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General Insurance Communications Committee

Current Issues Newsletter - January 2009

The content of this newsletter is a summary of some of the current issues that might be of interest to UK General Insurance actuaries and that have come to the attention of the Communications Committee. As such it is not a complete list. Anyone who feels that relevant issues have been omitted or that the summaries are in anyway misleading is invited to contact the Chairperson of the Committee, Kate Angell.

The information provided has been derived from a variety of sources. The Committee has not been able to check independently the veracity of all of the facts stated. Any opinions expressed are those of the Committee members, and do not necessarily reflect the position of the Institute or Faculty of Actuaries.

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1. Market News

AIG - to the rescue

As someone said, “AIG was not too big to fail, but too connected”. And so AIG was rescued by a September 2008 government package, which at $85 billion was larger than the GDP of most developing countries.

The package was later revised in November to $40 billion of preference shares, a credit facility of $60 billion and additional government capital backing if necessary. The revised bail-out package totalled $150 billion, bigger than the 2007 GDP of Kuwait and only marginally less than that of the UAE. This package came at a price, not only in terms of high interest rates, but also in terms of government intervention and control.

Market analysts have stated that AIG could not be allowed to fail, as the repercussions would have been unfathomable. Not only is AIG a household name in general insurance, life insurance and retirement services, with individuals and companies worldwide relying on the insurance cover they provide, but bankruptcy would quite probably have voided the debt insurance that AIG provided through its Financial Products arm, triggering emergency capital raisings from counterparties around the world.

It was marked-to-market losses in this Financial Products arm, non-core to the insurance business, that broke the back of AIG. Banks that entered credit default swaps with AIG could assure auditors and regulators that the risk of the underlying asset failing was collaterilised, and with a triple A rated counterparty. As noted by a recent AIG 10-Q filing, AIG’s Financial Products division had been built “to provide regulatory capital relief rather than risk mitigation”, with the transactions it entered allowing banks to free up more capital in order to pursue other ventures. It has become clear that neither AIG, its banking clients or even the regulators have fully (or even partially) understood the complex nature of these instruments along with the level of systematic risk it has brought to the financial system.

Following the rescue, AIG has recently announced planned disposals worth around $15 billion in order to repay part of its $60 billion emergency loan. These included the sale of its US personal lines business (valued at around $5 billion to $6 billion) and also the disposal of American Life Insurance Company (valued at more than $10 billion), with some high profile interested parties mentioned. Although no formal bid has been announced, AIG’s hope of restoring market confidence and surviving as an independent company hinges upon the rapid repayment of government emergency funding.

Only time will tell how the face of the insurance industry will change post the AIG debacle. Some argue that it is business as usual at its UK operation, with property and casualty renewals as expected and the market not seeing the rapid rate increases expected. Others sources noted that there has been an observable change in the D&O line of business, where directors have become more assertive when deciding who to purchase insurance from.

Tax advantages for offshore insurers

A major concern for US domiciled insurance companies is the unfair advantage offered by the preferential tax rates enjoyed by insurers domiciled in tax havens such as Bermuda. These companies would avoid paying the higher rate of US corporate tax by reinsuring policies written in the US companies to their Bermuda-based subsidiaries.

During his election campaign, Obama frequently mentioned closing corporate tax loopholes and ensuring that companies pay their fair share. This was highlighted by a television campaign that said: “John McCain went to Bermuda and, while he was there, pledged to protect tax breaks for American corporations that hide their profits offshore”.

A bill that seeks to end the perceived advantage of offshore reinsurers over American companies has already been brought before the house of representatives in September. Under the proposed new legislation, companies not subject to US tax would be forbidden from charging premiums less than the industry average paid to insurance companies subject to US tax. The bill is backed by a coalition of US-based insurers including WR Berkeley, Chubb and the Travelers Companies, and with the Federal deficit increasing substantially in light of the current economic environment, this might prove to be on the cards with the increased Democratic majority in both houses of Congress.

