PCI Presentation on ICS 2.0/Activities-Based Approach

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Agenda

- Principles for Development of ICS 2.0
- Thoughts on the Kuala Lumpur Agreement
- Undecided Issues for ICS 2.0
- Serious Consideration of Aggregation Approach
- Initial Comments on Activities-Based Systemic Risk Approach

Principles for Development of ICS 2.0

- Should be transparent and tested from development through application
- Should be appropriate for the variety of insurance business models and jurisdictional approaches to solvency regulation worldwide
  - The simpler and more principles-based, the better
  - Should be a minimum standard that can be applied in a wide variety of jurisdictions
  - Based on audited financial statements with appropriate regulatory adjustments
- Group capital regimes that produce comparable outcomes in policyholder protection should be considered consistent with the ICS
  - Recognizing that capital is only one piece of group-wide supervision

Thoughts on Kuala Lumpur Agreement

- What justifies elevation of the MAV approach to "reference method" status?
  - Implicit assumption that MAV produces the correct result, despite lack of objective standard with which to compare it
  - 2018 MAV field testing must continue to test viable options for outstanding items, including liability discounting and capital resources
- As the KL agreement moves forward, clarification needed as to what basis will be used to evaluate models and GAAP Plus methods after the monitoring period ends
- Pleased that IAIS will consider aggregation approaches, but clarification regarding eventual evaluation is needed

Open Issues for ICS 2.0

- Capital Resources
  - Surplus Notes – should be included as Tier 1 capital
  - Senior Debt – if structurally subordinated, should be included as capital
  - Common Stock – should be included as capital regardless of whether supervisory approval for repurchases is required
- MOCE (Margin over Current Estimate) overstates economic liabilities
- 99.5% VaR/one year PCR level should be re-evaluated and reopened for comment
  - Level is too high for an appropriate PCR
  - Lack of appropriate diversification must be addressed

Aggregation Approach

- Based upon audited financial statements
- Based upon legal entity capital requirements in the U.S. that have stood the test of time
- Relatively easy to calculate and understand
- Need open and transparent consideration of how comparability will be determined
- Should be included in 2018 ICS field testing

Preliminary Thoughts about ABA

- PCI welcomes IAIS development of activities-based approach
- For insurance groups, activities-based approach is superior to entity-based approach
  - IOSCO has made the same recognition for asset managers
  - IAIS should seriously consider replacing the EBA with the ABA once it is sufficiently built out
- ABA should focus on activities with links to known systemic risk transmission channels
- PCI will have further comments as our members complete their review of the consultation draft

Questions?