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Denmark: Financial Sector Assessment Program—Detailed Assessment of Observance of the Insurance Core Principles

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FINANCIAL SECTOR ASSESSMENT PROGRAM

DENMARK

DETAILED ASSESSMENT REPORT ON OBSERVANCE OF THE INSURANCE CORE PRINCIPLES

SEPTEMBER 2006

INTERNATIONAL MONETARY FUND
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Contents Page

GLOSSARY

AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
ATP	Danish Labor Market Supplementary Pension Fund
BCP	Basle Core Principles for Effective Banking Supervision
CP	Core principle
DFSA	Finanstilsynet, the Danish Financial Supervisory Authority
DSC	Danish Securities Council
EEA	European Economic Area
EU	European Union
EO	Executive orders
FATF	Financial Action Task Force
FBA	Financial Business Act
FBC	Financial Business Council
FIU	Financial Intelligence Unit
FSAP	Financial Sector Assessment Program
FSSA	Financial System Stability Assessment
IAIS	International Association of Insurance Supervisors
IAS	International Accounting Standards
ICP	Insurance Core Principles
IMA	European Insurance Mediation Act
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IT	Information technology
LD	Lønmodtagernes Dyrtidsfond
LEG	Legal Department of the IMF
MFD	Monetary and Financial Systems Department of the IMF
MoEB	Ministry of Economic and Business Affairs
MoU	Memorandum of understanding
NAO	National Audit Office
OTC	Over-the-counter
REMOS	Reinsurance monitoring system
SP	Special pension savings scheme

I. International Association of Insurance Supervisors Core Principles

A. Introduction

General

1. The assessment of the observance the *Insurance Core Principles* (ICP) developed by the *International Association of Insurance Supervisors* (IAIS) dated October 2003, was carried out as part of the first Financial Sector Assessment Program (FSAP) mission to Denmark, November 7–18, 2005.[1]

2. The assessment reviews the effectiveness of Danish insurance legislation (including supporting regulation and rules) as well as the effectiveness of the supervisory body, that is Finanstilsynet (DFSA). Given the highly developed nature of the Danish insurance market, this assessment comments on both the essential and advanced criteria underpinning each core principle. However, in accordance with Annex 2 of the ICP, only essential criteria have been taken into account in assessing the overall level of observance of a core principle.

3. A recent audit by the National Audit Office (NAO) found that further improvements, especially supervision of nonlife insurance, should be made.[2] Specifically, the NAO noted that frequency of comprehensive on-site inspections needed to be shortened, and supervision of IT systems needed to be upgraded, and the follow-up of inspections made more effective.

4. Key recommendations arising from the assessment cover two main issues. One is the fact that DFSA bases its system to assess the appropriateness of key functions on the assumption that is the core responsibility of the senior management to ensure adequate personnel to be assigned to relevant tasks in the supervised companies. There was no evidence that this has led to severe problems so far. However, this may well have been justified by the limited size of the market. The second issue relates to a requirement that internal audit functions should be made compulsory for smaller companies. Guideline 9680 does not sufficiently clearly define what Finanstilsynet requires in the area of internal control. The guideline does not expand on requirements from section 71 in the Financial Business Act (FBA), the subsequent control procedure may thus not cover all relevant issues. The importance of this function requires an executive order.

5. Pension products dominate the insurance sector, and 94 percent of such products carry a guaranteed rate of return to policyholders—some with a guaranteed return above the present risk free interest rate. The investment risk matched with the interest rate risk on

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[1] The assessment was performed by Henning Goebel (Bafin, Germany) with the assistance of Kirsten Nordbø Steinberg (Kredittilsynet, Norway).

[2] The report was published in September 2005 on http://www.rigsrevisionen.dk/, but is only available in Danish. It covered the period 2001–04, but with the focus on the supervision of small and medium-sized banks and non-life insurance companies during the period 2003–04.

liabilities is still a concern, as mismatches poses a risk to the level of buffer capital, albeit several measures have been implemented to increase provisions and buffer capital.

B. Information and Methodology Used for Assessment

6. The *IAIS Methodology* approved in October 2003, together with an IMF template based on this Methodology, was employed in preparing this assessment. The assessment was greatly facilitated by the detailed self-assessment and other information supplied by the authorities. The assessors would like to express their appreciation for the substantial efforts, inputs, and time the DFSA provided, which facilitated the assessment. Other representatives from the public and private sectors with whom the assessors interacted were also generous with their time, hospitable, open in their views, and invariably helpful.

C. Market Analysis—The Danish Pension and Insurance Market

The pension system

7. The Danish pension system consists of several layers. The first pillar is the entitlement of all citizens in Denmark to an old-age pension from the age of 65, and the Danish Labor Market Supplementary Pension Fund (ATP). The next layer is the mandatory labor market pension schemes: Lønmodtagernes Dyrtidsfond (LD) and the Special Pension Savings Scheme (SP). The last pillar is the private and individual pension savings. The old-age pension is founded by taxation and is a "pay-as-you-go" scheme. The other pension schemes are funded by employers and employees. There are three main schemes established: (i) by law; (ii) by agreements between the parties in the labor market; and (iii) as individual contracts.

8. The general retirement age is 65 for pillar I. However, a number of schemes will include options to consumers to retire before (e.g., from the age of 60). Most pension schemes include life insurance, disability and old-age/survivor pensions. Further, spouse's pension and child pension are usual. The options vary among the pensions funds.

9. The schemes established by law are ATP, SP, and LD. The labor market schemes consist of savings in life insurance companies, general pension funds, company pension funds, and credit institutions. The individual schemes are savings in life insurance companies and credit institutions. Table 1 shows total pension savings spilt on different types of entities.

10. In 2005, total pension assets have grown by almost 17 percent. This is the largest growth in the last 5 year period. Credit institutions and ATP have experienced the largest increase, followed by the life insurance companies. The schemes based on law accounts for 22 percent, and the life insurance companies and general pension funds accounts for 62 percent of the total pension assets.

Table 1. Total Pension Assets Split on Types of Entities, End-2004 and End-2005

	2004		2005	
	Value of Assets Billion DKr	Percent of Total Value	Value of Assets Billion DKr	Percent of Total Value
Life insurance companies	810	43.9	953	44.2
General pension funds	339	18.4	381	17.7
Company pension funds	39	2.1	42	1.9
Credit institutions	244	13.2	298	13.8
ATP	307	16.7	365	16.9
SP	46	2.5	51	2.5
LD	58	3.2	64	3.0
Total	**1,844**	**100.0**	**2,154**	**100.0**

Source: Danish Financial Supervisory Authority.

Life insurance and pensions

11. The life sector is dominated by a relatively small number of groups and the major insurance products are with-profit pension schemes. These products have similar characteristics to those sold in a number of other countries with minimum guaranteed rates of return. In the first half of this decade, pension suppliers suffered financial stress during the equity price downturn and in the low interest rate environment. The Danish life insurance industry has historically produced adequate profits, but the dominance of the guaranteed life products and the associated asset-liability matching issues have rendered results contingent on asset side performance. Falling asset markets and returns have introduced new financial pressures.[3]

12. At end 2005, there were 36 life insurance companies and 29 general pension funds (Table 2). Some of these entities are organized as groups. Effectively, there are 18 life insurance companies/pension funds (groups). Life insurance companies and pension funds are covered by the same legislative framework. In addition, there were 44 company pension funds.

Table 2. Number of Life Insurance Companies and Pension Funds (Legal Entities), 2000–05

	2000	2001	2002	2003	2004	2005
Life insurance companies	63	58	43	41	37	36
General pension funds	31	31	31	30	30	29
Company pension funds	54	50	47	47	44	44

Source: Danish Financial Supervisory Authority.

13. During the last 10 years, there have been a number of new entrants and exits at the level of legal entities. However, most of these entrants and exits have taken place within

[3] See the technical note *Pensions with Profit Contracts* by Kirsten Norbø Steinberg.

individual insurance groups due to changes of tax rules. In the case of life insurance groups, the number of companies is largely unchanged. No exits were caused by winding-up or other insolvency procedures. New entrants and exits form part of normal adjustment to market conditions, including mergers. Recently, a couple of general pension funds merged, but the scope for further consolidation of general pension funds mainly depends on the parties in the labor market.

14. The life insurance market is dominated by a few large groups (Tables 3 and 4). In 2005, the top 5 companies have a market share of 59.9 percent and the top 10 companies have a market share of 79.0 percent. In the commercial market, the top 5 companies have a market share of 89.2 percent and the top 10 companies have a market share of 99.9 percent. In 2004, the life insurance companies and general pension funds amount for 63 percent of the total asset in pension saving schemes. The company pension funds amount to approximately 2 percent of these assets.

Table 3. Market Concentration Measured by Gross Premium of Life Insurance Companies (Groups) and General Pension Funds (Excluding Company Pension Funds), 2003–05

	2003	2004	2005
Danica Pension	19.0	17.4	17.6
PFA Pension	17.4	17.2	17.4
PensionDanmark	-	-	9.0
Nordea Pension	8.3	7.9	8.8
Kommunernes Pensionsforsikring	7.6	7.6	7.3
Industriens Pensionsforsikring	5.1	5.2	
Top 5 total	57.4	55.3	59.9
Industriens Pensionsforsikring	-	-	5.2
SEB Pension (Codan)	4.8	5.0	4.7
Pen-Sam Liv	3.8	3.9	3.8
B&A Pension	3.1	3.5	-
Topdanmark Liv	2.8	3.1	3.1
HTS Pension	2.4	2.6	-
MP Pension	-	-	2.2
Top 10 total	74.4	73.4	79.0

Source: Danish Financial Supervisory Authority.

15. Cross-border activities are limited in both life insurance and general pension funds, as well as for foreign insurers operating in Denmark and Danish insurers operating abroad. The major reason for this is the tax legislation. Premiums paid to foreign undertakings according to the tax law are not tax deductible for the insured.

16. The major distribution channels are direct sales from the insurer, through banks, and through intermediaries. For life and pension the parties of the Danish labor market, as part of the labor market agreements, to a large extend decide the supplier, as well as the level of premiums and coverage.

Table 4. Market Concentration Measured by Gross Premiums of the Commercial Part of the Market of Life Insurance Companies and General Pension Funds (Excluding Company Pension Funds) 2003–05

	2003	2004	2005
Danica Pension	32.5	32.1	32.3
PFA Pension	29.7	26.3	26.3
Nordea Pension	14.1	14.7	16.1
Codan Pension (SEB)	8.2	9.2	8.7
Topdanmark Liv	4.8	5.7	5.8
Top 5 total	**89.3**	**87.9**	**89.2**
AP Pension	2.9	3.7	3.6
Skandia	3.1	3.2	2.6
Alm. Brand Liv & Pension	1.7	1.8	1.7
ALKA	1.6	1.6	1.6
PKA+Pension	1.1	1.2	1.3
Top 10 total	**99.7**	**99.5**	**99.9**

Source: Danish Financial Supervisory Authority.

Note: The commercial part of the market amounts to approximately 55 percent of the total market of life insurance companies and general pension funds.

17. The life insurance companies and general pension funds are mainly providing a second supplementary pension, which is a mandatory pension scheme for employees, where the major products are traditional life insurance contracts with a guaranteed return. For these mandatory pension schemes that are part of the labor market agreements, the typical contributions rates range from 12 to 17 percent of the wage. In all contracts, the profit is distributed to each contract according to the so-called *contribution principle* on a fair basis, unless the contract states otherwise. Policyholders are allowed to transfer their contract from one company to another, but are not entitled to undistributed profits (collective bonus reserves).

18. The market for individual life insurance contracts and unit link products from the insurance sector is limited (Table 5).[4] Unit link products were introduced in the late 1980's, and just recently the market share of these contracts has begun to increase. Some life insurance companies have introduced unit linked products with an embedded zero interest rate option.

19. As in a number of other countries, the principal vulnerabilities for the insurance sector arise from the requirement to achieve a specified return for the duration of in-force policies, which may span several decades, in an environment where higher returns are difficult to achieve. Until mid-1994, pension companies applied mostly a maximum technical interest rate of 4.5 percent on the traditional insurance contracts with a guaranteed return. It was then lowered by the DFSA to 2.5 percent. In 1999, the maximum technical interest rate was reduced further to 1.5 percent. The agreed guaranteed interest rate applies throughout the lifetime of an in force pension scheme, so that the agreements established up to mid-1994

[4] Unit link products mean that the policy holder carries the investment risk.

still yield a guaranteed rate of interest of 4.5 percent. These are maximum guaranteed rates of interest, and the pension companies have been at liberty to create pension schemes based on lower guaranteed rates of interest, or without any guarantees at all.

Table 5. Distribution of Gross Premiums, 2000–05

	Gross Premiums Percent			
	2000	2003	2004	2005
With profit contracts –nonlinked	88.1	83.4	82.3	75.7
Term risk	--	1.4	1.7	4.6
Unit linked insurance	...	5.1	6.6	8.8
Unit linked life insurance—with zero percent return option	2.6	1.7	0.9	1.6
Group pension insurance	9.2	8.4	8.5	9.3

Source: Danish Financial Supervisory Authority.

