

Update on 2019 Field Testing

10 April 2019

ICS Stakeholder Meeting, Orlando, Florida



Agenda

1. Update on decisions for 2019 Field Testing
2. Key Dates
3. Kuala Lumpur Agreement
4. ICS Monitoring Period
5. Q&A Session

UPDATE ON DECISIONS FOR 2019 FIELD TESTING

Purpose of the 2019 FT update section

- This section provides an overview of the changes or clarifications for 2019 Field Testing. As such, decisions made for 2019 Field Testing do not prejudice the decisions that will be made for ICS Version 2.0 for the monitoring period.
- This slide deck is for information purposes only. Full details and instructions will be provided in the Technical Specifications, which is the reference document for 2019 Field Testing.

General information

Please refer to the notice on slide 4

- Template will include a full ICS calculation on both a MAV and GAAP Plus basis
- As in 2018, there will be two calculations for capital resources, related to the presence of acceleration clauses that may be triggered in going concern.
- A single approach to the Margin Over Current Estimate (MOCE) will be included in 2019 Field Testing, not prejudging the decision for ICS Version 2.0 for the monitoring period. This single approach is the percentile-MOCE with no deduction from the capital requirement. Different calibrations of the percentile-MOCE will be tested (see slide on MOCE).
- Supervisory-owned and controlled credit assessment processes (SOCCA) (eg NAIC Designations) will be recognised in the calculation of ICS coverage ratios, this does not preclude how (i.e. national discretion in reference ICS or other method) these will be considered for ICS Version 2.0 for the monitoring period.

Market-adjusted valuation (MAV)

Three-Bucket Approach

- Focus on refining the Middle Bucket to address concerns that it is too restrictive
- Three MAV scenarios will be tested with a full ICS capital requirement calculation on the central scenario only
- An additional table will be provided for Volunteer Groups to report risk charges for those risks that change materially under the two additional scenarios
- Top Bucket: clarify criterion b that legal ring fencing is not required
- General Bucket: no changes

Main changes	Central Scenario	Additional 1	Additional 2
Middle Bucket criterion c – carry forward ratio	LOT/200 if LOT < 20; 10% otherwise	10%	LOT/200 if LOT < 20; 10% otherwise
Middle Bucket criterion c – widening of matching bands	5 years	3 years	5 years
Middle Bucket – spread by duration (where data allows)	Yes	No	Yes
Increased granularity for the real interest rate component of the LTFR	Yes	No	Yes
Spread over the LTFR	15 bps	5 bps	25 bps

Market-adjusted valuation

Three-Bucket Approach

- Similar to last year, the MAV scenarios will be complemented by additional calculations:
 - Balance sheet based on the risk free rate, but not a full ICS calculation, to inform future refinements to the Three-Bucket Approach
 - Stressed economic conditions balance sheet
- To assess the impact of potential further refinements to the Middle Bucket qualifying criteria ahead of November's decision, the IAIS will also collect information through an **additional table**
- Revised scenario for the stressed balance sheet based on feedback from Volunteer Groups
 - Anchor the stress to a specific historical scenario (eg Financial Crisis, European Sovereign Debt Crisis)
 - Reflect economic realities
 - Single stressed scenario with three components:
 1. Increased spreads
 2. Downward parallel interest rate shift
 3. Increase in credit defaults

Market-adjusted valuation

Other refinements

- **LTFR** - Introduction of an intermediate classification (“Other Developed”) for the real interest rate component of the long-term forward rate (in addition to the Developed and Emerging Markets classifications included in 2018 Field Testing)
- **Expenses** - Clarification on the treatment of expenses in the current estimate
- **Premium Receivables** - Clarification on the treatment of premium receivables

GAAP Plus

- **Japanese GAAP:** Technical Specifications consistent with 2018 Field Testing. Japanese Volunteer Groups reporting IFRS will follow the IFRS GAAP Plus approach.
- **U.S. GAAP:** Testing a GAAP Plus method for the U.S. that incorporates new U.S. GAAP rules.
- **IFRS:** New 2019 Field Testing Technical Specifications for IFRS GAAP Plus. EU Volunteer Groups will continue to provide adjusted Solvency II balance sheet under GAAP Plus.
- **Chinese C-ROSS:** New 2019 GAAP Plus Field Testing Technical Specifications for Volunteer Groups reporting Chinese C-ROSS.

