

7.19 Operational risk

Q146 Section 7.19 Are the proposed Operational risk exposures appropriate for ICS Version 2.0? Please explain. If “no”, please provide specific suggestions for alternatives and the practicality of their application in a standard method.

Organisation	Jurisdiction	Confidential	Answer	Answer Comments
CLHIA	Canada	No	No	The exposures may be appropriate but the risk charges, particularly the risk charge of 4% applied to Life operations, is excessive. As a comparison, the similar risk charge used for Canadian regulatory capital regime LICAT (calibrated to a CTE level of 99% over a one-year time horizon including a terminal provision) is 2.5%.
China Banking and Insurance Regulatory Commission (CBIRC)	China	No	No	ICS charges operational risks for premium growth over 20% per year. We view that this is not reasonable for emerging market. A high growth in developed market may often represent aggressive business behaviors of the individual firm, which can generate high operational and management risks for the firm. But for emerging market, a 20% growth can often be an average growth of the insurance industry, and the rapid growth of the industry is mostly due to the low starting basis, the economic development of the country or an increase of insurance awareness of the general population. The growth is not firm-specific and may not directly link to operation risks. We suggest that the premium growth threshold be set considering the average premium growth of the market, and the charge should be applied to firms that grow too fast compared to the market average.
European Insurance and Occupational Pensions Authority (EIOPA)	EIOPA	No	No	EIOPA would prefer a more accurate exposure for premiums such as earned premiums – therefore reflecting the effective date and term to which the premium applies.

				This shall be gross, without deduction of premiums for reinsurance contracts. This is because the process of reinsurance gives rise to additional operational risk (e.g. legal risks).
Allianz	Germany	No	No	The calibration appears extremely conservative. In general factor-based approaches based on accounting information do not show sufficient risk sensitivity for operational risk since a change of the exposure size does not automatically lead to an increase of the underlying risk. A risk sensitive measure that considers operational risk losses should be used to calibrate operational risk.
Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)	Germany - BAFIN	No	No	We would prefer a more accurate exposure for premiums such as earned premiums – therefore reflecting the effective date and term to which the premium applies. This shall be gross, without deduction of premiums for reinsurance contracts. This is because the process of reinsurance gives rise to additional operational risk (e.g. legal risks).
International Actuarial Association	International	No	No	The Insurance Regulation Committee of the IAA believes that the results in paragraph 468 (second bullet) are counterintuitive. Operational risk is the potential for significant losses due to a failure of a process. The principal processes for non-life are generally pricing/underwriting and claim handling. We would have expected failures in these two areas to show up in the data used to parameterize the Pricing and Claims Reserving risks, hence we would have expected operational risk from the predominant processes for non-life insurers to already be included in the ICS before the calculation of a separate Operational Risk charge. Can the IAIS explain what types of operational risk are contributing most to this counterintuitive result? If a factor-based approach is retained then we suggest changing the exposure base for non-life to a size indicator that would be less likely to double-count the risk of operational failures in pricing/underwriting and claim operations. One alternative exposure basis for operational risk might be expense levels excluding commissions and claim adjustment expenses. In any event, some would expect it may be a more appropriate operational risk charge to produce a lower charge for non-life than for life (due to the reflection of operation failures in the data used to parameterize the premium and claims reserve risk charges). But, more importantly, operational risk rises to the level of a solvency concern only to the extent of a control weakness. Process failures are inevitable to some extent, but what



