Ong Chong Tee: Confidence in and resilience of the life insurance industry

Speech by Mr Ong Chong Tee, Deputy Managing Director (Financial Supervision) of the Monetary Authority of Singapore, at the Life Insurance Association (LIA) Annual Luncheon 2015, Singapore, 4 March 2015.

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Dr Khoo Kah Siang, President of the Life Insurance Association,

Distinguished guests,

Ladies and Gentlemen.

1. Thank you for inviting my colleagues and I to the Association's 13th Annual Luncheon.

2. Modern life insurance is said to have its beginnings in London more than 300 years ago by a company called Amicable Society for a Perpetual Assurance, with the aim of allowing an amicable distribution of contributions to be made by deceased members to their surviving wives and children. But even during the times of Ancient Rome, it is believed that some forms of life insurance existed to help mitigate the costs of burials of deceased members and to provide for their surviving families. While clearly much has changed in the industry, the central tenet of the industry has remained – to provide financial protection to dependants and in current times, also as a means of savings and wealth management.

3. A life insurance purchase is in essence a legal promise. In exchange for payment of premiums, an insurer will honour claims and make payment as agreed under the insurance policy. Hence given the typically long term nature of the commitments, confidence in and resilience of the life insurance industry must underscore its growth and development. If one were to type "life insurance" and do an image search over the internet, a very common picture is that of the umbrella; and it is easy to understand why – insurance as protection, a cover, or a shield. But the umbrella has to be a dependable one, when one needs it most.

4. Two critical factors underlie consumers' confidence in the life insurance industry:

i. First, insurers, together with financial advisers, must be regarded as trustworthy and reliable. Consumers must be able to depend on them to provide appropriate financial advice and life insurance products to meet their needs; and issues of fairness and transparency must underscore the relationship.

ii. Second, given the long-term commitments, insurers must be financially resilient to be able to weather different economic, financial and industry cycles and have adequate financial resources to be able to honour claims.

5. Today, let me therefore take stock of two key policy thrusts that MAS has embarked on with many of you here – the FAIR initiatives and RBC2 – to enhance trust and resilience of the insurance industry respectively.

Enhancing consumers' trust in the life insurance industry: FAIR initiatives

6. I will start with the Financial Advisory Industry Review or FAIR. MAS first announced FAIR in 2012 with the formation of a review panel. FAIR aims to improve the quality of financial advice provided by the financial advisory industry by promoting fair dealing, and to raise the efficiency of the distribution of life insurance and investment products in Singapore.

7. There are three key initiatives under FAIR of particular relevance to the life insurance industry. These are the web aggregator, direct purchase insurance products and the balanced scorecard framework.

Web aggregator

8. First, the web aggregator. Life insurers offer a wide range of life insurance products to cater to the varied financial needs of consumers. However, it can often be a daunting task for consumers to be sufficiently informed of what's available to meet his needs and to have some easy way to compare life insurance products.

9. I am pleased to note that a web aggregator will be launched in early April as a collaborative effort between MAS, CASE and the life insurance industry. This will provide a single information portal that will enable consumers to easily look up available life insurance products and compare indicative quotes based on specified parameters in a user-friendly and interactive manner.

Direct Purchase Insurance

10. Second, direct purchase insurance products, or DPI. This is a new class of life insurance products for basic needs that is "retail-access friendly".

- It will be simpler as the features of DPI are broadly standardised. This allows a consumer to make straightforward product comparisons when deciding which DPI to purchase.
- It will be easier to buy as consumers who know what they want and do not need financial advice will be able to buy DPI directly from life insurers.
- It will be cheaper as no commissions will be charged.

11. There has been keen consumer interest in the DPI since its recommendation by the FAIR panel. Again, the DPI products will be rolled out in early April, along with the web aggregator. MAS will continue to work with the industry and consumer groups to conduct regular reviews to ensure that the product suite and features of DPI remain relevant in meeting the needs of consumers.

Balanced Scorecard Framework

12. Third, the balanced scorecard or BSC framework as proposed by the FAIR panel. MAS has implemented this framework in January 2015 with a one year transition period for the industry to be familiar with the framework before the requirements are legislated in January 2016.

13. While many financial advisors do their work professionally, it is also a reality that compensation system can shape sales behaviours, and sales-based remuneration models may not always align the interests of financial advisers with the consumers.

14. Under the BSC framework, a major proportion of a representative's remuneration will be based on whether the representative has acted professionally such as consumer needs analyses, recommendation of suitable products, and adequate disclosures. This BSC initiative will help to align the interests of financial advisers with their customers. Over the longer term, the BSC framework will boost consumer confidence in the professionalism of the financial advisory industry.

