to complement state-pension schemes, making the overall system more robust and resilient.

#### Incentives to long-term retirement saving

To increase the effectiveness of a multi-pillar system, participation in complementary pillars two and three should be encouraged. To this end, governments can use certain policy tools — enrolment rules, tax incentives, state contribution for pensions, education — that are recognised to incentivise long-term retirement savings:

- Different types of enrolment rules help make pension participation possible for all segments of society. Auto-enrolment, for example, can improve savings rates, particularly among those who may not otherwise be saving for retirement. Quasi-mandatory enrolment (eg some types of employer-sponsored plans) and voluntary pension products can also help to maximise the availability of long-term savings products to all segments of the population.
- Tax incentives and state contributions, when well designed and communicated properly, can encourage consumers to save for retirement. They can also disincentivise people from exiting the workforce early. It is absolutely crucial that the value of these incentives should be stable over time, as pension provision is a long-term business. Governments should resist the temptation to curtail incentive schemes when faced with short-term public finance challenges.
- Financial literacy campaigns can educate citizens and help them make prudent financial decisions.

#### The role of insurance

Given the urgent need to address the issue of ageing populations, it is essential for governments to take serious steps to ensure their citizens can receive an adequate retirement income. A good step would be to stimulate the availability and uptake of pension products beyond mandatory state schemes.



As major providers of occupational, workplace and personal pensions, as well as life insurance, insurers have a key role to play. In particular, they can provide protection for very different life risks: provision for dependants should a saver die prematurely, protection against outliving assets and morbidity risk coverage. Risks can be covered both in the accumulation and — by annuities and drawdown products — in the pay-out phases. Insurers can also offer a wide range of pension products tailored to the individual traditions and practices of different countries. The advantages for policyholders are numerous and include:

- sustainable lifetime income
- less volatile, long-term returns due to investment pooling
- access to the higher yields available from long-term and illiquid investments
- access to professional investment expertise and information services
- lower direct and indirect costs due to economies of scale

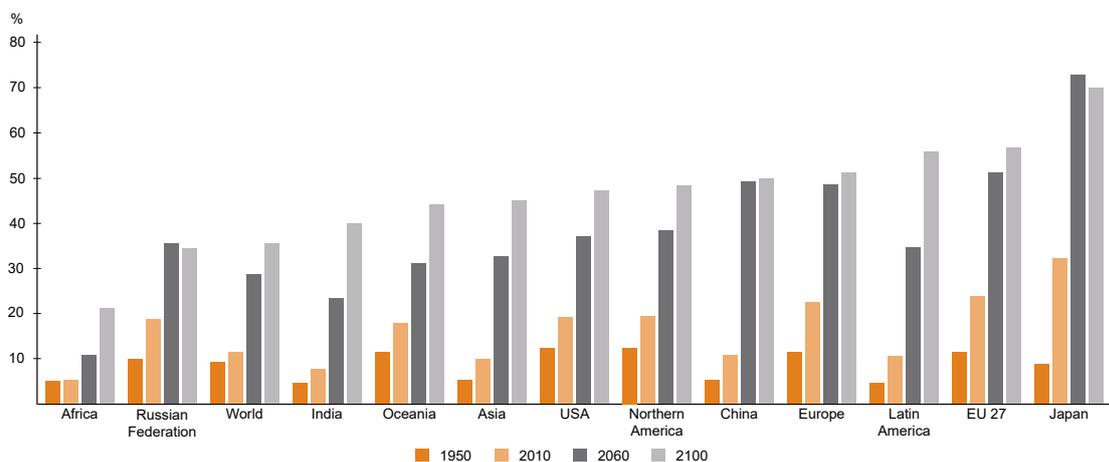
#### How capital requirements affect pension solutions

The nature of the insurance business model — ie, long-term coverage of policyholders' risk in exchange for premiums that are paid upfront — means that insurers need to match their liabilities to policyholders with long-term and stable assets.

If policymakers are to succeed in their goals of increasing retirement saving and wish insurers to remain a fundamental part of a multi-pillar system, they must create and preserve a well-designed prudential framework for insurers. It needs to both ensure security for policyholders and enable insurers to invest in long-term and/or illiquid assets (eg infrastructure).

Given the long-term nature of the business, the framework must provide stability but also be flexible enough to allow insurers to innovate, so that they can develop the products consumers want. ➤

#### Old-age dependency ratio (people aged 65 or above relative to working-age people — 1950, 2010, 2060, 2100 (%))



Source: UN World Population Prospects: The 2012 Revision



**Peter Cooke**  
Senior policy advisor  
*International Association of Insurance Supervisors*

## Best behaviour

The IAIS sets out the initiatives of its busy market conduct working group

Insurance supervision plays a key role in promoting consumer protection. The IAIS's objectives highlight policyholder protection and the need to maintain fair, safe and stable insurance markets in support of this aim.

Historically, in seeking to protect policyholder interests, many supervisors have focused on the financial soundness of individual insurers and, more recently, have extended this focus to groups and conglomerates. Protecting consumers from unfair business practices has in recent years typically been seen as a secondary objective.

The IAIS market conduct working group (MCWG) felt there was a need to raise awareness of the risks that can arise from poor business conduct. This led to an Issues Paper on conduct of business risk and its management published in late 2015. In developing the paper, we were conscious that IAIS material on risk management has historically focused on prudential risks. It therefore highlights that financial sector supervision addresses both prudential and conduct of business risk. It also discusses the differences and interlinkages between prudential and conduct supervision in addressing these risks.

As well as looking at the sources and impacts of conduct of business risk and its place within risk management frameworks, the paper considers the broader consequences of inadequate conduct risk management. These include harm not only to policyholders but also to insurers and the sector as a whole, reminding us of the linkages between conduct of business risk and prudential — or financial soundness — risk.

While some jurisdictions have consistently placed emphasis on conduct supervision through their supervisory structure

(eg in a “twin-peak” model, where there are separate prudential and conduct supervisors), conduct of business is now coming more generally into focus and occupies a higher place on the agenda of many supervisors.

Working closely with the IAIS MCWG, I can attest to the large amount of activity on conduct-related matters reported by members from a wide variety of jurisdictions. This ranges from addressing unfair treatment, such as the mis-selling of certain credit insurance and other insurance add-on products, to studies of what drives consumer behaviour and biases, and more recently to exploring how developments in innovation and technology are changing the insurance business model and the related risks to consumers.

### **New paper on conduct of intermediaries**

The MCWG has been working on an Application Paper on supervising the conduct of intermediaries, due for publication later this year. This is a broad topic with a number of elements that could justify more in-depth discussion in separate papers, such as the increasing use of digital technology in distribution.

The working group is also reviewing the two Insurance Core Principles most relevant to conduct supervision — ICP 18 (Intermediaries) and ICP 19 (Conduct of business) — following a thematic self-assessment and peer review of IAIS members on their implementation of these ICPs. This work has already identified areas where IAIS supporting material may be useful, with conflicts of interest, the effectiveness of disclosure in consumer protection and unfair contract terms among the potential areas identified.

We are seeking IAIS members' views on priorities for future conduct-related initiatives. ➤



Chair, GFIA market conduct working group  
**Leslie Byrnes**  
*Canadian Life and Health Insurance Association*

## Coming together on intermediaries

GFIA welcomes closer cooperation with the IAIS on its work on conduct of business

GFIA continues to be actively engaged with the IAIS on issues related to the fair treatment of customers.

In August 2016, GFIA responded to the IAIS public consultation on its “Application Paper on approaches to supervising the conduct of intermediaries”.

The Paper set out ideas on approaches that supervisors could consider when implementing its Insurance Core Principle (ICP) 18 (Intermediaries) and 19 (Conduct of Business). In GFIA’s view, it is a thoughtful and well-balanced Paper.

### Comments on proportionality

In its submission, GFIA urged the IAIS to reinforce the importance of proportionality and flexibility when supervisors consider introducing new requirements in their supervisory frameworks for intermediaries, so that customers’ access to products and services is not impaired. The IAIS rightly states in its Paper that different business models and their scale should be considered.

**“GFIA urged the IAIS to reinforce the importance of proportionality, so that customers’ access to products and services is not impaired.”**

GFIA also expressed concern that the Paper appears to endorse a shift towards greater insurer responsibility for intermediary conduct, noting that intermediaries are often regulated entities in their own right, with specific accountabilities, and suggesting wording along the lines that “even where there is shared responsibility between intermediary and insurer, this does not dilute the intermediary’s obligations”.

