

Tokyo Executive Seminar on Insurance Regulation and Supervision

27-28 September 1999, Tokyo

SUMMARY RECORD

Introduction

The Tokyo Executive Seminar on Insurance Regulation and Supervision was held at the Asian Development Bank Institute (ADBI) in Tokyo on 27-28 September 1999. It was hosted by the Financial Supervisory Agency (FSA) of Japan in collaboration with the Organisation for Economic Co-operation and Development (OECD), the International Association of Insurance Supervisors (IAIS), the ADBI and the Ministry of Finance of Japan. Approximately 90 high-level officials and experts attended the seminar from the insurance authorities of 51 jurisdictions, as well as representatives of four international organisations (European Commission, OECD, IAIS and Joint Forum). The seminar provided a good opportunity for these officials and experts to get together, exchange views and develop a better understanding of key issues on insurance regulation and supervision. More specifically, this seminar focused upon: (1) organisation of insurance supervisory authority, (2) prudential regulation, (3) supervision of financial conglomerates, (4) exchange of information among supervisors, (5) financial sector convergence, and (6) supervision of insurance companies in difficulties.

The seminar started with a welcoming speech by Mr. Masaharu Hino, Commissioner, FSA of Japan. It was followed by four opening remarks delivered by Mr. Hanley Clark, Chairman, Executive Committee, IAIS, Mr. Everette James, Vice Chairman, Insurance Committee, OECD, Mr. Makoto Fukuda, Director-General, Financial System Planning Bureau, Ministry of Finance, Japan, and Mr. S.B. Chua, ADBI.

Session I: Organisation of Insurance Supervisory Authority

Session I intended to explore issues related to the organisational arrangements of an insurance supervisory body, which vary considerably among jurisdictions. The session was divided into two parts: Part A dealt with the aspect of organisational structure, while Part B focused on operational arrangements such as recruitment and funding. Mr. Andre Swanepoel of South Africa moderated this session.

Part A discussed “**Organisation Structure of an Insurance Supervisory Body.**” An overview presentation on the recent international phenomenon to establish an “integrated” financial supervisory body was first made, which was followed by two country presentations.

Mr. Sakura Shiga from Japan made a presentation on an “Overview of organisation structure of an insurance supervisory body.” The establishment of an “integrated” financial supervisory body that covers different financial sectors, including insurance, has emerged as a global trend in the recent years. To date, an integrated supervisory body has been created in such countries as the UK, Canada, Australia, Sweden, Norway, Denmark, Korea, Singapore and Japan, which attended the Meeting of Integrated Regulators hosted by Australian authority in May. The Japanese integrated supervisory body, the Financial Supervisory Agency (FSA), was formed in 1998, in line with the Japanese financial “Big Bang” that intends to lower the walls between the banking, securities and insurance sectors. Financial conglomerates are expected to be active in the Japanese markets in the near future. How to cope with such

conglomerates is an issue for the FSA, as its organisation is structured on a mixed functional and institutional basis.

Mr. Darryl Roberts from Australia then explained the “Organisation of Insurance supervision in Australia.” The Australian Prudential Regulation Authority (APRA) was established in July 1998 as the country’s solo prudential regulator of banks, insurance companies, pension funds and other credit institutions, merging 11 separate supervisory entities. In its first year, it had a “silo” structure in which supervisory functions from different organisations simply sit side-by-side under the APRA banner. However, in August 1999, the APRA’s internal structure was reorganised to be more consistent with the trend towards convergence in the marketplace, and with the Government’s objective of regulating similar risks in a similar manner, irrespective of institutional boundaries. Mr. Roberts pointed out that the challenges for creating integrated supervisors are: merging cultures, training staff, integrating systems, cost cutting, harmonising prudential regimes, establishing credibility in the marketplace, minimising disruption, maintaining operations.

Mr. Manuel Aguilera of Mexico presented the “Organisation Structure of an Insurance Supervisory Body: Mexican Case.” The opening of the Mexican insurance industry to foreign competition in the early 1990s has brought major changes in the market structure and consequently significant adjustments in the regulation and supervision of insurance sector. The regulatory reform has been implemented in the direction of removing “administrative” regulation that causes unnecessary costs to the industry and limits unnecessarily its management freedom, while strengthening solvency regulation to protect policyholder interests. Since 1995, the CNSF, the Mexican insurance commission, has implemented a programme to develop a new supervisory scheme. The new scheme focuses on three “key aspects”: financial, actuarial and reinsurance supervisions. The ruling body of the CNSF is the Board of Government, which is constituted by both regulatory and private representatives in the financial sector. The organisation of the CNSF is designed based on the “key aspects” of supervision, and it is therefore structured on a functional basis.

Part B dealt with issues related to “**Professionalism and Independence of an Insurance Supervisor.**” Among many issues, the major ones in this respect are recruitment and funding of a supervisor. Three presenters provided their respective experience with these questions.

Ms. Lim Shu Chiau of Singapore described “Monetary Authority of Singapore’s Policies on Staff Recruitment and Training.” In order to have effective and efficient supervision, it is pertinent that a supervisory authority has professional, competent and dedicated staff. Recruitment of the right people is the first determinant in ensuring competent staff. Selective recruitment has to be followed by appropriate training to ensure the staff is equipped with up-to-date knowledge and skills to supervise the industry. Apart from recruitment and training, the MAS must also do its best to motivate and retain quality staff. This can be done, for example, by offering attractive remuneration packages, comparable to those in the financial sector, and flexible job rotation schemes. Human resources assets are important for the supervisory authorities, and the MAS is committed to providing well-rounded career development plans, and building a vivacious working environment and culture that each and every staff member can identify with.

Dr. Helmut Muller from Germany discussed his view on “Funding and Independence” of an insurance supervisor. He pointed out five theses. First, insurance supervision has to distinguish itself by high professional quality. Effective supervision requires well-trained and experienced staff and technical equipment comparable to that of the industry. Second, insurance supervision has to be independent from the insurance industry. Only government institutions independent from the industry can inspire the public confidence on which insurance businesses rely. Third, adequate financing is the basis for professional quality. Fourth, adequate financing encounters difficulties in the structure of traditional administration, in

which the insurance supervisor suffers from limitations in staff, equipment and budget as the ministerial bureaucracy does. Fifth, adequate financing and consequently the attendant quality could be achieved by separating the insurance supervision from the organisation of the traditional administration and by transferring it to an independent institution having an independent organisation and budget.

Mr. Nambi Rangachary of India discussed the Indian experience in “Funding and Independence of an Insurance Supervisor.” In line with a move to deregulate the Indian insurance industry, moving away from the monopoly of the State companies, the creation of a new regulatory body, the Insurance Regulatory and Development Authority is currently planned. This regulatory body is designed to be autonomous and independent in its functioning. It would consist of professional members who could make their decisions transparently and independently from political interference, though being appointed by the government. The funding of the Authority would be provided by the industry. In order to avoid a situation in which the payer dictates the piper’s tune, various alternatives including the license charge, a levy based on annual gross premium and fines would be imposed so that the varied interests of different parties could be balanced. In ultimate analysis, one could say that the independence of an insurance supervisor depends primarily on its credibility and commitment to professional competence.