Aon fined by FSA

Aon has been fined £5.25 million by the FSA for failing to take reasonable care to establish and maintain effective systems and controls to counter the risks of bribery and corruption associated with making payments to overseas firms and individuals. Between 14 January 2005 and 30 September 2007, Aon failed to properly assess the risks involved in its dealings with overseas firms and individuals who helped it win business and failed to implement effective controls to mitigate those risks.

As a result of Aon's weak control environment, the firm made various suspicious payments, amounting to approximately US$7 million, to a number of overseas firms and individuals, the FSA said.

Margaret Cole, director of enforcement at the regulator, said: “This is the largest financial crime related fine imposed by the FSA to date. It sends a clear message to the UK financial services industry that it is completely unacceptable for firms to conduct business overseas without having in place appropriate anti-bribery and corruption systems and controls”.

Aon cooperated fully with the FSA and agreed to settle at an early stage of the FSA's investigation. As a result, the firm qualified for a 30% discount under the FSA's settlement discount scheme. Without the discount the fine would have been £7.5 million.

A&L & Egg fined in relation to Payment Protection Insurance sales failings

Alliance & Leicester were fined £7 million by the FSA as a result of a review of their Payment Protection Insurance sales practices. According to the FSA "... there was a general failure by advisers to give customers details of the cost of PPI. In addition A&L sought to find reasons to sell PPI without properly considering what customers needed. A&L did not make it sufficiently clear that PPI was optional and it trained its staff to put pressure on customers where they queried the inclusion of PPI in their quotation or challenged advisers' recommendations."

Egg was also fined by the FSA in relation to its PPI practices. The fine, of £721,000, was levied by the FSA after they found failings in approximately 40% of telephone sales of credit card PPI made by Egg between January 2005 and December 2007. Egg sold PPI either when receiving a customer services call, or when making a sales call to a new customer. When Egg customers said they did not want PPI on their credit cards, the firm directed its sales staff to use techniques to persuade the customer to take the insurance - called 'objection handling'.

Terrorism in India

The recent terror events in the Indian city of Mumbai could have a wider impact on insurers than just increased terrorism claims. Claims from the terrorist attacks could cost the insurance industry around $600 million, with the Taj Mahal hotel expected to be a total loss.

The losses will leave insurers with a nasty tab, but should also increase demand for terrorism coverage, leading to an increase in revenues. Rock bottom Indian terrorism premium rates should also harden substantially as underwriters update their pricing models after being reminded of the real threat that exists in this area.

In addition, the heightened political tension between India and Pakistan should see many revisions to current underwriting terms on the cover provided. Another interesting twist is the impact of the Afghan war on relations between the US and India. America has been working with Pakistan and is unlikely to put pressure on them in resolving the Indian situation.

Pirates off Somalia

During 2008, there were 92 attacks off the Gulf of Aden and East coast of Somalia, including 36 successful hijacks. In response to these concerns, a number of new Kidnap & Ransom (K&R) policies have been launched by various market players. As an example, both Aon and Transmarine have launched policies to protect charterers' cash-flows on a standalone basis or as an extension to a current policy. The cover indemnifies against charterers' liability to continue paying rent to ship owners where a charterer is deprived of the use of a vessel as a result of piracy. A large uptake is expected as these clauses are not included in standard K&R policy wordings.

Other players have also issued dedicated Marine K&R policy wordings, designed in light of the recent piracy of the supertanker Sirius Star, offering to indemnify against kidnapping and extortion, lost ransom and costs incurred in resolving the situation. These include cover to cargo owners for loss of revenue or earnings due to delays or destruction of cargo in event of piracy. One example is a loss of hire extension to an existing policy with no deductible and pays from day one. Another example is where the standard limit of cover has been increased from $10 million, in response to pirates' demand of $25 million for the release of ransomed vessels.

2. Claims & Legal Issues

KNIC court case

North Korea's state-owned insurance company has won a long-running legal battle against a group of London market re-insurers that had refused to pay out a claim relating to a helicopter crash in Pyongyang. The group of reinsurers (including Allianz, Generali and three Lloyd's syndicates) agreed to pay €40 million, which is 95% of the reinsurance claim. The reinsurers also agreed to retract and withdraw all allegations of fraud and impropriety made against Korea National Insurance Company.

