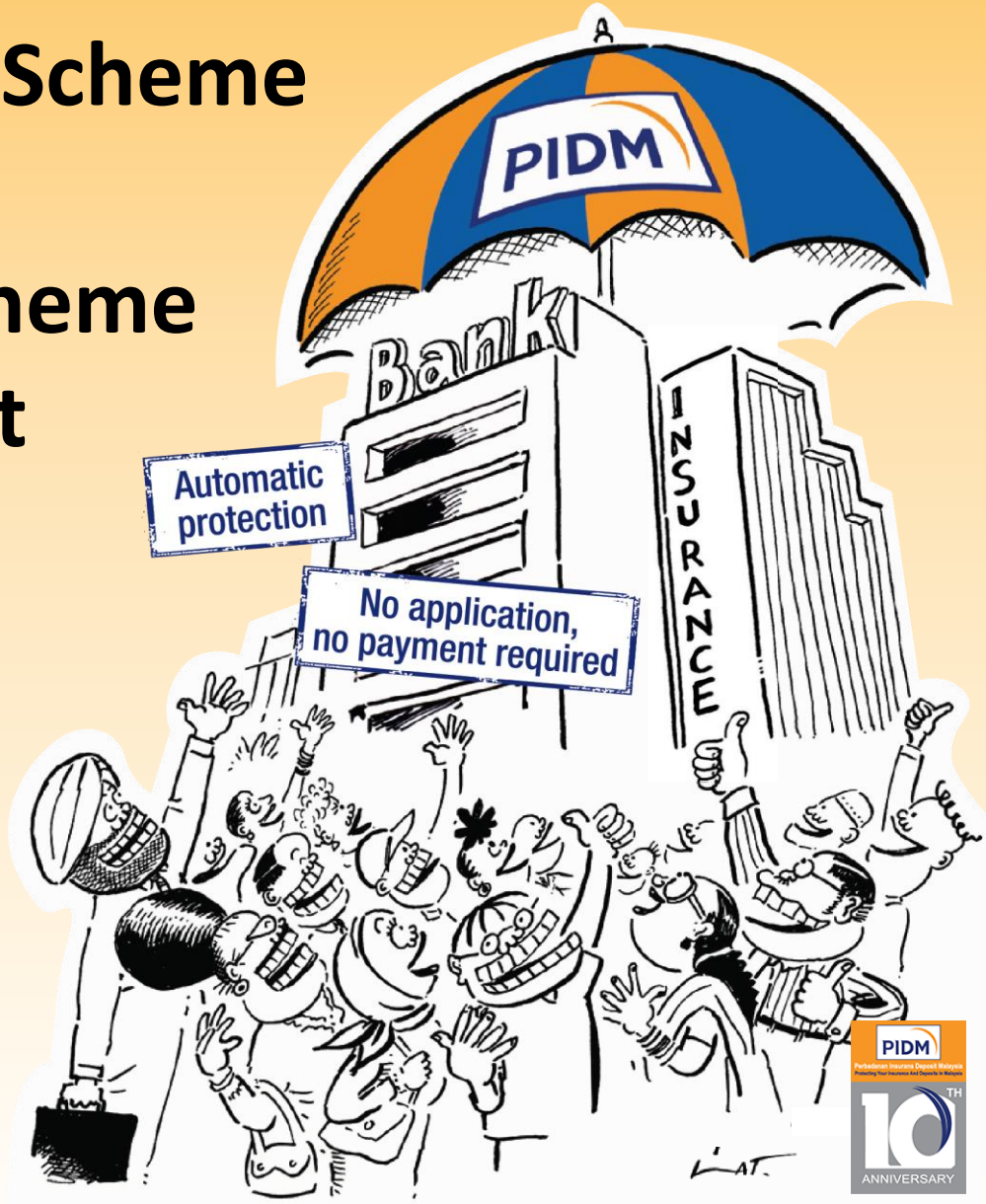
How do Insurance Guarantee Scheme and Deposit Insurance Scheme Collaborate to Protect Consumers



19 April 2016

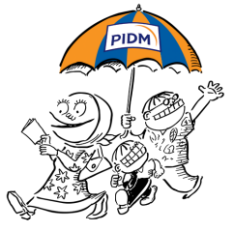
Lee Yee Ming

PIDM

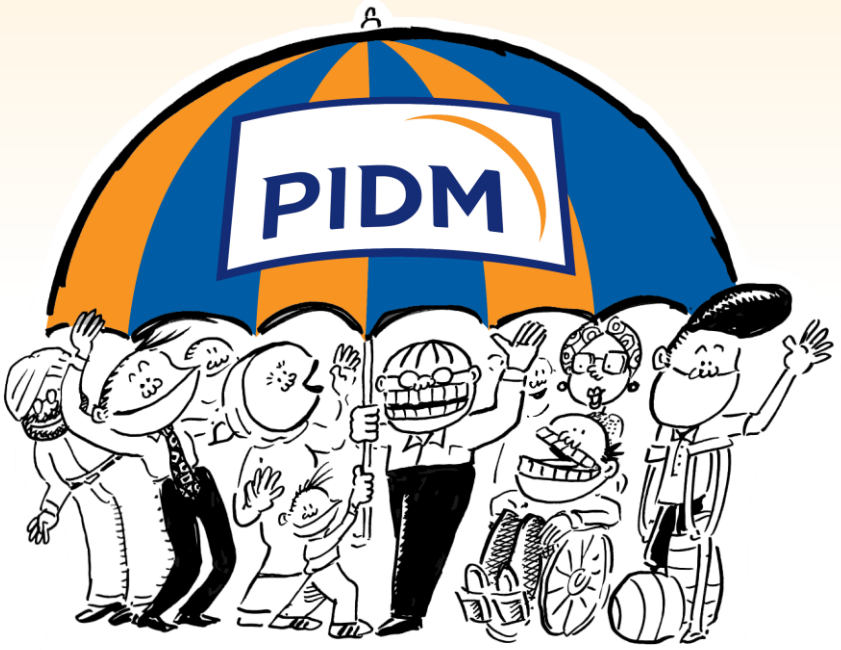
Perbadanan Insurans Deposit Malaysia
Protecting Your Insurance And Deposits In Malaysia

Agenda

- Introduction
- How policyholders and depositors are protected by MDIC
- Benefits of Integrated System - Malaysian Experience
- Conclusion



Introduction

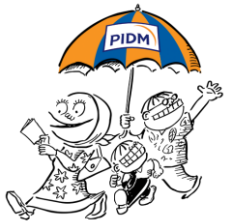


Something about MDIC

- MDIC is a statutory body established under the Malaysia Deposit Insurance Corporation Act (MDIC Act) in September 2005 to administer the national deposit insurance system aimed at protecting depositors

- MDIC Act was amended in 2010:
  - Enhanced mandate to protect Takaful and Insurance Benefits Protection System ("TIPS")
  - Exit Government Deposit Guarantee (implemented on 16 Oct 2008)
  - Increased deposit protection limit to RM250,000
  - Wider intervention and resolution toolkits

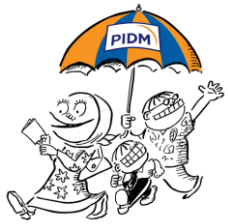
- MDIC is the resolution authority for member institutions (insurance companies and banks) under the Financial Services Act 2013 and Islamic Financial Services Act 2013



What's New?