Session II: Two Parallel Workshops (A, B)

Workshop A: Prudential Regulation

Workshop A covered a variety of classic regulatory issues, ranging from solvency regulation to liberalisation of insurance services. During the first half of the workshop, three presenters spoke about the issues related to solvency regulation and its techniques. After a break, three other presenters discussed liberalisation, disclosure, and accounting, respectively. This workshop was moderated by Mr. Rinaldo Pecchioli of the OECD Secretariat.

Mr. Per Simonsen of Norway provided an “Overview of Solvency Regulations and Early Warning Systems.” The solvency position of an insurance company depends at least on: (1) sufficient technical provisions, (2) sound investment assets corresponding to the technical provisions, and (3) a satisfactory solvency margin. These elements are considerably intertwined. The solvency margin requirement could therefore be relaxed if the other two are well satisfied. It should be noted, however, that adequate regulation of solvency capital is always necessary, because however sophisticated, the technical provisions or investment regulations cannot eliminate the risk that the insurer becomes unable to meet its obligations. There are a variety of approaches applied for stipulating statutory solvency requirements, including fixed ratio model, risk-based capital model and the models based on risk or ruin theoretic considerations. In many jurisdictions, one or more control levels of solvency margin are set, which trigger certain supervisory interventions.

Mr. Alfred Gross from the United States then explained the “Risk-Based Capital” method. In the US, the capital requirement for insurance companies is calculated according to the risk-based capital formula. This method has been introduced in response to a number of insolvency cases in the US in the 1980s and 1990s, which highlighted the limitations of fixed minimum capital standards. The risk-based capital formula intends to establish a minimum capital level for each insurer, taking into consideration the actual risks it assumes, such as asset risk, insurance risk, interest rate risk, underwriting risk and administrative risk. There are separate formulas for life, non-life and health insurers. The risk-based capital ratio is not an indicator of the financial strength of an insurer, but a measure for granting insurance supervisors to take specific actions. Four levels are established to trigger particular regulatory interventions, from requiring the insurer to submit a comprehensive financial plan to seizing the control of the insurer by the authority.

Mr. Darryl Roberts of Australia presented the “Pessimistic Scenario Testing in Australia.” The Australian supervisory regime for life insurers has a two-tier capital requirement: Solvency Standard to ensure the ability of a company to meet its current obligations and Capital Adequacy Standard to contemplate sufficient capital as a going concern to accept new business. Each capital requirement needs to be determined, taking into account the scenarios of adverse market movements that may affect the value of the liabilities or assets, so as to secure a certain level of capital even under adverse conditions. The scenario testing has various advantages: it is forward-looking; it can account for many adverse factors occurring concurrently; and it can be tailored to the risk profile inherent in each company’s business mix. Currently, only life insurers are required to undertake this pessimistic scenario testing that is prescribed by the standards, but Mr. Roberts sees that Australian regulatory regimes for insurers evolving in the direction from the blunt ratio model to stress testing and from the prescriptive approach to the internal model one.

After a break, **Mr. Masamichi Kono** of Japan made a presentation on “Liberalisation of Insurance Services.” Market liberalisation improves efficiency, quality and diversity in the market through competition and innovation, and thereby enhances benefits for the consumers and the economy as a whole. Efforts should be made, therefore, to eliminate limitations to market access and national treatment and to review the domestic regulations that effectively restrict the supply of services. This general proposition can apply to the insurance market. It should be noted, however, that for the insurance market, the economic gains of liberalisation must be underpinned by adequate prudential regulation to protect policyholders and to ensure the integrity and stability of the market. The next round of negotiations at the World Trade Organisation, starting at the end of 1999, will include liberalisation of insurance services in its agenda. Many countries have already made commitments on insurance. Mr. Kono suggested a strategy in which the initial emphasis can be placed on liberalisation of commercial presence, followed by that of cross-border transactions and other modes of supplying insurance services.

Ms. Florence Lustman from France explained “International Accounting Rules for Insurance Companies.” There are many reasons to be in favour of a worldwide harmonisation of accounting principles for insurance companies. The internationally comparable financial information on insurance companies is beneficial not only for supervisors but also for the consumers and investors. The increasing number of internationally operating insurers also wish to have a single basis for their accounting. From a practical point of view, however, the harmonisation is not at all an easy task, as accounting practices are actually very close to the heart of the insurance business. Moreover, various factors related to insurance, such as pension and tax systems, are far from being harmonised. Since 1997, IASC has been running a project for developing the international standards of insurance accounting, but this will take time. Ms. Lustman therefore sees a need for an interim, practical solution catering to the immediate concerns of international insurance and reinsurance groups.

Finally, **Ms. Jane Lamb** of Canada discussed “Disclosure: the good, the bad and the ugly.” Disclosure requirement can be an important supervisory tool for the insurance sector as it encourages discipline, honesty and efficiency in management, which also leads to more stability in the market as a whole. In order to ensure effective disclosure, the quality of information is important. The information disclosed must be both verifiable and actually verified. Moreover, in Canada, it must also be approved by the board or “signed off” by a senior official of the company. Almost all information collected on the regulatory returns is now made public in Canada, with limited exceptions, such as details on particular investments or client transactions, proprietary information and the evaluation of the company by the supervisor. The current process of demutualisation of insurance companies intends to apply more stringent disclosure requirements for publicly traded companies. Furthermore, Ms. Lamb regards it as important to improve the comparability of the disclosed information within a sector and, given the evolution of financial sector convergence, with other financial sectors.

Through the presentations and floor discussion, participants shared the sentiment that the environment surrounding insurance regulators and supervisors is changing rapidly. As the business and markets evolve, regulation has to follow quickly in order to avoid becoming obsolete and irrelevant. Some regulators from emerging markets may think that the sophisticated regulatory tools presented today, such as pessimistic scenario testing and the risk-based capital method are not quite relevant to regulating their markets. It may be true today, but will probably not be tomorrow. One of the general trends among the changes in the insurance markets is internationalisation. Whether regulators like or not, this trend will continue in line with advancing telecommunication technologies. In response, international co-ordination becomes increasingly important for insurance regulation and supervision. In this context, regulators should pay great attention to the current efforts in harmonising insurance accounting and disclosure as well as to those of market liberalisation.

Workshop B: Supervision of Financial Conglomerates

Workshop B focused upon the supervisory issues related to financial conglomerates, with which more than one financial supervisor is concerned. The first three presentations intended to share the salient aspects of the discussions underway at the international and inter-sectoral level concerning supervision of financial conglomerates. The following two speakers introduced their views on supervisory challenges in facing financial conglomerates, based on their country experience. Mr. Arend Vermaat from the Netherlands was the moderator of this workshop.