20. The sector remains susceptible to low interest rates, and also to other market risks, including equity prices and property prices. These factors place an important premium on sound risk management by life insurance institutions, and effective oversight by supervisors. Albeit several measures have been implemented to increase provisions and buffer capital, as well as hedging risk in the form of derivatives, this is an area that still needs to be closely monitored. The investment risk matched with the interest rate risk on liabilities still is a concern as mismatches poses a risk to the level of buffer capital.

21. The investment strategy has changed over time (Table 6). Until 1999, the proportion of shares in the investment portfolios was growing. After 1999, this changed to an increased bond portfolio. This development came even more through in 2001. In 2004, the mix between bonds and shares accounts for 61.7 percent and 13.8 percent, respectively. The return on investments fell substantially in the years 2001 and 2002. Due to the rise in equity prices in recent years, the investment returns increased in 2003, 2004, and 2005. In 2003, the profit on investments was above the high guaranteed rate of 4.5 percent, and 2004 showed the best investment profits during the last 5 year period. As the life insurance companies and pension funds are large institutional investors, situations could arise were the market would not be sufficiently liquid, if there was a sudden need for changes in the investment mix. This is most dominant for the equity market, since the bond market in Denmark is large and liquid. This would mainly be a problem in the event of solvency problems of one of the larger companies.

22. The return on investments have been quite volatile in recent years (Table 7). In 2005, the insurance companies and pension funds achieved a result before tax of over DKr 16 million, with the result on investments amounting to DKr 165 million. The results are the best during the recent five year period. The administration costs have been reduced from 6.49 percent in 2001 to 5.33 percent in 2005.

Table 6. Distribution of Investments of Life Insurance Companies and General Pension Funds, 2000–05

	2000		2002		2004		2005	
	Value	Percent of Total	Value	Percent of Total	Value	Percent of Total	Value	Percent of Total
Land and buildings	3,514	3.0	4,620	3.8	3,825	2.6	4,224	2.5
Investments in subsidiary and associated companies	10,785	9.1	6,179	5.1	8,440	5.8	19,644	11.8
Participating interests	36,630	30.9	14,700	12.2	19,974	13.8	25,113	15.0
Bonds	61,002	51.5	84,769	70.3	89,227	61.7	94,026	56.2
Interests in investment associations	5,692	4.8	7,962	6.6	18,981	13.1	14,773	8.8
Other investments	867	0.7	2,349	1.9	4,195	2.9	9,509	5.7
Total investments	118,490	100.0	120,579	100.0	144,643	100.0	167,289	100.0

Source: Danish Financial Supervisory Authority.

Table 7. Return on Investments for Life Insurance Companies and General Pension Funds, 2000–05

	2000	2001	2002	2003	2004	2005
Return on investments before tax	5.65	-1.63	1.77	6.86	10.40	14.25
Return on investments after tax	4.95	-1.20	1.71	6.05	9.11	12.46

Source: Danish Financial Supervisory Authority.

23. The owners and policyholders in life-insurance companies may have diverging interests regarding the distribution of profits. On the one hand, the owners may be interested in carrying the profit to equity capital, while on the other hand the policyholders may prefer distribution to policyholders. The life insurance companies and pension funds must set up rules for the return on equity. These rules generally comprise two elements, a return that is in line with the yield paid to policyholders, and a risk premium that must be reasonable in relation to the risk associated with providing equity capital. The actual profit to policyholders has been equal for all policyholders independent of the level of guaranteed returns.

Table 8. Return on Equity for Life Insurance Companies and General Pension Funds, 2000–05

	2000	2001	2002	2003	2004	2005
Return on equity before tax	4.11	-15.96	-12.68	19.66	17.59	17.82
Return on equity after tax	3.94	-14.31	-10.59	18.15	15.91	15.65

Source: Danish Financial Supervisory Authority.

Note: The ratio of profit before/after tax to average equity capital

24. The life insurance companies' and pensions funds' buffers against losses comprise: the collective bonus potential, the bonus potential related to benefits on premium-free policies, and the capital base. The two first buffers belong to the policyholders, while the capital base, comprising equity belongs to the owners of the company. In principle, the bonus potential related to benefits on premium-free policies cannot be regarded as an aggregate buffer for the entire company, as this bonus potential is related to the individual policy and can only be used to cover negative results for policies within the same portfolio.

25. The weighted average solvency ratio was 2.6 at the end of 2005 (Table 9). In 2004, half of the companies had a solvency ratio under this average. The companies with a solvency ratio less than 2.8 represent approximately 73 percent of the market, indicating that some of the largest companies have a solvency ratio below average. In 2005, the 10 percent of the companies with least capital had a solvency ratio below 1.5—none less than 1.2—and the 10 percent best capitalized companies had a solvency ratio exceeding 6.4.

Table 9. Buffer Capital, Weighted Average, 2000−05

	2000	2001	2002	2003	2004	2005
Solvency ratio in percent	4.2	2.4	2.2	2.6	2.7	2.6

Source: Danish Financial Supervisory Authority.

26. Four life insurers have not been able to meet the solvency requirements during the last five years. For all four life insurers the capital was successfully restored by restoration plans accepted by the DFSA. All four failures were due to losses on investments (decrease of equity prices and low interest rates) and were related to mismatch between interest rate sensitivity of assets and liabilities. All companies have continued their business and no direct losses were observed.

Sensitivity test

27. In 2000, the regulatory limit for investments in equities was raised to 70 percent of the technical provisions on the condition that the match between the assets and the liabilities of the industry should be improved. In June 2001, after negotiations with the industry, the DFSA introduced the red and yellow "traffic light" stress test scenarios for life insurers and pension funds. From end-2003, similar test scenarios were introduced in nonlife insurers. Companies and funds report the result of the stress tests biannually. The traffic light system supplements the required capital margin. At the end-2005, there were no life insurance companies or general pension funds in red light, but 6 companies in yellow light.

28. The red light scenario is a decrease of 12 percent in the price of stocks, a decrease of 8 percent in the price of real estate, and a change of the interest rate level of 0.7 percentage points. Credit risk and foreign exchange risks are stressed as well. If a company cannot meet the red scenario, the DFSA requires monthly reporting and the company in question is not allowed to increase its overall risk.

29. The yellow scenario is an early warning indicator. The yellow light scenario is a decrease of 30 percent in the price of stocks, a decrease of 12 percent in the price of real estate, and a change of the interest rate level of 1.0 percentage point. In case a company cannot meet the yellow scenario, the DFSA requires quarterly reporting.

Company pension funds, ATP, LD/SP

30. There are additional funded pension plans established by law, and these can also be characterized as private pension plans. The largest funded pension plan is the Labor Markets Supplementary Pension Scheme (ATP). There are also several private pension funds covering mandatory pension schemes. Company pension funds administer pension schemes for employees or a group of employees in one single firm or in a group of firms. According to the law, company pension must be autonomous legal entities segregated from the company where the beneficiaries (members) are employed. According to the law, pension liabilities must be fully funded. Three company pension funds for the telephone operator, TDC, accounts for more than half of the total assets of the company pension funds. The total assets of these company pension funds amounts to approximately € 5 billion (pension fund assets). The company pension funds cover 2 percent of the total pension assets in the Danish market.

31. The regulatory framework, the financial prudential supervision and the supervision practices for LD, ATP/SP and company pension funds are largely the same as those that apply to the insurance companies. The licensing procedures for company pension funds are also in line with the licensing procedures for insurance companies. LD and ATP/SP are also partly supervised by the Danish Ministry of Employment.

32. The number of company pension funds has been steadily decreasing for many years (Table 10). Only a few new funds have been established and old pension funds are discontinued. Some of the pension schemes established in company pension funds have also been transferred to life insurance companies. The schemes of the company pension funds are mostly defined benefit. However, three schemes are defined contribution. A large part of the funds are closed for new members.

Table 10. Number of Company Pension funds (legal entities) 2000–05

	2000	2001	2002	2003	2004	2005
Company pension funds	54	50	47	47	44	44

Source: Danish Financial Supervisory Authority.

33. In 2004, the company pension funds, in contrast to ATP, LD/SP, showed a negative result after taxes (Table 11). The negative result was caused by the pension risks due to a marked increase in the technical reserves, and paid contributions amounting to the double of the premiums paid. A lot of company pension funds are under liquidation and there are more passive than active members of these schemes.

34. The investment result was the best during the last five years. The bond portfolios have increased and amounted to 67 percent of total assets ultimo 2004. Equity investments have decreased and amounted to 15 percent ultimo 2004.

Table 11. Aggregate Balance Sheet and Income Statement for ATP, LD, AES, SP, and Company Pension Funds (CPF), Selected Items, 2004 (€ million)

€ m	ATP 2004	LD 2004	SP 2004	CPF 2004
Profit and loss account				
Gross premiums	898	0	-26	111
Net pension benefits	689	329	41	216
Net costs related to pension operations	19	5	28	5
Investment result	5,693	838	458	325
Net profit for the year	766	14	398	-105
Balance sheet				
Total assets	41,354	7,812	6,252	5,270

Source: Danish Financial Supervisory Authority.

35. These pension schemes have the same capital requirements as insurance companies and general insurance funds, but the possibilities of easing the regulation for the small pension funds with less than 100 members, as set out in Directive 2003/41/EC, have been implemented to the full extent. By end-2004, the total company pension funds had a solvency ratio of 6, meaning a buffer capital is 6 times the minimum capital requirements. At end-2004, five company pension funds were in red light and eight companies were in yellow light in the DFSA's traffic light stress test.

Nonlife insurance

36. There are currently 124 nonlife insurance companies in the Danish market (Table 12). The number of companies has declined during the last five years, but there is still room for further consolidation. Exits from the market were mainly due to normal changes in market conditions, including mergers. A number of small nonlife insurers have recently merged and some are planning to do so in near future.

Table 12. Number of Nonlife Insurance Companies, 2000–05

	2000	2001	2002	2003	2004	2005
Nonlife insurance companies	136	131	128	124	125	124

Source: Danish Financial Supervisory Authority.

37. During the last five years, one nonlife insurers failed and one went into run-off. The reason for one of the nonlife insurers failing in 2001 were claims after September 11. A restoration plan is running to wind up the company, and no direct losses are observed. The other direct nonlife insurer failed for a number of reasons: mispricing, underpricing,

excessive overheads, inadequate reinsurance, decrease of equity prices, and poor management. The company is under forced liquidation by the court. No direct losses were observed for private costumers, as the guarantee fund has covered the losses for these costumers. The cost for the guarantee fund is estimated to € 16 million.

38. The nonlife market is also highly concentrated (Table 13). It is dominated by four insurers, Tryg, Topdanmark, Codan, and Alm. Brand. Increasing competition is seen in the Danish market from foreign insurers. In 2003, 19 foreign insurers chose to be member of *The Danish Insurance Association* (Forsikring & Pension). However, foreign insurers overall market share is still limited for the private lines of business.

Table 13. Market Concentration Measured by Gross Premiums, 2003–05

	2003	2004	2005
Tryg	22.4	22.1	20.9
Topdanmark	18.9	19.7	19.0
Codan	13.8	13.4	12.9
Alm. Brand	10.3	10.2	9.4
Sygeforsikringen “danmark”	4.9	4.7	4.4
Top 5 total	**70.3**	**70.1**	**66.7**
International Health Insurance	3.3	3.3	3.7
Alka	3.9	3.7	3.3
Lærerstandens Brandforsikring	3.2	3.2	3.3
Kommune Forsikring	2.9	3.3	3.1
Nykredit	3.5	3.0	2.8
Top 10 total	**87.1**	**86.6**	**82.9**

Source: Danish Financial Supervisory Authority.

39. The total nonlife market is small representing 0.46 percent of the world nonlife insurance market. The market is mainly one of personal line business, motor and household insurance, representing approximately 70 percent of the nonlife market (Table 14). The market is not thought to be vulnerable to the withdrawal of one of the major suppliers, as this type of business, characterized by homogeneity of products, can be supplied by market entrants from other countries.

Table 14. Nonlife Insurance Premiums by Class of Business, 2004 and 2005

	Premiums written			
	2004		2005	
	Gross	Net	Gross	Net
Commercial insurance	32.1	28.1	32.4	28.9
Property and casualty	18.7	20.3	18.9	20.3
Personal accident insurance	15.6	15.7	16.6	16.4
Motor insurance	26.6	29.6	27.0	30.0
Total direct business	94.3	94.3	96.0	96.1
Total indirect business	5.7	5.7	4.0	3.9
Total	**100.0**	**100.0**	**100.0**	**100.0**

Source: Danish Financial Supervisory Authority.