The claim arose from an accident in July 2005 when a helicopter crashed into a Pyongyang warehouse, which contained emergency relief goods such as food, clothing and medical supplies. KNIC obtained a judgment in the Pyongyang Court, the agreed jurisdiction of the reinsurance policy, for €44 million, and commenced litigation in the UK High Court in January 2007 to enforce it. The re-insurers however had contested that the underlying insurance claim was fraudulent and that the domestic legal judgment was also fraudulently obtained.

Increases in litigation

Lloyd's of London has published a report stating that investors are expected to increasingly provide financing for claims in both the United States and Europe as a chance to profit from a surge in corporate lawsuits. Third party funding of suits has emerged in the United Kingdom relatively recently, although has been available in other countries for some time.

Businesses are expected to spend more time defending claims as shareholders, disgruntled by large financial losses, target firms and their senior executives with class action lawsuits. The current economic conditions may actually accelerate this trend, as investors become keen to find new opportunities for investing capital not correlated with volatile financial market performance. Businesses will also need to be aware of the ability of claimants to pursue claims in jurisdictions that have a track record for ruling in favour of plaintiffs and awarding higher awards than courts in other regions.

Whiplash claims in the UK

The ABI (Association of British Insurers) reported that badly-fitted head restraints in cars and increased tailgating are making the UK the whiplash capital of Europe.

Claims for motor-accident whiplash injuries have risen by a quarter in the last five years and are now costing nearly £2 billion a year in compensation. Every day nearly 1,200 people claim for whiplash injuries. Apparently, 75% of motor personal injury claims are for whiplash, compared to an average of 40% throughout the rest of Europe.

Motor premiums on the rise

The latest figures from the AA's benchmark British Insurance Premium Index show that the cost of car insurance premiums rose by 8.7% over the past year, to an average of £741.66. Increasing legal costs and personal injury claims continue to be the biggest cause of concern amongst UK motor insurers, with personal injury claims and their associated legal expenses rising by around 22% last year to about £6.16 billion. Indeed, whiplash injury alone represents around £66 for every car insurance policy sold.

Average quoted premiums are expected to rise by around 10% to 12% over the next year.

Household premiums on the move too

According to the AA, building insurance premiums have also risen recently. However the average quoted premium for an annual buildings insurance policy of £213 is only about £13 higher than since the 2007 UK Floods, considerably less than some commentators had predicted.

In contrast, the average quoted premiums for both contents and combined buildings and contents insurance has fallen recently. Contents premiums dropped by nearly £5 over the past quarter while £6 was wiped from the average quoted premium for combined buildings and contents policies.

Pleural plaques

Ministers have called on the Government to publish the findings of its consultation into pleural plaques compensation. In October 2007 the Law Lords ruled that pleural plaques victims could no longer claim compensation. Following a long running campaign by unions, MPs and asbestos campaigners, the Government agreed to consult on whether the Law Lords' ruling should be overturned and whether compensation should be paid to pleural plaques victims. The consultation closed on 1st October 2008.

Medicare

The Centers for Medicare & Medicaid Services, a federal agency within the United States Department of Health and Human Services, is hoping a new measure will deter fraudsters hiding behind phony medical equipment companies. Officials announced this week that some companies across the country must now post $50,000 surety bonds if they want to continue as Medicare[1] providers.

Medicare paid about $1 billion in fraudulent claims for medical equipment alone in 2007, with more than half of the 500 Medicare fraud cases nationally in 2008 involved medical equipment providers, according to the Department of Justice.

[1] *Medicare is a social insurance program administered by the United States government, which provides health insurance coverage to people who are aged 65 and over, or who meet other special criteria.*

3. Solvency II

Group support regime at risk

As the Solvency II implementation process moved towards a critical phase which would have seen a final vote on the draft Solvency II Framework Directive in the European Parliament in December 2008, divisions have emerged at a political level within the institutions of the European Union ("EU").

