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Mr. Roger Cole
Chairman of the Risk Management Group
Basel Committee on Banking Supervision
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel

Munsbach, July 30, 2003

Our ref. : CDS/ccd 2003-76

Dear Mr. Cole,

Concern : Commentary on the third Consultative Document, The New Basel Capital Accord Distinction between « Direct Insurance Captives » and « Reinsurance Captives »

Gecalux Group welcomes the decision of the Basel Committee on Banking Supervision to invite the industry to comment on the third consultative document of the New Basel Capital Accord.

In this respect, we would like to comment on the advanced measurement approach for operational risk and in particular in respect of risk mitigation through insurance policies and captive affiliates. More specifically, we would like to discuss the possible introduction of a distinction between **insurance and reinsurance captives** within this context (V. Operational Risk, iii risk mitigation, 638, pg. 130 of the report).

The consultative document mentions that for a bank to benefit from risk mitigation through insurance, the following is required :

> *« The insurance is provided by a third party entity. In the case of insurance through **captives** and affiliates, the exposure has to be **laid off to an independent third party entity, for example through re-insurance**, that meets the eligibility criteria »*
> *(pg. 130)*

We would like to draw your attention to the fact that **reinsurance captives**, contrary to insurance captives, operate exclusively by re-insuring the insurer that issues an insurance policy to the bank. The reinsurance captive therefore **never** insures the bank directly and as such we deem that, **unlike insurance captives, reinsurance captives should not require that exposures be laid off to an independent third party** as there is de facto already a third party insurer issuing the insurance policy.

... / ...

In fact, the insurer that has issued the insurance policy to the bank is always **fully liable** for the payment of claims to its insured even in the case when its own reinsurer, either the reinsurance captive or a professional reinsurer, is unable to fulfil its contractual obligations. This is the reason why local insurers closely examine the financial situation and the quality of the captive and its retrocessionaires to assess its own credit risk prior to issuing insurance policies and they are remunerated for this risk.

As you are aware, the insurance market, and particularly in the current context, does not provide sufficient coverage for operational risks, captive structures are then the only options left for some operational risks and as such, render most valuable services to their shareholders and contribute to improve the risk management of the banks. Requiring that **reinsurance captives** lay off the exposures to a third party (a retrocessionnaire) would be, from our point of view, counterproductive.

Gecalux Group therefore suggests that the text of the consultative document could be amended as follows to take into account the differences between direct insurance captives and reinsurance captives :

> ***« The insurance is provided by a third party entity. In the case of insurance through <u>direct</u> insurance captives and affiliates, the exposure has to be laid off to an independent third party entity, for example through re-insurance, that meets the eligibility criteria. <u>In the case of reinsurance captives and affiliates, the exposure does not have to be laid off to an independent third party entity, for example through retrocession, if the underlying insurers are meeting the eligibility criteria</u> »***

We thank you very much for your help in clarifying this sensitive matter. Should you have any questions regarding the issue we have raised in this letter please don't hesitate to contact us.

Best regards,

Claude Dierkens
Chief Executive Officer