Mr. Knut Hohlfeld from the IAIS Secretariat made a presentation on “Global Co-operation among Supervisors of Different Financial Sectors”. The IAIS has been working with other international financial standard-setting bodies for the Joint Forum on Financial Conglomerates. The IAIS has also been actively involved in other international co-operation efforts such as the Co-ordination Group, the Joint Year 2000 Council, the Multidisciplinary Working Group on Enhanced Disclosure, the Financial Stability Forum (FSF), and the Working Group on Offshore Financial Centres. Moreover, co-operation has been achieved with other international organisations, such as the IMF on the Code of Good Practice, as well as the World Bank, the OECD and UNCTAD. In general, close co-operation between countries around the world is an indispensable foundation for international stability and prosperity. The IAIS plays an important role in global co-operation.

Ms. Johanne Prevost from the Secretariat to the Joint Forum explained “The Work of the Joint Forum.” Supervisory objectives and approaches vary among different financial sectors, i.e. banking, securities and insurance. This variation creates complications for a group-wide approach in conglomerate supervision. The Joint Forum was established in 1996 as a formal group to discuss conglomerate supervision, consisting of regulators of the three sectors in 13 countries. Its mandate covers: exploring practical ways to share information, identifying the impediments to information sharing, establishing criteria for the lead supervisor and its role and responsibilities, and developing supervisory principles. In February 1999, the Forum issued a set of papers on capital adequacy principles, fit and proper principles, principles for supervisory information sharing, and co-ordinator, as well as the supervisory questionnaire. The intra-group transactions and exposures principles and the risk concentration principles are now under consultation. It will work on the issue of transparency of structures under the current mandate. Its new mandate is under consideration, which includes issues common to all three sectors.

Mr. Jarl Symreng of Sweden made a presentation on “Supervision of Financial Conglomerates.” Finansinspektionen is the single financial supervisory authority that covers all Swedish financial sectors. In countries like Sweden, that have an integrated financial environment, a single regulator has many advantages such as a good overview of all financial businesses, a common supervisory framework and methodology structure, easy communication, and a co-ordinated supervisory approach with supervision of individual companies and group supervision. The integration is in progress not only between the financial

market segments but also across the borders. In the Nordic countries, for example, a recent large merger has resulted in a Swedish insurer controlling half of the Norwegian and a third of Finnish insurance markets. Finansinspektionen will therefore be responsible for the overall supervision of the company, based on memoranda of understanding to be negotiated among the supervisors of all three countries.

Mr. Arend Vermaat of the Netherlands discussed “The Supervision of International Financial Conglomerates: Some Issues.” International financial conglomerates are becoming more important for international financial markets. While conglomeration may reduce the overall degree of vulnerability through risk diversification, it has potential threats from a supervisor’s viewpoint, such as capital inadequacy, contagion, intra-group exposures and transactions, and large exposures at a group level. Financial supervisors have to cope with these challenges across borders. Effective co-ordination arrangements among supervisors are essential for the supervision of international financial conglomerates. A list of such arrangements includes: realising a level of familiarity between the supervisors involved, agreeing on information exchange procedures, attaining sufficient transparency of the reviewed group, getting carried out fit and proper tests for the relevant management levels, defining basic financial parameters for a quick scan opinions, and applying tests to prevent multiple gearing.

Finally, **Mr. László Asztalos** of Hungary presented “The Key Issues of Bank-Insurance’s Regulation.” Bank-insurance is a fashionable expression nowadays, without any clear definitions available. In the narrowest interpretation, it means any form of co-operation between licensed insurers and banks. The “financial holdings” interpretation, which Mr. Asztalos recommends, generalises it to indicate the co-operation between the institutions licensed to offer financial services. A broader definition can include the cases in which the institutions supplying non-financial services participate in the co-operation. Co-operation in bank-insurance may be classified at the product and institution levels. At the product level, the co-operation can be either combined or integrated, depending on whether banking and insurance products save their independence or not. At the institution level, the supervisors should pay attention to five aspects: ownership arrangements, compositions of management, credit relationships, distribution and outsourcing.

Session III: Two Parallel Workshops (C, D)

Workshop C: Exchange of Information among Supervisors

Workshop C examined issues of information exchange among insurance supervisors. The first three speakers presented models for information exchange arrangements among supervisors. They were followed by two presenters who discussed exchange of information among supervisors in specific situations. This workshop was moderated by Mr. Edward Forshaw from the UK.

Mr. Edward Forshaw of the United Kingdom started the workshop by his presentation on the “G7 Ten Key Principles and the IAIS Model MOU.” In May 1998, the Finance Ministers of the G7 countries endorsed Ten Key Principles on information exchange and agreed to promote these internationally. The Ten Key Principles envisage a greater level of freedom for exchange of information than currently exists. They include; authorisation to share and gather information; cross-sector information sharing; information about systems and controls; information about individuals; information sharing between exchanges (not applicable in the insurance context); confidentiality; formal agreements and written requests; reciprocity requirements; cases which further supervisory purposes; and removal of laws preventing supervisory information exchange. Since even before these Principles were published, the IAIS has been seeking to encourage the exchange of information between its members. The IAIS model Memorandum of Understanding on exchange of information has been developed for this purpose.

Mr. Alessandro Iuppa of the United States talked about the “Exchange of Information among United States Insurance Regulators” and briefly described the arrangements for information exchange between the 55 US jurisdictions. The National Association of Insurance Commissioners (NAIC) has developed a number of effective information systems. For example, it has created a financial information database containing details of the annual financial statements of insurance companies. The companies are required to file this information through their States to the NAIC, using a common electronic format. The Special Activities Database (SAD) contains limited information on the individuals and companies that have caught the attention of regulators for potentially illegal action. It includes a contact person from whom further details can be obtained. The Regulatory Information Retrieval System (RIRS) holds information on all the individuals and companies that have been subject to enforcement action by any of the States. These US schemes may not be appropriate for all jurisdictions, but they do illustrate the need for a multi-faceted approach to information sharing making full use of technology.

Mr. Henke Bjerre-Nielsen of Denmark presented the “Exchange of Information among Supervisors in EU countries.” Many insurers do business across borders in Europe in the form of cross-border transactions and/or via branches or subsidiaries. Therefore, the exchange of information among the supervisors and the co-ordination of their supervisory actions are of necessity in Europe. Formal impediments to co-operation and exchange of information have been removed, as, thanks to European directives, confidentiality rules have been harmonised and certain “rules of the game” in a protocol on the collaboration have been agreed upon among the European insurance supervisors. In fact, Danish supervisors, for example, meet with other European supervisors on a regular basis and exchange information both formally and informally. Some European supervisors make on-site inspections in foreign branches of their national insurers, which usually includes a visit to the host supervisor. The exchange of information is also important with outside the EU, but the lack of a formal framework is a challenge.