MOCE

Approach for 2019 Field Testing

- The single approach to MOCE included in 2019 Field Testing is the Percentile-MOCE with no deduction from the capital requirement
- The inclusion of the Percentile-MOCE in 2019 Field Testing does not prejudice its inclusion in ICS Version 2.0, nor does it mean that the C-MOCE (without deduction from the capital requirement) and the P-MOCE (with deduction from the capital requirement) are no longer under consideration
- Data for C-MOCE and P-MOCE will not be collected again in 2019 Field Testing to minimise burden on Volunteer Groups

MOCE

2018 FT vs 2019 FT

Two families of approaches to MOCE tested in 2018 FT			Single approach to MOCE for 2019 FT								
Cost of Capital MOCE (C-MOCE)	Prudence MOCE (P-MOCE)	C-MOCE (default MOCE for 2018 FT)	Percentile-MOCE								
Variable cost of capital rate	n/a	Fixed cost of capital rate (5%)	Three calibrations of the percentile-MOCE with no deduction from the capital requirement will be tested: <table><tr><th>Life</th><th>Non-Life</th></tr><tr><td>75%</td><td>60%</td></tr><tr><td>80%</td><td>65%</td></tr><tr><td>85%</td><td>70%</td></tr></table> No single calibration defined as the default or baseline	Life	Non-Life	75%	60%	80%	65%	85%	70%
Life	Non-Life										
75%	60%										
80%	65%										
85%	70%										
No deduction from capital requirement	Full deduction from capital requirement	No deduction from capital requirement	No deduction from capital requirement								

Market risks

Interest rate risk (IRR)

- The aggregation of IRR across currencies is refined for 2019 Field Testing in order to appropriately calculate the risk charge when individual currency portfolios are non-linear

Equity risk

- Equity volatility stress was revised to address feedback from consultation document and field testing results to raise the short-term, and lower the long-term implied volatility.
- Additional data is requested to run the level and volatility shocks separately and together.

Currency risk

- The pair-wise Currency risk stresses have been recalibrated based on 20 years of data (as the Euro was introduced 20 years ago).

Market risks

Non-default spread risk

- The results of 2018 Field Testing indicated that there were inconsistencies between currencies, in particular for the up shock. This was driven by the relative limit. The impact of NDSR was much higher for currencies with high spreads, compared to currencies with low spreads
- A revised design and calibration will be included in 2019 Field Testing
- The revised design and calibration attempt to resolve the inconsistencies by removing the relative limit on the up shock and halving the magnitude of the shock
- The inclusion of NDSR in 2019 Field Testing does not prejudge its inclusion on ICS Version 2.0

Other clarifications or changes

Capital resources

- Criteria for the recognition of structurally subordinated capital instruments have been clarified
- Certain issues will be resolved during the monitoring period, in particular:
 - Potential requirements relating to Principal Loss Absorbency Mechanisms (PLAM)
 - Issues relating to availability / fungibility of capital resources within a group

Risk mitigation

- The renewal cap will not apply if an IAIG is able to demonstrate to the satisfaction of its group-wide supervisor that certain conditions are met

Management actions

- The cap applied to management actions has been refined in order to address discounting discrepancies under some risk modules

Other clarifications or changes

Life risks

- Following the data collection run in 2018, the calibration of some Life risks (namely Mortality, Lapse and Morbidity/Disability) has been reduced for business written in Japan
- The data collection exercise will be run again in 2019, and the calibration may be further reviewed as a result

Non-Life risk

- A factor based approach is used for insurance liabilities. Catastrophe risk is based on insurer models
- Revised calibration for a limited number of lines of business.
- Introduction of correlations within ICS segments
- Exposures for non-life claims reserves for U.S. GAAP Plus will be adjusted to address undiscounted liability exposures

Other clarifications or changes

Credit risk

- Haircut approach will be used to determine Credit risk for collateralised non-life reinsurance exposures
- Granular information collected on agent/broker's balances and commercial mortgage loan portfolios of Volunteer Groups
 - Information will be used to review the current Credit risk factors for these items

Asset concentration risk

- A granularity adjustment will be incorporated to calculate the Asset Concentration risk charge.
 - a granularity adjustment links the calculation to the level of Credit risk underlying the investments
- Continue to collect data on the approach from 2018 Field Testing
- If field testing results shows that the granularity adjustment is volatile and not credible, then the 2018 Field Testing approach could still be used for the monitoring period

