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Perbadanan Insurans Deposit Malaysia

Protecting Your Insurance And Deposits In Malaysia

NRS | NATIONAL RESOLUTION SYMPOSIUM 2024

23 - 24 September 2024

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NATIONAL RESOLUTION SYMPOSIUM 2024

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Protecting Your Insurance And Deposits In Malaysia

PANEL SESSION 1:
Merger and acquisition and transfer in resolution

Moderator:

AFIZA ABDULLAH

Executive Vice President,
Perbadanan Insurans Deposit
Malaysia

Panelist:

BRUCE MATTHEWS

Partner, Head of Restructuring &
Performance Improvement, KPMG
Lower Gulf

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Senior Vice President, Islamic
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16 years later ...

Bruce Matthews

Partner, Turnaround & Restructuring

KPMG

The Risk – Confidence – Reaction cycle

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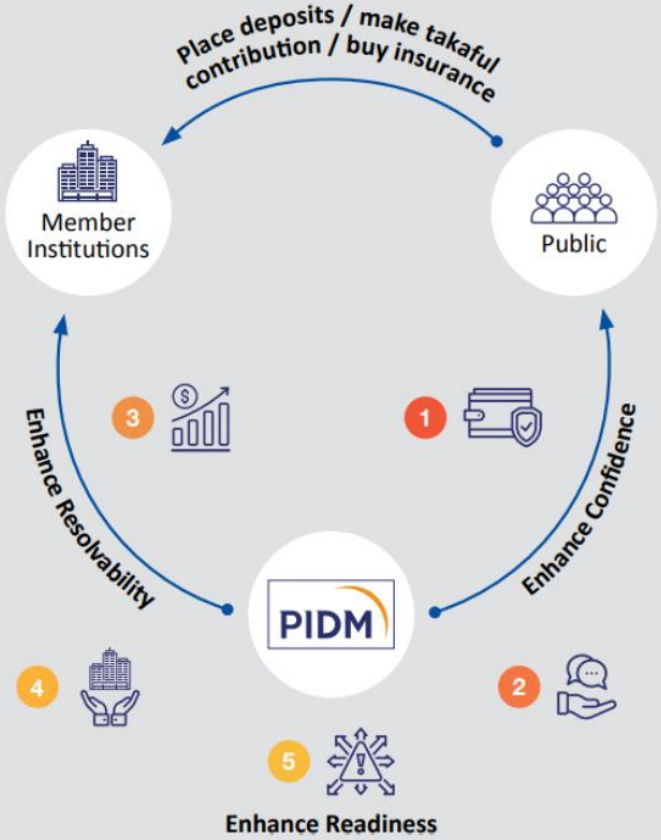
HOW PIDM PROTECTS FINANCIAL CONSUMERS

PIDM is a statutory body established in 2005 under the Malaysia Deposit Insurance Corporation Act (PIDM Act). In fulfilling our mandate as a financial consumer protection authority and resolution authority for our member institutions, PIDM protects financial consumers in Malaysia by:

1. **Protecting deposits and takaful and insurance benefits**
2. **Creating awareness and enhancing trust**
3. **Providing incentives for member institutions to remain safe and sound**
4. **Ensuring member institutions can be resolved effectively**
5. **Enhancing readiness for crisis**



Source: PIDM website

It's just over **16 years** ago that Lehman went into Bankruptcy.

What **lessons** have we learned or not learned ?

How does that **impact** your current thinking and what might need to change for stability and value ?

Linking it into **READINESS, CONFIDENCE & RESOLVABILITY** … with a **different perspective**

What is the magic ingredient ?

We’re going to begin with the end in mind …

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Reminder of Lehman

… its easy to forget

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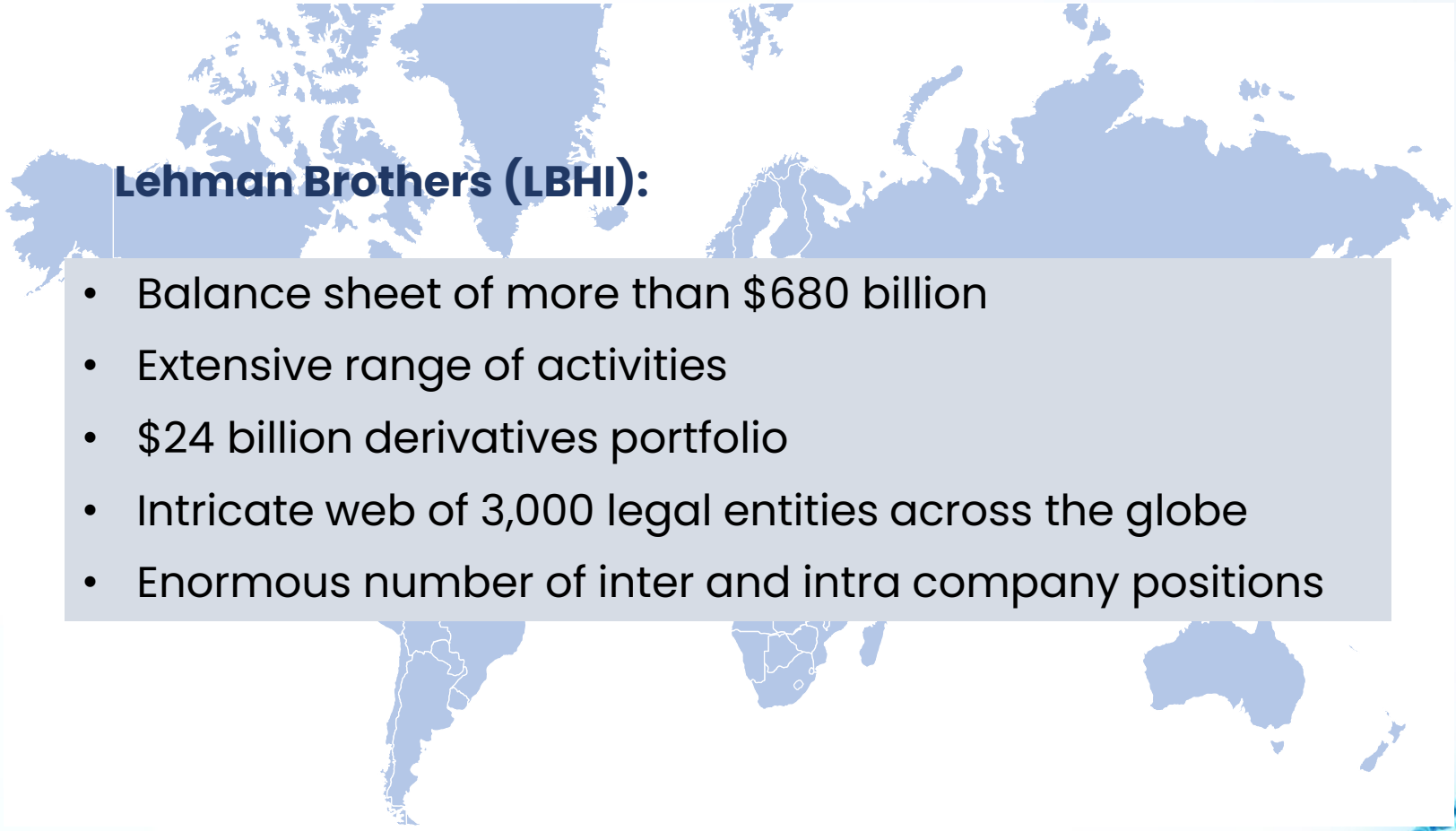
Lehman Brothers:

The largest global bankruptcy **to date**

At bankruptcy, LBHI listed $613 billion in debts and $691 billion in assets



Lehman Brothers (LBHI):

- Balance sheet of more than $680 billion
- Extensive range of activities
- $24 billion derivatives portfolio
- Intricate web of 3,000 legal entities across the globe
- Enormous number of inter and intra company positions

Timeline of Events

Things can unravel quickly …

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August

August 22 *(T-23)*

- Korea Development Bank (KDB) in talks to buy Lehman.

September

September 9 *(T-5)*

- KDB withdraws from negotiations to buy Lehman.

September 10 *(T-4)*

- Announcement of $3.9b loss.

September 13 *(T-1)*

- Barclays withdraws from negotiations to buy Lehman
- Federal reserve call emergency meeting to discuss 'liquidating' Lehman assets.

September 14 *(T)*

- File for Chapter 11
- 10:30pm Advisors hired by LBHI board

September 19 *(T+5)*

- Bankruptcy court appoint CRO
- Sale of LBI USA to Barclays Capital

September 22 *(T+8)*

- Sale of Asia Trading and Investment Banking to Nomura

October

October 6 *(T+22)*

- Sale of Indian processing centre to Nomura.

October 13 *(T+29)*

- Sale of Europe and ME investment banking equities unit to Nomura.

Key lessons learnt

At a high level, these lessons haven't changed …

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People

Have a clear picture of all staff
Identify key people & decision makers

Assets and data

Know your assets
Understand and simplify your IT

Entities

Keep internal ownership clear & control simple

The Lessons learnt in a time of crisis for Lehman have very practical applications in the day to day life of any financial institution

This is good business practice
– not rocket science

Cash is King

Look after the cash
Non trading bank accounts

Human Behaviour

Face up to the situation

Don't Panic

Clear, effective leadership and communication

Be practical

Be prepared to turn to non standard practices

Destruction of Value

Why M&A as a transfer tool is important …

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An orderly sale of assets in a depressed market **could have returned to the estate significantly higher value than** what was ultimately recovered at a much lower cost

Fire sale of businesses

Fire sale of LBHI's trading and investment banking businesses

- Businesses that generated USD4bn of annual profits, were sold for less than USD500m
- Experts believe that it could have gotten more than $24 billion (once separated from its real-estate portfolio)

Derivative trade defaults

Default of 1.1 million derivative trades

- Derivative trades worth a "notional" value of USD23.8bn
- Over 90% of transactions by counterparties resulted in being terminated, with over 0.9 million transactions terminated, including those with parties owing money to LBHI

How is it different now ?

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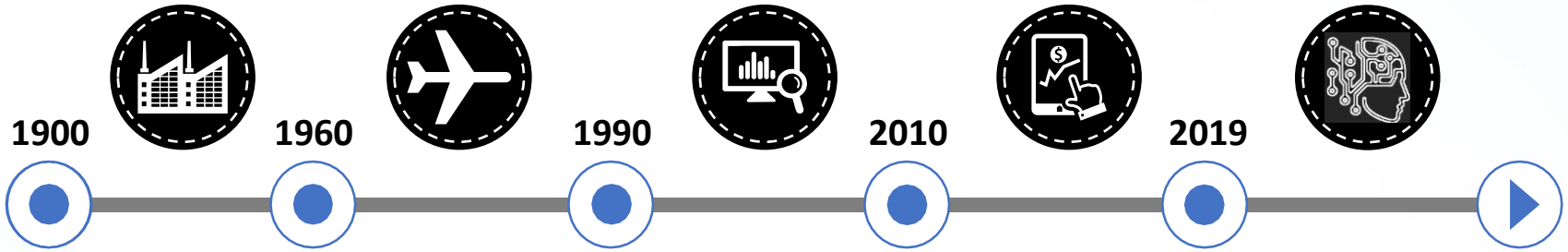
Passage of Time

Current Ecosystems

Events

Passage of time

… just think for a minute how much the world has changed in the last 25 years



Age of manufacturing

Mass manufacturing makes industrial powerhouses successful

Age of distribution

Global connections and transportation systems make distribution and supply chain key

Age of information

Connected PCs and supply chains mean those that control information flow dominate

Age of the client

Empowered buyers demand new levels of engagement and personalization

Age of AI

Advent of LLM and variety of AI powered applications

Beyond imagination

Quantum computing

Alternative energies

Key takeaways

- Technological evolution has both simplified and complicated business processes
- From the age of manufacturing to AI, **businesses must adapt to technological**
- Evolving technologies like **AI and smart tools** need to be adopted

Source: Forrester Research Inc.

