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Regulation and supervision of insurance risk transfer to the capital markets

**FSD CoP International Insurance Seminar:
*In pursuit of a more resilient and inclusive insurance sector***

Manila, Philippines – 21/22 October 2013

Marcelo Ramella



Agenda

- Transferring insurance risk to the capital markets
- Insurance risk transfer to the capital markets - Regulatory and supervisory developments



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Transferring insurance risk to the capital markets

Securitisation – Basic Structure

Securitisation of assets



Securitisation of liabilities



Source: IAIS (2009) ‘*Global Reinsurance Market Report – Midyear Edition: Developments in (Re)insurance Securitisation*’. (26 August 2009)



Transferring insurance risk to the capital markets

Securitisation

Insurance \neq Banking

Key differences

Insurance securitisation is ***liability-based***

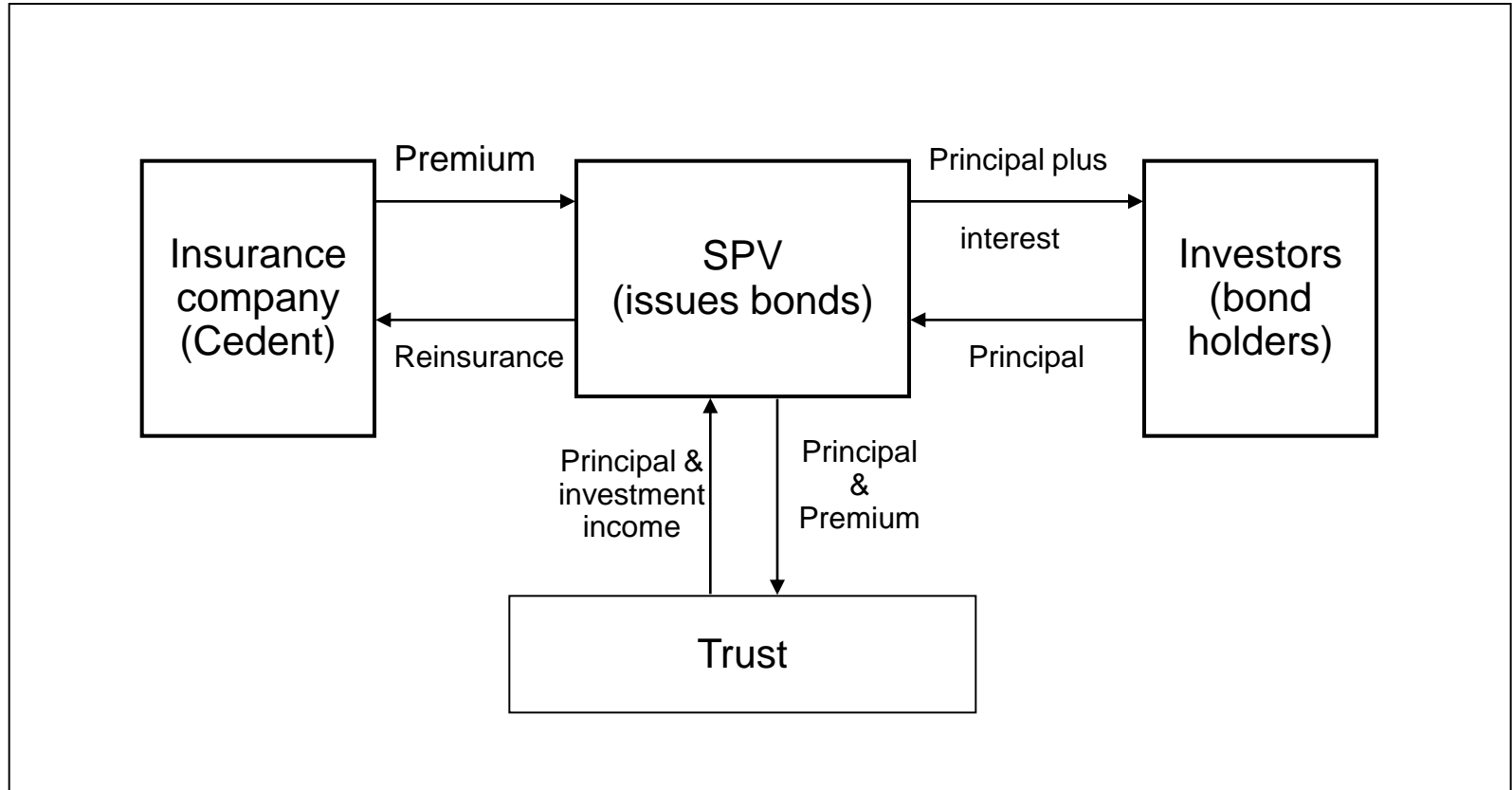
Ceding insurers remain liable to policy holders

Source: IAIS (2009) *GRMR MY Edition 'Developments in (Re)insurance Securitisation'*.



