

# Explanatory note on the draft criteria for the Aggregation Method comparability consultation

## Background

In November 2017, the International Association of Insurance Supervisors (IAIS) set out an agreement on the implementation of Insurance Capital Standard (ICS) Version 2.0, including a unified path to convergence of group capital standards in furtherance of its ultimate goal of a single ICS that achieves comparable outcomes across jurisdictions.<sup>1</sup> The agreement acknowledges the development by the United States of the Aggregation Method (AM) to a group capital calculation. While the AM is not part of the ICS, the IAIS aims to be in a position by the end of the monitoring period to assess whether the AM provides comparable (ie substantially the same (in the sense of the ultimate goal)) outcomes to the ICS. If so, it will be considered an outcome-equivalent approach for implementation of ICS as a prescribed capital requirement (PCR). At the same time, the IAIS agreed to help collect data from the US and interested jurisdictions that will aid in the development of the AM.

In November 2019, the IAIS agreed on a process and timeline for developing criteria to assess whether the AM provides comparable outcomes to the ICS. As previously communicated in an [Explanatory Note](#), the IAIS agreed on a draft definition of comparable outcomes and an overarching approach (ie areas of focus) to guide the development of high-level principles (HLPs) and criteria. Based on the draft definition and overarching approach, the IAIS developed draft HLPs to inform the criteria that will be used to assess whether the AM provides comparable outcomes to the ICS.

## Consultation on draft comparability criteria

The IAIS has released a public consultation on the draft criteria that will be used to assess whether the AM provides comparable outcomes to the ICS. Stakeholders are invited to respond to the consultation at the following [link](#) until 15 August 2022.

In March 2021, following public consultation, the IAIS agreed on a definition of comparable outcomes and six high-level principles (HLPs) to guide the development of the comparability criteria. The IAIS began developing the draft comparability criteria in April 2021. Detailed criteria have been developed for each HLP. These draft criteria are the subject of this further consultation. The draft criteria have been developed in such a way that the AM is neither precluded at the outset as an outcome equivalent approach to the ICS for measuring group capital nor given a free pass. The draft criteria also took into account the comments from the first consultation on the draft HLPs, including the need for clarity in certain areas<sup>2</sup>. Annex 1 sets out how that feedback is reflected in the draft criteria for the purpose of this public consultation. Stakeholders are invited to provide feedback on whether each criterion is clear, adequate, sufficient or too restrictive, considering the HLP to which it relates.

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<sup>1</sup> Refer to the document [Implementation of ICS Version 2.0](#)

<sup>2</sup> The summary and resolution of comments document can be accessed [here](#).

The task of designing the comparability assessment is a complex one, given that the ICS and the AM framework are methodologically and conceptually quite distinct. IAIS members recognise that further work on the draft criteria may be needed post-consultation; however, there is consensus that the draft criteria are at a stage where moving forward with the public consultation is worthwhile.

As such, stakeholder feedback on the draft criteria is particularly important to provide a range of perspectives on this unprecedented area of work and gauge views on the appropriateness of the draft criteria. Responses to the consultation will help ensure the criteria take account of the complex issues that have to be addressed with this work

The consultation also provides the opportunity to obtain perspectives and technical input on various parameters included in the criteria. In particular, the IAIS seeks input to aid in the development of specific scenarios for the sensitivity analysis envisaged in the draft criteria for HLP 1. The IAIS is also seeking feedback on considerations for determining the representativeness of the non-life insurance sample. Following consideration of stakeholder comments, as well as ongoing work within the IAIS on the technical parameters, the IAIS will finalise the criteria that will be used to assess whether the AM provides comparable outcomes to the ICS. The final criteria, along with the definition of comparable outcomes and six HLPs, are expected to be adopted at the IAIS Annual General Meeting in November 2022.

## **Comparability assessment methodology, process and governance**

In parallel to its work on the draft criteria, the IAIS has been advancing discussions on how the comparability assessment will be conducted, focusing on the methodology, process and governance. The work to date has focused on three areas: selection of the assessment team, the oversight role of the ICS and Comparability Task Force<sup>3</sup> (ICSTF) and how each criterion will be assessed and contribute to the final decision on comparability.

The composition of the assessment team will follow the general principles and practices of the IAIS, including provisions to help ensure fairness with respect to ensuring the neutrality of the assessment team, independence, geographical diversity and prevention of potential conflicts of interest. The assessment team will comprise Secretariat employees who meet the above-mentioned principles and have sufficient technical expertise in both the AM and ICS. The assessment team will be responsible for delivering the necessary technical analysis to support the ICSTF in making an informed recommendation to the IAIS Executive Committee (ExCo) on the outcome of the comparability assessment.

The ICSTF will oversee the assessment team's work, including addressing questions from the assessment team and reviewing the interim and final results of their analysis. Based on the ICSTF's recommendations, the final decision on whether the AM provides comparable outcomes to the ICS will be made by ExCo.

The comparability criteria will be assessed using a scaled approach that considers the degree to which each criterion is met. However, the final decision on comparability will be binary (ie the AM provides comparable outcomes to the ICS or it does not).

