INTERNATIONAL ACTUARIAL ASSOCIATION
ASSOCIATION ACTUARIELLE INTERNATIONALE

Draft Statement of Intent (SOI) for ISAP [7] – "Current estimates" and other matters in relation to the IAIS capital standards

Submitted by: The Actuarial Standards Committee (ASC)

1. Background

In response to a request from the Financial Stability Board and the G20, the International Association of Insurance Supervisors (IAIS) is developing a series of capital standards over the coming years, starting with a Basic Capital Requirement (BCR) for the largest global systemically important insurers (those identified as "G-SIIs"). They will go on to expand their work to cover the IAIGs (the internationally active insurance groups) through a global Insurance Capital Standard (ICS) and possibly to others in due course, through local adoption. All of these standards will, necessarily, require a consistent valuation of insurance liabilities between different insurers for the results to be meaningful.

There is a degree of uncertainty as to the exact timing of implementation of the proposals. Currently the IAIS timetable calls for the BCR to be adopted in late 2014 and progressively implemented during 2015 and beyond. While the actuarial aspects of the work involved for the ICS will have some similarities to the BCR, suggesting that one International Standard of Actuarial Practice (ISAP) to cover both would be preferable to two different ISAPs, additional detail regarding the ICS will be forthcoming only in 2015. In order to be able to publish an Exposure Draft of an ISAP in a timely manner with respect to the BCR, the ASC is proceeding with this Statement of Intent now for such an ISAP. Depending upon how the development of the ICS by the IAIS evolves, either the initial ISAP for the BCR will be extended to cover the ICS as well, or a separate ISAP for the ICS will be called for. In either case, the ASC will prepare/revise the SOI with its intentions, following Due Process.

2. Purpose

Because actuaries in many jurisdictions acting for or on behalf of many different insurers covering many different types of insurance contract will be providing actuarial services in connection with IAIS requirements, an ISAP is the most effective means to facilitate convergence in actuarial practice within and across jurisdictions (as per IAA Strategic objective 3). It is also the wish of the IAIS that the IAA assists by providing a model standard for this work, which may then be adopted by local standard setters or possibly as a requirement from supervisors. Hence this ISAP is expected to:

- Provide guidance to actuaries providing actuarial services in relation to these IAIS requirements to facilitate convergence in actuarial practice with respect to these services within and across jurisdictions;
- Increase public confidence in actuaries' services in relation to these IAIS requirements;
- Increase insurers' confidence in actuaries' contributions to solvency reporting connected to these IAIS requirements; and
- Demonstrate the IAA's commitment to support the work of the IAIS.

This purpose may differ from that underlying investor reporting standards and the ISAP will reflect differences where appropriate.

3. *Scope, roles and content*

The proposed ISAP will provide guidance to actuaries providing actuarial services in relation to these IAIS capital requirements.

The ISAP is expected to address the following aspects of actuarial services in accordance with IAIS requirements, to the extent not covered in ISAP 1:

- The calculation of the value of insurance liabilities on a "current estimate" basis (which is currently intended by IAIS to be an estimate of the mean value of the distribution of possible outcomes) where such will be defined in accordance with IAIS requirements and the legal status, and not with regard to IFRS definitions; and
- Such elements of the BCR calculation as might require actuarial judgement in their application, and possibly also of the ICS calculation at a later stage when more detail becomes available.

It is envisaged that these two areas will be approached in different ways. For the insurance liabilities calculations it is expected that all key areas will be within scope, provided that sufficient common ground can be found to meet the acceptability standards of the IAA, with only those areas where the IAIS lays down specific requirements being out of scope. At present it seems the IAIS does not intend there to be a risk margin included in the calculation of the value of insurance liabilities which will be on a "current estimate" basis, though it is quite possible this will change with time. The ISAP will follow the IAIS in this regard. For the BCR itself (i.e., the minimum amount to be held by an insurer in addition to the "current estimate" liabilities) and possibly later for the ICS itself, the opposite approach is envisaged, where only those areas where specific IAIS requests are received or where clearly the IAIS requirements lead to actuarial judgement will be addressed in the ISAP.

It is expected that the calculation of the value of insurance liabilities on a "current estimate" basis will cover the following areas:

- Financial elements
  - Discounting
  - Inflation
  - Financial Options and Guarantees
  - Profit Sharing
- Insurance elements
  - Actuarial reserves in respect of life assurance type liabilities, in particular in respect of mortality, longevity and morbidity
  - Unexpired Premium / Risk reserves, in particular for property/casualty type risks (including short-term morbidity risks)
  - Outstanding claims reserves including IBNR and claim management costs
  - Impact of policyholder behaviours
  - Impact of management actions
  - Claims inflation
- Other effects
  - Expenses
  - Other risks not covered elsewhere but arising from the operation of insurance contracts
  - Taxation effects
  - ~~Reinsurance considerations~~Considerations of reinsurance and other mitigation techniques

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It is expected that certain key principles will be adopted:

- The criticality of a consistent approach to liability valuation with the IAIS's preference for fair or market valuation of assets

- The desire to avoid artificial instability in the relative values of assets and liabilities, especially where these are well-matched

In respect of the BCR itself and the ICS itself, no specific areas are yet identified, but these may arise as IAIS develops its thinking, but where necessary the insurance liability standards may be designed to avoid any double counting or excessive prudence (such as can, in particular, arise from tax effects where capital requirements do not directly address the potential release of tax provisions)

Consideration will be given to whether there is a need to extend or clarify the application of the requirements of ISAP 1 in paragraphs 2.7.7, 3.2.1 b and 3.2.2 d in this proposed ISAP to cover the uncertainties in insurance liability reserving.

4. __Principle of Subsidiarity__

The ASC considered whether the proposal for a model ISAP conflicts with the principle of subsidiarity and concluded that it did not. The ASC confirms its intent that the proposed ISAP is to comply with the principle of subsidiarity.