Other clarifications or changes

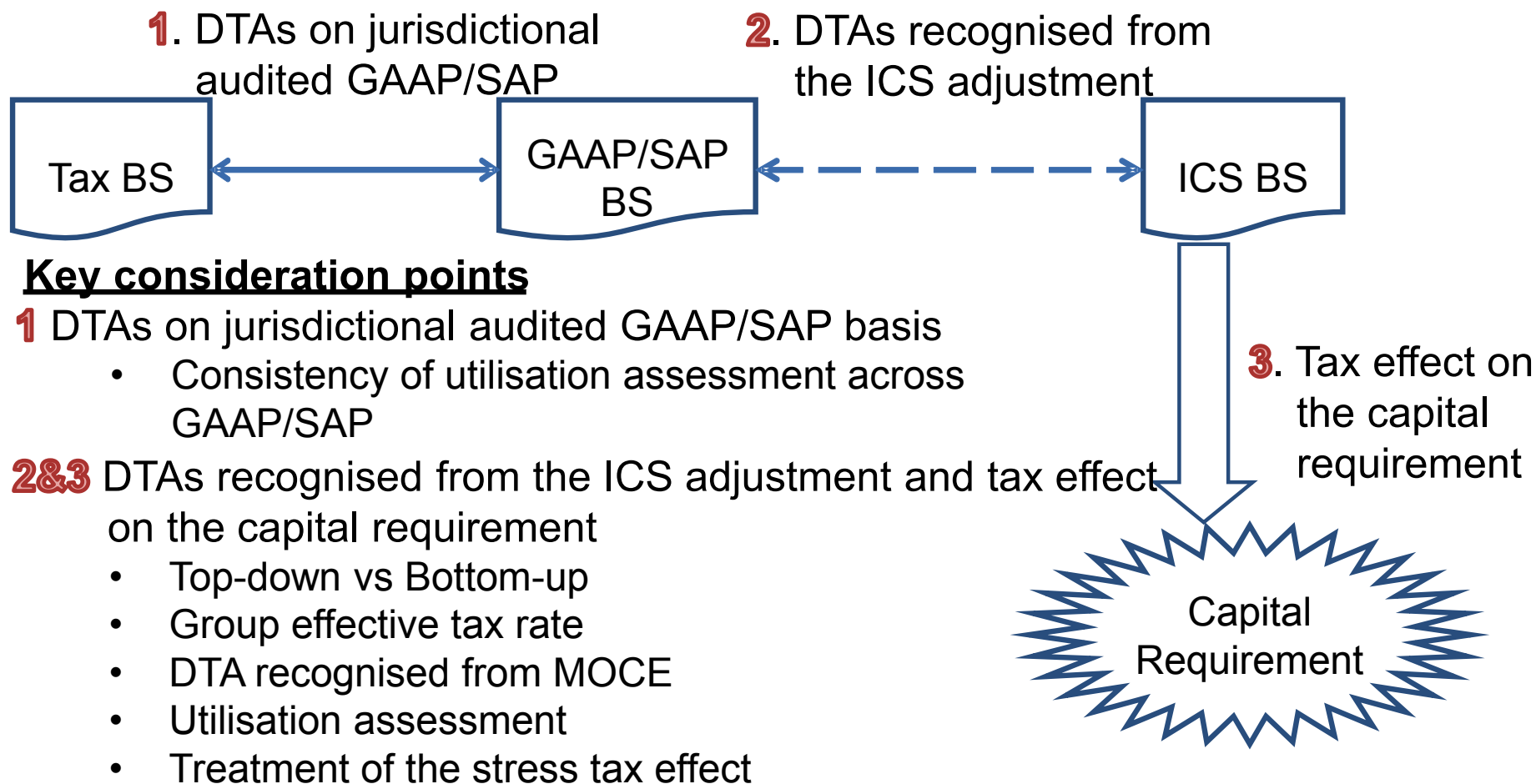
Operational risk

- The Life (Risk) factor applied to liabilities will increase from 0.4% to 0.45% and the Life (Non-Risk) factor will decrease from 0.45% to 0.4% to better reflect expected risk of the exposures

Internal Models

- Continue to collect Baseline Supplementary Internal Model data
- Dry run (pilot) of the Internal Models Self-Assessment Template
 - Volunteer Groups will assess their compliance with the pre-requisites for reporting Internal Model results during the monitoring period
 - Feedback from Volunteer Groups will be used to refine the Self-Assessment Template for the monitoring period