Financial services ecosystem

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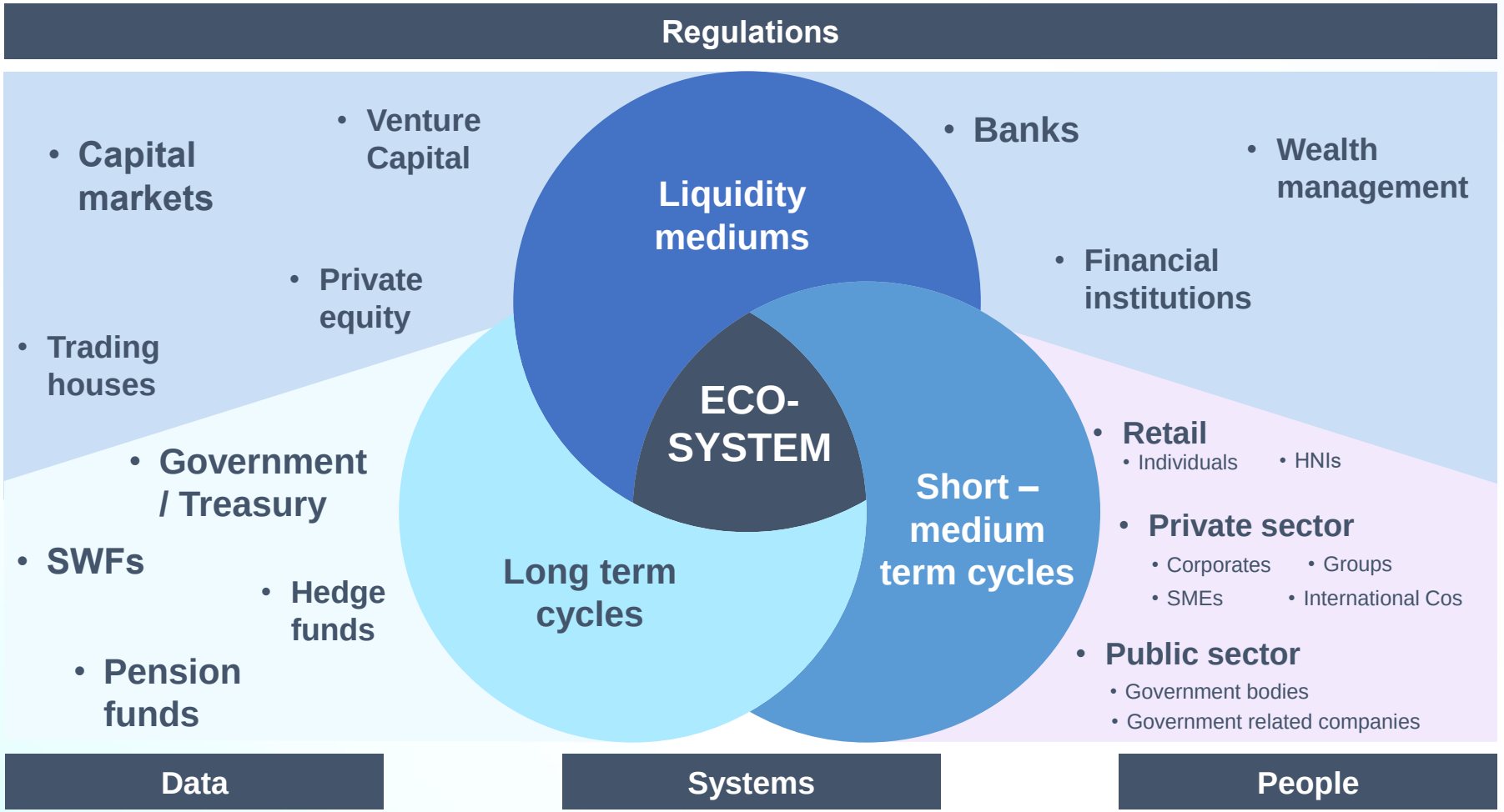

Complexity

- Complex and interlinked ecosystem
- All parts needed to work in harmony

Maturity

- Different stages of maturity require different measures / focus

Pillars

- Four core pillars - regulation, data, systems and people
- Strength of the pillars, fundamental to growth

2024 … a few of the current events

In addition to the operating elements, external geopolitical factors also add to the complexities of managing businesses

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- **Central bank policies resulting in interest rate hikes** to combat inflation, resulting in high debt burden and reduced economic activity
- **Volatile exchange rates** have impacted trade activity, revenues and costs for businesses
- **High inflation rates** have impacted purchasing power of consumers, increased cost of raw materials, and pressured profit margins
- **Trade tensions and strategic competition between countries** impact global trade, technology supply chain, and international investment.
- **Prevalent political instability and regional conflicts and wars** resulting in disruption of global oil & energy supplies and supply chain / trade, leading to impact on global markets.
- **Over half of the world's population will have voted during 2024**, this could have significant foreign policy implications, impacting monetary policies and commodity prices.
- **Escalation of climate change** has resulted in heightened frequency and cost of natural disasters, impacting agricultural yields and supply chain, resulting in higher costs and reduced revenues for businesses.
- **Rapidly evolving technological and digital environment** is impacting customer demands, the traditional approach to business and requiring organisations to continuously evolve to stay relevant.

The things we don't see

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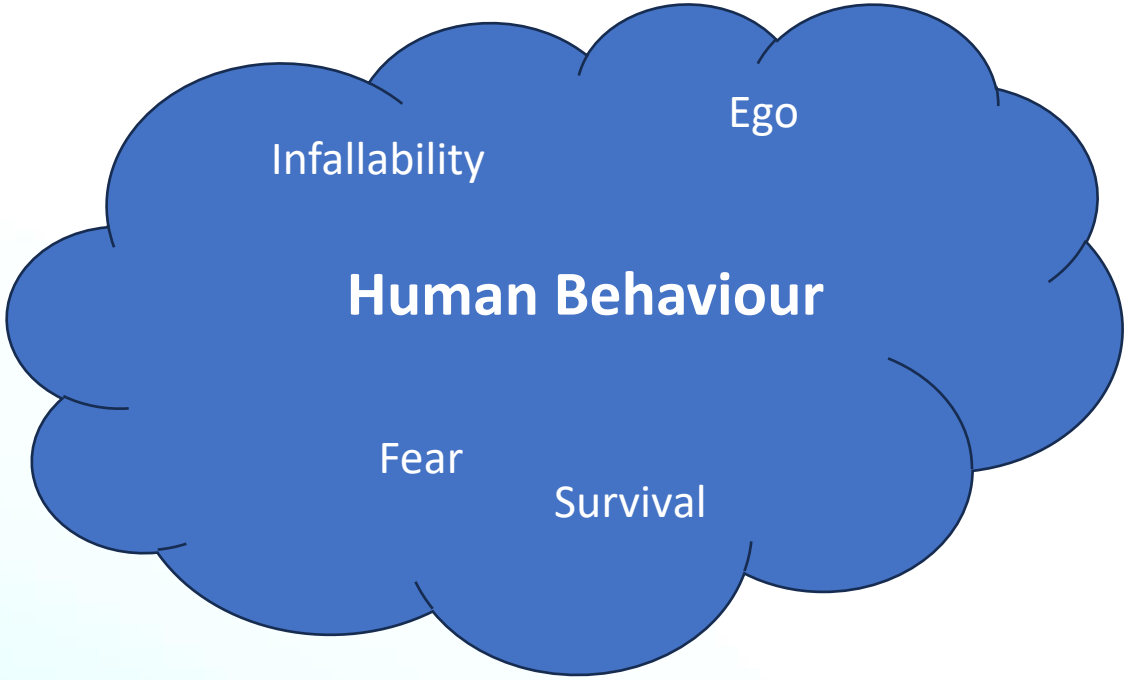

