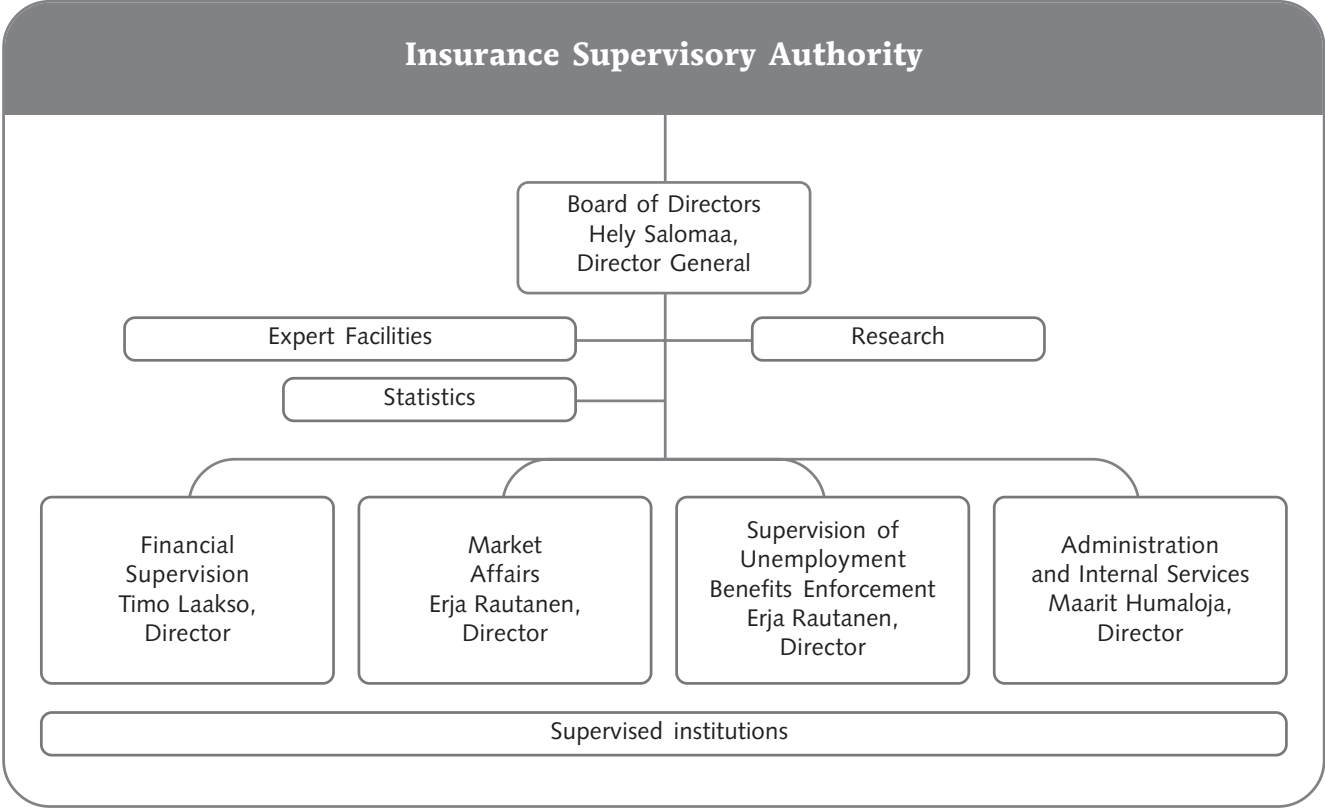


**Insurance
Supervisory
Authority
2003**



VAKUUTUSLAITON

Organisation (31 December 2003)



The administration of the Insurance Supervisory Authority (ISA) is regulated by the Act on the Insurance Supervisory Authority (78/1999), the subsequent amendments thereto (534/2000 and 915/2000) and the decree issued by virtue of the said Act (102/1999). More detailed regulations concerning supervision as well as the powers of the ISA are specified in the special enactments regarding the insurance industry.

The Insurance Supervisory Authority is an institution subordinate to the Ministry of Social Affairs and Health but with independent decision-making powers. The ISA has a Board of Directors established by the Ministry, while the Director General, assisted by the other Directors, is in charge of day-to-day management.

The ISA is divided into four departments: Financial Supervision, Market Affairs, Supervision of Unemployment Benefits Enforcement, and Administration and Internal Services. In addition to these, Expert Facilities, Research, and Statistics units function under the direct supervision of the Director General.

2003

Insurance Supervisory Authority
Annual Report

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Director General's Review

The solvency of the institutions supervised by the ISA improved considerably in 2003, and is generally rather good. The future solvency trend will depend to a great extent on general economic development and its impact on the financial market.

After occupational pension insurance companies' real-estate transactions initiated a major public debate, the ISA performed a relatively extensive investigation on such transactions. Generally speaking, the investigation provided no evidence that properties bought from policyholders would systematically provide a lower yield than those bought from others. A few transactions included in the analysis will be subject to a more detailed examination, and a couple of them may lead to the ISA issuing a reminder to the insurance company involved.

The ISA based its investigation on the net return yielded by properties subsequent to the transactions, measured at current value. The property's estimated market value is normally based on its net present value calculation in which the property's long-term net return and value at the end of the analysis period as well as the investor's yield requirement are taken into account. Furthermore, the result of the analysis is compared to similar transactions performed on the market. However, it is not possible for the ISA to evaluate the correct price of each individual transaction – in fact, the concept of correct price is difficult to apply to property transactions in the first place.

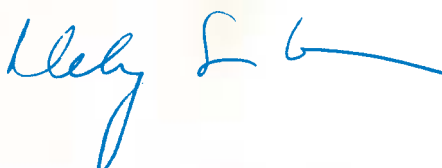
Instead of analysing individual transactions performed in the past, we should focus on the principles that will be applied to future transactions. In my opinion, good insurance practice calls for fair and equal treatment of customers. Property transactions concluded between occupational pension insurance companies and their customers should be based on market terms, and no customers should be granted extra bonuses by purchasing their properties at a premium. The buyer must be able to provide a reliable account, either an appraisal document issued by an independent expert or other such proof, on the justification for the purchase price. Furthermore, the occupational pension insurance company's auditor should verify in his or her audits that property

transactions have been concluded on proper grounds.

