

International Symposium

Enhancing

Life Insurance Regulatory Regimes in **ASIA**

**ALIGNMENT OF INTERESTS OF BOTH INSURANCE REGULATORS & INSURANCE
COMPANIES**

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ALIGNMENT OF INTERESTS OF BOTH INSURANCE REGULATORS & INSURANCE COMPANIES

by

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Good morning ladies and gentlemen and thank you for the opportunity to speak with you this morning.

It is an honour that you have decided to come to Australia to discuss regulatory developments because Australia is also keenly interested in developing its regulatory environment. Some of you will no doubt have heard of the recent inquiry into our own financial system the famous “Wallis Inquiry”.

But what is behind all of this? What brings us together at events like this, regulators from many nations in our region on the one hand and companies operating businesses across the region on the other.

The simple answer is that our interests are perfectly aligned to serve our customers and be competitive.

It is these two topics at which I will direct my talk this morning, drawing as I do, on the similarities of our collective interests.

Firstly customers.

Clearly the primary objective of any company is to maximise the wealth of its owners. This is as much the case for insurance companies as it is for any company. Almost uniquely however in the case of insurance companies the owners and customers are often one and the same. This is particularly the case for mutual companies – even where they have

demutualised, their shareholder lists still contain many policyholders. Of AXA Australia's 500,000 shareholders more than 90% are policyholders.

Maximising the wealth of our owners can only be sustainably achieved by protecting the interests of our customers and providing them with the best value and service. Whilst I accept some mis-practice will always exist hence the need for market order most major financial institutions realise their longevity relies upon looking after their customers.

In order to provide best value and service one needs to understand that customer needs are changing rapidly as we have already heard in terms of demographics, that is aging population, increasing wealth, longevity and increasing sophistication. Therefore it is imperative that companies provide customers with what they want, where and how they want products and services delivered and when they want them.

Let us consider this in more detail.

What do customers want?

Customers are becoming increasingly knowledgeable and concerned about their financial needs and wants. The proliferation of products from both insurers and non-traditional market players has provided a large choice for consumers. In addition, customers are increasingly searching for integrated financial solutions which address needs and therefore products need to be more innovative and sophisticated. For example we now see mortgage and superannuation products linked to transaction accounts; insurance products with critical illness riders designed specifically for women; growth in master trusts; portable superannuation schemes; importantly, customers also expect to obtain professional financial advice and options before being offered product solutions. This has seen the advent of the financial planning industry in many countries.

Secondly, where and how do customers want to obtain these products and services?

As we are all aware, agents have represented the predominant distribution channel for insurance products and will continue to be a significant method of distribution in the future. However, agents are changing their focus in a number of ways, particularly in terms of selling to needs rather than only providing products and also improving their professionalism to ensure that they are well positioned to provide more sophisticated product solutions and financial advice to their customers.

Over more recent times, we have seen a growth in alternative distribution channels. Accredited financial planners are providing products in addition to pure advice. Bancassurance is significant in some countries and represents a lower cost alternative to agency with a large potential given a bank's distribution capability and an extensive client-base. For example, Mayban Life is a specialist bancassurer operating in the Malaysian life insurance market. After a few years of operation, it has gained a 7% new business market share and its bank agents are highly productive, selling not only Mortgage Reducing Term products, but also a significant amount of traditional life insurance.

Technological innovation has seen the emergence of E-commerce and the Internet as potential distribution outlets. These represent low cost distribution alternatives for an increasing number of clients. In addition, consumers are able to compare and contrast products and services through these channels and also provide detailed knowledge regarding financial products. Importantly, transactions can be done on-line without an intermediary if the customer wishes it that way.

Other channels such as Direct Mail and Call Centres have had mixed success to date. However, they are likely to become more popular as technology advances even further.

Finally, when do customers want products and services?

Customer expectations of service have been increasing rapidly in line with their greater sophistication and knowledge of financial services.

Turnaround times for administration processes are shortening due to technological and system improvements, pressure from serviced-orientated non-traditional players and the need for rapid responsiveness expected by customers.

For example, 24 hour call-centres are becoming the norm and document processing times are being shortened. A customer-centric focus is now a key initiative for insurers that wish to maintain a good relationship with their clients, and improved client servicing, communications and support are keys to success.

It is clearly evident that the customer is of fundamental importance to the insurance company. However, regulators have an equally significant interest in the customer as well.

Let us consider the insurance model in its simplest form – we have Government, shareholders, policyholders and distributors all vying for a slice of the pie. The Government's primary role is to serve the public. Indeed, a healthy growing insurance industry provides employment for a large number of people as well as representing a vehicle through which consumers can be educated about their financial needs and how insurance products can satisfy these needs. The regulator has an important responsibility to protect the consumer and ensure that they get a fair deal. In an unregulated environment, it is likely that the shareholder and the distributor would gain a disproportionately larger slice of the pie at the expense of the customer, the policyholder.

Importantly, the monies from customer premiums are used by Government to fund projects, develop infrastructure and to finance forays into newer, technology-based industries. The development of a regulatory environment where customers are satisfied with the level of protection, servicing and strength of the industry is necessary to ensure the mobilisation of significant savings for the benefit of the country.

