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NAIC's Solvency Modernization Initiative – An Opportunity for Broader Enhancements

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Solvency Wagon

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National Association of Insurance Commissioners

The Center for Insurance Policy and Research

Center for Insurance Policy and Research
Who Are We?

- The Center is comprised of three FT personnel: Mary Weiss (distinguished scholar from Temple University); Edward Toy (capital markets advisor); and Ramon (previously with the California Department of Insurance – Financial Surveillance; 30+ years)
- The Center focuses on promoting sound insurance regulation from a policy perspective; providing support to state insurance regulators and building relationships and communicating with federal policy makers; and participating in solvency-based international initiatives.

NAIC National Association of Insurance Commissioners & The Center for Insurance Policy and Research

Purpose

- The purpose of this presentation is to discuss the NAIC’s Solvency Modernization Initiative and its relationship to some of the international developments. These highlights are not a comprehensive view of all outstanding international issues.
- I will provide a few comments about Solvency II.

NAIC National Association of Insurance Commissioners

2008 Premium Volume -- Worldwide

Rank	Jurisdiction	Premium Volume (In Millions US $)	Market Share	Rank	Jurisdiction	Premium Volume (In Millions US $)	Market Share
1	United States	$1,641,104	35.14%	26	Finland	$23,336	0.50%
2	Japan	$473,197	10.13%	27	Portugal	$22,704	0.49%
3	United Kingdom	$450,152	9.64%	28	Norway	$20,481	0.44%
4	France	$273,007	5.85%	29	Luxembourg	$19,319	0.41%
5	Germany	$243,085	5.21%	30	Mexico	$19,023	0.41%
6	PR China	$140,818	3.02%	31	Singapore	$16,528	0.35%
7	Italy	$140,689	3.01%	32	Israel	$10,823	0.23%
8	Netherlands	$112,611	2.41%	33	Venezuela	$10,060	0.22%
9	Canada	$105,174	2.25%	34	Malaysia	$9,335	0.20%
10	South Korea	$97,023	2.08%	35	Thailand	$9,138	0.20%
11	Spain	$87,038	1.86%	36	Turkey	$8,807	0.19%
12	Australia	$70,951	1.52%	37	Argentina	$8,396	0.18%
13	Taiwan	$64,265	1.38%	38	Czech Republic	$8,168	0.17%
14	India	$56,190	1.20%	39	Indonesia	$6,903	0.15%
15	Belgium	$49,077	1.05%	40	Greece	$6,673	0.14%
16	Switzerland	$48,718	1.04%	41	New Zealand	$6,613	0.14%
17	Brazil	$47,493	1.02%	42	Chile	$5,783	0.12%
18	Ireland	$44,918	0.96%	43	Liechtenstein	$5,479	0.12%
19	South Africa	$42,515	0.91%	44	Hungary	$5,028	0.11%
20	Russia	$38,778	0.83%	45	United Arab Emirate	$5,016	0.11%
21	Sweden	$36,432	0.78%	46	Ukraine	$4,299	0.09%
22	Denmark	$31,457	0.67%	47	Iran	$4,243	0.09%
23	Poland	$24,403	0.52%	48	Columbia	$4,106	0.09%
24	Hong Kong	$24,096	0.52%	49	Romania	$3,523	0.08%
25	Austria	$23,925	0.51%	50	Saudi Arabia	$3,070	0.07%
	All the Rest	$56,228	1.2%				
	Worldwide Total	$4,670,198	100.00%				

Sources: NAIC Financial Database for USA, residual market mechanisms and health insurers not filing to the NAIC, and SwissRe Sigma No. 3/2009 for the remainder

NAIC National Association of Insurance Commissioners & The Center for Insurance Policy and Research

2008 Premium Volume -- Worldwide (An Alternative Look)

Rank	Jurisdiction	Premium Volume (In Millions US $	Market Share	Rank	Jurisdiction	Premium Volume (In Millions US $	Market Share
1	Japan	$473,197	10.13%	26	Ireland	$44,918	0.96%
2	United Kingdom	$450,152	9.64%	27	Massachusetts	$43,521	0.93%
3	France	$273,007	5.85%	28	South Africa	$42,515	0.91%
4	Germany	$243,085	5.21%	29	Georgia	$38,961	0.83%
5	California	$212,811	4.56%	30	Russia	$38,778	0.83%
5	PR China	$140,818	3.02%	31	North Carolina	$37,202	0.80%
6	Italy	$140,689	3.01%	32	Sweden	$36,432	0.78%
7	New York	$127,393	2.73%	33	Virginia	$35,631	0.76%
8	Netherlands	$112,611	2.41%	34	Denmark	$31,457	0.67%
9	Florida	$108,470	2.32%	35	Washington	$31,353	0.67%
10	Canada	$105,174	2.25%	36	Wisconsin	$29,702	0.64%
11	Texas	$99,551	2.13%	37	Minnesota	$29,266	0.63%
12	South Korea	$97,023	2.08%	38	Missouri	$28,738	0.62%
13	Spain	$87,038	1.86%	39	Maryland	$27,629	0.59%
14	Pennsylvania	$81,543	1.75%	40	Indiana	$26,303	0.56%
15	Australia	$70,951	1.52%	41	Tennessee	$26,092	0.56%
16	Taiwan	$64,265	1.38%	42	Arizona	$25,900	0.55%
17	Illinois	$60,178	1.29%	43	Colorado	$24,992	0.54%
18	Ohio	$56,411	1.21%	44	Poland	$24,403	0.52%
19	India	$56,190	1.20%	45	Connecticut	$24,359	0.52%
20	New Jersey	$55,783	1.19%	46	Hong Kong	$24,096	0.52%
21	Michigan	$51,303	1.10%	47	Austria	$23,925	0.51%
22	Belgium	$49,077	1.05%	48	Finland	$23,336	0.50%
23	Switzerland	$48,718	1.04%	49	Portugal	$22,704	0.49%
24	Brazil	$47,493	1.02%	50	Louisiana	$22,294	0.48%
	All the Rest	$592,760	12.69%				
	Worldwide Total	$4,670,198	100.00%				