The policy adopted by the Finnish Government on changes in the taxation of personal pension schemes has triggered extensive public debate. The ISA sees the proposed change in the taxation of old policies problematic: it is difficult for the policyholder to understand such a change in his or her agreed pension coverage, although the insurance company did not guarantee future tax deductions when the insurance contract was concluded. This will certainly increase the number of enquiries addressed to the ISA by the policyholders. Proposals also require the amendment of the insurance policies and modification of the insurers' information systems in order to enable the maintenance of two coverages for each old policy, one in accordance with the old tax model and one in accordance with the new one. This would generate extra costs, the fair allocation of which to different policyholder groups would be difficult. For these reasons, I find that the tax treatment of old pension schemes should not be changed.

The ISA's reputation was charted as part of a joint survey covering the entire administrative branch of the Ministry of Social Affairs and Health. Carried out in the spring of 2003 and directed at the ISA's stakeholder groups, the survey respondents gave the ISA the grade 7.4 on a scale from 4 to 10. The clear strengths of the ISA indicated by the survey included neutrality, reliability and responsibility. However, the ISA's knownness was found to be rather weak, and the respondents would also like us to improve our humanity, dynamics and initiative as well as the proactiveness of our operations. The overall results of the survey were quite satisfactory for the ISA, considering that it is a rather new organisation.

Finally, I would like to extend my warm thanks to the personnel of the ISA for their hard work in performing and developing our supervisory activities and enhancing our working environment.



Director General Hely Salomaa

I

Strategic resources



1. Business idea

The Insurance Supervisory Authority aims to secure the benefits covered by insurance, ensuring the stability of operations of insurance and pension institutions, and maintaining general confidence in the insurance business. The ISA's vision is to be a skilled, efficient and credible insurance supervisor.

The ISA's task is to monitor and control insurance and pension institutions as well as other operators in the insurance industry. In its financial supervisory capacity, the ISA controls and assesses the supervised institutions' solvency and solvency development, internal control and risk management systems as well as the reliability of their administration. The ISA monitors the institutions under its supervision to make sure that they abide by the law and good insurance practice and that insurance and pension institutions, insurance brokers and unemployment funds apply proper procedures in their customer relationships. The ISA also supervises that insurance terms and conditions as well as statutory non-life insurance premiums conform to law. Furthermore, the ISA promotes research related to the insurance industry.

2. Customers

The ISA's largest customer group is formed by the supervised institutions which, besides being subject to supervision by the ISA, seek from the ISA registration and other decisions as well as permissions and approvals required by law. Other important customers of the ISA include citizens who ask the ISA to examine whether the procedures of the companies it supervises have been properly applied in cases involving complainants. Other customers of the ISA include Finnish and foreign authorities, insurance industry organisations and the media, through which the ISA can enhance its general knowledge of the insurance markets.

3. Starting points and focus of supervisory activities

The starting points of the ISA's operations have been defined from the perspective of their social impact. The cornerstones of the ISA's activities are supervision of the supervised institutions' financial position and procedures, legal supervision and supervision of insurance products, as well as research and communications related to the insurance industry.

Financial Supervision

The aim of the ISA's financial supervision is to ensure that insurers have sufficient resources to fulfil their obligations under the insurance policies they have granted.

The supervision is based on reports linked mainly to the supervised institutions' financial position, which they file to the ISA on a regular basis, as well as supervisory visits to these institutions. The ISA applies computerised solvency analysis to insurance and pension institutions, and performs more detailed supervision on the basis of such analyses.

Another key area of financial supervision is the analysis and assessment of the supervised institutions' internal control and risk management operations.

Legal Supervision

Legal supervision focuses on the interpretation of the rules and regulations in force as well as whether the supervised institutions' operations conform to law. The ISA also undertakes initiatives to develop legislation and participates in the preparation of legislative proposals.

The ISA issues regulations, instructions and statements concerning the parties under its supervision, makes decisions at their request (for example, registration decisions) and issues statements to various authorities and the European Commission. The ISA examines the acceptability of insurance brokers and assesses the reliability and propriety of insurance companies' management. The ISA also monitors compliance to the rules and regulations concerning the prevention of money laundering and maintains various statutory registers.

Supervision of Procedures

The supervision of procedures aims to strengthen the public's trust in the appropriate treatment of customers' affairs by insurance and pension institutions, insurance brokers and unemployment funds.

The ISA evaluates the conformity to law of the procedures taken by the supervised institutions in their customer relationships, handles claims related to such procedures and makes supervisory visits to supervised institutions. Furthermore, the ISA sees to it that unemployment funds enforce unemployment benefit acts in accordance with rules and regulations and that unemployment funds' operating models are consistent.

The ISA's supervision focuses on the procedures taken by each of the supervised institutions in their customer relationships as well as on the marketing activities of insurance companies and insurance brokers.

Supervision of Insurance Products

The purpose of the supervision of insurance products is to promote the availability of lawful insurance

products. The ISA monitors major new products launched by life and non-life insurance companies, and the pricing of statutory insurance policies.

This supervision takes place in connection with regular inspections and supervisory visits as well as in response to cases reported to the ISA by external parties.

With regards to the supervision of insurance products, the general focus is on ensuring that insurance terms and conditions conform to law. In particular, the ISA checks that workers' compensation insurance and motor third party liability insurance premiums are both reasonable and secure with respect to compensation payments.

Research

The purpose of the ISA's research activities is to ensure that knowledge of the risks associated with the insurance business as well as related Finnish research is of as high a quality as possible. The ISA's research activities focus on developing models for the supervision of the insurance companies' solvency and investment operations. Furthermore,



the ISA organises research seminars with various partners and arranges teaching in actuarial mathematics and risk theory in co-operation with the University of Helsinki and other universities.

Communications

The purpose of the ISA's communications is to provide information on its operations and increase general knowledge of the regulation of the insurance industry. The ISA issues analyses of the state and development of the insurance markets as well as statements concerning the insurance industry, when needed.

4. Supervised institutions

At the end of 2003, the ISA supervised the operations of 855 institutions, 50 of which were insurance companies. The largest group subject to monitoring by the ISA consisted of insurance brokers – both brokerage companies and individual brokers – the number of these exceeding 300.

