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FINANCIAL SECTOR ASSESSMENT PROGRAM

TECHNICAL NOTE—INSURANCE REGULATION AND SUPERVISION

This Technical Note on Insurance Regulation and Supervision for the Switzerland FSAP was prepared by a staff team of the International Monetary Fund as background documentation for the periodic consultation with the member country. It is based on the information available at the time it was completed in May 2019.

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June 12, 2019

TECHNICAL NOTE

INSURANCE REGULATION AND SUPERVISION

Prepared By
Monetary and Capital Markets Department

This Technical Note was prepared by IMF staff in the context of the Financial Sector Assessment Program in Switzerland. It contains technical analysis and detailed information underpinning the FSAP's findings and recommendations. Further information on the FSAP can be found at http://www.imf.org/external/np/fsap/fssa.aspx

CONTENTS

Glossary

EC	European Commission
EFK	Swiss Federal Audit Office ("Eidgenössische Finanzkontrolle")
EIOPA	European Insurance and Occupational Pension Authority
EU	European Union
FDF	Federal Department of Finance ("Eidgenössisches Finanzdepartement")
FINMA	Swiss Financial Market Supervisory Authority
FINMASA	Financial Market Supervisory Authority Act 2007
FOPH	Federal Office of Public Health ("Bundesamt für Gesundheit")
FSAP	Financial Sector Assessment Program
G-SIB	Global Systemically Important Bank
G-SII	Global Systemically Important Insurer
IAIS	International Association of Insurance Supervisors
ICP	Insurance Core Principle
IGT	Intra-Group Transaction
ISA	Insurance Supervision Act ("Versicherungsaufsichtsgesetz")
ISO	Insurance Supervision Ordinance ("Aufsichtsverordnung")
MMoU	Multilateral Memorandum of Understanding
OAK BV	Occupational Pension Supervisory Commission ("Oberaufsichtskommission Berufliche Vorsorge")
ORSA	Own Risk and Solvency Assessment
SIF	State Secretariat for International Finance
SST	Swiss Solvency Test
UFR	Ultimate Forward Rate
UL	Unit- and Index-linked Life Insurance

EXECUTIVE SUMMARY

Switzerland's regulatory framework for the insurance sector is highly sophisticated, but oversight of operational risk management and conduct regulation should be strengthened. Switzerland has one of the most developed insurance markets in the world, and is home to some large, internationally active insurance groups. The highly sophisticated regulatory framework, centering around the Swiss Solvency Test (SST), has contributed to better risk management practices in the insurance sector, and the supervisory approach of FINMA is forward-looking and risk-based. Nevertheless, the FSAP recommends laying down more SST features in binding ordinances and monitoring operational risks more closely. Furthermore, FINMA should be equipped with more legal powers and resources for the supervision of business conduct, anticipating new legislation foreseeing more stringent supervision of insurance intermediaries, and a specific resolution regime for insurance companies should be established.

The Swiss insurance market is large and well developed, with one of the highest penetration and expenditure-per-capita ratios in the world. Switzerland is home to large internationally active insurance groups, including one of the two largest reinsurers in the world. Accordingly, the share of domestic business for the two largest Swiss groups is only very minor. In 2017, gross premium income amounted to CHF 130 billion. The sector has accumulated almost CHF 700 billion in balance sheet assets (104 percent of GDP), with the life insurance sector being the largest segment, accounting for 51 percent of total assets. Almost 40 percent of insurers' assets are invested in sovereign and corporate bonds, but also (mostly domestic) real estate accounts for a sizable portion of 8 percent.

The prolonged low-yield environment remains challenging for insurers although business models were adapted earlier than in other European countries. Low interest rates pose a drain on life insurers' profitability, in particular on those with larger legacy business carrying high interest rate guarantees. Swiss insurers have reacted by reducing the volume of guaranteed business, focusing more on protection products and products with low or even no guarantees attached. Furthermore, the regulatory framework, in particular, the design and early implementation of the SST, based on market-consistent valuation, has contributed to a closer match of assets and liabilities, which has reduced interest rate sensitivities. Non-life insurers, which are less affected by the low-yield environment, record fairly comfortable profits. Solvency ratios have improved both in the life and the non-life sector since 2014/15, standing on average at about 180 and 230 percent, respectively.

The regulatory framework is robust and the solvency regime is one of the most developed in the world. The SST, in place since 2011, provides a robust solvency regime for the insurance sector, and has contributed to a proliferation of modern risk management practices across the sector. While originally the SST relied a lot on insurance companies developing their own internal models for calculating their capital requirements, a revision of the Insurance Supervision Ordinance (ISO) in 2015 led to a promotion of standard models which were subsequently developed by FINMA in consultation with the insurance sector. As a result, only few large (or complex) companies now use an internal model.

Some shortcomings exist in conduct regulation where a new law is expected to strengthen the legal framework and policyholder protection. The 2014 FSAP found that while laws clearly stipulated the intention to protect policyholders and entrusted FINMA to intervene on behalf of the policyholders and their beneficiaries, Switzerland had yet to articulate specific rules on business conduct. It was further noted that supervision of tied agents was only indirectly performed through insurers, and there were no on-going reporting requirements for intermediaries. So far, only marginal improvements have been made: a revision of the Insurance Supervision Act is being consulted during winter 2018/19 but will not enter into force before 2021 or 2022. The draft act foresees a more stringent supervision of insurance intermediaries, more transparency towards policyholders, and also adds a specific restructuring law for insurance companies.

While FINMA is the main supervisory body for the insurance sector, further authorities are in charge of supervising specific types of insurers and providers of retirement provisions. Basic (mandatory) health insurers are supervised by the Federal Office of Public Health (FOPH). Undertakings providing both basic and supplementary health insurance in one single legal entity are supervised by the FOPH (for the mandatory health insurance) and FINMA (for the supplementary health insurance). In such cases of shared duties, FOPH supervises the institute, including its solvency position, while FINMA supervises the supplementary health products only. Cantonal authorities supervise small cantonal building insurers.

FINMA is exercising its insurance supervision powers diligently, but more frequent audits on operational effectiveness could support accountability, and more binding requirements are needed. FINMA has strengthened its supervision of internal control mechanisms and requests insurers to perform an annual Own Risk and Solvency Assessment (ORSA). Newly set-up teams dedicated for onsite inspections, will further bundle expertise. In the development of the SST, FINMA uses non-binding circulars and guidelines to specify high-level principles enshrined in laws. While insurance undertakings generally adhere to these non-binding instruments, more SST features should be laid down in binding Ordinances. The previous wide-spread use of internal models had caused some concerns about legal certainty; increasing standardization of the solvency regime has alleviated those concerns. FINMA's annual accounts are audited by the Federal Audit Office; audits of FINMA's operational effectiveness would further enhance accountability.

Table 1. Switzerland: Main Recommendations on Insurance Regulation and Supervision

#	Recommendations and Responsible Authorities	Timing*	Priority**
1	Lay down more key SST features in legally binding Ordinances, and make insurance regulation more transparent (FDF, FINMA). ¶10	ST	H
2	Systematically collect relevant information on exposures towards the banking sector, in particular with regard to contingent convertible bonds (FINMA). ¶109	ST	H
3	Require that basic mandatory health insurance and supplementary health insurance are provided by two separate legal entities (FDF, FINMA). ¶22	ST	M
4	Use aggregated ORSA findings as input for macroprudential surveillance (FINMA). ¶108	ST	M
5	Strengthen regulation of business conduct, create corresponding competences for supervision by FINMA, and allocate sufficient resources to this task (Government). ¶87	ST	M
6	Intensify the analysis of group-specific risks, including liquidity risks and the fungibility of capital (FINMA). ¶95	ST	M
7	Increase the frequency of assessments of FINMA's operational effectiveness by the Federal Audit Office (Federal Audit Office). ¶21	MT	M
8	Intensify further the technical cooperation between FINMA and the FOPH (FINMA, FOPH). ¶23	C	L
9	Strengthen the analytical framework for assessing operational risks, and prescribe capital add-ons if needed (FINMA). ¶99	ST	L

* C = Continuous; I = Immediate (within one year); ST = Short Term (within 1–3 years); MT = Medium Term (within 3–5 years).

** H = High; M = Medium; L = Low.

INTRODUCTION

1. **This technical note analyzes the key aspects of the regulatory and supervisory regime for insurance companies in the Switzerland.**[1] The analysis is part of the 2019 Financial Sector Assessment Program (FSAP) and based on the regulatory framework in place and the supervisory practices employed as of November 2018. This note is based on a review of regulations, market analyses, and meetings with the Swiss authorities. The FSAP team also met with representatives from insurers, industry associations, and other private bodies.

2. **The note does not include a detailed assessment of observance of the Insurance Core Principles.** This technical note refers to the Insurance Core Principles (ICPs) issued by the International Association of Insurance Supervisors (IAIS) in October 2011, as revised most recently in November 2017. The ICPs selected for review are broadly those with macrofinancial relevance and with material regulatory changes. They include the ICPs on solvency requirements (valuation and capital adequacy), risk management (including reinsurance), business conduct (including insurance intermediaries), supervisory approach (including supervisory authority, supervisory review, macroprudential surveillance), as well as group supervision and cross-border cooperation. In respect to the 15 ICPs analyzed in the note, the authorities provided a full self-assessment, supported by anonymized examples of actual supervisory practices and assessments. The most recent detailed assessment, conducted on the basis of the 2011 version of the ICPs (as amended in 2012), was carried out in 2013.

3. **The note further updates on recent developments and risks to the Swiss insurance sector.** The sector is large and well developed, but is also undergoing a consolidation. This trend is driven, inter alia, by the continuing low interest rate environment which poses a major challenge for the life insurance sector. A separate technical note summarizes the results of the stress tests carried out on the insurance sector and elaborates more on current market risk sensitivities.

4. **The FSAP mission team is grateful to the authorities and private sector participants for their excellent cooperation.** The note draws on extensive discussions in Switzerland. Meetings were held with the Swiss Financial Market Supervisory Authority (FINMA), which also shared examples of actual supervisory practices and assessments, a selection of insurance companies and industry and professional bodies. The author is grateful to the authorities and private sector participants for their cooperation. The work benefitted greatly from their readiness to discuss issues and share information.

[1] The main author of this note is Timo Broszeit, independent expert on insurance regulation. Jane Anvari and Olya Kroytor (both IMF Legal Department) contributed on the proposed framework for insurance resolution.

REGULATORY AND MARKET STRUCTURE

A. Regulatory Structure

5. **The Financial Market Supervisory Authority Act of 22 June 2007 (FINMASA) serves as an umbrella law for sector-specific laws governing financial market regulation and supervision.** In addition to setting organizational parameters for FINMA as an institution including its liability, the FINMASA, together with two related Ordinances, defines principles for the regulation of financial market, as well as a set of harmonized supervisory instruments and sanctions. Eight sector-specific federal acts complement the FINMASA:

- Mortgage Bond Act of 25 June 1930;
- Federal Act on Contracts of Insurance of 2 April 1908;
- Collective Investments Act of 23 June 2006;
- Banking Act of 8 November 1934;
- Stock Market Act of 24 March 1995;
- Anti-Money Laundering Act of 10 October 1997;
- Insurance Supervision Act of 17 December 2004; and
- Financial Market Infrastructure Act of 19 June 2015.

