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November 15, 2016

Swiss Re Comments on the Consultation Document for Review on the Federal Financial Sector Framework
Delivered Electronically

Dear Sir or Madam,

Swiss Re Canada respectfully submits this comment letter in response to the Department of Finance Canada's ("Department") consultation document for the review of the federal financial sector framework. Swiss Re is a 153-year-old global reinsurance company that has helped Canada recover from disasters since 1911. Swiss Re currently employs approximately 230 highly skilled professionals throughout Canada, each dedicated in their professional capacity to our higher purpose of making the world more resilient.

Introduction

Swiss Re supports the efforts of the Department of Finance to review Canada's federal financial sector legislative and regulatory framework. It is our belief that regulators and lawmakers who develop these frameworks should seek to balance the need to protect consumers and the wider economy, with the desire to create and support a robust financial services industry. Most importantly, policymakers should seize the opportunity to create a financial services sector that actively makes society more resilient, more inclusive and more equal.

In that spirit, the three core policy objectives articulated by the Department that guide Canadian financial sector policy resonate strongly with the value proposition of the (re)insurance industry and our own. By paying claims in a timely fashion, (re)insurers ensure stability and promote long-term prosperity. By diversifying risk across the world, (re)insurers actively transfer the costs and benefits across national borders. In addition, by providing solutions that range from simple personal coverage to very complex business interruption and supply chain risk mitigation, (re)insurers innovate every day to be relevant to their broad range of clients. Consistently updating the financial framework of reference to reflect the changing world we operate in is critical to ensure that (re)insurance can continue to help all clients – individuals, business and the public sector – assess their risk and close their protection gap.

The following are three specific recommendations that would greatly enhance the existing framework:

Internationalization of the insurance sector

The internationalization of the insurance sector is a self-evidenced phenomenon that is only accelerating over time, the main reason being that it harnesses many of the intrinsic benefits of insurance on an ever-greater scale. The international re/insurance sector relies on the ability to diversify risk and deploy capital globally, across borders. The ability for insurers to diversify and pool risk is a cornerstone of making the sector more efficient and resilient to economic shocks. By accessing large numbers of policyholders in markets across the world, insurers develop portfolios of products that address different risk factors and geographies, and are thereby able to provide a wide array of products to consumers at competitive prices. Developing and enforcing a robust and appropriate financial sector policy framework is essential to supporting the internationalization of the insurance markets.

As an example of regulation that would support internationalization and consumers, the Department of Finance could assess the feasibility and marginal risk introduced by allowing US based accounts and securities that settle through the Depository Trust Company to be eligible for inclusion in a Reinsurance Security Agreement (RSA), assuming the account is created with necessary legal control similar to US-based credit for reinsurance trusts with the Canadian ceding company named as a beneficiary. The advantages to doing so would increase the investment flexibility for both Canadian and foreign insurance companies doing business in Canada, allowing greater options to enhance yield and improve pricing for Canadian consumers. Additionally the expanded investment universe allows additional options for managing risk in the liability profile such as interest rate risk and credit risk; while the risk it introduces, currency risk, is more easily monitored and controlled. This also would serve to increase the diversification of the portfolios held as collateral currently for Canadian ceding insurers.

Stabilization and long term support of financial markets across diverse asset classes

The insurance industry is a major investor in financial markets across diverse asset classes. This results in liquidity and stability, thanks to the conservative investment profile and low trading volume that characterize our asset management strategy. By the nature of the long-term liability the industry assumes, we are the perfect investor in long-term asset classes, such as securitized infrastructure development projects. This type of investment is however not recognized as a class of its own and defaulted under the broader credit category, which results in a de facto cap to the industry's ability to support a proper expansion of the asset class and the broader government policy, which we encourage. In other regulatory environments around the world, for instance Solvency II, corporate and securitized infrastructure investment market risk are separately acknowledged and risk factors are expected to be lowered during the ongoing 2018 regime revision, in recognition of the different risk profile and consistently with the broader EC's agenda on long term investment in green infrastructure.

Climate risk and closing the "insurance" protection gap
Climate change is materially increasing the frequency and severity of natural disasters and weather related events. These catastrophes, large and small, create volatility for businesses and individuals - disrupting budgets, long-term planning and resource management. While mitigation and adaptation strategies will help in reducing the burden, we believe climate risk insurance for catastrophic events such as wildfires, floods and droughts can be an added measure of protection, financial security and business continuity planning. Various levels of the Canadian Government can support the development of such a domestic industry through regulatory, policy and budget measures that will create incentives for the development and purchase of such tools.

We would like to offer an example from overseas of how such a supporting role could be expressed in practice. In 2014, the China Development and Research Foundation, a prominent think tank at the Central Government level of China published a public policy research report - Parametric Insurance Solutions for National Disaster Relief System. Alongside investments by the Central Government in weather data, as well as sponsorship of technical workshops, this policy recommendation spurred several Chinese provincial governments to begin examining the frequency and severity of climate events and financial tools to mitigate the risk. These efforts culminated earlier this year in the launch of a new multi-peril parametric weather insurance coverage for the Heilongjiang province, which for the first time provides the provincial government a clear market indicator of climate risk in addition to structural incentives to invest in mitigation. With the support of the Federal Government, Swiss Re believes similar climate risk insurance solutions can help Canada better price, manage and mitigate its exposure to climate change.

