

Office of the Commissioner
Received 04/05/2007



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May 4, 2007

Mr. Thomas Abe
Commissioner & CEO
Independent Consumer & Competition Commission
P.O. Box 6394
Boroko, NCD

Dear Sir,

Submission on the Issues Paper on the Review of the General Insurance Industry in Papua New Guinea

As a locally licensed general insurer and member of the PNG Insurance Council we are pleased to present our submission in response to the Issues Paper recently released by the Independent Consumer & Competition Commission (ICCC). Our submission is tendered on the understanding that the Issues Paper is the first step in a detailed and positive review of the industry and that all stakeholders will be provided with the opportunity to participate in, and contribute to, any future dialogue and recommendations which may result from the review.

This paper will respond to those points we consider we are able to and for clarity and ease of reference has adopted similar sub-headings used in the issues paper.

The effectiveness of the Legal and Regulatory Framework

It is our opinion that the Insurance Act 1995 does provide an adequate legal framework for the efficient operation of the industry, however, it may be in need of a review and update to properly reflect current market dynamics. Perhaps the major weakness of the legislation is its' generously broad scope, which has allowed ambiguity, misinterpretation and inconsistency to manifest over the years.

AIG Papua New Guinea subscribes to the principles of good governance and proper adherence to prudential requirements, and supports any endeavors of the Office of Insurance Commissioner (OIC) to ensure all industry participants are totally compliant. The recent demise of an industry participant suggests that prudential scrutiny needs to be closely and regularly administered. That notwithstanding, such scrutiny should be focused and purposeful and not result in overly onerous and unnecessary requirements being placed on industry.

We consider that the current 'admitted market' scenario is the most appropriate for Papua New Guinea, given the size of the local market relative to the global insurance



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community. The PNG market does not possess the scale of larger overseas markets and any moves to 'liberalize' the market and remove safeguards for locally licensed entities could result in the demise of indigenous players and the flight of those with overseas shareholding.

Licensing has been an area of concern for the industry and discussions are currently underway with the regulator to review the process. It is our view that new entrants to the market should be thoroughly scrutinized and licenses only granted after an exhaustive process. A provisional period of close scrutiny should then follow to ensure bona fides are well maintained. Licensing for 'established' entities on the other hand, should be simple and straightforward and consideration should be given to multi year licenses for these proven entities. Such a scenario is workable as the rights of license revocation sit with the regulator at all times, and it would render unnecessary the current practice of issuance of provisional licenses.

A simple and straightforward licensing process should also clearly define the types of insurance that are allowed to be written by general carriers and there should be clear demarcation between life and general products. Furthermore, any process should be free of any ambiguity and applied fairly and uniformly to all industry participants.

The issue of adequate capital requirements is a complicated one and is, we understand, being addressed through a separate study on risk based capital assessment that has been commissioned by the OIC. AIG is supportive of any initiatives to safeguard policy holders through the imposition of adequate prudential standards, however, because of the modest size of the PNG market, we would urge caution in the conduct of any review of this nature to ensure that any model considered was appropriate to the sustainability of a local market.

The proposed introduction of new legislation such as the Insurance Contracts Act, Complaints Tribunal and Risk Based Capital Assessment has its merits but again, needs to be considered in terms of the size of the market. Positive dialogue on all of these initiatives has either recently commenced or is well underway between the Insurance Council and the regulator. If these initiatives are introduced steps should be taken to ensure that they are relevant and manageable in the context of the PNG market.

Market Operation and Competition

We consider our current arrangements with the PNG reinsurance market to be appropriate and effective. In respect of Section 36 we would dispute the contention, on Pages 16 and 42 of the Issues Paper, that general insurers are not compliant with reinsurance requirements. AIG follows all protocol in terms of facultative reinsurance placements and we would suggest that this is the intention of the Act. Given that the Act was written prior to the formation of Pacific Re, or any local reinsurance entity for that matter, we submit treaty arrangements fall outside the scope of Section 36.

We would contend that there is sufficient competition amongst existing insurance companies to provide an effective and efficient general insurance market. This point is well covered in the separate submission of the PNG Insurance Council and we are in

agreement with the perspective put forward in that paper. It is also worth noting that competition for insurance business is not exclusive to the PNG market, and insurance buyers, and their brokers, are at liberty to seek offshore terms, subject of course to the 17.5% differential prescribed by the Act. Whilst some may argue against the differential we would contend that it is necessary for the same reasons that an 'admitted market' is deemed to be.

There are more than an adequate number of brokers and loss adjusters in the market and competition amongst these entities is quite keen. Those that AIG transacts business with are considered to be adequately skilled and experienced to meet market needs. There may of course be exceptional circumstances which would require the intervention of specialist offshore expertise, however such circumstances are very occasional.

The questions of premium and coverage adequacy are well addressed in the PNG Insurance Council submission. It is suffice to say that we support the premises put forward in that paper that pricing and coverage models are appropriate to market dictates.

Current prudential requirements are considered to be modest enough to attract new players to the market, and this is reflected by the entrance of two new indigenous players in the last twelve months. What is of interest however is the fact that, apart from the joint venture commitment by Allianz to Pacific MMI, there has been no foreign capital injection into the insurance provider market for some time. This is coupled with the fact that the market has seen the withdrawal of a number of foreign players in the last decade, either through acquisition or by attrition. A number of conclusions could be drawn from this fact however we would suggest that every measure should be taken to ensure that there is no further flight from the market.

The Insurance Commissioner's levy has been in place for the best part of a decade and properly utilized is a worthwhile underwriter for the regulatory regime. What should be said however, is that the levy is an impost on the insurance buyer, and there needs to be regular reporting and accountability to that stakeholder.

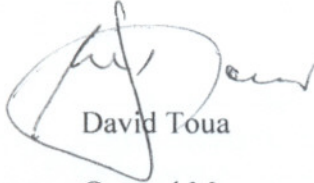
We are unsure why Lloyds of London has a unique position in the PNG insurance market, in that it is not required to undergo the same regulatory requirement as other Insurers. To the best of our knowledge, no known statistics exist as to the size and composition of the Lloyds market share. Whilst it may be an historic arrangement we feel that it is outdated and that Lloyds should be brought into line with other Insurance companies.

AIG does not feel it appropriate to provide commentary on brokerage and fees apart from confirming that our arrangements with the local broking community are similar to our arrangements in other jurisdictions.

In conclusion, we wish to state that AIG Papua New Guinea subscribes to the rigorous requirements of our New York based parent company. As a company with assets in excess of US\$900 billion and with representation in over 130 countries and jurisdictions throughout the globe, we are committed to providing superior security to our clientele. In 2008 the company will celebrate 30 years of trading in Papua New Guinea, a fact that

underpins our commitment to this market and we look forward to reviewing the outcomes of this Issues Paper and would welcome an invitation to participate in any ongoing dialogue that may eventuate.

Yours Faithfully,



David Toua

General Manager
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