

Biennial Convention 2007

# Adventures in Risk

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Institute of Actuaries of Australia



# International Developments in Insurance Regulation

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## Presentation Outline

- Phase II of the IASB project on Insurance Contracts
- The joint IASB/FASB project on fair value measurement
- The development of a range of standards by the IAIS in the area of insurer solvency
- Developments in the supervision of conglomerates



## IAIS over-riding principle

- The IAIS believes that it is most desirable that the methodologies for calculating items in general purpose financial reports can be used for, or are substantially consistent with, the methodologies used for regulatory reporting purposes, with as few changes as possible to satisfy regulatory reporting requirements.



## IASB Insurance Contracts Phase II

- Australia has been doing lots of it already so these are just the interesting bits ...
- Controversial items where:
- IASB views different from both supervisors and industry
- IASB views different from industry but aligned with supervisors



## Entry/Exit value & P/L on inception

- Industry organizations (CFO Forum & GNAIE) very keen on implementation A – i.e. entry value style calibration of risk margin and no profit on inception. P/L geography?
- CFO Forum quoting US\$7.2bn profits on inception for 11 of its 20 members
- IAIS view: “similar obligations with similar risk profiles should result in similar liabilities” – incompatible with implementation A.



## Discretionary Participation Features

- IASB claims these do not meet the definition of liabilities
- IAIS & most industry counter that recording expected dividends in equity is misleading and creates a profit up front which is reversed by a subsequent loss
- IAIS arguing issue is one of measurement, not of recognition: IASB is unbundling expected cash flows!



## Own Credit Standing

- IAIS view: completely bonkers, and US may introduce at the IAIS a proposed standard to make reduction of insurer liabilities as a result of own credit standing an event leading to suspension of license
- Only explanation in FAS157 is a symmetry of assets and liabilities argument



## “Beneficial” policyholder behaviour

- IASB has got itself into a real pickle over this
- Problem is future premiums (unbundled) don't meet the definition of an asset
- Long term policies have acquisition costs  $>$  1<sup>st</sup> year premium so loss on inception
- IASB solution: policyholder relationship intangible
- IAS solution: read building block 1!





## Other issues

- Non-life discounting – issue for GNAIE
- Discount rates – appropriate rate, liquidity
- Service margin – lots of confusion
- Recognition of bound but not incepted business