In early December the Economic and Financial Affairs Council ("ECOFIN"), made up of the economic and finance ministers of the EU's member states, adopted a French proposal to delete the group support regime from the draft Solvency II Framework Directive. Several member states, including Spain and Poland, had been concerned about dilution of national regulatory powers under Solvency II and strongly supported the French position.

ECOFIN's position puts it at loggerheads with other institutions of the EU, such as the European Commission and European Parliament, both of which are in favour of the group support regime. The European Parliament had itself approved the draft Framework Directive at committee level in October 2008. The group regime also has strong support from within the industry from bodies such as the Committée Européene des Assurances ("CEA"), the CRO Forum and the Pan-European Insurance Forum which had jointly addressed a letter to the French Presidency of the EU on the matter in November 2008.

The group support regime, in addition to enhancing regulatory co-operation between national supervisors, also enshrines the principle of assessment of capital adequacy requirements on a cross-group basis. Deletion of the group support regime could affect the competitive position of insurers with subsidiaries in different EU member states by reducing the amount of cross-group diversification benefit that can be recognised in the capital assessment process. This loss of diversification benefit in turn potentially affects consumers as insurers will not be able to pass on the diversification benefit through the pricing of policies.

The ABI issued a statement expressing their disappointment at these latest developments, stating "While Finance Ministers are, quite rightly, dealing with the current economic crisis as an international problem needing global solutions, they are proposing a European regulation that ignores the cross-border nature of how companies operate . . . The lack of this kind of international perspective in banking lies behind the current crisis. Solvency II is an opportunity to put this in place for the insurance industry."

The political divisions also put at risk the October 2012 target implementation date for Solvency II. The Solvency II Framework Directive is unlikely to be finalised until April 2009 and subsequent Implementation Measures cannot take place until the Directive is approved by the relevant bodies of the EU. Some commentators believe that the political difficulties make it likely that Solvency II will be delayed until 2013.

CEIOPS publishes QIS4 results

In November 2008, the Committee of European Insurance and Occupational Pensions Supervisors ("CEIOPS") issued its report on the fourth Quantitative Impact Study ("QIS4"), which the industry had participated in between April and July 2008. The report can be found at http://www.ceiops.eu/media/files/consultations/QIS/CEIOPS-SEC-82-08%20QIS4%20Report.pdf.

Some high-level messages from the CEIOPS report are as follows:

- CEIOPS pointed to an "impressive" participation rate with overall participation up 40% relative to QIS3 and a total of 1,412 companies participating.
- A total of 129 UK firms participated, of which 59 were non-life insurers.
- Approximately 11% of participants would not meet the Solvency Capital Requirement ("SCR") under QIS4, compared to 16% under QIS3. In the non-life sector 11.2% would fail to meet the SCR.
- Overall the European insurance industry is confirmed as being adequately capitalised. The median SCR coverage ratio for non-life firms under QIS4 was 193%.
- General support was expressed for the cost-of-capital approach to non-life reserve risk while a number of firms questioned the 6% cost-of-capital factor.
- Feedback on internal models suggests there may be incentive for some firms to use these, with approximately half of participants potentially expecting capital requirement reductions of up to 20% relative to the standard formula approach.

. . . as does the FSA

In addition to the CEIOPS report described above, a UK country report on the results of the QIS4 exercise for participating firms was published by the FSA in December 2008. This report is available on the FSA's website at http://www.fsa.gov.uk/pubs/international/QIS4_report.pdf.

For QIS4 the participation level within the industry increased relative to QIS3, with 63 UK authorised non-life firms (representing around 88% of the market by volume) undertaking the QIS4 exercise. Of this cohort, approximately 90% of UK non-life firms hold sufficient capital to meet the QIS4 capital requirement standard (compared to 80% in QIS3).

FSA DP - Insurance Risk Management: The Path to Solvency II

At the end of September, the FSA published a Discussion Paper "Insurance Risk Management: The Path to Solvency II" which is viewed in the industry as a key paper for practitioners in the UK capital modelling and management arena. The full paper can be found at http://www.fsa.gov.uk/pubs/discussion/dp08_04.pdf.