In relation to the disclosure of information on the structure of the charges for a product, particularly for investment-related products, GFIA stressed that any such disclosure should be brief, clear and easy to understand. This reinforces that disclosure for the sake of disclosure is not necessarily in the best interests of customers and that disclosure should not be unnecessarily long and detailed.

With respect to managing conflicts of interest, the Paper gives as an example making structural changes to remuneration. GFIA pointed out the many other tools available to supervisors and the industry to align intermediary and customer interests.

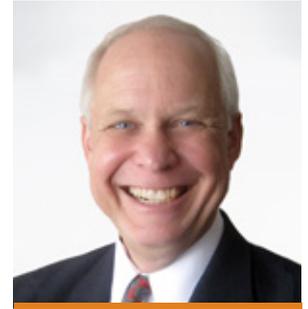
### Face-to-face discussions

Also in August 2016, members of GFIA’s market conduct working group joined the IAIS’s market conduct working group in Quebec City, Canada for a discussion on the Application Paper, as well as possible subjects for ongoing IAIS work.

While the IAIS is already committed to reviewing ICP 18 and ICP 19 by the end of 2017, possible future work could include a deeper look at: what constitutes meaningful disclosure to consumers; digitisation and other emerging distribution channels; and the implications of insurers’ growing use of “big data”.

### The way forward

This was the first time that the IAIS’s market conduct working group had invited GFIA and other stakeholders to attend one of their meetings since IAIS observer rules changed at the end of 2014. It was a productive meeting and was well-received by the IAIS. GFIA would strongly recommend that it becomes an annual event. ➤



Chair, GFIA corporate governance working group  
**David Snyder**  
*Property Casualty Insurers Association of America*

## A matter of principles

GFIA has focused this year on the governance work of the OECD and FSB

Good governance is an essential ingredient in maintaining a healthy insurance industry and in ensuring satisfied customers. Upholding high standards of governance is therefore a shared goal of regulators and insurers around the world.

A year ago, GFIA's focus was the IAIS consultation on its governance-related Insurance Core Principles (ICPs). In the last 12 months, it has turned more to the activities of the OECD and FSB, although at the end of 2016 GFIA will contribute to the IAIS's planned review of the governance aspects of its common framework for the supervision of internationally active insurance groups (ComFrame) (see p10).

### Sector-specific guidelines ...

The OECD sent a questionnaire to stakeholders, including GFIA, for input on its guidelines for insurer governance, with a view to publishing a revised draft in 2016. In May, the OECD launched a public consultation on an updated draft of its guidelines. The OECD's new draft includes some minor changes, but overall does not constitute a strong change of direction or emphasis to guidelines that GFIA generally supports as being appropriately high-level and flexible.

GFIA contributed to the consultation. In particular, it suggested that the proposal to move oversight of products to board level undermines the function of executive management. It proposed instead that the guidelines should make clear that the board should oversee the process of product development from a high-level perspective, rather than overseeing the products themselves. GFIA also took issue with some added provisions that could put actuaries in an untenable position, answering simultaneously to their employer and the supervisor.

### ... and general principles

Besides its sector-specific guidelines for insurer governance,

the OECD in 2015 also produced the more general G20/OECD principles of corporate governance. These were created as supporting material to help work towards the G20 priority of supporting investment as a powerful driver of growth. They were made public in September 2015 at a meeting of G20 finance ministers and central bank governors in Ankara, Turkey.

The overall intention of the principles is to help policymakers improve the legal, regulatory and institutional framework for corporate governance to support economic efficiency, sustainable growth and financial stability. This is primarily achieved by providing shareholders, board members and executives, as well as intermediaries and service providers, with the right incentives to perform their roles within a framework of checks and balances.

These principles were recently subject to a peer review by the FSB, to which GFIA submitted comments. GFIA broadly commended the transparency of the principles. It called for them to remain high-level and outcome-based enough to respect the governance rules and supervisory practices that exist for specific sectors and the well-functioning laws of individual jurisdictions.

In September 2016, GFIA participated as one of the few insurance representatives in an all-day FSB session on its review of governance guidelines. GFIA reiterated its messages and interacted constructively with the regulators. This unique opportunity is a recognition of the significance of GFIA's work.

More generally, GFIA sees emerging and evolving issues of governance, including increasing regulation of compensation and greater pressure for environmental, social and governance-related disclosures. GFIA will maintain its engagement with international bodies that become active in this domain. ➤





Co-chair, GFIA financial inclusion working group  
**Recaredo Arias**  
*Interamerican Federation of Insurance Companies (FIDES)*

## Bridging the protection gap

GFIA focuses on both advocacy and implementation in its efforts to promote financial inclusion

Without insurance, many aspects of a modern society and economy do not function. The protection that insurance provides gives individuals the confidence to go about their daily lives and gives businesses the confidence to innovate and grow. Yet a third of the global population remains excluded from formal financial services.

According to the World Bank, in 2014 only 6% of adults in developing economies had crop, rainfall or livestock insurance, despite so many being dependent on agriculture, and just 17% paid for health cover. Financial exclusion is an issue in developed markets too. Barriers to access can include affordability, geography, culture, administration, logistics, language and education.

The GFIA financial inclusion working group promotes both financial inclusion and financial literacy. Its action plan is based on two pillars: advocacy and implementation, and it has developed a position paper stressing the importance of insurance in economic growth and the need to promote inclusive insurance through public policies. On advocacy, it is engaging with international organisations and stakeholders to promote access to insurance in any financial inclusion strategy, as well as to propose a set of public policies to promote healthy and sustainable inclusive insurance market development. The second pillar's objective is to identify, develop and promote tools to facilitate financial inclusion and to encourage best practices for bringing down barriers that hinder inclusive insurance market expansion.

### Role of the G20

The G20 often includes sustainable development, financial inclusion and protection of the economically vulnerable as core priorities in its annual plan. GFIA meets with representatives of each G20 presidency to present the value of insurance and

how a commitment to financial inclusion helps economies in many ways. The 2016 Chinese G20 presidency has been no exception. GFIA's meetings with the secretariat helped underscore the role insurance can play in achieving public-policy objectives such as reducing poverty rates, ensuring economic stability, promoting inclusive growth and fostering economic efficiency.

### Surveying inclusion trends

This year, GFIA's working group surveyed its members to establish how different jurisdictions define inclusive insurance and microinsurance, and to gather examples of experiences and initiatives. The most common priorities for promoting inclusive insurance were found to be promoting financial education, improving distribution channels and product design, and establishing a more suitable regulatory framework. There is still much that can be done in terms of designing regulation to facilitate further financial inclusion and to foster microinsurance.

Special regulatory measures to foster microinsurance distribution, along with incentives and subsidies, are widely used public-policy tools for achieving financial inclusion. However, if not applied properly, they can have a negative effect, excluding efficient providers from the market, creating moral hazard and encouraging fraud, so there needs to be an open and frequent dialogue between governments and the industry on such policies.

As this Annual Report is published in November 2016, GFIA and its member FIDES will be co-hosting a workshop in Asunción, Paraguay to exchange best practices in microinsurance and inclusive insurance and the distribution channels both require. The International Labour Organization's Impact Insurance Facility will join the workshop. ➤



**Miguel Solana**

Senior technical officer, Impact Insurance Facility  
International Labour Organization

## Opening the door

The ILO's Miguel Solana explains why insurance associations hold the key to inclusive insurance

The World Bank's 2014 World Development Report emphasised the importance of effective risk management as a powerful tool for social and economic development. The following year, the leaders' declaration of the G7 summit in Germany's Schloss Elmau announced their aim to increase by up to 400 million the number of people in the most vulnerable developing countries who have access to direct or indirect insurance coverage against the negative impact of climate change-related hazards by 2020.

These announcements reflect a climate of rapidly evolving risks, which affect national budgets, individual income and everything in between. And in such a climate, the role of insurance in the global social and economic development agenda is becoming more vital than ever. It offers a way for households to protect their route out of poverty. It allows businesses to manage their risks and invest in higher productivity. It provides governments with a tool to create more

resilient societies and to handle the economic consequences of disasters and climate change.

### Opportunities ...

The insurance industry has a vital role in tackling the challenges the world faces in terms of the financial impact of risk and the behavioural change needed to reduce risks. Yet, in order to fulfil this role, it will need to be more inclusive — to reach out to people who have never had an insurance product before. To do so, the industry will need to learn about the needs of new market segments and develop new partnerships, business and operational models fit to provide access to millions of new clients. This inclusive insurance agenda, and the millions of new clients it brings, also represents one of the industry's most important growth opportunities.