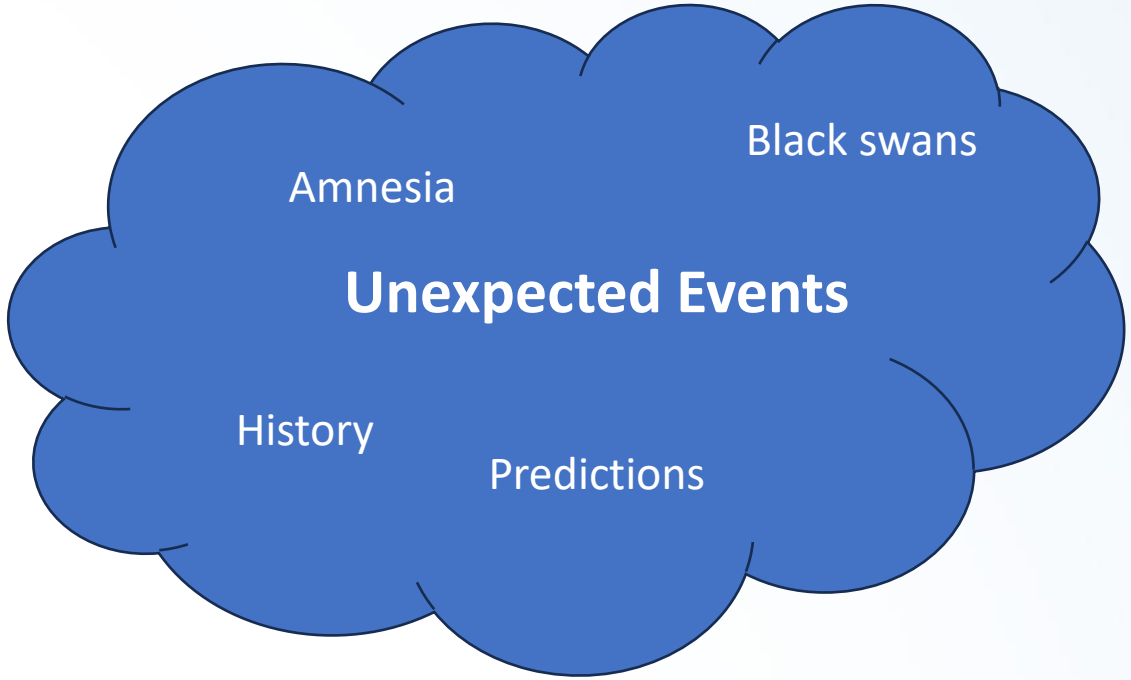

To Build Collaborative Resolvability we need to look for the things that we don't usually see. Awareness and curiosity, being practical and using all the tools at our disposal. Joining the dots but without inducing panic.

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**Video recording*

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Sale in Resolution post Credit Suisse

Michael Piller

Senior Legal & Policy Manager – Recovery & Resolution

FINMA

A look back to March 19, 2023

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The available options were

- SPoE Bail-in of Credit Suisse Group including a restructuring of its business model and a change in leadership
- Aquisition of Credit Suisse Group by UBS supported by a second loss guarantee of the Swiss Federation

What are the lessons to be learnt? From the FINMA perspective

- How can sale/transfer tools support resolution? How can they help to reduce the economic impact of official interventions?
- What needs to be done in the planning phase?
- What needs to be done to the legal framework?
- How to deal with UBS going forward

The Swiss approach to Sale in Resolution

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The Swiss bank insolvency act…

- Allows for FINMA to sell a bank or its assets and liabilities to a third party. Why was it not used in the CS Crisis?
- Is mainly aimed at small to mid sized banks
- Is under review to adress the lessons learned from the CS crisis

FINMA works towards…

- Making resolution actions more foreseeable,
- Improving uncertainty factors (e.g. creditor consent, Shareholder votes, procedureal aspects, etc.) in the current sale in resolution tool

What does it mean for UBS…

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…and the rest of the Swiss banks population?

What about potential aquirers…?

…especially for G-SIBs?

How will FINMA approach it in the resolution plan, and what are the obstacles?

Do we need to change the framework?

Is sale in resolution going to be an option in resolution planning?

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Consideration for Islamic Transfer of Business : Acquirer's Perspectives

Amir Alfatakh Yusof

Islamic Banking UOB Malaysia

23 September 2024

Citi and UOB announced the acquisition of Citi's Retail Banking portfolio on 14 January 2022, as part of a broader sale agreement covering consumer banking across Malaysia, Thailand, Vietnam and Indonesia and excluding the bank's institutional businesses.

October 2022

- Signing of Asset Liabilities Transfer Agreement (ALTA)
- Vesting Order Obtained from Court
- Signing of Transfer Agreement
- Signing of Sale of Debt Agreement

UOB | citi

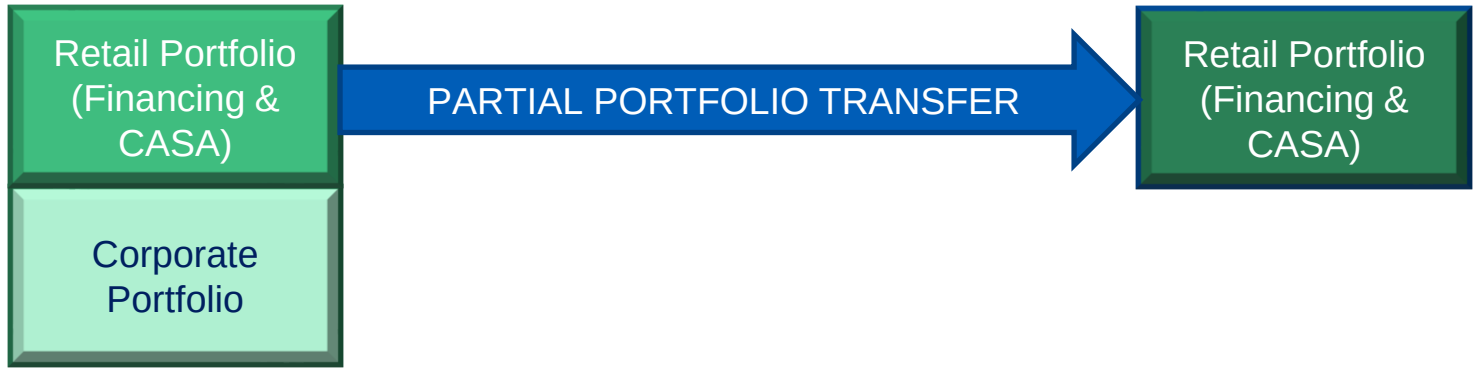
Legal Day One : November 2022

Start of Migration & Conversion Actions : December 2022
Completion of Migration & Conversion : June 2023