The key messages presented within the paper include the following:

- The Solvency II regime is expected to come into force in October 2012 and goes further than the existing ICAS regime in that it will require further development of risk and capital management systems as well as additional disclosure requirements.
- The FSA will write to all firms by March 2009 instructing them to appoint a senior individual within the company responsible for the implementation of Solvency II.
- The FSA recommends that all firms undertake a QIS4 analysis if they have not already done so.
- The FSA recommends that firms undertake a gap analysis to identify areas where there are expected shortfalls in complying with Solvency II requirements.
- Firms planning to use an internal model for calculating capital requirements under Solvency II should inform the FSA of such plans by June 2009. The Discussion Paper also provides an informative chapter on the use and approval of internal models as well as an annex on engaging with the regulator in the internal modelling process.

4. Government & Regulatory Issues

Consultation paper on stress & scenario testing

The FSA has issued a consultation paper on stress and scenario testing, in which it is proposing to introduce a "reverse stress test" requirement. This 'reverse-stress test' requirement, which would apply to banks, building societies, CRD investment firms and insurers, would require firms to consider the scenarios most likely to cause their current business model to become unviable.

The FSA's aim is to ensure that firms more fully explore 'tail risks' which, if they were to crystallise, would cause counterparties and investors to lose confidence in them, so that a firm is more aware of its business model vulnerabilities when making strategic business decisions, when contingency planning and when considering its risk management arrangements. The consultation paper (which is available at http://www.fsa.gov.uk/pages/Library/Policy/CP/2008/08_24.shtml) was published in December 2008 and the period for consultation responses closes on 31 March 2009.

FSA concludes its review of insurance comparison websites

A further FSA review of insurance comparison websites has found that many sites have made significant improvements and are consistently providing clear, fair and not misleading information, but some firms need to go further to address a few specific concerns. The FSA visited a sample of the firms responsible for the 17 websites that were assessed during the initial review (in May 2008) and found that many of them had made improvements to their websites and processes. However, the FSA has identified two specific areas where some firms need to make further improvements:

- obtaining better information from insurers about the level of excesses that apply to insurance policies; and
- making more clear the assumptions about consumers' needs and circumstances that some websites use to obtain quotes.

In addition, the FSA carried out a review of aggregator firms' advertising and found the vast majority of firms have clear, fair and not misleading adverts. In a small number of cases, the FSA found a lack of clarity in some of the terms used, and adverts which could give consumers a misleading expectation of the firm's market coverage and the amount they could save on insurance premiums.

Further details of the review can be found at http://www.fsa.gov.uk/pages/Doing/Regulated/Promo/thematic/gi_comparison.shtml.

FSA consults on changes to the rules for approved persons

The Financial Services Authority ("FSA") has published a consultation paper (CP08/25) that clarifies the FSA's expectations of those people within firms that perform a 'significant influence' function. The Consultation Paper ("CP") proposes amendments to the FSA handbook to extend the approved persons regime and sets out how the FSA is enhancing its scrutiny of senior management competence. The CP proposes to:

- extend the definition of the existing CF1 (director) and CF2 (non-executive director) controlled functions to include certain individuals in parent companies to which an authorised firm is accountable;
- clarify the role of non-executive directors to make clear that the FSA will, in future, look at non-executives more closely where it believes they should have intervened more actively with a firm's management;
- extend the definition of CF29 (significant management function) to include all proprietary traders where they can exert a significant influence over a firm;
- amend the application of the approved persons regime to UK branches of overseas firms based outside the EEA; and
- extend the rule obliging firms to provide references for applicants of the CF30 (customer function) to all controlled functions if requested to do so.

5. International

Europe

France – Government to offer credit insurance aid to companies

The French state is to help cover the credit insurance needs of viable companies so that they are not left in the cold by credit insurers worried about rising defaults as the country heads into recession. Plans were announced for insurer Caisse Centrale de Reassurance, which is publicly owned, to provide businesses with cover when private insurance is withdrawn.