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				prevents them from becoming material solvency events is a sufficiently strong control structure. Basing the charge for this risk based solely on exposure measures, with no reflection of the control structure, is a weakness of the current design. Such an approach, while not yet widespread, has already been implemented in Bermuda and China and is described in Chapter 4 of the IAA Risk Book.
General Insurance Association of Japan	Japan	No	No	Reflecting the different characteristics of the insurance business, underlying operational risk differs significantly. Therefore, applying merely their size as exposure may not necessarily be appropriate. Considering that the underwriting of risk is the source of return, risk quantified (required capital) that takes due account of underlying operational risks could be regarded as exposure. Also, when using premiums as exposure, the current practice to apply written premium will be affected by the method of payment. Therefore, earned premium or annualized premium income of policies in force is more appropriate.
Financial Supervisory Service (FSS) & Financial Services Commission (FSC)	Korea (Republic of)	No	Yes	
Aegon NV	The Netherlands	No	No	We do not believe using the insurance liability is the most appropriate driver for operational risk, especially for unit-linked or separate account business. Instead, we believe that (maintenance) expense is a better driver for this risk.
Legal & General	UK	No	No	We do not believe that determining operational risk capital using a "Percentage of Current Estimate" approach is appropriate for ICS Version 2.0 because it is an overly simplistic methodology that provides no real link to the risk exposures being run by an IAIG. We propose that the ICS approach to operational risk capital is changed to a composite approach, as set out in the steps below: i. Where an IAIG already has an approved Internal Model for operational risk it would seem logical to require this to be used for ICS, particularly where output from that model is used (in some cases (e.g. the Solvency II Use Test) local regulatory compliance will be require it to be used) in running the IAIG's business and/or assessing local capital requirements;