Transferring insurance risk to the capital markets

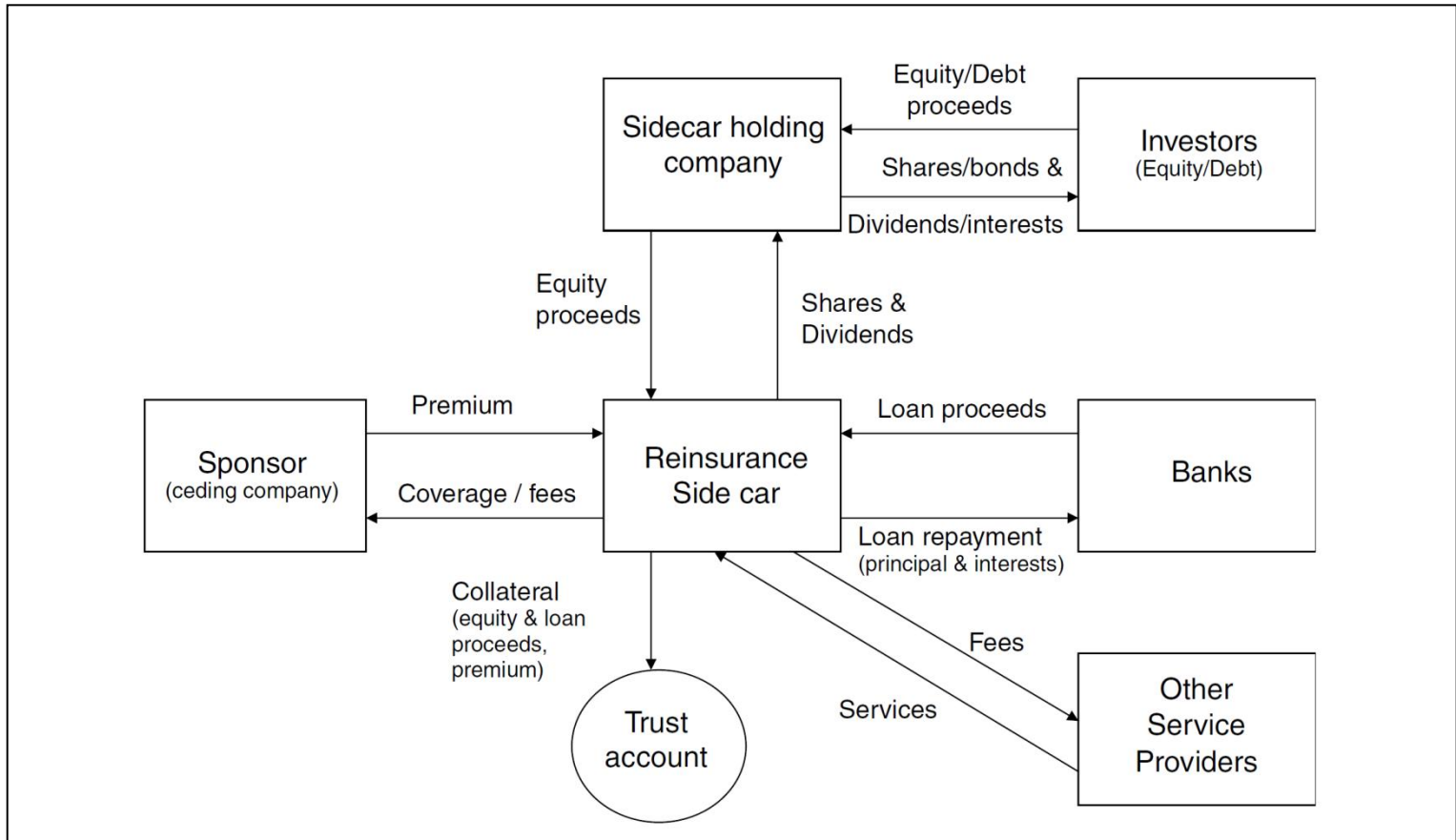
Basic *Cat Bond* Structure





Transferring insurance risk to the capital markets

Basic *Sidecar* Structure

