



# Regulatory, Accounting and Performance Measurement Convergence

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For Fun and Profit

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November 7, 2008

## For Today . . .

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- Global Solvency Standards - IAIS/ Solvency II/PBA
- ERM/EC – Regulators, Rating Agencies, Shareholders
- IASB Insurance Project
- CFO Forum MCEV
- Common Principles
- Fun and Profit

# Global Solvency Standards – IAIS, Solvency II, PBA

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- IAIS Solvency Framework for Global Consistency
  - Preconditions – supervisory authority, market conditions
  - Regulatory requirements – financial, governance, market conduct
  - Supervisory assessment and intervention
  - Principles-based – local adaptation
  - Individual company risk profiles – realistic internal models
- Solvency II
  - “Blueprint” for IAIS solvency standards
  - Pillar I – quantitative requirements calculated by standard formula or internal models
  - Pillar 2 – risk management requirements; supervisory interaction
  - Pillar 3 – public disclosures
- Principles-Based Approach
  - Selective, e.g., reserve and minimum capital standards for life and variable annuity business – stochastic internal models

## ERM/EC – Regulators, Rating Agencies, Shareholders

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- Individual company solvency standards requires comprehensive understanding of enterprise risk profiles
  - Traditional risk silos
  - Correlation of risk – single event, counterparty, diversification
  - All jurisdictions, all sectors
- Regulators
  - Fundamental for understanding/managing risks
  - Foundation for internal models – risk-based capital needs
  - Group-wide supervision
- Rating Agencies
  - Demanding more comprehensive enterprise risk analysis, sound controls, clear governance, transparency and move to economic capital
  - Insurers face more complex and extreme risk profiles
- Shareholders – increasing awareness, demands on all

## IASB Insurance Project

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- Adding market consistent approach to liability measurement
- Discounted mean (“best”) estimate of future cash flows
- Market-consistent assumptions for hedgeable risks with risk margin for non-hedgeable risks
- Methods (e.g., exit value, others) at issue
- Coordinated with IAIS standards – same or explicit variations
- FASB and IASB discussing system convergence
- SEC acceptance IASB-compliant reporting

## CFO Forum MCEV

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- What is profit or value in insurance?
- Supplementary embedded value reporting
- CFO Forum – CFOs of major European insurers – build consistency
- European EV 2004
- 2008 CFO Forum MCEV
  - Market consistent, e.g., market price for valuation
  - Separate valuation of in force and new business
  - Distinguishes financial and non-hedgeable risks
  - Greater consistency in practice
- EV methods require assumptions about future behavior of critical profit drivers – similar to pricing and M&A valuations

## Common Principles

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- Principles based
- Best estimates, time value of money
- Market consistent – mark-to-market
- Risk based
- Transparent, including method variations
- Individual company/group specific
- Cross jurisdiction, cross sector
- Enterprise view
- Used for strategic business decisions
- Explicit risk margins
- Auditable
- Address “tail” risk
- For “normal” markets and “stressed” markets

## Fun and Profit – An Opportunity

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- Understand business better at an enterprise level
- Use compliance tools for product design, new business models
- Global response to systematic failures
- Leverage today's information systems to find alternative solutions
- Build consensus on solutions
- Rebuild stability and confidence – limit contagion
- Improve support for needed retirement product guarantees (e.g., hedging)
- Expand the scope and coverage of insurable risk
- Use compliance tools for business decisions – ultimate convergence