General IAA Views on ICS Version 1.0

Presented by Dave Sandberg
Chair IAA Insurance Regulation Committee
IAIS Stakeholder Meetings, La Jolla, CA January 17, 2017

IAA Perspective on ICS

- The IAA supports the efforts of the IAIS and is actively engaged to seek a workable framework thanks to its global and diverse membership.
- Agree with the overall goal of comparability of financial statements and required capital worldwide for insurance entities.
- The IAIS approach is reasonable as a Step 1.

Framework

- There is value in a standard approach to assess insurer capital requirements and the IAA is supportive of many aspects of the design of the ICS standard approach as detailed in the CD. (Past support for one-year shock horizon and VaR at a confidence level such as 99.5% as a run-off basis for single entities.)
- However, the design requires improvement or correction in many areas. (Q 236)

Framework

- The use of confidence levels as a benchmark is not a precise number and is often misinterpreted. The results have much less precision in them than is implied by the use of a confidence level such as 99.5%. (Q 236)
- Especially when added to the assessment of a group and its diversification benefits.
- Risk dependencies and their impact can vary considerably from one insurer’s circumstances to another. (Q210)

IAA Responses on ICS

What Objectives Are Most Important?

- Comparability – How precise can/should it be for Averages vs. Tail/Extreme Events
- Risk Sensitivity – today vs. long term?
- Run off, going concern, viable market?
- Trigger Legal Authority and/or regulatory insight in and between colleges?
- Shareholder Valuation or Solvency Valuation?
- Harmonizing Capital with other tools

Groups

- Groups can have multiple supervisors/regulators
- Regulators can have different objectives, different approaches & risk tolerances e. g.
  - Bottom up vs. Top down regulation
  - Save group vs. legal entities or market

- Entire capital standard needs a coherent use of ingredients and shared regulatory objectives

Group Capital

- Until Solvency 2, required capital focused on legal entity. Group capital introduces additional issues.
- Groups typically have greater access to capital markets, but …
- Location of the capital matters
- Fungibility matters
- What is the Head of the Insurance Group?
  - Weighing Influence vs. Affliation

Specific IAA Views on ICS Version 1.0

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Common recovery measures and potential barriers to resolvability

- Support from external suppliers
- Use of intra group loans/finance structures
- Internal reinsurance
- Fungibility
- Disposal of valuable assets and business
- Support from regulators
- Strengthen capital position
- Legal entity structure
- Key Senior Staff
- Funding Recovery

Valuation Issues

- Why not leverage more of existing and coming new accounting frameworks versus build a new accounting framework for the ICS?
  - Does auditable = comparable?
- Support dual approach for field testing
  - Shared caveats with each approach
- MOCE
  - IASB Risk Margin has different purpose than IAIS MOCE though have many shared elements
  - MOCE definition must comprehend interdependency of GAAP, IFRS, Taxes, time horizon, credit/market risks

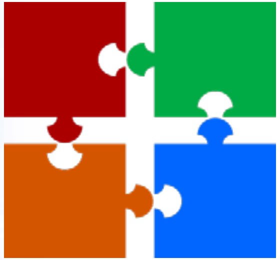
Valuation Issues (Cont.)

- Risk and Resolution different for Time Horizon:
  - Liquidity (0-90 day horizon)
  - Bad experience on insurance (1-3 to 5 year horizon)
  - Valuing long term guarantees (3-30 year horizon)
- Assessing value of Risk sharing with Policyholder (Par/Dividend Products)
  - Discount guarantees at a “bottom up” rate or
  - Discount likely cash flows at real world rates
- After tax required capital number
  - Simple methods not comparable

Next Steps for 2.0?

- Clearer linkage with resolution and other tools such as stress testing, actuarial function and accounting (new IASB)
- Any standardized calculation framework will have “holes” as trade offs occur between accuracy and materiality
  - Who owns disclosing those emerging and recognized gaps?
- How to sustain maintenance over time

Linkage/Integration



Aggregated risk measures + Qualitative (ORSA, stress tests, financial condition report, etc.)

- Actions to be taken by Reg and Firm
  - Rate increases
  - Sell assets or segments
  - Delay claims
  - Supervisory coordination (esp. capital movement)

How to Address Speed of Global Change

- Will impact:
  - Actuarial Standards
  - Actuarial Function
  - Degree of Regulatory Dialogue
  - ORSA
  - Internal Models
- To assess new or changing risks and legal conditions

Effect on Regulator and Corporate Behavior

- Checklists versus principled governance
- More transparency and dialogue or a constraint on insurance effectiveness?
- Numbers whether Factors or Internal Models will always be “wrong”
  - Need to increase the speed to understand if they are materially wrong and what remedies can be used (ERM processes)

Thank you

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