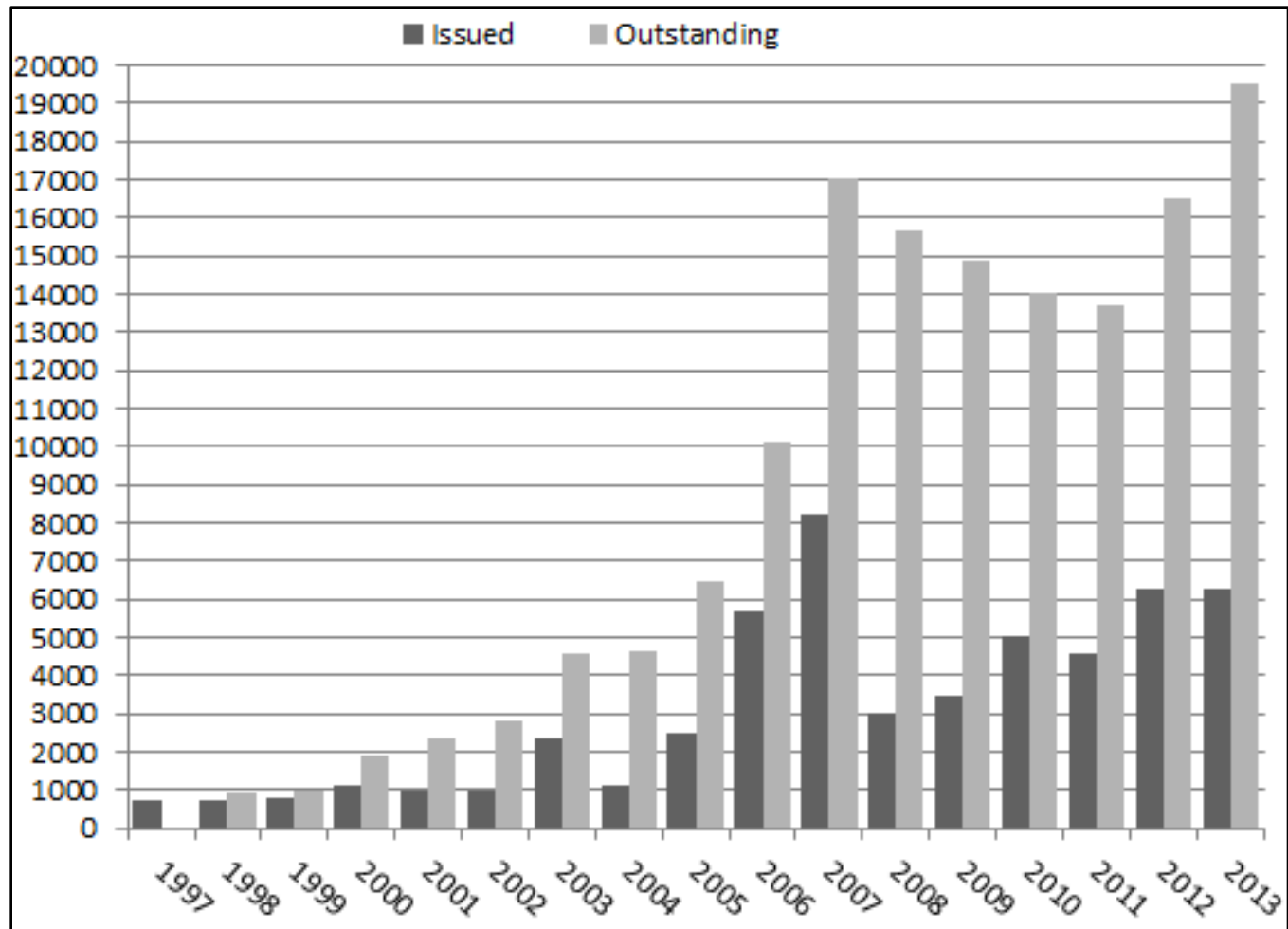


Source: Ramella, M. & Madeiros. L. (2007) *'Bermuda Sidecars: Supervising Reinsurance Companies in Innovative Global Markets'*, Geneva Papers, Issues & Practice, Vol.32(2).