French officials said the move, which was due to take effect in December and have an initial shelf life of six months, was the first of its kind in Europe since the onset of the financial crisis. The measure will ensure that companies wishing to subscribe to credit insurance and supply goods to other firms on deferred payment terms can continue to be protected against potential defaults by their clients. The French government was not earmarking any specific level of funding to help cover the credit insurance needs of companies given that the amounts would depend on requests made by credit insurers and the market situation.

Poland – Industry to opens doors to reinsurance firms

The government's draft amendment to the Insurance Act opens the door to establishing reinsurance firms in Poland. According to the draft amendment, reinsurance firms will be able to function as joint stock companies, mutual reinsurance companies and European companies.

The document also introduces new rules concerning financial management of reinsurance firms and investing assets used for creating technical and insurance reserves. It will be considered by the Sejm, the Polish parliament, during the next parliamentary session.

Ukraine – Insurance Federation initiating introduction of compulsory insurance of mortgaged property

The Ukrainian Insurance Federation has moved forward with an initiative to introduce compulsory insurance of mortgaged property and life of borrowers for the whole period of credit agreements. The anti-crisis program for the insurance market has been submitted for the consideration of the State Commission for Regulating Markets of Financial Services.

Americas

New York – Regulator push for change on contract certainty

The New York State Insurance Department is calling for insurers and producers doing business in the state to develop and implement practices in one year to assure that documentation is delivered to policyholders within 30 days of inception in most circumstances.

The prolonged coverage dispute that arose from the September 11th attacks played a key role in crafting of the new policy, New York Insurance Superintendent Eric Dinallo said in an interview shortly after the department announced the policy. Mr Dinallo brokered 2007's $2 billion settlement of the WTC coverage dispute. The WTC dispute "was based on a lack of contract certainty," Mr Dinallo said. "They had slips and binders in place, but no policies. That's what the litigation was about."

The regulator is seeking to provide "contract certainty", which means that the complete and final agreement to all terms of a policy exists by the time the policy takes effect, and the issuance and delivery of the policy occurs "before, at or promptly after" the inception date. The circular noted that contract certainty is not an issue with most policies because they are written on standardized forms that have received regulatory approval, but under certain circumstances, including manuscripted large commercial accounts, the excess lines market and reinsurance, "the unique nature or size of the risk" gives rise to issues regarding contract certainty.

In its announcement of the circular letter, the department noted its "action is similar to that taken by the United Kingdom Financial Services Authority in 2004". The FSA called on "the London market to provide greater contract certainty at the inception of a contract, with full documentation delivery promptly thereafter", adding that "significant progress toward contract certainty in that market resulted from the FSA's action."

NAIC adopts proposal to update reinsurance regulation

The National Association of Insurance Commissioners ("NAIC") announced on 7th December that it had adopted its Reinsurance Regulatory Modernization Framework Proposal.

The proposal creates two new classes of reinsurers in the United States: US-domiciled national reinsurers and non-US-based port of entry ("POE") reinsurers, and introduces modified collateral requirements for eligible reinsurers. The proposal also establishes a new framework for state-based reinsurance regulation based on the concepts of supervisory recognition, single-state licensure for US reinsurers and single-state certification for non-US reinsurers from approved jurisdictions.

Under the proposal, alien reinsurance companies would no longer need to deposit 100% of their US liabilities in a trust fund as required collateral. Under the new proposal, Lloyd's reinsurers would have to post just 20%.

The proposal also creates the NAIC Reinsurance Supervision Review Department ("RSRD"), which will evaluate the reinsurance supervisory regimes of other countries and establish standards for a state to be certified to regulate reinsurance on a cross-border basis. In order to be certified as a POE reinsurer, a reinsurer must be licensed by a non-U.S. jurisdiction recommended as eligible for recognition by the RSRD.