The number of supervised institutions has remained virtually unchanged during the past few years. In general, we can say that the number of company pension funds has fallen by a few dozen, whereas that of insurance brokers has increased correspondingly. Furthermore, the number of notifications submitted by foreign EEA insurance companies on the basis of the freedom to provide insurance services has increased; however, for the time being, the actual operations of these companies are estimated to be minor.

Number of Supervised Institutions (Registered by ISA)

Group Subject to Supervision	31 Dec 2003	31 Dec 2002	31 Dec 2001	31 Dec 2000	31 Dec 1999
Life insurance companies *)	15	15	15	15	15
Non-life insurance companies *)	29	31	33	34	34
Employment pension insurance companies	7	6	6	6	6
Company pension funds *)	110	128	168	208	222
Industry-wide pension funds *)	17	17	18	18	20
Employee sickness and other employee benefit funds *)	166	165	167	169	180
Pension institutions founded on the basis of law	3	4	4	4	4
Local Government Pensions Institution, State Pension Fund, Church Pension Fund	3	2	2	2	
Local mutual insurance associations	105	116	116	117	118
Insurance brokerage firms	67	69	57	44	36
Insurance brokers	260	248	215	190	152
Unemployment funds	42	42	43		
Unemployment Insurance Fund + Educational	2	2	2		
Other	9	9	8	6	6
Foreign EEA insurance companies' representative offices	20	18	17	14	12
Total	855	872	871	827	805

Foreign EEA insurance companies' notifications based on the freedom to provide insurance services 375 347 323 302 267

* The above figures include institutions in liquidation as follows:

Life insurance companies	1	1	1	1	1
Non-life insurance companies	1	1	1	1	1
Company pension funds	17	31	67	98	107
Industry-wide pension funds	2	1	2	1	3
Employee sickness and other employee benefit funds	10	9	12	12	17

5. Co-operation and interaction

The ISA functions in close co-operation with the Finnish Financial Supervision and the Insurance Department of the Ministry of Social Affairs and Health. The ISA has a separate co-operation agreement with the Financial Supervision on the supervision of finance and insurance clusters.

Both the ISA and the Financial Supervision have joined a general co-operation agreement enhancing co-operation between finance and insurance supervisory authorities in the Nordic countries. With respect to the supervision of Nordea, a financial services group which operates in the Nordic region, the relevant supervisors have concluded a more detailed co-operation agreement.

Co-operation between the EEA supervisory authorities regarding the supplementary supervision of insurance undertakings in an insurance group is based on an EU directive. Practical application of this co-operation is defined in the so-called Helsinki Protocol signed by the relevant supervisory authorities. Furthermore, the ISA has a more detailed co-operation agreement on the supervision of the pan-Nordic If Group with the Swedish and Norwegian supervisory authorities.

With respect to the Baltic countries, the ISA has concluded co-operation agreements with the authorities in charge of insurance supervision in Estonia, Latvia and Lithuania.

To promote education in actuarial mathematics, the ISA has a co-operation agreement with the Department of Mathematics of the University of Helsinki. In accordance with this agreement, the ISA funds part of the salary costs of a lecturer of mathematics. The lecturer is in charge of basic and further education in actuarial mathematics provided by the field of research of Actuarial and Financial Mathematics at the University of Helsinki, as well as related scientific research and theses tutoring.

The ISA has had its own national expert in the Insurance Unit of the European Commission since the beginning of 2003. His duties include participation in the Solvency II project aimed at reforming insurers' solvency framework, in the creation of a harmonised reinsurance supervision system within the

EU, as well as in the supervision of the enforcement of EU legislation in the EU-applicant countries.

International Activities

Following a decision adopted by the European Commission, the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) was founded in November 2003. The CEIOPS will advise the Commission in the preparation of draft implementation measures in the fields of insurance, re-insurance and occupational pensions and contribute to the consistent implementation of EU directives and the convergence of EU member states' supervisory rules and regulations. It also constitutes a forum enhancing supervisory co-operation, including the exchange of information on supervised institutions, and thus contributes to the convergence of the supervisors' supervisory practices.

The CEIOPS is composed of high-level representatives from the insurance and occupational pensions supervisory authorities from EU member states. Finland's CEIOPS representative is the Director General of the ISA.

Within CEIOPS, the ISA is actively involved in co-operation based on the Helsinki Protocol, both through a working group which develops the co-operation framework and by participating in joint supervisory groups which focus on the practical supervision of specific insurance groups.

The ISA participates in the work of various working groups functioning under the EU Solvency II project aimed at reforming insurers' solvency frameworks. The purpose is to implement Solvency II through the so-called Lamfalussy process which involves a two-level development of regulation: only general principles would be included in the EU directives whereas the more detailed regulation would be handled by working groups operating under the CEIOPS umbrella.

The ISA is also a member of a working group analysing the possibilities for a harmonised reinsurance supervision system. The proposed system would be based on the fact that an authorisation would be required for taking up the business of reinsurance in any of the EU countries, after which supervision would be based on the principle of one licence. At present, the EU member countries apply national regulations concerning reinsurance supervision. The working group has worked on a draft for a reinsur-

ance supervision directive as well as on the necessary amendments to other regulations, including current life and non-life insurance directives.

The ISA's regular activities include participation in the general meetings of the International Association of Insurance Supervisors (IAIS). The ISA has also been involved in the European Commission's working group, evaluating insurance regulation and control in the EU-applicant countries by monitoring these activities in Estonia and Latvia.

The ISA attends the annual meetings of Nordic insurance and financial supervisors, and is a member of two permanent, pan-Nordic working groups focusing on unemployment benefit systems.

6. Personnel

The ISA's personnel policy is based on a skilled, well-motivated and flexible personnel whose well-being the ISA maintains and enhances through measures that target their ability to work and professional skills as well as the work community.

On 31 December 2003, the ISA employed 62 officials, one less than on the previous year, and there were four vacancies during the year. However, the number of actual person-years was 63.5, up by 3.7 years on the previous year. The average age

of staff was 43.9, which is clearly lower than that of the entire Government personnel.