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			ii. Where point (i) does not apply, Percentage of Current Estimate could be retained as the default option (appropriately calibrated), but with caps and floors based on one of the other formulaic options (discussed further down our response to this question) to prevent extreme and unintuitive results being generated in certain situations. Given that it is already available, we would suggest Percentage of ICS Required Capital on other risks (already aggregated up to the level of total SCR excluding operational risk and tax) would be the most suitable method for setting the caps and floors. We would recommend a lower limit of 5% and an upper limit of 10% based on the average operational risk proportion of 7.3% from the 2017 field testing quoted in the consultation document. This combines simplicity of approach with an allowance for differences in the risk profiles and business models of different IAIGs. iii. We believe that ICS 2.0 should include sufficient flexibility to allow an IAIG to override the formulaic output of point (ii) with an alternative calculation if it can demonstrate to its local supervisor that this would give a materially more appropriate result and is subject to appropriate governance. This could be any one of options (b), (c) or (e) in the list further down our response to this question, or several in combination; iv. Beyond this, in certain situations it should be allowable for an IAIG to agree with the supervisor that a new Internal Model should be developed where the IAIG can demonstrate that none of the formulaic approaches in the table above would represent their operational risk exposures in a materially accurate manner. We have developed this proposal following a process whereby we have identified five possible alternative methodology options to calculate operational risk capital and considered them against each other as well as the existing methodology from 2018 field testing (designated (f) in the list below): a) Internal Model (appropriately calibrated and governed) b) Multiplier of Operational Risk Losses over recent years, potentially including some allowance for trend c) Percentage of Expense Level d) Percentage of ICS Required Capital on other risks
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			e) Multiple of Number of Contracts sold/in back book f) Percentage of Current Estimate (best estimate liabilities less reinsurance assets) We have considered, but have excluded, the following alternatives: • Percentage of Profit/Turnover, due to the inherent difficulty in calibrating this meaningfully across all IAIGs. • Multiple of Number of Employees, as gathering this information for IAIGs is likely to require disproportionate effort. However, we would expect that both of these factors would be available to IAIGs to use as part of an Internal Model if they so desired. We have identified a number of key considerations for any method to be chosen, and assessed each of the six options above against each consideration. The considerations are as follows (in broad order of importance): • The capital for operational risk should provide a materially accurate representation of the actual operational risk exposure for an IAIG • The operational risk capital framework should offer incentives to an IAIG to improve both its risk management and risk measurement processes • The operational risk capital methodology should produce sensible and meaningful output in all circumstances • The operational risk capital methodology should provide a level playing field between types of IAIGs and not unfairly penalise certain types of IAIG or business lines. This level playing field would be between IAIGs, and with firms outside the scope of ICS • The operational risk capital methodology should transparent and not disproportionately
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			complex to use and understand for all stakeholders, including regulators. The summary below summarises how we have assessed each option against each consideration (where "Y" represents positive features and "N" represents negative). Some of these are subjective judgements, but all should be broadly indicative. These ratings are justified in more detail (for each consideration in turn) later in this response (below the subheadings). a) Internal Model Reflects actual exposure: YYY Incentive for improvement: YYY Sensible in all circumstances: YYY Level playing field: Y Simplicity: Y b) Multiplier of Past Losses Reflects actual exposure: YY Incentive for improvement: YY Sensible in all circumstances: NN Level playing field: YY Simplicity: YY c) Percentage of Expense Reflects actual exposure: Y Incentive for improvement: NNN Sensible in all circumstances: YY Level playing field: YY Simplicity: YY d) Percentage of ICS Required Capital Reflects actual exposure: Y Incentive for improvement: NNN
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				Sensible in all circumstances: Y Level playing field: YY Simplicity: YYY e) Multiple of Number of Contracts Reflects actual exposure: N Incentive for improvement: NNN Sensible in all circumstances: Y Level playing field: YY Simplicity: YY f) Percentage of Current Estimate Reflects actual exposure: NNN Incentive for improvement: NNN Sensible in all circumstances: NNN Level playing field: N Simplicity: YYY In summary, there is no single option that provides a good outcome against all criteria. Internal Models score strongly in several important columns but have drawbacks in terms of the effort required to set up and manage them (for those IAIGs that do not already have one). The weakest option appears to be the current Percentage of Current Estimate approach, which we consider overly simplistic for the importance and materiality of this risk. We expect that, in aggregate, IAIGs' operational risk is likely to be one of the most material risks and yet the ICS model for operational risk is much cruder than that for other risks that we expect will be less material. Below we give further detail on each of these criteria to give some context to the rating that we have chosen. Reflects actual exposure to operational risk
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				An Internal Model performs best here as it allows an IAIG to tailor capital to the risks that it is running at a given valuation date. Operational risk exposure depends on a number of factors (company culture, complexity of product design, control environment and risk mitigations, legacy systems, external market) that are not easily quantified and used in a formula. Indeed some operational risks do not relate directly to the insurance business written, making current estimate a particularly poor choice of risk driver. The only other option with a direct link to actual operational risk exposures is a Multiple of Past Operational Risk Losses, which means that companies that incur relatively high operational risk losses will tend to hold higher capital against that risk. Percentage of Expense has some logical support since operational risk losses are often associated with the kinds of activity that generate expense outgo in “normal” years (i.e. years without significant operational risk loss). Percentage of ICS Required Capital provides some link to the general riskiness of an IAIG by looking at magnitude of exposure to other risks, although this may not be a good proxy to exposure specifically of operational risk. Of the remaining options, Multiple of Number of Contracts is considered preferable to Percentage of Current Estimate as many of the key operational risks are run on a per contract rather than per unit of current estimate basis. However, this may be harder to calibrate than some of the other options. Incentive for improve management of risk/other links to actual risk An Internal Model and Multiple of Past Operational Risk Losses are the only options that provide an incentive to IAIGs to improve their control framework and mitigation of operational risk as this would (assuming that the reduction in riskiness can be evidenced within an Internal Model) have a beneficial impact on the capital position. An Internal Model allows a more forward-looking assessment to reflect improved controls sooner, but a Multiple of Past Operational Risk Losses arguably requires the actual delivery (rather than expected delivery) of improvements. Our experience with Solvency II Internal Models is that development of an operational risk capital framework can provide an opportunity to greatly improve the transparency and awareness of key operational risks across an organisation. The other four options ((c) to (f)) provide no incentive for IAIGs to improve operational risk