40. The financial results suggest that premium rates are sufficient to allow an adequate underwriting profit across all participants. In 2004, net profit of the nonlife insurance companies increased by 11.1 percent and the technical result doubled compared to 2003. The growth in premiums mainly stems from risk adjustment of premiums due to more sophisticated risk assessments in the commercial market, but also from increased cover due to regulatory requirements (e.g., workers compensation). The return on equity increased further from 14.5 percent in 2004 to 17.0 percent in 2005 (Table 15).

Table 15. Return on Equity for Nonlife Insurance Companies, 2000–05

	2000	2001	2002	2003	2004	2005
Return on equity after tax	15.5	5.6	0.9	14.1	14.5	17.0

Source: Danish Financial Supervisory Authority.

Note: The ratio of profit after tax to average equity capital

41. Both the loss ratio and the expense ratio of the nonlife insurers have decreased the last two years (Table 16). The combined ratio is now below 100, which makes profit on investments a direct return on capital.

Table 16. Loss and Expense Ratio for Nonlife Insurance Companies, 2000–05

	2000	2001	2002	2003	2004	2005
Net claims ratio	83.1	78.8	80.3	71.2	74.5	80.1
Net expenses	25.3	23.5	22.8	21.7	17.5	17.3
Net operational ratio	108.4	100.9	106.1	97.2	94.1	91.6

Source: Danish Finanancial Supervisory Authority.

42. The improved situation also allows nonlife insurance companies to have a more risk sensitive portfolio, with a larger part of the portfolio in the stock market (Table 17). The investment mix has given higher yields the last two years. At end-2005, only one nonlife insurance company was in red light and no companies in yellow light. The company in red light is in run off.

Table 17. Investments of Nonlife Insurance Companies, 2000, 2004, and 2005

	2002		2004		2005	
	Value € Million	Percent of Total	Value € Million	Percent of Total	Value € Million	Percent of Total
Land and buildings	325	3,2	288	2,2	230	1.5
Investments in subsidiary and associated companies	3.481	34,5	3.803	28,5	4371	28.7
Participating interests	1.047	10,4	758	5,7	997	6.5
Bonds	4.853	48,1	7.734	58,0	716	4.7
Interests in investment associations	213	2,1	422	3,2	8175	53.7
Other investments	180	1,8	334	2,5	738	4.8
Total investments	**10.099**	**100,0**	**13.338**	**100,0**	**15226**	**100.0**

Source: Danish Financial Supervisory Authority.

43. The solvency ratio has been stable for the last five years. In 2004, half of the nonlife insurance companies had a solvency ratio of more than 5 according to the current minimum capital requirements. In 2005, the solvency ratio increased marginally. The 10 percent of the companies with least capital had a solvency ratio below 1.9, while the 10 percent of the companies being best capitalized had a solvency ratio exceeding 13.7. Effective January 1, 2007, the minimum capital requirement will increase to the equivalent of the requirements in EU Solvency I Directive. The capital requirement may be reduced for mutual insurance companies, which fulfill certain conditions, and after application, the DFSA may extend the time limit to January 1, 2009. So far no companies have been granted an exemption. There are 6 limited companies and 22 mutual companies, which at the moment do not fulfill these new minimum capital requirements; however a number of these will qualify for the exemptions according to the Directive. During 2005, the DFSA will ask the companies to report on how they plan to fulfill the stricter requirements. Market participants are also anticipating changes to the capital levels in future years, when the EU continues to make progress on the insurance capital adequacy (Solvency II). Minimum levels of regulatory capital are also likely to increase under Solvency II.

Reinsurance

44. Reinsurance cover is mainly provided from the international reinsurance market. There are five pure Danish reinsurance companies, which primarily reinsure risks originating from the group (captives). The direct insurers in Denmark typically buy reinsurance cover from foreign reinsurers in the international reinsurance market. In 2004, gross reinsurance premiums of companies on the Danish market amounted to DKr 2.5 billion. Gross reinsurance premiums of the largest reinsurer—GE Frankona—amounted to DKr 1.2 billion. Of the total insurance business of GE Frankona, direct insurance accounts for more than half. A number of large companies in Denmark formed captive insurance companies in 2004. This tendency has continued in 2005.

D. Principle-by-Principle Assessment

Conditions for Effective Insurance Supervision	
Principle 1.	**Conditions for effective insurance supervision** Insurance supervision relies upon a policy, institutional and legal framework for financial sector supervision a well developed and effective financial market infrastructure efficient financial markets.
Description	The government's economic strategy for sustainable economic growth addresses financial sector stability. Well-functioning money and securities markets exist to support the availability of both long-term and short-term investment opportunities. Furthermore, an annual contract, concluded between Finanstilsynet (DFSA) and the Ministry for Economic and Business Affairs (MoEB), addresses the overall objectives of effective supervision. This contract is published as an annex to the annual business statement of the DFSA. The legal framework is well defined, constantly updated when necessary, and publicly disclosed.

	Regulation is based on the Financial Business Act (FBA), executive orders (EO), and guidelines. The latter are not legally binding but express how the DFSA expects the FBA and the EO to be understood and applied by the businesses. The judicial system in Denmark fulfils all criteria for a sound and independent court system. It is fully separated from the lawmaking and administrative authorities. The legal process is public, and there is at least one possibility for appeal. Decisions taken at the administrative level can be brought to court. Alternative dispute mechanisms in the financial area will normally be headed by a professional judge. Auditing and actuarial standards are in line with international practice and publicly available. Accounting standards are in line with international accounting and financial reporting standards (IAS/ IFRS). Danish insurance companies have already adopted to a measurement of market values for assets and liabilities. Therefore, the introduction of IFRS is not expected to create additional challenges for the DFSA. Certified auditors have to pass relevant exams. They are subject to ethical standards. Appointed actuaries (life insurers and pension funds only) have to prove appropriate. Since the DFSA does not issue regulation on the behavior or qualification of functionaries below the senior management, a rather broad provision exists in section 71(1) of the FBA and requires regulated entities to have good administrative and accounting practices in place. Section 108 (2) and (7) of FBA addresses the position of an actuary within the company. Ethical standards for accountants, actuaries and auditors have been developed by the professional associations and are published. Basic economic, financial, and social statistics are published by the Government Statistical Office (Danmarks Statistik), the Central Bank (Danmarks Nationalbank) and a number of other bodies. These statistics are accessible to the public. Markets exist and they are supervised by the DFSA.
Assessment	Observed
Comments	Conditions for effective supervision exist. All professional resources are available and of high standards. The market infrastructure allows for an efficient management of the sector. A wide range of operational services are available to insurance undertakings and allows them to focus on technical related aspects of the business. The regulation is very principle-based but allows for risk-based supervision. Specifically, the requirements in section 71 FBA in conjunction with the relevant guideline 9680 guide a company to consider measures without defining minimum standards applicable. Therefore, some more specific rule based requirements should be applicable to all companies.
The Supervisory System	
Principle 2.	**Supervisory objectives** The principal objectives of insurance supervision are clearly defined.
Description	The objectives of insurance supervision are clearly defined in ensuring that supervised undertakings do comply with the FBA. The DFSA articulates and publishes its self-understanding in their statement on mission, vision, and values of Finanstilsynet. This statement aims to ensure that market participants and staff of the DFSA share a clear understanding of the objectives and direction of supervision. The objectives of the DFSA are part of a performance contract concluded with the MoEB. This contract however, is not legally binding but rather a declaration of pre-agreed intentions of Finanstilsynet. The Mission of Finanstilsynet reflects on the contribution to the MoEB and on conditions for economic growth. The DFSA also wants to contribute by assisting in preserving confidence in the Danish financial sector by citizens and companies in Denmark and abroad.

	In its vision statement, the DFSA aims to contribute to the best conditions for growth in Europe in order to make Denmark an attractive place to live, work and run a company. The DFSA also applies a cost-benefit consideration of regulations. It wants to contribute to market confidence at the lowest possible cost of supervision. During the assessment, there has been no evidence that sufficient supervisory activity has been sacrificed in order to be a low-cost supervisor. The DFSA reflects in its annual report reports on compliance with the mission, vision, performance contract, and on the rulings of the year. The prudential regulation is constantly updated and provides no significant contradicting objectives for effective supervision.
Assessment	Observed
Comments	None
Principle 3.	**Supervisory authority** The supervisory authority: has adequate powers, legal protection and financial resources to exercise its functions and powers is operationally independent and accountable in the exercise of its functions and powers hires, hires, trains and maintains sufficient staff with high professional standards treats confidential information appropriately.
Description	**Legal framework** Legislation identifies the DFSA as the principle authority to supervise insurance companies in section 344 (1) of FBA. Finanstilsynet also has the authority to issue EOs and guidelines to ensure further development and compliance with the FBA. The effective discharge of supervision is referred to in section 350 of FBA. Finanstilsynet is able to order that a financial undertaking take the measures necessary within a time limit specified, if the financial position of the undertaking has deteriorated and that the interests of the depositors, the insured parties, are at risk, or if there is a significant risk that the financial position of the undertaking will develop so that the undertaking loses its license. Where the measures ordered have not been taken within the time limit specified, the Danish FSA may withdraw the undertaking's license. The legislation and prudential regulation for insurance and pension funds does not automatically cover Greenland. The legislation and regulation is entered into force separately in Greenland approximately one year after the changes enter into force in Denmark. The Faroe Islands have separate legislation, regulation, and supervision. **Independence** The DFSA has been set up as an independent authority for all financial sectors. The most senior decision making body is the Financial Business Council (FBC) or the Danish Securities Council (DSC). EO 1363 defines which matters should be brought to the attention of the respective councils. Section 4 requires the FBC to decide on matters of principle nature, significant financial consequences for undertakings, and prior to issuing regulation. In case of ties, the chairman of the council has the casting vote. If an issue is under the responsibility of one of the two councils, the Minister of Economic and Business Affairs cannot give instructions or dictate specific actions. However, since the DFSA is an institution under the MoEB, the Minister is the ultimate superior. The FBA also allows the MoEB to issue further regulation on procedures for Finanstilsynet. The Minister may also give instructions regarding other matters to the DFSA, such as examining specific areas or entities. In practice, the Minister asks questions regarding specific cases and approve the annual performance contract, which lays down the goals for supervisory activities in

	the following year, including investigation work. The contract states, that the DFSA acts independently within the limits of the contract and legislation. The budget of the DFSA is determined annually by the government in the fiscal budget law—subject to approval by the legislature. Regulation concerning the financing of the DFSA is laid down in section 360 to section 370 of FBA. There are no special processes for the appointment and dismissal of the head of the DFSA other than those applicable to any senior civil servant. There is not any regulation that demands public disclosure. There is no indication that executive or juridical branches have interfered in the performance of supervisory responsibilities. The decisions of the DFSA are published once they have been accepted by the FBC. Also, issued guidelines should support that undertakings are aware of how the DFSA expects the business to be conducted and managed. Finanstilsynet consults with market participants prior making material changes to the insurance legislation. Warnings, decisions, and other relevant matters are disclosed on its web page (http://www.ftnet.dk/sw99.asp) and in its annual reports (http://finanstilsynet.inforce.dk/sw1237.asp) subject to confidentiality considerations, cf section 354 of FBA. **Powers** The DFSA has adequate powers to impose immediate sanctions to protect policyholders. Section 373ff provides a sufficient range of options to act accordingly. **Financial resources** The FBA stipulates that the costs of supervision shall be allocated to the institutions under supervision at the end of the fiscal year. The legislature grants the DFSA an appropriation at the beginning of the year and Finanstilsynet distributes the costs and interests among the various groups of institutions at the end of the year as described by the FBA. The allocation shall be carried out by the DFSA, but is reviewed by the executive branches according to the regular government budget appropriation procedures, which set the limits on the DFSA's total resources. The DFSA endeavors to recruit sufficient and qualified staff to perform its supervisory task. The remuneration system for civil servants applies, which does allow for some flexibility to attract staff with special expertise. **Human resource and legal protection** A large part of the staff are university graduates. There is no evidence of shortfall of qualifications. Decisions made by staff are on behalf of the DFSA. Any challenge by legal action would have to address the DFSA, unless the civil servant has acted with gross negligence or with purpose. The public authority will be held responsible for the unlawful and negligent conduct of its civil servants—unless there is gross negligence or purpose on behalf of the civil servant—and can in some instances hold the respective staff liable subsequently. *The DFSA has also issued a set of ethical rules and guidelines applying to the employees. These guidelines should avoid potential conflicts of interest.* Section 344 (4) FBA allows Finanstilsynet to contract external resources. **Confidentiality** The DFSA maintains high measures for the protection of confidential information in its possession. Section 354 of FBA requires employees and other parties acting on behalf of the DFSA to respect confidentiality requirements. At the same time sufficient provisions are granted to enable the DFSA to share information with other domestic agencies and relevant supervisors.
Assessment	Largely observed