Mr. Steve Butterworth from Guernsey discussed “Insurance Fraud and Exchange of Information.” The origins of the IAIS are rooted in a desire amongst certain insurance regulators to increase the exchange of information on fraud. Insurance fraud can be categorised into claims fraud, insurer fraud, money laundering and fit and proper issues. It tends to be more complicated and internationalised. In general, insurance fraud results from uncontrolled agents, unregulated reinsurers, bad management, poor insurance regulation and gullible customers. In this connection, the Insurance Fraud Subcommittee of the IAIS has made the following recommendations: (1) Monitor reinsurers and intermediaries, and intervene when necessary; (2) Publish a list of reinsurers; (3) Create an accessible database of established insurers, reinsurers and insurance brokers; (4) Establish a standard for enforcement procedures; (5) Establish fit and proper standards; (6) Develop controls on websites. The international insurance fraud could be significantly prevented by such actions as: co-ordinating international regulation; giving more responsibilities to independents, auditors, actuaries and managers; regulating reinsurers; educating insurance consumers; and building effective systems for information exchanges.

Ms. Jane Lamb of Canada made a presentation on “Exchange of Information in a Winding-Up Situation.” Establishing relationships with other supervisors, whether formally through a memorandum of understanding, or informally, is essential to having an efficient flow of information in a crisis situation. This is because in crisis situations the regulator must act quickly and therefore has no time to learn about another supervisory system or to find out whom to contact. When the OSFI faced the case of the demise of a major Canadian insurance-led conglomerate, it co-operated particularly with the regulators in the UK and the State of Michigan in the US. In a crisis situation, one needs to select key regulators to work with, because the information should be kept secret and because there is no time to contact many counterparts. The selection was based not only on the influence of the demise over a given jurisdiction but also on the relationship of trust developed through co-operation in the past. Thanks to such co-ordination, the OSFI was able to act timely and quickly and work the case out smoothly.

Workshop D: Regulatory Issues on Financial Sector Convergence

Workshop D discussed the regulatory issues on financial sector convergence. After an overview presentation, three speakers provided the experience in their respective countries as to the penetration of banks in the insurance market, or “bancassurance.” The following two speakers then discussed the regulation of private pension funds that are sometimes managed by insurance companies. The moderator of this workshop was Mr. Rinaldo Pecchioli.

Professor Lutgart Van Den Berghe from Belgium presented an overview of “Convergence in the Financial Service Industry.” Looking at the market scenery today, one can witness one or another form of financial convergence in many, if not all, developed markets. Financial convergence is a broader concept than the emergence of financial conglomerates. It includes many different forms, ranging from simple cross-selling to integrated services, and from a sector-based structure to a functional, client-oriented organisation. Supervisors cannot prevent this convergence movement, as it is embedded in a much wider trend towards integrated financial services in an effort to offer convenience, switching from mass production to customisation and individualisation. The current sectoral regulation and supervision, however, face difficulties in creating a level playing field to avoid hindering the innovation and expansion of the financial sector. Professor Van Den Berghe argues that the solo-plus supervision, which is currently discussed in relation to financial conglomerates, will probably be only a temporary solution in the broader convergence movement in which the distinction between “lead” and “plus” parts becomes more difficult. Further discussion is necessary as regards a need for a matrix approach, combining institutional and service/product typologies, and a need to go beyond the focus on legal entities in the financial sector.

Mr. Bruno Bézard of France outlined the development of “bancassurance” in France. The influence of banks in the insurance markets has grown remarkably in the last few decades. Especially in the life insurance market, the share of bancassurance has reached more than 60 percent today, while it remains not more than 6 percent in the non-life sector. The development of bancassurance seems to be driven by the various synergy effects raised from combining bank and insurance (especially, life insurance) businesses and also the strategy of the banks against disintermediation in the French financial market of the 1980s. Mr. Bézard sees the development of bancassurance as beneficial for consumers by lowering the price of insurance products as well as contributing to simplification and moralisation in their supply. However, regulators also need to be aware of the risks associated with bancassurance. These include risk concentration at the group level, intra-group transactions and crisis contagion, double use of capital, the opacity of group structure, and the involvement of several supervisory authorities. He stressed that more work to address these risks should be done at both the national and international levels.

Mr. George Reider of the United States described the situation in the US concerning the activities of banks in the insurance sector. Even though banks are not legally allowed to market insurance products, convergence between the banking and insurance sectors is not uncommon in the US. The selling of insurance products by banks has already been admitted by Court decisions. The recent merger of Travelers Insurance and Citicorp suggests the emergence of financial conglomerates as well. Bills have been submitted to Congress in order to allow banks to do insurance business and to own insurance companies. The Commissioners of Insurance will continue to supervise the activity related to insurance products, but given the general trend towards financial sector convergence, deeper co-operation, especially exchange of confidential information, with banking supervisors is necessary.

Mr. Chee Siew Eng from Malaysia discussed “The Regulatory and Supervisory Challenges for Bancassurance in Malaysia.” While the insurance industry has grown rapidly over the last decade in Malaysia, the market penetration of insurance products remains at a low level. This is partly because the industry, especially the life sector, is almost totally reliant on the agency channel for distribution, which involves a vast sales force with low productivity and quality. In response, Bank Negara Malaysia, which

supervises both the banking and insurance sectors, is in favour of bancassurance. In Malaysia, bancassurance arrangements are of two forms: strategic alliance with which banks merely market insurance products using their customer bases, and full integration through merger and acquisition between banks and insurance companies. So far, the former model has been more popular but less successful. From Malaysia's experience, the main regulatory issues in the development of bancassurance include: the financial and administrative responsibilities of the insurers, the appropriate passing-on of lower distribution costs to benefit customers, training of the sales force, protection against personal information abuses and pressure selling, and the commitment by the management in promoting insurance products.

Ms. Mónica Cáceres Ubilla of Chile explained the "Regulation of Insurance Companies and Pension Funds Administrators in Chile." This decade, the social security sector has been strongly incorporated into the financial sector in Latin America, especially in Chile where the private pension system emerged in the early 1980s. Both pension fund administrators and insurance companies are active in the service of providing annuities after retirement. Being the major institutional investors in Chile, pension fund administrators and insurance companies are subject to very similar investment regulation, though the latter have a greater degree of flexibility in investment. For example, insurance companies may invest, up to certain limits, in mortgages, mutual funds and real estate abroad, which is not allowed for pension fund administrators. Eighteen years after the introduction of the private pension system, efforts are continuing to improve its regulation. The legal changes currently proposed are to allow discounts on commissions and creation of multiple funds by a pension fund administrator, the extension of the measurement period for "minimum yield" required to pension funds administrators, and "early retirement discounts" so as to reduce high commissions charged by insurance brokers.

Mr. Matthew King of the European Commission made a presentation on "Supplementary Pensions in the European Union: Funding Retirement through Private Savings." Pensions attract considerable attention in Europe, as the society is ageing rapidly: the number of workers per pensioner is expected to decrease sharply from the current four to two in 2020. Among the three pillars of pension structure, the EU debate focuses upon pillar 2: pension funds linked to firms. The Community intends to make these funds, where they are set up, more efficient through increased returns and security and through increased competition. Due to their long-term nature, small changes in the real rate of return make a huge difference in pension funds. In order to help alleviate the future tax burden in the pension system, it is vitally important to invest the funds productively. In this context, investment in the real economy, new technologies and start-ups with great diversity including those in emerging market countries, is recommendable. Mr. King also asserted that investment in the stock market should be preferable to that in government bonds as stocks are more profitable and less volatile over the long run.

