AMERICAN ACADEMY *of* ACTUARIES

September 18, 2014

Kevin M. McCarty, Chair
ComFrame Development and Analysis Working Group
International Insurance Relations (G) Committee
National Association of Insurance Commissioners

RE: September 19th ComFrame Development and Analysis Working Group Meeting on Approaches to Group Capital

Dear Commissioner McCarty:

On behalf of the American Academy of Actuaries'[1] Solvency Committee, I would like to provide you and the working group members input on certain key priorities and principles that should be contemplated when considering and developing insurance group solvency and capital standards. Actuaries have worked for decades with insurance and other financial sector regulators to develop prudent rules addressing insurer solvency, including capital requirements. As regulators continue to discuss and develop insurance group capital and solvency standards, the American Academy of Actuaries offers its support for the efforts of US regulators in engaging and shaping this challenging area of public policy. To this end, we request that the following principles be considered as the National Association of Insurance Commissioners (NAIC) develops its perspectives concerning the elements of US insurance group capital and solvency proposals:

1. A group solvency regime should be <u>clear regarding its regulatory purpose and goals</u>. For example, the purpose could be to protect policyholders, enhance financial stability, ensure a competitive marketplace, provide a level playing field, identify weakly capitalized companies, rank well-capitalized insurers, improve risk management practices and procedures or some combination of the above. The regulatory purpose and goals will inform the development of a standard itself, as well as the associated regulatory actions and priorities.

2. Any <u>metrics, information or other output</u> of a group solvency standard should be useful to all relevant parties (regulators, management, shareholders, rating agencies etc.).

3. A group solvency regime should <u>promote responsible risk management</u> in the regulated group and <u>encourage risk-based regulation</u>. For example, a solvency regime should recognize risk mitigation activities, such as asset / liability matching, hedging and

[1] The American Academy of Actuaries is an 18,000-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

reinsurance. The actuarial functions are critical in the risk management process and their role should be clearly defined, as it is in the U.S. reserving and solvency framework. Actuaries can and should identify where factor-based systems may miss key emerging risks, set reasonable boundaries around more subjective estimates and modeling and, as appropriate, render actuarial opinions.

4. Methods should recognize and take into consideration the local jurisdictional environment(s) under which members of an insurer group operates, including the local regulatory regime, product market and economic, legal, political and tax conditions.

5. A group solvency standard should be compatible across accounting regimes, given the political uncertainties in achieving uniform standards.

6. A group solvency standard should minimize pro-cyclical volatility, so as to avoid unintended and harmful consequences on regulated insurance groups, insurance markets and the broader financial markets.

7. A group solvency standard should present a realistic view of an insurance group's financial position and exposures to risk over an agreed-upon time frame.

8. All assumptions used in any capital or solvency model should be internally consistent.

9. It is more important to focus on the total asset requirement than the level of required reserves or capital on a separate basis. The focus should be on holding adequate total assets to meet obligations as they come due. Whether a jurisdictional standard requires the allocation of these assets to liabilities versus capital / surplus should be irrelevant to the overall solvency regime.

10. It must be demonstrated that the capital held is accessible, including in times of stress, to the entity facing the risk for which the capital is required.

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Thank you for this opportunity to provide our views on the key principles that should inform the development of insurance group solvency and capital standards. If you have any questions or would like to discuss these issues in more detail, please contact Lauren Sarper, the Academy's senior policy analyst for risk management and financial reporting, at 202.223.8196 or sarper@actuary.org.

Sincerely,

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Chairperson, Solvency Committee
Risk Management and Financial Reporting Council
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