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				processes as the capital requirement would not change no matter how robust or comprehensive the underlying control framework is, or how extensively improvements are embedded or actual risks mitigated. Generates sensible results in all circumstances The calibration of each option will be a key determinant of whether it produces sensible results, but for some of the options it is highly unlikely that a single calibration can give sensible capital for all participants. An Internal Model should give sensible output in the widest range of circumstances, assuming that appropriate validation and controls are put in place around the operation of the Internal Model. A Multiple of Past Operational Risk Losses may give volatile results, particularly in the years following a large operational risk event. This may reinforce the impact of a significant operational risk event on the regulatory surplus as the capital required increases at the same time as the company is suffering the loss, which is not ideal. In addition, it could be argued that a large operational risk event makes a further operational risk event less likely in its immediate aftermath as the loss will cause controls to be strengthened. Percentage of Expense should provide sensible results in a reasonably broad range of situations, unless a company has a significant proportion of expenses relating to activity that is not associated with significant operational risk exposure. This appears less likely than the circumstances leading to an inappropriate result under some of the other approaches. Percentage of Current Estimate is unlikely to give sensible output in any circumstances. For example: • Certain products where future premiums exceed future benefits may have a negative BEL and would therefore generate negative operational risk capital, which is unlikely to be appropriate. • More generally, a single premium version of a contract is likely to have significantly higher BEL than a regular premium version even though the only difference (the need to collect premiums on an ongoing basis) is relatively minor in terms of operational risk exposure
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			• Current estimates will vary depending on a number of factors that would not be expected to materially impact upon operational risk exposure, such as discount rate (including allocation of liabilities between buckets), best estimate demographic assumptions, and assumed contract boundaries • This does not reflect the riskiness of the business underlying the current estimate. For example, for business where an IAIG is managing a large volume of assets for a small number of institutional clients it does not appear likely the same multiple would apply as for an IAIG transacting a large number of small-value contracts with members of the public, due to the relative lack of conduct-related issues on the former. Recent experience of large-scale operational risk losses (i.e. PPI and mortgage endowments in the UK) is very much skewed toward conduct risk issues. Percentage of ICS Required Capital may tend to give output that is broadly comparable to the general level of riskiness of the business of an IAIG. It will be driven many of the same factors as Percentage of Current Estimate that would not be expected to materially impact upon operational risk exposure, but it should address the other shortcomings listed above. Multiple of Number of Contracts addresses many of the shortcomings of Percentage of Current Estimate but may still give unintuitive output in certain cases if a single multiplier is used for all business types. Level playing field/comparability between IAIGs One shortcoming of an Internal Model is that it is not always straightforward to compare exposures between IAIGs, although a robust approvals process will mitigate this to some degree. Additionally, it is possible to specify a common granularity of operational risks to be calibrated which would allow direct comparison between IAIGs for certain operational risks of interest (i.e. cyber risk). For some of the formulaic options (i.e. those other than Internal Model) the variables in the formula would need to be defined precisely to ensure consistency (and therefore a level playing field) between IAIGs. In particular Multiple of Past Operational Risk Losses and Percentage of Expense may not be completely comparable as “operational risk loss” and “expense” are not necessarily uniquely defined between IAIGs. Indeed even Multiple of Number of Contracts may not be completely unambiguous in terms of what constitutes a
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			single contract. However, it should be possible to put guidelines in place to mitigate this to some extent. There may be optionality around the contract boundary on which the current estimate for Percentage of Current Estimate is calculated. Percentage of ICS Required Capital and Percentage of Current Estimate are easy to specify in a way that is comparable between IAIGs as it uses information that is already clearly and unambiguously defined in the technical specifications. However neither of these options provides IAIS with any additional information about how an IAIG is exposed to operational risks. All of options other than an Internal Model are approximations of true operational risk exposure to some extent, and so there will be winners and losers between IAIGs depending on whether the approximation tends to overstate or understate potential loss. In some cases this mis-estimation could be material. In extreme cases (i.e. an IAIG with very large current estimate of low-risk and well-controlled business) this lack of comparability may lead to IAIGs exiting markets or being uncompetitive, particularly where the approximate treatment of operational risk gives materially different answers to local competitors outside the scope of ICS. Simplicity Percentage of ICS Required Capital and Percentage of Current Estimate are very simple to apply as they can be derived from data that is already collected as part of ICS field testing, and that would continue to be required going forwards to assess capital adequacy on an ICS basis. Multiple of Past Operational Risk Losses, Percentage of Expense and Multiple of Number of Contracts would all be reasonably simple once a clear definition had been set out and the company had set out processes to gather the information required. The data for number of contracts is likely to be available without significant additional overhead, and it is likely that most companies within the scope of ICS will already gather information on expenses that can be used for Percentage of Expense. Whilst some companies may not collect the data on past operational risk losses it is arguable that the incentive to do is one of the main benefits of this alternative. An Internal Model is unlikely to be available across all IAIGs and in some cases would need to be developed from scratch. The cost of doing so is one of the main downsides of this
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				option, albeit that we believe that there are benefits of this development aside from the ability to calculate capital. Other IAIGs, particularly those with a Solvency II Internal Model, will already have this option available. For an IAIG where operational risk is immaterial they could develop a simple Internal Model that reflected the disproportionality of a more detailed assessment.
National Association of Mutual Insurance Companies	United States	No	No	Operational risk and all other risks and their factors should be determined by the local jurisdictional supervisor. NAMIC disagrees with the mandate of a standard method, the 99.5% VaR calibration level and the IAIS dictating the factors to be used in the formula. Jurisdictional flexibility is the appropriate way to capture these risks with mutual recognition and shared understanding of the jurisdictional approach at supervisory colleges. The ICS is not yet fit for purpose. Significant additional work is needed to achieve an appropriate global capital standard and it may be completely unachievable.
RAA	United States and many other jurisdictions	No	No	Given that the measurement of operational risk is highly subjective, we prefer a simple capital add on requirement based on a percentage of the capital requirement.
American Academy of Actuaries	United States of America	No	No	The results in paragraph 468 (second bullet) are counterintuitive. Operational risk is the potential for losses due to failures of a process. The principal processes for non-life are generally pricing/underwriting and claim handling. Failures in these two areas show up in the data used to parameterize the Pricing and Claims Reserving risks, hence operational risk from the predominate processes for non-life insurers are already included in the ICS before the calculation of a separate Operational risk charge. In contrast, the data used to parameterize the major risk charges for life insurance generally comes from financial markets, i.e., it does not include actual experience from the major operations of life insurers. This would mean that the need for a separate Operational risk charge would be greater for life insurers than for non-life insurers. The fact that field test results have produced the opposite (see paragraph 468) implies a flaw in the design of this charge. If a factor-based approach is retained then we suggest changing the exposure base for non-