Transferring insurance risk to the capital markets

Catastrophe bond risk capital issued and outstanding by year



Source: Artemis, October 2013 (www.artemis.bm)



Transferring insurance risk to the capital markets

The growing influence of insurance risk transfer to the capital markets in emerging economies

- “The new risk transfer mechanisms that reinsurers have created for advanced markets could help to expand reinsurance business in developing markets and fill the insurance gap in those countries to some extent ... demand for new innovative risk-transfer reinsurance schemes in the emerging markets could increase to \$10 billion by 2023 from about \$2.8 billion in 2013” (Standard & Poor’s, 9/Sep/13)
- A 2013 example:
 - ✓ ***Bosphorus 1 Re Ltd – USD400M risk capital protecting the Turkish Catastrophe Insurance Pool against earthquake risks in the Istanbul region for the period 2013 – 2016***



Agenda

- Transferring insurance risk to the capital markets
- Insurance risk transfer to the capital markets - Regulatory and supervisory developments



Regulatory and Supervisory Developments

Insurance Core Principle # 13

Standard # 6

Where risk transfer to the capital markets is permitted, supervisors are able to understand the structure and operation of such arrangements and to assess issues which may arise.

Source:

IAIS (2011) 'Insurance core Principles, Standards, Guidance and assessment methodology'. October 2011



Regulatory and Supervisory Developments

Authorising, supervising and winding-up SPVs

- The importance of the authorisation stage

Four sets of relationships:

- *Cedant(s) and SPV*
- *SPV and investor(s)*
- *Cedant, SPV and investors*
- *SPV and service providers*

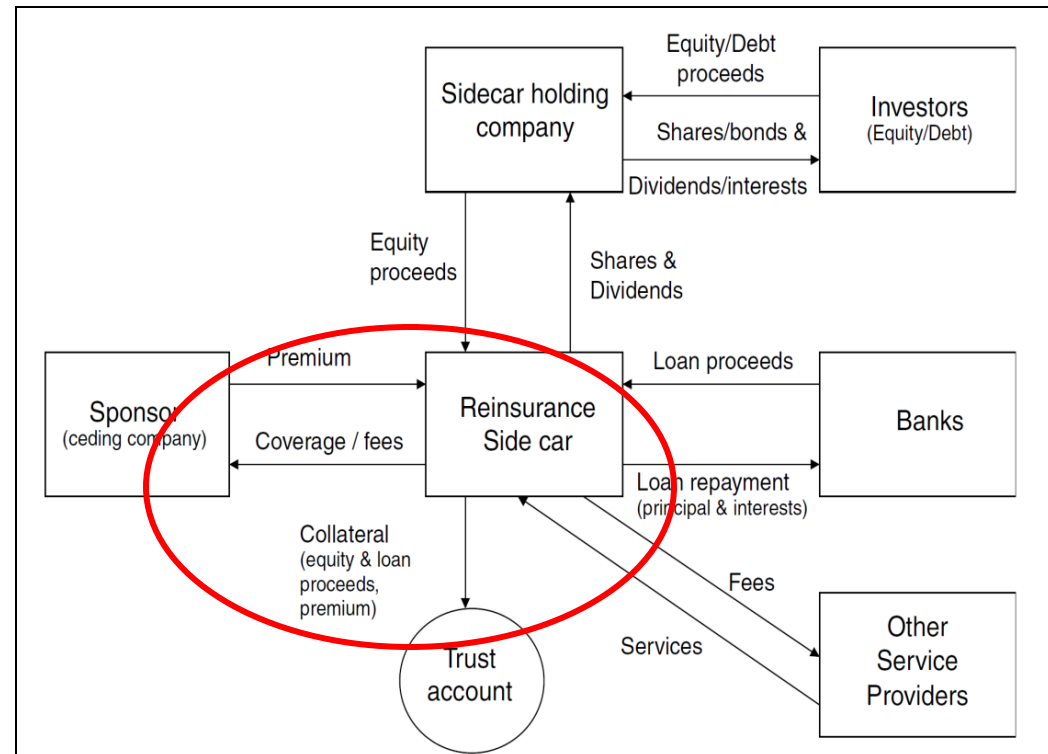
SPV “stand-alone“ issues



Regulatory and Supervisory Developments

Cedant(s) – SPV relationship

- ***The ‘fully funded’ condition***
- ***Cedant(s) access to SPVs funds***
- ***Effective risk transfer***
- ***SPV’s effect on solvency of cedant***