- MDIC Act amended further in 2015:
  - Strengthened resolution powers - included compulsory share transfer power
  - Aligned the provisions with Financial Services Act 2013 and Islamic Financial Services Act 2013 (law governing the member institutions)

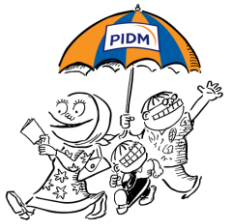
- Going forward:
  Malaysia Financial Sector Blueprint 2011-2020 envisages to enhance the role of MDIC as a resolution authority for dealing in an orderly manner with large, non-viable financial institutions in Malaysia that can affect financial stability



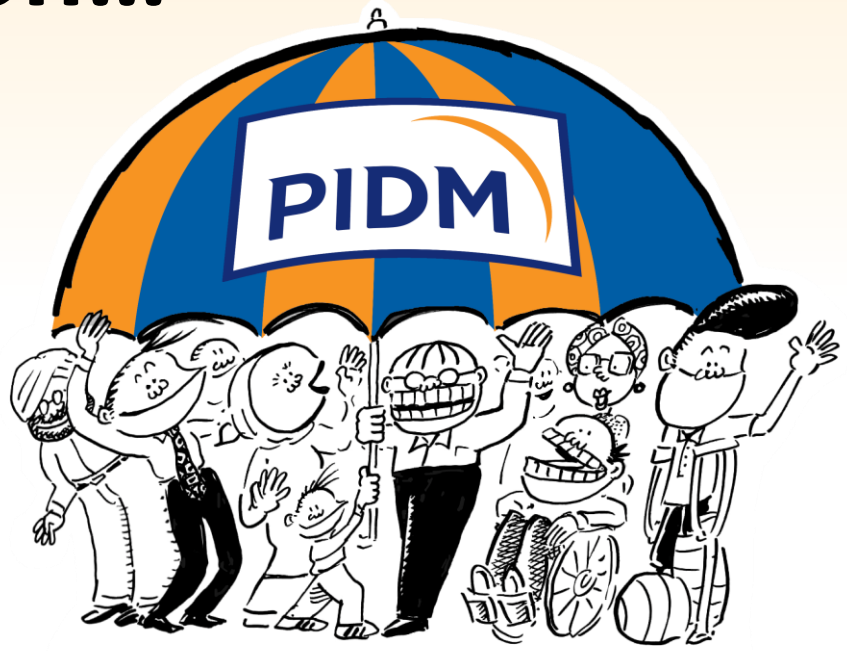
Principles on financial consumer protection

G20 High Level principles to enhance financial consumer protection ("FCP")
Consumer confidence and trust in financial services promotes financial stability, growth, efficiency and innovation over the long term

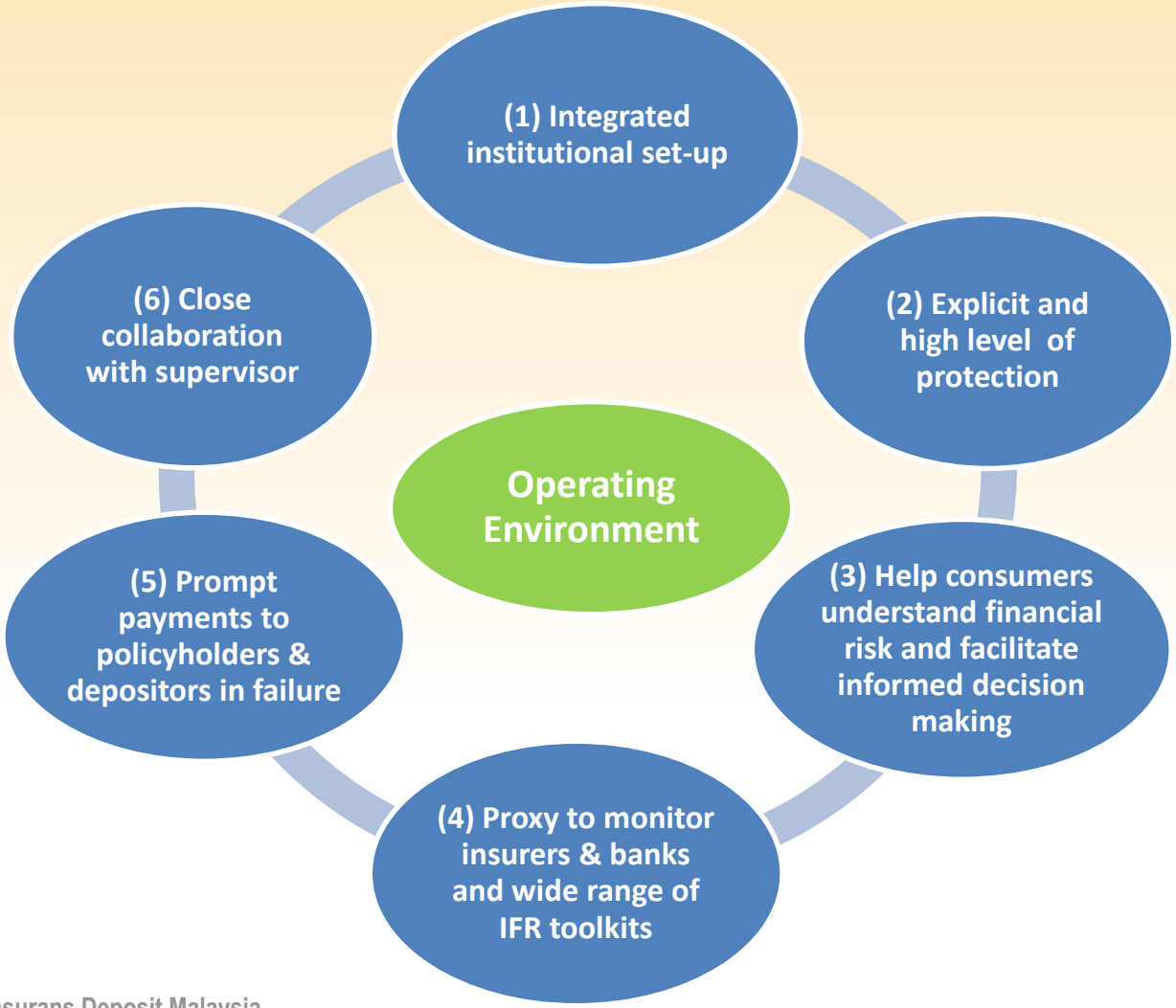
1. FCP should be an integral part of the legal regulatory and supervisory framework.
2. FCP oversight bodies should have the necessary authority to fulfil their mandates.
3. All financial consumers treated equitably, honestly and fairly – special attention dedicated to the needs of vulnerable groups.
4. Provision of key information on fundamental benefits, risks and terms of the product.
5. Promote financial education and awareness on consumer protection, rights and responsibilities. Help consumers to understand the risks and make informed choices.
6. Financial service provider and its agents responsible for upholding financial consumer protection.
7. Protection mechanism to protect consumers' assets (deposits, savings etc.) with high degree of certainty.
8. Protection of consumers' financial and personal information.
9. Access to complaints handling and redress mechanisms.
10. Promote competitive markets – provide consumers with greater choice.

