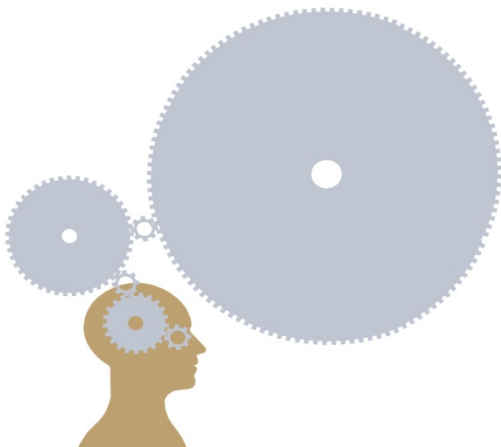


Insurance guarantee schemes: International perspective and EU developments

Jahrestagung—Deutscher Verein für
Versicherungswissenschaft

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March 16th 2011



Overview

- background: evolution of the EU debate on insurance guarantee schemes (IGS)
- status quo in Europe
 - is there a need for EU policy action on IGS?
- the European Commission White Paper and beyond
 - open questions and challenges
 - implications in the German market
- concluding remarks

Evolution of the EU debate



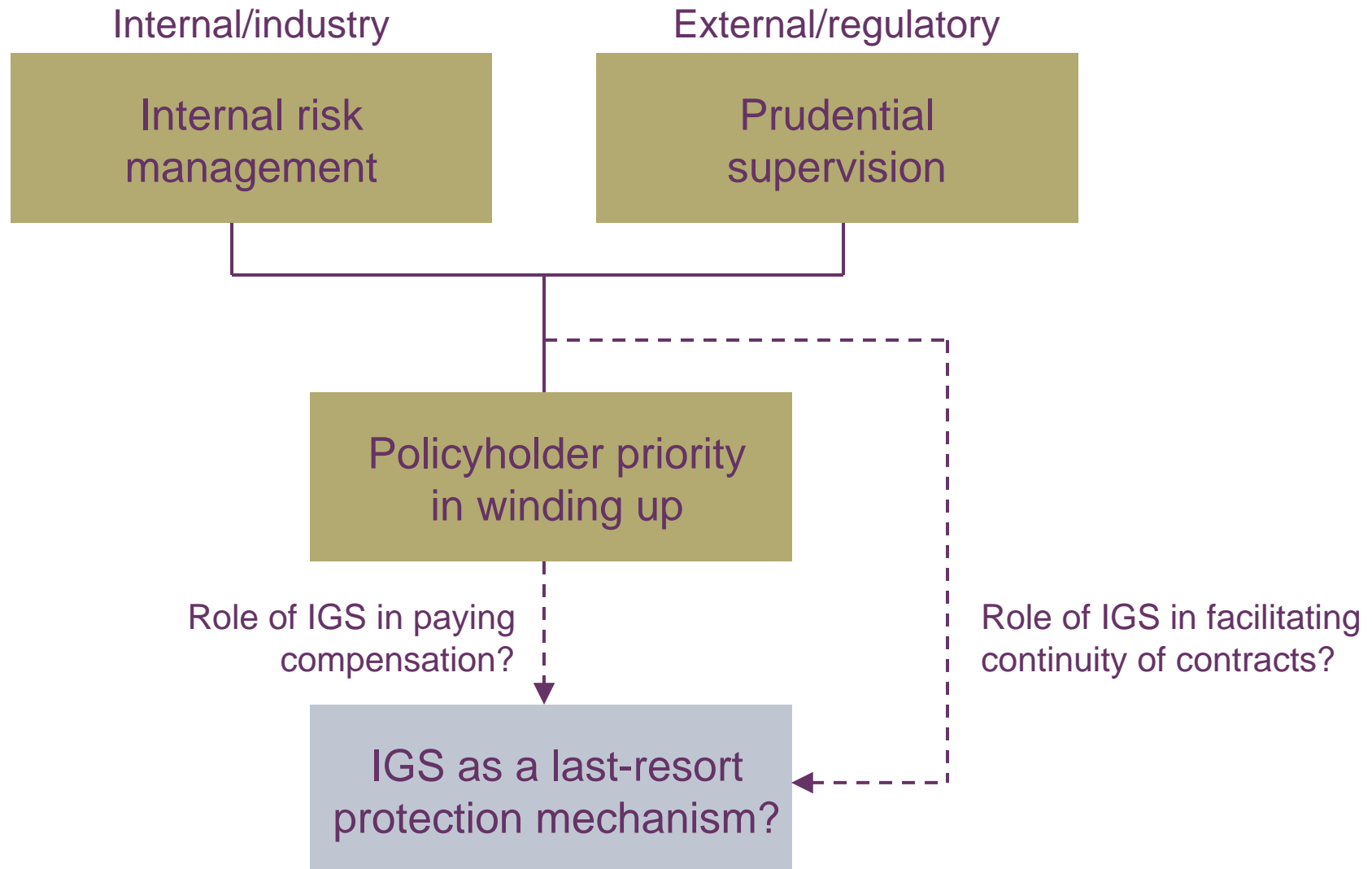
Notes: ¹ European Commission (2010), 'White Paper on Insurance Guarantee Schemes', COM(2010) 370;
²Oxera (2007), 'Insurance guarantee schemes in the EU: comparative analysis of existing schemes, analysis of problems and evaluation of options', final report prepared for European Commission DG Internal Market and Services, November.

