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AN APPROACH TO STRENGTHENING CORPORATE GOVERNANCE AND COMPLIANCE IN THE EGYPTIAN INSURANCE INDUSTRY

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Introduction

Corporate governance and the decision-making processes of insurance companies are key components of insurance supervision. The “Insurance Core Principles on Corporate Governance” published by the International Association of Insurance Supervisors (IAIS) on January 19, 2004, serves as an internationally recognized resource on this subject for insurance supervisors.

With the increasing complexity of the insurance sector in Egypt, companies will be forced to make significant modifications in the way they manage risk. New supervisory and operational challenges will require companies to re-think their approach to corporate governance and compliance. The successful insurance companies will realize that an effective control environment not only helps manage risk but results in corporate behavior which positively affects the bottom line.

The Egyptian Insurance Supervisory Authority (EISA) can work with the insurance industry to strengthen corporate governance in several ways, such as:

- Discussing the expanding and increasing risks faced by insurance companies
- Explaining why it is important to manage these risks through integration of governance and compliance, and
- Advising the insurance industry on how to develop, manage and sustain an environment which integrates governance and compliance.

It is important that every insurance company project a single vision that embodies its values, ethics and principles which define and distinguish it from its competitors. Senior management and the Board of Directors should speak to this vision with a single voice so that its employees, intermediaries, consumers, investors and supervisory agencies understand and embrace the vision.

The Expanding View of Risk

Insurance companies are facing more risks today, including; operational risk, strategic risk, reputational risk and compliance risk. These broad risks require effective controls but the controls within many insurance companies have often not kept pace with the risks.

New laws, decrees, investor pressure and media scrutiny all play a role in more supervisory oversight. Government budgets for enforcement and monitoring is increasing as well as emerging global standards from organizations like the IAIS.

Shareholder pressure and expansion beyond core competencies are challenges created by new insurance products, multiple distribution channels, competitive pricing, unstable financial markets, reduction in expenses and often industry convergence.

Companies must have effective controls in place to manage all risks.

Measuring Efficiency and Effectiveness of Controls

A company's efficiency can be categorized as: high, medium or low.

High efficiency is characterized as: (1) reliance on continual monitoring and review of periodic testing, (2) use of dashboard for key indicators and controls, and (3) reliance on certifications and acknowledgements.

In a company with medium efficiency, we find (1) some marginal testing required for key activities, (2) some reliance on automated monitoring, and (3) reliance on certification and acknowledgements.

A low efficiency environment, however, involves (1) substantial manual efforts, and 2) testing and validation is required of activities.

The effectiveness of the above controls may fall into one of the following categories: unreliable, informal, standardized, monitored or optimized.

- *Unreliable-*
  This is described as an unpredictable environment where controls are not designed or operational.

- *Informal*
  Controls are designed and in place but are not adequately documented. Risk identification is narrow and the process lacks maturity.

- *Standardized*
  Controls are designed, in place and are adequately documented. A broad category of risks are targeted.

- *Monitored*
  There are standardized controls in place with periodic testing for effective design and operation with reporting to management. Performance is measured.

- *Optimized*
  Integrated internal controls with real-time monitoring by management and continuous improvement. These are both strategic and value enhancing.

A company which desires to differentiate itself in the Egyptian market must put in place controls of medium to high efficiency to achieve standard to optimized effectiveness.

A New Perspective on Compliance and Governance

The control objective here is to create a comprehensive control environment where all governance and compliance management issues across the organization embody and support the company's vision. Areas may include:

- Laws, regulations and decrees
- Financial and operations compliance
- Business practices
- Contracts
- Policies and commitment
- Voluntary standards and industry best practices

Some Egyptian insurance companies will not be able to meet these new challenges if they rely on old assumptions such as:

- Our employees will simply have to work harder
- Fines/penalties are just a "cost" of doing business
- EISA will understand if it takes time to get controls in order
- We have good people so we do not need additional controls
- More control will cost too much.

Insurance companies must begin to embrace a new set of governance assumptions to create a comprehensive control environment:

- Subsidiaries, business units and shared services must all work together to leverage expertise and best practices
- Senior management and the Board must continually monitor the effectiveness of compliance controls and modify the design of these controls as necessary to adapt to a changing environment
- Compliance enabling technologies may be required to facilitate and coordinate an insurance company compliance program
- Management must establish a compliance infrastructure that is robust and flexible enough to handle changing compliance requirements.

The "payback" for senior management and the Board when using this integrated approach is that it allows for new business opportunities as a result of:

- Enhanced reputation and brand
- Secure license to operate
- Maximizing shareholder value
- Legal protection from consumer lawsuits
- Effective and efficient management of the organization
- Enhanced morale and productivity of staff, and
- Sustainable value by managing expectations of stakeholders.

Governance and the Compliance Road Map

The terms envision, improve, operate and sustain provide a framework for the execution of beginning- to- end governance and compliance which provides a foundation for the success of a company in a changing environment. These activities must be linked to a company's business objectives and supporting capabilities. They allow value to be added through governance and compliance. The steps for this integrated approach Include:

- **Envision***:* Set objectives, Assess, Plan

  Senior management and the Board must define governance and compliance objectives in the context of the company's risk appetite, profile, resources, mission and vision. There must be a clear message from the top so senior management and the Board must be involved in this process. A clear vision with a mission statement, set of principles and code of conduct must be put in place (Exhibit 1).

  A risk assessment must be completed against strategic objectives with an evaluation of the cost and the potential for rate of return. Additional steps include; assessing the risk profile and the capability framework, as well as benchmarking. What will be the plan for continual improvement?

