



AIA

Remarks on the Proposed IAIS ICS

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Topics



- Equivalence
- Discount rate
- Sovereign debt
- Prescribed stresses that vary by region
- Holding company senior debt

Equivalence (1 of 2)



- Capital regimes are being / have recently been upgraded across the Asia Pacific region. In each case, ICP's 14 (Valuation) and 17 (Capital) are either “Observed” or “Largely Observed” (or will be so after the changes under consideration).
 - China Risk Oriented Solvency Standard
 - Singapore RBC 2
 - Malaysia RBC
 - Thailand RBC 2
 - Hong Kong RBC Framework
 - Australia LAGIC
 - Philippines
 - Indonesia
- All of these regimes are designed by local regulators taking into account the particular circumstances of their jurisdictions. Compliance with the ICP's is, to a greater or lesser degree, an objective of all the regimes.

Equivalence (2 of 2)



- The local regimes protect policyholders at the legal entity level in the various jurisdictions.
- The local regimes apply to all insurers in the jurisdiction.
- Any ICS, applied at the local will either be stronger or weaker than the local standard:
 - To the extent it is stronger, it creates an non-level playing field
 - To the extent it is weaker, it is irrelevant
- The ICS should set out principles for when a local regime may be considered equivalent based on observance of ICP's 14 and 17.
 - If the IAIS feels this provides inadequate protection, the ICP's should be upgraded lest non-IAIG's be subject to inadequate supervision.

Discount Rate



- We favour a discount rate that:
 - Is stable at durations beyond the point of deep and liquid markets (last liquid point or LLP)
 - Recognizes the reality that insurers earn a spread over government / swap rates
- The approach of simply extending the current curve to tenors beyond the LLP provides misleading information. The value of liability cash flows beyond this point shouldn't change based on a change in unobservable rates.
- Companies earn a spread (after credit losses and investment management expenses) on their assets. This is true *regardless* of whether the assets are held to maturity or perfectly matched with the liabilities. Not to recognize this reality provides incentives to:
 - Raise the price of products to consumers
 - Withdraw products with long term guarantees and/or saving elements

Sovereign Debt

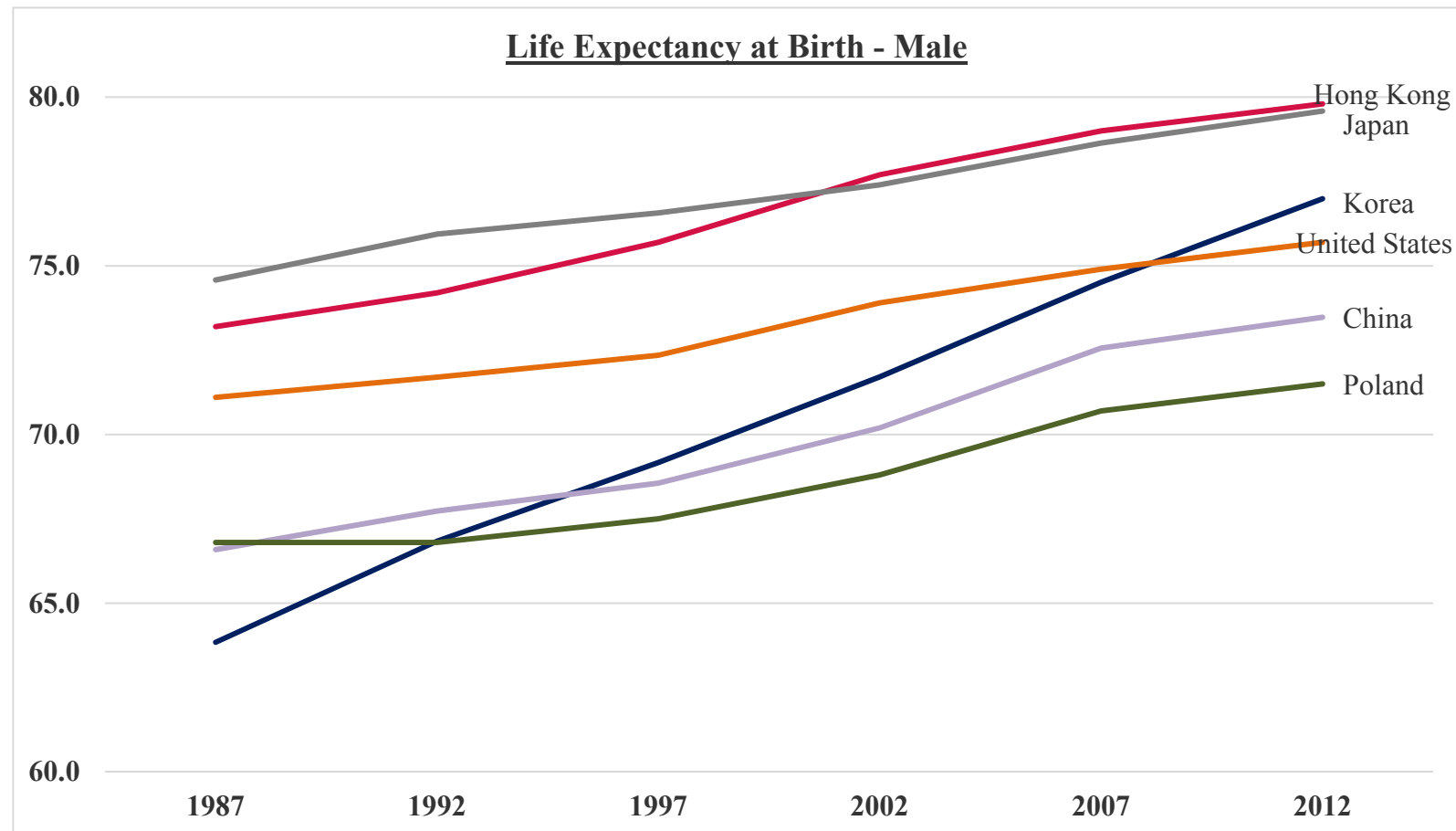


- In most developing economies sovereign debt denominated in the local currency is the most appropriate investment to back liabilities denominated in the same currency. It is the highest quality investment available in the local currency.
- Investment in foreign currency denominated assets of higher quality is NOT a solution.
 - Investment in foreign denominated assets may be restricted or prohibited.
 - Even if permitted, foreign investments introduce currency risk that is substantial. Currency hedges are typically short dated with uncertainty as to the cost at rollover.
- Introducing a credit risk charge for sovereign debt is a policy decision that
 - Makes insurance less affordable to people in emerging markets. Attempting to protect policyholders in extreme cases may prevent any protection at all!
 - Attempts to provide a higher level of security to insurance contract holders than the local government does to its sovereign debt holders. In many countries the social safety net is weak

Prescribed Stresses that Vary by Region



- The IAIS is considering varying risk charges for insurance risk by region.
- We believe that any differentiation by market needs to be based on scientific facts.



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Holding Company Senior Debt



- Senior debt at the holding company level is not a policyholder liability.
 - When proceeds are injected into a holding company, the result is a higher level of security for policyholders than if subordinated debt had been raised at the operating company level.
- A default will not impact the policyholders of any operating entity
- We believe senior debt should therefore not be considered a liability for the ICS.
- Functionally, from a group perspective, senior debt at the holding company level is equivalent to subordinated debt at the operating company level.