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ASIA-PACIFIC FINANCIAL FORUM ROUNDTABLE ON FINANCIAL REGULATION

An Overview of APFF Work Related to Financial Regulatory issues Insurance and Retirement Income

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APFF Interim Report 12 Action Plans

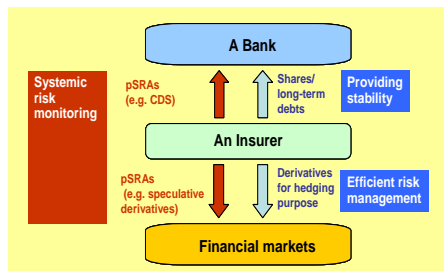
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- 1) A pathfinder initiative to develop **credit information sharing systems**
- 2) A pathfinder initiative to improve the **legal and institutional architecture** for security interest creation, perfection and enforcement and related workshops
- 3) Dialogues on regulatory issues in **trade and supply chain finance**
- 4) Workshops on emerging facilitators of **trade and supply chain finance**
- 5) A pathfinder initiative to develop **classic repo markets**
- 6) Workshops to develop strategies to improve legal and documentation infrastructure for the development of **OTC derivative market**
- 7) Self-assessment templates on **information for capital market investors**
- 8) **ARFP (Asian Region Funds Passport) support initiative**
- 9) Workshop series to develop an enabling **Asia-Pacific securities investment ecosystem**
- 10) **Dialogue series on regulation and accounting issues impacting the long-term business of the insurance industry in Asia Pacific economies and longevity solutions**
- 11) **Collaboration with APEC Finance Ministers' Process in promoting long-term investment, including infrastructure**
- 12) Conference and workshop series on **linkages on structural issues**

Regulatory issues Bank-centric regulations

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- **Unintended consequences might occur if banking regulations were copied for insurers**
 - Insurers play an important role as **long term investors** and in the **social security system**
 - **Diversity** needed to support a sound development of the environment



(Photo – Sydney, Australia)

(Note:pSRAs = potentially systemically risky activities)

Regulatory issues Short-term oriented economic regime

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- **Economic-based regime should have a long-term vision**
- **If a short-term-minded economic regime were implemented**
 - **Significant volatility** for long term products
 - Driven to transfer risks over to customers
 - Refrain from investing in non-fixed income assets



(Photo – Santiago, Chile)

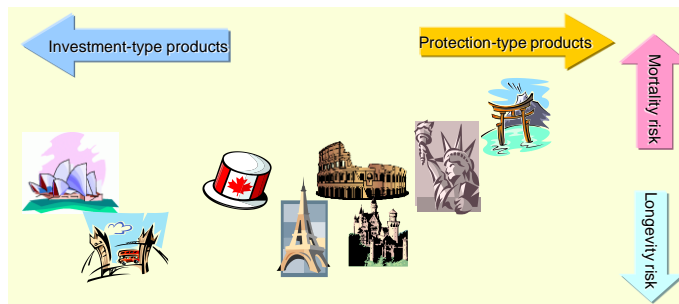


(Photo – USJ, Osaka, Japan)

Regulatory issues "One-size-fits-all" models

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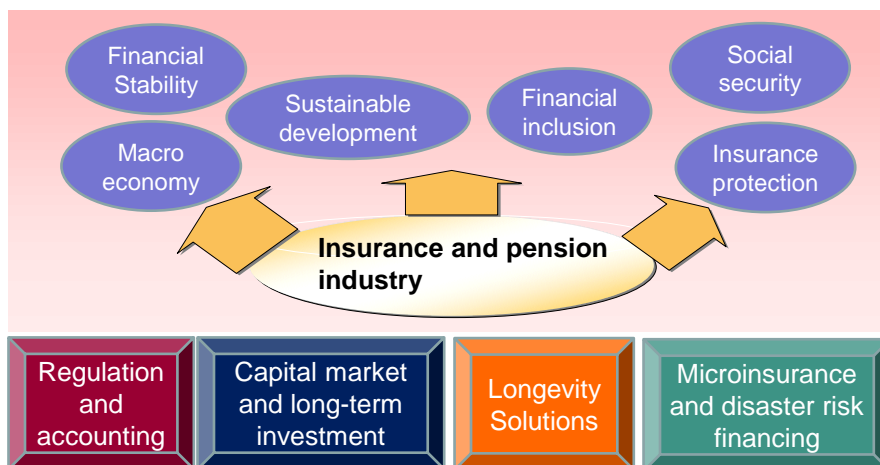
- **"One-size-fits-all" models would not work**
- **Different business models and existing regulatory framework**
 - the application of prescriptive international standards would not ensure the overall comparability or level playing field in the region



APFF Insurance and Retirement Income Work Stream

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- A holistic framework to support the long-term roles of insurance and pension industry in the Asia-Pacific



Asia Pacific Financial Forum (APFF) Insurance and Retirement Income Work Stream

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For more details on the APFF, visit mackglobe.com
or email Makoto Okubo, Nippon Life (m-okubo@nliinter.com)

APPENDIX

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You can find **APFF Interim Report to the APEC Finance Ministers** here:

- Executive Summary
<https://www.abaconline.org/v4/download.php?ContentID=22611923>
- Full report
<https://www.abaconline.org/v4/download.php?ContentID=22611921>
- **E. Insurance and Retirement Income** (see page 56-62)
- Annex H: Constrains on Promoting Long-Term Investment in the Asia-Pacific
<https://www.abaconline.org/v4/download.php?ContentID=22611898>
- **High-level issues and recommendations** (regulatory, accounting, market and operational issues) as a basis for discussion with policymakers and regulators

Constraints and recommendations

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Bank-centric regulations

- **Bank-oriented regulations may negatively impact on insurers' role to provide long-term investments and stabilize the financial system**
 - Insurance regulations should take into account **the specific nature of the insurance business** and
 - should not apply regulations which are targeted for bank deposits and other financial products **with short-term liquidity needs**
- **High risk charges for long-term investment, including infrastructure projects and equities, may discourage insurers and pension funds to provide such investments**
 - Avoid bank-centric capital-weighted rules and
 - consider **the characteristics of long-term assets supporting long-term liabilities** as well as
 - the effect of **asset diversification**

Constraints and recommendations

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Bank-centric regulations (Cont.)

- **Capital constraints on traditional long-term products may drive the companies to shift to short-term investment products**
 - Capital charges should be looked into, for the companies to have incentives to promote long-term products, taking into account the interaction between long-term assets and liabilities
- **Bank-oriented regulations with focus on systemic risk and interconnectedness may dis-incentivize insurers to stabilize the financial system and market, rather than mitigate systemic risks**
 - Regulatory framework should holistically promote the role of insurers and pension funds to support macro-economy, sustainable development, social security and long-term insurance protection, and
 - pay due care to the issue of **pro-cyclicality**

Constraints and recommendations

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Bank-centric regulations (Cont.)

- **It may affect negatively on the equity and long-term debt instruments and efficient risk management tools, such as hedging instruments**
 - Regulations should be in designed in a way to promote and incentivize the insurers' and pension providers' role to stabilize the financial system and market and its ability to manage risk efficiently

Constraints and recommendations

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Short-term oriented economic regime

- **Economic valuation may produce significant volatility for long-term business, which may not be relevant to the insurers' capacity to meet long-term obligations**
 - Economic based regime should have a long-term vision
 - **Avoid replacing the existing regulatory regimes** simply with a regime based on an economic based regulations
- **If such regime is used for regulatory interventions, insurers with no concern in solvency positions for the foreseeable future may be forced to take remedial actions, including the exit from long-term business and investments, in response to short-term fluctuations in financial markets**
 - Avoid the introduction of a regulatory regime which would require **immediate regulatory actions in response to short-term market fluctuations**

Constraints and recommendations

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Short-term oriented economic regime (*cont.*)

- **Short-term oriented regimes tend to capture the risk assessment with a snapshot and consider long-term business and investments excessive risk taking**
 - Long-term nature of the business model and illiquid nature of liabilities should be properly taking into account when designing the regulatory regime
- **Short-term oriented economic solvency regimes may incentivize insurers to transfer risks to customers, shift away from long-term protection business and investments, and discourage them from investing assets other than fixed income assets**
 - Measures should be taken to mitigate impact on long-term protection business and the assets supporting such contracts

Constraints and recommendations

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"One-size-fits-all" models

- **Adoption of "one-size-fits-all" regulatory models would not capture the diversity that exists in the region and may produce unexpected negative consequences for insurance/capital markets, and social security system**
 - Consider an approach to start from the regulatory framework in each jurisdiction, evolved and tested on its characteristics and harmonize those regimes from a unified point of view
- **A model based on one jurisdiction may not meet the regulatory objectives in other jurisdictions**
 - Consider the use of the different valuation approaches for different purposes
 - The use of existing regulatory regime in each economy may be an option

Constraints and recommendations

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"One-size-fits-all" models (*cont.*)

- **Due to the difference in business models and existing regulatory framework, the application of prescriptive international standards would not ensure the overall comparability or level playing field in the region**
 - International standards should be principle-based and aim to achieve the comparable outcome by taking into account the diversity in the region

Accounting issues

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- **Volatility in the balance sheet**
 - Short-term fluctuation should be avoided
 - Assets-liabilities interaction should be reflected for a wide range of products sold in the region
 - Discount rate should reflect the business model
- **Volatility in the income statement**
 - The (optional) use of OCI for insurance liabilities and corresponding assets
- **The proposed IFRS contains other significant issues for traditional long-duration products**
 - Complexity
 - Consistency
 - Transition requirements
 - Presentation

Market and operational Issues

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Market issues

- Underdeveloped long-term capital market
- Small number of bankable projects available
- Lack of infrastructure financial instruments
- Lack of market instruments (i.e. derivative, hedging tools) to manage portfolio risk
- Constraints on long-term insurance business (both demand side and supply side)

Operational issues

- Weakness in credit rating
- Lack of experience
- Uncertainty in legal framework (i.e. creditors rights, resolution)

*Collaboration with
Capital market/FMI/PPP
work is the key*

Longevity solutions

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- The work on longevity solution will focus on addressing demand- and supply-side issues in the development of lifetime retirement income solutions

Figure: Interrelated Issues in Providing Lifetime Retirement Security