### ... and challenges

However, it also poses several challenges for the industry as a whole. How can the insurance industry build trust and ensure that these new clients have a positive first experience? How can the industry develop a culture of risk management and insurance among populations?

Insurance associations are in a unique position to meet these challenges. They are able to help the insurance industry to learn from other experiences around the globe and to support the industry in developing its capacity. They can help create the right environment to foster innovation. They are best placed to engage with governments to promote the role of insurance in development and public-policy objectives. They can promote trust and develop campaigns to educate insurance consumers.

In this way, insurance associations hold the key to creating inclusive and impactful insurance markets, while creating new markets and business opportunities for the industry. ➤



*Farming women in Kirina, Mali, who — within a year — should get access to insurance against climate risks linked to their savings products. Insurance should help to protect their livelihoods and create incentives to invest in more economic activities.*



**Joan Lamm-Tennant**  
Co-chair, working group on  
microinsurance  
*Insurance Development Forum*



**Shaun Tarbuck**  
Co-chair, working group on  
microinsurance  
*Insurance Development Forum*

## Scoring goals

The co-chairs of the IDF working group on microinsurance have ambitious financial inclusion projects

In 2015, the G7 initiative on climate risk insurance, “InsuResilience”, endorsed a goal of expanding coverage for climate risks in vulnerable jurisdictions globally by 400 million people by 2020. Ambitious indeed, but consistent with the UN’s dramatic Sustainable Development Goals. The initial activity of the IDF is based on the view that the G7 target and wider UN Goals can be met with two complementary approaches — microinsurance projects that build financial inclusion and protection programmes — both of which can cover life/health and property/casualty insurance.

### Microinsurance

Under its “Risk Sharing & Transfer: Microinsurance” workstream, the IDF is supporting efforts to reach 100 million unprotected people through microinsurance projects. As early work commences, two initiatives have been identified and more will follow.

One is run by the International Cooperative and Mutual Insurance Federation (ICMIF) and the other by Blue Marble Microinsurance, a consortium of eight insurers. In total, the two organisations represent over 300 institutions in over 190 countries employing more than 575 000 staff whose expertise can be mobilised. This collaboration is unique in bringing

together the mutual and commercial insurance sectors. The ICMIF and Blue Marble collaboration has already committed to reaching 45 million people by 2021. These two groups have 15 projects identified and funded with \$25m over the next five years through both cash and technical assistance. The aim of the IDF working group is to work with civil society to scale up the projects and reach the 100 million people target by 2020.

A little more about the two projects. ICMIF launched the 5-5-5 Mutual Microinsurance Strategy to develop mutual microinsurance in five countries in emerging markets over five years, reaching five million low-income households (effectively 25 million lives). The five countries are Colombia, Kenya, India, the Philippines and Sri Lanka. Blue Marble is a for-profit social enterprise that aims to create a market for microinsurance by using “collaborative innovation” to design and execute ventures enabling risk protection for the emerging middle class. The IDF will add projects to this microinsurance workstream and welcomes GFIA’s assistance in identifying projects and promoting the work with policymakers.

Expansion and development of sovereign protection programmes, such as the African Risk Capacity initiative and the Caribbean Catastrophe Risk Insurance Facility, can support up to 300 million exposed people with new insurance-based protection. The IDF workstream “Risk Sharing and Transfer: Technical Advisory Facilities on Financial Protection” is working to advise on, design and build such partnership programmes with international organisations, governments and the industry. Under these partnerships, governments purchase insurance protection, but the ultimate beneficiaries are exposed communities. The IDF is assembling a team of technical experts that can work directly with the World Bank and other organisations to design efficient partnerships with an effective, targeted risk management and resilience design. ➤

### About the Insurance Development Forum (IDF)

Created in April 2016 by the UN, the World Bank and the insurance industry, the IDF aims to:

- incorporate insurance industry risk-measurement know-how into government disaster risk reduction and resilience frameworks
- build a more sustainable and resilient insurance market in a world facing growing natural-disaster and climate risk



Chair, GFIA trade working group  
**Brad Smith**  
*American Council of Life Insurers*

## Protection against protectionists

GFIA seeks to remove (re)insurance trade barriers and promote open markets

International trade plays an important role in enabling economies to grow. It also facilitates the sharing of skills and knowledge on a global scale, which allows economies to develop more quickly, benefiting citizens and businesses. Global (re)insurers facilitate this growth through innovation, capacity and best practices in products and services. The ability of global (re)insurers to protect and contribute to economic growth is closely tied to their ability to be authorised by regulators to do business and be treated the same as local competitors.

Even as the world becomes more interconnected in practice, several jurisdictions are adopting protectionist (re)insurance measures that could have serious unintended consequences for their economies, leaving them not only isolated but — more dangerously — exposing them to a much greater concentration of risks. The GFIA trade working group addresses such moves with the authorities in question. We also continue to advocate an ambitious set of insurance commitments for the Trade In Services Agreement (TISA) negotiations, which would support open and efficient insurance markets based on sound regulation.

### Indian interventions

While in early 2015 the Indian government took important and welcome steps towards reducing trade barriers and improving access to its (re)insurance market by allowing global reinsurers to establish branches, some of these positive changes were reversed in implementing regulations, which are intended to offer first preference to the government-owned General Insurance Corporation of India. GFIA has written to bodies including the Indian Finance Ministry, the Insurance Regulatory and Development Authority of India (IRDAI) and Invest India (which promotes foreign investment) to highlight concerns about this discriminatory regulatory development, which places

the Indian domestic reinsurer ahead of foreign companies in the order of preference of cessions by Indian insurers.

GFIA has brought to the attention of the Indian authorities the significant positive role that foreign (re)insurers can play in the Indian market. It has stressed that, in addition to capital, foreign (re)insurers bring to the Indian market operational expertise, skills and discipline in underwriting, access to a wider range of products, a strong risk management culture, technological developments and training, all of which can benefit other companies and sectors in India.

Against this background, GFIA has warned that limiting Indian insurers' access to foreign reinsurance would constrain their ability to optimise the management of their risk exposures and corresponding capital requirements, and as a direct consequence could increase costs for both insurers and their customers. Such a move could also result in the accumulation of risks by insurers faced with less interesting opportunities to cede risks, thus compromising their underwriting performance.

### Joint-venture jitters

Another example, representing one step forward two steps back, follows a much-delayed bill that the Indian government enacted in early 2015, which makes it easier for foreign (re)insurers to open joint ventures with Indian firms. Despite this welcome move, subsequent guidelines from the IRDAI unfairly tipped the balance of power heavily in the Indian investor's favour, requiring that both the majority of the directors on the boards and the CEOs of such joint ventures be nominated by the Indian party. Even though some key management executives may be appointed by the foreign investor, they too must be approved by the Indian investor-controlled board.

GFIA has written to the IRDAI to warn that these guidelines

would undermine existing contractual relationships between many foreign insurers and their Indian partners, which would be inconsistent with the new guidelines. GFIA pointed out that the guidelines could discourage new foreign investors from entering the market and existing foreign investors from increasing their stakes. This completely undermines the core goal of the 2015 legislation, which was to increase the amount of investment foreign companies could make in the Indian (re)insurance market. Also, these new IRDAI guidelines appear inconsistent with the government's promises to promote clarity and certainty in foreign investment.

India's most recent regulatory proposals that are of significant concern to GFIA members would require all insurers that have been operating for a certain number of years in the Indian market to list their shares on the Indian stock exchange. GFIA considers such a proposal drastic and unreasonable from a business management perspective. A forced and complete restructuring of Indian shareholding could have significant unintended consequences on the development of the insurance market, since it challenges a board's ability to manage its company. GFIA has urged the IRDAI to conduct a rigorous cost-benefit analysis and to give careful thought to less-invasive regulatory approaches that would achieve its goals of transparency and good corporate governance.

A common theme uniting the three issues above is the lack of adequate public consultation by the Indian government when designing new regulations and guidelines. GFIA has stressed that public comment periods are an integral aspect of global regulatory best practices that provide investors — domestic and foreign alike — with the opportunity to have their perspectives heard on key decisions affecting their investments. GFIA has therefore encouraged the Indian authorities to aim for more stakeholder engagement in their regulatory initiatives.