In the floor discussion, participants reconfirmed that there is a general trend towards more convergence in the financial sector. Regulators now need to realise that the insurance sector is becoming a part of a broader industry, though it may retain some special aspects. A participant argued, however, that this general trend should not necessarily end up with global financial conglomerates everywhere. There was a case that the decision by management of a bank to acquire an insurance company was put in question by investors. Ultimately, corporate strategy on whether to be a conglomerate or instead focus on core business will be tested by the market. Another attendant pointed out that when an institution does more than one line of business, cross subsidy between the business lines could be an issue for financial supervisors. The institution may distort competition in a financial market, using the profits gained from its operations in other sectors.

Session IV: Crisis Management - Supervision of Insurance Companies in Difficulties

Session IV centred on the issue of how the supervisors should prepare and handle an insurance company in distress. Three speakers made the relevant presentations based on the respective experience in

their countries, which was followed by a thematic presentation on policyholder protection schemes. The moderator of this session was Mr. Andre Swanepoel from South Africa.

Mr. Jean-Louis Bellando of France presented “The Control of Insurance Companies in Difficulties.” The protection of policyholders is essentially provided through financial supervision of insurance companies, first as prevention and subsequently as a cure if necessary and possible. When the supervisor finds an ailing company, it asks the company to submit a recovery plan. The implementation of the plan may be ensured by safeguard measures, such as restriction on asset disposals, to be taken if the company fails the implementation. The supervisor may further ask the company to seek external support in such forms as mergers and transfer of the portfolios of contracts. If the company keeps deteriorating after all these efforts, the supervisor must put an end to its business, either by the compulsory transfer of its portfolio or by the withdrawal of its licence. The latter should be the last resort, as in France it automatically leads to the liquidation of the company. A guarantee fund was introduced in France in 1999. In general, however, such a fund does not have sufficient resources for coping with a systemic crisis.

Mr. Andre Swanepoel of South Africa explained the experience of South Africa on supervising insurance companies in difficulties. Over the past fifteen years, eight insurance companies could be classified as those in crises in the South African market. Out of them, two were managed back to financial soundness, three were wound up, and the remaining three were liquidated after transfer of the business to other insurers. In all cases, policyholders were well protected, though in those years the Insurance Registrar, the South Africa’s insurance supervisor, had very limited powers to rectify the situation. The new life and non-life insurance acts, promulgated in January 1999, give more options and powers to the Registrar, such as the authority to ask an insurer for a plan of action. Mr. Swanepoel concluded his presentation by mentioning: (1) Winding up or managing companies in crisis situations is an important issue for policyholders and claimants, since there are no protection or guarantee funds in South Africa: (2) Intervention of supervisors should be treated with respect and circumspection, because insurance is based on trust between the policyholder and insurance company.

Mr. Alan Wong from Hong Kong, China, shared his experience in crisis management of insurance companies. Crisis management starts with the setting up of an early warning system. The supervisor should find the early warning signals and assess the seriousness of situations through its supervisory work. Concurrently, the supervisor needs to ensure the implementation of preventive measures by companies, which include fit and proper management and adequate reinsurance arrangements. When necessary to safeguard the interests of policyholders, the supervisor should intervene by appropriate regulatory actions. In Hong Kong, protection would also be provided to policyholders in winding-up through the preferential treatment of insurance claimants and assistance under insolvency funds. In a financial crisis, insurers face various problems. The regulator should be prepared against such a situation by an effective early warning system and preventive measures and adequate powers to handle crisis situation, as well as by greater market transparency and a reasonable balance between the market mechanism and regulation.

Finally, **Professor Gerry Dickinson** from the United Kingdom gave a presentation on “Policyholder Protection Funds and Guarantee Schemes: Some Theoretical and Practical Issues.” The protection fund/scheme concept was first developed for banking and then extended to other financial sectors. While there are pros and contras for the protection fund/scheme, it has been introduced in most of the advanced market countries. Professor Dickinson presented six key principles for developing protection schemes in insurance as follows: (1) The scheme must contain incentives to supervisory authorities to actively explore other solutions: (2) The design of scheme must consider moral hazard, equity and administrative cost: (3) The scheme must not come into operation only when liquidation has taken place, but it must allow for earlier action: (4) The scheme should only benefit policyholders and third parties, it should not benefit managers, owners or other creditors of a failing insurance company: (5) The design of the scheme must carefully consider the international dimension: (6) Within a country, there will be a need

for greater co-ordination between insurance protection schemes and protection schemes for the banking and securities industries.

Concluding Session

The moderators summed up their respective workshops. A summary was also provided by Mr. Roberts for Session I and by Mr. Wong for Session IV. The seminar was successfully concluded and participants expressed their appreciation to the FSA of Japan and to the other organisers. The success of the seminar was also confirmed by the evaluation questionnaire in which most, if not all, participants answered that the seminar was useful and well organised.

In the concluding session, several attendants voiced their wish that this kind of seminar would continue to be organised in the future. A variety of topics were suggested in the questionnaire for future meetings, which include reinsurance, outsourcing of supervisory functions, crisis management, supervision of financial conglomerates, risk-based capital, emerging market issues and so on. It was generally agreed that the continuation of this kind of effort in the future would be of the utmost importance.

Attachments:

- Seminar Agenda
- Note to the Agenda
- List of Participants

Tokyo Executive Seminar on Insurance Regulation and Supervision

27-28 September 1999, Tokyo

PROGRAMME

Day 1: Monday 27 September

08:00 Registration

09:00 Opening

Moderator: Mr. Sakura Shiga (Japan) and Mr. André Swanepoel (South Africa)

- Mr. Masaharu Hino (Financial Supervisory Agency, Japan)
- Mr. Hanley Clark (International Association of Insurance Supervisors)
- Mr. Everette James (Organisation for Economic Co-operation and Development)
- Mr. Makoto Fukuda (Ministry of Finance, Japan)
- Mr. S.B.Chua (Asian Development Bank Institute)

09:30 Session I: Organisation of Insurance Supervisory Authority

Moderator: Mr. André Swanepoel (South Africa)

Part A: Organisational Structure of an Insurance Supervisory Body

- Overview: Mr. Sakura Shiga (Japan)
- - Country experience: Dr. Darryl Roberts (Australia)
- Country experience: Mr. Manuel Aguilera (Mexico)
- Floor discussion

Coffee break

Part B: Professionalism and Independence of an Insurance Supervisor

- Recruitment and training of staff: Ms. Lim Shu Chiau (Singapore)
- Funding and independence: Mr. Helmut Müller (Germany)
- Funding and independence: Mr. Nambi Rangachary (India)
- Floor discussion