- Citi Home Financing (BBA)
- Citi Home Financing (Musharakah Mutanaqisah)
- Citi Current Account / Savings Account (Qard)

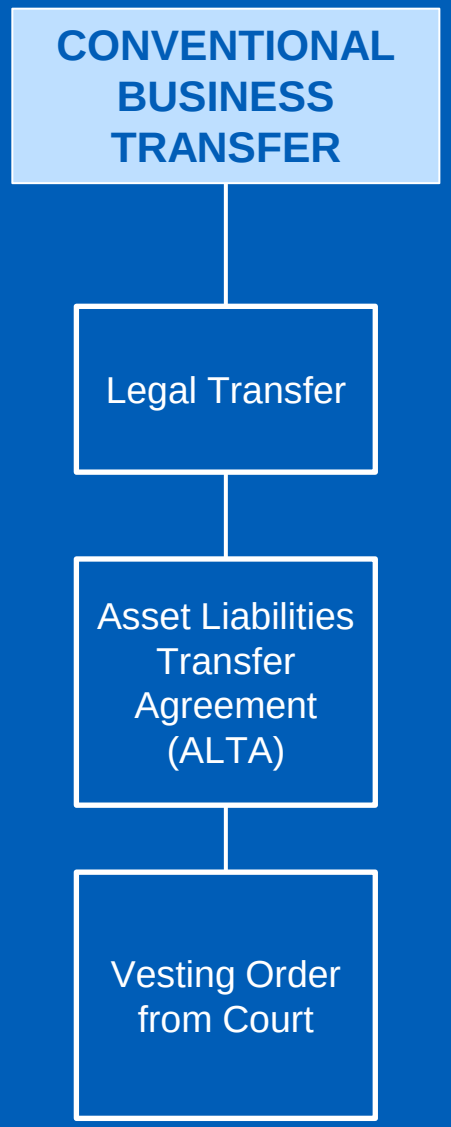
Operational Day One and System Cut Off : July 2023

Outlook : Partial Transfer of Citibank Islamic Retail Portfolio to UOB Malaysia



Transfer Timeline

Shariah Requirements for Business Transfer



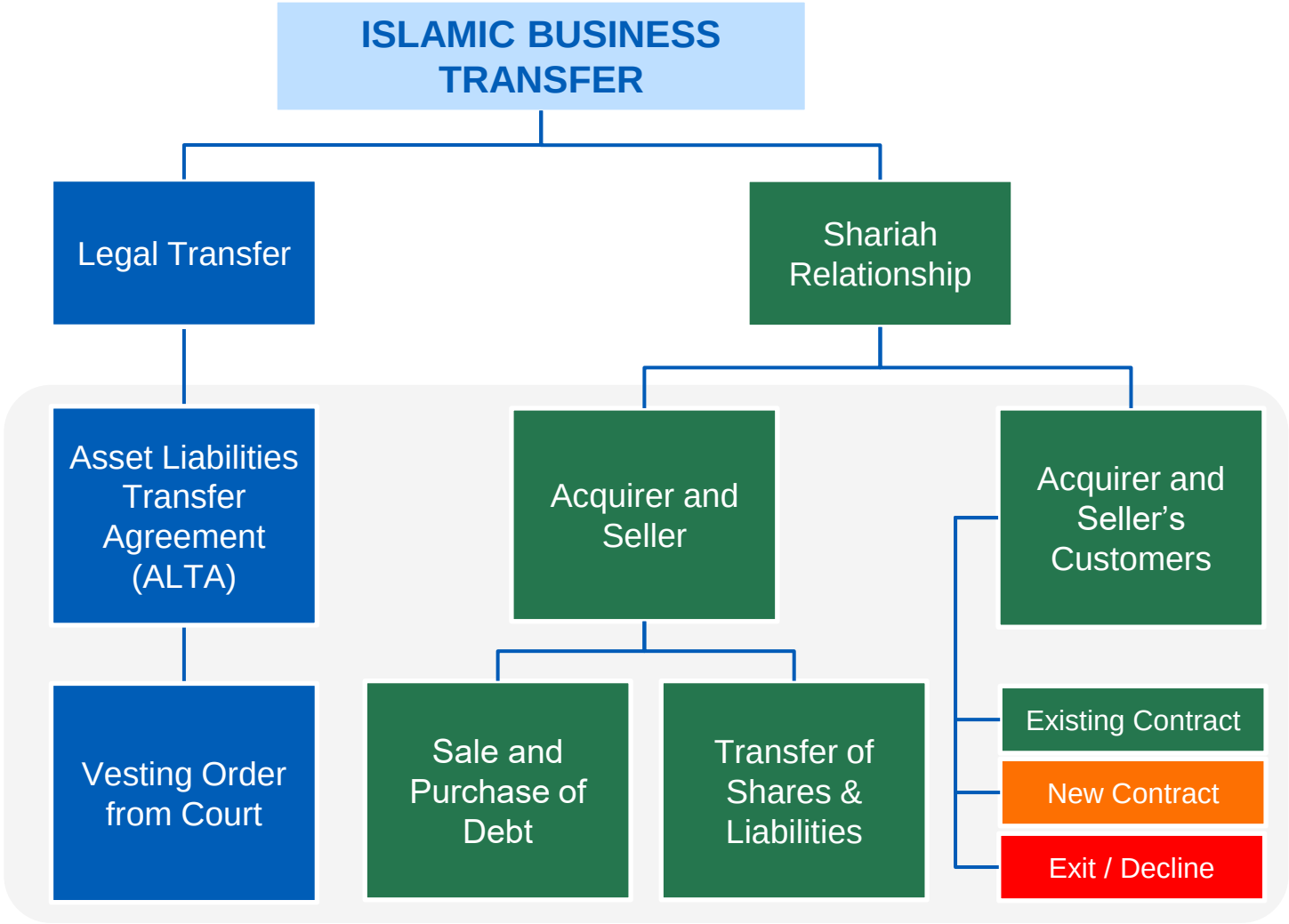
Differences In Transfer Methodology

In the Conventional Business Transfer, the key transfer mechanism is the Vesting Order issued to validate the scope outlined under the Asset Liabilities Transfer Agreement, giving the Acquirer full right, ranking pari-passu as the Seller of the Portfolio.