Thanks to personnel development and the increase in the processing of data in electronic form, staff numbers are expected to remain virtually unchanged, despite certain needs for growth. The outsourcing of services also reduces the needs for recruitment. The ISA has outsourced various support services, including the information systems of the personnel and payroll administration, IT services, access control and telephone exchange.

The ISA personnel have a relatively high level of education. The great majority of them have a university degree, most usually in law, economic sciences or (actuarial) mathematics, thus representing a wide variety of expertise in the various sectors of the insurance industry.

The ISA monitors its employees' job satisfaction and management skills development through related surveys carried out on alternate years. In 2003, the first survey analysing the level of management at ISA was carried out. The results indicated that the ISA management and supervisors should continue to develop their managerial behaviour. Future surveys will provide comparative material enabling the ISA to measure developments in this field.

The highest decision-making body of the ISA is the Board of Directors which convenes once a month.

Board of Directors 31 December 2003

Chairman

Tarmo Pukkila
Director General
Ministry of Social Affairs and Health

Vice Chairman

Carin Lindqvist-Virtanen
Ministerial Adviser
Ministry of Social Affairs and Health

Members

Kaarlo Jännäri,
Director General
Financial Supervision Authority

Pekka Laajanen,
Legislative Director
Ministry of Finance

Matti Louekoski,
Deputy Governor
Bank of Finland

Hely Salomaa,
Director General
Insurance Supervisory Authority

Deputy Members

Matti Toiviainen
Deputy Director General

Leena Väänänen
Senior Actuary

Pirkko Pohjoisaho-Aarti
Deputy Director General

Ilkka Harju
Legislative Counsellor

Heikki Koskenkylä
Head of Department

Timo Laakso
Director

7. Funding of operations

All costs incurred by the Insurance Supervisory Authority's operations are covered by supervision and procedural fees collected from the companies under its supervision. The financing of the ISA's operations is based on the Act on the Financing of the Insurance Supervisory Authority (479/1944).

The ISA's finances are based on net budgeting and a so-called zero budget, which means that the supervision and procedural fees it collects must cover all of its expenses. Any surplus will be taken into account when determining the supervision fee to be collected from the supervised institutions in the following year.

Supervision fees are determined on the basis of cost accounting and the supervised institutions' annual accounts in accordance with the grounds confirmed by the Ministry of Social Affairs and Health. The ISA's budgeted income for 2003 was EUR 5,010,000, of which supervision fees accounted for EUR 4,782,000 and performances under public law and commercial performances, defined in the Act on Criteria for Charges Payable to the State, accounted for EUR 228,000. The invoicing surplus of EUR 0.6 million for 2002 was credited in the supervision fees for 2003. The actual income for 2003 amounted to EUR 4.5 million.

Key figures (EUR '000)

Expenses	2001	2002	2003
Materials, supplies and goods	60	81	60
Personnel costs	2,599	3,001	3,361
Rents	454	579	522
Purchased services	548	443	486
Separate costs in total	93	164	107
Separate costs in total	3,754	4,268	4,536
Depreciation	89	133	107
Imputed interests	21	23	24
Co-operation payments to State agencies and institutions	17	19,9	
Share of joint costs in total	110	174	151
Acquisitions of fixed assets	56	96	25
Total expenses *)	3,812	4,320	4,531
*) Excluding depreciation, imputed interests, sales losses, change in holiday pay liabilities, and rehabilitation based on State Employees Pensions Act			
Number of person-years	54.5	59.8	63.5
Total expenses/person-year	69.9	72.2	71.4

The 4.9 per cent increase in costs was mainly caused by the filling of vacancies. Personnel expenses increased by 12 per cent while other costs decreased from the 2002 level.

8. Changes in the operating environment

According to Eurostat, the estimated increase in GDP in the euro area was 0.3 per cent, whereas preliminary information from Statistics Finland indicates that Finland's GDP grew by 1.9 per cent in 2003. The average unemployment rate in Finland was 9.0 per cent and the employment rate was 67.3 per cent. Unemployment benefits paid by unemployment funds and the Social Insurance Institution of Finland amounted to EUR 2.7 billion, representing an 8.1 per cent increase year on year.

In December 2003, the annual inflation of the euro area was 2.0 per cent, compared to 1.2 per cent in Finland. Market interest rates have been on the rise in the euro area since mid-2003, but the level of interest is still low. The 10-year interest rate is slightly over 4 per cent and the three-month interest rate is 2 percentage points lower. The rise in share prices which commenced in spring 2003 has continued both on the US and European stock exchanges. The euro strengthened against the US dollar by approximately a fifth during 2003.

Insurance and Pension Institutions' Financial Performance

With regards to the solvency of insurance and pension institutions, 2003 was a year of two-sided development. Until the end of March, insurers' overall solvency declined despite the clear fall in the level of interest because, following the general trend in the equity market, the value of their equity assets decreased significantly. The revival of the equity market which commenced at the end of March clearly improved the insurers' solvency towards the end of the year, whereas the impact of changes in the level of interest was minor. The high volatility in interest rates during 2003 affected the total return on bonds, particularly in those insurance institutions that operate actively in the interest-rate market. Individual insurers' solvency status varied quite a lot depending on their investment allocations.

II

Impact of operations



1. Financial supervision

The Financial Supervision department focuses on financial supervision and legal supervision. The department also prepares regulations, instructions and statements and participates in law-drafting. As part of the Financial Supervision department, Expert Facilities focuses mainly on the supervision of the insurers' investment operations as well as on matters involving actuarial mathematics.

Expressed in person years, the Financial Supervision department accounted for 31.5 per cent of the entire operations of the ISA, divided by unit as follows: Expert Facilities 8.3 per cent, Pension Insurance Supervision 10.6 per cent, and Life and Non-life Insurance Supervision 12.6 per cent. The Expert Facilities staff function, which reports to the General Manager, accounted for approximately 4.6 per cent of ISA's total person years.

Financial Supervision

Financial supervision was performed on the basis of confirmed supervisory plans drawn up separately for each supervised institution. As part of its continuous financial supervision, the ISA examined the supervised institutions' financial reporting as well as the quarterly follow-up reports submitted by them. On the basis of this continuous supervision, the ISA focused more detailed supervision activities onto individual operators when necessary. During supervisory visits, the ISA examined the supervised institutions' administrative minutes, targets selected on the basis of supervisory plans as well as targets triggered by continuous supervision.