Overview of existing IGS

	General scheme for life and non-life	General scheme for life	General scheme for non-life	Specific scheme for non-life
Belgium		✓		✓
Bulgaria	✓			
Denmark			✓	
Finland				✓
France		✓	✓	
Germany		✓		✓
Ireland			✓	
Italy				✓
Latvia	✓			
Malta	✓			
Poland		✓		✓
Romania	✓			
Spain	✓			✓
UK	✓			

Source: Oxera report, updated using European Commission impact assessment.

IGS as a last-resort protection mechanism?



Operation of existing IGS (I)

- IGS have often been established as a result of failure(s) in the relevant national market

Country	Year established	Name of failed insurer (year)	Total cost to date
Denmark (non-life)	2003	Plus Forsikering A/S (2002)	€12.2m
France (life)	1999	Europavie (1997)	€0 (scheme was not required to intervene)
		International Claims Services (1999)	
		Groupement d'Assurances Européennes (2000)	€20.3m
		Independent Insurance (2001)	(total compensation paid with respect to the five failures, excluding motor insurance claims)
		Compagnie Internationale de Caution Pour le Developpement (2001)	
France (non-life)	2003	Caisse Générale d'Assurance (2003)	
Germany (life)	2002	Mannheimer Lebensversicherung	€100m

Source: Oxera report.

Operation of existing IGS (II)

- overall, cases of IGS intervention have been infrequent
 - and some IGS have not dealt with a single case of failure
- UK Financial Services Compensation Scheme (FSCS) has paid out most
 - FSCS provides most comprehensive protection of all EU IGS
 - payment mainly in relation to 25 non-life failures that occurred in or before 2001 (largest case is Independent Insurance)

	Total payment (cost) (€m)	Total number of payments
2002/03	191.9	44,245
2003/04	193.1	94,106
2004/05	170.8	41,104
2005/06	136.5	40,817
2006/07	97.9	16,844
2007/08	54.9	n/a
2008/09	60.9	n/a
2009/10	80.1	n/a

Source: Oxera report for payments until 2006–07. Updates since are from FSCS annual reports and refer to reported compensation costs in relation to insurance failures, converted at £1 = €1.20.

Levies paid by industry

Ex ante-financed IGS

	Annual levy in 2006 (€m)	Calculation of levy	Size of IGS fund in 2006 (€m)
Life assurance			
Latvia	0.2	1% of relevant premiums	0.8
Malta	0.1	0.125% of relevant premiums	0.2
France	n/a	Total fund size is 0.05% of provisions per year, rebalanced annually among participants (half cash, half pledges)	480.0
Germany	123.0	0.02% of life net reserves (until target fund of 0.1% of net reserves reached)	615.0 (target)
Non-life insurance			
Latvia	0.6	1% of relevant premiums	2.8
Malta	0.1	0.125% of relevant premiums	0.2
Spain	94.1	0.3% of non-life premiums	1,099.0
Denmark	7.8	DKK10 (€1.3) per policy	11.6

Source: Oxera report.

Levies paid by industry

Ex post-financed IGS

€m	2002	2003	2004	2005	2006
General IGS					
UK (life)	0	0	0	0	0
UK (non-life)	215.9	0	206.9	15.21	0
Poland (life)	0	0	0	0	0
Ireland (non-life)	0	0	0	0	0
Specific IGS					
Belgium (workers' accident)	0	0	0	0	0
Finland (patient insurance)	0	0	0	0	0
Germany (private health insurance)	—	0	0	0	0

Source: Oxera report.