				life to a size indicator that would be less likely to double-count the risk of operational failures in pricing/underwriting and claim operations. One alternative exposure basis for operational risk might be expense levels excluding commissions and claim adjustment expenses. In any event, we would expect a more appropriate Operational risk charge to produce a lower charge for non-life than for life (due to the reflection of operation failures in the data used to parameterize the premium and Claims Reserve risk charges). We also note that Operational risk rises to the level of a solvency concern only to the extent of a control weakness. Process failures are inevitable to some extent, but what prevents them from becoming material solvency events is a sufficiently strong control structure. Basing the charge for this risk based solely on exposure measures, with no reflection of the control structure, is a weakness of the current design.
MetLife, Inc	USA	No	No	We believe the factors applied to gross written premium/gross current estimates of insurance liabilities result in an operational risk charge that is in excess of the targeted calibration of 99.5% confidence level. We do not feel that the application of an additional growth charge is fully appropriate. Well established lines of business that have strong internal controls in place within their processes are not more likely to have higher operational risk driven by increased growth. The current methodology applies an additional capital charge due to growth above the specified threshold on a blanket basis. The ICS framework for Operational Risk continues to consider Operational risk across regions as fully correlated – meaning when an Operational risk event or loss occurs in one country or region, it also occurs in all the others. This is not consistent with best practices.
Property Casualty Insurers Association of America (PCI)	USA	No	No	PCI's yes or no response was simply required in order to open the text box and file comments. We believe this question to be best addressed by field test volunteers who have the ability to do so with the benefit of actual data for support and context. The absence of a response by PCI should not be taken one way or the other with respect to the subject of the question.
National Association of Insurance Commissioners (NAIC)	USA, NAIC	No	No	No. It would be more appropriate to base Op Risk on a percentage of the capital requirement.