Inspection practices related to ceded reinsurance were recorded in the form of instructions added to the Supervisor's Handbook. The standardised inspection model will be implemented as of spring 2004.

A working group focusing on measures to be taken when dealing with problematic situations convened several times during 2003. The purpose of this was to record instructions to be provided by the supervisor in various types of problematic situation encountered by the supervised institutions. The working group will continue its work in 2004.

Supervision of Investment Operations

The reporting and monitoring linked to life and non-life insurance companies' investments were revised. Information in line with the new regulations was collected for the first time for the period ending 30 September 2003, to be followed by quarterly reporting from that day on. The report indicates the division of the company's entire investment assets into investment categories which comply for the most part with the practice applied in solvency calculations. The purpose of the report is to collect information in order to assess the risk of value changes affecting the investments. A corresponding reporting practice has been previously introduced in employment pension companies. Furthermore, the supervision of investment operations continued via a number of special inspections.

The ISA charted new investment risks by carrying out a special inspection on selected insurance companies. This involved an analysis of their participation in risk transfers in the form of asset-backed securitisation issues and credit derivatives. In this connection, the ISA also inspected their investments and investment liabilities in private equity funds. These inspections indicated that Finnish insurance companies' participation in asset-backed risk transfers was minor.

An investigation of the employment pension insurance companies' property transactions during the period 1 January 1999–30 September 2003 was carried out at the end of the year. This investigation was found necessary after public allegations regarding property transactions at a premium which employment pension insurance companies were said to have concluded with their customers. The investigation covered 261 property transactions, 19 of which were subjected to a more detailed investigation to be performed in 2004. In other respects, the investigation did not indicate that properties purchased by insurers from their policyholders would systematically provide a lower yield than those purchased from others.

Supervisory Co-operation Involving Sampo and the If Group

The ISA supervised the Sampo Group in close co-operation with the Finnish Financial Supervision. This co-operation included meetings between the representatives of the ISA and the Financial Supervision approximately once a month, as well as a regular exchange of information on the financial status of the supervised institutions and other relevant topical issues. Furthermore, the ISA and the Financial Supervision performed several joint inspections in various fields at Sampo.

In 2003, the ISA and the Financial Supervision started to develop a model enabling them to better quantify and evaluate financial risks within the Sampo Group. The aim of this work is to supply a joint assessment of Sampo's sector-specific risks in as commensurable terms as possible.

Close co-operation between the Nordic insurance supervisory authorities in the supervision of the If Group continued in 2003. This included a significant amount of electronic communications involving the exchange of information and documents between the supervisors regarding the institutions supervised by one of them, as well as on joint supervisory projects. Furthermore, the ISA participated in the Nordic supervisors' joint meetings approximately once a month.

Internal Control

The ISA inspected the internal control of five groups of companies involving a total of eight companies. Three inspections included in the supervisory plan were transferred to 2004. The inspections covered each company's 1) management method and control culture, 2) risk identification, assessment, limitation and control, 3) control measures and differentiation of tasks, 4) reporting and communications, and 5) monitoring of operations and correction of defects.

Based on these inspections, the status of internal control in the supervised institutions is estimated to be satisfactory and continuously improving. The ISA will get an overall impression of the matter in 1 to 2 years after it has inspected all major groups/companies.

The fit and proper supervision

In summer 2002, the ISA issued instructions on the assessment of the fit and proper qualifications of insurance companies' management. In 2003, the ISA finished the handling of basic fit and proper reports of Managing Directors and Board members and their deputies, as well as the general agents in charge of foreign companies' representative offices. These reports covered approximately 265 persons. At the end of 2003, this supervisory task was transferred from the Market Affairs department to the Financial Supervision department.

Workers' Compensation Insurance

In 2003, the ISA developed "Workers' Compensation Insurance Analysis", an entirely new report to be submitted to the ISA by the supervised institutions. This report substantially improves the possibilities of the ISA to analyse the profitability of this line of insurance, the adequacy of its technical provisions, as well as certain special features, such as occupational diseases, which are typical of this field. The first, pilot-type reports in this field were collected in 2003, and related results were utilised to fine-tune the report into its final form. The first official reports complying with this procedure will be submitted to the ISA in connection with the financial reporting for 2003.

Motor Third Party Liability Insurance

The ISA performed an investigation into the conformity to law of motor third party liability (motor TPL) insurance premiums charged by insurers. The Finnish Motor Insurance Act requires that the premiums are reasonable and secure the compensation payments from these policies. The investigation was based on the information on motor TPL insurance premiums, operating expenses, claims and technical provisions during the period 1997–2001, collected from the companies at the end of 2002. The investigation indicated that motor TPL insurance premiums were too low in almost all of the companies at the beginning of the said period, after which the companies started to raise their prices in such a manner that pricing was profitable in approximately half of the companies by 2001. The results provided by this investigation were examined in company-specific meetings at-

tended by a representative of the ISA and normally two representatives of the insurer, one of whom was the company's actuary.

2. Market affairs

The ISA's Market Affairs department focuses on the supervision of insurance products, on the procedures and marketing activities of insurance institutions and insurance brokers as well as on legal supervision. Furthermore, the department prepares regulations, instructions and statements and participates in law-drafting. Market Affairs accounts for approximately 11.3 per cent of the ISA's total person years.

With respect to market affairs, the ISA is in continuous co-operation with the Finnish Insurance Ombudsman Bureau, the Finnish Consumer Agency and the Finnish Financial Supervision and, with respect to EEA companies, with foreign supervisory authorities.

Insurance Terms and Conditions

The European Commission's insurance directives provide the basic framework for the supervision of insurance terms and conditions. Accordingly, the ISA examines, through subsequent supervision, whether insurance terms and conditions conform to law by comparing them to the mandatory stipulations of the Insurance Contracts Act aimed at protecting consumers. The ISA has, for example, issued reminders to insurance companies on unclear clauses in their terms and conditions. In 2003, the ISA continued to focus on the supervision of insurance terms and conditions linked to savings products.

Marketing

Following its statement on the marketing of savings products in 2002, the ISA initiated an inspection, directed at all life insurance companies operating in Finland, into how they handle customers' requests for quotations. An analysis of the results indicated that companies' offers on savings products complied for the most part with the aforementioned ISA statement issued in 2002.