Sources: NAIC Financial Database for USA, residual market mechanisms and health insurers not filing to the NAIC, and SwissRe Sigma No. 3/2009 for the remainder

Solvency II – General Comments

- We welcome Solvency II for Europe…it's a dramatic improvement over Solvency I.
- We're all in the same boat…we seek prudent regulation and a competitive marketplace.
- But there are still open questions about Solvency II: some features haven't been tested; there is much caution about reliance on models; how far can we go in group supervision.
- Much has been said about equivalence testing of third countries (the US being one of them) against a system that is not even in place yet, and certainly not tried and tested.

Solvency II – General Comments

- Is the U.S. Solvency Framework comparable to Solvency II, or is Solvency II comparable to the U.S. Financial Accreditation System?
- The U.S. Solvency Framework is tried and tested under fire; it is a multi-jurisdictional system; there is a supervisory culture in place; we speak the same language; and we even see the same tv shows.
- Seriously, though, the US is active in international venues; takes leadership roles in the IAIS committee structure; maintains healthy relationship with CEIOPS.

Solvency Modernization Initiative

- Except for certain specialized monoline companies, the US insurance industry largely survived the economic crisis of 2008/2009. The underlying nature of the insurance business, the U.S. solvency framework, and fundamental risk management systems worked together.
- But survival is not without cost; the insurance regulators cannot be complacent. After significant deliberation, in June of 2008, the NAIC adopted the Solvency Modernization Initiative.

Solvency Modernization Initiative

Fundamentally speaking, the SMI is a multi-dimensional initiative involving: 1) a self-examination "looking within"; 2) "looking outside" of ourselves; and 3) identifying potential changes to our solvency framework.

Primary Components of the SMI

The five primary components include:

1) Capital requirements
2) International Accounting
3) Valuation Issues (e.g., PBR)
4) Group Issues
5) Reinsurance Modernization

Capital Requirements

- Global solvency standards are under development. These include capital requirements and capital resources; the role of enterprise risk management; the role of internal models when using them for capital requirements.
- Should there be a "pre-approval" of models used in RBC, what are the relevant definitions of RBC safety levels
- Solvency standards are being created to apply to group supervision: How will group capital be assessed? How can group capital be used; insurance group only, non-insurance companies in the group?

Capital Requirements
(continued)

- ORSA ("Own Risk and Solvency Assessment") – actually, to fully comply with current IAIS standards, some changes are most likely needed in the U.S. regarding ORSA requirements. The Canadian model, as an example, would permit some of its companies to use scenario modeling integrated with the insurer's risk management process.
- Does it make good regulatory sense to incorporate this within our regulatory framework?

International Accounting

- The Financial Accounting Standards Board (U.S. accounting standard setters) and the International Accounting Standards Board (international counterpart) are engaged in a “joint project” to reformulate global accounting standards for insurers scheduled to be completed in 2011.
- Is it the demise, or the future foundation of U.S. Statutory Accounting Principles for U.S. insurers? (Statutory accounting principles were codified effective 2001; currently maintained by reviewing GAAP pronouncements; with the potential elimination of GAAP, how would this impact statutory accounting principles?

International Accounting
(continued)

- Many investment statutes as well as the risk-based capital formula are based on statutory-based financial statements? How will this framework continue to exist?

- There may be political pressure to have insurance regulators adopt the “new and improved” converged accounting basis because of the cost of maintaining dual accounting bases and to avoid a perceived failure to converge internationally.

Group Issues

Numerous group issues:

- IAIS Groups Subcommittee has adopted a principle which states that group capital should be assessed. Various issues remain outstanding: definition of groups (insurance groups, financial conglomerates?); fungibility of capital (how easily can capital move within the group? Is fungibility of capital enforceable?)
- What is the role of supervisory colleges in the context of group supervision?

Financial Sector Assessment Program (FSAP)

- The United States has committed to undergo regular FSAP reviews as part of a declaration of the G20 and Financial Stability Board.
- The United States (NAIC in conjunction with several states) is currently under an FSAP review by the International Monetary Fund.
- FSAPs are essentially based on the IAIS Insurance Core Principles, which will most certainly incorporate IAIS Standards beginning in 2011.
- It becomes imperative that the U.S. insurance regulators become engaged in the IAIS process as we will be judged by those IAIS standards that are adopted.

Common Assessment Framework Task Force

- Based on demands from the G20 and the Financial Stability Board, as well as from IAIS members, this recently created task force was created to develop options for a broad, new “vision” for the IAIS.
- The initial work includes a design and practicality of a potential common assessment framework for insurance groups.
- Depending on the outcome of this exercise, the Executive Committee will assess the merits of further advancing the work.