"This proposal sets forth a conceptual framework only", said New Jersey banking and insurance commissioner Steven Goldman, chairman of the NAIC Reinsurance Task Force, which drafted the proposal. "Now, we must focus on developing the specifics of this new regulatory regime and taking the appropriate legislative steps to make the proposal a reality."

The proposal still has to pass through congress. Proponents of the proposal will be all eyes to gauge the new administration's approach to insurance regulation. It can be expected that they will pay close attention to the current financial regulatory system, although their attention will at first be more focussed on that of the banking system.

US – Personal lines insurance

One major area of concern is the provision of state funded insurance coverage to lower income households in hurricane prone areas, such as New Orleans. The Bush regime was heavily criticised for the lack of support provided to households in this area following the vast damage caused by Hurricane Katrina. Critics said that the government did not deliver on improvements to hurricane and flood defences in the area compared to that of other comparable hurricane prone areas.

Canada – PACICC calls for insolvency clauses in arrangements between insurers and reinsurers

Only reinsurance arrangements that include an appropriate insolvency clause should be recognized by Canada's solvency regulator as an allowable asset, Canada's insurance guarantee fund has recommended in a report. The Property and Casualty Insurance Compensation Corporation ("PACICC"), which reimburses Canadian policyholders in the event of an insurer bankruptcy, made this and several other recommendations in its recent report "(Re)assurance of Solvency: reinsurance assets in insurance company liquidations".

The PACICC report looks at, among other things, the thorny issue of whether insolvent insurers should be able to recover from reinsurers (and therefore count those 'recoverables' against their assets in the event of an insurer bankruptcy). Traditionally, insurers have to pay a 'loss' first in order to recover funds for that loss from reinsurers. But in the case of an insolvency, insolvent insurers "allow" claims against the assets of the estate for future distribution to policyholders and creditors in the order of priority established under US law. Noting this, reinsurers have made the case that since insolvent insurers do not technically pay the claims, reinsurers should not have to pay if the insolvent insurer can't pay its claims obligations.

The US courts have sided with reinsurers, causing US regulators to require an "insolvency clause”. An insolvency clause, as PACICC notes, "clarifies that if the reinsured stops making payments for losses because of insolvency, the reinsurer must continue to make payments to the reinsured or to its liquidator as if the insolvency had not occurred”. In Canada, while the Reinsurance Research Council of Canada (“RRC”) developed wording for an insolvency clause in 1991, it is not currently a requirement before reinsurance recoverables can be recognized as an asset for regulator capital purposes, according to PACICC. PACICC wants the insolvency clause to be required before the federal solvency regulator recognizes reinsurance recoverables as an asset of the insolvent company.

Asia

India – Insurance reform bill

The insurance reforms bill was introduced in the Rajya Sabha, the upper house of the Parliament of India, to increase the cap on foreign investment in private companies in the sector from 36% to 49%, to allow overseas reinsurers to enter the market through branches and to allow state-owned general insurance companies to raise funds from capital markets.

If the bill becomes an Act, the four state-owned general insurance companies (Oriental Insurance Company, New India Assurance, United India Insurance and National Insurance Company) will be able to access the capital markets to raise funds after obtaining permission from the government.

China – Insurers need capital injections

The China Insurance Regulatory Commission (“CIRC”) has given approval for 10 insurance companies to raise their operations' registered capital base in China since November 2008.

The biggest capital injection was made by China's second-largest insurer, Ping An Insurance Co Ltd, for both its life and non-life subsidiaries, of 20 billion yuan (€2.1 billion) and 1 billion yuan, respectively.

The capital injections were aimed at maintaining financial strength in the wake of the global financial crisis, according to the CIRC. The regulator said it also imposed tighter controls on insurance companies' financial bases and liability for compensation.

The global financial crisis is gradually having a deeper impact on China and the insurance market's capital flow has been tightened up, said Dingfu Wu, chairman of the CIRC. Insurance companies are having more difficulties raising capital from their shareholders and from other fundraising channels, said Wu in a statement.

China – Tighter rules on property insurers' investments

The China Insurance Regulatory Commission (“CIRC”) has tightened rules on the launch of investment-related products by property insurers, reflecting its concerns about the solvency of some insurers, which have suffered big losses on their investments in the domestic capital markets.