Complaints and Enquiries

The ISA received around 60 customer complaints or enquiries concerning insurance companies and five complaints involving insurance brokers. Most of these complaints were handled within the target schedule, i.e. within two months from the day they arrived at the ISA. Approximately 20 per cent of the investigations resulted in some type of a reminder from the ISA to the supervised institution.

The ISA receives telephone calls related to industry operators' procedures and insurance products almost every day. To increase the flexibility of its operations, the ISA added to its website instructions for drawing up a complaint or a request for investigation.

Insurance Brokers

The ISA started a systematic supervision of insurance brokerage firms at the end of 2002 and inspected 14 such companies in 2003. In October 2003, the ISA issued a statement regarding insurance brokerage firms' agents and other partners and, at the end of the year, instructions for drawing up an assignment contract between an insurance broker and a customer. Furthermore, the ISA was actively involved in the implementation of the Directive on insurance intermediaries, and made preparations for a related new register for which it will be responsible in the future.

Motor Third Party Liability Insurance in Russia

Russia introduced statutory motor third party liability insurance in July 2003, after which the ISA made extensive investigations into whether motor TPL insurance policies granted by Russian companies could be sold in Finland through insurance brokers and other parties, such as travel agencies. The ISA's Market Affairs department answered numerous enquiries related to this matter. Furthermore, on its own initiative the ISA informed non-insurance companies, reported to have sold Russian motor TPL insurance, as well as Russian authorities and the Finnish media on the relevant regulations.

Motor Third Party Liability Insurance

Motor third party liability insurance premiums aroused general interest after the Finnish Broad-

casting Corporation YLE had reported that the insurance premiums on motorcycles were unreasonably high in Finland. Consequently, the ISA received four written complaints and one request for an investigation into the pricing of motor TPL insurance granted for motorcycles. A subsequent investigation carried out by the Finnish Motor Insurers' Centre showed that, in fact, these policies were unprofitable for insurers in 2001.

3. Supervision of unemployment benefits enforcement

The Supervision of Unemployment Benefits Enforcement department focuses on financial supervision, supervision of practices related to the granting of unemployment benefits, and supervision of procedures. Furthermore, the department prepares regulations and instructions, provides consultancy and training for those enforcing unemployment benefits, and participates in law-drafting.

The department draws up statistics and reports, and maintains beneficiary and unemployment fund registers.

The Supervision of Unemployment Benefits Enforcement accounted for 18.9 per cent of the total person years of the ISA.

Financial Supervision

Unemployment benefits are funded from the assets of the Government, the Unemployment Insurance Fund and various unemployment funds. The Ministry of Social Affairs and Health confirms their funding shares on the basis of a proposal of the ISA on an annual basis. In 2003, the minimum amount of the unemployment funds' equalisation reserve confirmed by the ISA was 100 per cent and the maximum amount was 400 per cent of the expenses on the fund's own account. The aggregate funds consisting of membership fees, state subsidies and the amount granted by the Unemployment Insurance Fund must cover the unemployment fund's liabilities. In November, the ISA confirmed the unemployment funds' membership fees for 2004.

In its supervision of the unemployment funds' finances, the ISA pays attention to their independent administrative practices. In 2003, the ISA carried out a special investigation into the service agreements between unemployment funds and trade unions. In summer 2003, the ISA issued a statement on the independence of unemployment funds.

Supervision of Practices and Procedures Related to the Granting of Unemployment Benefits

The amended Unemployment Security Act, which contains substantial changes compared to the previous act, came into force at the beginning of 2003, after which the Ministry of Social Affairs and Health confirmed the application directives prepared by the ISA regarding the central amendments. The ISA also provided training on the subject. The amendments increased the number of enquiries made by unemployment funds regarding the implementation of the new Act, particularly at the beginning of the year.

The round of inspections of all unemployment funds initiated by the ISA in 2002 was completed in 2003. The inspections covered the handling of membership issues by the funds; decisions concerning the insurance requirement, minimum employment requirement and certain other preconditions for the granting of benefits; and the inspection of refusal, recovery and fraud cases. The ISA carried out inspections at a total of 22 unemployment funds in 2003.

The ISA started to monitor the unemployment funds' application handling-times more closely and more comprehensively than before. The ISA also compared information in the taxation, pension and beneficiary registers to find out whether applicants had failed to disclose information on income affecting the benefits. The ISA has requested related reports from the funds, after which it will evaluate whether the procedures taken by the funds in cases of fraud are consistent and comply with the ISA's instructions.

The ISA handled 18 complaints submitted by citizens in 2003 and issued 7 statements to the Parliamentary Ombudsman in response to complaints addressed to him regarding unemployment security.

4. Research

The Research unit continued to develop a model for the assessment of risks involved in investment operations. The unit drafted a research article on the section of the model that handles equity investments. The article was presented at the AFIR 2003 meeting of actuarial and financial mathematics, and an extensive report (in Finnish) on the subject was written for the ISA's publication series.

The ISA arranged several research seminars with various co-operative partners and supported Finnish universities providing training in the insurance business.