Q147 Section 7.19 Should the IAIS introduce changes to the design of the Operational risk charge to address these issues? Please provide sufficient detail and rationale.

Organisation	Jurisdiction	Confidential	Answer	Answer Comments
China Banking and Insurance Regulatory Commission (CBIRC)	China	No	Yes	Please refer to Q146.
European Insurance and Occupational Pensions Authority (EIOPA)	EIOPA	No	Yes	EIOPA would prefer a more accurate exposure be reflected such as gross earned premiums.
Insurance Europe	Europe	No	Yes	Insurance Europe supports further investigation into the issues raised by the IAIS. In particular, the alignment of the operational risk charge with the most reflective exposure base for each class of business.
Allianz	Germany	No	Yes	A calibration of a risk-sensitive risk measure should be based on information from loss databases.
German Insurance Association	Germany	No	Yes	Calibration appears extremely conservative. In general factor based approaches based on accounting information do not show sufficient risk sensitivity for operational risk since a change of the exposure size does not automatically lead to an increase of the underlying risk. A risk sensitive measure that considers operational risk losses should be used to calibrate operational risk, like for example a scenario-based approach.

Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)	Germany - BAFIN	No	Yes	We would prefer a more accurate exposure such as gross earned premiums.
Global Federation of Insurance Associations	Global	No	Yes	Given that the measurement of operational risk is extremely subjective, GFIA supports a factor-based approach as currently envisaged by the IAIS. GFIA supports further investigation into the issues raised by the IAIS, and in particular, the alignment of the operational risk charge with the most reflective exposure base for each class of business.
International Actuarial Association	International	No	Yes	As mentioned in our response to Q146, the Insurance Regulation of the IAA suggests changing the non-life exposure basis to relate to expense levels excluding commissions and claim adjustment expenses. This should reduce the risk of the operational risk charge double-counting the risk of operational failures included in the data used to parameterize the premium and reserve risk charges. With regard to growth charges, growth increases operational risk to the extent it overwhelms the existing processes and control environment. That occurs when real growth is large, not when nominal growth is large due to inflation. Hence the growth threshold should inflation-adjusted and not based on a fixed level.
General Insurance Association of Japan	Japan	No	Yes	Please refer to our comments on Q146.
Financial Supervisory Service (FSS) & Financial Services Commission (FSC)	Korea (Republic of)	No	Yes	
Legal & General	UK	No	Yes	Our response to Q146 covers the points that we would raise in response to this question.

National Association of Mutual Insurance Companies	United States	No	Yes	The use of a capital add-on approach that includes a percentage of overall capital is a better option.
RAA	United States and many other jurisdictions	No	Yes	Given that the measurement of operational risk is highly subjective, we prefer a simple capital add on requirement based on a percentage of the capital requirement.
American Academy of Actuaries	United States of America	No	Yes	As mentioned in our response to Q146, we suggest changing the non-life exposure basis to be expense levels excluding commissions and claim adjustment expenses. This should reduce the risk of the Operational risk charge double-counting the risk of operational failures included in the data used to parameterize the Premium and Claims Reserve risk charges. With regard to growth charges, growth increases operational risk to the extent it overwhelms the existing processes and control environment. That occurs when real growth is large, not when nominal growth is large due to inflation. Hence the growth threshold should be based on the underlying rate of inflation and not based on a fixed level.
Property Casualty Insurers Association of America (PCI)	USA	No	Yes	PCI's yes or no response was simply required in order to open the text box and file comments. We believe this question to be best addressed by field test volunteers who have the ability to do so with the benefit of actual data for support and context. The absence of a response by PCI should not be taken one way or the other with respect to the subject of the question.
National Association of Insurance Commissioners (NAIC)	USA, NAIC	No	Yes	Yes. The operational risk charge should be a percentage of the capital requirement.

