



**ASSOCIATION ACTUARIELLE INTERNATIONALE  
INTERNATIONAL ACTUARIAL ASSOCIATION**

May 12, 2003

Mr. Robert Esson  
International Association of Insurance Supervisors  
c/o Bank for International Settlements  
CH-4002 Basel  
Switzerland  
Email: [REsson@naic.org](mailto:REsson@naic.org)

Dear Mr. Esson,

**Subject: Draft Issues Paper on Insurance Securitization**

Further to my letter to you of December 5, 2002 forwarding the International Actuarial Association's (IAA) draft comments on the Draft Issues Paper on Insurance Securitization, I am pleased to confirm that the IAA's due process is now complete. The draft comments were approved by the Full Member associations for release as an IAA public statement, subject to certain revisions which are incorporated in the attached submission.

A copy of the final document is enclosed for your files.

Yours sincerely,

W. James MacGinnitie  
President

Attachment

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**A Commentary on the  
DRAFT ISSUES PAPER ON INSURANCE SECURITIZATION  
Released by the International Association of Insurance Supervisors: October 2002**

**International Actuarial Association**

The International Actuarial Association (the “IAA”) represents the international actuarial profession. Our Full Member actuarial associations exceed forty-five in number, and represent more than 95% of all actuaries practising around the world. The Full Member associations of the IAA are listed in an Appendix to this statement. The IAA promotes high standards of actuarial professionalism across the globe and serves as the voice of the actuarial profession when dealing with other international bodies on matters falling within or likely to have an impact on the areas of expertise of actuaries.

**Due Process**

These comments have been prepared by two committees of the IAA, the members of which are listed below by name and association. These comments, which were circulated for approval to the Full Member associations of the IAA as part of our due process procedures, have been approved as a public statement of the IAA.

**Members of the IAA Insurance Regulation Committee**

Jukka Rantala	Chairman
David Hartman	Co-Vice-Chairman
David Sandberg	Co-Vice-Chairman
Félix Arias Bergadà	Col.Legi d'Actuaris de Catalunya
Morris Chambers	Canadian Institute of Actuaries
Isagani de Castro	Actuarial Society of the Philippines
Nelson Emiliano Costa	Instituto Brasileiro de Actuária
Joubert Fereira	Actuarial Society of South Africa
Rainer Fürhaupter	Deutsche Aktuarvereinigung e. V. (DAV)
K.S. Gopalakrishnan	Actuarial Society of India
Gyula Horvath	Hungarian Actuarial Society
Thomas Karp	Institute of Actuaries of Australia
Jean-Michel Kupper	Association Royale des Actuaire Belges
Won How Lo	Actuarial Institute of the Republic of China
Helge-Ivar Magnussen	Den Norske Aktuarforening
Ibrahim Muhanna	Cyprus Association of Actuaries, Lebanese Association of Actuaries
Ryoichi Nakamura	Institute of Actuaries of Japan
Gennaro Olivieri	Istituto Italiano degli Attuari
Ian Perera	New Zealand Society of Actuaries
Thierry Poincelin	Institut des Actuaire
Angus John Robertson	Faculty of Actuaries
Norma Alicia Rosas	Colegio Nacional de Actuarios A.C.
Simon Van Vuure	Het Actuarieel Genootschap
Robert E Wilcox	Society of Actuaries; Conference of Consulting Actuaries

**Members of the IAA Financial Risks Committee**

David Kingston	Chairperson
Anthony Coleman	Vice-Chairperson
Jean Berthon	Institut des Actuaire
Leonardo Camozzato	Instituto Brasileiro de Atuária (IBA)
Paolo De Angelis	Istituto Italiano degli Attuari
Charles Hill	Canadian Institute of Actuaries
R Kannan	Actuarial Society of India
Christoph Krischanitz	Aktuarvereinigung Österreichs (AVÖ)
Janina Slawski	Actuarial Society of South Africa

The IAA appreciated the opportunity to respond to this paper at the draft stage. The issues surrounding “insurance-linked securitization” are of considerable interest to the actuarial profession as actuaries have been centrally involved in the technical development of many of the schemes described in the paper.

We support the development of securitization and other financing structures that can improve the efficiency of insurance systems, encourage innovation and in a competitive market can thus be expected to lower the costs of insurance. An effective regulatory framework will support this.

**The Areas for Regulation**

From the insurer’s viewpoint, insurance-linked securitization is a means of financing. To subsequent holders, including other insurers, the instrument is a security. We support the development of a framework of regulations to cover, among other things, the origination of the security, the value at which such a security may be held, the ways in which the security may be traded and the means by which policyholders are protected.

As the paper describes, insurance-linked securities have provided limited means for insurers to access markets traditionally reached through reinsurance. As the market for these securities continues to grow, insurers' risk management alternatives will expand beyond reinsurance. It would be useful to identify areas where regulations treat economically identical transactions in disparate fashion in order to avoid situations where regulation dictates the form rather than the substance of market activities. Clearly, the securitization of insurance risks should not relieve an insurer of the ultimate contractual liability to its policyholders.