5. Administration and internal services

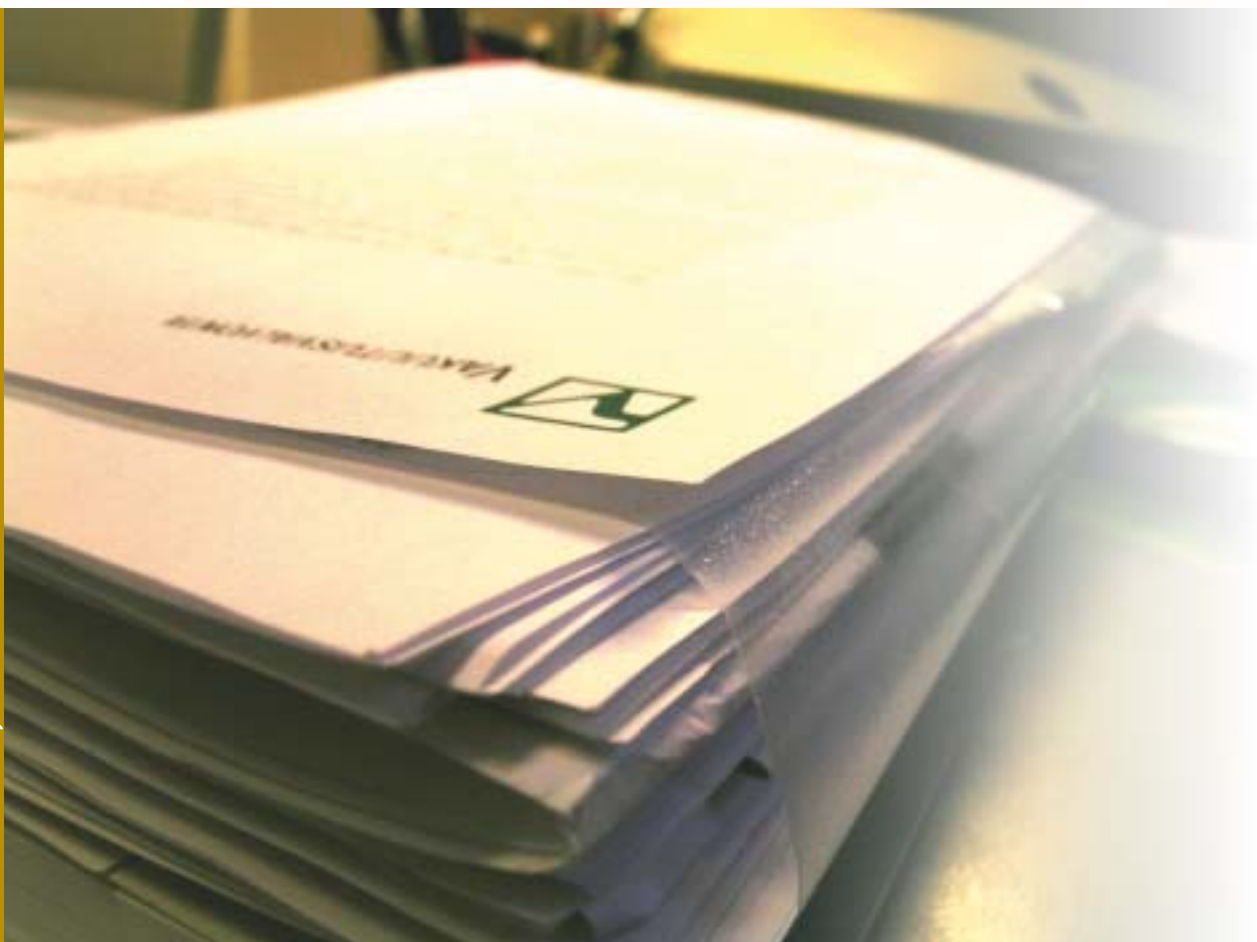
The Administration and Internal Services department provides financial services, personnel administration services, information services, real-estate services and internal services, and reports to and communicates with the government group. The ISA has outsourced most of its administrative support functions. Personnel, financial and data administration accounted for approximately 9.1 per cent and internal services for 10.6 per cent of the ISA's total person years.

The ISA transferred over to the electronic processing and delivery of purchasing documents (invoices) and to the electronic filing of invoices and accounting material.

The ISA began to further define the profitability indicators it will adopt later on by launching a profitability reporting project aimed at generating profitability indicators for the ISA as well as a related follow-up database to support its management.

III

Framework and structures



1. Operational trends

The key success factors enhancing operational processes and structures include the consistency of supervisory activities and the utilisation of information systems as well as a well-functioning co-operation with the Finnish Financial Supervision and foreign insurance and financial supervisors.

To ensure the consistency of its supervisory activities, the ISA continued to prepare the Supervisor's Handbook (supervisory code of practice) in several fields of activity in which it is engaged.

The ISA's follow-up database on pension funds and employee benefit funds was upgraded, and a related reporting system was introduced. A corresponding reporting system for monitoring non-life insurance companies and local mutual insurance associations is in use, and the ISA continued to examine its functionality.

In 2003, the ISA also started to construct verification programmes aimed at assessing the correctness of information as well as error reports, launched a systematic documentation of information systems, and produced a document folder and initiated its maintenance.

The most significant challenges that the insurance supervisors are expected to encounter in the future include international issues, such as the solvency regulations reform within the EU, which is currently being handled by the Solvency II project, as well as the impact of the International Accounting Standards and the amendments to the EU Directive on insurance institutions' annual accounts, on financial supervision. The supervision of financial groups and investment risks will also require additional resources.

2. Reform

From the viewpoint of ongoing reform and well-being, the ISA's most important resource is its personnel's ability and willingness to work. Other success factors include competence management and the ISA's competitiveness as an employer.

In line with its needs for competence management and the ability and willingness to work, the ISA charted its personnel's needs for further education in connection with the annual performance reviews. The ISA arranged training, both in-house and as a bought-in service, and staff members also participated in various externally managed training events and seminars. Furthermore, a staff survey aimed at the assessment of managerial behaviour within the ISA was organised. The results will be utilised to further enhance management development within the ISA.

An incentive payment system and performance reviews covering each ISA employee are important management elements at the ISA. A pay system reform initiated in 2002 is almost completed, lacking no more than a related negotiation outcome. However, the ISA has sided with its personnel on the immediate implementation of procedures that comply with the new system in tandem with the valid civil servant salary system until a negotiation agreement on the new pay system has been reached.