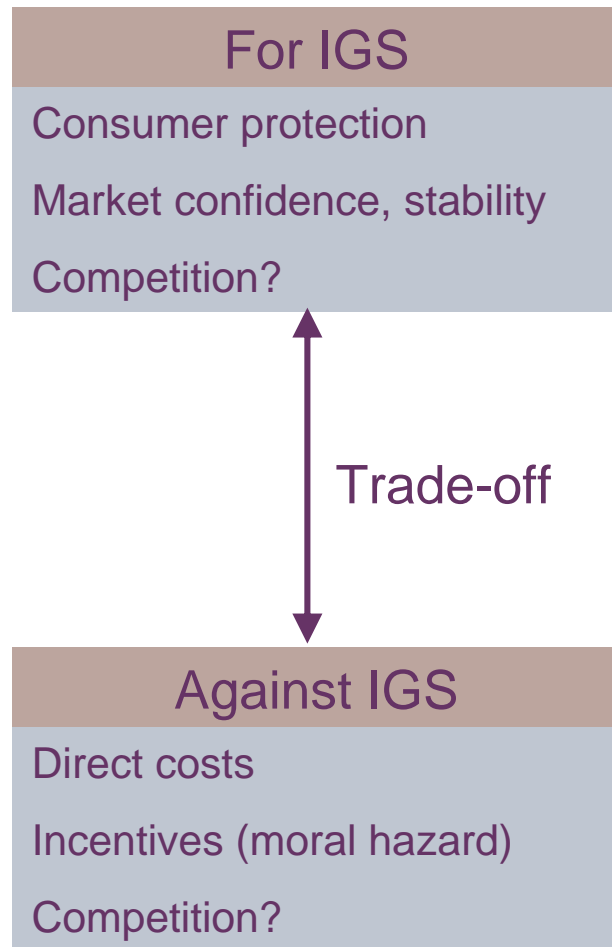
Levies paid by industry

Annual caps on levies: maximum exposure

General IGS	Annual cap on industry levy
Latvia (life and non-life)	1% of relevant premiums
Malta (life and non-life)	—
Spain (life and non-life)	—
UK (life and non-life)	0.8% of relevant premiums
France (life)	0.05% of technical provisions (plus borrowing from industry)
Germany (life)	0.1% of life net reserves for extraordinary contributions
Poland (life)	—
Denmark (non-life)	1% of relevant premiums
France (non-life)	€700m is total intervention limit (around 1.3% of non-life premiums)
Ireland (non-life)	2% of relevant premiums

Source: Oxera report.

The key policy decision: IGS or not



Main considerations in the trade-off

- distributional preferences
- likelihood and impact of failures
- effectiveness of other protection mechanisms, including supervision
 - Solvency II
 - IGS as a last-resort protection
- existence of schemes in banking and investment sector
- how significant are the direct and indirect costs?
 - can be low, or (if no failure) close to zero, based on experience of existing IGS
- can an IGS be structured to contain costs (including negative market impacts)?
 - ⇒ a matter of IGS design

A case for EU policy action?

- status quo implies differences in consumer protection
 - *within* Member States: protection depends on whether policy is purchased from domestic or incoming EU insurer
 - *across* Member States: failure of cross-border insurer may result in different protection depending on country of residence
- status quo implies differences in demand- and supply-side conditions depending on location of headquarters and type of cross-border provision (subsidiary, branch or under freedom of services)
 - but no evidence of significant distortions

⇒ case for EU policy action depends on weight attached to:

- consumer protection within and across Member States
- distortions in the *conditions* for a single EU insurance market (as opposed to evidence of actual distortions)

The European Commission White Paper on IGS

- 'to establish at EU level a coherent and legally binding framework on IGS protection, applicable to all policyholders and beneficiaries, by means of a directive' (p. 8)
- stated policy objectives
 - consumer protection and competition/level playing field
- key design features include:
 - coverage of life and non-life insurance
 - protection of natural persons (and certain legal entities)
 - portfolio transfer and/or compensation of claims
 - home state principle
 - ex ante funding (with risk-weighted levies)

Open policy questions

IGS funding

- is ex ante funding required?
 - insurance is different from banking
 - systemic risk: less or no risk of runs on insurers
 - payout profile: less need for quick access to funds in insurance
- are risk-weighted levies beneficial?
 - incentive effects limited, but often perceived to be 'fairer'
 - risk of duplicating risk-based approach under Solvency II?
- how to deal with large failures?
 - limits of industry-financed IGS

Open policy questions

EU cross-border insurance business

- home state approach chosen mainly for practical reasons and to fit supervisory framework
- it falls short of delivering the two main White Paper objectives
 - consumer protection: no equivalence of IGS protection within a Member State
 - competition: no level playing field for domestic and incoming EU insurers
- what are the implications for cross-border insurance business?

Potential implications for Germany (I)

Little change for life assurance

- Germany has an IGS that is a 'de luxe' version among EU schemes
 - continuity of contracts, pre-funding with risk-weighted contributions, additional funding commitment by industry, etc.
- possible extension of home state arrangements to allow 'top-up' participation by incoming EU insurers?

Potential implications for Germany (II)

key change would be requirement to implement IGS for non-life insurance

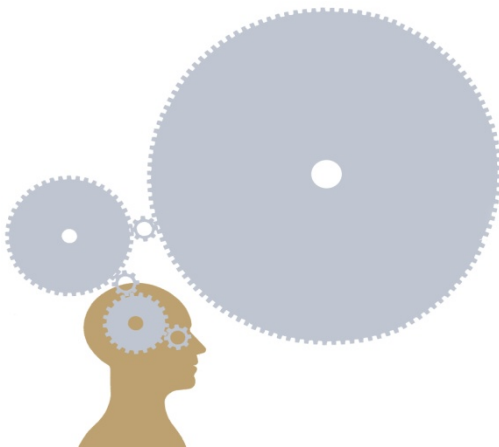
- but if risk and cost of failure low, IGS can in principle be designed to operate at minimal cost for industry
 - eg, experience from the currently post-funded scheme for private substitutive health insurance in Germany
 - unless EU requirement for significant ex ante funding

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