Comments	The DFSA has to agree its budget with the MoEB although the expenses of the agency are covered by fees of the supervised entities. The DFSA is also subject to an annual budget reduction program of the public sector. There is a possibility that resources could be allocated to regulation to the disadvantage of supervisory activity. The possible interference of the executive branches should be limited or restricted.
Principle 4.	**Supervisory process** The supervisory authority conducts its functions in a transparent and accountable manner.
Description	The supervisory process is based on defined processes, which are known to and followed by the staff. A summary of the activities is published in the DFSA's annual reports. The regulation is updated regularly and publicly available. The DFSA applies a risk based approach and applies supervisory activity in response to the outcome of the individual risk assessment of each company. Equal treatment is provided in accordance with Danish Administrative Law. Supervisory process are defined and laid out in manuals. Dedicated teams ensure that the processes are applied in a consistent manner. The levels of authorities are clearly defined and understood by the DFSA staff. Unauthorized decisions could be legitimized subsequently if needed. The administrative decisions of the DFSA can be subject to substantive judicial review without impeding the ability of the supervisory authority to make timely interventions. According to section 372 (1) of the FBA, decisions made by Finanstilsynet and/or the Danish Commerce and Companies Agency under this Act or regulations issued pursuant to this Act may be brought before the Company Appeals Board by the person against whom the decision is directed. The Business Appeal Board may decide that the filing of a case has delaying effect. According to the DFSA, this does not compromise effective supervision. The Appeals Board does not make many decisions concerning delaying measures. A decision, which led to a transfer of portfolio or liquidation, remains registered with the company until the appeal process is finished. Finanstilsynet publishes an annual report on the conduct of its policies and activities, objectives, and performance. The DFSA provides and publishes information on recent developments and releases key figures in press releases on a bi-annual basis. The MoEB also receives reports according to section 353 (1) of FBA.
Assessment	Observed
Comments	None.
Principle 5.	**Supervisory cooperation and information sharing** The supervisory authority cooperates and shares information with other relevant supervisors subject to confidentiality requirements.
Description	The DFSA is able to share information with other relevant supervisory authorities subject to confidentiality requirements. Although information sharing does not require respective agreements, there are some in place to set out the framework and procedures for the information exchange process. The agreements to support co-operation and information sharing within EU/EEA are signed by the DFSA: The Sienna Protocol, dated October 30, 1997, the Helsinki Protocol, dated May 11, 2000, and guidelines for Co-ordination Committees, February 2005, issued by CEIOPS. Other agreements include: The Memorandum of Understanding (MoU) between the Estonian Financial Supervision Authority and The Danish Financial Supervisory Authority (dated August 2002). The Memorandum of Understanding (MoU) between the Latvian Financial and Capital Markets Commission and The Danish Financial Supervisory Authority (dated August 2002). Memorandum of Understanding between Kredittilsynet in Norge (Norway), Finansinspektionen in Sverige (Sweden), Finansinspektionen in Finland, Finanstilsynet in Island (Iceland), and

	Finanstilsynet in Danmark (dated 2000). Finanstilsynet has established internal procedures for handling cases of cross-border activities and foreign branches. These procedures are in conformity with the above mentioned protocols. The agreements on cooperation and exchange of information with regard to supervision of insurance undertakings and insurance groups contain the procedures for exchange of information between supervisory authorities with regard to all aspects of supervision of insurance undertakings. Statistical information on the activities undertaken by Danish insurance undertakings in other European Union (EU) Member States shall be provided to the host supervisory authority of that member state (amount of premiums) in accordance with Article 43 of Directive 92/49/EEC and 49 of Directive 2002/83/EC. A regular annual reporting of all such activities takes place in accordance with 5.4 in the Siena Protocol. There is no reciprocity requirement in the legal provisions. The DFSA may require that the information given by Finanstilsynet to other supervisory authorities may only be used for supervisory purposes as mentioned in the FBA. The information given shall be treated as confidential by the receiver. Information that the DFSA has received from foreign supervisory authorities may only be passed on with the consent of the authority concerned and only for the purposes for which consent is given. According to the procedures prescribed in the EU Directives on direct insurance business, the DFSA may order an insurance company to cease providing insurance business in Denmark if the company is guilty of gross or persistent violation of its obligations pursuant to other laws and regulations in force in Denmark.
Assessment	Observed.
Comments	None
The Supervised Entity	
Principle 6.	**Licensing** An insurer must be licensed before it can operate within a jurisdiction. The requirements for licensing are clear, objective and public.
Description	Licensing procedures and requirements are set out in the FBA. Applicants will be provided with all relevant information about the licensing process and its requirements. A definition of what is defined as an insurance company is given in section 11 (1). Undertakings, which carry out insurance activities shall be licensed as insurance companies. The legal entity should be, according to FBA section 12, either a limited company, a mutual company, or a lateral pension fund. The responsibility for granting a license lies with the DFSA. Regulations regarding board members and senior management are defined in the FBA. Auditors and appointed actuaries have to meet professional standards. Finanstilsynet has issued "Guidelines on requirements in financial legislation for fitness and propriety of members of boards of management and boards of directors and requirements for approval of owners of qualifying interests. Applicants have to provide the DFSA with detailed information about the business plan, risk management, and control systems. According to Executive Order no. 1399 section 15, the operating plan shall cover the first three accounting years of the company and it shall be divided into quarters. If the first financial statements are submitted for a period of less than one year, the operating plan shall cover this period and the three subsequent accounting years. The operating

	plan shall include—among other things—an opening balance, the expected accounting results, a report on the intended reinsurance programs, and a report on the investment policy of the insurance company. The DFSA requires in accordance with section 71 (1) FBA that a financial undertaking shall have good administrative and accounting practices, written procedures for all significant areas of activity, full internal control procedures, adequate information technology (IT) control and security measures, and the resources necessary for proper carrying out of its activities, and use these appropriately. An application for a license for insurance class 10 (third-party motor liability) shall be accompanied by information on whom the company will appoint as claims representative in each of the other countries in the EU. Finanstilsynet supervises domestic insurance companies and subsidiaries in Denmark of foreign insurance companies in accordance with section 346 FBA. All branches of Danish insurance companies established abroad will be supervised by the DFSA as the home country supervisor. There is currently one branch to be supervised in that respect. The DFSA has implemented the provisions in the EU-directives regarding the sharing of supervisory tasks and cooperation between home supervisors and host supervisors. In addition, a general MoU between all the Nordic supervisory authorities, and specific MoU's on cooperation with respect to individual insurance groups or conglomerates have been established. Cf. also ICP 17. A foreign insurer can carry on business in Denmark by way of a local branch or subsidiary, or on a services basis only. Cf. FBA section 30, 31, and 37 above in ICP b and c. The legal framework for licensing of a foreign insurer is found in FBA section 30–37. The DFSA requires to receive information from the supervisory authorities of the home country and a declaration that the activities planned are covered by the company's license in the home country. The FBA also requires that life and nonlife activities be conducted in separate entities. Life assurance companies may, however, carry out activities within insurance classes 1 and 2, cf. annex 7, and may carry out reinsurance of life assurance and other insurance. According to Executive Order no. 1399, the DFSA shall assess whether an insurance company has adequate capital in order to obtain a license. If however, the submitted plans allow for reasonable doubts regarding the financial soundness of the operation and business projections, then Finanstilsynet can either require additional capital or decide not to grant a license. A refusal to grant a license will be addressed to the applicant within a six month period. Danish law also entitles the applicant to an explanation what lead to the decision. The DFSA grants a license on the condition that the insurance company shall submit quarterly financial statements to the DFSA in such a form as to make it immediately possible to compare the actual results and compare them to the submitted operating plan.
Assessment	Largely Observed
Comments	The DFSA pays specific attention to the licensing process. The risk-based approach requires a tighter and rather rule-based supervision within the first, say three, years of the newly established businesses. There after, the ongoing supervisory process does not demand the same amount of detailed operating plans. As also Finanstilsynet has distinctive rules for the supervision of new entities, it also should require the suitability for auditors and actuaries to be assessed.

Principle 7.	**Suitability of persons** The significant owners, board members, senior management, auditors and actuaries of an insurer are fit and proper to fulfill their roles. This requires that they possess the appropriate integrity, competency, experience and qualifications.
Description	Where the FBA recognizes key functions in insurance company as actuaries and auditors, there are no specific requirements other than requirements regarding their professional ability and academic qualifications to the individuals performing those duties. The position as actuary shall not be compatible with the position as a member of senior management or the board of directors of the insurer according to section 108 (2) of the FBA. The DFSA does not assess the fitness and propriety of auditors and actuaries. However, actuaries and auditors must fulfill certain requirements regarding education and practical experience. The professional bodies of both actuaries and auditors issue standards of professional conduct. Since Finanstilsynet does not assess the fitness and propriety of auditors and actuaries, Finanstilsynet do not rely on standards from professional bodies. The dominant management structure in Danish insurance companies is based on a two-tier system. There is a board of directors representing the shareholders. The board contracts an executive team, the senior management (board of management), which is in charge of managing the business. Technically, the senior management reports to the board of directors and the responsibilities of the senior management are carried out jointly. It is the philosophy of the DFSA to hold the senior management, namely the executives, registered for the company, responsible for the fulfillment of responsibilities. FBA section 64 (1) identifies that a member of the board of directors and the senior management of a financial undertaking, shall have adequate experience in carrying out the duties and responsibilities of such a position. Consequently, all requirements on the propriety of individuals are restricted to this senior management. Finanstilsynet would not disqualify the appointment of an auditor or actuary. Nor could the DFSA disqualify a member of the board. In accordance with section 62 (1) of the FBA, the DFSA may order a financial undertaking or holding company to follow specific guidelines and withdraw the owners' voting rights, if the owner of a qualified holding acts contrary to appropriate operation of a financial undertaking or a financial holding company. According to FBA section 351(1), the DFSA may require a financial undertaking to remove a member of senior management within a time limit specified by Finanstilsynet, if the member does not fulfill the fit and proper requirements in section 64(2) of the FBA. Section 199(4) FBA allows the DFSA to dismiss an auditor, who is deemed clearly unfit to perform his duties and appoint another auditor, who shall act until a new auditor can be elected. The DFSA exchanges information with other authorities inside and outside its jurisdiction where this is deemed to be necessary to assess the fitness and propriety. Finanstilsynet has described the exchange of information with other authorities in an internal procedure.
Assessment	Largely observed
Comments	The DFSA bases its system to assess the appropriateness of key functionaries on the assumption that is the core responsibility of the senior management to ensure adequate personnel to be assigned to relevant tasks in the supervised companies. The attitude on fit and proper is applied consistently by Finanstilsynet. There was no evidence that this has led to severe problems so far. However, that might well be justified by the limited size of the market.

Principle 8.	**Changes in control and portfolio transfers** The supervisory authority approves or rejects proposals to acquire significant ownership or any other interest in an insurer that results in that person, directly or indirectly, alone or with an associate, exercising control over the insurer. The supervisory authority approves the portfolio transfer or merger of insurance business.
Description	**Changes in control:** Section 5(3), (4), (5), and (6) of FBA defines ”qualifying interest” as direct or indirect ownership of 10 percent or more of the capital or voting rights or ownership of an interest, which provides the opportunity for exercising significant influence on the management of the insurer. Section 61 of FBA describes the regulation of “qualifying interests”. Potential controlling owners have to apply for approval for the acquisition. Section 61 of FBA states that any natural or legal person planning directly or indirectly to acquire a qualifying interest of 10 percent or more, in a financial undertaking or a financial holding company shall notify the DFSA in advance, and the DFSA shall approve the acquisition planned. The same shall apply to an increase in the qualifying interest which, after the acquisition, results in the interest equaling or exceeding a limit of, respectively, 20 percent, 33 percent or 50 percent of the share capital or voting rights, or results in the financial undertaking or the financial holding company becoming a subsidiary undertaking. According to section FBA section 61 (2), the DFSA shall only approve an acquisition or increase of the interest, when such approval is not contrary to ensuring appropriate operation of the financial undertaking. Finanstilsynet can approve or refuse a projected acquisition. Where owners of capital holding in an undertaking act contrary to appropriate operation, Finanstilsynet may order the undertaking to follow specific guidelines or withdraw the voting rights of those owners. Section 347 of FBA describes the general obligation to provide the DFSA with all necessary information. Financial undertakings and financial holding companies shall provide Finanstilsynet with such information as is necessary for the performance of Finanstilsynet's duties. **Portfolio transfer:** According to section 204 (1), a financial undertaking may not, without the permission of the Minister of Economic and Business Affairs, be amalgamated with another financial undertaking or a specific business function of another financial undertaking. This authority is delegated to Finanstilsynet through an executive order. The same applies when the continuing undertaking is a foreign undertaking.
Assessment	Observed
Comments	None
Principle 9.	**Corporate governance** The corporate governance framework recognizes and protects rights of all interested parties. The supervisory authority requires compliance with all applicable corporate governance standards.
Description	Regulations on corporate governance are covered by the Danish Public Companies Act, the FBA, and a guidance note. FBA stipulates that all sections relevant to corporate governance laid out in the public companies act are also binding for nonlisted companies and mutual insurance companies. Corporate governance is regulated in sections 70 and 71 FBA. Compliance is verified by the auditor and by the supervisor during on-site inspections. The Danish Public Companies Act chapter 9 and the general articles of association for insurance companies set out the responsibility