Q148 Section 7.19 Are the proposed Operational risk factors appropriate for ICS Version 2.0, both in terms of size and relativity? If "no", please propose evidence for alternative factors and their practicality for implementation in a standard method.

Organisation	Jurisdiction	Confidential	Answer	Answer Comments
China Banking and Insurance Regulatory Commission (CBIRC)	China	No	Yes	
European Insurance and Occupational Pensions Authority (EIOPA)	EIOPA	No	No	The ICS factors are significantly lower than the ones shown in the Table 16 of the consultation document, based on a CEIOPS study. As they stand, the current ICS factors risk not being prudent enough.
Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)	Germany - BAFIN	No	No	The ICS factors are significantly lower than the ones shown in the Table 16 of the consultation document, based on a CEIOPS study. As they stand, the current ICS factors risk not being prudent enough.
International Actuarial Association	International	No	No	As stated in our response to Q 146, the Insurance Regulation Committee of the IAA sees that a major difficulty with regard to quantifying Operational Risk for non-life insurers is to avoid double-counting. Any measurement of Operational Risk needs to remove Operational Risk events that also show up in the data used to quantify the Premium and Claims Reserving risks, and we are not aware of any reliable way of doing so. Hence, even if the factors shown in Table 16 of the Consultation Paper are reasonable estimates of the risk, the factors would need to adjust for any double-counting of the risk already reflected in other areas on the ICS. Based on the size of the resulting charges in last year's field test, we believe that the results from using these factors are not reasonable. We recommend instead using an approach similar to that used in Bermuda and China (which use a capital add-on approach with the factor adjusted based on an assessment of the control environment strength).
General Insurance Association of Japan	Japan	No	Yes	

Financial Supervisory Service (FSS) & Financial Services Commission (FSC)	Korea (Republic of)	No	Yes	
Legal & General	UK	No	No	We do not believe that it is possible to derive a materially appropriate capital amount for operational risk across a diverse range of IAIGs by simply using Percentage of Current Estimate and/or Premiums. See our response to Q146 for detailed consideration of alternative methodologies. Within the Percentage of Current Estimate methodology we do not understand the rationale for non-risk business to have a higher liability multiple than risk business. We observe that the IAIS appears to be deriving operational risk capital as a percentage of capital on other risks and using average and median values to assess the reasonableness of the calibration. We do not believe that looking at the average or median values is sufficient to get a meaningful view on the suitability of the methodology. Instead we believe that the extreme values observed across IAIGs are more relevant as they are likely to indicate situations where the methodology is not producing suitable output.
National Association of Mutual Insurance Companies	United States	No	No	Operational risk and all other risks and their factors should be determined by the local jurisdictional supervisor. NAMIC disagrees with the mandate of a standard method, the 99.5% VaR calibration level and the IAIS dictating the factors to be used in the formula. Jurisdictional flexibility is the appropriate way to capture these risks with mutual recognition and shared understanding of the jurisdictional approach at supervisory colleges. The ICS is not yet fit for purpose. Significant additional work is needed to achieve an appropriate global capital standard and it may be completely unachievable.
American Academy of Actuaries	United States of America	No	No	From the description provided in the consultation paper, we believe that the approach used and method relied upon by Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) may have been flawed. A major difficulty with regard to quantifying Operational risk for non-life insurers is avoiding double-counting. Any measurement of Operational risk needs to remove Operational risk events that also show up in the data used to quantify the Premium and Claims Reserving risks, and we are not aware of any reliable way of doing so. Hence, even if the factors shown in Table 16 of the consultation paper are