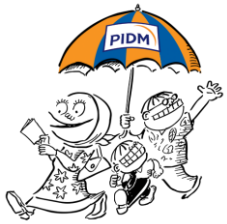


MDIC:
One Stop Centre for Policyholders and Depositors Protection…



How policyholders & depositors are protected by MDIC - areas of collaboration





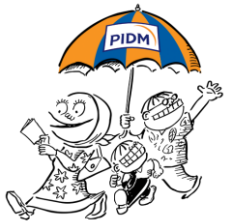
Operating Environment:
Characteristics of the Financial System and Financial Supervisor facilitates collaboration

Integrated Financial System

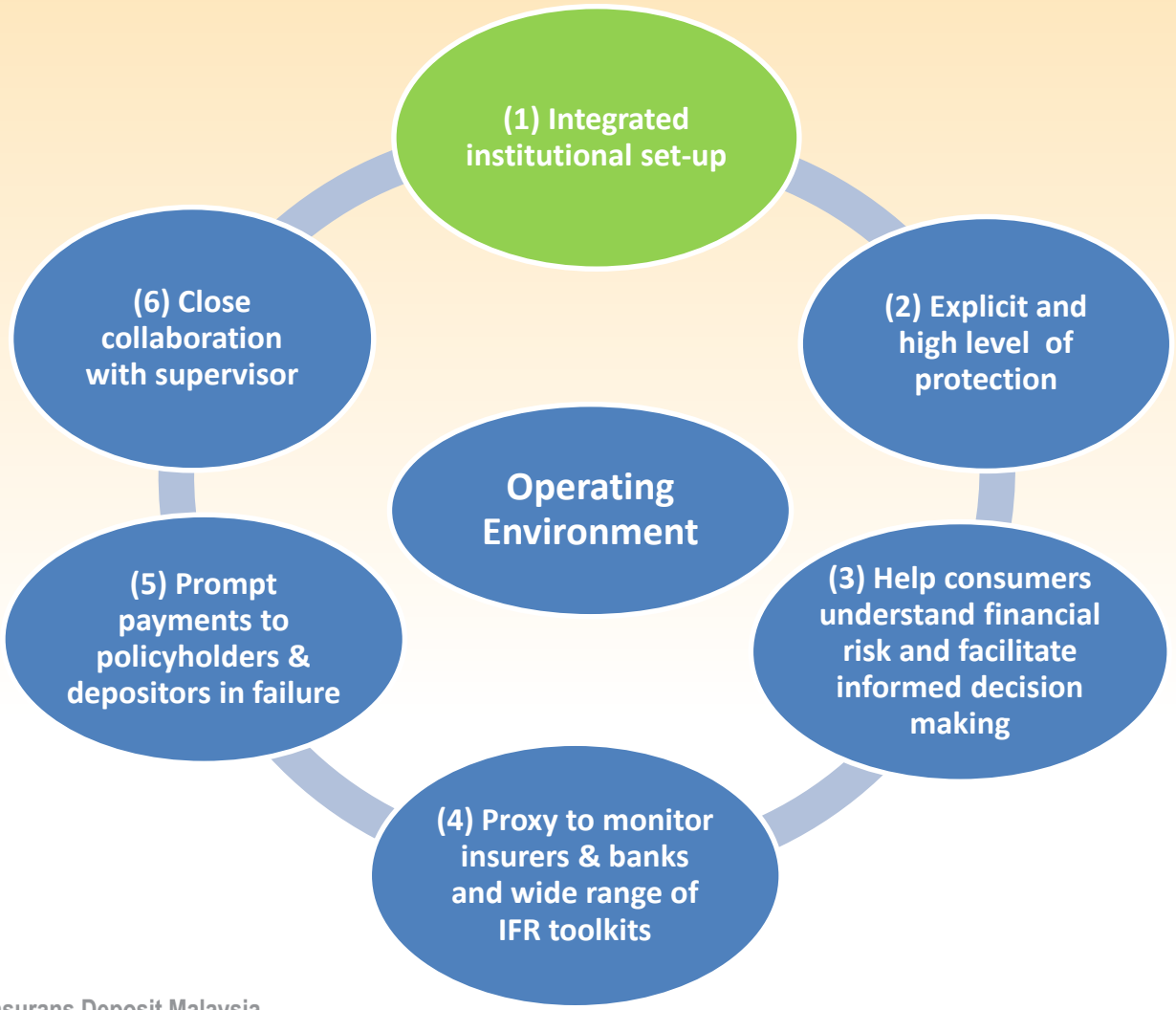
- Most banks and insurance companies (4 of the 6 largest insurance companies) in Malaysia are within the same financial group/conglomerate
- Increasing complex interactions and interconnectedness between sectors and players

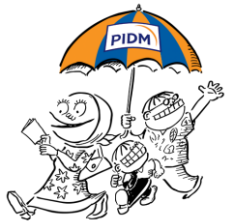
Integrated Financial Supervisor

- Bank Negara Malaysia (BNM) is the supervisor for banks and insurance companies in Malaysia



How policyholders & depositors are protected by MDIC - areas of collaboration





Integrated institutional set-up: Mandate; Legal Framework; Governance Structure

Mandate Encompass IGS & DIS

(1) Administer deposit insurance system ("DIS") and takaful and insurance benefits protection system ("TIPS") under the MDIC Act

(2) Provide insurance or protection against the loss of part or all of:

(a) deposits; and (b) takaful or insurance benefits

(3) Provide incentives for sound risk management in the financial system

(4) Promote or contribute to the stability of the financial system

In achieving its objects under (2) and (4), MDIC shall act in such manner as to minimize costs to the financial system

Common legal framework

IGS and DIS administered by MDIC

IGS and DIS governed under MDIC Act 2011

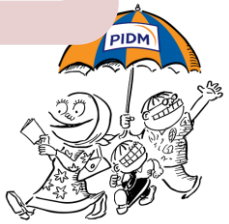
Common governance structure

Board of Directors:

(i) from other safety net members (Governor of Central Bank and Secretary General of Treasury)

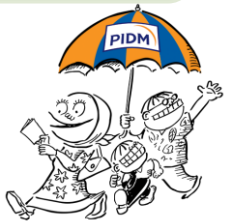
(ii) with banking and insurance industry expertise

Consolidated Annual Report tabled at Parliament and published to public



Common public policy objectives: Public interest as primary objective

Provide a financial safety net for financial consumers of the insurance and banking industry	• by alleviating financial loss to the policyholders and depositors in the event of a failure and enhancing the stability of the financial system
Accord similar protection for consumers of the insurance and banking industry	• by minimising competitive distortion amongst players in the financial sector
Promote and contribute to the growth of the insurance and banking industry	• by education • by maintaining public confidence
Complement supervisor's efforts to promote sound risk management of insurers and banks	• through risk assessment & monitoring • through differential levy/premium system and premium surcharge
Explicit intervention and resolution powers	• enable prompt and effective intervention and resolution measures • in a manner as to minimise cost to the financial system



Membership requirements for IGS & DIS

Mandatory & automatic - Included retail insurers/banks, excluded wholesale

IGS and DIS member institutions subject to same obligations and responsibilities

(to promote safety and soundness as well as facilitate prompt intervention and failure resolution)

IGS

MANDATORY

- ✔ Life and General insurance companies
- ✔ Family and General takaful operators