	of the board of directors. Pursuant to this, the board of directors has the responsibility for the undertaking's activities and business management, and must ensure a satisfactory organization of the undertaking's activities, and ensure that the accounts and asset management are subject to satisfactory controls. According to the FBA, Finanstilsynet shall ensure that supervised undertakings operate in an appropriate and proper manner in accordance with law and provisions issued pursuant to law and with the intentions underlying the establishment of the undertaking, its purpose and articles of association. That includes good administrative and accounting practices, written procedures for all significant areas of activity, full internal control procedures, adequate IT control and security measures, and the resources necessary and used appropriately for proper carrying out of its activities. The DFSA has issued guidelines No 9680 to interpret FBA section 70 and section 71. The guidelines are an important part of Finanstilsynet's inspections. Reviews and assessments related to an undertaking's strategy, corporate governance, and internal controls are key elements during on-site inspections performed by Finanstilsynet. The inspection manual describes the DFSA's practices for conducting on-site inspections and verifying FBA section 70 and 71. Finanstilsynet also reviews the audit records (long form audit minutes) and auditor's report in the annual report to verify if the undertaking has implemented or taken action on issues noted by the auditor in either the report or records (the audit minutes). The overall general rule on the responsibility of the board of directors is laid dawn in The Danish Public Companies Act section 54. The obligations for the board of directors to establish policies and strategies, the means of attaining them, and procedures for monitoring and evaluating the progress toward them are laid down in section 108 of the FBA. The Danish Public Companies Act, the FBA, and the guidelines, require the board of directors to establish audit functions, actuarial functions, and in general maintain strong internal controls. Remuneration policy is not regulated nor has the senior management to appoint a compliance function. The appointed actuary is part of the supervisory process and can demand access to the board.
Assessment	Observed
Comments	None
Principle 10.	**Internal control** The supervisory authority requires insurers to have in place internal controls that are adequate for the nature and scale of the business. The oversight and reporting systems allow the board and management to monitor and control the operations.
Description	The board of directors must ensure that the administration of the undertaking is adequate in all respects. Guideline No. 9680 has been issued to interpret section 71 FBA and elaborates on internal controls and procedures. The application of the guidelines will be assessed during on-site inspections. In a Danish financial undertaking, the internal audit handles part of the financial audit. In case an internal audit function is established, the financial audit task is divided between the internal and the external auditors. The division of labor between the internal and the external auditors shall be specified in an agreement approved by the board. According to the executive order, external auditors shall in the auditors report relating to the annual report, for instance, state whether the undertaking's administrative and accounting practices, including general business procedures and internal control procedures, are adequately planed and executed.

	If complete segregation of duties is not possible, this must be taken into account in the preparation of guidelines and procedures and in the planning of internal controls. The appointed actuary must have access to all information that is considered necessary for the execution of his or her duties, including the minutes of meetings of the board of directors. In connection with the adoption by the board of directors of the annual financial statements, the appointed actuary shall prepare a written report to the board of directors. The report to the board of directors shall contain all essential conclusions, which are stated in the actuary's report to the DFSA regarding the financial statements for the year to which the report pertains and which are of relevance to the presentation of accounts. According to section 108 of the FBA, the appointed actuary shall ensure that the undertaking complies with its technical assumptions, etc. The actuary shall, in this connection, review the actuarial contents of the undertaking's activities and material in general, including marketing material and bonus projections, and ensure that the technical basis etc. complies with the law at any time. During on-site inspections, the DFSA will have separate meetings with the appointed actuary. An internal audit function is required for larger undertakings and shall report to the board of directors. According to section 4 of Executive Order No. 1324, the external auditors shall prepare and maintain long form audit minutes to be used by the board of directors. If the board of directors decides to outsource insurance activities, the board of directors shall lay down guidelines for how the external supplier shall handle the outsourced activities. The guidelines shall ensure that the activities are handled adequately and that the undertaking's policies and strategies for the activities are observed. The guidelines shall further ensure that the board of directors together with the supplier lay down procedures, which the board of directors subsequently can monitor. It is the responsibility of the board of directors that outsourced activities comply with the guidelines laid down by the board of directors and in are handled in accordance with the FBA and that the reporting procedures are adequate, so that the reporting is suitable for ensuring that the guidelines, and thus the legislation, are met. The board of directors shall regularly monitor that their guidelines are observed and evaluate the handling of the activities. Insurance companies with more than 50 employees and gross premium income in excess of DKr 2 billion, and in addition for life-insurance if they have total gross premiums in excess of DKr 30 billion, are required to have an internal audit function. The board of directors of smaller entities should consider establishing this function on a voluntary basis. For undertakings with internal audit, the external auditors' report related to the annual report shall state whether: (i) the tasks agreed upon in accordance with the audit agreement have been carried out, and whether the internal auditors perform their duties in a satisfactory manner, and (ii) the external auditors concur with the audit book comments prepared by the internal auditors for the accounting year, and, where this is not the case, the cause of the disagreement.
Assessment	Largely observed
Comments	The requirements to establish internal audit functions should be made compulsory for smaller companies. Guideline 9680 does not define clearly enough what Finanstilsynet requires in the area of internal control. As the guideline does not expand on requirements from section 71 FBA, the subsequent control procedure may not cover all relevant issues. The importance of the function requires an executive order.
Ongoing Supervision	
Principle 11.	**Market analysis** Making use of all available sources, the supervisory authority monitors and analyses all factors that may have an impact on insurers and insurance markets. It draws the conclusions and takes action as appropriate.

Description	Regular analyses carried out by the DFSA focus on individual insurers and on different sub-sectors of the insurance market—ratings, analysis of general developments in the life and nonlife sectors, and stress testing. Macroeconomic surveillance in the context of the insurance sector is largely limited to financial markets data. Finanstilsynet contributes to the preparation of a Financial Stability Report on an European level of the insurance and occupational pension fund sector on a semi-annual basis. Finanstilsynet currently identifies the vulnerability of individual companies and aggregates to market scale. The analysis is mostly quantitative, based on reports from the companies and includes reporting on the two stress test scenarios. Information obtained during meetings with the companies and professional associations is also used as input for analysis. Both the DFSA and the Danish Insurance Association publish aggregated data on developments in the insurance industry on their respective websites and to a lesser extent also some financial markets data of relevance to the insurance sector. The DFSA requires systematic reporting from all insurance companies subject to supervision. The core of the reporting system is the biannual electronic reporting of accounting figures as well as reports on the two stress test scenarios from all companies subject to supervision. On an ad hoc basis, Finanstilsynet also requires the companies to submit extraordinary reports on subjects of immediate importance, e.g., on the use of derivatives in the life insurance industry. The DFSA primarily monitors trends within the insurance sector and in the financial markets. Currently most information is derived out of the aggregation of company related data. That does not address some issues which could well affect future stability and performance of the sector. Information about legislative trends, macro-economic information, e.g., on inflation, capital markets, should be obtained in a structured manner, and the relevant impact that could have on supervised entities should be considered. Also, trends within the domestic economy which influence the portfolio of insurance companies should be included.
Assessment	Observed
Comments	Finanstilsynet should ideally enlarge its activities on market analysis and obtain information which would enable a forecast of market trends and allow for a projection of potential impacts for the sector.
Principle 12.	**Reporting to supervisors and off-site monitoring** The supervisory authority receives necessary information to conduct effective off-site monitoring and to evaluate the condition of each insurer as well as the insurance market.
Description	The FBA requires the submission of annual accounts and reports, actuarial reports (mandatory only for life insurer), insurance provisions, registered assets, as well as other information to Finanstilsynet. The DFSA can request all information, which is necessary for the performance of its duties. Information on financial performance is submitted on a bi-annual basis. FBA section 193–198 sets some general requirements regarding annual reports and auditing. Detailed regulations are set in Executive Order no. 1406. All insurers are subject to the same reporting requirements. Reporting requirements are set in the law or in relevant regulations. For each report, the requirements define whether the reporting has to be on a solo basis or on a group-wide basis. There are no specific requirements that the insurer reports on their outsourced functions unless the company experiences problems in that area. Finanstilsynet laid down regulations in EO1406 on consolidated financial statements, including regulations on when the annual report has to

	include consolidated financial statements and which companies have to comply. Off-balance sheet exposures are reported as an integrated part of the annual report. Nearly all reports submitted to the DFSA are electronic and designed for on-going monitoring. Finanstilsynet use the information to monitor the financial condition and performance of the insurer by analyzing the information in different ways, e.g., rating of the companies, stress-testing, and benchmarking. Finanstilsynet reviews and revises reporting requirement on a regular basis. Insurance companies are required to inform the DFSA immediately of matters which are of material significance to their continued operation. This also applies correspondingly to individual members of the board of directors, members of the board of management, and responsible actuaries of a financial undertaking. Where a member of the board of directors, board of management, external auditors, or responsible actuary of a financial undertaking have cause to believe that the undertaking does not comply with the capital requirement of sections 124–126 or the solvency need under section 124(3) and section 125(5), such a person shall immediately notify Finanstilsynet of this fact.
Assessment	Observed
Comments	None
Principle 13.	**On-site inspection** The supervisory authority carries out on-site inspections to examine the business of an insurer and its compliance with legislation and supervisory requirements.
Description	According to section 346.1 of the FBA, the DFSA shall examine the circumstances of financial undertakings and financial holding companies. This shall include reviews of regular reports and inspections of individual undertakings. Financial undertakings shall provide Finanstilsynet with such information as is necessary for the performance of the duties of the DFSA. Finanstilsynet is authorized to gain access to a financial undertaking and its branches or a financial holding company with a view to obtaining information, including during inspections. The detailed procedures for performing on-site inspections are defined in the on-site inspection manuals for nonlife insurers and reinsurers and life insurers respectively. The manuals apply the same methodology for life and nonlife, and they are reviewed on a regular basis. The manuals include procedures for announcing the inspection, the performance of the inspection on-site, and reporting the conclusions. Manuals also list the elements to be covered by a full scale inspection and provide standard letters, agendas, and annotated agendas as well as reasoning and explanations. Based on the authority in FBA section 346 and 347, Finanstilsynet performs regular on-site inspections in insurance undertakings. Inspections are performed by teams of inspectors from the DFSA. The same inspectors perform on-site as well as off-site supervision. One of the purposes of on-site inspections is verification of the regulatory returns. Other purposes include an evaluation of the risk profile and capital strength as well as compliance with legislation. Company law requires auditors to verify annual reports prepared in accordance with FBA section 183.1, cf. FBA section 193 and 199, as well as the Executive Order No. 1183 of December 15, 2003 on Auditing Financial Undertakings and Financial Groups. Section 4.1, of this executive order requires auditors to prepare and maintain audit book comments (a long form audit report). A copy of the audit book comments is submitted to the DFSA. The audit book comments include a number of statements and information on the regulated entity. Other regulatory returns such as the returns on registered assets are certified separately by the auditor. The DFSA plans and prioritizes its on-site inspections based on results of an overall risk

	assessment system including the results of a rating system (seven indicators), stress-tests, as well as a qualitative assessment by a supervisor. The most important stress-test is labeled the traffic-light-system. This system has improved risk awareness and directs Finanstilsynet in identifying companies where tighter inspection seems necessary. The planning of on-site inspections is done on an annual basis following overall principles set by the DFSA management. Larger nonlife insurers are subject to a full scale inspection every four years. Smaller nonlife and all life insurers are subject to a full scale inspection every seven years. Vulnerable insurers are subject to more frequent full scale or focused inspections. Based on regular evaluations of risk, insurers may be subject to more frequent full scale or focused inspections. The procedure for reporting of findings to the insurer following an on-site inspection are described in FBA sections 346.2–3. Material findings and conclusions are presented and discussed in a meeting with the board of directors, management, auditors, and the responsible actuary. Subsequently, material findings and conclusions are submitted in the form of a written report. A follow up procedure is included in the report to the board of directors, management, and auditors cf. the answer to ICP 13, d. If necessary, the DFSA will perform a focused inspection to follow up on actions required as a result of an on-site inspection. Information on service providers will normally be obtained via the supervised entity. This information includes the outsourcing contract, reporting, and internal control. Currently, the DFSA has no specific powers to inspect most service providers directly.
Assessment	Observed
Comments	The risk-assessment, however, does not consider the size of the company and thus tends not fully balance risk sensitivity and potential financial impact for the market. Larger life companies should also be subject to a full inspection on a 4-year cycle.
Principle 14.	**Preventive and Corrective Measures** The supervisory authority takes preventive and corrective measures that are timely, suitable and necessary to achieve the objectives of insurance supervision.
Description	The DFSA supervises compliance with the FBA and regulations laid down in section 344.1. FBA section 350 entitles Finanstilsynet to order that a financial undertaking take the measures necessary within a time limit specified by the DFSA, if the financial position of the undertaking has deteriorated to such a degree that the interests of the depositors, the insured parties, the bond owners are at risk, or if there is a significant risk that the financial position of the undertaking will develop so that the undertaking loses its license. If the measures ordered have not been taken within the time limit specified, the DFSA is entitled to withdraw the undertaking's license. The FBA also includes provisions on restoration and other measures (FBA section 248–252). These provisions are applied in cases where the insurer does not comply with the capital requirement, cf. Also ICP 16. Where appropriate, the DFSA will require the insurance undertaking to forward a report on a problem identified, including a plan for rectification of the problem. In case of noncompliance with the capital requirement, a restoration plan will be required (FBA sections 248–252). The DFSA is entitled to order a company to take the steps necessary within a time limit in a number of specified circumstances.
Assessment	Observed
Comments	The DFSA possesses all means to ensure that shortfalls or misuse of regulation will be supported. The range of sanctions is rather biased to drastic measures and could be of more variety to respond to less severe shortfalls. It can be assumed that the withdrawal of license is