#### Indonesian inexpediency

Another jurisdiction proposing protectionist regulations is Indonesia. In December 2015, following the merging of the four state-owned reinsurers into Indonesia Re, GFIA wrote again to the regulator to warn of the likely negative effects of its draft regulation introducing compulsory local reinsurance cessions.

GFIA warned that this could lead to risk concentration in the Indonesian insurance market, which could have a severe impact on the market and the wider economy. GFIA stressed that the optimum insurance coverage of natural catastrophe events is only possible through a wide geographic diversification of risks. Local compulsory cessions would diminish this possibility and place additional budgetary strain on the government, as the owner of Indonesia Re, which would have a significant exposure if there were a local natural disaster.

In parallel, GFIA has liaised with other governments, and their delegations in Indonesia, to make them aware that such a restrictive move by Indonesia would place it in breach of its WTO commitments. We have also drawn this issue to the attention of the IMF as inconsistent with the Core Principles of the IAIS, and have urged the IAIS to develop more explicit standards in support of cross-border reinsurance.

#### China concerns

Coordinating through the GFIA trade working group, individual GFIA members have contacted the WTO Technical Barriers to Trade Committee to deliver GFIA's concerns regarding the regulations proposed by the China Insurance Regulatory Commission (CIRC) on the informatisation of insurance institutions, which would require all (re)insurers doing business in China to maintain all their servers in China and to use Chinese software and hardware, including providing encryption access to Chinese officials. ➤



**Bachir Baddou**  
 Director general  
 Moroccan Federation of Insurance & Reinsurance Companies (FMSAR)

## Countdown to COP 22

Bachir Baddou explains why the Moroccan insurance federation takes climate change so seriously

A record 198 events were categorised as natural catastrophes by reinsurer Swiss Re in 2015<sup>1</sup>. In the hottest year since 1850<sup>2</sup>, over half the natural catastrophes were storms and well over a quarter were floods.

Insured losses from those natural catastrophes totalled \$28bn — three times the losses from the year's man-made disasters. From this figure alone, it is clear why the insurance industry devotes significant time and resources to developing and promoting measures that can help communities and businesses both to adapt to such events and to reduce or prevent losses from them.

Given the scientifically-proven link between the steady increase in natural catastrophes (see chart on p35) and global temperature rises, insurers also support efforts to limit climate change. My country, Morocco, is greatly concerned by the effects of climate change. It has over 3 500 km of coastline vulnerable to sea-level rises and an agricultural sector accounting for around 16% of GDP that faces increasing aridity. I was therefore personally heartened by the COP 21 Paris Agreement in December 2015. In Paris, the parties to the UN Framework Convention on Climate Change committed to strengthening the response to the threat of climate change by keeping the global temperature rise this century below 2°C above pre-industrial levels. The wider insurance industry also welcomed this concerted international step in tackling global climate change.

Now, as a matter of urgency, the COP 21 commitments must be turned into actions. As this Annual Report is published, in November 2016, COP 22 is taking place in Marrakesh,

<sup>1</sup> Swiss Re sigma No.1/2016: "Natural catastrophes and man-made disasters in 2015"

<sup>2</sup> According to the HadCRUT4 dataset produced by the UK's Met Office Hadley Centre and University of East Anglia Climatic Research Unit

Under the leadership of Dennis Burke of the Reinsurance Association of America, GFIA's natural catastrophes working group monitors and responds to regulatory issues related to natural disaster mitigation and prevention. It also serves as a forum in which insurance associations from around the world can share solutions that their markets have found for handling natural catastrophes.

Morocco — beginning preparations for the entry into force of the Paris Agreement. There is much to be discussed: the enhanced transparency framework and compliance with it; cooperative approaches; the sustainable development mechanism; and much, much more.

**“Now, as a matter of urgency, the COP 21 commitments must be turned into actions.”**

The insurance industry will be following the COP 22 discussions closely. Insurers themselves are not only changing their own practices to reduce their emission of greenhouse gases, they are also developing products that incentivise policyholders to reduce their carbon footprint and are investing in renewable energies. Adapting to the inevitable consequences of climate change is vital too, not least to safeguard the affordability and availability of insurance cover. As for public authorities, in addition to measures to reduce the emission of greenhouse gases, they must also prioritise adaptation and prevention measures, such as the implementation of strict climate-resilient building and zoning plans.

To coincide with COP 22, my federation, FMSAR, has taken the initiative to engage with Morocco’s public authorities to put in place a roadmap to promote:

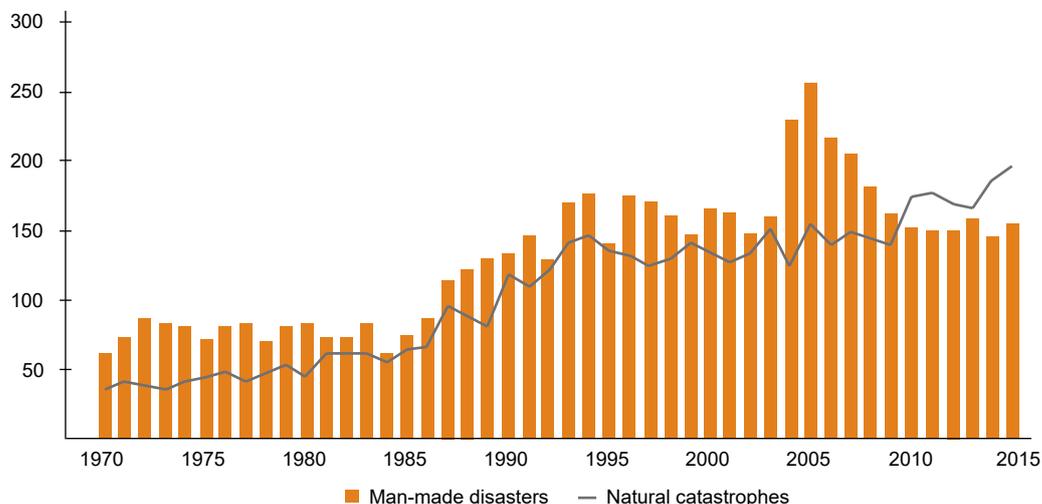
- insurance companies’ responsibility for the social and environmental impact of their own activities
- the financing of and investment in renewable energies
- the management of climate risk by enlarging the quality and quantity of climate risk-related insurance for the farming industry (Morocco is fairly unique in Africa, since over one million hectares are already insured against a number of climate-related perils and that amount is growing)
- “green” savings products, with the savings generated invested ecologically and to the benefit of the environment

Ahead of COP 22, and to inform its discussions, FMSAR

is holding a conference to examine the role of insurance in the fight against climate change — yet another example of the global insurance industry’s commitment to reducing the devastating effects that natural catastrophes can have on lives and economies.

This conference, which was awarded the official COP 22 label, will enable insurers — in front of a large number of European and African participants — to highlight the issues and challenges that climate change poses for our industry and more particularly for Africa, a continent extremely vulnerable to changes in climate. The development of climate-change financing will not be ignored, with a workshop dedicated to investing in green funds and clean energies, and GFIA’s general secretary, Michaela Koller, is speaking at the conference. 🏹

Number of catastrophic events, 1970–2015



Source: Swiss Re Economic Research & Consulting and Cat Perils (Swiss Re Sigma No.1/2016)



Chair, GFIA taxation working group  
**Peggy McFarland**  
*Canadian Life and Health Insurance Association*

## In the line of duty

GFIA has been fulfilling its obligation to ensure tax rules are appropriate for insurers

Policymakers around the world, and international organisations such as the G20 and the OECD, continue to focus on measures to address tax avoidance and evasion. Insurers, in turn, continue to support these broad objectives and GFIA has been engaging with the OECD to ensure that any tax rules are measured and effective, without creating unintended consequences and imposing unnecessary administrative burdens on insurers.

GFIA has been very active over the past year on the OECD's initiatives on base erosion and profit shifting (BEPS) and on some complex US tax developments. In addition, the working group has monitored developments around the OECD's Common Reporting Standard for the automatic exchange of tax information and the possibility of a European financial transaction tax.

### Fast work on BEPS

BEPS refers to tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations. The OECD was moving quickly to try to complete its ambitious two-year BEPS action plan, and finalise the plan's 15 action items in 2015. However, the OECD has continued to work on several of the action plan items in 2016, including on some key issues affecting insurers. During the year, the OECD has published several discussion drafts on action items that could have potentially negative implications for insurance. GFIA responded to the discussion drafts on:

- Action 4: Approaches to address BEPS involving interest in the banking and insurance sectors
- Action 7: Additional guidance on the attribution of profits to permanent establishments

In its responses, GFIA has continued to highlight the

many unique characteristics of the insurance industry that need to be considered by the OECD when developing its recommendations, including the highly regulated nature of the industry and the importance of adequate capital levels and capital management.