The earthquake protection gap is another area that requires urgent attention. This is especially true in eastern Canada where the take-up rate for earthquake insurance is extremely low. For context, in the event of a 7.1 magnitude quake in the St. Lawrence River Valley between Montreal and Quebec City, the total economic damages are expected to be in the CAD 60 billion range. The large majority of homeowners currently do not have insurance coverage, hence uninsured property owners would look to various levels of government for substantial reconstruction funding. This will be quite a drag on the Canadian economy, beyond the province of Quebec, as studied in a number of independent rating agencies reports on the impact of natural catastrophes on sovereign ratings.

From international experience, we know that when earthquake insurance penetration is high amongst homeowners, the rebuilding effort is evidently smoother and faster; resilience against major events is a proven benefit for those markets. Government funds can be used to deal with immediate safety measures and disaster relief, and to rebuild critical infrastructure rather than having to help homeowners rebuild their private properties. Further, insurance would also absorb a substantial part of the post event mass evacuation and additional living expenses cost for their insureds, and stabilise financial resilience at the individual level, which, if not kept in check, has the potential to result in credit contagion beyond mortgage obligations and further aggravate the economic downturn.

Our considerations do not factor in the additional social cost of displacement, a well-researched phenomenon, which manifests itself through the housing market impact in the abandoned and receiving communities, employment challenges, and often physical and mental health conditions suffered by individuals, families and entire communities.

We would like to offer two real life, contrasting examples. In Italy, where the insurance take up rate is very low, the rebuilding efforts following each of the earthquakes occurred over the last 30 years have been paralyzingly slow, as homeowners have had to wait years if not decades for government actions to actually result in a permanent roof on thousands of families' heads. On the other hand, a close to 100% earthquake insurance take-up rate amongst homeowners in New Zealand allowed them to recover and return to a seemingly normal life relatively quickly following the major back-to-back earthquake events in 2011, without putting additional strain on governmental budgets or the economy. The same virtuous dynamic manifested itself in the well-protected country of Chile, following the devastating 2010 earthquake.

Financial inclusion and the insurance sector

Inclusive insurance plays a key role in providing access and stabilizing the livelihoods of populations that do not traditionally benefit from the full spectrum of financial solutions. From life, accident, and health protection to funding for longer lives, to mitigation of threats from climate change and food security; the financial sector can and does play a key role in enabling access to much needed protection to small and medium enterprises, millennials, indigenous peoples, impaired and low-income populations, among other target groups, either in urban or rural environments, that tend to be under-insured. Credit unions, caisses populaires, small banks, credit card companies, microfinance institutions, governmental agencies, charities and even utility companies, supported by the right regulation, can become the natural distribution channel for new insurance protection. Moreover, financial technology solutions, a growing industry in Canada and worldwide, are anticipated to support a much reduced cost of operations both on the front and back-end, and open the possibility – unattainable so far – for secure and instantaneous settlements on a very large scale. The Government of Canada can support these emerging developments via regulation and policy measures that encourage insurance access and extend protection to all cohorts of the Canadian population.

For example, in Australia, Swiss Re collaborated with non-governmental organizations (NGOs) and the local government to develop a first-of-a-kind solution, focused on providing home contents and car insurance to low-income households. This new product takes a flexible approach to premium payments and reduces administrative costs by allowing payment to be made through the government's social security payment system. The product has no complex features or hidden fees but offers flexible payment options and a simple underwriting and claim process centred on defined events, specified categories, and limits which are specifically selected to be relevant. To further reduce costs, the product is initially distributed

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via a leading microfinance operator; other trusted partners, such as charities and financial counsellors will be brought on as distributors over time.
Swiss Re today is working on more than twenty such initiatives around the world, each bespoke to address a real issue, and believes that such programs – combining product simplicity and affordability with client accessibility – offer a powerful tool to broaden financial inclusion and improve income equality.

Inclusion is further fostered by proper access to relevant medical information; by keeping its knowledge current and complete, the (re)insurance industry can better reflect the benefits of medical advances on healthcare effectiveness and longevity and extend coverage to groups of the population that so far have gone uninsured, or lower the premium for those individuals with improved risk profiles. Nascent examples of broader inclusion in this context are covers for AIDS and diabetic patients, which Swiss Re has pioneered in South Africa years ago and progressively extended to other geographies, including Canada most recently.

Conclusion
Swiss Re appreciates the opportunity to provide our views on this important topic. Since 1863, we have endeavored to make our society more resilient and we strongly support the Department's efforts to review the financial sector framework and look forward to any questions that may arise.

Yours sincerely,

Veronica Scotti
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