Overview of tax treatment in the ICS



Summary of Tax Treatment for 2019 Field Testing

Item	FT2018 approach	Refine	Refined FT2019 approach
DTAs on jurisdictional audited GAAP/SAP basis	Use DTAs on jurisdictional audited GAAP/SAP basis for ICS BS	Partially	Keep the FT2018 approach, but allow USSAP volunteers to use USGAAP DTA for the ICS BS.
Top-down vs Bottom-up approach	Use Top-down approach	No	-
Group effective tax rate	Use jurisdictional audited GAAP consolidated financial statements	Yes	Use weighted average statutory effective tax rate, weighted using the three year average of GAAP earnings before tax on a sub-group/entity level basis.
DTA recognised from MOCE	DTA on MOCE was not recognised.	Yes	Considering impact of DTA recognised from MOCE subject to whether MOCE is determined to be a temporary or permanent difference for assessment purposes. A midpoint is used for FT2019.
Utilisation assessment of DTA on ICS BS	Cap by DTL on ICS BS	No	-
Utilisation assessment of tax effect on capital requirement	Cap by DTL on ICS BS	Yes	Incorporate tax loss carry backs, and future taxable income projections stemming from insurance business for the utilisation assessment, while applying DTL limitations.
Treatment of DTA on ICS BS as capital resource	Classify net DTA on ICS BS as tier 2 basket item	No	-
Treatment of tax effect on the capital requirement	Net the tax effect on the capital requirement with the capital requirement	No	-

2019 Key Dates

- Launch of 2019 Field Testing: 30 April
- IAIS Global Seminar: 13-14 June
- Data Due: 31 July
- Public release of 2019 Field Testing Package: August
- Adoption of ICS Version 2.0 for the monitoring period: 11-14 November (IAIS Parent Committee Meetings and AGM)

KUALA LUMPUR AGREEMENT

Kuala Lumpur Agreement

November 2017

- Implementation of ICS Version 2.0 will be conducted in two phases:
 - A five-year “monitoring period”, during which ICS Version 2.0 will be used for confidential reporting to the group-wide supervisors (GWS) and discussion in supervisory colleges.
 - The “implementation of the ICS as a group-wide PCR”.
- Implementation of ICS Version 2.0 will have two equally important components:
 - Mandatory* confidential reporting by all IAIGs of a reference ICS; and
 - Additional reporting, at the option of the GWS, of ICS based on GAAP Plus valuation and/or other methods of calculation of the ICS capital requirement.

* During the monitoring period, each group-wide supervisor will need to ensure the reporting of the reference ICS.

Kuala Lumpur Agreement

November 2017

- During the monitoring period, ICS will not be used as a prescribed capital requirement (PCR) (ie the ICS results will not be used as a basis to trigger supervisory action). This will allow GWSs and host supervisors to discuss and assess the ICS in comparison with existing group capital standards or calculations that are in development. The monitoring period will last for five years starting from 2020
- Once implemented as a PCR at the end of the monitoring period, ICS Version 2.0 will be a measure of capital adequacy for IAIGs. It will constitute the minimum standard to be achieved and one which the supervisors represented in the IAIS will implement or propose to implement taking into account specific market circumstances in their respective jurisdictions.