GFIA was very pleased to note that its previous efforts to explain the unique nature of the insurance industry appear to have been successful, since both of these recent discussion drafts included comments that are favourable from the industry's perspective, including:

- Recognition that excessive leverage in insurance companies has not been identified as a key BEPS risk at this point in time (ie, indicating BEPS risk is low).
- The Additional Guidance on the Attribution of Profits to Permanent Establishments is directed to entities outside the financial sector, so it should have a minimal impact on insurers, particularly if GFIA's recommendations are accepted by the OECD.

In addition, at the public consultation organised in Paris, France in October, the OECD recognised that increasing the administrative burden for business and tax authorities should be avoided, especially when little profit would be attributed to permanent establishments.

### EU in line

In addition to comments to the OECD, GFIA also commented on the EC's corporate Anti Tax Avoidance Directive, which aims to set out a minimum harmonisation of BEPS implementation in Europe. Given GFIA's recommendations that EU measures should not be more onerous than the OECD's, GFIA was pleased to note that the EU's final approach has become more consistent with the OECD's BEPS recommendations. GFIA's tax working group will monitor individual countries'

implementation of the various OECD BEPS recommendations into domestic law and tax treaties, given the possibility of uncertainty and increased international tax disputes.

#### Automatic exchange

The other initiative that the OECD has moved very quickly on is a global model for the automatic exchange of tax information. The OECD's Common Reporting Standard (CRS) model is loosely based on the US Foreign Account Tax Compliance Act (FATCA), although there are some significant differences. 54 countries (including many European countries) are adopting the CRS in 2016, with the automatic exchange of information beginning in 2017. Another 47 countries are adopting it in 2017, with first exchange in 2018. Detailed guidance has not yet been issued in many jurisdictions that are implementing the CRS in 2016, which has resulted in financial institutions having to make assumptions that could potentially lead to increased compliance costs.

#### Other submissions

GFIA has made submissions on several other complex tax proposals of significance to the industry. These include:

- **US proposed regulations on dividend equivalents** These could potentially result in the application of a 30% US withholding tax on payments under variable and indexed life insurance and annuity contracts, and indemnity reinsurance contracts as they could potentially be considered "dividend equivalents". GFIA's submission to the US Treasury and Internal Revenue Service recommended that payments under annuity, life insurance and reinsurance contracts be excluded from possible treatment as "dividend equivalents".
- **US proposed regulations on debt/equity recharacterisation** These could recharacterise related party financings as equity, even if they are legally debt

that has routinely arisen in the ordinary course of both domestic and international business. GFIA's submission to the US Treasury recommended that transactions conducted in the ordinary course of (re)insurance business be excluded from the scope of the proposed regulations, in addition to a number of more technical recommendations on this complex proposal.

- **India's goods and services tax (GST)** GFIA recommends preferential treatment of insurance under the new GST rules, given insurance's important role in protecting financial security. It asks that insurance be zero-rated under the GST regime and that insurers are eligible for an input tax credit for GST paid on their purchases of input goods and services. If that is not fiscally possible, GFIA recommends insurance be afforded a preferential rate.

#### Keeping an eye on the FTT

GFIA continues to monitor developments on the proposed European financial transaction tax (FTT). To date, interested member states have not been able to reach consensus on an acceptable proposal. There are now just 10 countries left in negotiations; just one above the minimum needed for "enhanced cooperation" among groups of EU governments.

The countries still committed to the FTT are Austria, Belgium, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia, and Spain. While a tentative agreement on the scope of the tax has been reached, a full political agreement is still uncertain. The 10 countries are working towards an end-year 2016 deadline. Should a revised proposal be put forward, GFIA will reiterate its recommendations to minimise the impact on life insurers and their policyholders, and to ensure the FTT does not have unintended consequences, such as a negative impact on investment returns and, implicitly, policyholders' long-term benefits. ➤



**Pascal Saint-Amans**  
Director, Centre for Tax Policy and Administration  
OECD

## It all adds up

The OECD explains why country-by-country reporting will be effective in increasing tax transparency

The OECD's base erosion and profit shifting (BEPS) project is the product of unprecedented cooperation among countries — over 60 countries were directly involved in its initial development. Today, over 85 countries and jurisdictions are participating in the implementation of the BEPS project on an equal footing under the Inclusive Framework on BEPS. The result will be widespread changes in international tax policies and greater transparency, greater alignment of substance with taxation and greater coherence and certainty.

### Lucky thirteen

BEPS Action 13 is a standardised package of transfer-pricing documentation for multinational enterprises. The package provides for three tiers of documentation to increase the transparency of the transfer-pricing positions of multinational enterprises (MNEs) around the world.

First, MNEs give tax administrations a “master file” containing high-level information regarding their global business operations and transfer-pricing policies, as well as descriptions of the value chain and group-financing policies. The master file will be available to all relevant tax administrations.

Second, taxpayers provide detailed transaction-specific transfer-pricing documentation in a “local file”, which is particular to the local entity within an MNE. The local file identifies material related-party transactions, the amounts involved in those transactions and the company's analysis of the transfer-pricing determinations they have made with regard to those transactions.

Third, large MNEs (with consolidated group revenue of €750m or more) will be required to file a country-by-country

(CbC) report. The report includes financial and tax data for each jurisdiction in which the group operates in the world, and is prepared on an annual basis. The required data includes the amount of related party revenue, unrelated party revenue, profit before income tax and income tax paid and accrued. MNEs must also report their number of employees, stated capital, retained earnings and tangible assets in each tax jurisdiction. The CbC report requires reporting of each entity within the MNE, the jurisdiction in which the entities are tax residents and an indication of the business activities in which each entity engages.

Taken together, these three tiers of transfer-pricing documentation require taxpayers to articulate consistent transfer-pricing positions and to provide tax administrations with useful information to assess transfer-pricing risks, make determinations about where audit resources can most effectively be deployed, and, in the event audits are called for, provide information to commence and target audit enquiries.

### Global consensus on a minimum standard

One of the critical outputs of the BEPS Project was the endorsement of four new minimum standards, which each of the members of the Inclusive Framework commit to implementing. The significance of a minimum standard is that there is an expectation that jurisdictions will implement in a consistent manner and in a specific (and in the case of BEPS ambitious) timeframe. CbC reporting is one of those four minimum standards, and jurisdictions around the world have already made significant progress in adopting new legislation to implement it, with the first CbC reports to cover fiscal periods from 1 January 2016. Although CbC reports are designed to be used in conjunction with the master and local files, it is CbC reporting that is being implemented as a global standard.

A global consensus was reached and endorsed by OECD members and the G20 leaders regarding CbC reporting. This established two things that are fundamental to the secure, efficient and appropriate functioning of the CbC reporting standard.

#### Fundamental elements of CbC

First, that the primary means by which CbC reports would be made available to tax administrations is through the MNE filing in the parent jurisdiction. This is followed by the tax administration undertaking international exchange of reports with the tax administrations where the MNE's subsidiaries are resident.

This ensures that CbC reporting is efficient and reduces burdens on MNEs, as they prepare one report according to the same set of domestic rules from year to year, rather than multiple filings around the world. In addition, the well-developed international exchange of information infrastructure allows CbC reports to be exchanged in a standardised electronic format, enhancing efficiency for tax administrations.

Second, that confidentiality safeguards and rules as to appropriate use protect the information exchanged. This is ensured by using the international exchange mechanisms — which operate pursuant to international treaties and which generally include mechanisms for taxpayers to initiate international dispute resolution — as they provide a balanced system of safeguards and protections. This guarantees that commercially sensitive information remains confidential and that tax administrations are held to account for ensuring that they do not directly assess taxpayers on the basis of CbC report information alone, without having undertaken the necessary additional investigations.

#### Project well underway

The implementation of the CbC reporting standard and other elements of the BEPS project is well underway. The global consensus reached ensures a standardised approach to the implementation of CbC reporting. The immediate focus should be on the proper collection of information and on making it accessible to tax administrations. A coordinated and consistent implementation will be necessary.