All legal documents have the same rights transferred to the Acquirer.

Differences In Transfer Methodology

However for Islamic Transfer of Business, the Shariah relationship must be established and formalised to ensure continued contractual obligations agreed by all parties



Key Considerations for Valid Islamic Transfer of Business

Key Considerations to Address an Islamic Transfer of Business

- Business
- Legal
- Shariah
- Customer

UOB

OPERATIONAL DAY ONE : 17 JULY 2023

The Acquisition Price to be Agreed

The Equivalency of like-to-like Portfolio

Unresolved Shariah Non-Compliant Issues

Sufficiency of ALTA & Vesting Order for Shariah Transaction Requirements

Legal

Shariah

Customer

Business

- ✓ What is the Selling Price to be agreed upon, including the date of settlement?
- ✓ Does the Acquirer have the same equivalent product and able to effectively migrate or convert?
- ✓ **Any unresolved Shariah issues?**
- ✓ Does the scope of the Vesting Order and ALTA contains Islamic elements?

In general, ALTA do not contain any specific instructions for Islamic facilities or Shariah requirements

Asset Liabilities Transfer Agreement (ALTA)

Vesting Order issued by Court

Business

Shariah

Customer

Legal

- ✓ **Asset Liability Transfer Agreement (ALTA) as the Main Legal Agreement**
- ✓ Vesting Order provides new Ownership rights to portfolio
- ✓ Notice of Acquisition Provided to Customers
- ✓ Existing Contractual Documents remains intact

Identification of necessary transactions, contracts and documents to be executed:

- ▶*Acquirer to Seller*
- ▶*Acquirer to Customer*

Robust deliberation by Shariah Committee to ensure validity of Acquisition, with references to existing market practices

Business

Legal

Customer

Shariah

Between Acquirer and Seller

- ✓ Sale and Purchase of Debt Agreement
- ✓ Transfer of Shares & Liabilities Agreement

Between Acquirer and Seller's Customer

- ✓ Variation of Terms / Change of Terms
- ✓ Explicit Consent / Deemed Consent / Notification / Exit Options
- ✓ Migration or Conversion
- ✓ New or Retained Contractual Agreement

Fairness in Terms & Conditions if there is any material variations

Provide Sufficient Notice and Information

Conversion Benefits or Options to Restructure / Exit

Business

Legal

Shariah

Customer

- ✓ **Permanent Acquisition** - No Turning Back, Short time-limit for the transfer / conversion
- ✓ **Validity of Existing Aqad** - Customers have completed the Aqad and may not want to be involved into a re-Aqad.
- ✓ **Notification of Changes** - Material or adverse terms to be informed with notice period
- ✓ **Option to Decline** - right to reject the changes, right and options to be provided

UOB Approach to Partial Transfer of Citi Portfolio

Financing (Tangible Assets & Debts) - Sale
BBA (Debt) – Sale & Purchase of Debt with Immediate Settlement (Bay Ad-Dayn)

Financing (Shares Receivables) - Transfer
MM (Shares) – Transfer of Rights with Immediate Settlement (Hawalah)

Deposits (Liabilities) - Transfer
Qard (Debt) - Transfer of Debt with Immediate Settlement (Hawalah)

Note : UOB did not adopt AAOIFI approach for the sale of debt (calculation of tangible assets vs intangible assets)

Summary:

While Vesting Order is deemed to be sufficient to transfer the rights to the Bank, clear Shariah consideration must be made to ensure the contract (and its roles) clearly captures the validity of the transfer. This is captured via specific agreements to address the relationships between UOB and Citi.

Right By You

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Merger and Acquisition and Transfer in Resolution

John Spence

Managing Director,

Asian Capital Advisors

23 September 2024

Discussion Topic

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1

M&A Process: Insurers v Banks: key differences & similarities in the M&A involving an insurance company vis-a-vis a bank;

2

M&A Process: Healthy Insurers v. Distressed Insurers: different risks, considerations and challenges for M&A transaction involving a healthy financial institution during business-as-usual vis-a-vis M&A transaction involving a distressed financial institution, and the role of financial institution in supporting the transaction; and

3

Role of Regulators and Resolution Authorities: particularly for a distressed financial institution deal, how can the regulators or resolution authorities address these risks in facilitating a transfer during the run up to or upon the failure of a financial institution.

The challenge of insuring uncertainty

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The distressed M&A process is inherently flawed.

Insurers, policymakers and regulators are to work together to strengthen the industry for the benefit of policyholders

- Atrophying business.
- Stringent deadlines,
- Insufficient buyer information
- Unpredictable customer behaviour,
- Deteriorating business conditions,
- Exodus of employees and policyholders,
- Competitor response and frequently diminished contractual safeguards.

The challenge of insuring uncertainty

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Five key steps in dealing with a distressed insurer:

1. Monitor, Predict and Prevent
2. Expeditiously Enforce the Process
3. Protect Policyholders
4. Structure the Deal
5. Enhance Regulatory Certainty

Monitor, Predict and Prevent

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Insurers, Policymakers and Regulators should monitor and predict the impact of declining capital and solvency position and if required take proactive steps to resolve the emerging deficiencies

> **The greatest victory is that which requires no battle.**

- Sun Tzu

Monitor, Predict and Prevent

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Aspirations	Observations
Concentrated and strongly capitalised insurance market	• Conventional Life: 14 insurers Top 10 - 96% GWP • Conventional General: 19 insurers – Top 10 - 80% GWP
Promote a national insurance champion	• Market dominated by foreigner insurers
Domestic investors participation	• Handful of local investors • BNM permitting foreign shareholders exceed FDI cap if they undertook "national service" to acquire a weaker player • Contribute to the B40 Health Protection Fund – one contributor Great Eastern RM 2 billion 2018
Insurers contribute to Malaysian capital markets development	• Malaysia's stock market is lacks liquidity resulting in discounted pricing
Islamic financial products leadership	• Takaful licences – 15 Takaful operators issued to 11 Groups

Monitor, Predict and Prevent

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Stakeholder Issues:

- Shareholders: Inability to access capital to fund the business or unwilling to contribute further capital
- Management: Dishonest/Incompetent management – Insurers without sufficient qualified and experienced staff
- Customer: systematic sales and advisory complaints and compensation
- Investments: Strategic Asset Allocation and Asset Selection Issues, Dealing with Credit Risk
- Regulatory Reporting: Reflect the capital ands solvency position of the Insurer
- Regulator: Intervention