6. **The statutory framework for the regulation and supervision of private insurance business is provided both by the FINMASA and the Insurance Supervision Act (ISA).** Whereas the FINMASA confers on FINMA the responsibility for insurance supervision in accordance with the ISA, and provides FINMA with the necessary supervisory powers and instruments, the ISA sets out the regulatory rules on the insurance business. The ISA thus defines the insurance-specific regulation, complementing the regulations defined in the FINMASA. The ISA lays down the general principles with regard to subject, purpose and scope of regulation and supervision, and contains provisions for the commencement, exercise and termination of insurance activities. There are also specific rules on ongoing supervision, safeguarding measures, cooperation and procedures, and sanctions, as well as regulations applying to individual lines of insurance. Finally, there are special rules for the supervision of insurance groups and insurance conglomerates.

7. **Statutory ordinances issued by the Federal Council, the executive branch of government, and by FINMA implement the Financial Market Acts on a second and third level.** Under the ISA, the specification of many of the details of insurance regulation is delegated by the Federal Parliament to the Federal Council (i.e., the executive branch of government). The Federal Council's Ordinance on the Supervision of Private Insurance Companies (ISO) elaborates in more detail on the provisions of ISA. The ISO also delegates some rule-making powers to FINMA who has enacted an Ordinance on the Supervision of Private Insurance Companies (FINMA-ISO).

8. **Circulars issued by FINMA provide further guidance on FINMA's interpretation and practical implementation of relevant financial market legislation.** They provide substance to the intention of the legislator as conveyed in acts and ordinances. These circulars address, inter alia, solvency, reserves and the investment of tied assets, governance and risk management, the position of the responsible actuary, the internal audit function and the external auditors, group supervision, and reporting. In the development of the SST, FINMA has specified a large number of technical details via circulars and guidelines, which are per se not binding in legal terms, but codify FINMA's interpretations of the law. FINMA may thus take enforcement actions in case of non-compliance. While in the past the wide-spread use of internal models had caused some concerns about legal certainty, the increased level of standardization in the solvency regime has alleviated those concerns.

9. **FINMA is the integrated supervisory authority for the Swiss Financial Market.** FINMA supervises banks, insurance companies, stock exchanges and securities dealers as well as other financial intermediaries according to FINMASA as an umbrella-law, and the sector-specific financial market acts. Where necessary, FINMA conducts financial restructuring and bankruptcy proceedings. FINMA is also responsible for preventing money-laundering and terrorist financing in the financial sector. In addition, it has supervisory powers with respect to holdings of participations and is the complaints body for decisions of the Takeover Board relating to public takeover bids for listed companies.

Recommendations

10. **More key SST features should be laid down in legally binding Ordinances, and transparency of insurance regulation should be improved**. FINMA is reviewing whether more key features of the SST should be enshrined in binding Ordinances instead of non-binding Circulars. The FSAP welcomes this initiative. While market participants generally adhere to FINMA Circulars, binding Ordinances would better serve legal certainty and enforcement. This applies particularly to key features such as the level of safety for the target capital. Elevated legal instruments should be supported by robust internal decision-making processes and clear communications with the industry and policyholders, clarifying how FINMA Ordinances comply with high-level principles enshrined in the ISA and the ISO. The Federal Council and FINMA should further improve transparency vis-à-vis the industry and other stakeholders (e.g. policyholders) by explaining in more detail the rationale of each insurance regulatory measure.

B. The Supervisory Authority

11. **FINMA is an independent institution, being accountable to and subject to the overall supervision of the Federal Parliament and Government.** However, this supervision is not interfering into concrete supervisory actions but is limited to checking if FINMA is correctly functioning and administering its resources. FINMA is financed by fees received from the supervised institutions such as banks or insurance companies. FINMA's annual accounts are audited by the Federal Audit Office, but there are no regular assessments of the supervisory effectiveness by that institution.

12. **It is possible to appeal against rulings issued by FINMA to the Federal Administrative Court.** Against the decisions of the Federal Administrative Court appeals are available to the Federal Supreme Court for a number of counts.

13. **FINMA has a two-tier board structure.** The Management Board, headed by a Chief Executive Officer (CEO), has operational responsibility for FINMA, whereas the Board of Directors has oversight responsibility. This structure is designed to allow efficient decision making, while ensuring proper checks and balances and oversight. FINMA has an internal audit function whose role and responsibilities are defined in an Audit Charter. The Audit Charter guarantees the full independence of the audit function in carrying out its duties.

14. **The Federal Council appoints the Board of Directors including the Chair and the Vice-Chair, and determines the level of remuneration.** The Board of Directors has to comprise seven to nine expert members, who are independent of the supervised persons and entities. The Board of Directors is appointed for a term of office of four years; each member may be reappointed twice. The Federal Council removes members of the Board of Directors "if the requirements for holding office are no longer fulfilled" (Art. 9 paragraph 5 FINMASA).

15. **The CEO and members of the Management Board are appointed by the Board of Directors.** The appointment of the CEO is subject to approval by the Federal Council. Consequently, the Federal Council has to approve the decision of the Board of Directors to terminate the employment of the CEO "if the requirements for holding office are no longer fulfilled" (Art. 9 paragraph 5 FINMASA). Moreover, the ordinance on FINMA staff states that the termination of an employment contract must have objective grounds which have to be communicated to the person concerned in writing.

16. **FINMA staff are not personally and directly liable in civil law for discharging their duties.** Article 19 FINMASA determines that FINMA is liable if: a) its management bodies or its staff have committed a breach of fundamental duties; and b) loss or damage is not due to a breach of duty by a supervised person or entity. A breach of fundamental duties might have occurred if measures were taken in bad faith. FINMA therefore benefits from appropriate protection from being held liable for supervisory measures in good faith. Under criminal law, FINMA bears the expenses of a criminal procedure if a staff member acts in good faith. For a criminal procedure against staff of FINMA the criminal prosecutor needs an authorization of the Federal Department of Justice and Police.

17. **FINMA can appoint third-party agents or mandataries to assist it in performing its duties—a practice far less common in insurance supervision than in banking supervision.** Agents and mandataries are an essential element in FINMA's repertoire of tools, giving the authority swift and flexible access to external experts when needed and enabling complex audits or investigations to be completed within a reasonable time. Agents can be deployed in every area of FINMA's work. In terms of supervisory tasks, the types of agent or mandatary may include the following:

- Mandated auditors: Mandated auditors conduct audits on FINMA's behalf as part of ongoing supervision of a supervised institution. They are used, for example, in response to special or institution-specific events if particular expert knowledge is required, or there are doubts about the quality of the audit conducted by the audit firm.

- Investigating agents: Investigating agents clarify circumstances relevant to enforcement proceedings or monitor the implementation of supervisory measures ordered by FINMA. In individual cases, they may be empowered to act in place of the intermediary's executive bodies.

18. To ensure that an agent or mandatary can be deployed swiftly on matters of urgency, FINMA maintains a list of suitable candidates. They must have knowledge and experience of mandates in the specific field, as well as an appropriate infrastructure. The selection criteria include the nature and scope of the mandate, specialist expertise and experience, language skills, costs and availability at the time. If no suitable candidate is available, FINMA may also select from outside its list. Agents and mandataries must in all cases be independent of the supervised institution concerned. Mandataries are obliged to fulfil their mandates diligently and cost effectively. FINMA defines the content and the expected costs of the mandate at the outset. It also monitors discharge of the mandate on an ongoing basis and checks that costs remain proportionate. The costs of agents and mandataries are borne by the supervised institutions concerned.

19. In its Insurance Supervision Division, FINMA employs about 100 staff, which are considered adequately skilled by market participants. The Insurance Division of FINMA has adequate resources to perform its supervisory duties, including offsite monitoring and onsite inspections. The Insurance Division has about 100 full-time equivalents for this purpose, being structured as follows:

- Regular supervisory teams:
  - Two teams for smaller and medium-sized insurance companies (supervisory categories 4 and 5),[2]
  - One team for large insurance firms in supervisory category 3,
  - One team for groups and their insurance entities, and
  - One team each for Zurich Insurance Group and for Swiss Re Group.
- Two specialized supervisory teams for onsite inspections, and more intensive supervision.
- Specialized teams to support the supervisory teams:
  - Qualitative risk management,
  - Quantitative risk management and Swiss Solvency Test (insurance risks and financial risks), and
  - Actuarial office.

[2] See paragraph 89 for a more information on the supervisory categories.

- Division operating office (including legal expertise and authorizations).

The Insurance division can also:

- Ask for cross-functional expertise on accounting and money laundering aspects; or
- Task the Enforcement and Recovery and Resolution divisions with certain activities to help it with investigations and the implementation of supervisory measures.

20. While FINMA is the main supervisory body for the insurance sector, further authorities are in charge of supervising specific types of insurers and providers of retirement provisions. Basic (mandatory) health insurers are supervised by the FOPH. Undertakings providing both basic (mandatory) and supplementary health insurance in one single legal entity are supervised by the FOPH (supervision of the mandatory health insurance) and FINMA (supervision of the supplementary health insurance). In such cases of shared supervisory duties, FOPH is competent for the supervision of the institute, including the solvency position, whereby FINMA is competent for the supervision of the supplementary health products only. In those cases where one legal entity provides both types of health insurance could, conflicts of interest among supervisors in times of financial distress can potentially arise as policyholder interests in both schemes might differ.[3] Cantonal small building insurers are supervised by cantonal authorities. More importantly, the occupational pension fund sector, comprised of nearly 1,700 rather heterogenous entities, managing close to CHF 1 trillion (149 percent of GDP), does not fall under FINMA's supervision. Instead, it is supervised by a two-tier structure of eight cantonal authorities and a federal body which directly supervises certain entities, and exercises an indirect supervision of the sector by auditing the cantonal authorities.

Recommendations

21. The Federal Audit Office should increase the frequency of assessments of FINMA's operational effectiveness. Regular assessments of FINMA's operational effectiveness, while fully respecting its independence in individual supervisory cases, could further strengthen FINMA as an institution. The Federal Audit Office, which is already auditing FINMA's financial statements, would be a suitable institution to do so, as they already conducted a similar (but slightly narrower) assessment in 2015 on the cooperation between the FOPH and FINMA in the supervision of health insurance companies.

22. The basic mandatory health insurance and supplementary health insurance should be provided by two separate legal entities. This would ensure a clear separation of responsibilities between FINMA and the FOPH, each authority being the competent supervisor for just one of the two companies. Such a mandatory separation would broadly reflect recent market developments as some companies have already restructured their health insurance business accordingly.