Property insurers that plan to launch products with both insurance and investment functions must have had a solvency ratio of more than 150% in the past four consecutive quarters, the regulator said. The notice said a company whose solvency ratio had fallen below 150% in the latest quarter must immediately stop selling such products and make a report of its situation to the regulator.

Before this notice, the regulator restricted all insurers' business activities when their solvency ratio fell below 100%. For insurers with solvency ratios between 100% and 150%, the regulator monitors their operations and asks them to submit contingency plans to ensure their solvency is sufficient.

Concerns about China's insurers have risen as their investments have been hit by the benchmark Shanghai Composite Index's fall of nearly 70% from an all-time high of 6,124.04 on 16th October 2007.

The regulator also urged property insurers to target 'reasonable' returns for their products, and said any promised return must be no higher than 80% of the bank savings deposit rate of the same term as the product. It said that it will limit or stop approvals and sales of investment products by the companies if there are sharp swings in either the money or stock markets.

South America

Brazil – Additional restrictions on foreign-denominated insurance

Brazil's insurance regulator, Susep, and national insurance council, CNSP, have added rules regulating foreign-denominated insurance, insurance federation CNSeg said in a statement.

The new rules determine the specific lines and risk types that can be insured in foreign currency, generally allowing clients to purchase any policy type not available in Brazil, the statement said. Susep also comes away with the right to review any such policy.

Another aspect limits naturalized citizens of Brazil to using policies with overseas coverage only when they are outside the country. The insurer and purchaser are also subject to any relevant central bank or national monetary council regulation.

Susep can also obligate any insurer with low equity levels to present a plan to increase their solvency, CNSeg said in another statement. Insurers will have a maximum of 45 days to present such a plan, the statement said.

Chile – New rules on foreign insurers to boost capital markets

The finance and economy ministries made an announcement on 13th October to lift a capital gains tax applied on investments by foreign insurers in the country, with a view that it should further strengthen and deepen local capital markets. The measure also includes giving tax breaks to endowments and sovereign wealth funds that invest in Chile.

The announcement was part of a series of measures by both the finance and economy ministries to the tune of US$850 million to keep credit markets flowing and ease access to financing for local exporters and small/medium sized enterprises.

Australia

APRA releases prudential framework for supervision of general insurance groups

The Australian Prudential Regulation Authority ("APRA") published in December 2008 their prudential framework package for the supervision of general insurance groups domiciled in Australia.

The package consists of three new prudential standards, one revised prudential standard and a response paper that addresses submissions received from the general insurance industry in relation to a consultation package released in April 2008. The standards are the result of more than three rounds of consultation with industry, over a three-year period, on general insurance group supervision. The requirements of these standards will apply to all general insurance groups that have either an APRA-authorised general insurer or an APRA-authorised non-operating holding company as the parent entity of the group.

According to APRA Executive Member John Trowbridge "With these new standards, APRA is aiming to ensure that insurance groups are financially sound and that group interrelationships do not compromise the financial soundness of individual APRA-authorised insurers within the group".

APRA's approach to general insurance group supervision is to treat, in principle, the insurance group as one economic entity and apply requirements to the group similar to those applying to individual APRA-authorised general insurers, in relation to:

- capital;
- risk management;
- audit, actuarial reporting and valuation;
- governance; and
- fitness and propriety of responsible persons.

The governance and the fitness and propriety requirements already apply to general insurance groups, and so precede these new standards.

The prudential standards will become effective on 31st March 2009. Among other things, they will enable APRA to implement recommendations 38 and 39 of the HIH Royal Commission in relation to general insurers that operate as part of a corporate group. The new standards will also enable APRA to meet Insurance Core Principle 17 of the International Association of Insurance Supervisors, which requires insurance supervisors to supervise general insurers on a group basis and a solo basis.

The standards and the response paper can be viewed on APRA's website at www.apra.gov.au/Policy/Supervision-GI-Groups-December-2008.cfm.