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<sup>3</sup> The ICSTF comprises Executive Committee (ExCo) members from jurisdictions where internationally active insurance groups that are participating in the ICS monitoring period are headquartered. The mandate of the ICSTF is to provide strategic steering to ExCo on the monitoring, further improvement and practical implementation of the ICS as a PCR. It is also responsible for oversight of the work related to the comparability assessment.

## Key dates

Following the end of the consultation period, the upcoming milestones of the comparability assessment project are:

- 2022, Q4: *Adoption at the AGM of the definition, high level principles and criteria to assess whether an AM provides comparable outcomes to the ICS;*
- 2023, Q3: *Assessment of whether the AM provides comparable outcomes to the ICS begins;*
- 2024, Q2: *Assessment of whether the AM provides comparable outcomes to the ICS ends;*
- 2024, Q3: *Decision on whether the AM provides comparable outcomes to the ICS; and*
- 2024, Q3: *Publication of a report on the outcome of the assessment of whether the AM provides comparable outcomes to the ICS.*

## Annex I: How draft criteria address previous consultation feedback

The IAIS undertook a public consultation in November 2020 on the draft definition of comparable outcomes and High-Level Principles (HLPs) to guide the drafting of comparability criteria. In May 2021, the IAIS published a summary and resolution of comments received during the public consultation. The IAIS retained the definition and HLPs as drafted as the basis for developing the draft criteria, while at the same time indicating that those comments that are consistent with and do not contradict the HLPs and/or previous IAIS decisions regarding comparability will be considered in the development of the draft criteria. This annex sets out how that feedback is reflected in the draft criteria for purposes of this public consultation. As stated in this Explanatory Note, IAIS members recognise that further work on the draft criteria may be needed post-consultation. As such, the content of this annex is based on the status of the draft criteria at this point in time, but may change further following this current round of public consultation.

Reference	Comments or resolution referring to the draft criteria	How addressed in draft criteria
Definition	<p>Several comments related to clarifications and suggestions for revising the definition:</p> <ul style="list-style-type: none"> <li>• “<i>produce similar... results over time</i>” is unclear and should be clarified in the criteria;</li> <li>• AM should have the same level of policyholder protection as the ICS, so it is suggested to replace “<i>similar, but not necessarily identical, results</i>” with “<i>the same level of policyholder protection</i>”;</li> <li>• Scenarios should be defined for which outcomes will be compared (eg high/low interest rates, high//low spreads, pure life vs pure non-life vs mixed entities, different group sizes, different asset mixes, mature low growth/high growth company, etc.); and</li> <li>• AM and ICS should remain comparable over time (ie continuous follow-up monitoring).</li> </ul> <p>In addition, several comments related to the reference to supervisory action in the definition. At the time, the IAIS indicated that as it undertakes its work</p>	<p>See criteria 1.1 and 1.2, which provide more information on how this will be assessed.</p> <p>See criterion 3.1, which clarifies that the level of solvency protection in totality of the AM could be more but not less prudent than the ICS.</p> <p>In parallel with the public consultation on the draft comparability criteria, the IAIS will continue work on the technical parameters, including the development of scenarios. As part of the public consultation, the IAIS is seeking stakeholder input to aid in the development of specific scenarios for the sensitivity analysis envisaged in draft criterion 1.3.</p> <p>The question of follow-up monitoring is an implementation issue rather than an issue of the comparability criteria, and will be discussed separately.</p>

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	<p>on the development of the comparability criteria, the IAIS will determine if any further elaboration is needed compared to ICP 17.</p>	<p>The IAIS has resolved to retain the definition set out in ICP 17, without creating a new definition or a new guidance at this stage. ICP 17 is currently being reviewed with the aim of agreeing any revisions by the end of the ICS Monitoring Period.</p>
<p>HLP 1</p>	<p>Several comments related to clarifications and further suggestions for revising the HLP:</p> <ul style="list-style-type: none"> <li>• Clarify or remove reference to “<i>significantly correlated</i>” as it is ambiguous and inconsistent with the definition of comparable outcomes;</li> <li>• Business cycle is unclear, no standard definition – it should be adequately defined or removed;</li> <li>• Clarify or remove reference to “<i>short-term market fluctuations</i>”; and</li> <li>• Allowing the “<i>quantum of change</i>” to differ can lead to cases where the change in one method (ICS or AM) would lead to supervisory actions and the other would not, so suggest to remove reference to quantum of change.</li> </ul>	<p>The draft criteria do not define the terms.</p> <p>With respect to the reference to “<i>significantly correlated</i>”, the assessment team will undertake a technical analysis of the degree of correlation between the AM and ICS results; the IAIS will then apply judgment in considering whether the degree of correlation is sufficient to meet the comparability outcomes.</p> <p>With respect to references to “<i>the business cycle</i>” and “<i>short-term market fluctuations</i>”, this will be an issue that the IAIS will return to after the development of scenarios for the sensitivity analysis, to check whether through the development of the scenarios these concepts are sufficiently clear, or whether further work is needed on definitions.</p> <p>The consultation is seeking technical input on scenarios which would provide input for more detailed information on how scenarios will be designed.</p> <p>Regarding “<i>quantum of change</i>”, draft criterion 1.2 a. reflects that the analysis considers direction and quantum of change together over the business cycle to understand how the ICS and AM respond to changing economic and financial market conditions.</p>
<p>HLP 2</p>	<p>There was broad support for the first paragraph of the HLP, which recognises that while individual elements of a group solvency approach</p>	<p>Regarding capital requirements, draft criterion 2.2 specifies that the AM should capture the same underlying risks as the ICS, acknowledging that this could be</p>