[3] E.g., in basic (mandatory) health insurance, it is easy to switch to another insurance company while in supplementary health insurance such a switch is typically subject to comprehensive health checks and could involve higher tariffs than under the previous policy.

23. The technical cooperation between FINMA and the FOPH should be intensified further. The information exchange between both authorities has improved since updating the legal basis in 2016. Further technical cooperation and common tools should be sought. This could be facilitated, e.g., by promoting temporary secondments of staff.

C. Market Structure

24. The Swiss insurance market is large and well developed, with one of the highest penetration and expenditure per capita ratios in the world. As of end-2017, there were 204 insurance and reinsurance companies licensed in Switzerland, down from 223 in 2013. Most of these companies (130) were non-life insurers, in addition there were 28 reinsurers, 27 captives, and 19 life insurers. With USD 6,811 per capita in 2017, Switzerland recorded the third highest insurance density in the world (behind the Cayman Islands and Hong Kong), according to Swiss Re data[4]. The insurance penetration (premiums as a percentage of GDP) reached 6.9 percent—the thirteenth highest in the world and the sixth highest in Europe (behind Finland, Denmark, United Kingdom, the Netherlands, and France). Switzerland is home to large internationally active insurance groups, including one of the two largest reinsurers in the world. Accordingly, the share of domestic business for the two largest groups is only very minor. The majority of the business is generated by tied agents, followed by brokers, while banks and post offices play a relatively minor role. Most insurers use a multiple distribution strategy (including direct offerings).

[4] Swiss Re (2018), World Insurance in 2017, sigma 3/2018.

Table 2. Switzerland: Number of Insurance Companies

The number of life and non-life insurers as well as of captives has been declining since 2013, while new companies enter still regularly, particularly in non-life.

Number of Insurers (year-end)

	2013	2014	2015	2016	2017
Life	23	21	20	19	19
Non-life	138	141	135	133	130
Reinsurance	28	29	30	30	28
Captives	34	33	29	25	27
Total	223	224	214	207	204

New Entries of Insurers

Life	0	1	0	0	0
Non-life	3	4	1	2	2
Reinsurance	2	2	1	0	2
Captives	0	0	1	1	2
Total	5	7	3	3	6

Exits of Insurers

Life	0	3	1	1	0
Non-life	3	1	7	4	5
Reinsurance	3	1	5	0	4
Captives	0	1	0	5	0
Total	6	6	13	10	9

Source: FINMA.

25. There has been a material decline in new individual life business over the last years, in particular with regard to traditional (guaranteed) life products. Compensating for this decline, hybrid products are offered which are partially unit-linked and partially classic long-term interest rate guarantees (currently with a maximum 0.05 percent for single premium and 0.25 percent for annual premium due to regulatory requirements). Furthermore, products with shorter-term guarantees and “capital light” products with internal equalization reserves have been introduced by some companies.

26. In group life business, insurers scaled back the available capacity in the full coverage insurance sector (“Vollversicherung”) and concentrated instead on reinsuring the risks of death and disability. Full coverage contracts are contracts in which the life insurer assumes full ownership of the capital investments, manages them and bears the investment risk as well as the longevity risk. The main products sold are still full insurance contracts, but new business acceptance is highly selective, and insurers are trying to grow in the business of semi-autonomous pension schemes with coverage for death and disability. Group life insurance contracts in Switzerland are relatively short term by statutory requirements which foresee a maximum term of five years.

Table 3. Switzerland: Premium Income

Health insurance and group life occupational pension schemes are by far the most important lines of business for non-life and life insurers, respectively.

Non-life: Gross premiums written (CHF million, 2017)

Health	10.675	38,6%
Fire/property	3.988	14,4%
Land vehicles (comprehensive)	3.309	12,0%
Accident	3.031	11,0%
Land vehicles (liability)	2.690	9,7%
Liability	1.976	7,1%
Legal expenses	618	2,2%
Financial losses	433	1,6%
Marine, aviation and transport	352	1,3%
Credit and surety	332	1,2%
Tourist assistance	244	0,9%
Total	27.648	100,0%

Life: Gross premiums written (CHF million, 2017)

Group life occupational pension schemes	22.399	71,0%
Classical individual capital insurance	4.240	13,4%
Unit-linked life insurance	1.664	5,3%
Classical individual annuity insurance	313	1,0%
Capitalization and tontines	258	0,8%
Life insurance linked to internal investment positions	198	0,6%
Other life insurance segments	497	1,6%
Health and casualty insurance	4	0,0%
Foreign branches	1.603	5,1%
Reinsurance accepted	368	1,2%
Total	31.544	100,0%

Source: FINMA.

27. **For private clients, the main non-life products are complementary health insurance, home insurance, motor insurance, liability insurance and accident insurance**, but a lot of other products cover almost every insurable niche. There is no approval on property& casualty tariffs and products (except certain health and accident products with a social security function). Natural catastrophe insurance (excl. earthquake) is mandatory together with fire in most cantons, and building insurance is a state monopoly in 19 of 26 cantons.

28. **Swiss reinsurers are typically very international and domestic business often accounts for less than 5 percent of total underwritten business.** In terms of specific products emerging, cyber risks might create business opportunities. Swiss reinsures are as their international peers active providing some capacity with rather small limits considering the uncertainties in pricing models.

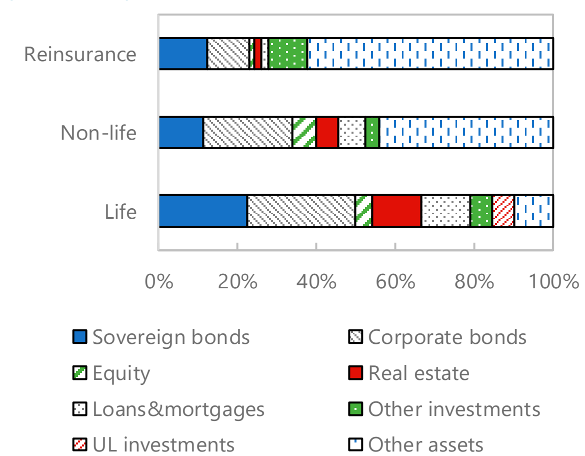
29. The sector has accumulated almost CHF 700 billion in balance sheet assets (104 percent of GDP), with the life insurance sector being the largest segment, accounting for 51 percent of total assets. Almost 40 percent of insurers' assets are invested in sovereign and corporate bonds, but also stocks and (mostly domestic) real estate account for sizable portions with 16 and 8 percent, respectively. As investment opportunities in Swiss francs are rather limited, the (primary) insurers' investment assets are more diversified in foreign currencies than the currency breakdown of liabilities would suggest. This mismatch is usually hedged with derivatives.

Figure 1. Switzerland: Asset Allocation in the Insurance Sector

Real estate and (mortgage) loans account for a substantial part of the asset mix, in particular for life insurers.

Asset Allocation

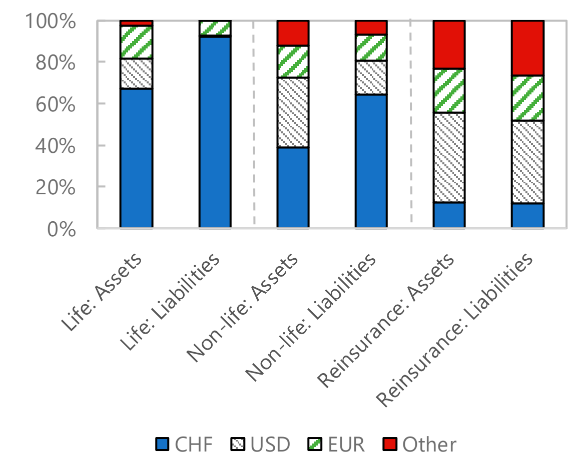
(End-2017)



Primary insurers diversify their assets more than their CHF concentrations on the liability side would suggest, while reinsurers are closely matched.

Currency Breakdown

(End-2017)



Source: IMF staff calculations based on FINMA data.

Notes: Reinsurance includes captives.

RISKS AND VULNERABILITIES

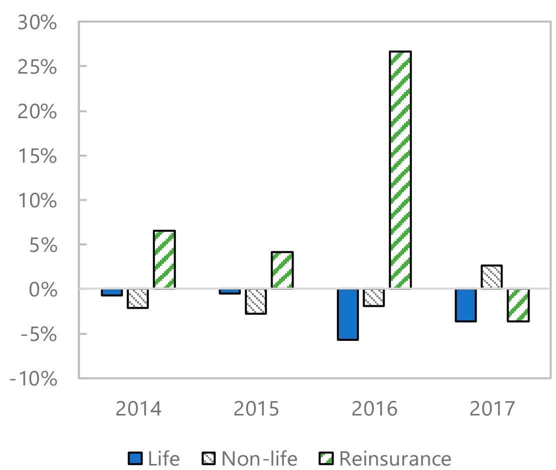
30. The prolonged low-yield environment is still challenging for insurers although business models were adapted earlier than in other European countries. Life insurance premiums have been declining in recent years, and low interest rates pose a drain on life insurers' profitability, in particular on those with larger legacy business carrying high interest rate guarantees. Investment yields came down from 3.3 percent in 2013/14 to 2.5 percent in 2017, and the return on equity averaged 8 percent over the last five years. In this environment, Swiss insurers have reacted by reducing the volume of guaranteed business, focusing more on protection products and products with low or even no guarantees attached. Furthermore, the regulatory framework, in particular the early implementation of the Swiss Solvency Test, has contributed to a closer match of assets and liabilities which has reduced interest rate sensitivities.

31. Non-life insurers, which are less affected by the low-yield environment, record fairly comfortable profits. Non-life premiums declined between 2014 and 2016. Nevertheless, combined ratios of primary non-life insurers were consistently below 90 percent over the last five years, and the return on equity averaged 17 percent. In the reinsurance sector, profits tended to be more volatile, but even in years with large natural catastrophes like 2017, with a very intense hurricane season, the sector on aggregate remained slightly profitable.

Figure 2. Switzerland: Profitability Indicators for the Insurance Sector

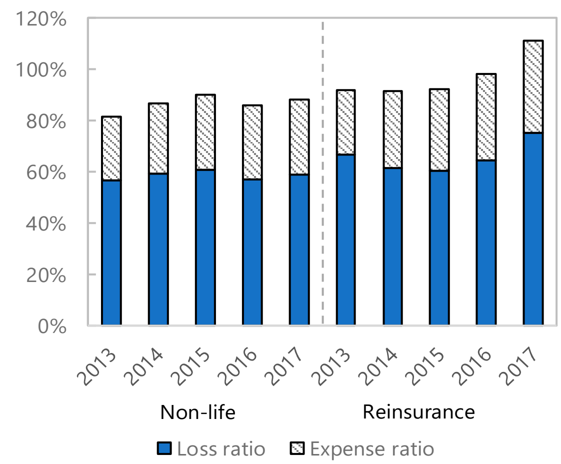
Life premiums remain pressurized while reinsurance premiums reflect the very volatile nature of that business on a global scale.