Regulators in a number of territories have recently drawn attention to the scope for complex reinsurance transaction to cause a misunderstanding of balance sheets to the peril of investors and perhaps also policyholders (e.g. APRA’s comments in Australia concerning the failure of HIH). Full disclosure of insurance related securities in the accounts of all involved parties is essential for the operation of a healthy marketplace. All transactions of insurance related securities should be at arms length and standards should be developed for an appropriate disclosure of all such transactions, irrespective of their legal form.

**Risk Pooling**

A traditional approach to risk diversification has been the setting up of mutual risk pools, whereby several insurers agree to share their joint experience. Reinsurers have generally run

such pools. Insurance-linked securitization could provide the means to achieve such risk pooling more widely across financial markets. It would clearly be helpful if the regulatory framework recognized and facilitated this possibility.

Insurance-linked securitization should offer particular attractions to mutual insurers who are of course unable to raise additional capital from shareholders to finance growth. A marketable security can be constructed which provides for a loan to be raised with payment of interest and repayment on terms linked to the surplus emerging from a block of business and subordinated to the interests and 'reasonable expectations' of policyholders. National Provident Institution's subordinated debt fund raising in the UK market in the early 1990's is a well-known example to UK actuaries.

Paragraph 4 of the draft states that "Portfolio theory holds that the addition of uncorrelated risks to an investment portfolio reduces the overall risk of the portfolio." While it is true that when an uncorrelated risk is added to an existing investment portfolio that the risk of the new portfolio is less than the sum of the two separate risks before pooling, it is not true that the overall risk of the new portfolio is less than the overall risk of the old portfolio. It might be clearer to replace '...reduces the overall risk...' with '...enhances the risk-return characteristic...' and also '...diminish the overall risk...' with '...improves the risk-return characteristic...!.

### **Closing Remarks**

As noted above, we believe this is an important area of development for the insurance industry and we are pleased to support the IAIS as it develops its regulatory framework.

*Appendix*

**FULL MEMBER ASSOCIATIONS OF THE IAA**

Consejo Profesional de Ciencias Económicas de La Ciudad Autónoma de Buenos Aires (Argentina)  
Institute of Actuaries of Australia (Australia)  
Aktuarvereinigung Österreichs (AVÖ) (Austria)  
Association Royale des Actuaire Belges (Belgique)  
Instituto Brasileiro de Atuária (IBA) (Brazil)  
Canadian Institute of Actuaries (Canada)  
Cyprus Association of Actuaries (Cyprus)  
Česká Společnost Aktuárů (Czech Republic)  
Den Danske Aktuarforening (Denmark)  
Egyptian Society of Actuaries (Egypt)  
Estonian Actuarial Society (Estonia)  
Suomen Aktuaariyhdistys (Finland)  
Institut des Actuaire (France)  
Deutsche Aktuarvereinigung e. V. (DAV) (Germany)  
Hellenic Actuarial Society (Greece)  
Actuarial Society of Hong Kong (Hong Kong)  
Hungarian Actuarial Society (Hungary)  
Félag Íslenskra Tryggingastærðfræðinga (Iceland)  
Actuarial Society of India (India)  
Society of Actuaries in Ireland (Ireland)  
Israel Association of Actuaries (Israel)  
Istituto Italiano degli Attuari (Italy)  
Institute of Actuaries of Japan (Japan)  
Japanese Society of Certified Pension Actuaries (Japan)  
Lebanese Association of Actuaries (Lebanon)  
Colegio Nacional de Actuarios A. C. (Mexico)  
Het Actuarieel Genootschap (Netherlands)  
New Zealand Society of Actuaries (New Zealand)  
Den Norske Aktuarforening (Norway)  
Actuarial Society of the Philippines (Philippines)  
Polskie Stowarzyszenie Aktuaruszy (Poland)  
Instituto dos Actuários Portugueses (Portugal)  
Academia de Actuarios de Puerto Rico (Puerto Rico)  
Slovensko Aktuarsko Drustvo (Slovenia)  
Actuarial Society of South Africa (South Africa)  
Col.legi d'Actuaris de Catalunya (Spain)  
Instituto de Actuarios Españoles (Spain)  
Svenska Aktuarieföreningen (Sweden)  
Association Suisse des Actuaire (Switzerland)  
Actuarial Institute of the Republic of China (Taiwan R.O.C.)  
Faculty of Actuaries (United Kingdom)  
Institute of Actuaries (United Kingdom)  
American Academy of Actuaries (United States)  
American Society of Pension Actuaries (United States)  
Casualty Actuarial Society (United States)  
Conference of Consulting Actuaries (United States)  
Society of Actuaries (United States)