  Finally, a strategic plan must be developed to address the gaps and achieve the vision and objectives. The road map must also be defined and aligned with resource requirements. Senior management and the Board must keep in mind the cost of change versus no change.

- **Improve*:*** Develop, Deploy, Change

  The development stage involves designing and developing organizational, process, people, information flows and technology components of the framework.

  Deploy refers to implementing structures, written company and business unit policies, procedures and processes. The company should leverage existing technology infrastructure and add where necessary to achieve governance and compliance objectives.

  Change or the implementation stage involves cultural and program alignment with the company's objectives through communication and training programs to achieve the desired change.

- **Operate***:* Execute, Monitor, Respond

  Execution involves managing the requirement and executing on governance and compliance objectives, policies, procedures, processes and organizational activities. Identify events and leverage the program to accelerate any issue identification and resolution. Effective technology for "real time" monitoring should be used.

In the monitoring phase, internal and external benchmarking is conducted to evaluate efficiency and effectiveness. Continuous monitoring of performance, quality and efficiency is also done. Audits, performance reviews and evaluations are completed. Costs and/or savings of the implementation are reviewed.

The next step is to respond by identifying and managing incidents. Here it may be necessary to clarify and refine the company's internal communication.

- **Sustain***:* Communicate, Review, Adapt

  In the final step of the framework engage external and internal stakeholders to communicate performance and validate expectations. Coordinate communications, reporting and assurance with emerging and existing requirements and standards.

  A review should be completed by senior management and the Board to evaluate the effectiveness of the program.

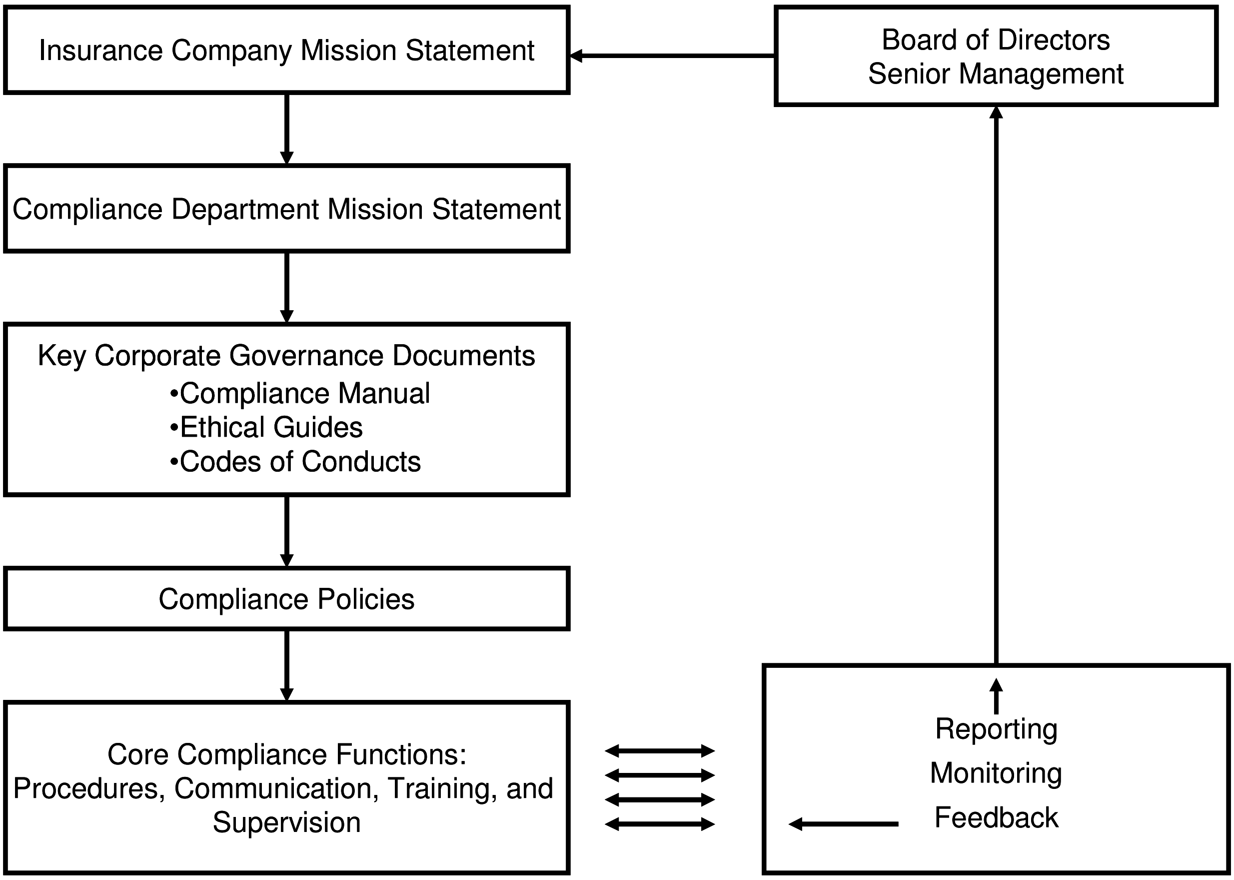
  Lastly, adapt by continuously improving the organization, processes and technology. Continuously improve cost efficiency and return on investment. Adapt the company's vision, objectives and management model to align with new requirements and new expectations.

Summary

The key to managing expectations using this governance and compliance model is to align controls with risks, goals and objectives. This is a recommended approach for the insurance industry in Egypt but does not have to be limited to this sector. The more complex any company becomes the more operational and compliance challenges it faces to meet expectations. EISA can assist the insurance industry in meeting these challenges by discussing corporate governance and compliance with senior management of insurance companies through informal presentations as well as, during market conduct and financial examinations.

Exhibit 1:

Governance and Compliance Model



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