Change in Gross Written Premiums



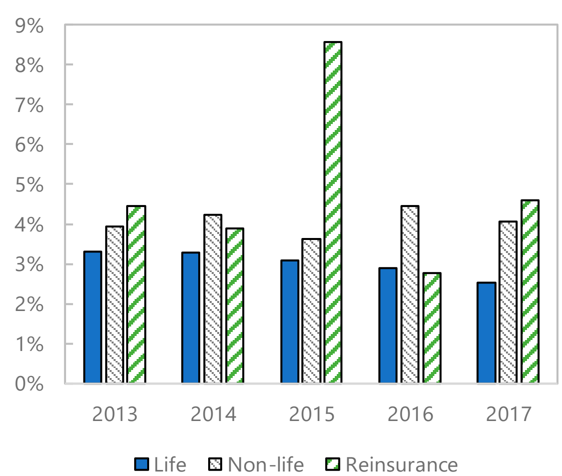
Combined ratios in the non-life sector are traditionally below 90 percent and can exceed 100 percent for reinsurers in years of large catastrophic losses.

Combined Ratio



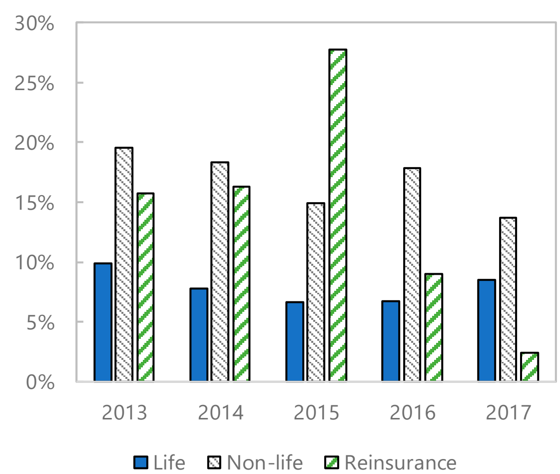
The investment yield in the life sector has been constantly declining in recent years…

Investment Yield



…contributing to a relatively low profitability as compared to the non-life sector.

Return on Equity



Source: IMF staff calculations based on FINMA data.

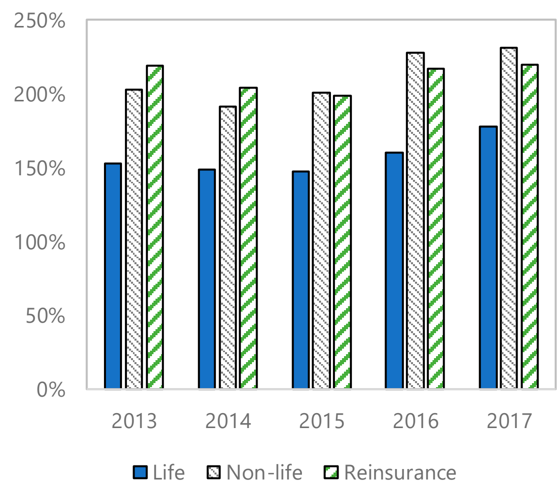
Notes: Reinsurance includes captives.

32. The Swiss insurance sector is well capitalized and solvent. Solvency ratios have improved both in the life and the non-life sector since 2014/15, standing on average at about 180 and 230 percent, respectively, which is well above the binding regulatory requirements.

Figure 3. Switzerland: Capitalization in the Insurance Sector

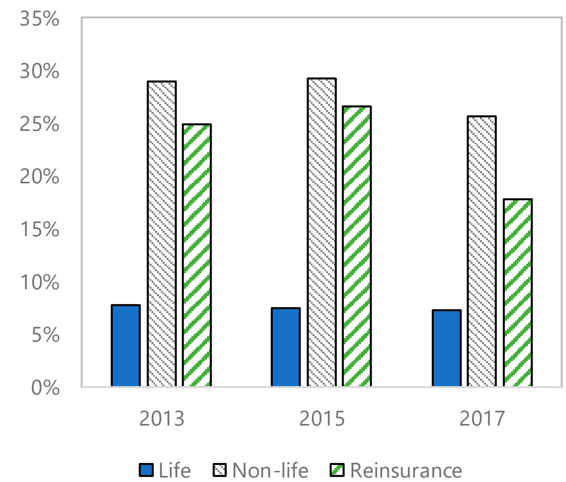
Solvency ratios (based on the Swiss Solvency Test) have improved since 2014/15 for all sectors…

Solvency Ratios



…while the pure balance sheet perspective reveals a slight increase of the leverage.

Capital and Reserves to Assets



Source: IMF staff calculations based on FINMA data.

Notes: Reinsurance includes captives.

INSURANCE REGULATION

33. The Swiss regulatory framework has been strengthened since the last FSAP. A major revision of the Insurance Supervision Ordinance (ISO) in 2015 has contributed to a more stringent regime, in particular with regard to a promotion of the standard model for calculating capital requirements, introduction of the Own Risk and Solvency Assessment (ORSA), better corporate governance, and enhanced public disclosure. The European Commission has recognized the Swiss insurance regulation and supervision system as equivalent with the Solvency II Directive in 2015.

A. Prudential Regulation

Valuation of Assets and Liabilities for General Accounting Purposes and for the SST

34. The valuation for prudential purposes (SST) and for general accounting purposes differ by the extent to which market-consistent values are used. While the SST uses a market-consistent valuation for all assets and liabilities, the basis for general accounting purposes is prudence with a view to presenting the economic position in such a manner that third parties can make a reliable assessment of the same. This can result in assets valued below and liabilities valued above market-consistent amounts. The valuation rules for tied assets, which may also be subsumed under prudential purposes, are also based on a prudent stance, i.e., upper bounds for valuations are established.

35. For general accounting purposes, valuation must be carried out prudently, but this must not prevent the reliable assessment of the economic position of the undertaking. If there are specific indications that assets have been overvalued or that provisions are too low, the values must be reviewed and adjusted if necessary. Assets and liabilities are normally valued individually, provided they are significant and not consolidated as a group for valuation purposes due to their similarity.

36. Generally, when first recorded as well as in any subsequent valuation, assets must be valued no higher than their acquisition or production costs. Loss in value due to usage or age must be taken into account through depreciation, while other losses in value must be taken into account through valuation adjustments. Depreciation and valuation adjustments must be applied in accordance with generally recognized accounting principles. They must be deducted directly or indirectly from the relevant assets and charged to the profit and loss account and may not be recognized as a liability.

37. In subsequent valuations, assets with a stock exchange price or other observable market price in an active market may be valued at that price, even if this price exceeds the nominal value or the acquisition value. Any company which exercises this right must value all assets in corresponding positions on the balance sheet that have an observable market price at the market price as of the balance sheet date. If assets are valued at the stock exchange price or market price as of the balance sheet date, a value adjustment to be charged to the profit and loss account may be recognized in order to take account of fluctuations in prices. Such valuation adjustments are not permitted, however, if they would result in both the acquisition value and the lower market value being undercut. For domestic insurance companies, the valuation of fixed-income and comparable structured instruments must not exceed the amortized cost value. If such an instrument is held in relation to business activities abroad, FINMA might permit the regulatory valuation method of the respective jurisdiction for that instrument. For investments related to unit-linked and similar contracts, the current market value must be used as the valuation. For derivative instruments, the valuation must be prudent and not exceed the market price. If no market price is available for such an instrument, then the valuation must not be higher than that of an acknowledged valuation model. Valuation adjustments must be considered if there is indication of an impairment of a financial instrument.

38. Liabilities must be valued at their nominal value. If past events lead to the expectation of a cash outflow in future financial years, the provisions probably required must be recognized and charged to the profit and loss account. Provisions may also be recognized in particular for regularly incurred expenditures from guarantee commitments, renovations to tangible fixed assets, restructuring and securing the long-term prosperity of the undertaking. Provisions that are no longer required need not be reversed.

39. Technical provisions, representing obligations due to insured parties, are calculated based on the corresponding business plans agreed with the regulator. ISA Art. 16 requires an insurer to hold sufficient technical provisions for the entire scope of business. ISO Art. 54 requires in the business plans the disclosure of the conditions for recognition and derecognition of technical provisions. Provisioning and valuation methods must be documented. Technical provisions which are no longer in use must be derecognized. In ISO Art. 54 reference is also made to FINMA's circulars with regard to the scope and extent of technical provisions. In FINMA Circular 2008/42 the core principle is to hold sufficient technical provisions, which means they must be equal to or higher than the market-consistent valuation of the insurance obligation. In FINMA Circular 2008/43 the core principle is to use assumptions and methods in determining the technical provisions in such a way that the provisions are sufficient to allow the fulfilment of the insurance obligations at any time.

40. For SST purposes, the valuation of assets has to be based on reliable market values whenever these are available. For assets that are difficult to value, FINMA can describe how to value them. A mix of mark-to-market and mark-to-model or a pure mark-to-model is possible. Valuation models for assets may only be used if they are accepted within the realm of financial mathematics, make use of—and are not in contradiction to—observable market data whenever possible and are tied to the internal processes of the undertaking. FINMA Circular 2017/3 furthermore determines that the valuation must take into account the most recent information gathered from trading in liquid and transparent markets. Valuation models must lead to arm's length prices. Finally, a model-based valuation of assets has to allow for default risk of the counterparty as well as other risks.

41. The valuation of insurance liabilities for SST purposes is based on their market-consistent value, which is defined as the sum of the best-estimate and the market value margin. The best-estimate of insurance liabilities is defined as the discounted value of the expected value of future, contractually agreed cashflows, applying a risk-free yield curve for discounting. Material options and guarantees included in the liabilities have to be taken into account, whereas benefits from future non-guaranteed bonuses as well as future company taxes are not to be taken into account. The value of said options has to be derived applying accepted methods from financial mathematics. Allowances for expected losses and claims incurred but not yet reported have to be made. According to the best-estimate-principle, the valuation should not include any explicit or implicit margins for prudence. The market value margin (MVM) is defined as the capital costs for the risk bearing capital which would have to be held during winding-up the current insurance liabilities.

42. For discounting liabilities, risk-free yield curves have to be used, and FINMA makes counterparty risk-free yield curves available in the most commonly used currencies (CHF, EUR, USD, and GBP) as at 1 January of every year. FINMA's risk-free yield curves currently are derived using an ultimate forward rate (UFR) to extrapolate the "long end" of the curves. While this is very similar to the approach taken under Solvency II, it is worth noting that for the currencies EUR, USD, and GBP the UFR used by FINMA is considerably lower (i.e., 30 basis points) than the respective UFRs chosen under Solvency II. As for the main currency CHF, the UFR equals 2.55 percent for the

SST 2018. FINMA has communicated to lower it by 15 basis points each year during at least the course of the next four years, so that it will reach 1.95 percent in 2022.