Strengthening the resilience of the life insurance industry: RBC2

15. Let me now turn to the new risk-based capital framework or RBC2.

Why the move from RBC to RBC2?

16. Insurance regulators around the world are adopting risk-based capital and Singapore has been a frontrunner with our current Insurance Risk-Based Capital (RBC) framework introduced in 2004. This risk framework has served us well, and our insurers have navigated largely unscathed through recent financial crises; while the framework allowed for regulatory

intervention in a timely and effective manner. Now, I know this begs the question – if it isn't broken, why fix it?

17. The answer is that the operating environment for global finance including insurance, has and will become increasingly complex given the more connected global markets, the vulnerability of contagion, an overall low interest rate environment that pushes investors including insurers to target more risky higher-yielding products and potential new risk areas such as in some emerging markets or in technology risks.

18. It is important that our insurance capital framework remains relevant and effective and that insurers operating in Singapore are well-capitalised to weather different crises and risk forms.

19. At the global level, the International Association of Insurance Supervisors (IAIS) has also embarked on the development of capital standards for internationally Active Insurance Groups ("IAIGs"); while the International Accounting Standards Board is expected to finalise its guidance on insurance contracts under IFRS4 sometime this year.

Progress on RBC2

20. Last year, MAS published our second consultation paper, which outlined our key proposals for RBC2. We also conducted the first quantitative impact study (QIS1) to assess the potential impact of the proposed changes on the industry. All direct life and composite insurers had participated in QIS1. I would like to thank the LIA and its members for the active participation and feedback. Indeed, many of you have expressed understanding and support for many of the proposed enhancements in the RBC2 framework.

21. Let me share a couple of high level observations from the QIS1 results with you.

22. First, there is an increase in risk requirements compared to the existing RBC framework. This is to be expected, given the more comprehensive risk coverage and higher target confidence level under RBC2. RBC2 targets a 99.5% confidence level over a one-year period, which is increasingly seen as the benchmark for insurers globally. From the results that I have seen, most of our insurers are able to maintain capital adequacy ratio or CAR of well above 100% under the preliminary set of RBC2 proposals.

23. Some industry players are naturally anxious if they will still have to maintain the same high buffers of way above 100% CAR or FSR under RBC2, as they do currently for RBC. This is not our expectation, given that the risk requirements under RBC2 are designed to be more risk sensitive, comprehensive and calibrated to a higher target confidence level.

24. A second observation is the greater differentiation in CAR between firms with different risk profiles. This is again to be expected as one of the main objectives of the RBC2 review is to improve risk sensitivity of the capital framework so as to more accurately reflect the different risk profiles of insurers.

25. MAS will continue to review and study the QIS results and take on board many of your feedback and suggestions.

26. As examples, we are going through comments from some industry participants relating to widening the eligibility criteria for the matching adjustment feature of RBC2, the possibility of giving some credit to the illiquid nature of some other liabilities that do not qualify for the matching adjustment, the calibration of risk charges for equities and long-dated corporate bonds, and the calibration of the operational risk charge, which has also been discussed with the industry.

27. Let me emphasize that we will implement RBC2 only after we have done a thorough calibration and assessment. We want the new capital framework to be more risk-sensitive and robust, but it should also be fit-for-purpose and not hamper well managed insurance businesses unduly. At individual firm level, the new framework does not seek to make it

better or worse for you compared to the current RBC, but only that how much capital that you will hold in future be more sensitive to your risk profile.

28. The MAS will embark on another stage of consultation and we are also targeting an additional QIS in Q2 2015. We will of course work closely with the LIA in this regard.

Conclusion

29. Let me conclude with a broad note on talent development for the insurance industry.

30. Over the years, MAS has been working closely with many of you on various manpower development initiatives. The Insurance Talent Development framework jointly developed with the industry in particular, focuses on expanding the talent pipeline for leadership positions. Last year, MAS successfully rolled out the non-life track under the Insurance Management Associate Programme and is now working closely with the Singapore College of Insurance to launch the life track this year.

31. I strongly encourage all of you to continue with your investment in talent development. This should go beyond technical competencies but to include issues of ethics and conduct.

32. To end off, I am sure some of you may have seen the internet discussion around the Chinese New Year on whether this is the Year of the Sheep, the Goat or the Ram. I think many of us have settled for the Goat. As one of my colleagues noted, goats are resilient and intelligent creatures; able to maintain their balance in the most precarious of places but yet, possess a calm and unexcited exterior with a beard that conveys a certain wisdom. So may I wish everyone all these fine qualities of the Goat.