EXCLUDES

- ✗ Reinsurers
- ✗ Financial guarantee insurer

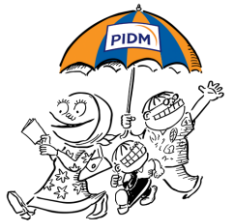
DIS

MANDATORY

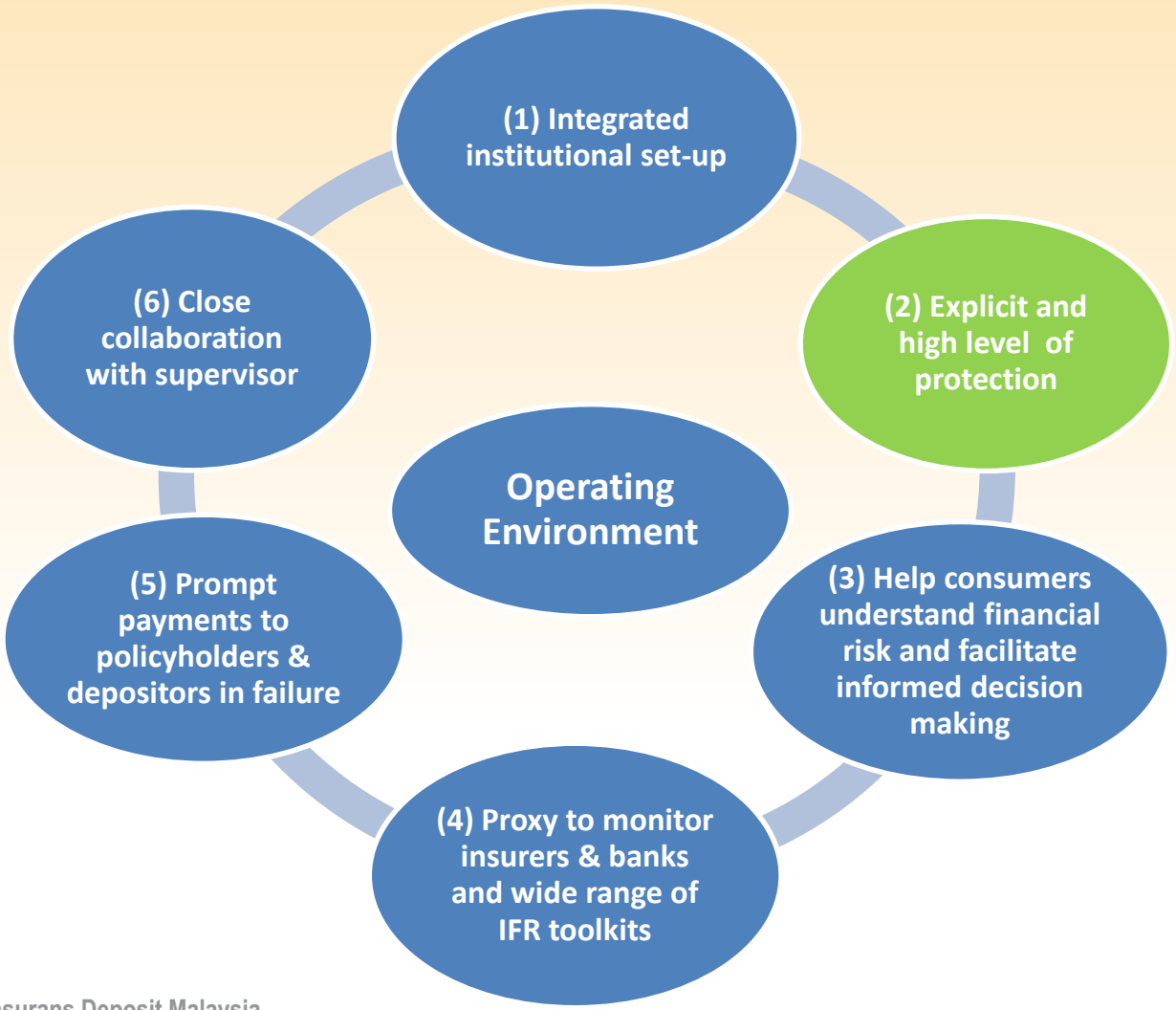
- ✔ Commercial banks
- ✔ Islamic banks

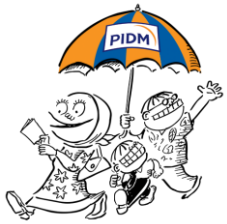
EXCLUDES

- ✗ Investment banks



How policyholders & depositors are protected by MDIC - areas of collaboration

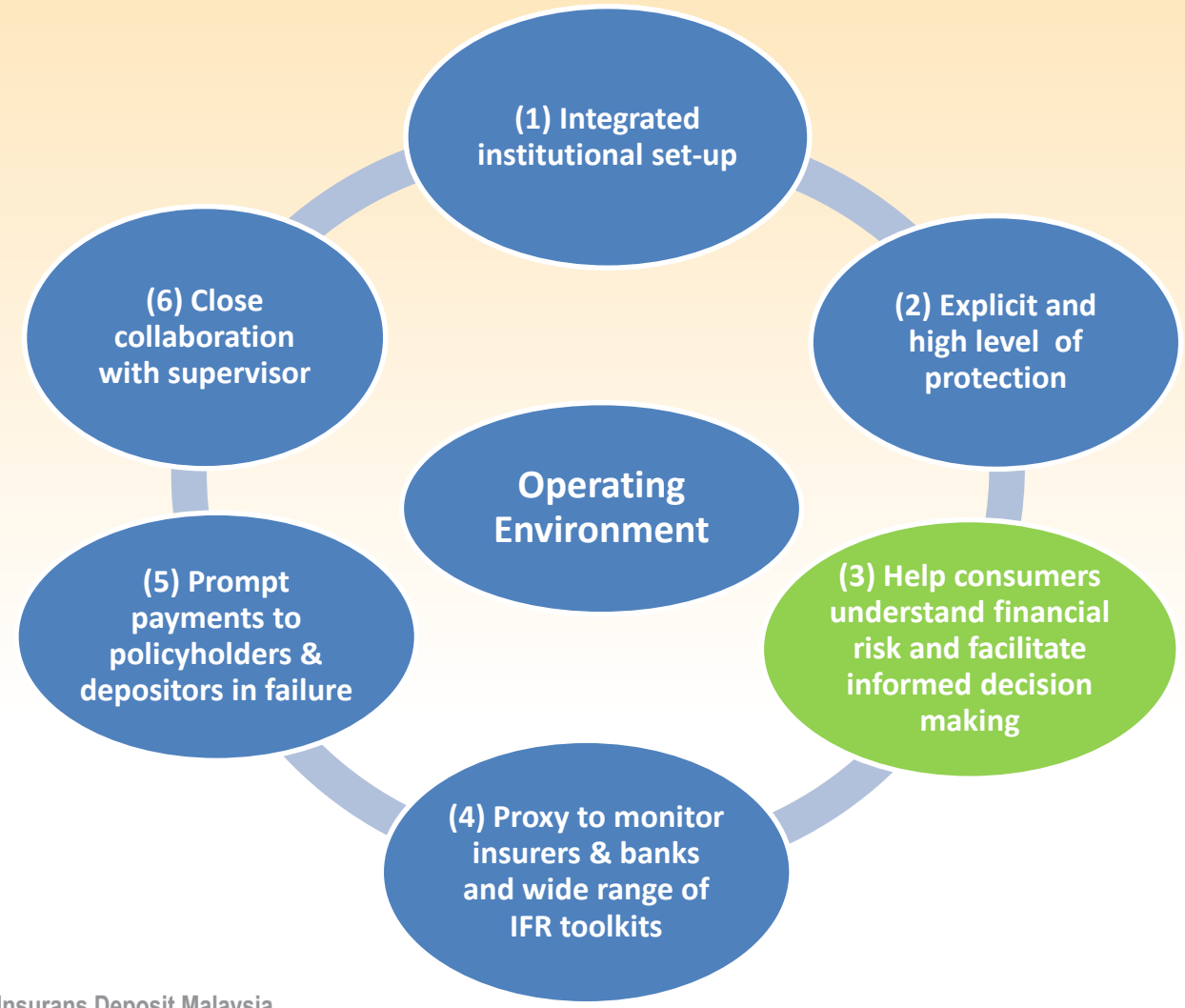


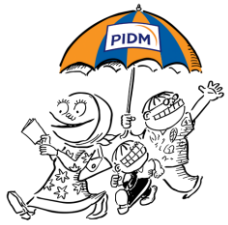


Policyholders and depositors are accorded explicit and high level of protection

Explicit Protection for IGS and DIS	• Absolute protection limit (generally RM500,000 for policyholders and RM250,000 for depositors) • Application of aggregation rule • Prohibition on policyholders or depositors being charged for the protection
High level of coverage - prevent run or surrender	• Majority of the policyholders and depositors protected in full • Majority of benefits insured and deposit products are protected • Regular assessment of coverage
Geographical Limit - Host Country Principle	• Protects policies issued by insurer and deposits placed with banks licensed in Malaysia
Policyholders and Depositors Protected	• Generally all types of policyholders and depositors are protected - individuals, corporations, sole proprietors, partnerships etc.