13:00 Lunch break (Tokyo Kaikan, the 35th floor of Kasumigaseki Building)

15:00 **Session II: Two Parallel Workshops**

Workshop A: Prudential Regulation

Moderator: Mr. Rinaldo Pecchioli (OECD)

- Overview of solvency regulation and early warning system: Mr. Per Simonsen (Norway)
- Risk-based capital method: Mr. Alfred Gross (USA)
- Pessimistic scenario test: Mr. Darryl Roberts (Australia)
- Floor discussion

Coffee break

- Liberalisation of insurance services: Mr. Masamichi Kono (Japan)
- International accounting rules for insurance companies: Ms. Florence Lustman (France)
- Disclosure principles: Ms. Jane Lamb (Canada)
- Floor discussion

Workshop B: Supervision of Financial Conglomerates

Moderator: Mr. Arend Vermaat (Netherlands)

- Co-operation among supervisors of different financial sectors: Mr. Knut Hohlfeld (IAIS)
- Introduction to the Joint Forum: Ms. Johanne Prevost (Joint Forum Secretariat)
- Models for co-ordination of financial supervisors: Mr. Jarl Symreng (Sweden)
- Floor discussion

Coffee break

- Supervisory issues for international financial conglomerates: Mr. Arend Vermaat (Netherlands)
- Supervisory issues for national conglomerates: Mr. László Asztalos (Hungary)
- Floor discussion

18:00 End of Day 1

19:00 Reception (Room "Zuiun", the B1 Floor of ANA Hotel, hosted by the Commissioner of the Financial Supervisory Agency of Japan)

Day 2: Tuesday 28 September

09:00 **Session III: Two Parallel Workshops**

Workshop C: Exchange of Information among Supervisors

Moderator: Mr. Edward Forshaw (UK)

- G7 ten key principles for exchange of information and the model MOU of IAIS: Mr. Edward Forshaw (UK)
- Exchange of information among supervisors in USA: Mr. Alessandro Iuppa (USA)
- Exchange of information among supervisor in EU countries: Mr. Henrik Bjerre-Nielsen (Denmark)
- Floor discussion

Coffee break

- Insurance fraud and exchange of information: Mr. Steve Butterworth (Guernsey)
- Winding-up and exchange of information: Ms. Jane Lamb (Canada)
- Floor discussion

Workshop D: Regulatory Issues on Financial Sector Convergence

Moderator: Mr. Rinaldo Pecchioli (OECD)

- Overview of regulatory and supervisory issues on financial sector convergence: Prof. Lutgart Van Den Berghe (Belgium)
- Country experience (bank/insurance): Mr. Bruno Bézard (France)
- Country experience (bank/insurance): Mr. George Reider (USA)
- Country experience (bank/insurance): Mr. Chee Siew Eng (Malaysia)
- Floor discussion

Coffee break

- Country experience (insurance/pensions): Ms. Mónica Cáceres Ubilla (Chile)
- Supplementary pensions in the European Union: Funding retirement through private savings: Mr. Matthew King (European Commission)
- Floor discussion

12:00 Lunch break (Tokyo Kaikan, the 35th floor of Kasumigaseki Building)

13:30 **Session IV: Crisis Management: Supervision of Insurance Companies in Difficulties**

Moderator: Mr. André Swanepoel (South Africa)

- Country experience: Mr. Jean- Louis Bellando (France)
- Country experience: Mr. André Swanepoel (South Africa)
- Country experience: Mr. Alan Wong (Hong Kong)
- Policyholder protection schemes and guarantee funds in the event of insurer insolvency: Professor Gerry Dickinson (UK)
- Floor discussion

16:10 Coffee break

16:30 **Concluding Session**

Moderator: Mr. André Swanepoel (South Africa)

- Reports by workshop moderators
- Floor discussion on future work
- Closing remarks: Mr. Sakura Shiga (Japan)

18:30 End of the Seminar

19:00 Reception (“Royal Room”, the 34th floor of Kasumigaseki Building, hosted by the Life insurance Association and the Marine and Fire Insurance Association of Japan)

Tokyo Executive Seminar on Insurance Regulation and Supervision

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NOTES TO THE AGENDA

Procedural Issues

1. The second and third sessions will have two parallel workshops respectively (Workshop A and B for Session II, and Workshop C and D for Session III). Participants are expected to attend either of the two workshops in each session.
2. The presentations should be limited to approximately 15-20 minutes each in all sessions and workshops. This stringent time limit is required in order to have ample time for general discussion. Participants are invited to provide texts of their major interventions, background papers or other documents on the subject of this seminar.

Session I: Organisation of Insurance Supervisory Authority

Part A: Organisational structure of an insurance supervisory body

3. The organisation of a body which is responsible for insurance supervision varies considerably among countries, while the regulatory function is generally, at least partly, reserved to the concerned ministry. In some jurisdictions, particularly those that have small insurance markets, the concerned ministry tends to conduct supervision of insurance companies as well. In contrast, the economies that have larger markets tend to create supervisory bodies separately from the ministries.
4. Recently, one can observe a general tendency to establish an “integrated” financial supervisory body which covers not only insurance sector but also banking and other financial sectors, while a “solo” supervisory body specialising in the insurance supervision is still common worldwide. This movement seems driven by the fact that the traditionally segregated activities of various financial institutions have been increasingly interrelated and converged. It should be noted, however, that the currently existing integrated supervisors differ significantly in their scope, mission, power, structure, management and relationship with the ministry, etc.

Key items for discussion:

- What kinds of factors do participants regard as important and/or influential in determining the organisation of an insurance supervisory body? How do the delegates from integrated financial supervisory agencies explain the momentum for the establishment of such integrated bodies?

- What are the advantages and drawbacks of an integrated financial supervisor in comparison with a solo supervisor specialised for insurance sector? How could such drawbacks be relieved in an integrated organisation? On the contrary, how could such advantages be achieved in a specialised body?

Part B: Professionalism and independence of an insurance supervisor

5. However organised, insurance supervisors need to pursue professionalism and independence in their operations. In order to maintain the professionalism in supervisory operations, a high-quality staff with sufficient expertise in the insurance business is indispensable. In some countries, the supervisors often recruit qualified experts from the industry or even outsource some parts of their operations. In other jurisdictions, however, this practice is not common, because it is sometimes thought to tarnish the independence of supervision, or otherwise, simply because the supervisors cannot afford such “high market price” experts. In this case, the supervisors have to train their staffs and keep them equipped with updated expertise, which is not an easy task.

6. Independence of supervision is often discussed in relation to the financial resources of supervisors. In many of the advanced market countries, the supervisors raise the funds necessary for their activities from the industry, considering that the supervision is a kind of service for the companies. It is pointed out, however, that financial reliance on the industry could cause conflicts of interest in the supervisors and deteriorate people’s confidence in the quality of supervision. On the contrary, in the countries where the supervisors are financed by the government, they often have serious budget constraints for a sufficient level of operations and are likely to be exposed to political pressure.