With the first CbC reports to be exchanged internationally around the world starting in 2018, tax administrations will have an enhanced global picture of the largest MNEs. This is one of the key ways to provide efficient tools to counter BEPS, to strengthen the international tax rules and to give taxpayers greater confidence in tax systems. CbC reports, as well as other information-exchange standards, including the BEPS Action 5 minimum standard on exchange of information on tax rulings and data that will be exchanged under the US Foreign Account Tax Compliance Act (FATCA) and the Common Reporting Standard, will ensure tax administrations are equipped with information to correctly and fairly administer taxes.

The OECD will continue to support this through a peer-review process to ensure that all members of the Inclusive Framework implement and apply the standard consistently, which will assist in delivering the intended policy objectives while also reducing compliance costs for businesses. In addition, the OECD will issue interpretive guidance where it would assist with consistency in global implementation, and, in 2020, review the effectiveness of the CbC reporting standard. All aspects of CbC reporting will be part of this review and, as was the case with the original design of the CbC reporting standard, input from the business community will be vital. 



Chair, GFIA anti-money laundering/  
countering terrorism financing working group  
**Ethan Kohn**  
*Canadian Life and Health Insurance Association*

## The war on terror financing

GFIA helps the FATF to research the use of terrorism-financing indicators

High-profile terrorist attacks around the world keep terrorism in the news and the fight against terrorist organisations on the political agenda. Cutting terrorists' access to funds is one — significant — weapon in governments' armoury to tackle terrorism and, in May 2016, the G7 group of industrialised democracies adopted an action plan on combatting the financing of terrorism. In the plan, it reiterates its support for the work of the intergovernmental Financial Action Task Force (FATF).

### **Insurers: low-risk but committed**

Insurance is at relatively low risk of being either used to fund terrorism or targeted by money launderers. The industry is nevertheless committed to fighting both.

GFIA contributed to the FATF's work in developing internationally endorsed recommendations for combatting money laundering and the financing of terrorism, which were adopted in 2012.

In particular, GFIA supports the risk-based approach that was taken in the FATF recommendations. This allows resources to be targeted where they are needed most. It allows insurers to choose where best to focus their efforts, based on their assessment of the risks.

### **Focus on terrorism indicators**

Having developed its recommendations, the FATF has in recent months focused on monitoring the adoption and implementation of its rules by national governments.

At the start of 2016, the FATF asked GFIA for information on insurers' use of terrorism-financing indicators. This was part of an attempt by the FATF to determine whether the private sector has developed indicators to identify terrorism-

financing risks, such as customer, country, geographic, product, service, transaction or delivery channel risk factors.

### **National authorities must lead**

Insurers consider various risk factors to identify customers or third parties who may be involved in transactions that are part of a scheme to finance terrorist activities. GFIA stressed in its response that insurers nevertheless tend to look to national authorities for help in identifying terrorism-financing risks. The role played by financial intelligence units (FIUs) is key here, as are the national risk assessments (NRAs) that the FATF requires governments to carry out.

**“Insurers tend to look to national authorities for help in identifying terrorism-financing risks.”**

In the US, Italy and Germany, for example, the FIUs disseminate patterns and indicators of suspicious transactions. Several insurance associations support the efforts of these units by regularly exchanging information with them.

National governments carry out NRAs to identify particular countries where the risk of terrorist financing is greater. The assessments also help insurers to identify businesses that may pose a heightened risk. GFIA pointed out to the FATF that it would be useful if the NRAs could include case studies demonstrating how insurance products might be used to fund terrorist activity.

The FATF wishes to develop terrorism-financing risk indicators that could be used by the private and public sectors. This is a follow-up to the report it published in October 2015 on emerging terrorism-financing risks. ➤



# Member associations



Association for Savings and Investment of South Africa (ASISA)

[www.asisa.org.za](http://www.asisa.org.za)  
[info@asisa.org.za](mailto:info@asisa.org.za)



Moroccan Association of Insurance and Reinsurance Companies (FMSAR)

[www.fmsar.org.ma](http://www.fmsar.org.ma)  
[contact@fmsar.ma](mailto:contact@fmsar.ma)



South African Insurance Association (SAIA)

[www.saia.co.za](http://www.saia.co.za)  
[info@saia.co.za](mailto:info@saia.co.za)



Tunisian Federation of Insurance Companies (FTUSA)

[www.ftusanet.org](http://www.ftusanet.org)  
[ftusa@planet.tn](mailto:ftusa@planet.tn)



American Council of Life Insurers (ACLI)

[www.acli.com](http://www.acli.com)  
[contact@acli.com](mailto:contact@acli.com)



American Insurance Association (AIA)

[www.aiadc.org](http://www.aiadc.org)  
[lpusey@aiadc.org](mailto:lpusey@aiadc.org)



America's Health Insurance Plans (AHIP)

[www.ahip.org](http://www.ahip.org)  
[info@ahip.org](mailto:info@ahip.org)



Association of Bermuda Insurers and Reinsurers (ABIR)

[www.abir.bm](http://www.abir.bm)  
[bradley.kading@abir.bm](mailto:bradley.kading@abir.bm)



Association of Mexican Insurance Companies (AMIS)

[www.amis.org.mx](http://www.amis.org.mx)  
[contacto@amis.com.mx](mailto:contacto@amis.com.mx)



Brazilian Insurance Confederation (CNseg)

[www.cnseg.org.br](http://www.cnseg.org.br)  
[presi@cnseg.org.br](mailto:presi@cnseg.org.br)



Canadian Life and Health Insurance Association (CLHIA)

[www.clhia.ca](http://www.clhia.ca)  
[ccsubscription@clhia.ca](mailto:ccsubscription@clhia.ca)





**Chilean Insurance Association (AACH)**

[www.aach.cl](http://www.aach.cl)  
[seguros@aach.cl](mailto:seguros@aach.cl)



**Insurance Bureau of Canada (IBC)**

[www.ibc.ca](http://www.ibc.ca)  
[info@ibc.ca](mailto:info@ibc.ca)



**Interamerican Federation of Insurance Companies (FIDES)**

[www.fidese seguros.com](http://www.fidese seguros.com)  
[rda@fidese seguros.com](mailto:rda@fidese seguros.com)



**National Association of Mutual Insurance Companies (NAMIC)**

[www.namic.org](http://www.namic.org)  
[nalldredge@namic.org](mailto:nalldredge@namic.org)



**Property Casualty Insurers Association of America (PCI)**

[www.pciaa.net](http://www.pciaa.net)  
[PDR@pciaa.net](mailto:PDR@pciaa.net)



**Reinsurance Association of America (RAA)**

[www.reinsurance.org](http://www.reinsurance.org)  
[infobox@reinsurance.org](mailto:infobox@reinsurance.org)



**General Insurance Association of Japan (GIAJ)**

[www.sonpo.or.jp/en/](http://www.sonpo.or.jp/en/)  
[kokusai@sonpo.or.jp](mailto:kokusai@sonpo.or.jp)



**General Insurance Association of Korea (KNIA)**

[www2.knia.or.kr/eng](http://www2.knia.or.kr/eng)  
[cjh@knia.or.kr](mailto:cjh@knia.or.kr)



**Korea Life Insurance Association (KLIA)**

[www.klia.or.kr](http://www.klia.or.kr)  
[info@klia.or.kr](mailto:info@klia.or.kr)



**Life Insurance Association of Japan (LIAJ)**

[www.seiho.or.jp/english/](http://www.seiho.or.jp/english/)  
[kokusai@seiho.or.jp](mailto:kokusai@seiho.or.jp)



**Non-Life Insurance Association of the Republic of China (NLIA)**

[www.nlia.org.tw](http://www.nlia.org.tw)  
[admi\\_dept@nlia.org.tw](mailto:admi_dept@nlia.org.tw)





#### All Russian Insurance Association (ARIA)

[www.ins-union.ru](http://www.ins-union.ru)  
[mail@ins-union.ru](mailto:mail@ins-union.ru)



#### Association of Mutual Insurers and Insurance Cooperatives in Europe (AMICE)

[www.amice-eu.org](http://www.amice-eu.org)  
[secretariat@amice-eu.org](mailto:secretariat@amice-eu.org)



#### Association of Spanish Insurers (UNESPA)

[www.unespa.es](http://www.unespa.es)  
[relaciones.internacionales@unespa.es](mailto:relaciones.internacionales@unespa.es)



#### British Insurance Group (BIG)

comprising:

##### Association of British Insurers (ABI)

[www.abi.org.uk](http://www.abi.org.uk)  
[info@abi.org.uk](mailto:info@abi.org.uk)



##### Corporation of Lloyd's

[www.lloyds.com](http://www.lloyds.com)  
[enquiries@lloyds.com](mailto:enquiries@lloyds.com)