43. Between 2013 and 2015, FINMA had allowed temporary adjustments to be made to the yield curve for discounting liabilities during the then prevailing low interest rate phase. This possibility of adjustments was valid for a period of only three years, and for existing liabilities only: Starting in 2016, insurance companies had again to use unadjusted risk-free yield curves to value their liabilities, thus—in line with recommendations of the last FSAP—these temporary measures had been fully removed already in 2016.

44. Generally, the SST concept requires capital to be held to absorb uncertainty and/or volatility from any source rather than introducing margin requirements on specific positions: All inherent risks are reflected in the capital requirements. In order to determine the margin over current estimate and to achieve market-consistency, the SST is following a cost-of-capital-approach: the MVM thus reflects the capital costs, since all other costs are already part of the current estimate and all relevant risks are already reflected in the capital requirements. The MVM shall be such as to ensure that the value of the technical provisions is equivalent to the amount of capital that accepting insurance undertakings would be expected to require in order to take over and meet the insurance obligations. The MVM at a given point in time is calculated as the sum of the expected values at that point in time of the discounted capital costs (6 percent above the risk-free rate) of each one-year risk capital over the future one-year periods required by the insurance company to fulfil its insurance liabilities.[5]

45. The valuation of liabilities may not contain any allowance for own counterparty risk, with the sole exception of liabilities which are considered risk bearing in the risk-bearing capital (supplementary capital).

Valuation of Assets in the Tied Asset Regime

46. For the purpose of tied assets allocation, the valuation rule of tied assets as prescribed by FINMA Circular 2016/5 is to be understood as an upper bound. However lower values can be used for precautionary reasons. In terms of valuation, the valuation of tied assets can be generally differentiated among the following three patterns: assets valued at market value, assets valued at nominal value (with some corrections, where appropriate) and assets valued at amortized cost.

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[5] More specifically, each "one-year risk capital" is referring to the regulatory capital requirement under the SST over the whole period until final settlement of the insurance liabilities. Thus, the inherent risks in future years require in principle an SST calculation for each future year during the entire expected duration of fulfillment of the insurance liabilities, and an ancillary SST calculation is to be performed in order to determine the one-year SST risk capital, where the following assumptions are made: the insurance company does not write any new business; legally enforceable reductions in insurance benefits may be made; the assumptions regarding policyholder behavior and financial expenditures (including expenses) and other assumptions are realistic given the situation in question; and the insurance company follows a plan to fulfil its insurance liabilities.

47. Assets valued at market value:

- Money market debt claims can be valuated at most at their market value. If they are not exchange traded, a market standard valuation method should be used.
- Structured products are to be valuated as a whole at their market value.
- Securitizations can be valuated at most at their market value. The quality of the valuation e.g. with regard to the market liquidity has to be taken into account.
- Equity and convertible bonds with equity character can be valued at most at their market value.
- Real estate investments can be valued at most at market value. For direct investments, if audited market values according to IFRS, US-GAAP or Swiss-GAAP-FER exist, these have to be used. For determining the market value, the discounted cash flow method, the capitalized earning method, and the hedonic method are allowed. The principles of individual valuation and valuation continuity must be adhered to. Every ten years, the value of each property has to be approved by a real estate appraiser. For investments in real estate companies, the pro rata net asset value is considered as the market value.
- Alternative investments are valuated at most at market value.
- Derivatives are valued at most at market value. For exchange-traded derivatives, the market value is the traded exchange value. For OTC derivatives, the market value is the price at which an open contract can be unwound.
- Collective investment schemes can be valuated at most at their market value. If they are not listed, the collective investments can be valuated at their net asset value.

48. Assets valued at nominal value:

- Cash deposits, bank accounts and fixed term deposits can be valuated at most at their nominal value. The security and income need to be taken into account.
- "Other loans" can be valued at most at their nominal value after taking the recoverability into account.
- Mortgages are valued at most at nominal values.

49. Assets valued at amortized cost:

Bonds can be at most valued at amortized cost with accrued interest added. The linear cost amortization or the scientific cost amortization methods may be used.

Investments

50. **Primary insurers must ensure that the claims from the insurance contracts are covered by tied assets.** The tied asset regime is laid out in Art. 17 ISA. Furthermore, Art. 79 ISO defines the types of assets that may be allocated to the tied assets, such as cash, deposits and money market investments, bonds, structured products, securitizations, loans, equities, participation certificates, convertible bonds with equity character, domestic residential and commercial real estate, mortgages, alternative investments, derivatives, shares in collective investment schemes and single-investor funds. Reinsurance business from reinsurance or primary insurance companies is not subject to the tied assets regulation. The detailed allocation rules for tied assets, limits, valuation rules and further guidelines on each asset class are described in FINMA Circular 2016/5.

Capital Adequacy

51. **The capital adequacy regime in Switzerland is one of the most developed in the world.** The Swiss Solvency Test (SST), formally introduced in 2006 and fully applicable since 2011, provides a robust solvency regime for the insurance sector, and has contributed to a proliferation of modern risk management practices across the sector. It uses a total balance sheet approach to measure available capital ("risk-bearing capital" in SST terminology) at the measurement day, typically 1 January of a calendar year. Positions are valued market-consistently. The insurer's own credit standing cannot be taken into account in the valuation of its own insurance liabilities and own other liabilities. In order to provide a full economic picture, the SST has no concept of off-balance sheet positions. It therefore includes positions which would be termed "off balance sheet" in traditional accounting terminology, for example contingent assets and liabilities. Consequently, it ensures the provision of a full economic picture while excluding any corporation tax items consistent with its gone-concern perspective.

52. **While originally the SST relied a lot on insurance companies developing their own internal models for calculating their capital requirements, a revision of the ISO in 2015 led to a promotion of standard models** which were subsequently developed by FINMA in cooperation with the insurance sector. As a result, only a few large (and complex) companies now use an internal model.

53. **The risk-bearing capital is compared to the target capital which is a measure of the risk to which the insurer is exposed to during the next twelve months after the valuation day.** Risk is measured as the tail value at risk at 1 percent of the discounted change of the risk-bearing capital over a one-year period allowing for risk mitigating features of eligible risk-absorbing capital instruments. The risk types to be taken into account are, as a minimum, market risk, credit risk and insurance risk. If other risk types such as operational risks or concentration of risks are not properly reflected in an insurer's SST figures, then FINMA uses deductions from the risk-bearing capital or add-ons to the target capital.

54. In the SST, risk bearing capital is composed of two layers called core capital and complementary capital. Core capital is defined as market value of assets (*A*) minus market value of liabilities (*L*) plus the market value margin (*MVM*):

$$Core\ Capital = A - \left[L - \frac{MVM_1}{1 + r_{0,1}}\right] - Corrections,$$

Liabilities do not include own credit standing, i.e., it is assumed for the purpose of valuation that the insurer fulfills its financial obligations as they fall due. Subordinated debt is not part of core capital, therefore core capital is considered to absorb losses in a going-concern as well as in a winding-up situation. "Corrections" in the above formula refer to deductions of (a) foreseen dividend payments to shareholders, (b) own shares, (c) potential immaterial funds, and (d) deferred taxes for real estate in Switzerland.

55. Complementary capital consists of eligible risk-absorbing capital instruments, which include hybrid instruments, if they meet the following conditions:

- Instruments are paid-in;
- Instruments cannot be offset against other obligations;
- Subordination is contractually fixed and irrevocable;
- The insurer has the right to suspend interest payments;
- The notional debt and interest bear losses of the company without triggering the winding-up of the firm;
- Notional is not callable by the investor before the date of redemption, except in case of the liquidation of the insurer; and
- Redemption prior to maturity needs the approval of FINMA.

56. Insurers usually determine the SST figures net of reinsurance. The ISO allows the calculation net of reinsurance provided the risk-mitigating effects can be captured appropriately. In particular, the reinsurer's counterparty credit risk must be taken into account. Eligible guarantees are recognized as part of the market-consistent balance sheet at their current market-consistent price, which is usually considerably lower than the notional amount or the guaranteed sum. The risk-mitigating effect of guarantees might be captured in the target capital, subject to FINMA approval of the guarantee in question, and its appropriate modelling.

57. An insurer meets the solvency condition under the SST if the risk-bearing capital is at least equal to the target capital. The SST ratio is the ratio of the risk-bearing capital less the expected value of the discounted market value margin in the numerator, to the target capital less the expected value of the discounted market value margin in the denominator, if the latter is positive. If this term is not positive, no SST ratio can be reported. The SST ratio is also shown in the following formula:

$$SST\text{-}ratio = \frac{RBC_0 - \frac{MVM_1}{1 + r_{0,1}}}{TC - \frac{MVM_1}{1 + r_{0,1}}}$$

58. **Each insurer is required to submit an SST report on an annual basis to FINMA.** In addition, every insurer is required to determine and report the target capital and the risk bearing capital if its risk situation changes considerably.

59. **Supervisory intervention levels are defined as specific levels of the SST solvency ratio, corresponding to four zones in which an insurance company can find itself:**

- Green zone: the SST ratio exceeds the 100 percent threshold;
- Yellow zone: the SST ratio is between the 100 and 80 percent thresholds;
- Orange zone: the SST ratio is between the 80 and 33 percent thresholds; and
- Red zone: the SST ratio is below the 33 percent threshold.

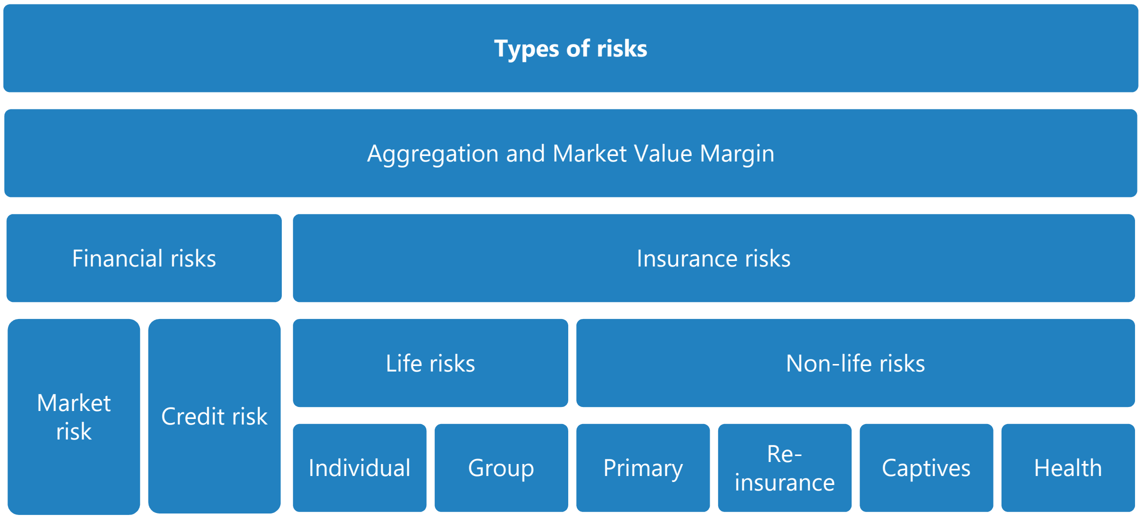
60. **If an insurance company is in the yellow or orange zone, the company draws up an action plan based on realistic assumptions and submits it to FINMA for approval** within two months of this being established. The action plan is designed such that, with a high probability,

- The company can reach the green zone from the yellow zone, normally within three years;
- The company can reach the yellow zone from the orange zone, normally within two years, and then reach the green zone, normally within another three years.