Insurance Product Risk Issues:

Product Design and Operationalization:

- Offering guaranteed crediting rates with negative spreads
- Margin compression from competitive pricing
- Underwriting issues – risk portfolio selection, risk pricing
- Claims management – fraud and claims costs
- Natural catastrophes coverage
- Pandemics coverage
- Inadequate Reinsurance
- Inability to reprice products and/or reshape benefits

Monitor, Predict and Prevent Malaysian Insurance Market

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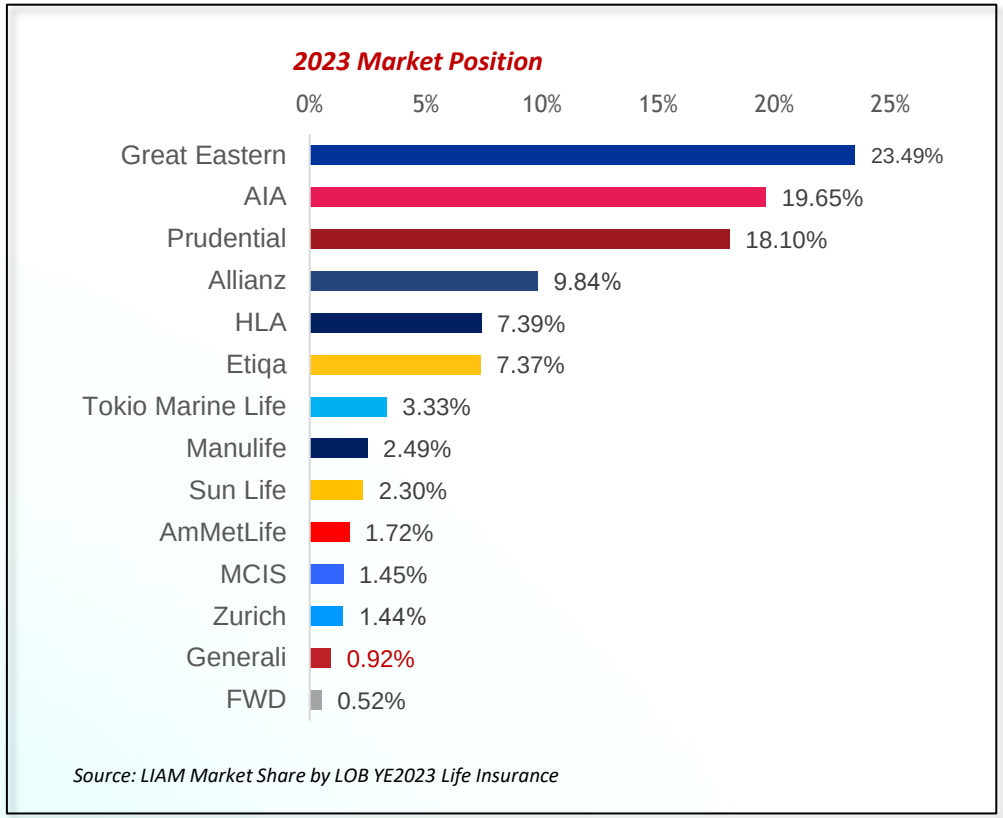
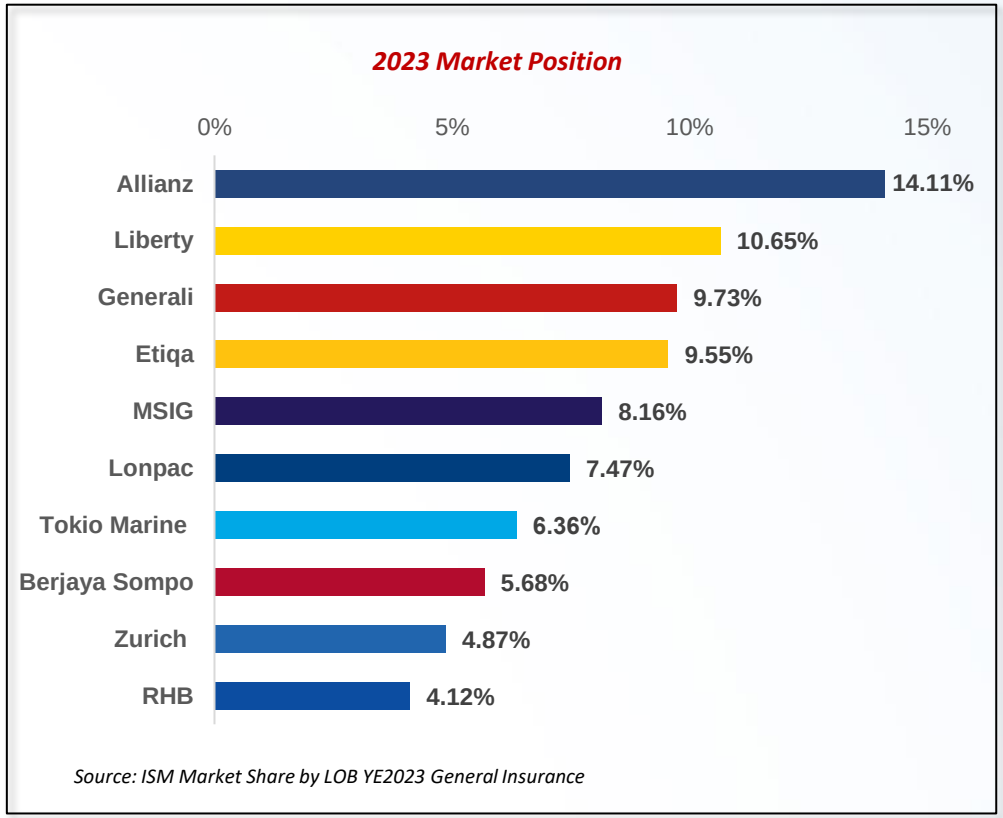
Conventional Life Insurance



Source: LIAM Market Share by LOB YE2023 Life Insurance

Conventional General Insurance



Source: ISM Market Share by LOB YE2023 General Insurance

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Monitor, Predict and Prevent

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Market	Example Insurers
Indonesia	• PT Asuransi Jiwa Adisarana Wanaartha (Wanaartha Life/PT WAL), • PT Asuransi Jiwa Kresna (Kresna Life/PT AJK) • Asuransi Jiwa Bersama Bumiputera 1912. • PT Asuransi Sosial Angkatan Bersenjata Republik Indonesia (Asabri)
Malaysia	• Tahan Insurance Malaysia Berhad (Tahan). Tahan. BNM assumed control in May 2009 due to Tahan's non-compliance with capital requirements and non-fulfillment of the capital restoration plans.
Thailand	• Syn Mun Kong Insurance • Asia Insurance 1950 Public Company, • The One Insurance Public Company • Southeast Asia Insurance.
Hong Kong	• Tahoe Life Insurance

