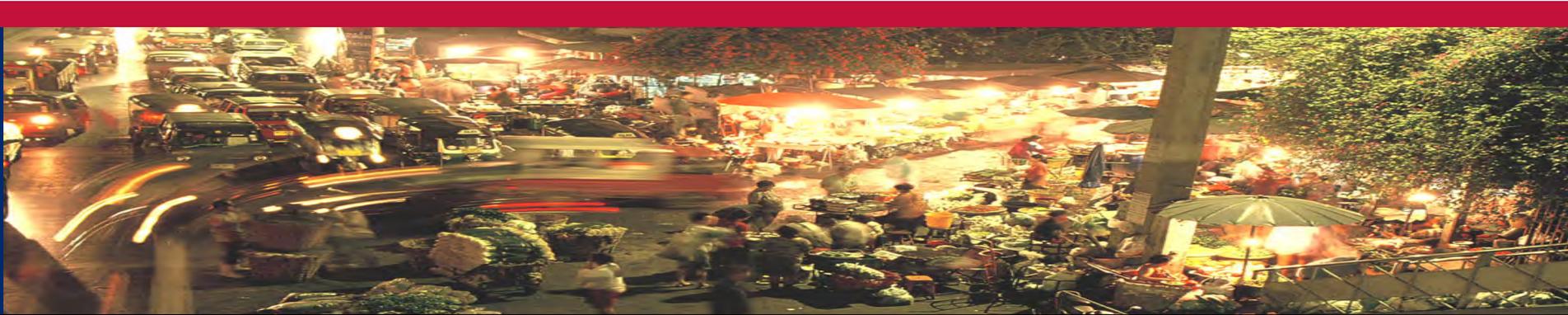




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Assessment of Best Regulatory Practices in ASEAN

June 15 2013

Prepared by Ray Willing



OBSERVATIONS

- Indonesia has promulgated a number of Insurance Laws over the last few years intended to bring it in line with International Standards.
- International Standards impacting insurance are primarily in three very important and related areas:
 - ❖ Insurance Prudential Standards set by the International Association of Insurance Supervisors (IAIS). The IAIS has 26 Core Principles which are considered the minimum standards with which a country should comply.
 - ❖ International Financial Reporting Standards (IFRS) set by the International Accounting Standards Board (IASB).
 - ❖ World Trade Organization (WTO) where free capital flows and freedom of services are preferred.



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OBSERVATIONS

- With a population of over 240 million Indonesian has great potential to be an insurance powerhouse among its ASEAN and other nearby countries.
- Its Insurance premiums pool could exceed Malaysia and Thailand anytime soon. However penetration is low.
- Insurance contributes significantly to growing investment opportunities and capital markets development.
- As GDP grows so will insurance which will assist further growth.



Some Asia Pacific Insurance Markets

| Country | 2011 | | | | |
|-----------|---------------------|---------------------------|-------------------------------|------------------------|-------------------------------|
| | Pop'n (Millions) | Life Premiums (USD) | Non Life Premiums (USD) | Life Premium (%GDP) | Non Life Premium (%GDP) |
| Australia | 21.8 | 45,187 | 43,899 | 3.0 | 3.0 |
| Singapore | 4.9 | 11,275 | 8,188 | 4.3 | 1.5 |
| Malaysia | 28.4 | 9,307 | 4,965 | 3.3 | 1.8 |
| Thailand | 68.6 | 9,218 | 6,028 | 2.7 | 1.7 |
| Indonesia | 235.3 | 9,437 | 4,655 | 1.1 | 0.6 |
| Vietnam | 88.8 | 8,818 | 1,027 | 0.7 | 0.9 |

Markets similar in size

Penetration to catch up?

Source: Ernst & Young; Swiss Re; Reserve Banks Australia NZ



Investments by the Insurance Market

| Description | Year | |
|-------------------------------------|-----------|-----------|
| | 2007 | 2011 |
| Life Insurance | 91,728.9 | 203,035.4 |
| Non Life Insurance | 19,061.0 | 39,949.3 |
| Reinsurance | 978.2 | 2,471.4 |
| Social Insurance and Workers | 62,039.6 | 117,507.1 |
| Civil Servants, Armed Forces/Police | 28,419.9 | 56,745.4 |
| Total | 202,227.6 | 419,708.6 |

Doubled
In
4 Years

Source: Bapepam 2011 (Billion Rupiah)



Where has the Insurance Market Invested?

| Description | Year | |
|-----------------------|------------------|------------------|
| | 2007 | 2011 |
| Government securities | 52,714.2 | 92,423.3 |
| Bonds | 24,138.3 | 58,601.6 |
| Deposits etc | 46,791.2 | 87,703.8 |
| Shares and Buildings | 32,805.6 | 82,417.5 |
| Mutual funds | 30,667.1 | 86,303.1 |
| Other | 15,074.2 | 10,280.4 |
| Total | 202,217.6 | 417,729.7 |