How policyholders & depositors are protected by MDIC - areas of collaboration





Policyholders and depositors are informed of MDIC's protection from pre to post-contractual stage

Pre-contractual
(to facilitate informed decision-making)

- Display of prescribed statement and membership representation in advertisements
- Display of MDIC's brochure and membership representation at offices and website of member institutions

At Point of Sale
(to facilitate informed decision-making)

- Disclosure of MDIC's protection at point of sale

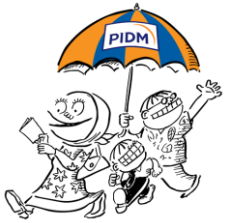
Face-to-face sales, online sales, sales through mail and telemarketing sales

At/After Conclusion of Contract
(continuous awareness)

- Display of prescribed statement in policy documents and correspondences

Prescribed statement:
(i) Call for action statement
(ii) Negative statement on non-protection

IGS (to be implemented) and DIS (in place)



Comprehensive and integrated public awareness and financial literacy programs

Public awareness programs

Inform public of IGS & DIS through:
(i) brochures, advertisements, website
(ii) social media, information video
(iii) briefings, roadshows
(iv) staff of member institutions, agents

Key messages:

(i) MDIC's functions

(ii) Existence of IGS and DIS

(ii) Limits and scope of coverage

(iii) Contact details of MDIC

Financial literacy programs

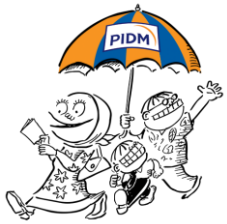
MoneySmart program for younger generation

Key messages:

(i) Know Your Products - understanding the type of financial product offered.

(ii) Know Your Financial Risks - assessing individual financial goals and risk tolerance, and understanding the risks associated with each financial product.

(iii) Know Your Financial Rights - awareness of consumer rights and responsibilities as well as the protection available through MDIC.



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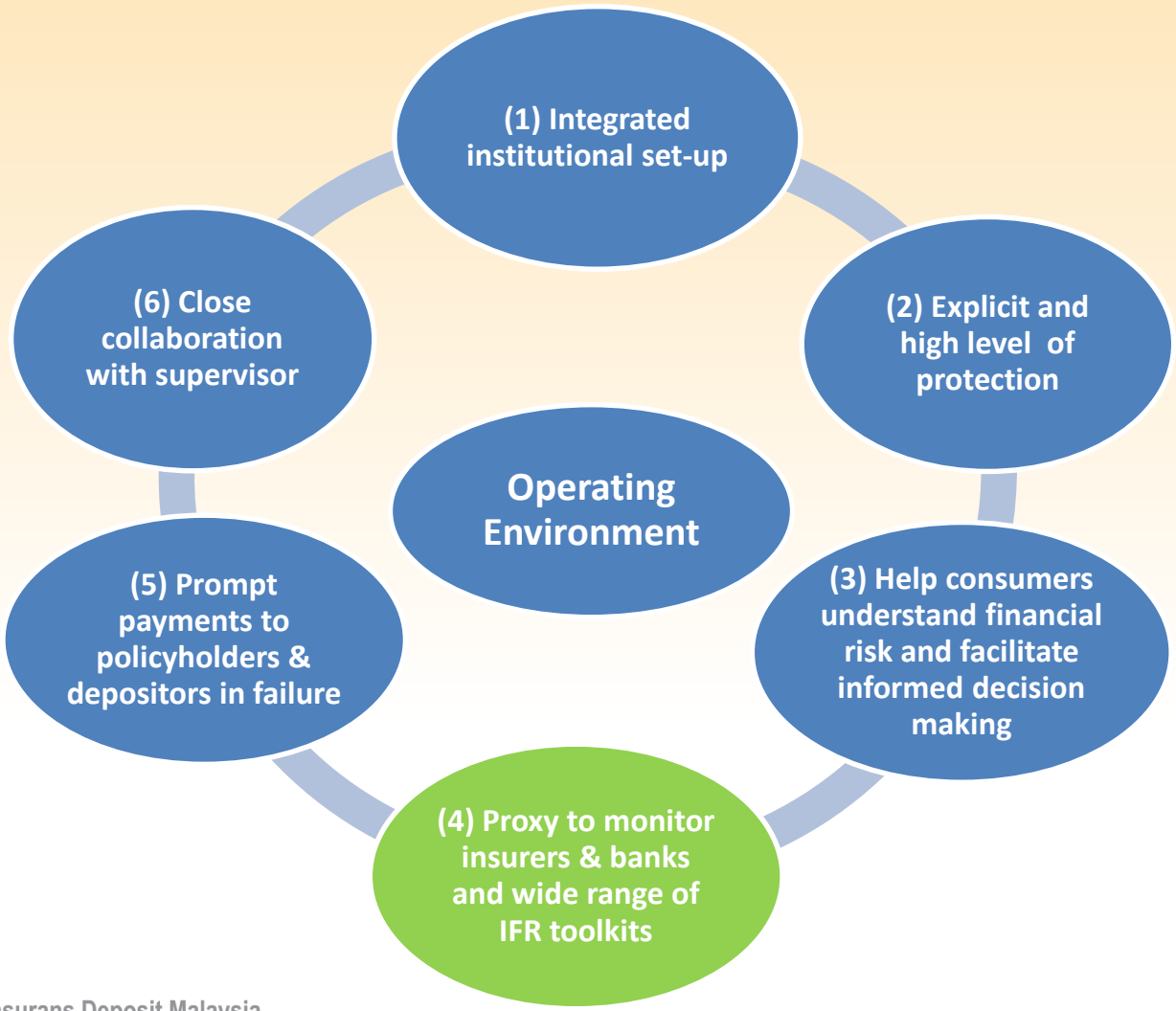
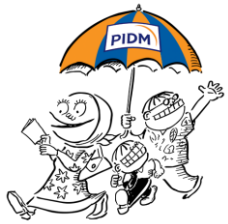




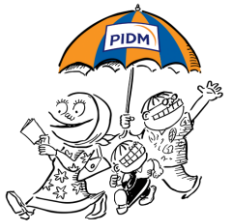
Act as proxy for retail policyholders and depositors to monitor the safety and soundness of insurers and banks

Based on structured risk assessment framework

Continuous risk assessment and monitoring of members safety and soundness

For early detection and intervention

Risk assessment and monitoring of IGS and DIS members



Loss Mitigation Powers: Intervention Powers and Actions

MDIC may acquire/subscribe to shares of a member institution.

MDIC may :
(a) provide loans or advances or financing with or without security, or guarantee with or without security any loan or advance or financing provided to a member institution, except for purposes of liquidity assistance.
(b) make a deposit with a deposit taking member.
(c) impose a premium/levy surcharge on the member institution.

MDIC may acquire assets from a member institution.

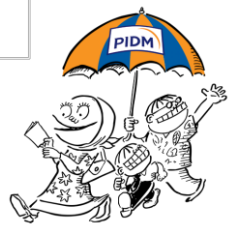
MDIC may guarantee or assume all or part of the liability of:
(a) a deposit taking member in respect of a deposit.
(b) an insurer member in respect of takaful/insurance benefit.

