U.S. State Insurance Regulators' Views: International Capital Proposals

April, 2015

Purpose:

The purpose of this document is to articulate the views of U.S. state insurance regulators toward the uses of capital within prudential regulation and to help guide their ongoing work and input during the development by the International Association of Insurance Supervisors (IAIS) of a risk-based global insurance capital standard (ICS) for internationally active insurance groups (IAIGs), as well as basic capital requirements (BCR) and higher loss absorbency (HLA) requirements for global systemically important insurers (G-SIIs). This document is also intended to identify the characteristics of such developments that are necessary for U.S. state insurance regulators to support their implementation in our national system of state-based insurance regulation. As these developments continue to evolve, financial regulation. As U.S. insurance regulators work within the IAIS to develop and consider implementing the various capital proposals, we will be mindful of the cost/benefit of the proposed standards, the impact on insurance product availability and affordability or other market impacts, and the compatibility of the proposed standards with the U.S. insurance regulatory system.

The following general views guide U.S. state insurance regulators' overall approach and expectations towards the development of capital standards and the various international proposals:

Capital standards:

U.S. state insurance regulators support the need to assess capital adequacy as part of coordinated solvency oversight and recognize that insurance supervisors in emerging markets are calling for basic international capital standards or benchmarks of some kind; however, a single uniform capital standard is not the silver bullet solution, but rather should be seen as one of many tools used to achieve more effective regulation and/or greater financial stability.

The business model for insurance is significantly different than the business model for banking and even the business models and risk management approaches amongst insurers are unique. The track record in the banking sector of a reliance on capital standards did not prevent a system-wide banking collapse during the recent financial crisis. Development of an ICS needs to reflect the distinct characteristics of the insurance business model and its supervision.

The risks inherent in insurance products, even for the same business line, can be very different jurisdiction to jurisdiction. A single risk charge for that business line may well lead to incorrect assessments of the relative capital strength of IAIGs.

Fungibility:

U.S. state insurance regulators are also concerned with a reliance on the assumption that capital can be freely moved within an insurance group. It is crilt les 53 5552(t)-4les 53 555luw1 204.2 sectorce on 1g

Accounting and Valuation:

There remain major differences among jurisdictions in accounting systems and approaches to valuation of assets and liabilities, as well as differences in regulatory objectives. As long as these differences exist, the development of an ICS, BCR and HLA will need to take this into account.

U.S. state insurance regulators support the development of a “GAAP Plus” valuation approach that can be utilized by insurance groups and which can result in comparable outcomes across jurisdictions. It achieves sufficient comparability, and differences between other approaches can readily be understood by the group-

Higher Loss Absorbency (HLA):

The HLA should be developed for application to G-SIIs as a way to address systemic risk issues; as it has a very specific purpose, HLA should not be applied to insurers which are not designated as systemically important. As it is specific activities that are the focus of assessing potential systemic risk within the insurance sector, not traditional insurance business itself, the HLA should be developed in a manner that addresses those specific activities which may pose potential systemic concerns.

Insurance Capital Standard (ICS):

A global ICS for IAIGs should continue to be developed as a supplement to jurisdictional capital requirements. For the U.S., it would supplement the U.S. RBC that applies at the legal entity level; we do not intend for RBC to be replaced by any new group capital rules but rather augment our existing approach.

It is important to have adequate capital at the group level, but this cannot be a substitute for having adequate capital at the legal entity level. Measurement of a global ICS should be against available capital resources (rather than existing jurisdictional requirements) on either an aggregated entity basis (bottom up approach) or a consolidated basis (top down approach). It should not be used to adjust jurisdictional entity requirements.

A primary objective of a global ICS should be enhancing the efficacy of capital requirements in order to help facilitate solvency systems in developing markets be on par with, though not necessarily identical to, such systems in developed markets.