61. **If an insurance company is in the red zone, it must submit emergency measures to protect policyholders to FINMA for approval without delay.** It must be immediately transparent to FINMA whether the emergency measures will result in the company leaving the red zone within a short period of time. If the insurance company is unable to take emergency measures that are likely to be effective, and the measures ordered by FINMA under Article 51 ISA are not effective within a short period of time, FINMA will withdraw the license.

62. **In determining the target capital, an insurance company has to employ a risk model that reflects its relevant risks in a suitable manner.** Following the amendment of the ISO in 2015, there is a precedence for standard models, and FINMA is asked to provide various standard models that can be used as a modeling approach for reflecting the risk profile of most of the supervised entities, and which of the standard models an individual insurance company has to use. Standard models and their technical documentation are published on FINMA's website, and during the development, reviewing and refining of the standard models, FINMA consults with the insurance companies affected, either directly or indirectly via the relevant associations (e.g., the Swiss Insurance Association). The following standard models are currently in use:

Figure 4. Switzerland: Swiss Solvency Test Modules



Source: FINMA.

63. (Partial) internal models can be used to quantify the risk of an insurance company only if none of FINMA's standard models is appropriate to reflect its risk profile. Such internal models always have to be approved by FINMA. The definition of target capital does not distinguish between standard model and (partial) internal models. Therefore, the modeling criteria (risk measure, level of safety and time horizon) apply equally for (partial) internal models as for the standard model.

64. Following the amendment of the ISO in 2015, FINMA has redesigned its approval process of (partial) internal models. As a first step, FINMA now conducts a summary review, focusing primarily on whether the (partial) internal model sufficiently reflects the material risks, the completeness of the internal model documentation, and compliance with the qualitative and organizational requirements. FINMA may approve the internal model for which the application is made subject to collateral clauses, adjustments or deductions from the risk-bearing capital or add-ons to the target capital. The insurance company has to conduct a regular review of the SST model accepted by FINMA, in particular with regard to whether it still sufficiently reflects the risk situation. Summary reviews, once carried out, are subsequently complemented by so-called material reviews. In case of an approved internal model for which a summary review has already been carried out, FINMA may only compel an insurance company to replace such a model on the basis of a material review conducted by FINMA or a material change in circumstances.

65. The solvency of a Swiss domiciled insurance group is measured by the group SST. There are two approaches to determine group solvency for insurance groups under group supervision of FINMA:

- Consolidated group SST: The group is modelled under the assumption that the assets and liabilities of all group companies are consolidated in a single, fictional legal entity (consolidated entity), and the target capital (required capital) and risk-bearing capital (available capital) are determined for the consolidated entity. The solvency condition for the consolidated group SST is met if the consolidated risk-bearing capital is at least equal to the consolidated target capital.

- Granular group SST: The group is modelled as a network of granular entities with intra-group participations and intra-group transactions between them. A granular entity is a single legal entity of the group or a cluster in the form of a sub-consolidation of several legal entities within the group. The solvency condition for the granular group SST is met if it is satisfied by each granular entity.

Reinsurance

66. **Switzerland is an important reinsurance market, and FINMA comprehensively supervises both reinsurance business and the ceding of business to reinsurers.** The strategy for reinsurance ceded is filed as an element of the business plan. In the annual supervisory reporting most of the insurance elements in profit and loss account as well as balance sheet items (premiums, claims, technical provisions) are distinguished between gross and net of reinsurance/retrocession. FINMA Circular 2011/3 outlines that the technical provisions have to be determined before and after retrocession and a meaningful segmentation has to be applied. In the calculation of the target capital of the SST, reinsurance is fully considered but the resulting counterparty risk from reinsurance is separately covered in credit risk in the target capital. Furthermore, transparency is ensured in the annual SST report, where the exposure against reinsurers is included and discussed. While there is no explicit test for a certain amount of risk transfer, accounting principles applied in the statutory accounting often follow to the extent possible international accounting principles.

67. **Switzerland's supervisory regime is considered equivalent to Solvency II regarding the supervision of groups, reinsurance and solvency.** In addition, Switzerland is a qualified jurisdiction from the perspective of the U.S. National Association of Insurance Commissioners (NAIC) which facilitates the process for Swiss-based reinsurers to be a certified reinsurer benefitting from reduced collateral requirements (depending on the financial strength).

68. **FINMA does not have a mandate to directly supervise reinsurance branches of foreign reinsurers operating in Switzerland.** In such cases, supervision is conducted by the respective home supervisor. However, a reinsurance transaction conducted by such a branch with a primary insurance entity domiciled in Switzerland is subject to the same supervision as if the reinsurance is bought from a reinsurance company. The supervision of reinsurance branches is foreseen in the current exposure draft for in the upcoming ISA reform.

Insurance Groups

69. **FINMA has no discretion with regard to the inclusion or exclusion of entities in the group supervision, as per law the largest possible scope of entities is used.** Article 64 ISA defines an insurance group as two or more companies, if

- At least one is an insurance entity;

- As a whole, they operate primarily in the insurance sector; and
- They are an economic unit or are linked in some other way through influence or control.

According to Article 65 ISA, FINMA can place an insurance group that has an entity in Switzerland under group supervision, if the insurance group

- Is actually managed from Switzerland; or
- Is actually managed from abroad, but is not subject there to equivalent group supervision.

70. **This ensures that group supervision includes all entities of a group irrespective of their activities**, be it insurers, operating and non-operating holding companies (including intermediate holding companies), other regulated entities (such as banks and/or securities companies), and non-regulated entities (including parent companies, their subsidiary companies and companies substantially controlled or managed by entities within the group, special purpose entities, etc.). Generally, insurance and banking/other financial sector activities are institutionally separate. Only one of the insurance groups owns a material banking activity (Baloise) and thus qualifies as a conglomerate.

71. **Insurance groups are required to report their legal structure on a regular basis and material changes on an ad-hoc basis.** The group structure and scope of group-wide supervision is included and regularly updated in the FINMA coordination agreement that forms the basis for cooperation and coordination with other involved supervisors in FINMA supervisory colleges. Depending on the nature of the group's business, FINMA also cooperates with involved supervisors from other financial sectors. At FINMA internally, for the purpose of group supervision, the insurance division cooperates with the banking, asset management or markets divisions.

72. **Intra-group transactions (IGTs) are valued according to the valuation rules for the respective asset class or transaction, and regularly reported to FINMA.** Generally, it is required that the value attributed to a position should be such that two independent knowledgeable persons would be willing to exchange this position for this value. Accordingly, IGTs must be effected at market terms and conditions. Swiss groups have to report IGTs to FINMA yearly or if they exceed predefined thresholds on an ad-hoc basis. If the portfolio or structure of the IGTs changes materially during the financial year as a result of IGTs which are not subject to ad-hoc reporting requirements, FINMA must be provided with an interim portfolio report. If the impact of IGTs which are not subject to reporting requirements becomes material, the insurance group must list them separately in the IGT portfolio report for each IGT category, indicating the quantity and total amount.

B. Winding-up, Recovery and Resolution

73. **The Insurance Supervision Act (ISA) defines several options for exiting the market:**

- Liquidation of solvent insurers (if FINMA revokes the license);
- Liquidation of insolvent insurers (insurance bankruptcy); or

- Exit from the market after voluntary surrender of the license (a liquidation is possible, but not compelling in every case).

74. If there is a justified concern that an insurer is over-indebted or has serious liquidity problems and a recovery is not possible, FINMA revokes its license and starts bankruptcy proceedings. But even before reaching this point, FINMA can revoke the permission to continue the business if the insurer no longer fulfills the requirements for its activity or seriously violates the supervisory provisions or the interests of the insured are endangered. In particular, FINMA will usually revoke the permission if the SST ratio is at or below 33 percent. FINMA can impose other measures in case of immediate risks to policyholder interests.

75. FINMA has the exclusive competence to declare an insurance company insolvent and to initiate a resolution procedure. There is no need for further court approval. After opening a resolution procedure FINMA is responsible for conducting the resolution procedure. FINMA can appoint a (bankruptcy) liquidator and oversee its activities. The courts do not have a direct function in the resolution of an insurer. They serve as a possibility to appeal the decrees of FINMA. Hence the decree to initiate resolution procedures is subject to appeal to the Federal Administrative Court and ultimately to the Swiss Supreme Court. In bankruptcy proceedings, the creditors and owners of an insurer may only appeal against realization activities.

76. There are special bankruptcy rules designated for insurance companies. The general process is based on normal bankruptcy proceedings, but special rules were required for the following reasons:

- Shift of competence for opening and conducting resolution procedures from the regular courts to FINMA;
- Speeding up the conduct of resolution procedures; and
- Dealing with the special feature of tied assets.

77. The policyholders in direct insurance are protected through the tied assets. All claims arising from insurance contracts must be secured with tied assets. In case of an insolvency proceeding all tied assets are for the sole use of compensating policyholders. Only if all claims of policyholders have been satisfied can a surplus be used to compensate other creditors. Furthermore, the IBO-FINMA aims to achieve the timely payout of benefits to policyholders. For example, FINMA is able to make up-front payments to policyholders even before their claim has been legally determined in the schedule of claims. To enable this there are strict rules on the composition of the tied assets, their security and the ability to sell them quickly if needed.

78. In reinsurance where there are no tied assets the policyholders are currently treated as regular, non-privileged creditors. In the current revision of the ISA a provision is being added that treats all policyholders as privileged to other regular creditors. This will enhance the protection of policyholders in reinsurance.

79. In 2018, the authorities initiated a public consultation on amendments to the Insurance Supervision Act that would cover the restructuring of insurers in the event of a crisis. The proposed amendments vest in FINMA restructuring powers when an insurer experiences financial distress. Although insurance resolution is subject to ongoing regulatory developments at the international level, several emerging policy positions may guide the development of the insurance resolution framework. The authorities may consider, for example, enabling FINMA to exercise resolution powers without requiring the consent of interested parties, incorporating provisions on run-off or envisaging the possibility of transferring reinsurance contracts associated with the transferred policies in resolution. Box 1 discusses these concepts in greater detail.

Box 1. Legal Framework for Insurance Resolution

Insurance resolution is the subject of ongoing regulatory developments at the international level. In December 2017, the FSB consulted on a proposed methodology for assessing the implementation of the Key Attributes of Effective Resolution Regimes for Financial Institutions ("Key Attributes")[1] in the insurance sector ("Insurance Methodology").[2] The Key Attributes remain the umbrella standard for resolution regimes covering financial institutions that could be systemically significant or critical in failure. However, the proposed Insurance Methodology provides additional guidance to jurisdictions when adopting or reforming insurance resolution regimes to implement the Key Attributes.