MDIC may make a loan or provide financing, whether with or without security, to a corporation other that a member institution

- **For the purpose of or in connection with the implementation of any resolution actions; or**
- **For purpose of reducing or averting a risk to the financial system or a threatened loss to MDIC.**

Failed Insurance Company/Bank comprises of:

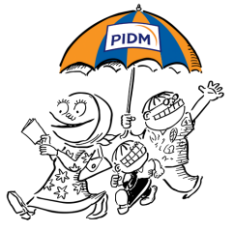
- **Assets**
- **Liabilities**
- **Employees**
- **Business Undertakings**



Special Examination Powers: Detailed Assessments and Investigations

Special examination of a member institution - reason to believe that a due diligence or other examination is required for:

- Exercise of loss mitigation and failure resolution powers
- Preparedness to reimburse insured policyholders & depositors (“payout”)



Failure Resolution Powers: Prompt Execution of FI Resolution Actions

(a) MDIC may acquire shares of a member institution from its existing shareholders.
(b) MDIC may reduce share capital and cancel shares of member institutions under assumption of control (subject to conditions and with Court approval).

Existing Shareholders

(a) MDIC may subscribe to shares issued by the member institution (i.e. new money).
(b) MDIC may transfer shares, warrants, rights of member institutions to any person (compulsory share transfer)

MDIC may:
(a) Require a member institution:
- To take any steps/action as MDIC considers necessary
- Cease soliciting , taking or repaying deposits or cease issuing, renewing or making payments under insurance policies
- Restructure the whole or part of its business.

(b) Terminate membership of member institution.
(c) Present a petition to the High Court for the winding up of the member institution.

Failed Insurance Company/Bank comprises of:

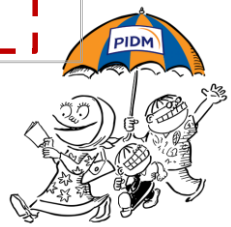
Assets

Liabilities

Employees

Business Undertakings

MDIC may:
(a) Assume control of the whole or part of the assets, liabilities, business and affairs of the member institution.
(b) Apply to the High Court to appoint a receiver, manager or receiver and manager to manager the whole or part of the assets, liabilities, business and affairs of the member institution.
(c) Transfer such assets, liabilities, business and affairs of the member institution to a Bridge Institution.



MDIC's Other Resolution Powers

Power to borrow/raise funds

- Ability to borrow funds from Government or otherwise raise funds in such manner as MDIC thinks fit

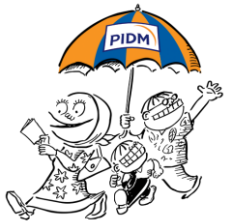
Powers to acquire and manage assets

- Appointment of conservators over delinquent assets of failed member institution
- Ability to set up subsidiaries (Bridge Institutions, Asset Management Company)

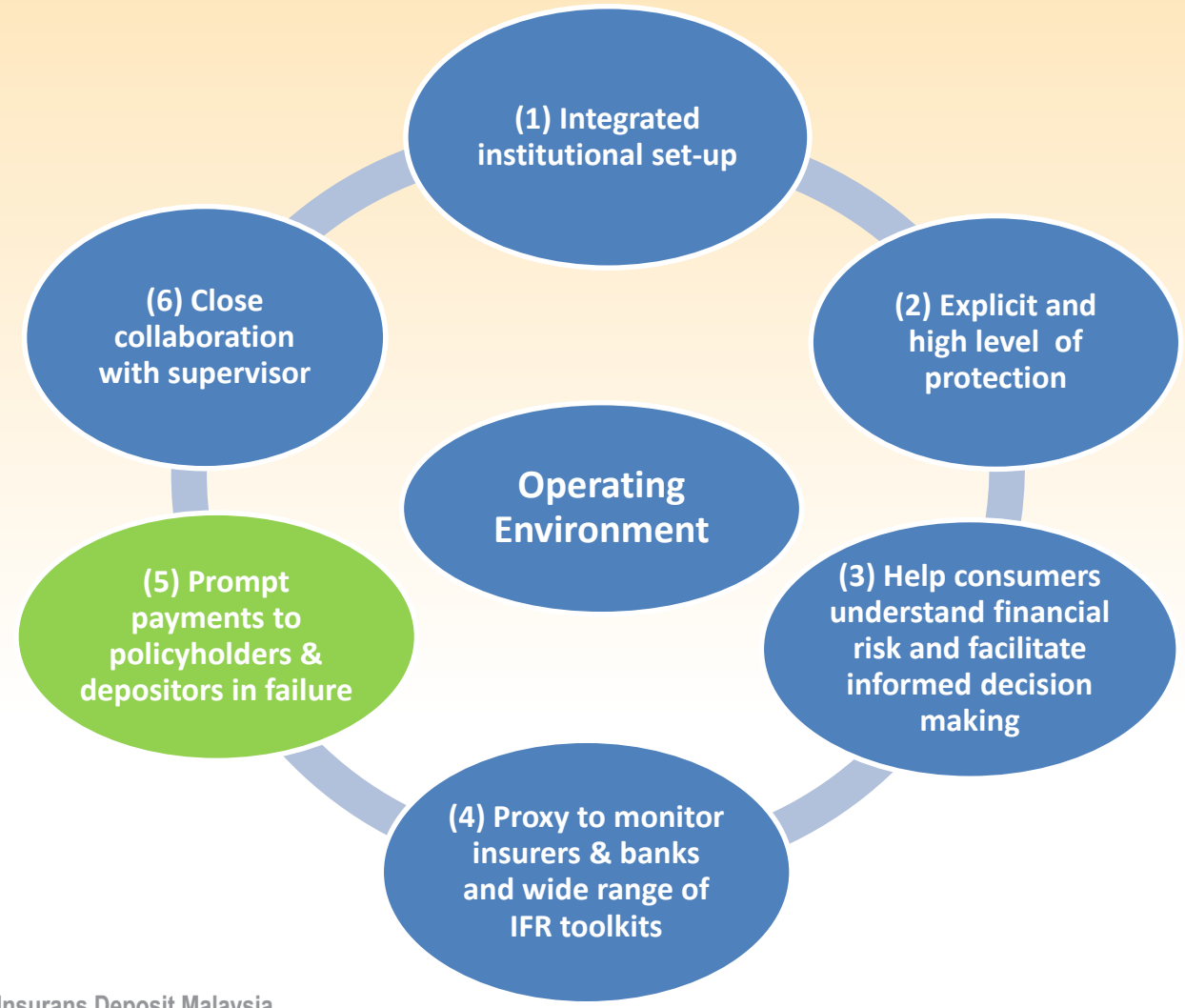
Developing Resolution Planning Framework

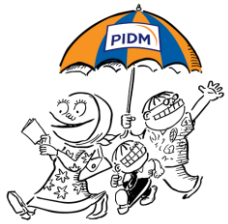
- For orderly resolution of troubled member institutions

Without systemic disruptions and minimize risk of loss to public funds and preserve continuity of systemically important functions.