	not an adequate response to all types of noncompliance. Finanstilsynet is not able to impose fines, except, for instance, daily or weekly fines until required reports have been submitted. A distinction is made between supervisory action, which is a forward looking measure, and supervisory penalty, which is a penalty for past breaches of legislation and regulations. The latter cases may be transferred to the police, which may impose a fine or refer the case to court procedures. Sanctions will generally not be published neither on company level or on country level. During 2002–05, there were in total six noncompliances reported to the prosecutor. In 2005, 169 orders have been issued so far (November 2005) to ensure corrective actions through the companies.
Principle 15.	**Enforcement or sanctions** The supervisory authority enforces corrective action and, where needed, imposes sanctions based on clear and objective criteria that are publicly disclosed.
Description	The DFSA can order the management to report on the financial circumstances and future prospects of the undertaking. It further requires measures necessary within a time limit specified by Finanstilsynet, if the financial position of the undertaking has deteriorated to such a degree that the interest of different parties are at risk, or there is a significant risk that the financial position of the undertaking will develop so that the undertaking loses its license. The DFSA may also order that a financial undertaking remove a member of senior management. The issuing of new policies can be stopped. According to section 252 of the FBA, Finanstilsynet shall, in consultation with the liquidators, implement an investigation of whether it would be appropriate to attempt to transfer the portfolio of insurance contracts fully or partly to one or more insurance companies. Sections 249, 250, and 350 of the FBA states that the DFSA has the power to place the undertaking under administration or withdraw the license. Finanstilsynet may determine a time-limit for disposal of the other activities, if an immediate disposal would result in a financial loss according to sections 24–26 FBA. The DFSA has—as referred to under the assessment on ICP 7—limited means to address management problems directly. Finanstilsynet does not possess the power to have controlling owners and managers to be replaced or their powers restricted. If measures have been ordered by the DFSA, implementation will be followed and progress will be monitored until all shortfalls have been resolved. Finanstilsynet cannot ensure that individuals will be barred from acting in responsible capacities in the future. The FBA only allows for restrictions to act as an executive. The management and board are not covered by this provision. Violation against sections of the FBA may incur a criminal liability according to the regulations in chapter 5 of the Criminal Code. Where provisions of the law are breached it may be sanctioned by way of fines, statutory debt collection, or by withholding wages against individuals and legal persons. The DFSA is authorized to sanction by way of statutory debt. Fines can only be issued subsequent to a respective courts decision. Individuals, who submit incorrect or misleading information on matters pertaining to the undertaking to public authorities, or who are guilty of gross or repeated negligence or carelessness which may entail losses for the undertaking, shall be liable to a fine or imprisonment for up to four months unless more severe penalty is incurred under other legislation. All sanctions will be imposed in a consistent manner. Should the DFSA assume that someone without the necessary authorization is engaged in activities that are subject to authorization, Finanstilsynet will publish warnings and require the person it assumes to be in charge of such activity to provide information about the activity.

	According to section 373 (1) of the FBA, unlicensed insurance activity is liable to fines or imprisonment.
Assessment	Largely observed
Comments	The DFSA should have means to address management problems directly. Currently, Finanstilsynet does not possess the power to have controlling owners and managers to be replaced or their powers restricted. Issuing of an executive order should be considered.
Principle 16.	**Winding-up and exit from the market** The legal and regulatory framework defines a range of options for the orderly exit of insurers from the marketplace. It defines insolvency and establishes the criteria and procedure for dealing with insolvency. In the event of winding-up proceedings, the legal framework gives priority to the protection of policyholders.
Description	FBA chapter 15 provides the framework for withdrawal of licenses and winding up of financial undertakings including insurance undertakings. The DFSA may withdraw the license on request or if it repeatedly violates the FBA. Finanstilsynet can withdraw the license and require a winding up if an insurance company has not, within the time limits set by the DFSA, carried out the measures listed in the restoration plans. Finanstilsynet is entitled to reduce the disruption to the provision benefits of policyholders to a minimum. A portfolio of insurance contracts shall be placed under administration if it appears that it is not possible to obtain the funds necessary to cover the insurance provisions within the time limit. Prior to transfer a portfolio, the DFSA must prepare a report regarding the transfer as well as draft an agreement with the relevant company. The report and the draft shall be published in the Danish Official Gazette and in daily newspapers. The report shall include an appeal to the policyholders to notify the DFSA. The company shall, at the same time, forward the report and draft to those policyholders whose address is known by said company. The MoEB shall, under consideration of the objections made, decide whether the portfolio of insurance contracts may be transferred in accordance with the proposal made. The DFSA can also review whether long-term insurance contracts are to be terminable by both parties according to the provisions that would have been in force if the duration of the agreement had expired. Provisions regarding such access to termination shall be indicated in the report from Finanstilsynet. If a portfolio will be administered under the direction of the DFSA, registered assets will be transferred immediately to the administration estate. The administration estate represented by the administrator shall be entitled to have full charge of said assets. With regard to investment securities, this shall be registered at a central securities depository and, with regard to real property, in the Land Register. Two companies have been winded up during the period from 2002–05. No shortfalls on provisions have been reported.
Assessment	Observed
Comments	None
Principle 17.	**Group-wide supervision** The supervisory authority supervises its insurers on a solo and a group-wide basis.

Description	The FBA provides clear definitions for identifying a group. Section 5 includes definitions of parent company, subsidiary undertaking, associated undertaking etc. All holdings of more than 10 percent in a financial institution are subject to notification and approval cf. section 61. It is an important factor in the approval process that group structures should be as clear and transparent as possible, so the structure of the group should be clearly defined. The DFSA has entered into the multilateral protocols with other supervisory authorities of the European Economic Area (EEA). An MoU amongst the Nordic supervisory authorities has been signed to agree the terms to supervise groups such as Nordea and others. As Finanstilsynet is an integrated supervisor for the financial sector in Denmark, a comprehensive outline is available for Danish groups. FBA, chapters 10 and 12 lay down the principles for applying solvency and capital adequacy rules on a consolidated basis both on a solo level chapter 10 and on a consolidated basis All intra-group exposures need prior approval from Finanstilsynet before they are allowed to be conducted. Approval is rules based and is often given for one year (maximum). The Executive Order No. 793 of July 10, 2004 on Reporting of Large Exposures for Groups where the parent Company is a Financial Holding Company or a Financial Undertaking and where full Consolidated Statements are not prepared is an implementation of the EU Conglomerates Directive. According to FBA section 179, the DFSA may under certain conditions order a parent undertaking that owns holdings in financial undertakings to separate such financial undertakings and finance institutions in a subgroup under a financial holding company. According to FBA section 180, the DFSA may under certain conditions order a financial holding company to dispose of holdings in a financial undertaking.
Assessment	Observed
Comments	The DFSA supervises three financial conglomerates with activities in the Danish market. Risk-assessment of the Danish business takes place on joint meetings of all involved parties within Finanstilsynet. The MoU with Nordic countries ensures a consistent approach. The simultaneous assessment of major risks in all countries of the respective groups impedes unsupervised risk transfer.
Prudential Requirements	
Principle 18.	**Risk assessment and management** The supervisory authority requires insurers to recognize the range of risks that they face and to assess and manage them effectively.
Description	Insurance companies are not explicitly required to have risk assessment and risk management systems in place. However, guideline 9680 requires that the management of insurance companies defines the procedures under which they delegate responsibility that insurance risks will be assessed and underwritten, financial and operational risks will be considered, and payment systems will be under control. The DFSA runs a traffic-light system, which addresses the financial resilience of the undertakings. Section 71 of the FBA requires the board of directors of a financial undertaking to prepare written guidelines on the most significant areas of activity of said financial undertaking, specifying the distribution of responsibilities between the board of directors and the board of management. The guideline on section 71 lays out the more detailed requirements on limits of the material risk areas including the insurance activity (underwriting), the reinsurance cover, and investments. The guideline stipulates that the board of directors receive reporting explaining the

	compliance with lines and limits set by the board as well as the current exposure. The regulation and guidelines specify a framework, provide minimum requirements and point out issues that the insurance company should consider in respect of its risk assessment, risk management systems, and required reporting. The motivations accompanying the bill at the time of presentation in the Danish parliament explains that the guidelines must define the risk profile of the undertaking and that the contents of the guidelines should reflect the actual business activity of the insurance undertaking. The motivations specify that an insurance undertaking include markets risk, underwriting policies, and reinsurance cover. The required degree of detail of the guidelines setting the risk profile will vary from undertaking to undertaking according to the complexity, size, and nature of their business. The FBA requires that the funds shall be invested in an appropriate manner, and a manner advantageous for the insured parties, such that there is adequate security that the company can meet its obligations at all times. In order to fulfill these requirements the insurer should have risk management policies and systems capable of identifying, measuring, assessing, reporting and controlling their risks at all times. The DFSA checks this during on-site inspections.
Assessment	Largely observed
Comments	The DFSA receives reporting on the results of stress test on assets (traffic light) on a regular basis. Finanstilsynet expects all companies to examine the financial robustness in all material risk areas, e.g. market risks and realistic disaster scenarios including reinsurance cover. In practice, a company must have a risk assessment framework in place, relative to its nature of the business, in order to produce internal reporting and results on stress tests. The requirement to establish a risk assessment framework should be obligatory for all companies and should be expressed in an executive order.
Principle 19.	**Insurance activity** Since insurance is a risk taking activity, the supervisory authority requires insurers to evaluate and manage the risks that they underwrite, in particular through reinsurance, and to have the tools to establish an adequate level of premiums.
Description	Section 71 FBA requires the board of directors of a financial undertaking to prepare written guidelines on the most significant areas of activity of said financial undertaking, specifying the distribution of responsibilities between the board of directors and the board of management. The board of an insurance undertakings is required to set risk limits including limits on underwriting, tariffs, and reinsurance cover (mitigating and diversifying risks and defining limits on the amount to be retained). The DFSA requires insurers to evaluate the risks that they underwrite and do have a clear strategy to mitigate and diversify risks by defining limits on the amount of risk retained. Reporting to Finanstilsynet includes an annual reporting by all newly licensed nonlife insurance companies and nonlife insurance companies with a gross premium exceeding DKr 25 million of their reinsurance contracts to the Reinsurance Monitoring System (REMOS). This enables the DFSA to evaluate the reinsurance cover and the security of reinsurers. According to the inspection manuals, underwriting risk is an important element of a full scale inspection, although it remains unclear what consequences could be applied by the DFSA. Finanstilsynet is able to review the methodology used by the insurer to set premiums. This is rather a notification and does not entitle to determine whether they are established on reasonable assumptions to enable the insurer to meet its commitments. This ability is restricted to life business.
Assessment	Largely observed
Comments	Finanstilsynet should consider whether it would issue an executive order with minimum