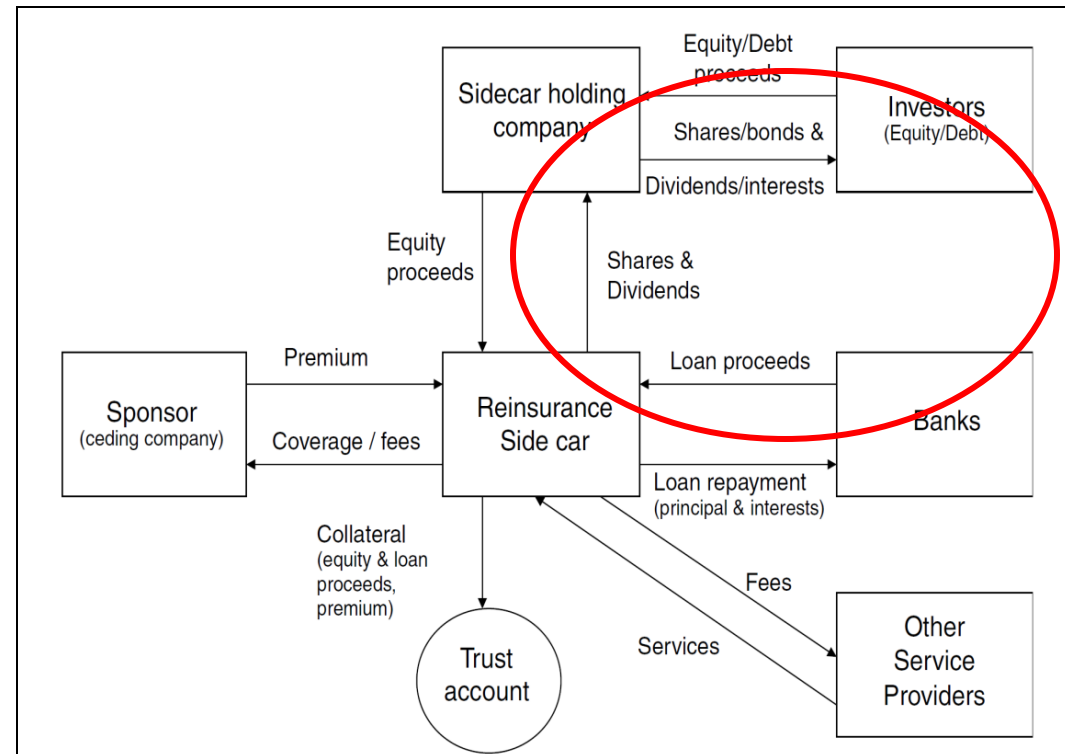




Regulatory and Supervisory Developments

SPV – Investor(s) relationship

- ***One or more investors***
- ***The ‘sophisticated participant’ nature of the investors***
- ***Risk disclosures***
- ***Subordinated nature of investors***