The authorities have recognized the need to strengthen the existing insurance legislation in response to recent regulatory developments. In November 2018, the Federal Council initiated a public consultation on amendments to the Insurance Supervision Act (ISA).[3] The proposed amendments cover the restructuring of insurers in the event of a crisis and include new powers for FINMA to transfer insurance portfolios, restructure the debt and equity of the insurer, amend insurance contracts and defer the termination of reinsurance contracts. These powers may be exercised in circumstances where an insurer has become "over-indebted" or has "major liquidity problems."[4]

The design of the proposed insurance resolution regime has been driven by the authorities' own experience of insurance failures. It is on the basis of this experience that the authorities have chosen to focus on the need for strong powers to amend the rights of policyholders under the insurance contracts of an insurer in resolution. In addition, in terms of design, the regime relies on each insurer having sufficient tied assets to cover claims under insurance contracts with bail in powers being available to absorb losses. As a result of this approach, there is no proposed legal mechanism for dealing with a situation where tied assets and bail-in prove to be insufficient and additional funding is needed. As the possibility of such a situation arising cannot be excluded, the authorities could reconsider this approach.

The proposed regime has not been designed to deal with the failure of a systemically significant insurer. This is on the basis that the authorities have determined that there are currently no systemically significant insurers. Further legal amendments would be needed to deal with the resolution of a systemic insurer.

[1] http://www.fsb.org/2014/10/key-attributes-of-effective-resolution-regimes-for-financial-institutions-2/

[2] http://www.fsb.org/2017/12/key-attributes-assessment-methodology-for-the-insurance-sector-consultative-document/

[3] https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-72921.html

[4] Article 51a of the proposed amendments to the ISA.

Box 1. Legal Framework for Insurance Resolution (Concluded)

Further work will be required to bring the proposed regime more in line with international standards on insurance resolution. The Key Attributes are designed to apply generally to insurers which are, or could be, systemically significant or critical in the event of failure. Depending on the circumstances at the time of their failure, an insurer that has not been identified as systemically significant or critical ex ante could prove systemic as a result of contagion or loss of confidence in the insurance system. The authorities should consider how their proposed legal framework could accommodate such a scenario.

Although developments at the international level are ongoing, there are emerging policy positions which could inform the development of the insurance resolution framework and enable it to accommodate a scenario where an insurer that has not been identified as systemically significant or critical ex ante proves systemic at the point of failure. In particular, based on the Key Attributes and the proposed Insurance Methodology, the authorities could consider the following non-exhaustive list of additional amendments to the ISA: (i) specify in the ISA suitable indicators of non-viability for the purposes of triggering the resolution of an insurer (e.g., the insurer is in breach of minimum capital, assets backing technical provisions or other specific prudential requirements in circumstances where there are no reasonable prospects of restoring compliance with these requirements);[5] (ii) include powers to ensure that FINMA can discontinue the writing of new business by an insurer in resolution while continuing to administer existing contractual policy obligations for in-force business (run-off);[6] (iii) ensure that FINMA is empowered to exercise resolution powers without requiring the consent of interested parties, including the policyholders, creditors or shareholders of the insurer in resolution;[7] (iv) provide a legal basis for FINMA to ensure continuity of essential services, including by requiring group companies to continue to provide such services to an insurer in resolution;[8] (v) allow FINMA, in addition to the powers to transfer assets and liabilities of an insurer in resolution, to effect the sale or merger of an insurer in resolution and for such powers to include the ability to transfer any reinsurance contracts which are associated with the transferred policies without the consent of the reinsurer subject to adequate safeguards (e.g., continuation of premium payments);[9] (vi) provide a legal basis for recovery and resolution planning.[10]

The provisions of the proposed insurance resolution regime are high-level. Further analysis is required to determine whether such an approach provides for an appropriately sound legal basis for the powers and tools that may be needed in the resolution of an insurer.

[5] See Key Attribute 3.1 and EN3(c).

[6] See Key Attribute 3.7.

[7] See Key Attributes 3.2, 3.3, 3.7.

[8] See Key Attribute 3.2.

[9] See EC 3.7 in the proposed Insurance Methodology.

[10] See Key Attribute 11.

C. Business Conduct

80. A fundamental objective of insurance regulation is to protect policyholders. This is elaborated further in the Insurance Supervision Act (ISA), the Insurance Supervision Ordinance (ISO) and the Insurance Contract Act (ICA)—especially the latter sets out the requirements on what needs to be disclosed to the customer before the conclusion of a contract and on the duration of the contract. The Unfair Competition Act also plays an important role in the protection of insurance customers. However, Swiss legislation is generally built on the assumptions that customers are mature economic subjects and able to understand and evaluate insurance contracts. The focus in this area is therefore primarily on transparency and the fight against misuse.

81. **In those limited situations where FINMA approves products, it has more opportunity to consider the angle of consumer protection.** This is the case for tariffs and General Insurance Conditions used in Switzerland for the insurance of risks in occupational pension plans for employed persons and for supplementary insurance to the basic (mandatory) health insurance. Also, with regard to natural hazard insurance, the scope of coverage and the premium rating for such insurance is uniform and binding for all insurers. FINMA examines within the approval process on the basis of the tariff calculations submitted by the insurance companies whether the proposed premiums are within a range which on the one hand is not threatening the solvency of the individual insurance undertaking and on the other hand protects insured persons against misuse.

82. **There are some planned legislative actions to improve disclosure and advice with regard to insurance products with an investment character.** The proposed revision of the ISA is expected to introduce more stringent rules on:

- Documentation of products characteristics in a "Key Investor Document"; and
- Conduct and organization of financial service providers ("Know your customer": review of appropriateness and suitability, documentation and accountability, third-party remuneration).

83. **Insurance intermediaries who are not legally, economically or in any other way tied to an insurance company must register with FINMA prior to engaging in their intermediation activities.** Registration is voluntary for the remaining insurance intermediaries ("tied insurance intermediaries") which are indirectly subject to FINMA's supervision over the responsible insurer.

84. **Various formal requirements have to be met by insurance intermediaries.** Any insurance intermediary who applies for registration has to demonstrate that he has adequate professional knowledge and experience or in case of a legal entity that it has sufficient staff with these qualifications. Individuals also have to demonstrate that they have no criminal conviction for behavior not compatible with their intermediation activities and that they are not subject to insolvency procedures related to their intermediation activities. All registered insurance intermediaries are required to have a professional liability insurance with a coverage of at least CHF 2 million per year. Finally, insurance intermediaries who handle client monies are required to be licensed according to the Anti-Money-Laundering Act.

85. **If an insurance intermediary is found not to meet the regulatory requirements, FINMA would set a deadline by which these have to be restored.** If an insurance intermediary fails to do this, FINMA would ultimately withdraw the registration. FINMA also carries out supervisory reviews of unregistered insurance intermediaries should it become aware of alleged activities of insurance intermediation.

86. There is scope for improvement in respect of conduct after registration, where the current requirements and supervision are more limited. The planned revision of the ISA includes a further strengthening of the framework against abusive practices in the market. Intermediaries will be required to exercise good conduct. If an intermediary fails to meet this requirement, FINMA will have a broad tool box for an appropriate supervisory response, ultimately leading to the exclusion of the intermediary from the market.

Recommendations

87. The regulation and FINMA's competences in the supervision of business conduct should be strengthened, and sufficient resources should be allocated to this task. Conduct supervision was already identified as being only in partial observance with the Insurance Core Principles in the 2013 FSAP. Revising the ISA as proposed is expected to substantially strengthen the regulatory framework with regard to insurance intermediaries. FINMA should carefully prepare for the new tasks and evaluate the need for further staff to implement the new regime.

INSURANCE SUPERVISION

88. FINMA exercises its powers in insurance supervision diligently. Following the revision of the ISO in 2015, FINMA has also strengthened its supervision of internal control mechanisms and requests insurers to perform an annual Own Risk and Solvency Assessment (ORSA). With newly set-up teams dedicated for onsite inspections, expertise is expected to be bundled further.

A. Supervisory Review and Reporting

89. FINMA applies a proportional and risk-based approach that applies to all areas of supervision. All of the institutions FINMA supervises are put into one of six categories, five of which are relevant in insurance supervision. Insurance companies are allocated mainly according to their risk impact on policyholders but also the system as a whole, as well as the reputation of the Swiss financial sector. None of the Swiss insurance companies is in Category 1 which is reserved for systemically relevant undertakings. The five insurers in Category 2 are primarily large, internationally active companies. Category 3 includes a varied cluster of 38 mid-sized insurers, which—with the exception of reinsurers—are generally focused on the Swiss market. The 161 companies included in Categories 4 and 5 are smaller companies. Many are subsidiaries or branches of non-Swiss insurers or domestic undertakings with a restricted business focus.

90. In addition to being allocated to a category, each institution receives a rating corresponding to FINMA's assessment of its current state. These two parameters—categorization and institution rating—serve as the basis for determining the extent of supervision and the use of supervisory instruments. The aim is to achieve a more proportional approach and systematic risk focus of supervisory activities.

91. The supervisory cycle builds on annual supervisory reporting and audit reports. Insurers must submit their annual supervisory reporting by end-April every year while reinsurers must submit their reports by end-June. Within the supervisory cycle, the audit companies perform regulatory audits on an annual basis according to the standard audit strategy and based on audit programs defined and provided by FINMA. Regulatory audits cover tied-assets, provisions, pension fund business, internal control systems, business continuity management and specific topics in the context of group supervision. FINMA examines these documents and concludes its reviews by providing feedback to the companies at the end of October.

92. In 2018, supervisory activities continued to focus on corporate governance whereby robust and stress-resilient structures were seen a priority by FINMA. Close attention is also paid to the impacts of the low interest rate environment. Ensuring that life insurers are maintaining adequate levels of reserves remains at the center of these activities. In 2018, all insurance companies published their financial reports including their solvency ratios for the first time.

93. Onsite reviews with an emphasis on identified risks play an important role. To make this supervisory instrument as effective as possible, FINMA's activities aims to ensure that all information on the condition of the insurance companies is analyzed systematically. Currently, two teams with 13.5 full-time equivalents are dedicated for onsite reviews, with support from other supervisory and expert staff. Focus topics in 2017 were corporate governance and internal control systems, ceded reinsurance/retrocession, tied assets, variable annuities and closed portfolios.

94. The frequency of onsite inspections depends on several factors, including the supervisory category and the rating of the insurer. In the last three years, eight out of the 49 big- and medium-size insurers and insurance groups were inspected onsite annually, 16 have been inspected onsite at least twice within three years. Besides onsite inspections, FINMA holds high-level meetings with the board of directors and executive management of the insurance companies (category 2 and insurance groups) as well as regular key account management meetings with the relevant function holders within the insurance companies (categories 2 and 3) and groups. Onsite inspections are conducted on the basis of a rolling schedule or "pipeline". This takes into account the supervisory category, key topics and the ratings of the supervised insurer, as described above. This rolling schedule allows FINMA to react quickly if further investigations are required or if the rating of an insurer changes.