Source: Bapepam 2011 (Billion Rupiah) modified

Doubled
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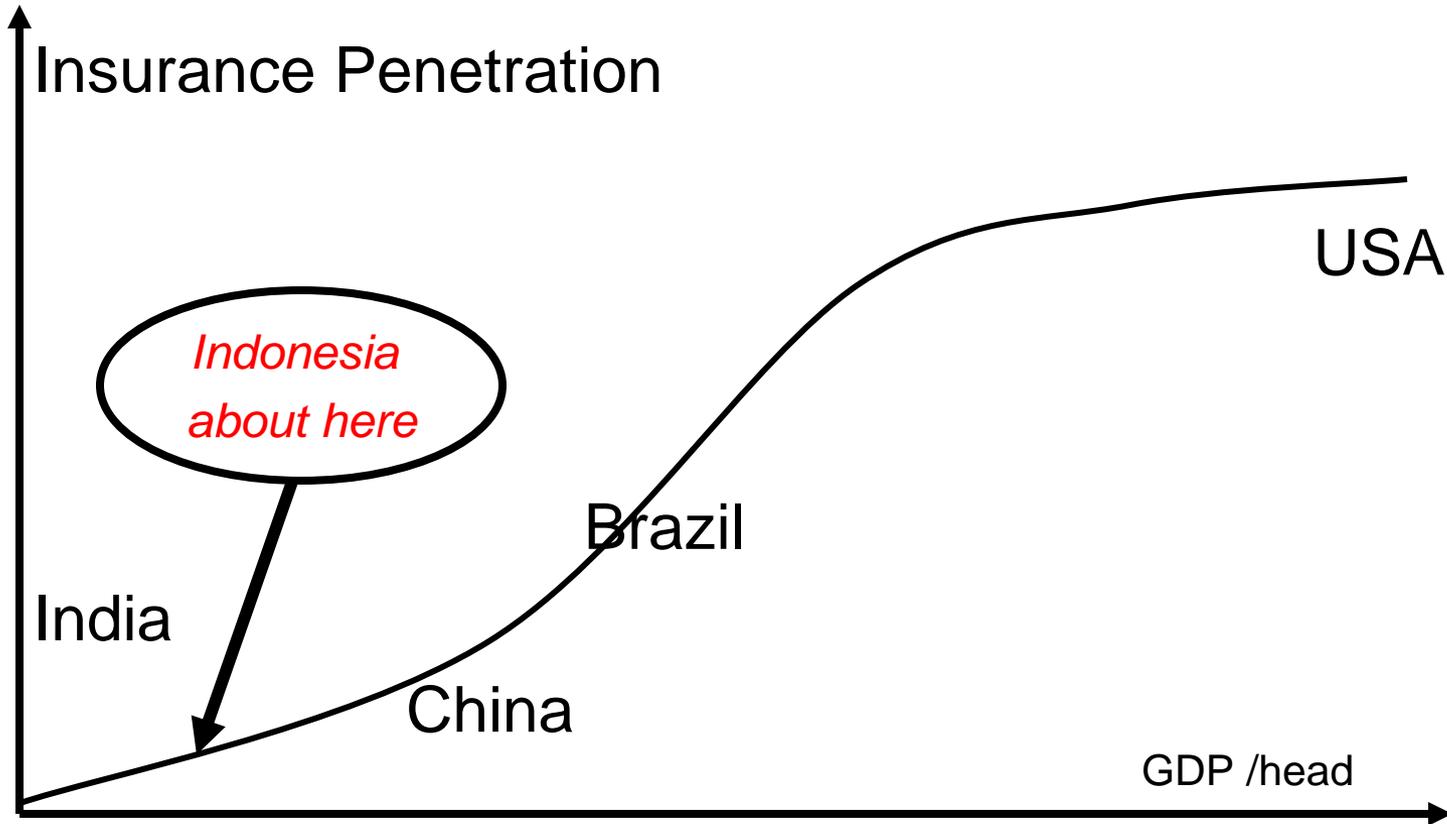
Source: Bapepam 2011 (Billion Rupiah) modified

Doubled
In
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As GDP Grows Insurance Grows



Source: Swiss Re Sigma No 3/2012 and Gerry Dickerson
London Business School



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OBSERVATIONS

- Best Practice in (some) WTO objectives, Insurance Regulation, Insurance Accounting and will assist insurance market development
- More insurance expertise and capacity need to be encouraged.
- More insurance awareness needs to be encouraged.



OBSERVATIONS

- The ASEAN Economic Blueprint aims to liberalize:
 - Life and Non Life Insurance and Reinsurance.
 - Insurance intermediation.
 - Services auxiliary to insurance.
- Liberalization in the above areas will assist the growth of the insurance market and help insurance prudential regulation
- More insurance expertise and capacity need to be encouraged.
- **More insurance awareness needs to be encouraged.**



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OBSERVATIONS

- OJK is requiring actuaries to become more involved. Good insurance accountants and auditors need to work with actuaries.
- Auditors will be required to audit Risk Based Capital (RBC) Statements in future.
- New International Insurance Accounting Standards should be adopted soon.
- There are some insurance companies who cannot meet RBC requirements.