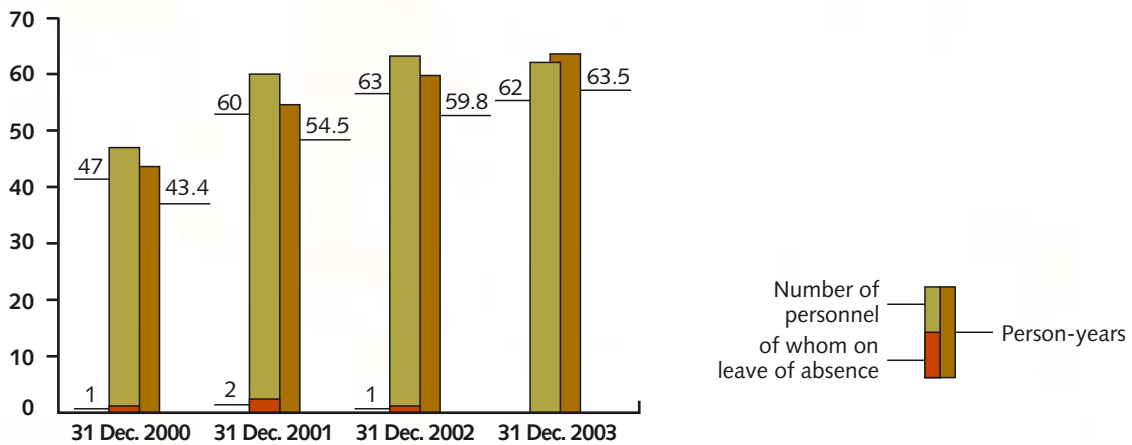
Staff well-being at work has been enhanced through related activities and by organising joint seminars. A group attending to matters related to well-being at work began operations in 2003. The purpose of this group is to ensure and enhance staff motivation, skills and well-being.

The ISA also encouraged staff participation in various forms of physical exercise.

Other key factors enhancing reform management and the profitability of operations include the efficient use of resources and the control of operating expenses. Consequently, the ISA examined its future resource needs and, for this purpose, charted the division of working hours between various tasks.

3. Key figures

Personnel and Person-years



Person-years by Area of Responsibility

Area of Responsibility	2001 Actual	2002 Actual	2003 Actual	Share, %
100 ISA Management and Joint Functions	2.0	2.0	2.0	3.1
101 ISA Expert Facilities	2.0	2.2	2.9	4.6
102 Statistics	2.8	4.0	3.9	6.1
103 Research	0.6	2.0	3.0	4.7
110 Administration	10.0	9.9	5.8	9.1
111 Internal Services (as of 1 March 2003)			6.7	10.6
140 Financial Supervision/Expert Facilities	6.1	6.9	5.3	8.3
141 Pension Insurance Supervision	9.0	8.6	6.7	10.6
142 Life and Non-life Insurance Supervision	5.9	5.7	8.0	12.6
143 Market Affairs	7.0	7.4	7.2	11.3
160 Supervision of Unemployment Benefits Enforcement (as of 1 March 2003)	9.1	11.1	12.0	18.9
Total	54.5	59.8	63.5	100.0

Person-years by Group of Supervised Institutions in 2003

Group of Supervised Institutions	Person years	Share, %
1 Life insurance companies	9.7	17.8
2 Non-life insurance companies	9.3	17.1
3 Employment pension insurance companies	7.2	13.2
4 Company and industry-wide pension funds	7.9	14.5
5 Other employee benefit funds	2.0	3.6
6 Pension institutions founded on the basis of law	0.6	1.0
6.a. Local Government Pensions Institution, State Pension Fund, Church Pension Fund	1.3	2.5
7 The Central Pension Security Institute	0.1	0.2
8 Local mutual insurance associations	1.5	2.7
9 Insurance brokers	2.4	4.4
9.a. Unemployment funds	12.0	22.1
9.b. Unemployment Insurance Fund and Educational Fund	0.3	0.6
10 Other supervised institutions	0.2	0.4
Groups of supervised institutions in total	54.4	100.0
Administration and internal services	9.1	
Total	63.6	100.0

Insurance Supervisory Authority's Income (EUR '000)

	2001	2002	2003
Supervision fees	3,562	4,145	4,317
Performances (Act on Criteria for Charges Payable to the State)	249	175	214
Other income	1	0	0
Income in total	3,812	4,320	4,531

Income by Group of Supervised Institutions in 2003 (EUR '000)

Group of Supervised Institutions	Supervision fees *)		Performances (Act on Criteria for Charges Payable to the State **)	
		%		%
Life insurance companies	851	19.7	10	5.1
Non-life insurance companies	856	19.8	23	11.4
Employment pension insurance companies	857	19.8	10	4.8
Company and industry-wide pension funds	523	12.1	81	39.4
Other employee benefit funds	86	2.0	24	11.6
Pension institutions founded on the basis of law	54	1.3	3	1.3
Local Government Pensions Institution, State Pension Fund, Church Pension Fund	83	1.9		0.0
The Central Pension Security Institute	13	0.3	1	0.4
Local mutual insurance associations	75	1.7	18	8.9
Insurance brokers	150	3.5	13	6.4
Unemployment funds	735	17.0	20	9.7
Unemployment Insurance Fund and Educational Fund	20	0.5	0	0.1
Other supervised institutions	14	0.3	2	1.1
Total	4,317	100.0	206	100.0

*) The reported invoicing surplus has been taken into account as deduction

***) Retained earnings as deduction of joint expenses

IV

Other financial information



Income and Expenses Account

	1 Jan. 2003 – 31 Dec. 2003		1 Jan. 2002 – 31 Dec. 2002	
OPERATING INCOME				
Income from fee-charging operations	4,530,654.57		4,319,807.17	
Other income from operations	251.95	4,530,906.52	17.61	4,319,824.78
OPERATING EXPENSES				
Materials, supplies and goods				
Purchases during the accounting period	-60,273.77		-80,629.23	
Personnel costs	-3,360,993.70		-3,001,421.52	
Rents	-521,687.79		-578,654.73	
Purchased services	-485,513.46		-442,777.07	
Other expenses	-107,287.33		-164,206.75	
Depreciation	-106,722.43		-133,447.69	
Internal expenses	-19,878.06	-4,662,356.54	-16,993.95	-4,418,130.94
SURPLUS/DEFICIT I		-131,450.02		-98,306.16
FINANCIAL INCOME AND EXPENSES				
Financial income	242.60		106.12	
Financial expenses		242.60		106.12
EXTRAORDINARY INCOME AND EXPENSES				
Extraordinary income		0.00	0.00	0.00
SURPLUS/DEFICIT II		-131,207.42		-98,200.04
SURPLUS/DEFICIT III		-131,207.42		-98,200.04
INCOME FROM TAXES AND OBLIGATORY FEES				
Value added taxes levied	296.02		542.63	
Value added taxes paid	-232,575.69	-232,279.67	-263,634.25	-263,091.62
DEFICIT FROM THE ACCOUNTING PERIOD		<u>-363,487.09</u>		<u>-361,291.66</u>

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