Key items for discussion:

- In the jurisdictions of participants, how does the insurance supervisor recruit its staff: from industry, other parts of the government or new graduates? What are the merits and drawbacks for such ways of recruitment? How can the quality of the staffs be effectively improved and maintained? How can the supervisors attract and retain qualified staff?
- How should an insurance supervisory authority be financed? In what situations is financing from the industry considered to be appropriate or inappropriate? How can the authority ensure sufficient funds for its operations? How can the authority keep its independence from the financial sources?
- Do participants have in mind any other issues than the human and financial resources that are important for insurance supervisors in ensuring their professionalism and/or independence?

Session II and Session III

Workshop A: Prudential Regulation

7. Insurance supervisors need to implement adequate supervision over the entire operations of insurance companies under their respective responsibility. Among various aspects of the activities of insurance companies, the supervisors should especially focus on:

- compliance of insurers with relevant legislation and contracts, and
- financial soundness of insurers to meet fully their commitments to policyholders.

In order to exercise their supervision effectively, the authorities should have accurate understanding of insurers’ operations through regular examinations. On-site as well as off-site inspections on the insurance companies are thus the central work of insurance supervisors.

8. **Although adequate tarification and technical provisions are the main pillars for solvency control, insurance supervisors need to pay particular attention to the capital adequacy of insurance companies. The level of the capital base or solvency margin, which serves as a financial buffer against possible adverse business developments, provides the information on financial standing of an insurance company and alerts the supervisor to take necessary actions for protecting policyholders. It is common in many jurisdictions to establish the so-called early warning system in which specific supervisory interventions are prescribed according to the levels of the capital base. Moreover, in order to reinforce the assessment by the capital base, the supervisors in some countries adopt “stress test” or “pessimistic scenario test” in which the robustness of the financial soundness of an insurance company and its capacity to face difficult financial conditions are monitored.**

9. Rapidly evolving globalisation of the insurance business puts pressure on insurance authorities to seek for more co-ordination even in prudential regulation. The international co-ordination in prudential regulation will foster a level playing field for insurance companies in various jurisdictions and thereby will supplement market liberalisation in encouraging the proper functioning of market mechanism on a global level. In this context, the Accounting Sub-Committee of the International Association of Insurance Supervisors (IAIS) is currently discussing international accounting rules for insurance companies, in co-operation with the International Accounting Standards Committee (IASC). Proper accounting practices should establish the basis for effective supervision as well as efficient management of a company. Moreover, they can provide accurate information for policyholders and investors through appropriate disclosure process.

Key items for discussion:

- How can the insurance authorities exercise their supervision most effectively to prevent various troubles in relation to the activities of the insurance companies at an early stage? How do they try to ensure adequate tarification and technical provisions covered by sufficient assets?
- How should solvency or capital adequacy of an insurance company be assessed? How should a solvency margin be calculated (according to the types of insurance business, i.e. life, non-life, etc.)? What are the difficulties in the calculation? How much can the supervisors rely on the calculated figures in their assessment of insurance companies? What kinds of prudential regulation are available as well as effective in order to reinforce the solvency margin regulation (tariff control, quantitative restriction on investment by category, etc.)?
- In the jurisdictions of participants, how important are solvency margin ratios in assessing the financial soundness of an insurance company? Do they use particular supervisory measures to reinforce solvency margin supervision such as the stress testing?
- Do participants have any comments on the accounting rules currently discussed in the IAIS Accounting Sub-Committee and the IASC? Are they generally acceptable?
- What is the role of disclosure in insurance regulation? How does the disclosure of insurance companies function to strengthen market mechanism?
- In what areas of insurance regulation do participants see the need for international co-ordination? Do participants agree that the international co-ordination in prudential regulation is desirable?

Workshop B: Supervision of Financial Conglomerates

10. Nowadays, there are a number of corporate groups operating domestically or internationally. When a corporate group contains different financial institutions, especially at least two of: a bank, a securities firm and an insurance company, it is called a “financial conglomerate.” The presence of financial conglomerates in various financial markets is increasing, which poses new challenges for financial supervisors.

11. As concerns an insurance company, which constitutes a part of a conglomerate, the insurance supervisor cannot be satisfied with investigation of the particular company, as its financial basis and management are interdependent with the other companies in the conglomerate. The insurance supervisor now needs to check the conglomerate as a whole in order to properly assess the financial and managerial adequacy of its affiliated insurance company. Moreover, in the case of a financial conglomerate, more than one supervisor oversees the responsible affiliates and then the conglomerate from different aspects and in different manners. Co-ordination among the concerned supervisors is necessary not only to avoid excessive supervisory burdens on conglomerates and their affiliates, but also to prevent synthetic errors in the supervision.

12. These supervisory challenges have been examined in individual jurisdictions as well as the international organisations of financial supervisors, i.e., the Basle Committee on Banking Supervision, the International Organisation of Securities Commissions (IOSCO) and the IAIS, and more recently, in their combined platform: the Joint Forum on Financial Conglomerates. This year, this Joint Forum issued a package of documents on supervision of financial conglomerates, which contain sets of supervisory principles for capital adequacy requirements, fit and proper rules, supervisory information sharing, and the role of co-ordinators in conglomerate supervision¹.

Key items for discussion:

- What are the commercial advantages and the potential risks resulting from combining different financial sector activities in a financial conglomerate? How about the case of a financial conglomerate that includes non-financial businesses?
- How can the supervisory authorities, whether integrated or specialised for insurance, assess such risks, without impeding the commercial benefits?
- In the views of participants, how important is the co-ordination among the supervisors of a particular financial conglomerate? What kinds of arrangements can be established, within rather a short timeframe, in order to improve the co-ordination for supervision of financial conglomerates?
- Do participants have any comments on the papers prepared by the Joint Forum, especially on the principles suggested in the papers? How should the papers or the principles be amended, if necessary?
- How applicable are the principles listed in the Joint Forum papers to financial conglomerates that only operate domestically?

¹ The documents are available at the website of the Bank for International Settlements (BIS) <www.bis.org/publ/index.htm>.

Workshop C: Exchange of Information among Supervisors

13. Traditionally insurance supervisors have relied on effective “solo” supervision of individual insurance companies, whereby the supervisor seeks to ring fence the activities of the company operating in their jurisdiction. However, supervisors are faced with a rapidly changing environment in which globalisation and the formation of complex groups and conglomerates are two significant trends. Whilst effective solo supervision in each jurisdiction will remain essential, there is an increasing requirement for supervisors to be able to take a broader view of the activities of the insurance groups and conglomerates of which their companies form a part. This points to the need to develop a freer flow of information between insurance supervisors.

14. The IAIS has sought to encourage the exchange of information between its members in several ways. At its second General Meeting in St Louis in 1995 a number of members agreed to declare their willingness to exchange information. The Exchange of Information Sub-Committee has conducted surveys on the barriers to the exchange of information which exist between insurance supervisors, and was responsible for the development of the IAIS model Memorandum of Understanding (MOU) on mutual assistance and the exchange of information. The Insurance Concordat² addresses the information needs of home and host supervisors where a parent insurer has material participations in insurers established in other jurisdictions.