Expeditiously Enforce the Process M&A Process Issues:

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Regulatory Scrutiny

Comprehensive Due Diligence

Valuation Complexity and Challenges:

Cultural Integration

Synergies and Cost Savings:

Time is of the essence: Speed to complete

Expeditiously Enforce the Process

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Insurers, Regulators and Resolution Agencies to deal with non-viable insurer expeditiously
Challenge is to have available fit for purpose data that enables a review and valuation of the distressed insurer

Key data requirement:	Clarity on key deal terms:	Regulatory assistance:
• Financial Statements • Asset Ownership and Valuation Assessment • Actuarial Liability Assessment • Legal Liabilities Assessment • Policyholder details • Staff and Distributor Liabilities	• Protection from post transaction legal action • Available (if any) representation and warranties • Approval criteria and timeline	• Regulatory cooperation in working with incoming shareholder/white knight. • Access to regulatory correspondence • Access to confidential insurer information

Expeditiously Enforce the Process
M&A Process Issues: Distressed Insurers

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Commercial Issues

- **Where's the bottom ?** Determining the extent of the liabilities
- **Can the business survive ?** Access to funding throughout any pre-closing period will also be essential and buyers may also be called upon to provide that interim funding.
- **What games can be played ?** Customer, Competitor, Staff and Distributor response
- **Impact on brand ?** What will customer say about the deal

Regulatory Issues:

- **Potential pricing claw back?** Government; Post Transaction Enquiry; Regulator; Shareholders
- **Impact of deal on long term business structure** – FDI caps; Takeover
- **Tax and Duties consequences –** regulatory concessions
- **Due Diligence** – assistance with due diligence, treatment of confidential information, access to regulatory correspondence
- **Regulatory concessions** - operational concessions till company can normalize.

Expeditiously Enforce the Process M&A Due Diligence – Knowns and Unknowns

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What do we know ?
How do we know it ?
What don't we know ?
What aren't we being told ?
Unknown unknowns ?
What is on the critical path ?

> There are known knowns; there are things we know we know. We also know there are known unknowns that is to say we know there are some things we do not know. But there are also unknown unknowns – the ones we don't know we don't know.

– Donald Rumsfeld, United States Secretary of Defense

Protect Policyholders

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The resolution approach for insurers reflects 'slow-burn' characteristic by prioritizing continuity of coverage to protect policy-owners (particularly for the life segment) through transfer of business or portfolio run-off.

General Insurance Policyholders:

- Provide option to cancel cover, provide refund of "unearned" premium and encourage new policy purchase
- Provide option to transfer policy to solvent insurer

Life Insurance Policyholders:

- Protection coverage – provide option to seek refund of premium and consider new policy purchase
- Long term savings or retirement – provide option to maintain policy and savings contribution

Policyholder Communication:

- Policyholders should be provided adequate information to protect their interests

Deposit Insurance:

- Last resort

Structure the Deal

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- Insolvency brings a process with no or limited scope for
  - MAC termination rights
  - Gap covenants
  - Indemnification for tax, capital, solvency, policy and other liabilities
  - Repetition of warranties (if indeed any are given).

- Purchaser may prefer a transfer of business rather than acquisition of the shares of the distressed insurer.

- As a result, pricing will be impacted.

Enhance Regulatory Certainty
Regulatory Qualification Requirements:

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- **FDI Caps**
  - Requirement for domestic investors
  - Reversing previously approved FDI caps
  - Regulatory policy of "domestification"
- **Single Presence** – as a matter of practice
  - Period to transition to single presence
- **Acquirer to be an insurer**
- **Holding Company and Financial Holding Company Requirement**
- **Mandatory Offer Trigger for Listed Insurers on 30% acquisition**
- **Market Competition Criteria**

Enhance Regulatory Certainty
Regulatory Qualification

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- **Approval to play. Approval to pay.**
- **National Service Requirements**
- **Reversion to pre-acquisition FDI requirements**
- **Consistent capital standards –** between Conventional, Takaful and digital insurers and takaful operators (DITO)

- **Voluntary exit plan** - clear, sound and feasible
- **Approval to withdraw or amend policy terms to unsustainable products**
- **Confidentiality of regulatory correspondence to Insurer's Boards and Officers**
- **Tax implications**

The challenge of insuring uncertainty

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Regulators during the resolution process should remain open for dialogue, provide timely guidance and approvals, and have sufficient talent to engage in the M&A transaction process.

1. Monitor, Predict and Prevent
2. Expeditiously Enforce the Process
3. Protect Policyholders
4. Structure the Deal
5. Enhance Regulatory Certainty

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John Spence is the founder of Asian Capital Advisors. Based in Hong Kong since 2000, John has focused on executing Asian insurance mergers and acquisitions transactions, fostering strategic alliances, launching innovative insurance customer offers, crafting digital initiatives and ecosystems partnerships, and evaluating insurtech business opportunities. John with M&A experience across Asia, North America and Australia is practiced at leveraging global teams and guiding local teams by aligning strategic insights and exercising rigour in corporate governance.

John has held a number of senior leadership roles across the financial sector. From 2015 to 2023, he served as the Regional Head of M&A and Strategy for Generali Asia. Prior to this, John held leadership roles at Keefe, Bruyette & Woods (KBW), Macquarie Funds Group, and Manulife Financial. Prior to moving to Hong Kong, John held various roles with Manulife Financial in Canada and in Australia he worked with National Australia Bank, Colonial Mutual, AMP Society, and KPMG.

John holds a Masters of Business Administration (MBA) from Australian Graduate School of Management (AGSM) at the University of New South Wales Business School, Bachelor of Economics (BEc) from Sydney University, is a Fellow Chartered Accountant Australia and New Zealand (FCA ANZ), Fellow Australian Institute of Banking and Finance (FFin), Governance Institute of Australia (FGIA FCIS); Australian Institute of Company Directors (FAICD) and the Hong Kong Institute of Directors (FHKIoD). He is Certified Financial Planner (CFP) of the Financial Advice Association of Australia, a Senior Associate of the Australian and New Zealand Institute of Insurance and Finance (ANZIIF (Snr Assoc) CIP) and is a Chartered Tax Advisor of the Tax Institute (CTA); Also he is a Member of the MBA Australasia (mMBAus).

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