	requirements regarding insurance activity.
Principle 20.	**Liabilities** The supervisory authority requires insurers to comply with standards for establishing adequate technical provisions and other liabilities, and making allowance for reinsurance recoverables. The supervisory authority has both the authority and the ability to assess the adequacy of the technical provisions and to require that these provisions be increased, if necessary.
Description	According to the Executive Order No. 1406, technical and other provisions have to be valued based on sound accounting and actuarial principles. If the DFSA assumes that reserve levels are not adequate, it has to question the company's actuarial principles and require a report about its circumstances and financial position. The DFSA receives at least bi-annual statement of all liabilities in both life and nonlife. It has also issued a guidance note to Executive Order 1406. Discount rates and mechanisms are defined for life and workers compensation business and are updated and published daily. Until 2008, undertakings are allowed to use a simplified rate, the average of three government bonds. The DFSA reviews technical provisions both off-site and on-site. With respect to nonlife insurers, Finanstilsynet will run a stress test of the liabilities off-site In life insurance, technical provisions are reviewed by notification of the technical basis to the DFSA. If an undertaking does not fulfill the requirements on technical provisions, Finanstilsynet has the power to require an increase of the technical provisions. Any persons violating the principles laid down shall be liable to a fine. For life insurance, the DFSA is notified of the methods and principles for calculating the technical provisions. Both in life and nonlife insurance, the methods and principles of technical provisions are verified and evaluated during on-site inspections. If Finanstilsynet does not approve the technical provisions, the DFSA will discuss the methods and principles with the undertaking and require changes in the methods, if necessary. Executive Order 1399 entitles Finanstilsynet to reduce the risk weighting of the solvency requirement, if the technical performance either differs from past experience or the technical risk transfer is insignificant. All liabilities are valued at market value, whilst nonlife claims liabilities do not require a market risk margin. There have been no reports on shortfall of reserving levels.
Assessment	Observed
Comments	None
Principle 21.	**Investments** The supervisory authority requires insurers to comply with standards on investment activities. These standards include requirements on investment policy, asset mix, valuation, diversification, asset-liability matching, and risk management.
Description	FBA section 159 (2) sets qualitative requirement on composition and diversification of investments. Due to EU directives, this specific requirement is limited to assets covering provisions. However, to prohibit any investments both those covering provisions and those not covering provisions, it is laid down in FBA 24–26 and 29 that an undertaking is not allowed to have permanent subsidiaries doing business outside core insurance business. Assets covering provisions are limited to the 14 listed different classes of assets. The qualitative requirement states that the funds under the charge of an insurance company or a pension fund shall be invested in an appropriate manner, and a manner advantageous for the insured parties, such that there is adequate security that the company can meet its obligations at all times. The DFSA reviews the performance through quarterly reports and through auditor's reports twice a year. Auditors are also required to do specific non-notified controls of assets covering technical

	provisions. FBA section 159 (2) requires the asset mix in general to be liquid with regard to the liabilities. During on-site inspections, Finanstilsynet requires undertakings to submit a full list of all assets and analyses the undertaking's investment strategy and diversification policies. The stress test (traffic light) measures, mismatch in interest rate exposures, and other assets are compared to the liabilities. All financial assets are valued at fair value. The only exception is loans with floating interest rates according to the Executive Order, section 49. These are valued at par. Guideline 9680 requires the board of directors to at least annually set the risk profile on the assets (equity, bonds, currency, credit and counterparty risk, derivatives). Finanstilsynet's on-site inspection manuals contain provisions to review whether the rules are applied. According to FBA section 64, all members of the board of directors or senior managers will have to fulfill fit and proper requirements. However, these requirements do not include the head of investments or the head of risk management functions if these functions are separate from senior management. The FBA sections 70 and 71 include no specific requirements on skills of certain staff. Auditors are required to provide an annual long form audit report to the DFSA, including certification of compliance with a number of issues, such as rules of investment and that the undertaking has written procedures in all important areas, including investments.
Assessment	Largely observed
Comments	Since the investment function is not subject to suitability requirements, the principle can only be assessed as largely observed.
Principle 22.	**Derivatives and similar commitments** The supervisory authority requires insurers to comply with standards on the use of derivatives and similar commitments. These standards address restrictions in their use and disclosure requirements, as well as internal controls and monitoring of the related positions.
Description	Guidelines 9680 requires undertakings to have in place limits on the use of derivatives and inherent risks before the undertaking take positions in derivatives. The executive order on financial reporting, sections 43−45 requires that all derivatives in force have to be disclosed in the annual report. Section 64 FBA requires the board has adequate knowledge related to the use of derivatives. Guideline No. 9680 requires that the undertaking have clear reporting lines and authorization levels, if it is delegated responsibility within the undertaking. The DFSA reviews the decisions made by the board during on-site inspections. Companies are also required to have in place internal control and reporting on all investments including derivatives. The internal control includes monitoring of risks. The FBA provide no specific requirements on skills for modeling and pricing of derivatives of certain staff. During on-site inspections, Finanstilsynet reviews that the undertaking has procedures on the parameters to value over-the-counter (OTC) products or on a regular basis receives alternative pricing from market participants.
Assessment	Largely observed
Comments	Since the usage of derivatives is not subject to suitability requirements, the principle can only be assessed as largely observed.

Principle 23.	**Capital adequacy and solvency** The supervisory authority requires insurers to comply with the prescribed solvency regime. This regime includes capital adequacy requirements and requires suitable forms of capital that enable the insurer to absorb significant unforeseen losses.
Description	The calculation of technical provisions and other liabilities for solvency purposes are based on the valuation used for accounting purposes. The valuation of the assets for solvency purposes is also based on the valuation measures used for accounting purposes. FBA sections 130, 131, and 135 lay down the eligible forms of capital elements. The eligible capital elements are implemented from European directives. However, some of the elements listed in the EU directives are either not considered eligible in Denmark (e.g. future profits) or only eligible with supplementary requirements (e.g. FBA sections 130 (1)–(2) on special bonus provisions (profit reserves)). The solvency requirements set out in FBA section 126 and in the Executive Order No. 1399 are calculated as a percent of liabilities in life-insurance and a percent of premiums/claims in nonlife insurance, as set out in the EU directives. The current regime is considered reasonable sensitive to size, complexity, and risks. However, the EU Solvency II project is expected to improve this at a later stage. The minimum capital requirements are laid down in FBA section 126 (1) no. 6-8, (4), (5), and 6, and 408. Further, Executive Order No. 1399 lays down some exceptions. The flat rate minimum capital requirement is € 3 million in most classes of business and € 2 million in nonlife (nonliability insurance). However, during a transitional period up to 2009, insurance undertakings are allowed to continue business with a lower amount of capital (FBA section 408). Some exceptions are given for small mutual insurance companies according to FBA section 126 (4)–(6) and to Executive Order No. 1399, section13. The minimum capital requirements are according to EU directives. Small mutual insurers with a lower capital requirement are required to give special notice to policyholders. If Finanstilsynet finds that the solvency position of an undertaking imprudent, it has the power in adjust the capital requirement. In most cases, the supplementary capital requirement of the stress test (traffic light) increases the level of the capital requirement. Solvency control levels are imposed if an undertaking does not fulfill the solvency requirement. According to FBA 248, an undertaking has to aim at restoration of its financial position over a shorter period to be determined by the DFSA. Finanstilsynet receives reporting on all the solvency control levels. Branches of companies outside the EU are required to possess sufficient funds to cover the company's gross liabilities originating from insurance business directly written in Denmark. There are about 28 companies operating under a granted exemption from Solvency I requirements.
Assessment	Observed
Comments	None
Markets and consumers	
Principle 24.	**Intermediaries** The supervisory authority sets requirements, directly or through the supervision of insurers, for the conduct of intermediaries.

Description	The DFSA has implemented the European Insurance Mediation Act (IMA). Undertakings carrying out insurance broker activities shall be licensed by Finanstilsynet. Any person carrying out insurance broker activities as an employee of an undertaking covered by subsection (1) shall be licensed by the DFSA to carry out insurance broker activities as an employee of the undertaking. Intermediaries have to pass exams of the Insurance Academy, established by the Danish Insurance Association. Finanstilsynet may withdraw the license of an insurance broker undertaking if the undertaking no longer fulfils the fit and proper requirements. In accordance to the IMA section 20 (2) an insurance broker undertaking shall, without delay, deposit funds entrusted to it in a special client's account and shall establish appropriate security for these funds. When an insurance broker undertaking solely uses one or several specific insurance companies without having entered into an explicit agreement with the insurance companies to this effect, the customer shall be notified hereof no later than at the time of entering into a specific insurance contract. Furthermore, the customer shall be informed of the right of access to the names of the insurance companies used by the insurance broker undertaking. It is illegal to carry out insurance intermediation without license. According to IMA section 54 (1), violation of the provision in section 4 regarding licensing shall be punishable by fine, unless more severe penalty is incurred under other legislation.
Assessment	Observed
Comments	None
Principle 25.	**Consumer protection** The supervisory authority sets minimum requirements for insurers and intermediaries in dealing with consumers in its jurisdiction, including foreign insurers selling products on a cross-border basis. The requirements include provision of timely, complete and relevant information to consumers both before a contract is entered into through to the point at which all obligations under a contract have been satisfied.
Description	Insurers and intermediaries shall be operated in accordance with honest business principles and good practice within the field of activity, cf. FBA section 43 (1) and IMA section 19 (1). The DFSA finds that it observes ICP 25, b. An insurance company is required to obtain a profile of customers' needs in order to ensure products sold to this customer are appropriate. Insurers and intermediaries may not without due cause disclose or use confidential information obtained through the performance of their duties, cf. FBA section 117 (1) and IMA section 18. The insurance company shall provide information on the most important element in the scope of cover of the selected insurance, about the customer's options, and about other important aspects of the insurance product. Prior to concluding a contract, the company has to provide information on any significant limitations in relation to the cover the customer could reasonably expect under the relevant insurance. The regulation is available at Finanstilsynet's website (http://www.ftnet.dk/sw99.asp). The scope of the FBA stipulates to what extent the provisions apply to cross-border offering of insurance, cf. FBA section 1 (3−5). Furthermore, Finanstilsynet provides this type of information to the public on request by telephone or in writing.

	The DFSA issues warning notices on its website if an insurer or intermediary carries out insurance or insurance intermediation without a license. Finanstilsynet publishes annual reports and other reports regarding insurance and insurance intermediation. Furthermore, the DFSA has published "frequently asked questions" on its website. Finanstilsynet receives complaints on questionable behavior of insurance companies on market conducts. Disputes related to contractual issues or settlements between policyholders and insurance companies will be settled in front of a national complaints board. The complaints board has been notified of 2,812 cases in 2004.
Assessment	Observed
Comments	None
Principle 26.	**Information, disclosure & transparency towards the market** The supervisory authority requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks to which they are exposed.
Description	The FBA applies to all financial undertakings and financial holding companies and contains general regulations regarding the annual report and audit. Reporting requirements are laid out in sections 186–188, 193, and 195. The annual report shall give a true and fair view of the enterprise's assets and liabilities, financial position, and results for the year. If consolidated financial statements have been prepared, also the group's assets and liabilities, financial position, and results for the year shall be included in the annual report. According to the Executive Order No. 1406 of December 14, 2004, on financial statements, the insurer shall in the annual report disclose detailed information—both quantitative and qualitative—on the financial position and performance. Any disclosure that is necessary to give a true and fair view is required (section 87 in the regulation). Specifically, a description of accounting policies is required, e.g. the basis, methods, and assumptions upon which information is prepared (sections 89 and 128 of the executive order). Any uncertainties and changes in accounting polices shall be disclosed and explained. A quantitative description of the exposure to certain changes in market risks and insurance risks is also required (sections 126–127). Further, a qualitative description of the exposure to financial risks and insurance risks and the manner in which these risks are managed is required (section 131 in the regulation). Executive Order No. 1406 requires a quantitative description of the exposure to certain changes in market and insurance risks. In accordance with section 344 in the FBA, Finanstilsynet shall supervise compliance with this Act and regulations laid down pursuant to this Act. Therefore, the DFSA shall examine the accounts of insurers to check that the financial statements are prepared in accordance with the relevant legislation. With regard to listed enterprises, this control is performed by Finanstilsynet together with the Danish Securities Council on behalf of the Danish Securities Council, which has the powers laid down in section 197. Section 197 in the FBA states that in order to ensure that the annual reports of financial undertakings and financial holding companies are in accordance with the relevant regulations the DFSA may: (i) provide guidance; (ii) take action against violations; and (iii) order that errors be corrected and that violations be remedied.
Assessment	Observed
Comments	None