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Best Practice in Insurance Regulation/1

- Thorough consultation processes before making changes to regulations or enforcement processes.
- A Risk-based capital (RBC) system – especially dealing with appropriate asset & liability valuation methodology.
- Prudential standards which are targeted at insurer behaviour (corporate governance, risk management, reinsurance, investments, etc)



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Best Practice in Insurance Regulation/2

- Supervisory practices (licensing, on-site inspections, risk rating of insurers, corrective powers & practice [eg directions to insurers, compulsory transfers of business])
- Infrastructure (contract laws and enforcement, insolvency laws and enforcement)



Recent Assessments against IAIS Core Principles

| Country | Outcome |
|-----------|-------------------------------------|
| Australia | A very good outcome |
| Indonesia | Not undertaken |
| Singapore | Underway – expected to be very good |
| Malaysia | Quite a good outcome |
| USA | A fair outcome |



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OBSERVATIONS

- There is a world wide group of insurance regulators (IAIS).
- The IAIS sets minimum standards against which countries can be measured. (IAIS ICP's – International Association of Insurance Supervisors Insurance Core Principles)
- Indonesia has recently joined the IAIS



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OBSERVATIONS

- Accounting standards need to be lifted significantly if Indonesia is to keep up with its peers in the insurance world.
- Overseas owned and locally incorporated insurers should be treated in the same manner as locally owned insurers.
- Directing overseas ownership through JV's need to be reconsidered.
- There are insolvent insurers allowed to continue operating in the Indonesian insurance market. This is unwise, unfair and represents poor governance from the regulator.
- Directing reinsurance locally may rebound on Indonesia if there is a significant loss in the market.



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INSURANCE AWARENESS

- Has been increasing through Shariah
- Micro Insurance and Crop Insurance might have some possibilities but they will need to be subsidized.
- Governments should encourage insurance take up by market based subsidies.
- Insurance companies want to expand markets and may be prepared to subsidize.
- MTPL is a good idea but needs significant forethought to avoid being a social stop gap



RECOMMENDATIONS – Trade related/1

- ❖ Review the undertaking in insurance services in relation to those “Services Auxiliary to Insurance” to clarify desired policy objectives. Settle on mechanisms that will facilitate insurance market growth and increase expertise whilst alleviating resource limitations.
- ❖ Require auditors to be independent and have the expertise to undertake an insurance audit. Require auditors to be nominated by a panel of auditors and independent insurance experts established to assess expertise thresholds.



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RECOMMENDATIONS – Trade related/2

- ❖ Place clearly on the ASEAN/APEC Agendas the formation of one umbrella ASEAN/APEC insurance regulator whose role is to obtain uniformity in regulations that impact cross border movement of goods and services.
- ❖ Consider very carefully all facets of MTPL before introduction to Indonesia whilst keeping in mind its ASEAN obligations



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RECOMMENDATIONS – Trade related/3

- ❖ That ASEAN assist development of Shariah and establishes processes with bodies such as IAIS which will facilitate good regulation. Stay closely in touch with the World Bank's work in this area. Consider very carefully all facets of MTPL before introduction to Indonesia whilst keeping in mind its ASEAN obligations



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RECOMMENDATIONS – General/1

- ❖ Remove directions on reinsurance placements. Continue to manage reinsurance exposure through the capital weightings (which are based on credit ratings) given to reinsurance assets in the RBC process.
- ❖ Allow foreign owned companies free access to the market provided of course that they can meet all RBC requirements which must be also be applied uniformly to all market participants.



RECOMMENDATIONS – General/2

- ❖ Explore high level socio-economic differences and explicit policy differences between Indonesia and Malaysia, India and Thailand in order consider policy options to expand the acceptance and purchase of life insurance products in Indonesia.
- ❖ Review the asset classes allowed to be invested overseas to ensure there is the best balance for prudential supervision and economic development.



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RECOMMENDATIONS – General/3

- ❖ Require life insurance companies to have a separate fund for each type of risk and investment fund. Require such separation to be legally enforceable importantly in any insolvency.
- ❖ Take action to remove in an orderly manner those companies whose RBC is inadequate.



In Summary

- ❖ Indonesia has promulgated many Insurance Laws.
- ❖ Does it have the capacity to implement these laws and ensure they do the job?
- ❖ It should:
 - ✓ Test the application of its insurance practices against its ASEAN peers. Arrange a Financial Sector Assessment Programme (FSAP) wherein its application of IAIS ICP's are tested.
 - ✓ Have better capitalised solvent insurers
 - ✓ Rapidly upgrade its technical competence starting with insurance audit expertise.