



ICS – Key Issues to Address

The GA/IIF response to the ICS consultation

17 January 2017, La Jolla
IAIS Stakeholder Meeting

ICS Consultation: Joint response by the GA and IIF

- ➔ Acknowledge progress on a range of technical issues – to be further elaborated as part of the Field Test Exercise
- ➔ The consultation focused on valuation, capital resources and calibration
- ➔ A number of important issues need to be dealt with before the future regime can be fully understood and evaluated
- ➔ Therefore a key goal for the GA/IIF has been to focus on these important issues
 - ➔ placing the ICS on top of existing local regimes as currently envisioned will result in conflicting solvency regimes
- ➔ it is critical to its success that the ICS project get the necessary political buy-in at all levels along its development.

Before ICS version 1.0 is released, further work must:

- » Explain the ICS' relation to existing capital regimes
- » Clarify the interplay of the ICS and the other modules and elements of ComFrame and the ability of the measure to reflect local circumstances
- » Make substantial improvements to the valuation approaches

Hence, the GA/IIF urge for a sequential approach in which higher-level, principles-based measures are designed and then fully tested before work is advanced further

GA/IIF Main Messages

Main messages submitted to the IAIS

- » Insurance markets around the world are characterized by **varying** supervisory **regimes**, regulatory requirements and market circumstances. The **current ICS** valuation approach, standard model and other technicalities **do not take these differences into account** – they should!
- » Hence, consistency with regional circumstances and capital regimes must be promoted

- » In its **current form** the ICS has a very **prescriptive nature**, which goes **beyond and above** the level of prescriptiveness for it to be a **basis to achieve real comparability** of solvency requirements and positions and seems to diverge from the principles based approach the IAIS seems to take with other parts of ComFrame
- » Hence, ICS needs to be truly embedded in ComFrame, where capital is viewed in the context of the broader supervisory framework including but not limited to corporate governance, ERM standards, ORSA and stress testing. ICS should be designed in a way that allows it to complement the existing tools rather than replace them.
- » A key issue is the **valuation approach** underlying the solvency calculation. We did not indicate a preference for one approach over the other. We stressed that both approaches aim to deal with excessive short term volatility. The two **approaches should bring about comparable results**
- » We pledged for the **ICS** to be **based** on a **valuation framework** that takes due account of the **insurance business model**, and reflects this in the way assets and liabilities are treated
- » **Existing work** on developing and refining solvency regimes – not least in the U.S. and Europe – must be **taken into account when developing the ICS**

GA/IIF on the level of calibration

Calibration seems to tight for a number of reasons – avoid material unintended consequences

- » Redundant layers of conservatism – valuation, MOCE, stress design and calibration
- » ICS seems to be a hard target. A ladder of regulatory intervention should be introduced
- » Most – not all – members believe that the MOCE merely acts as another layer of capital in addition to the 99.5% VaR requirement
- » A large majority of the GA/ IIF members consider that the introduction of the Margin Over Current Estimate (MOCE) as a key concern, and question its economic rationale for the application of a MOCE if current estimates and capital requirements are properly defined
- » In light of a MOCE, a vast majority of members believe that in an ICS, balance sheet valuations should be based on best-estimate assumptions for future liability cash flows, with any potential unexpected losses covered by capital requirements, hence the ICS should not include a MOCE.
- » Concrete example of shocks in the calibration which seem to overshoot 99,5 pct. VaR
- » The current ICS framework does not appropriately incentivize ALM and diversification. Insurance is often long-term in nature, the ICS however, takes a short-term perspective in assessing a group's solvency situation and does therefore not pay due attention to insurers' business models.