LLOYD'S

##### International Underwriting Association of London (IUA)

[www.iua.co.uk](http://www.iua.co.uk)  
[info@iua.co.uk](mailto:info@iua.co.uk)



#### Dublin International Insurance & Management Association (DIMA)

[www.dima.ie](http://www.dima.ie)  
[executive@dima.ie](mailto:executive@dima.ie)



#### Dutch Association of Insurers (VVN)

[www.verzekeraars.nl](http://www.verzekeraars.nl)  
[j.benning@verzekeraars.nl](mailto:j.benning@verzekeraars.nl)



#### French Insurance Federation (FFA)

[www.ffa-assurance.fr](http://www.ffa-assurance.fr)  
[c.pierotti@ffa.fr](mailto:c.pierotti@ffa.fr)



#### German Insurance Association (GDV)

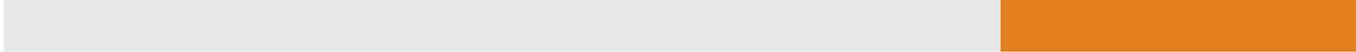
[www.gdv.de](http://www.gdv.de)  
[berlin@gdv.de](mailto:berlin@gdv.de)



#### Insurance Europe

[www.insuranceeurope.eu](http://www.insuranceeurope.eu)  
[info@insuranceeurope.eu](mailto:info@insuranceeurope.eu)





**Insurance Ireland**

[www.insuranceireland.eu](http://www.insuranceireland.eu)

[info@insuranceireland.eu](mailto:info@insuranceireland.eu)



**Italian Association of Insurance Companies (ANIA)**

[www.ania.it](http://www.ania.it)

[aniacea@ania.it](mailto:aniacea@ania.it)



**Polish Insurance Association (PIU)**

[www.piu.org.pl](http://www.piu.org.pl)

[office@piu.org.pl](mailto:office@piu.org.pl)



**Portuguese Association of Insurers (APS)**

[www.apseguradores.pt](http://www.apseguradores.pt)

[aps@apseguradores.pt](mailto:aps@apseguradores.pt)



**Swiss Insurance Association (ASA/SVV)**

[www.svv.ch](http://www.svv.ch)

[info@svv.ch](mailto:info@svv.ch)



**Financial Services Council of Australia (FSC)**

[www.fsc.org.au](http://www.fsc.org.au)

[info@fsc.org.au](mailto:info@fsc.org.au)



**Insurance Council of Australia (ICA)**

[www.insurancecouncil.com.au](http://www.insurancecouncil.com.au)

[info@insurancecouncil.com.au](mailto:info@insurancecouncil.com.au)



**Insurance Council of New Zealand (ICNZ)**

[www.icnz.org.nz](http://www.icnz.org.nz)

[icnz@icnz.org.nz](mailto:icnz@icnz.org.nz)





# Executives



## ◀ President

Governor Dirk  
Kempthorne  
President & CEO  
*American Council of  
Life Insurers*



## ◀ Vice-president

Recaredo Arias  
Vice-president  
*Interamerican Federation  
of Insurance Companies  
(FIDES)*



