

Andreas Dombret and Felix Hufeld: The Bundesbank and BaFin – “The two organisations benefit from each other’s specific expertise”

Interview with Dr Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank, and Felix Hufeld, Chief Executive Director of BaFin, by the “BaFin Magazin” published on 1 August 2013.

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The Bundesbank and BaFin are collaborating closely in insurance supervision. In an interview, Bundesbank Executive Board member Andreas Dombret and BaFin Chief Executive Director Felix Hufeld explain how that collaboration benefits both organisations as well as Germany as a financial centre.

Dr Dombret, Mr Hufeld, under the Financial Stability Act (Finanzstabilitätsgesetz), the Bundesbank and BaFin will now also cooperate in supervising insurance companies. How will the supervisory tasks be divided up?

Hufeld: I can answer that question quickly: microprudential insurance supervision, ie the supervision of individual insurers, insurance groups and pension funds, will remain the sole responsibility of BaFin. The Bundesbank is not involved. That is thus a different situation than in banking supervision.

Dombret: The Financial Stability Act mandates the Bundesbank to help ensure that the financial system remains stable. It is responsible for macroprudential oversight of all sectors of the financial system – which includes insurers. The act assigns analytical tasks, in particular, to the Bundesbank. It is our job to identify potential dangers and assess constellations that could impact financial stability as a whole. These analyses form the basis for the discussions within the Financial Stability Committee, where the Federal Ministry of Finance, BaFin and the Federal Agency for Financial Market Stabilisation add their own input. Building on this risk analysis, the Financial Stability Committee may then issue warnings and recommendations.

That means that BaFin and the Bundesbank exchange more information nowadays than they used to.

Dombret: Yes, the Financial Stability Act clearly stipulates that we share all observations, conclusions and assessments required to fulfil our respective tasks. The two authorities will mutually benefit from the information and the special expertise that they exchange. The express legislative intent underlying the act is for us to work hand in hand and swap notes regarding relevant data, facts and evaluations. And we will jointly ensure that this is the case.

What does that mean in concrete terms?

Hufeld: We have laid down the details in a joint administrative agreement, which at BaFin applies to all areas of supervision. The need now is to breathe life into that agreement. We have looked at all the data that we or the Bundesbank collect to determine for what prudential perspective they are relevant. Certain data that are collected on a regular basis are exchanged continuously. BaFin has access to all Bundesbank data and information – and vice versa – to the extent necessary for each institution to fulfil its respective mandate. We will now work out how best to proceed in practice.

Should insurers fear that the exchange of information will be to their disadvantage?

Dombret: On the contrary. It is in their own best interests that we seek to maintain a stable financial system. The experience of recent years has clearly demonstrated the dangers associated with systemic risks and cross-sector contagion.

Hufeld: I agree. And what Mr Dombret just said of course applies equally to microprudential supervision. If the Bundesbank shares valuable macroprudential insights with us, insurers

and their policyholders will be the first to benefit. Another advantage for insurers is that they will not need to establish a separate regular reporting channel to the Bundesbank as we forward the data that we receive to the Bundesbank. It goes without saying that the forwarded data will be treated confidentially since the Bundesbank, just like BaFin, is sworn to secrecy.

What do the Bundesbank and BaFin do with the information?

Dombret: That is laid down in the legal provisions: we use the information to fulfil our respective mandates. For us, that means that we use the data provided by BaFin to assess the stability of the financial system as a whole from a macroprudential view. BaFin, in turn, uses our data and insights to effectively supervise insurers and thus ensure that they can honour their contracts on a long-term basis. As I mentioned earlier, the insights gained also feed into the consultations of the Financial Stability Committee.

Hufeld: There are many ways in which the Bundesbank's macroeconomic and macroprudential expertise will be valuable to us. Take the issue of the current low-interest rate phase. The Bundesbank analyses and evaluates the information that we provide. We, in turn, can use the results for our microprudential supervision. The exchange of information is not, therefore, a one-way street; it results in a beneficial symbiosis of macroprudential and microprudential knowhow, which will strengthen Germany as a financial centre.

Regarding the low-interest rate setting: how will you collaborate specifically on this issue?

Hufeld: This issue demonstrates the importance of our cooperation. We can draw a reliable and comprehensive picture of the situation only if we take due account of both the relevant macroeconomic and macroprudential factors and the individual insurers' particular circumstances. And the ongoing period of low interest rates naturally also plays an important role in the Financial Stability Committee. We must, therefore, grapple with a difficult subject at the very outset of our collaboration. However, I am sure that will only strengthen our cooperation.

Dombret: The current low-interest rate setting is making itself felt in all financial sectors. Credit institutions and insurers must take this into account in their business plans. As the Bundesbank has, for some years, been observing the effects of the low-interest rate environment on the financial system and, not least of course, on life insurers, I expect our cooperation with BaFin to prove fruitful in this field, too.

Another key issue from both a macroprudential and a microprudential perspective is that of systemic relevance. The Financial Stability Board (FSB) recently ranked nine insurers as global systemically important insurers (see link below). How important do you think this step is?

Dombret: The publication of this first list of global systemically important insurers marks another step on the path towards a more stable financial system. Banks are not the only entities that can be systemically important – market infrastructures and insurers can be, too. The main factors determining an insurer's systemic importance are, first and foremost, its interconnectedness within the financial system and the size of its non-traditional and non-insurance business. I therefore fully support the FSB's recent move. However, it is clear that we still have a considerable way to go. We must now specify and finalise the regulatory consequences associated with this ranking. That will not be easy. Just think of the challenge of creating, for the first time, a harmonised international basis for imposing potential capital surcharges in the insurance sector.

Hufeld: It is good that we now know where we stand. Insurers are systemically important in a different way than, say, banks, as they do not trade with one another. Nonetheless, identifying global systemically important insurers is a key step towards maintaining financial stability and protecting policyholders. I believe that the best way of protecting policyholders is to establish effective recovery and resolution plans and to tailor supervision to the complexity

of the business. As I said earlier, we now need to spell out the regulatory consequences. May I just add that the fact that the list features no reinsurers does not mean that this group of insurance companies is not considered systemically relevant. A decision on this issue will be taken next year.