Let us now consider some examples of how regulators have acted with respect to developing an environment which supports the customer.

In Australia, we have seen a significant increase in the amount of regulation surrounding the conduct of agents in the market. Agents now conduct a needs analysis before they can recommend suitable products to meet customer needs. In addition, the benefit illustrations for these products have also been regulated in terms of consistent earnings rates and assumptions. This ensures that companies do not promise unachievable future benefits and it allows customers to make a fair comparison between products from different companies. Solvency and capital adequacy standards have also been raised to ensure that the industry players remain financially sound and are able to pay customer claims as they arise. A similar regulatory regime exists in the UK.

In Singapore the MAS has also made significant changes to the insurance regulations for the benefit and protection of customers. This includes increased solvency standards, the introduction of an appointed actuary, implementation of benefit illustration guidelines, licensing of brokers and dissolution of the multi-agent network.

More stringent regulations are also in place with regard to agency distribution. Agents must have suitable accreditation and be provided with stipulated training.

Companies are limited in their agent recruitment to the maximum of 40% of inforce agents or 150, whichever is the greater. Agency growth may be further restricted if companies cannot maintain a 90% 2-year persistency level. Agency is also limited to 3-tiers and distribution expenses are capped.

Malaysia's insurance regulations are also following a similar trend to those of its neighbour with a view to strengthening the industry and ensuring a professional approach to business from companies and their distribution networks. Anti-trust legislation has also been implemented in countries like Hong Kong, Indonesia and Singapore to protect policyholders and companies.

One might regard these regulations as strict and onerous for companies and their agents. However, they are designed to promote an environment where the customer is assumed of being protected and their "slice of the pie" fair and equitable. In the end, if the customer is happy, they will purchase insurance products from agents and the companies they represent, which is their objective in any case.

From both the insurers' and the regulators' perspectives, the reputation of the industry is enhanced by the customer endorsement of regulatory process, protection of their interests, servicing standards and financial security. Regulators also have a role in monitoring the market place to ensure that companies are compliant and to implement regulatory improvements in line with market trends.

It is evident from this discussion that one of the more difficult tasks for the regulator is to strike a balance between "protecting customer interests" whilst allowing companies enough flexibility to develop innovative products and distribution methods which leads to a broader choice of products, often at lower prices. It is also pleasing to note that regulators around the world have generally done an admirable job in balancing the share of monies obtained by Government, shareholders, distributors and policy owners.

Having discussed the importance of the customer to both the insurance company and the regulator, I now wish to elaborate on “being competitive”. This is as important for the insurance company as it is for the regulator.

The dismantling of trade barriers worldwide as well as the other global trends which have already been discussed this morning will see insurers that currently operate trans-nationally redefine themselves as truly global enterprises. In an environment where entry barriers are falling and traditional product and market boundaries are becoming blurred, there will be great pressure on smaller players to consolidate or exit the market and larger companies to globalise or develop a strong niche position in order to remain competitive.

This trend is expected to continue into the new millennium and we will see the emergence of a smaller number of large global players in many insurance markets alongside a number of strong, well-positioned niche players or specialists.

The other major effect of international insurance trends is increased industry consolidation. Regulators are encouraging smaller or weaker players to merge or be acquired by larger players in order to ensure their survival in an increasingly competitive environment and to strengthen the local industry. For example, in Malaysia, Bank Negara is encouraging the insurance industry to undergo M&A activity and they aim to finish up with some 15 strong insurance groups.

More sophisticated customers will want financial planning, product choice, high level of servicing, increased protection from mis-selling and good investment returns. Companies will need the freedom to be flexible, innovative and an environment which engenders growth and profitability in light of the trends.

Not only have these trends forced regulators to make significant changes in a relatively short space of time, but it has also placed an increasing focus on their own competitiveness.

Traditionally, regulators developed insurance legislation and regulations in isolation from other markets around the world. However, we now see many regulators spending considerable time and effort to study the insurance regulatory systems of other countries (eg. IRDA in India) to ensure that the regulatory changes they make reflect world best practice as well as being tailored to suit the local industry.

Regulators play a crucial role in ensuring both harmony and control in an increasingly competitive environment. Already we are seeing customers having choices for savings, protection and investment from non-traditional industry sectors. Eventually, through globalisation both companies and customers will have the ability to buy and sell on a cross-border basis. Hence it will become necessary for regulators to compete on both a cross-sector, cross-border basis to ensure that they retain the services of companies and customers within their own local markets.

Which brings me back to the beginning of my presentation. Ultimately the interests of both insurance regulators and insurance companies are perfectly aligned.

Insurance companies reason for existence is to maximise the wealth of their owners. This can only be sustainably achieved by protecting the interests of our customers and providing them with the best value and service. Often, particularly in the case of mutual companies, insurance companies' customers and owners are one and the same.

Insurance regulators reason for being is also to protect the interests of insurance companies' customers and ensuring they are provided with the best value and service.

With this common interest therefore I trust we can continue to work together to maximise the wellbeing of our common customer – the consumer. Thank you