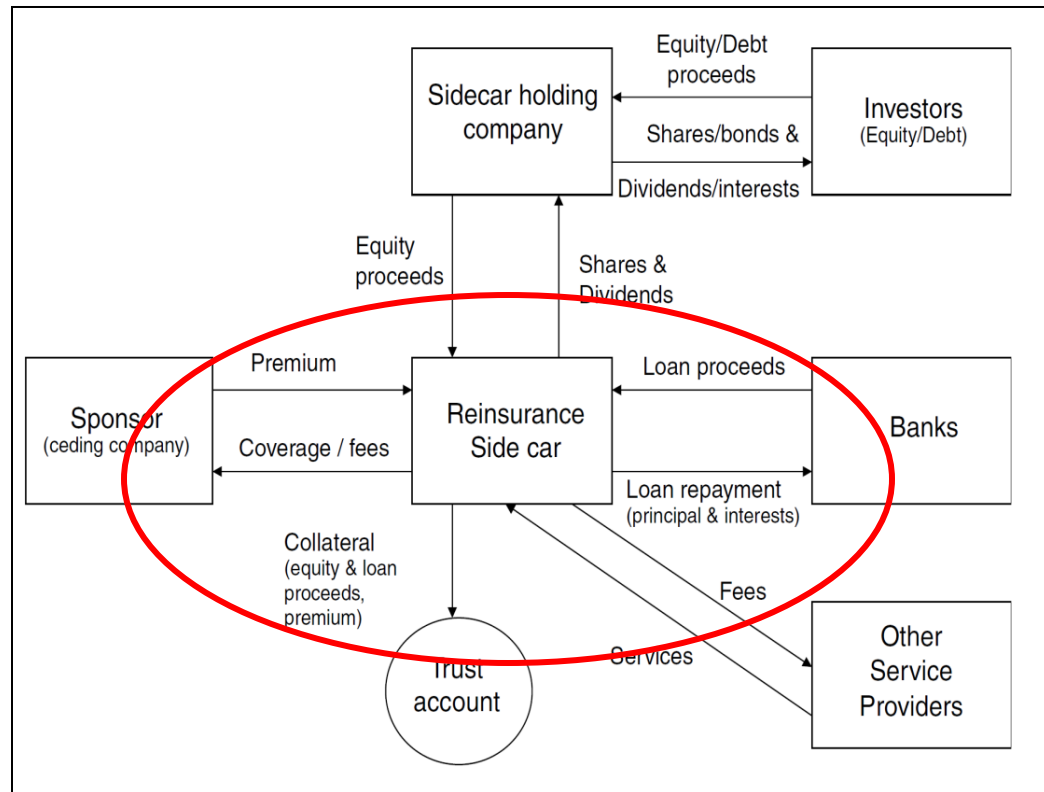




Regulatory and Supervisory Developments

Cedant(s) – SPV – Investor(s) relationship

- ***‘Prudent person’ principle***
- ***Maintenance of the ‘fully funded’ condition in time***
- ***Disclosure of SPV’s asset portfolio performance***
- ***Bankruptcy remoteness***