Principle 27.	**Fraud** The supervisory authority requires that insurers and intermediaries take the necessary measures to prevent, detect and remedy insurance fraud.
Description	The DFSA has the powers and resources to establish and enforce regulations and to communicate as appropriate with enforcement authorities, as well as with other supervisors, to deter, detect, record, report, and remedy fraud in insurance. The FBA does not address insurer fraud. It is addressed in the Danish legislation and insurance contract law. Committing insurance fraud is a crime under Danish law and will be prosecuted by the relevant branches. According to FBA section 71, an insurer shall have good administrative practices, full internal control procedures, the resources necessary for proper carrying out of its activities, and use these appropriately. These requirements contribute to ensuring that an insurer implement effective procedures and controls to deter, detect, record, and report fraud. The insurance company is protected against claims fraud, which is punishable under the Criminal Code, chapter 28, section 279. If the policyholder in connection with underwriting insurance deceitfully submits misleading information, the insurance contract is not binding for the insurer, cf. section 4 of the Insurance Contract Act. Insurance companies are required to set up internal control procedures to protect themselves sufficiently against fraudulent activity from staff and customers. Undertakings carrying out insurance broker activities shall be licensed by Finanstilsynet, cf. IMA section 4 (1). As a licensed insurance broker, the undertaking is obliged to allocate appropriate resources and implement effective procedures and controls to deter, detect, record, and report fraud. The insurance trade organization takes measures to prevent fraud, for instance, by taking measures to establish a fraud register. Exchange of information between insurers with respect to fraud complies with the provisions in chapter 9 of the FBA regarding disclosure of confidential information. Such a fraud register will be established in line with other protection legislation. Finanstilsynet will issue public warnings in case of illegal provision of insurance and cooperates with supervisors in other jurisdictions, as appropriate.
Assessment	Observed
Comments	None
Anti-money laundering, combating the financing of terrorism	
Principle 28.	**Anti-money laundering, combating the financing of terrorism (AML/CFT)** The supervisory authority requires insurers and intermediaries to take effective measures to deter, detect and report money laundering and the financing of terrorism.
Description	The DFSA is responsible for the Danish Act on measures to prevent money laundering and financing of terrorism (Consolidated Act no. 132 of March 1, 2005—The Act on Money Laundering). This Act covers, both life insurers and insurance intermediaries. This Act implements Directive 2001/97/EC amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering (The 2nd Money laundering Directive). The current Act on Money Laundering covers the FATF recommendations 4, 10, 13−15, 21, and special recommendation IV. Furthermore, the FATF recommendation 5 is also partially observed by the current Act on Money Laundering. The FATF recommendations 29−32 and special

	recommendation V are observed. The DFSA has proposed a new law, which was adopted in 2006. The law on measures to prevent money laundering and financing of terrorism (the bill on money laundering) aims to fully implement the EU 3rd Money Laundering Directive and thus comply with the FATF 40 revised recommendations, including recommendations 6, 8, 9, 11, 22, and 25. The DFSA shall, pursuant to section 346(1) of the FBA, examine the circumstances of life insurers, which include inspections of individual undertakings. Finanstilsynet carries out such inspections periodically. As an integrated element of such an inspection, the DFSA examines whether the insurance company complies with the act on money laundering. Finanstilsynet has an inspection manual, where all the areas to be reviewed are described. According to this manual, it is part of on-site inspections to inquire about the undertakings internal procedures to prevent money laundering. Pursuant to section 347(1)–(2) of the FBA, life insurers shall provide Finanstilsynet with such information as is necessary for the performance of the duties of the DFSA. Furthermore, Finanstilsynet may at all times, on proof of identity and without a court order, gain access to an insurance company and its branches or a financial holding company with a view to obtaining information, including during inspections. If the DFSA during an inspection or in another way ascertains that the Act on Money Laundering has not been complied with, Finanstilsynet will be expected to express criticism on the matter and order the company to comply with this act. Furthermore, sections 3, 4, 6, 9, and 10(2) of the Act on Money Laundering are subject to penalty (cf. section 13). As for insurance intermediaries, the DFSA shall, pursuant to the Insurance Mediation Act section 44(1), supervise compliance with the provisions of this act and regulations laid down pursuant to this act. Finanstilsynet may at all times, on proof of identity and without a court order, gain access to an insurance intermediary with a view to obtaining information, including during inspections. According to the new law on money laundering, the DFSA shall supervise both insurance companies and insurance intermediaries for compliance with this act. Furthermore, this law requires that these businesses shall provide Finanstilsynet with such information as is necessary for the performance of the duties of the DFSA. Finanstilsynet may at all times, on proof of identity and without a court order, gain access to an insurance intermediary with a view to obtaining information, including during inspections. According to section 61 (1)–(2) and section 62(1) of the FBA, the DFSA shall be notified and give authorization prior to any acquisition by a natural or legal person of a qualifying interest of 10 percent or more in an insurance company. Finanstilsynet has the appropriate authority to cooperate with the Danish Financial Intelligence Unit (FIU) and enforcement authority (Public Prosecutor for Serious Economic Crime). The terms of this cooperation is not in writing, but is a consequence of Finanstilsynet's duty to conduct its responsibilities sufficiently. The DFSA makes an effort to devote the necessary resources to the AML/CFT area. Finanstilsynet's banking division has specialist expertise in this area and has the day-to-day responsibility for the interpretation and revision of the Act on Money Laundering. The DFSA is kept up to date with the AML/CFT standards through its membership of the FATF, its participation in the FATF meetings, as well as its participation in the meetings of the Money Laundering Contact Committee appointed by the European Commission Services.

	Pursuant to section 4 of the Act on Money Laundering, both life insurance companies and insurance intermediaries shall conduct a customer due diligence. The new law on money laundering provides that life insurers and insurance intermediaries shall make sure that branches and subsidiaries located outside the European Community applies AML/CFT measures at least equivalent to the 3rd Money Laundering Directive.
Assessment	Largely observed
Comments	The new law is expected to contribute to an improved supervisory framework to support activities on AML/CFT.

Table 18. Summary Observance of IAIS Insurance Core Principles

Assessment Grade	Principles Grouped by Assessment Grade	
	Count	List
Observed	18	1, 2, 4, 5, 8, 9, 11, 12, 13, 14, 16, 17, 20, 23, 24, 25, 26, 27
Largely observed	10	3, 6, 7, 10, 15, 18, 19, 21, 22, 28
Partly Observed		
Materially nonobserved		
Nonobserved		
Not applicable		

E. Recommended Action Plan and Authorities' Response to the Assessment

Recommended action plan

20. The main recommendations are summarized in Table 19.

Table 19. Recommended Action Plan to Improve Observance of IAIS Insurance Core Principles

Reference Principle	Recommended Action
Conditions for Effective Insurance Supervision i.e., CP 1	While good conditions for effective supervision are in place, some more specific rule based requirements should be applicable to all companies. All professional resources are available and of high standards. Market infrastructure allows for an efficient management of the sector. A wide range of operational services are available to insurance undertakings and allow them to focus on technical related aspects of the business. However, the regulation is very principle based, but allows for a risk based supervision. Specifically, the requirements on organization of an undertaking in conjunction with the relevant guideline 9680 to guide the company to consider measures without defining minimum standards applicable to *all* companies.
The Supervisory Authority i.e., CP 2	None

Supervisory authority i.e., CP 3	The potential interference of the executive branches in the budget allocation should ideally be limited or restricted. Finanstilsynet has to agree on its budget with the Ministry of Economic and Business Affairs, although the expenses of the agency are covered by fees of the supervised entities. Finanstilsynet is also subject to an annual budget reduction program for the public sector. There is a possibility that resources could be allocated to regulation to the disadvantage of supervisory activity.
Supervisory process i.e., CP 4	None
Licensing i.e., CP 6	Considerations should be given to also require that the suitability of auditors and actuaries to be assessed. Finanstilsynet pays specific attention to the licensing process. The risk based approach requires a tighter and rather rule-based supervision within the first years of the newly established businesses. The ongoing supervisory process does not demand comprehensive detailed operating plans. As also Finanstilsynet has distinctive rules for the supervision of new entities, considerations should be given to also require that the suitability of auditors and actuaries to be assessed.
Suitability of persons i.e., CP 7	Consideration should ideally be given to apply fit and proper requirements to a broader range of senior management. Finanstilsynet bases its system to assess the appropriateness of key functionaries on the assumption that is the core responsibility of the senior management to ensure adequate personnel to be assigned to relevant tasks in the supervised companies. Nevertheless, the fit and proper requirements are applied consistently. There was no evidence that this has led to severe problems so far. However, this may be justified by the limited size of the market.
Changes in Control and portfolio transfers i.e., CP 8	None
Corporate Governance i.e., CP 9	None
Internal control i.e., CP10	The requirements to establish internal audit functions should be made compulsory for smaller companies. Guideline 9680 does not sufficiently clearly define what Finanstilsynet requires in the area of internal controls. As the guideline does not expand on requirements from section 71 FBA, the subsequent control procedure may not cover all relevant issues. The importance of this function requires an executive order.
Market Analysis i.e., CP11	Finanstilsynet should ideally enlarge its activities on market analysis and obtain information, including on macro economic developments, which would enable forecasting market trends that allow for projections of potential impacts on the sector.
Reporting to supervisors and off-site monitoring i.e., CP 122	None
On-site inspection	The risk-assessment should also take into account the size

i.e., CP 13	of the company to better balance risk sensitivity and potential financial impact for the market. Larger life companies should be subject to a full inspection on a 4-year cycle.
Preventive and Corrective Measures i.e., CP 14	Consideration should be given to have a broader range of graduated sanctions. Finanstilsynet possesses all means to ensure that shortfalls or misuse of regulation will not be supported. The range of sanctions is rather biased to drastic measures and could be of more variety to respond to less severe shortfalls. It can be assumed that the withdrawal of license is not an adequate response to all noncompliances. Finanstilsynet is not able to impose fines. Sanction swill not be published, neither on company level nor on country level. During 2002–05, there were in total six noncompliances reported to the prosecutor. In 2005 (until November), 169 orders had been issued with a view to ensure corrective actions.
Enforcement or sanctions i.e., CP 15	Finanstilsynet should have means to address management problems directly. Currently, Finanstilsynet does not possess the power to dismiss controlling owners and managers or to restrict their powers. Issuing of an executive order should be considered.
Winding-up and exit from the market i.e., CP 16	None
Group-wide supervision i.e. CP 17	The simultaneous assessment of major risks in all countries of the respective Group impedes unsupervised risk transfer. Finanstilsynet supervises three financial conglomerates with activity in the Danish market. Risk-assessment of the Danish business takes place on joint meetings of all involved parties within Finanstilsynet. The MoU with Nordic countries facilitates a consistent approach across borders.
Risk assessment and management i.e. CP 18	The requirement to establish a risk assessment framework should be obligatory for all companies and should be expressed in an executive order. Finanstilsynet receives reports on the results of the stress test on assets (traffic light) on a regular basis. Finanstilsynet expects all companies to examine the financial robustness in all material risk areas, e.g., market risk and realistic disaster scenarios including reinsurance cover. In practice, a company must have a risk assessment framework in place, relative to its nature of the business, in order to produce internal reporting and results on stress tests.
Insurance activity i.e. CP19	Finanstilsynet should consider whether it would issue an executive order with minimum requirements regarding insurance activity.
Liabilities i.e. CP 20	None
Investments i.e., CP 21	Consideration should be given to more detailed suitability requirements.
Derivatives and similar commitments i.e. CP 22	Consideration should be given to require suitability requirements for the derivatives function.
Capital adequacy and solvency i.e. CP23	None

Intermediaries i.e., CP 24	None
Consumer protection i.e., CP 25	None
Information, disclosure & transparency towards the market i.e. CP26	None
Insurance fraud i.e. CP27	None
Anti-money laundering i.e., CP 28	See separate detailed AML/CFT assessment.

F. Authorities' Response

We are broadly in agreement with the assessment team of the IMF, but would like to elaborate on the following issues.

As a follow-up to the recommendations by the IMF assessment team, consideration will be given to establish the DFSA as an independent institution by providing the agency a statutory basis in the legislation. Correspondingly, a separation of its regulatory and supervisory budget will be considered. In our view, how the budgetary procedure is organized is not the most important issue—instead it is essential to ensure that adequate funds are available at all times. A more distinct division of the budget, where the resources allocated to the supervisory activities are separated, would give a more clear and transparent overview.

The fit and proper test in place in Denmark is compliant with the EU directives. We understand that the IMF assessment team assessed ICP 6, 7, 21, and 22 "largely observed" because the suitability of auditors, actuaries, investment officers, and derivative functions are not subject to direct fit and proper. In view of this assessment, we will consider the possibility to adjust the regulation so that the DFSA will be able to take measures in case we discover that a person employed in one of these functions is not fit and proper. In our view, it would not be cost efficient to extend the fit and proper test to the functions mentioned, as it would increase the administrative burden of the industry as well as require the DFSA to allocate resources to this task. Furthermore, the management has the incentive to hire persons, who are suitable for the job. Thus from a corporate governance point of view, it seems preferable that the management of the company is responsible for hiring persons, who are fit and proper, and that the DFSA has the means to act in case it discovers that a person was not fit and proper after all.

The IMF team finds that ICP 15 is "largely observed," as the DFSA does not possess the power to dismiss controlling owners and managers or to restrict their powers in case they are not fit and proper. We would like to stress that the DFSA is able to abolish the voting right of shareholders in case a qualified owner counteracts the sound and safe operation of the company. In such cases the DFSA may also give specific instructions to the firms. Hence we do not see a need for further measures.

The IMF assessment team finds that ICP 6, 10, 18, and 19 are only “largely observed” because the rules are set out in guidelines rather than executive orders and because the requirements for companies' operational plans, internal control systems, risk assessment frameworks and insurance activities should be more detailed. The IMF also suggests that it should be compulsory for smaller companies to have an internal audit function. We would like to reiterate that in Denmark, the internal auditors participate in the financial auditing of the company. An internal auditor is not a part of the control system of the company. Therefore we do not se a need for a compulsory internal audit function in small companies. We realize that the Danish system differs from other jurisdictions in this regard. In addition, it is our experience that it may be difficult for small firms to attract internal auditors. Nevertheless, we will consider to make the requirements more detailed and to change the guidelines into an executive order. However, the benefits will have to be viewed against the general intension to keep the administrative burden on the industry at the lowest level possible.