15. Looking beyond the IAIS, the Joint Forum on Financial Conglomerates has also produced the principles of supervisory information sharing, as mentioned above. The G7 has also considered the issue and developed 10 Key Principles for exchange of information³. But despite all this attention, the evidence would seem to suggest that the level of information exchange amongst insurance supervisors remains relatively low, notably in comparison to the banking and securities sectors.

Key items for discussion:

- Which are the main areas in which an increased flow of supervisory information between the insurance authorities in different jurisdictions is considered desirable (licensing, branch operations, etc.)?
- In the experience of participants, are information needs already being sufficiently met through the informal exchange of information between supervisory authorities?
- What are the main obstructions to increasing the exchange of information on a formal basis (lack of legal gateways; confidentiality constraints; insufficient knowledge of supervisory counterparts in other jurisdictions, etc.)?
- Do the G7's 10 Key Principles address the main problems of information exchange? Are they too ambitious in their scope?
- How do participants view the necessity and desirability of exchanging information with:
 - non-insurance financial services regulators in other jurisdictions;

² The formal title of the Concordat is “Principles applicable to the supervision of international insurers and insurance groups and their cross-border establishments”.

³ This document is also available at the BIS website <www.bis.org/publ/index.htm>.

- criminal investigation authorities.
- What more should the IAIS be doing to address the problem of information exchange? Options might include a simplified IAIS multilateral MOU to which members could “accede” thereby precluding the need to sign numerous bilateral MOU, or the formal adoption by the IAIS of the G7’s 10 Key Principles (which might assist supervisors in lobbying for any necessary changes in their laws).

Workshop D: Regulatory Issues on Financial Sector Convergence

16. Recently one can observe the increasing interrelationship among different financial sectors, or the “convergence” of various segments of the financial industry. In addition to the growing presence of financial conglomerates, the cross-sectoral activities, especially between insurance and the other financial sectors, are evolving.

17. One of the typical examples of the cross-sectoral activities of financial institutions is the penetration of banks in life insurance market, which is often called "bank-assurance." The policy considerations in this respect seem to centre on issues related to underwriting segregation and regulation of cross-sectoral investments and distribution (including related commercial practices as tie-in sales) as well as emergence of new products. As long as it is kept within proper prudential bounds, convergence can be expected to bring many advantages. This is why governments have been changing their policies in order to allow convergence to proceed smoothly by making regulations more flexible and to ensure that different supervisory authorities can exercise proper control. Closer intersectoral and international co-operation among the supervisory authorities of the sectors concerned would help achieve these goals. A policy change of this kind certainly does not mean a general dismantling of controls but rather the establishment of a more flexible, more integrated but less watchful regulatory setting.

18. Another example of the evolving cross-sectoral activities of financial institutions is the participation of insurance companies in private pension business. The insurance companies do not only function through the provision of individual or collective pension products but also act as managers of pension funds assets. The supervision of this kind of activities can be rather complicated, because in some jurisdictions private pension schemes are regulated by different authorities than the insurance authority. In such a situation, the insurance authority may have to appropriately assess the impacts of the pension fund business on the overall management of insurance companies, paying attention to the level playing field considerations. This should lead to issues related to comparative regulation of solvency and investment of insurance companies and private pension funds,⁴ which could be enlarged to the arguments on functional versus institutional approach for financial sector regulation.

Key items for discussion:

- What are the main regulatory and supervisory issues related to the development of bank-assurance in terms of underwriting, investments and distribution? What are the regulatory and/or supervisory issues other than consumer protection, to which the insurance authorities should pay attention?
- What are the merits and demerits for allowing banks to distribute insurance products? What measures can be taken to alleviate these demerits? How should the distribution of insurance products by banks be regulated and supervised?

⁴ As regards regulation of private pension schemes, see OECD working paper AWP 2.2 Eng. "Private pensions systems: regulatory policies" available on the OECD website<www.oecd.org/subject/ageing/>.

- What are the issues related to growing activities of insurance companies in production/distribution of financial products?
- What are the regulatory and/or supervisory issues for the insurance authorities as regards insurance companies' activities in private pension business? How should the authorities supervise these activities to ensure the sound management of insurance companies without distorting fair competition in private pensions markets?
- What are the differences between solvency and investment regulation of insurance companies and pension funds? How should private pension funds be regulated?

Session IV: Crisis Management: Supervision of Insurance Companies in Difficulties

19. Even under strict supervision, insurance companies may come into distress for various reasons. Insurance supervisors need to detect premonitory symptoms of troubles in insurance companies at the earliest possible stage and prevent them through adequate intervention in their management before the situation becomes serious. For this purpose, the supervisors should be entitled to take necessary measures at a preclusive stage of problems, for example, even when problems appear only on the profit and loss accounting.

20. When an insurance company gets into serious trouble in spite of all corrective efforts, the supervisor needs to focus directly on how best to protect the interests of policyholders. The supervisors should not be hesitant to initiate decisive measures against the company, including liquidation procedure, when they believe such measures are the most effective in protecting the rights of policyholders, as deferment of the decision generally deteriorates the situation and expands their losses. In this regard, the supervisors should have clear rules or standards for establishing insolvency and for selecting appropriate measures. It should also be noted that in many jurisdictions policyholders protection funds have been established to provide a safeguard for policyholders in the case of default of insurance companies.

21. In a period of total financial crisis, an insurance supervisor may face an embarrassing situation in which a number of insurance companies under its supervision run into serious troubles or even become insolvent concurrently. In such a case, the supervisor should assess the impact of possible measures for these troubled companies carefully, as measures might trigger the significant loss of public confidence in the insurance industry and lead to the collapse of the market.

Key items for discussion:

- How can insurance supervisors detect the problems in insurance companies at an early stage? How can they assess the seriousness of the situations? Which criteria can be used for this purpose?
- What kinds of preventive measures should the supervisors be able to take especially at an earlier stage of problems? How can the supervisors intervene preventively at the right time? How much flexibility should the supervisors have in executing and choosing these measures?
- In what situation should an insurance company be regarded as insolvent? How should reinsurance be taken into account in the assessment? In the experience of participants, when should the supervisor decide to initiate the winding-up procedure of a troubled insurance company?
- How can the interests of policyholders be best safeguarded during winding-up procedures? How can the moral hazard problem arising from policyholders protection funds be avoided?

- In a time of financial crisis, should insurance supervisors pay great attention to the protection of the integrity of the domestic insurance market and thus act against troubled insurance companies differently from they would in a normal period?

Concluding Session

22. In the final concluding session, the moderators of the four workshops will be asked to prepare a summary of their respective workshops, to be presented within 10 minutes each.

23. The following concluding discussion will include the final comments by participants on the issues discussed in the preceding sessions and workshops as well as future works in regard to co-operation among insurance authorities and relevant international organisations.

Tokyo Executive Seminar on Insurance Regulation and Supervision

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