## Treasurer ▶

Shizuharu Kubono  
Vice-chairman  
*Life Insurance  
Association of Japan*



## Secretary general ▶

Michaela Koller  
Director general  
*Insurance Europe*



## ◀ Membership

Robert Whelan  
Executive director  
& CEO  
*Insurance Council of  
Australia*



## ◀ Past president

Frank Swedlove  
President  
*Canadian Life & Health  
Insurance Association*

## Secretariat



Cristina Mihai  
Tel: +32 2 89 43 081  
mihai@GFIInsurance.org

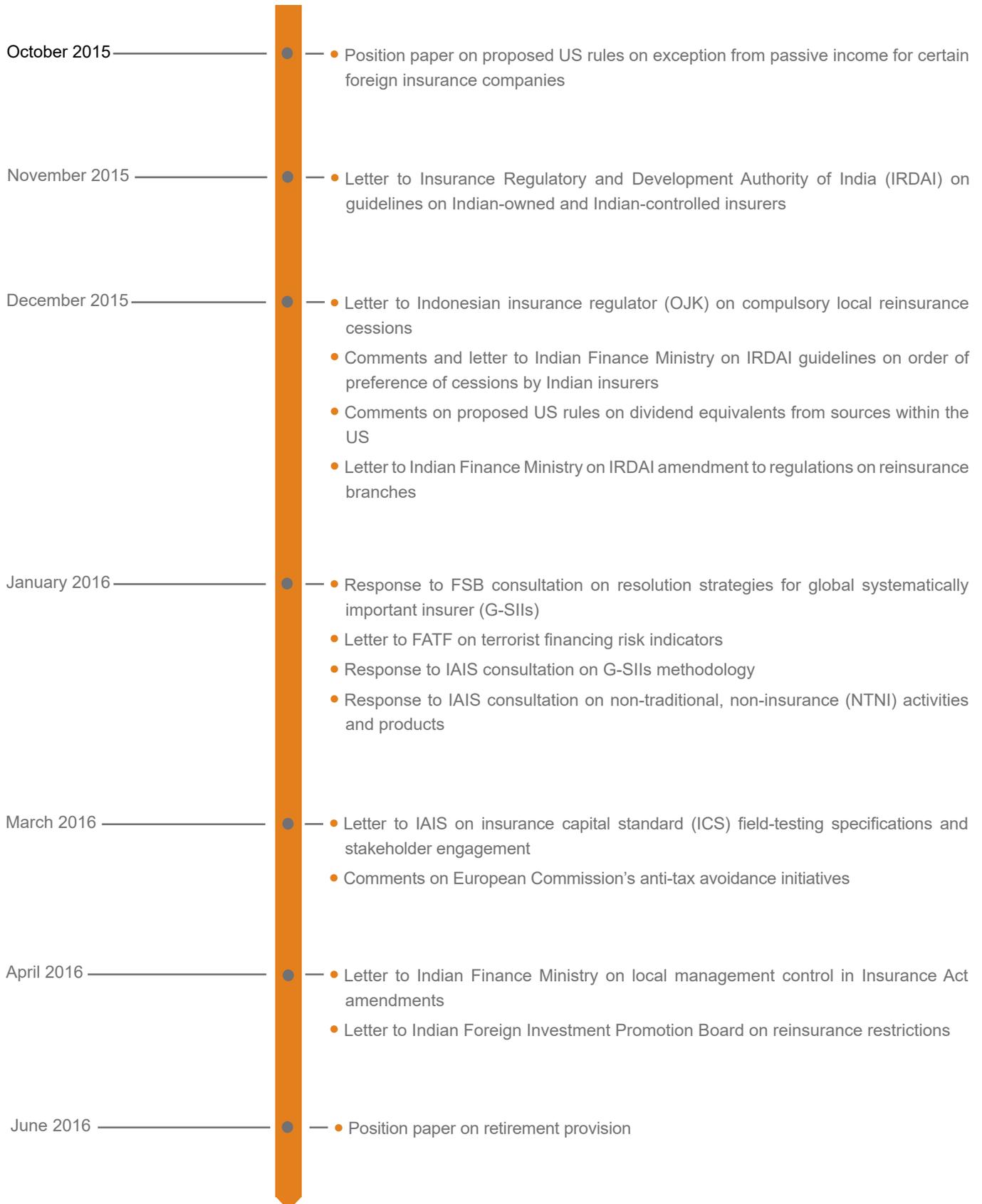


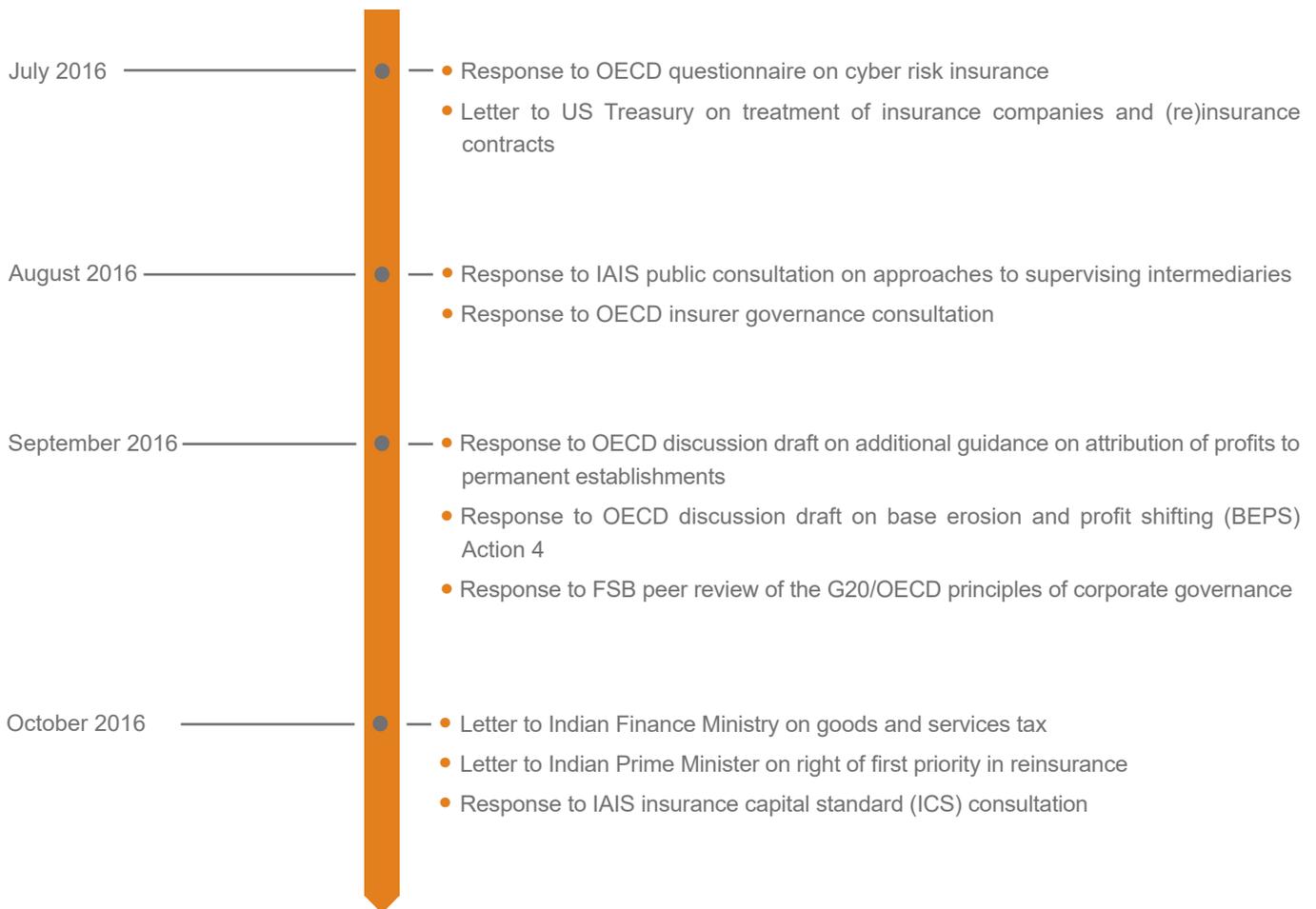
Oscar Verlinden  
Tel: +32 2 89 43 083  
verlinden@GFIInsurance.org



Richard Mackillican (press)  
Tel: +32 2 89 43 082  
mackillican@GFIInsurance.org

# Position papers

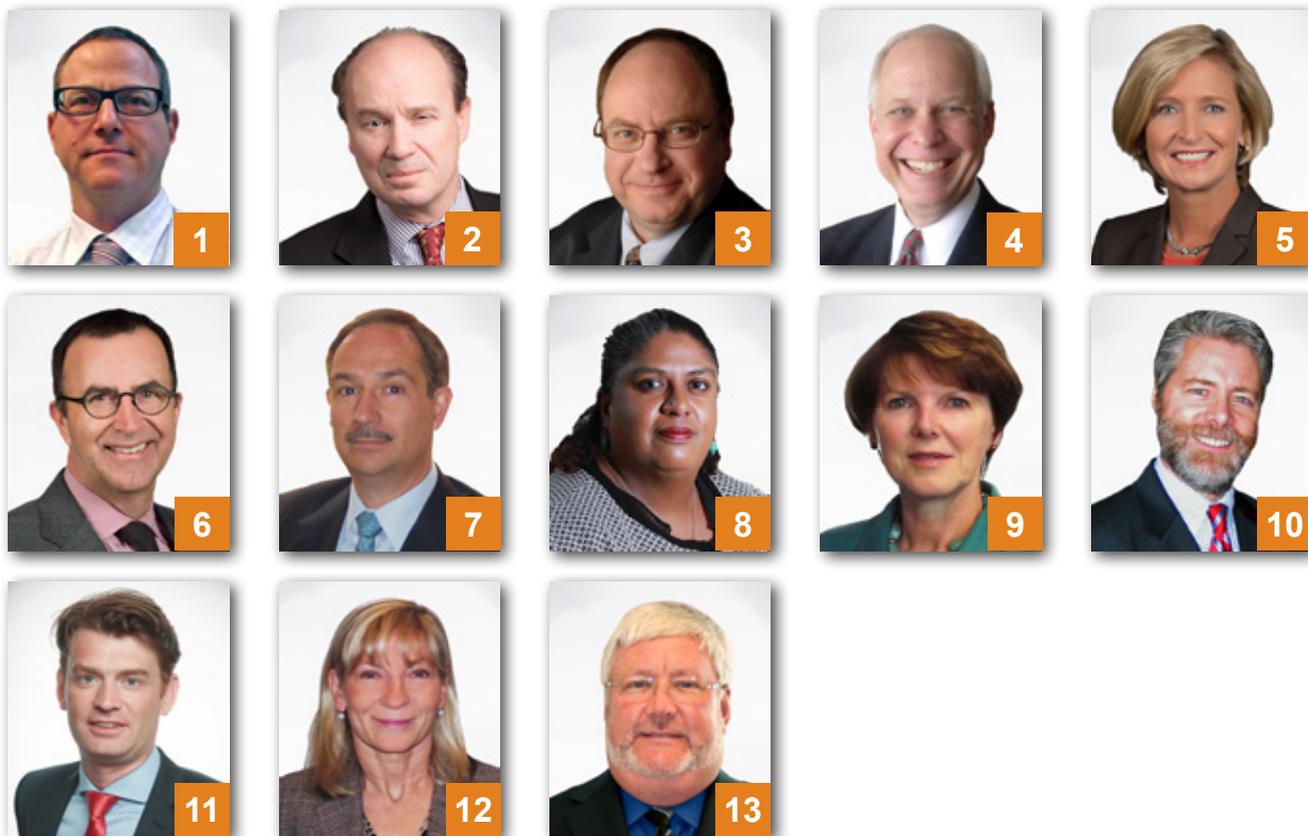




All GFIA's public statements are available on the GFIA website: [www.GFIAinsurance.org](http://www.GFIAinsurance.org)



# Working group chairs



## **1. Anti-money laundering/countering terrorism financing working group**

Chair: Ethan Kohn  
*Canadian Life and Health Insurance Association*

## **2. Capital working group**

Chair: Hugh Savill  
*Association of British Insurers*

## **3. ComFrame working group**

Chair: Stef Zielezienski  
*American Insurance Association*

## **4. Corporate governance working group**

Chair: David Snyder  
*Property Casualty Insurers Association of America*

## **5. Cyber risks working group**

Chair: Leigh Ann Pusey  
*American Insurance Association*

## **6. Disruptive technology working group (ad-hoc)**

Chair: Don Forgeron  
*Insurance Bureau of Canada*

## **7. Financial inclusion working group**

Co-chair: Recaredo Arias  
*Interamerican Federation of Insurance Companies (FIDES)*

## **8. Financial inclusion working group**

Co-chair: Leila Moonda  
*South African Insurance Association*

## **9. Market conduct working group**

Chair: Leslie Byrnes  
*Canadian Life and Health Insurance Association*

## **10. Natural catastrophes working group**

Chair: Dennis Burke  
*Reinsurance Association of America*

## **11. Systemic risk working group**

Chair: Nicolas Jeanmart  
*Insurance Europe*

## **12. Taxation working group**

Chair: Peggy McFarland  
*Canadian Life and Health Insurance Association*

## **13. Trade working group/Ageing society working group**

Chair: Brad Smith  
*American Council of Life Insurers*

The Global Federation of Insurance Association's Annual Report 2015–2016 is available on the GFIA website:  
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GFIA secretariat  
rue Montoyer 51  
B-1000 Brussels  
Belgium

[www.GFIAinsurance.org](http://www.GFIAinsurance.org)