On the radar

EXTERNAL INFLUENCES SUCH AS SEPA AND SOLVENCY II OFFER INSURANCE COMPANIES A PERFECT STIMULUS FOR STREAMLINING THEIR OPERATIONS, SAYS **CLAUS PAHLKE**.

Regardless of one's position in the business cycle, improving inefficient cash management arrangements will always have the potential to deliver significant benefits in terms of overall business profitability. Yet lessons learnt from recent events – combined with some ongoing uncertainty regarding market conditions – have led to this becoming a more pressing issue across all industry sectors as the imperative to make the best use of cash resources has grown. Of course, the insurance industry has been no exception to this and has been facing challenges similar to those that have affected all businesses. However, this sector is also unique in many ways.

Insurance is usually a cash-upfront business where cashflow shortages of the type experienced by businesses selling on 60 or 90-day terms are not an issue. However, it is possible that this has contributed to a degree of cash management inertia in this sector, where efficient underwriting and prudent investment strategies are normally the key factors determining an institution's success. As a consequence, some insurers may find that there are significant – and sometimes relatively easily attainable – benefits available through reassessing their end-to-end cash management structures and culture.

Indeed, it is precisely because of this possible abundance of cash that the benefits of overhauling cash management processes can be so great. And while some strategic changes may take time to implement, there are certainly some quick wins available to treasurers who wish to look closely at all aspects of how their organisations monitor and manage cashflows and balances.

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UNIQUE CHALLENGES FOR THE INSURANCE SECTOR The key cash management challenges faced by international insurers can be grouped into several broad areas: transparency issues; regulatory challenges; costs and risks associated with the use of disparate systems and procedures across subsidiaries; and changing data and format requirements due to harmonisation initiatives such as the Single Euro Payments Area (SEPA).

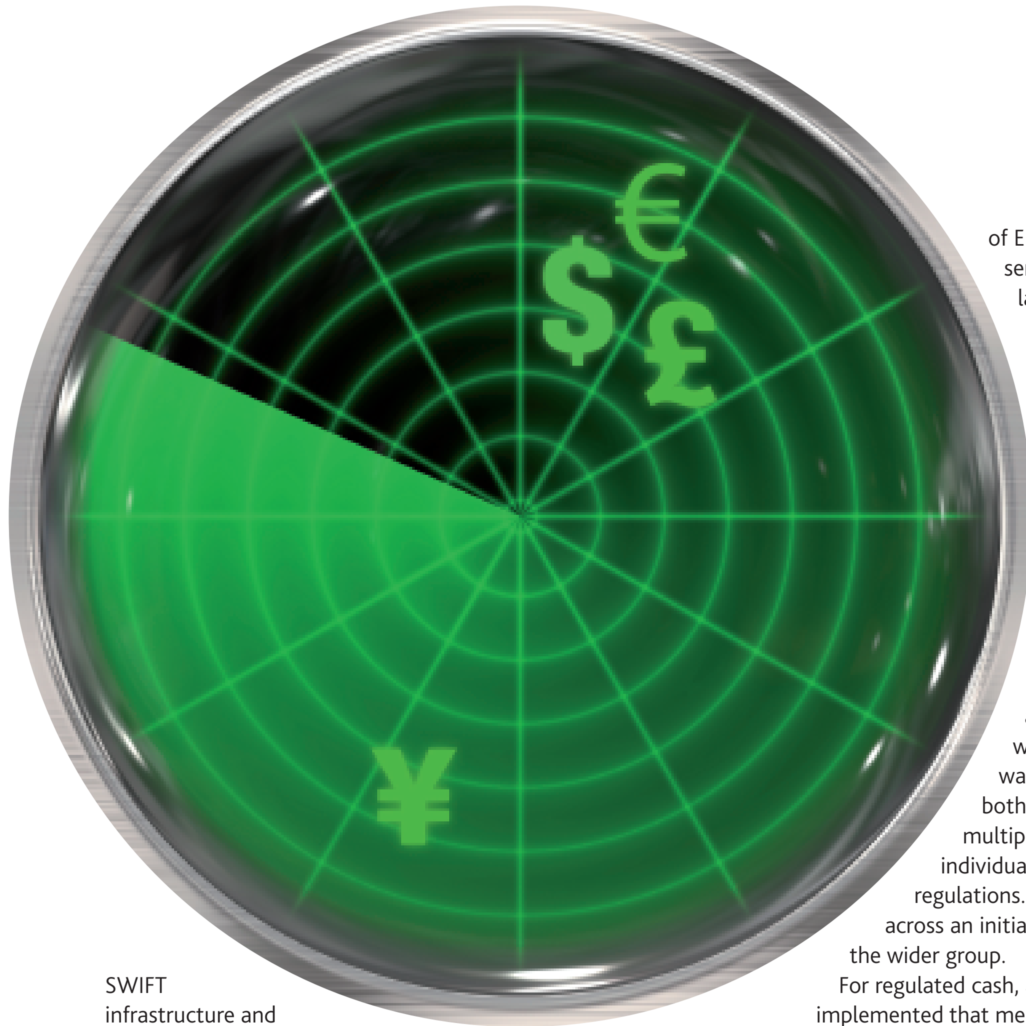
Addressing the first of these issues – transparency over funds and flows – forms the basis of resolving other cash management issues. Indeed, enhancing visibility allows treasurers to make more informed decisions regarding, for example, the timing of payments and the choice of short-term investment options, as well as facilitating more accurate reporting and planning. Fortunately, the real-time monitoring of flows and positions across and within subsidiaries is now a relatively straightforward exercise thanks to the development of web-based global banking platforms by the leading providers.