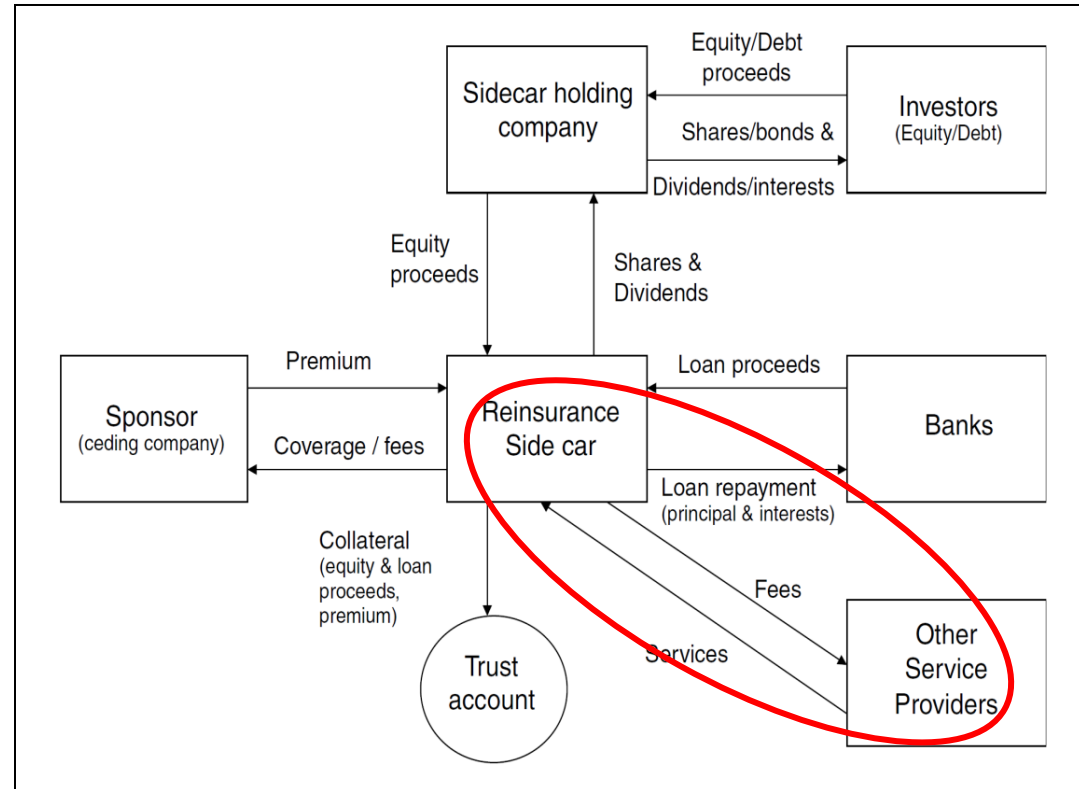




Regulatory and Supervisory Developments

SPV – Service Providers relationship

- ***Outsourced functions***
- ***Conflicts of interest***
- ***Management services providers***

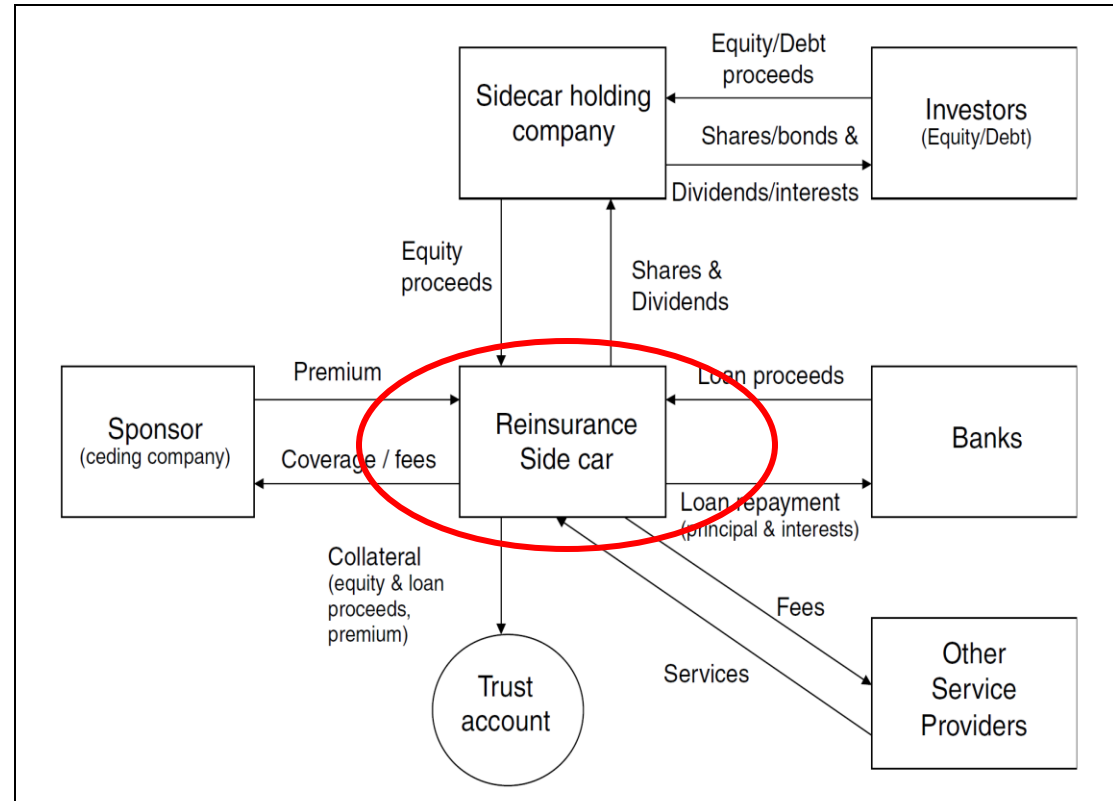




Regulatory and Supervisory Developments

SPV 'stand alone' issues

- ***At the authorisation stage***
- ***On-going supervision of the SPV***
- ***Oversight of SPV wind-up***





Summing up

Risk transfer to the capital markets

- **Crucial differences** between insurance securitisation and banking securitisation
- Growing trend of insurance risk transfer to the capital markets

Regulation and supervision of reinsurance and reinsurers

- Insurance Core Principles and Standards, ICP # 13
- Standard 13.6 – Risk transfer to the capital markets
- Understanding and addressing complexity and innovation
- Authorising, supervising and winding-up SPIs
 - ✓ Sophisticated parties
 - ✓ The ‘fully funded’ condition; policy-holder protection



Salamat!

Thank you!