How policyholders & depositors are protected by MDIC - areas of collaboration





Funding - Critical for prompt reimbursements

Common basis of funding
Combined ex-ante and ex-post

Common methodology
Based on risk profile of members to promote sound risk management practices

Separate funds by business type

Target fund in place to assess sufficiency of fund

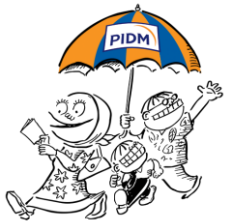
Cover annual operating expenses and build Insurance Funds over time

Government credit line facility for immediate liquidity needs

Ex-ante annual premium contributions

Ex-post levies to fund unexpected losses and to rebuild insurance Funds when necessary

Conventional Deposit | **Islamic Deposit** | **Life Insurance** | **General Insurance** | **Family Takaful** | **General Takaful**



Policyholders and depositors protected through prudent fund management, payout readiness and priority in liquidation

Investment of IGS and DIS funds subject to stringent permitted investment

- RM denominated securities issued by Government or BNM
- Deposits with BNM
- Deposits with FI - for day-to-day operational cash management only

Payout - timely, efficient and target publicly communicated

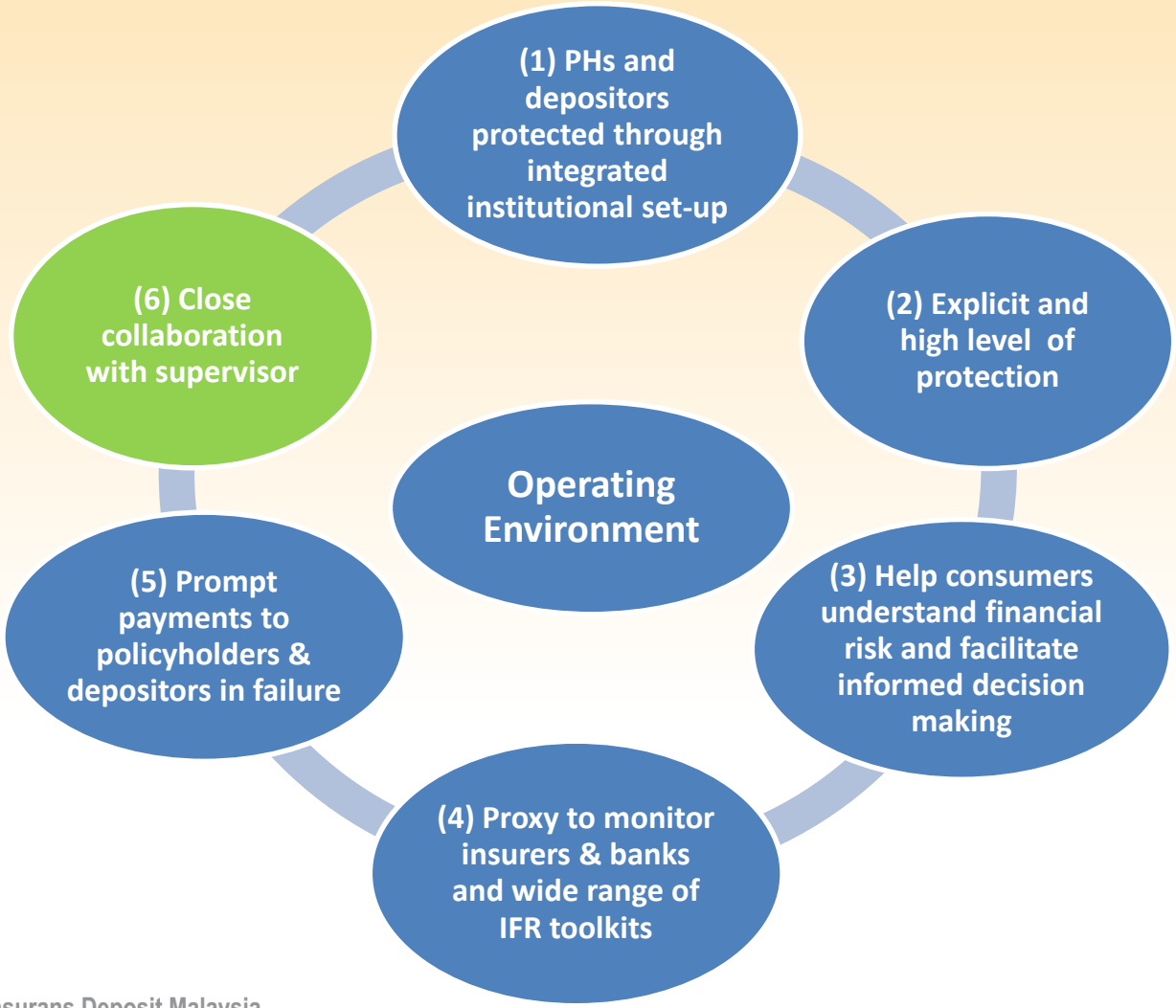
- Policyholders:
  - (i) Refund of premium to facilitate purchase of replacement policy
  - (ii) claims payment upon complete documentation
- Depositors reimbursed as soon as possible (mandatory within 3 months)
- Payout infrastructure:
  - (i) IGS - being developed
  - (ii) DIS - in place

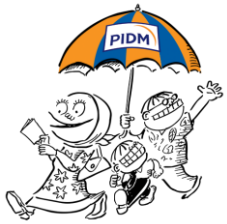
Statutory priority to policyholders and depositors in liquidation

- (i) Unpaid policyholders;
- (ii) Unpaid depositors; and
- (iii) IGS/DIS (subrogated amount)

rank pari passu and in priority over other unsecured creditors

How policyholders & depositors are protected by MDIC - areas of collaboration





Close collaboration with supervisor – key to effective risk assessment and resolution for IGS and DIS

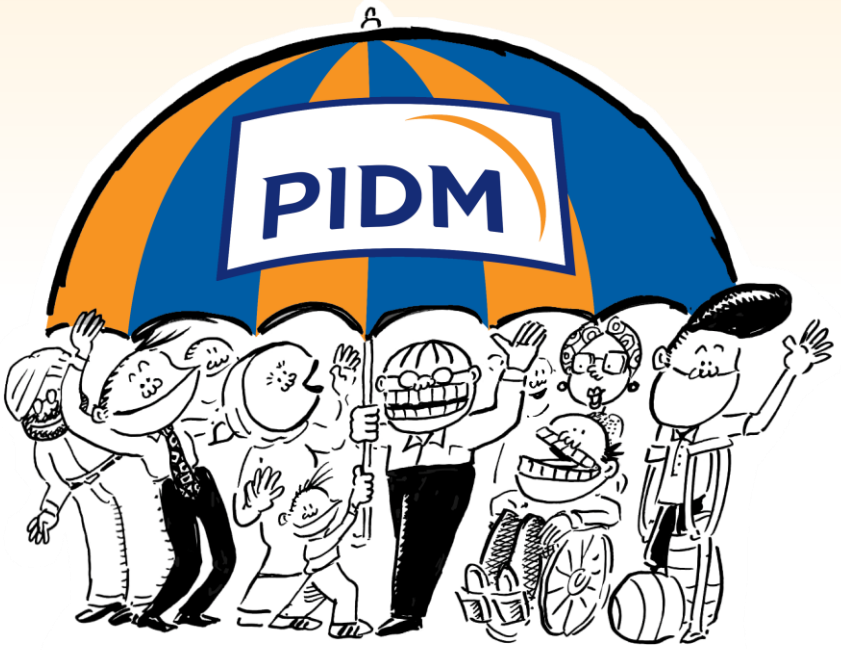
Strategic Alliance Agreement

- Formal arrangement
- Sets out areas of collaboration and cooperation between MDIC and supervisor (BNM)

Areas of cooperation covers IGS and DIS:

- (i) Timely exchange of information on member institutions of IGS & DIS
- (ii) Collaboration in risk assessment and monitoring activities
- (iii) Collaboration in intervention and failure resolution activities

Benefits of Integrated System - Malaysian Experience



Benefits of Integrated Approach

Integrated in Law and Operations

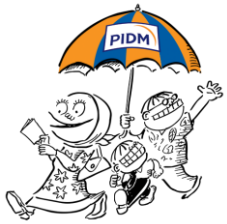
- MDIC Act as the single source of reference for both systems, without much changes required to the original Act