Resolving issues of transparency and visibility allows for the introduction of enhanced liquidity management structures that can deliver tangible benefits in terms of improved investment returns, as well as helping to address the challenges presented by regulatory changes such as the Solvency II capital adequacy rules for insurers.

Solvency II represents a continuation of efforts to establish a single European market for insurance service in the EU and has the explicit aim of introducing pan-European standards for capital reserve requirements, risk management and transparency. As the previous EU rules were considered inadequate by many member states, some had established their own standards, leading to a patchwork of regulatory requirements that impeded the functioning of a single market in this sector.

For many insurers, especially larger businesses with subsidiaries in a number of European jurisdictions, Solvency II is driving the take-up of regional and global pooling solutions that can facilitate a centralised management of cash at the group level and therefore help to maximise short-term investment income and optimise capitalisation of regulated subsidiaries locally. And such structures require both free and regulated assets to be flexibly managed, in compliance with all relevant regulation. Under Solvency II, regulated assets refer to those reserves that insurers have to hold to ensure they remain solvent under prospective stress environments. These reserves are ultimately held to protect policyholders.

The challenges presented by the existence of a diverse range of local systems and procedures, as well as the data and formatting requirements of harmonisation initiatives such as SEPA, can also be successfully addressed thanks to a combination of cross-industry and proprietary initiatives. Greater SWIFT connectivity for insurers, for instance, can assist in reducing the administration costs associated with dealing with numerous payment and information channels.



SWIFT infrastructure and expertise can be found in insurance groups, historically in their investment management units, and are increasingly being used for the cash management processes as well. The leading transaction banks should also be able to help clients with migrating to the new SEPA XML standards. Globally active groups will want to implement solutions which deliver the same on a global scale. Deutsche Bank sees its role also in promoting the interests of its insurance clients at cross-industry bodies such as the European Payments Council (EPC) or SWIFT working groups.

Significant benefits can also be realised through addressing specific issues which require the detailed analysis of operational procedures such as the management of cross-currency transactions. Lower-value payments of this type often slip below the radar as they are not considered large enough to warrant individual attention. However, the aggregate value of all such transactions within one organisation may amount to many millions of euros, with a small increase in efficiency therefore yielding significant savings. Indeed, while insurance is certainly a sector that executes large volumes of such payments, awareness of optimisation potential with such payments is growing across all industry segments, thanks to the development of platforms to address this specific issue.

The field of card acquiring is just another example where a sound understanding of payer behaviour and use of technical solutions can often generate great savings through redesign of processes that are currently often still manual – for example, chargebacks.

A SUCCESSFUL BUSINESS CASE Looking at an individual example can give us a clearer idea of what can be achieved by insurance providers that wish to overhaul their cash management arrangements. Deutsche Bank recently put in place a solution for one of Europe's most significant insurance and financial services groups. Companies across the group hold large amounts of operational cash that is dispersed across various balance sheets. The insurance regulation, the size of the liquidity positions and a historically diverse set of banking relationships globally meant that traditional liquidity management techniques could not adequately meet the treasurer's integration standards and automation requirements to achieve the desired scalability. Inter-company positions and cross-guarantees/pledges are generally not allowed for regulated cash held for policyholders.

The sole central clearing of all local accounts – as is often favoured by corporates – was therefore not sufficient. Instead, a solution was sought that allowed the centralisation of both free and regulated cash positions held at multiple banks, while at the same time providing individual entities with the flexibility to meet local regulations. A solution was successfully implemented across an initial four countries and is now being rolled out to the wider group.

For regulated cash, a bank deposit-based structure was implemented that meets the regulatory needs of the depositing subsidiaries, allows flexible management of the overall position at treasury level and is accounted for as an inter-company transaction, as would be the case with traditional cash concentration solutions. This is accompanied by daily physical sweeping of non-regulated cash. Pooling cycles are integrated with accounting, treasury and forecasting systems thanks also to direct SWIFT access. Automation and high levels of straight-through processing (STP) are achieved as a result of a centralised structure that updates the general ledgers of individual entities within the group.

TIME TO ADDRESS THE ISSUE Treasuries in the insurance industry should not view regulation and initiatives such as Solvency II and SEPA as a hindrance, but rather an opportunity to realise efficiencies and take full advantage of necessary group-wide investments in systems and processes – planned or already carried out. And while effective cash management should be a priority for all organisations at all times, the current environment for insurers makes this a particularly pertinent issue at present. Indeed, addressing these issues now could provide a timely windfall for many companies in the sector, and acts as a sound basis for future performance and growth.

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