Recommendations

95. The analysis of group-specific risks, including liquidity risks and the fungibility of capital, should be intensified. The Swiss insurance sector is dominated by a few large internationally active insurance groups. While the SST and other prudential regulations are well established and FINMA is monitoring intra-group transactions regularly, additional focus should be given to potential liquidity risks arising from those. Furthermore, the fungibility of capital needs to be assessed under stressed market conditions, allowing for smooth recovery and resolution at the group level.

B. Corporate Governance and Risk Management

96. FINMA has intensified its efforts in supervising the governance structure and internal control systems of insurance companies. The governance assessment involves evaluating periodically collected information about an insurer's corporate governance by focusing on the insurer's underlying governance structures, its supervisory and management bodies (board of directors, executive board) and its control functions (risk management, compliance and internal revision). The data collected allows FINMA to evaluate the insurer's governance structures and identify any deficiencies. Collecting the data periodically also allows FINMA to monitor any developments made in corporate governance during a particular period. Governance assessment findings are included in the overall assessment of the insurer and in FINMA's supervisory process. These can lead to follow-up activities at individual insurance companies, as well as for the entire market or for a selected group of insurance companies. With the audit program the insurer's internal control system on an entity level is assessed every two years by the external auditor. It provides considerable insight on the effectiveness and robustness of the internal control systems in place.

97. Swiss insurers have to perform an ORSA process and to document comprehensively its risk situation and solvency capital requirements. All processes and procedures used which are appropriate to the nature, scale and complexity of the risk have to be documented and used for capital management and solvency purposes. The results are to be documented in the annual ORSA Report under the responsibility of the board. Insurers provide FINMA with a report on the results of the ORSA process. Within the ORSA process the insurer has to analyze the impact of various downside scenarios including at least one scenario which is threatening the going-concern. The scenario analysis has to cover and quantify the impact in all relevant capital views (e.g., SST, statutory, IFRS/GAAP, etc.).

98. With respect to operational risks, FINMA normally does not require quantification for regulatory capital purposes under the SST. However, it does expect the identification, assessment and management of operational risks. If these results either require additional capital or could put regulatory solvency at risk, FINMA has the possibility to intensify its supervision of operational risks and/or increase the required capital under the SST. Furthermore, FINMA considers operational risk in its requirements regarding outsourcing.

Recommendations

99. FINMA should strengthen the analytical framework for assessing operational risks and prescribe capital add-ons if needed. The importance of operational risks is increasing as the insurance sector is digitalizing more processes, and overarching cost-cutting initiatives are undertaken. FINMA is recommended to investigate operational risks, including cyber risks, diligently and prescribe capital buffers if necessary.

C. Cross-Border Cooperation

100. FINMA leads five supervisory colleges in its role as group-wide supervisor and participates in 14 foreign colleges as host supervisor. From a home perspective, six insurance groups are under FINMA group supervision, of which five are cross-border groups with established FINMA-led supervisory colleges. Since 2016, FINMA has signed coordination agreements with all host supervisors participating in these supervisory colleges. The coordination agreements set out rules for cooperation between supervisors in the colleges (including confidentiality provisions).

101. FINMA-led supervisory colleges are permanent platforms for cooperation between various authorities which are involved in the supervision of a group or conglomerate. The aim of this regular exchange of information and experience is to step up cooperation between supervisory authorities and improve supervision of internationally active groups and conglomerates by means of:

- A yearly in-person meeting in (June or July) including written exchange of quantitative and qualitative information beforehand;
- For the two big colleges an interim call (November), and for the smaller colleges when needed or requested;
- A mid-year written information exchange about qualitative information (e.g., risk management, compliance, supervisory activities); and
- Ad-hoc cooperation on a multilateral or bilateral basis.

102. From a host perspective, FINMA decides to participate in foreign supervisory colleges based on a risk-based and proportionate approach. Criteria considered include the importance of the solo entity in the Swiss market, its interaction with the group and the importance of the Swiss entity for the group. In practice, this means that FINMA participates in supervisory colleges where the entity supervised by FINMA falls within supervisory categories 2, 3 or 4. For entities in category 5, FINMA usually does not participate in the colleges concerned. A decision on non-participation is coordinated with the responsible group-wide supervisor, whom FINMA always offers bilateral cooperation as an alternative. Currently, FINMA participates in 14 foreign supervisory colleges as a host supervisor and in all the regular and ad-hoc written information exchange initiatives as defined by the responsible group-wide supervisor. In the case of AXA, as it is a G-SII and given the size of its entities in Switzerland, FINMA also participates in the respective Crisis Management Group led by the French insurance supervisory authority.

103. In accordance with international standards, FINMA is legally authorized to share non-public information with foreign financial market supervisory authorities, facilitated by a wide range of cooperation agreements. FINMA has been an IAIS Multilateral Memorandum of Understanding (MMoU) signatory since 2011. With the signatories FINMA can share non-public information based on the MMoU. FINMA has also signed bilateral MoUs with the competent insurance supervisors of all EEA countries (except for Croatia, which was not an EU country at the time of signature). Furthermore, FINMA has concluded bilateral MoUs with the European Insurance and Occupational Pension Authority (EIOPA), various U.S. insurance supervisors, the Australian insurance supervisor (Australian Prudential Regulation Authority, APRA), the Dubai Financial Services Authority (DFSA) and the Monetary Authority of Singapore (MAS).

D. Macroprudential Surveillance

104. FINMA has set up a comprehensive assessment of the risk drivers that could lead to financial instability and the possible mitigating actions. The assessment is undertaken semi-annually within the "risk barometer" process and takes into accounts insights gained by national and international authorities. The risk drivers considered are grouped into: (1) macroeconomic and capital markets; (2) compliance and conduct; (3) operational; and (4) other. The macroeconomic and risk analysis is followed by discussions with supervision staff, in which the impact of identified risks is assessed and measures that could effectively improve the resilience of the financial sector are evaluated. The impact analysis is regularly discussed with FINMA's board of directors and executive board. Focusing on the development of the Swiss real estate market, the "Real Estate Barometer" analyzes on a semi-annual basis the latest developments in mortgage interest rates, domestic mortgage claims, real estate prices, rents and housing construction in depth.

105. Monitoring exposures towards the banking sector, in particular via contingent convertible bonds, is incomplete. Regular reporting to FINMA does not address exposures towards any special sector. During and after the financial crisis in 2008, FINMA established temporary quarterly reporting addressing explicitly the exposures towards the banking sector. This reporting ended in October 2015. From that point, some exposure data was only collected through targeted surveys, e.g., via a high-yield bond survey undertaken in 2016. Some insurers report on their exposures in bank bonds in their SST report on a voluntary basis, but as this is not required, FINMA has no overall view about trends in these exposures.

106. FINMA publishes aggregated market data in its annual "Insurance market report". Aggregated results for insurance branches (life, non-life, health and reinsurance) for the SST including assets and liabilities composition, market risk analysis, interest risk analysis and all scenarios are published in the annual SST Survey.

107. In Switzerland, the too-big-to-fail discussions have produced a different result for banks and insurances: Two banks (Credit Suisse and UBS) have been identified as global systemically important banks, and three other banks (Raiffeisen, ZKB, and Postfinance) are recognized as being domestically relevant. Additionally, three financial market infrastructures (Swiss Interbank Clearing payment system, SIX SIS central securities depository including the SECOM securities settlement, and SIX x-clear, the central counterparty) have been identified as systemically relevant, but none of the insurance companies. FINMA actively participates in the IAIS process designed to evaluate potential G-SIIs, however the final designation will be decided by the Financial Stability Board and FINMA after consultation of the IAIS.

Recommendations

108. Aggregated ORSA findings should inform macroprudential surveillance. The ORSA provides a rich source for risk analysis, and while the ORSA reports are already scrutinized and discussed with the companies, their findings could, at an aggregated level, also feed into the market-wide risk assessment, and ultimately macroprudential surveillance.

109. FINMA should systematically collect relevant information on exposures towards the banking sector, in particular with regard to contingent convertible bonds. The exposures towards Swiss banks, in particular the G-SIBs, cannot be tracked by FINMA on a regular and systematic basis. A regular monitoring of exposures, including exposures with equity characteristics like contingent convertible bonds, would help in understanding the macrofinancial implications of the interlinkages between the domestic banking and insurance sector.

Annex I. Financial Soundness Indicators of the Insurance Sector

(In percent)

	2013	2014	2015	2016	2017
Capital adequacy					
Shareholder equity and reserves / total assets - life	7.7	...	7.4	...	7.3
Shareholder equity and reserves / total assets - non-life	29.0	...	29.2	...	25.7
Shareholder equity and reserves / total assets - reinsurance	24.9	...	26.6	...	17.8
Solvency coverage ratio (SST) - life	153	149	147	160	178
Solvency coverage ratio (SST) - non-life	203	191	201	228	231
Solvency coverage ratio (SST) - reinsurance	219	204	199	217	220
Profitability					
Growth in gross written premiums - life	...	-0.7	-0.4	-5.7	-3.7
Growth in gross written premiums - non-life	...	-2.1	-2.7	1.9	2.7
Growth in gross written premiums - non-life	...	6.5	4.2	26.7	-3.7
Loss ratio (net paid claims / net premiums) - non-life	56.6	59.3	60.8	57.3	58.8
Loss ratio (net paid claims / net premiums) - reinsurance	66.9	61.7	60.6	64.6	75.4
Expense ratio (net expenses / net premiums) - non-life	24.9	27.5	29.2	28.9	29.3
Expense ratio (net expenses / net premiums) - reinsurance	25.2	30.0	31.6	33.7	35.8
Combined ratio (loss ratio plus expense ratio) - non-life	81.5	86.8	90.0	86.2	88.1
Combined ratio (loss ratio plus expense ratio) - reinsurance	92.0	91.7	92.2	98.3	111.2
Return on equity - life	9.9	7.8	6.6	6.7	8.5
Return on equity - non-life	19.6	18.3	14.9	17.8	13.7
Return on equity - reinsurance	15.7	16.3	27.8	9.0	2.4
Asset quality					
Bonds / total investments excl. unit-linked	46.3	...	44.2	...	40.4
Stocks / total investments excl. unit-linked	3.0	...	3.8	...	4.0
Investment yield - life	3.3	3.3	3.1	2.9	2.5
Liquidity					
Liquid assets / total investments excl. unit-linked [1]	53.8	...	53.4	...	50.8
Reinsurance					
Risk retention ratio (net premium / gross premium) - life	99.1	99.2	99.1	98.8	98.6
Risk retention ratio (net premium / gross premium) - non-life	87.5	87.7	87.2	88.8	87.3

Source: IMF staff calculations based on FINMA data.

Notes: Reinsurance includes captives.

[1] Liquid assets include bonds, equity, cash and deposits, and investment funds.