Kuala Lumpur Agreement

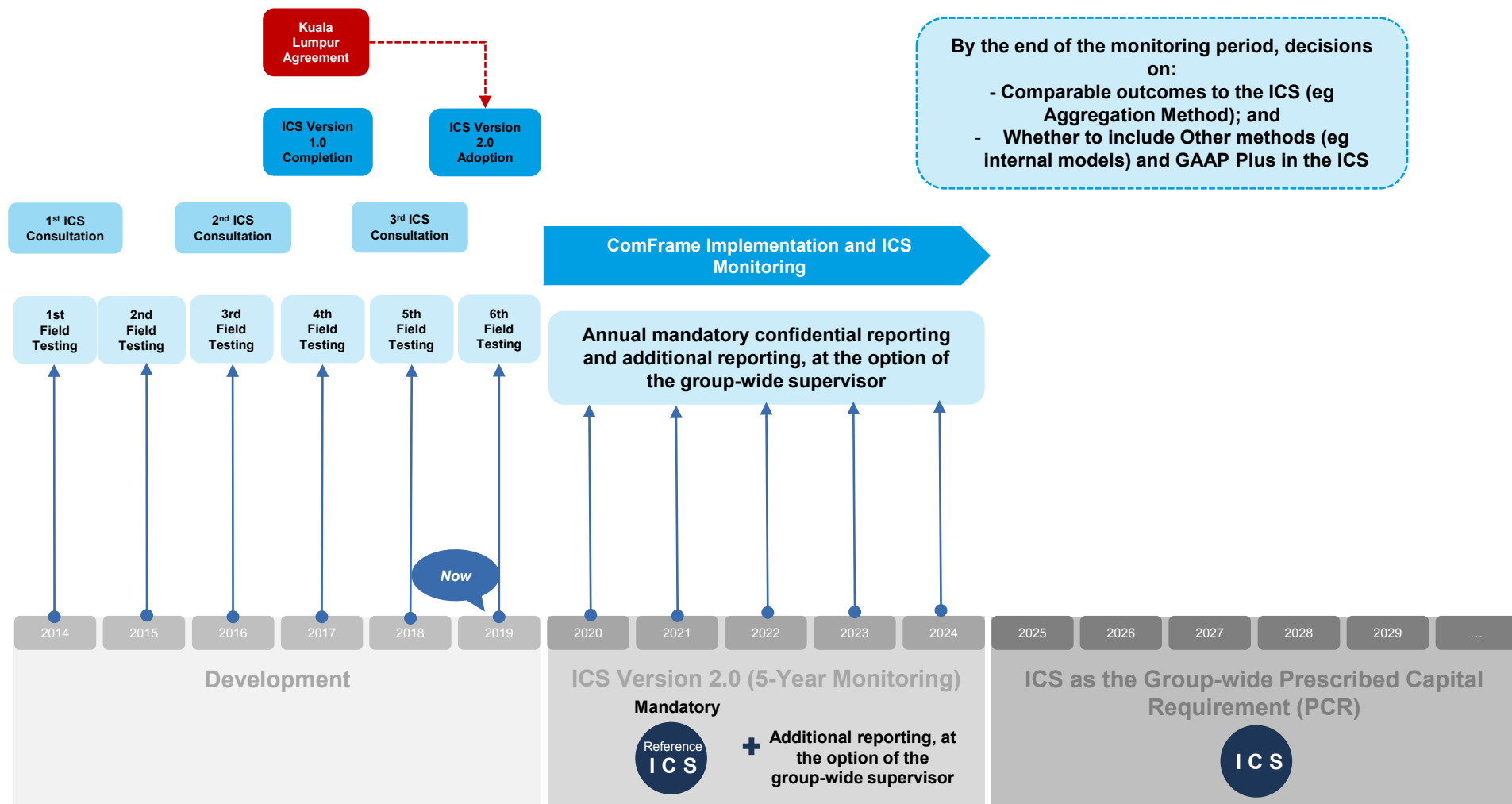
November 2017

- The Kuala Lumpur Agreement acknowledged the development of the Aggregation Method within the United States. The Kuala Lumpur Agreement states that, *“The IAIS has agreed to collect data from interested jurisdictions relevant to the development of the aggregation method. Although this is not part of ICS Version 2.0, the IAIS appreciates the significance of this development, and so it will collect data from interested jurisdictions that will aid in the development of the aggregation method. Through this approach, the IAIS aims to be in a position by the end of the monitoring period to assess whether the aggregation method provides comparable, ie substantially the same (in the sense of the ultimate goal), outcomes to the ICS. If so, it will be considered an outcome-equivalent approach for implementation of ICS as a PCR.”*

ICS MONITORING PERIOD

ICS Monitoring Period

ICS Timeline: Big Picture



Monitoring Period

Possible changes during the monitoring period

- Feedback received on the consultation document indicates concerns that the ICS specifications may not change or evolve during the monitoring period based on the outcome of the data collection
- During the field testing period, changes were made each year and in some cases various options were tested. The monitoring period is intended to be a period of relative stability for the reference ICS and the additional reporting
- However, this **does not preclude** possible clarifications/refinements and correction of major flaws or unintended consequences identified during the monitoring period to improve the ongoing development of the ICS

Monitoring Period

Confidentiality

- Feedback on the ICS Version 2.0 consultation documents indicates that stakeholders have concerns regarding:
 - Confidentiality of the data collection process during the monitoring period and the potential use of the confidential reporting by non-capital related IAIS working groups
 - The information supervisory colleges will receive (eg will colleges receive results regarding other IAIGs?). Some stated that access to results should be limited to the home supervisor rather than the supervisory college.
 - Public release of results by competitors (forcing others to disclose)
 - External pressures (rating agencies and analysts) to release results
- Throughout the Field Testing exercises, the IAIS has applied the highest standards to ensure the confidentiality of all collected data and will continue to do so in line with its commitment for confidentiality during the monitoring period
- The IAIS has engaged with relevant parties to assess the concerns expressed and will develop supplemental confidential safeguards as needed

Monitoring Period

Stakeholder engagement

- Per the IAIS Stakeholder Engagement Plan, “Effective stakeholder engagement should ensure that stakeholders are properly consulted in the development of IAIS policy and that the opportunity for timely, substantive and high quality contributions from stakeholders is maximised”
- The IAIS is committed to maintain the same level of engagement with stakeholders during the monitoring period
- The timing of stakeholder events will be influenced by the timeline used by IAIS to gather both qualitative and quantitative feedback, which is still under discussion.
- Further details on the monitoring period are expected to be presented at the IAIS Global Seminar, 13-14 June

Q&A SESSION