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				reasonable estimates of the risk, the factors would have to adjust for any double-counting of the risk already reflected in other areas on the ICS. Based on the size of the resulting charges in last year's field test, we believe that the results from using these factors are not reasonable. We recommend instead using an approach that applies a factor to expense levels excluding commissions and claims adjustment expenses, as a measure of the size of operations with the factor possibly adjusted based on an assessment of the control environment strength.
Prudential Financial, Inc.	United States of America	No	No	We note that the basis, rationale and details underpinning the operational risk factors have not been adequately disclosed and therefore we are not able to sufficiently assess their appropriateness.
Property Casualty Insurers Association of America (PCI)	USA	No	No	PCI's yes or no response was simply required in order to open the text box and file comments. We believe this question to be best addressed by field test volunteers who have the ability to do so with the benefit of actual data for support and context. The absence of a response by PCI should not be taken one way or the other with respect to the subject of the question.

Q149 Section 7.19 Are there any further comments on Operational risk that the IAIS should consider in the development of ICS Version 2.0? If "yes", please explain with sufficient detail and rationale.

Organisation	Jurisdiction	Confidential	Answer	Answer Comments
China Banking and Insurance Regulatory Commission (CBIRC)	China	No	No	

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European Insurance and Occupational Pensions Authority (EIOPA)	EIOPA	No	Yes	EIOPA believes that operational risk increases together with the activity size as it stems from inadequate or failed internal processes, personnel or systems. In turn, operational risk can be decreased if the insurer is well diversified and managed (which would mean a low value of the capital requirement in other ICS risks). Therefore, EIOPA would favour a cap of this risk, based on a percentage of the other risks.
Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)	Germany - BAFIN	No	Yes	We believe that operational risk increases together with the activity size as it stems from inadequate or failed internal processes, personnel or systems. In turn, operational risk can be decreased if the insurer is well diversified and managed (which would mean a low value of the capital requirement in other ICS risks). Therefore, we would favour a cap of this risk, based on a percentage of the other risks.
General Insurance Association of Japan	Japan	No	No	
Financial Supervisory Service (FSS) & Financial Services Commission (FSC)	Korea (Republic of)	No	No	
Legal & General	UK	No	Yes	We do not see any reason why operational risk should not be allowed to diversify against other risks as many types of operational risk loss event do not have a clear dependency on experience on other risks. Within the Solvency II regime many Internal Model firms have had approval for an aggregation methodology that allows for diversification between operational and other risks, consistent with this rationale.
National Association of Mutual Insurance Companies	United States	No	Yes	Operational risk and all other risks and their factors should be determined by the local jurisdictional supervisor. NAMIC disagrees with the mandate of a standard method, the 99.5% VaR calibration level and the IAIS dictating the factors to be used in the formula. Jurisdictional flexibility is the appropriate way to capture these risks with mutual recognition and shared understanding of the jurisdictional approach at supervisory colleges. The ICS is not yet fit for purpose. Significant additional work is needed to achieve an appropriate global capital standard and it may be completely unachievable.

Prudential Financial, Inc.	United States of America	No	Yes	Prudential Financial supports an operational risk capital standard that is simple, transparent and reflects the relative exposure to operational risk. The standard should be calibrated to reflect the true underlying operational risk profile for insurers. A potential methodology may be based on the concepts of The Standardized Approach defined in the Basel II Framework, adapted to appropriately apply to the Insurance business model.
Liberty Mutual Insurance Group	USA	No	Yes	Liberty Mutual repeats its comments in previous ICS consultations to urge the IAIS to eliminate operational risk from the ICS. No operational risk factor should be used because any attempt to do so inappropriately attempts to impose a “one-size-fits all” analysis on an issue that is inherently variable among insurers, given the wide variety of operational structures and management systems. The IAIS should recognize that the ICS cannot accurately account for varying levels of operational risk across companies.
Property Casualty Insurers Association of America (PCI)	USA	No	Yes	PCI’s yes or no response was simply required in order to open the text box and file comments. We believe this question to be best addressed by field test volunteers who have the ability to do so with the benefit of actual data for support and context. The absence of a response by PCI should not be taken one way or the other with respect to the subject of the question.

End of Section 7.19