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	<p>will be analysed, the decision on comparable outcomes will consider the elements in totality.</p> <p>Regarding capital requirements, some respondents provided the following comments:</p> <ul style="list-style-type: none"> <li>• having the same underlying risks is unrealistic, while others felt the AM should capture the same risks as the ICS;</li> <li>• the target criteria for capital requirements should be the same between ICS and AM; and</li> <li>• the overall level of solvency protection provided by the AM and ICS through valuation and capital requirement should be similar.</li> </ul> <p>Regarding capital resources, one respondent said ICS and AM should have the same approach, while another respondent said that local rules should be used with scalars applied to equate different regimes.</p>	<p>either an explicit risk charge (taking into account different risk groupings), prudence embedded in valuation (ie accounting conservatism) or other such quantitative measures (eg scalars).</p> <p>Regarding capital resources, draft criterion 2.4 specifies that the overall quality and eligibility of capital resources allowed in the AM is similar to the ICS for the representative sample. This determination is made by considering various aspects outlined in the criteria.</p> <p>Draft criterion 2.3 states that analysis will include whether the overall AM capital requirement provides a similar level of solvency protection as the ICS.</p>
HLP 3	Some respondents asked for clarity on what is meant by prudent, while other respondents were concerned that this would set an arbitrary floor for the AM.	The draft criterion provides elaboration on the meaning of this HLP and the analysis that will be conducted to assess it.
HLP 4	There was broad support for this HLP as drafted.	
HLP 5	<p>Several comments related to clarifications and further suggestions for revising the HLP:</p> <ul style="list-style-type: none"> <li>• Reference to “business cycle” should be removed as an objective comparability cannot be assessed based on such a vague, ambiguous, term;</li> <li>• Flexibility should be allowed if sufficient data cannot be collected,</li> </ul>	Clarifications are provided on the definition and assessment of representativeness (5.1 and 5.2). The draft criteria consider that the more heterogenous nature of life operations may require a relatively large sample, while the more homogenous nature of non-life operations in some jurisdictions, may require a smaller sample.

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	<p>possibly through the development of hypothetical but representative portfolios;</p> <ul style="list-style-type: none"> <li>• This principle should recognise that the representative sample need only be from the U.S. and other interested jurisdictions;</li> <li>• The representative sample should be from as large a population of such jurisdictions and markets as possible; and</li> <li>• The comparability assessment at inception should be followed by a monitoring exercise on an ongoing basis, in cases where either the ICS or the AM would undergo changes.</li> </ul>	<p>As part of the public consultation, the IAIS is seeking specific input on the appropriateness of the analysis to determine representativeness of the sample as described in criterion 5.2, including the appropriateness of the indicators and the level of homogeneity of the non-life market for the US and other interested jurisdictions (5.2 d).</p> <p>The question of follow-up monitoring is an implementation issue rather than an issue of the comparability criteria. IAIS plans to discuss at a later stage potential options for addressing changes to ICS and AM that may occur after the assessment which could be relevant to the comparability assessment.</p>
HLP 6	<p>General support was given by several respondents to this HLP while several comments related to clarifications and further suggestions for revising the HLP:</p> <ul style="list-style-type: none"> <li>• It is important to understand what is meant by "similarly transparent" and what is expected from this statement; and</li> <li>• The public disclosure clause should be eliminated.</li> </ul>	<p>Draft criterion 6.1 clarifies that ComFrame requirements related to reporting to group-wide supervisors and public disclosure will also apply to AM.</p>
General Comments	<ul style="list-style-type: none"> <li>• Comparability criteria should remain stable and robust enough to withstand any changes in the design of the ICS and AM;</li> <li>• It is desirable to have as many insurance groups that report AM results as possible report ICS results to deliver robust and credible output of the AM comparability assessment to the ICS; and</li> <li>• Suggest an additional clause that AM and ICS must not give rise to unfair competitive advantage to</li> </ul>	<p>Draft criteria have been developed with the perspective of being applicable to the candidate versions of AM and ICS as a PCR, as available at the time of the comparability assessment. The IAIS plans to discuss actions that could be taken, after the implementation of AM and ICS as a PCR, to ensure continuing comparability.</p> <p>The draft criteria have been developed with the view of defining representative samples of IAIGs providing both AM and ICS information. Representative</p>

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	groups based on which of the bases they are using.	samples will be determined so as to deliver robust and credible output.  It is expected that comparable outcomes would provide a level playing field.