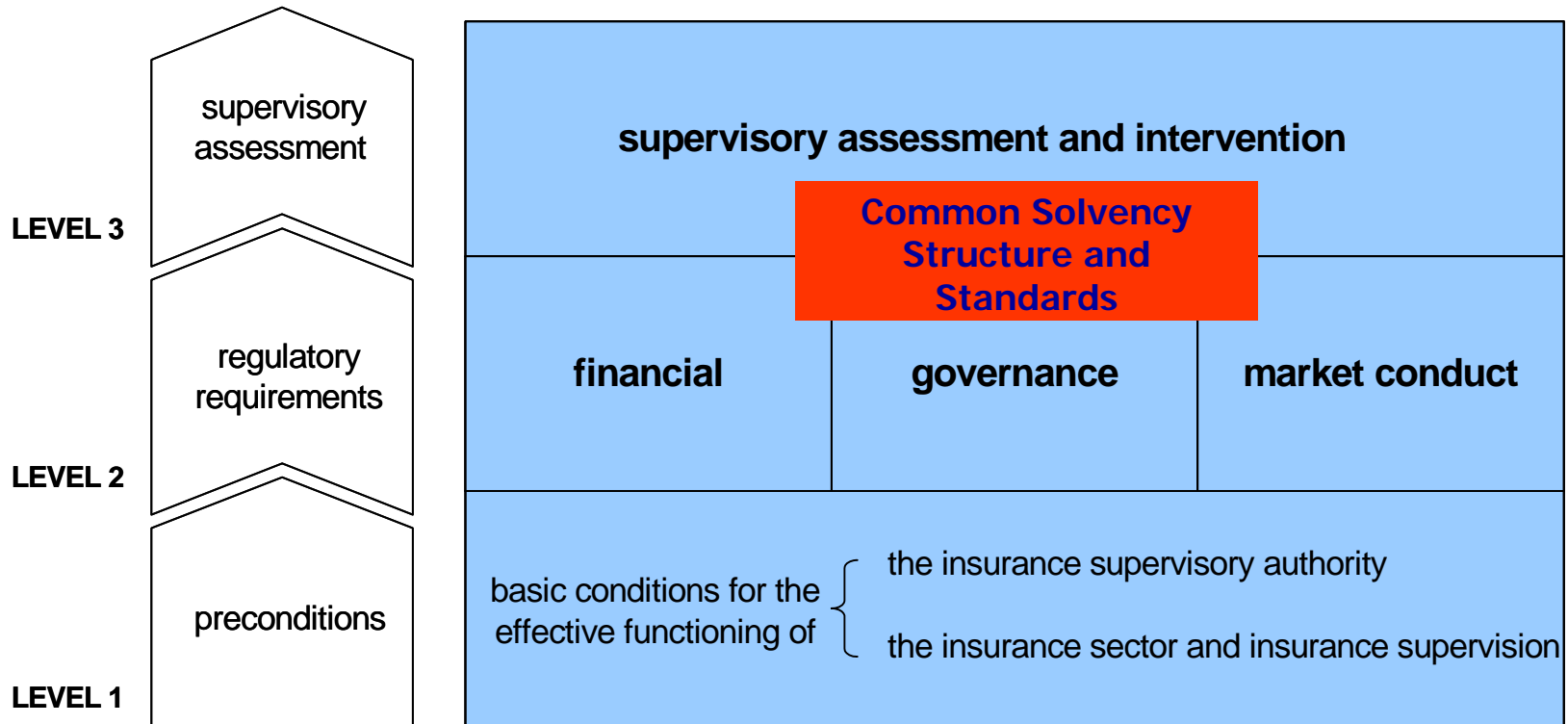


## IASB/FASB Fair Value

- IASB FV & review of FAS157 still underway
- Both Boards have announced a long term intention that all financial instruments be measured at fair value through profit and loss
- Poured cold water on my brilliant idea re: FV for level 1 being a step towards full FV
- Overall aim is consistent with the IAIS solvency view

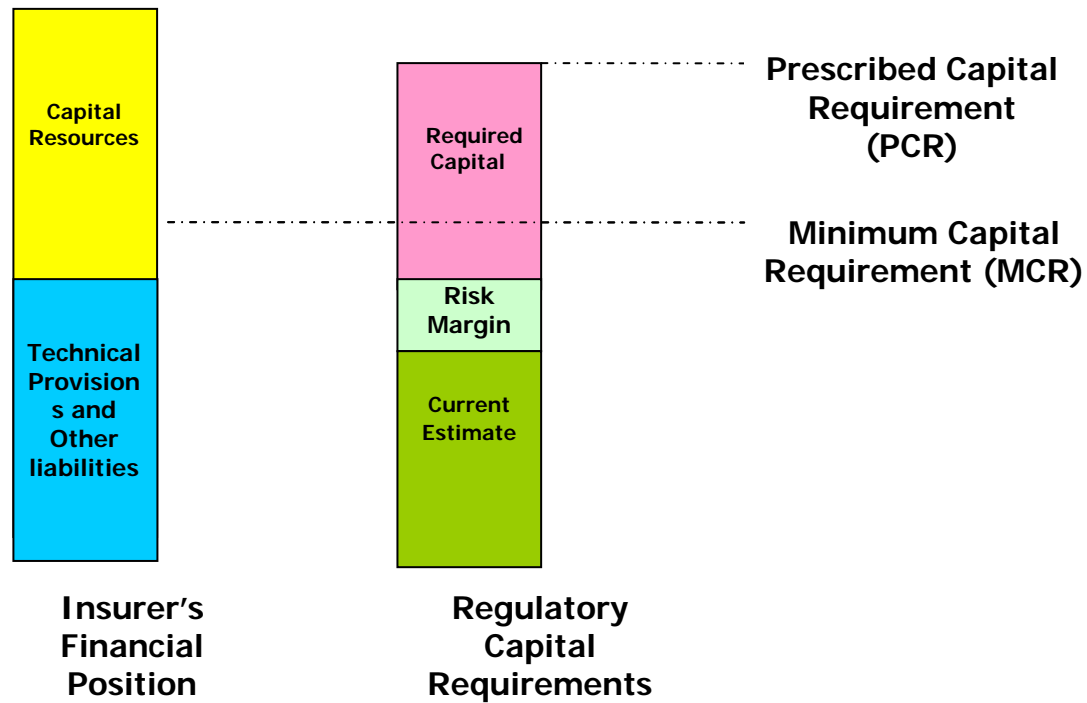


## IAIS Solvency





## Regulatory capital needs





## The key underlying principles

- Total balance sheet approach using economic values – “market consistent”
- Risk sensitive regime
- Sound corporate governance
- Sound market conduct policies
- Variable levels of supervisory intervention
- Boundary between liability & capital – e.g. diversification, AL mismatch, efficiency, etc.



## The future process

- Standards on valuation, capital, ERM and internal models – likely over the next couple of years
- Application guidance thereon
- Issues paper on Group Solvency Issues



## Group Supervision

- Draft principles on group supervision: may be adopted in October
- Open items for the future:
  - The concepts of lead supervisor and supervisory colleges
  - Issues of group internal models and mutual recognition.



## Questions?!

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