Co-ordinated Policy Decision

- Minimises inconsistencies and inter-agency conflicts in policy decisions and approach
- Avoid competitive distortions that may impede effectiveness in maintaining stability

Synergies in Implementation

- Synergies in implementation of policies vis-à-vis infrastructure and supervisory resources



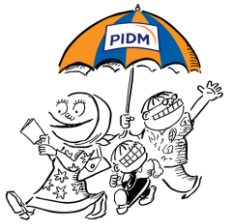
Benefits of Integrated Approach

Holistic Overview of Sectors

- Provides holistic overview of the sectors and their risks in an integrated manner

Improve Crisis Response Capabilities

- Single point of contact for intervention and failure resolution matters, especially during severe financial distress
- Integrated agency facilitates financial institution intervention & failure resolution



Benefits of Integrated Approach

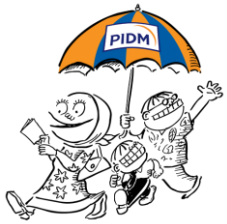
Operational Efficiency & Effectiveness

a) Specialised Skills

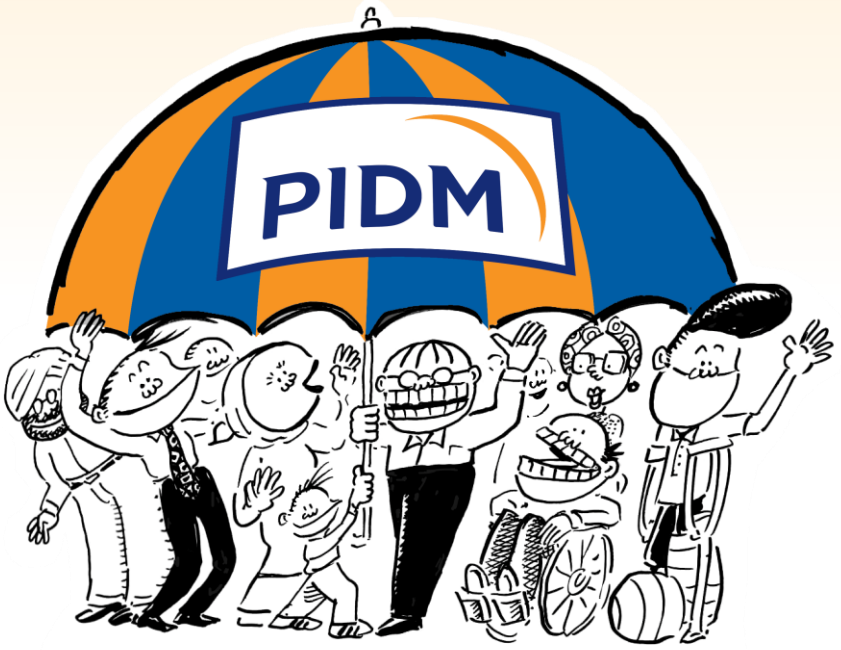
- Deposit insurance agency is well positioned to facilitate the resolution of a wider range of financial institutions including insurance companies

b) Economies of Scale and Scope

- Eliminate duplicate compliance requirements
- More efficient resource allocation as agency will leverage on similar infrastructure and supervisory resources
- Integrated primary prudential regulator needs to deal with only one agency for deposit insurance and insurance compensation issues



Conclusion

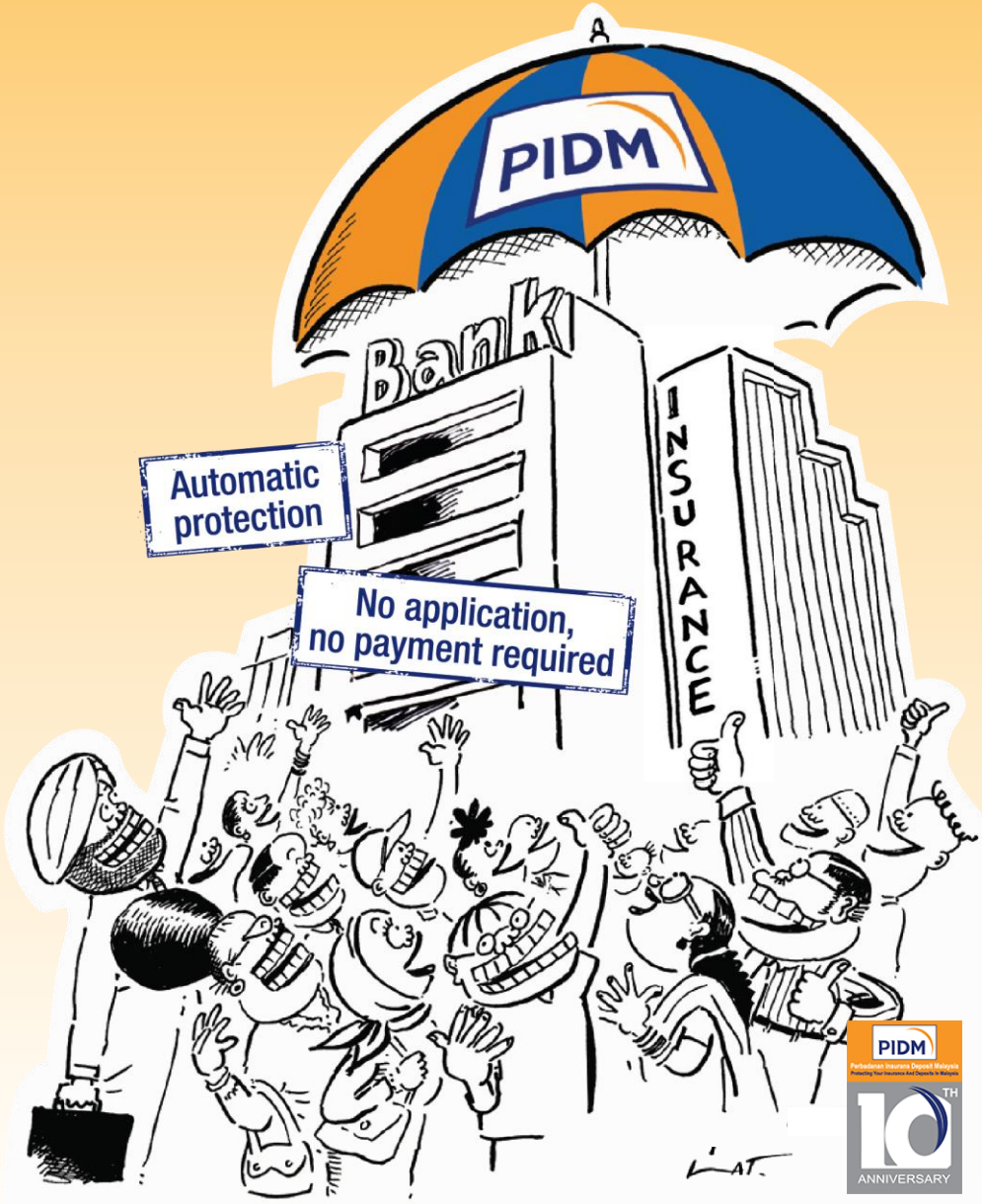


Regardless of institutional arrangements, financial stability is key

- Institutional arrangements are normally path dependent, no one right answer, it depends on history, cultures, experience, regulatory arrangement and financial system characteristics of each jurisdiction

- Effective safety net arrangement:
  - ✓ Promotes financial stability
  - ✓ Ability to make decisive and independent decisions
  - ✓ Effective resolution system
  - ✓ Access to seamless flow of information between all safety net players
  - ✓ Access to government support and backing in severe economic distress
- Any institutional arrangement that best promotes these would probably be the one to pursue.

Thank you



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