October 19, 2016

Yoshihiro Kawai
Secretary General
International Association of Insurance Supervisors (IAIS)
Centralbahnplatz 2
CH-4051 Basel
Switzerland

Re: IAIS consultation on a Risk-based Global Insurance Capital Standard – Version 1.0

Dear Dr. Kawai:

The Institute of International Finance (IIF) and the Geneva Association (GA) welcome the opportunity to provide comments on the Consultation Document dated 19 July 2016 on the Risk-based Global Insurance Capital Standard (ICS) - Version 1.0. The combined membership of the IIF and GA represent the vast majority of Internationally Active Insurance Groups (IAIGs), which will potentially be affected by the ICS. We have followed the development of the ICS with interest, responded jointly to the first ICS consultation in December 2014, and will continue to work constructively with the IAIS.

Our submission focuses on delivering important high-level messages regarding the ICS. At the same time, a number of our members, many of whom participate in the IAIS' field testing exercise, will independently respond to the many questions, which must be answered at a more granular, technical level.

I. First address the fundamentals of the ICS, then sequence further development

We acknowledge that progress has been made on a range of technical issues related to the ICS. However, a number of fundamental and technical issues remain. On the fundamental side, further work is needed to explain the ICS' relation to existing capital regimes, the interplay of the ICS and the other modules and elements of ComFrame and the ability of the measure to reflect local circumstances. On the technical side, further work is needed to improve the valuation approaches. We believe that these questions should be addressed before ICS 1.0 is released.

The industry and more generally all stakeholders in all jurisdictions involved in this project should be aware of the direction which will be followed by the IAIS and its members and not speculate on what the key features of the future framework may look like especially on these fundamental aspects. We would also like to insist that it is critical to its success that the ICS project get the necessary political buy-in at all

levels along its development. To date the IAIS has not demonstrated that there is clear political commitment among domestic or regional regulators to the development and ultimate implementation of the ICS in particular to justify the extensive resources required of both supervisors and stakeholders. Furthermore, placing the ICS on top of existing local regimes as currently envisioned will result in conflicting solvency regimes and costly disruption to insurer's asset and liability management (ALM), the availability and affordability of insurance, and insurers' ability to continue their role as stable, long-term investors and contributors to global economic growth.

We urge the IAIS to take a sequential approach in the development of the ICS. We suggest a step-by-step approach in which higher-level, principles-based measures are designed and then fully tested before work is advanced further. This would provide an opportunity to evaluate fully the impact of the capital standard against its agreed objectives and within the broader context of ComFrame, and to determine cost-benefit trade-offs associated with the level of prescriptiveness in the ICS necessary to meet appropriate regulatory objectives.

This will help to ensure that the ICS fulfills its role within ComFrame as a supervisory tool that contributes to achieving comparable outcomes and respects the insurance business model, and provides a basis for sound risk management, resilient and stable provision of insurance protection and vigorous, fair competition in local and regional markets.

We further note the following issues as essential to the ICS' development:

1. *Promoting consistency with regional circumstances and capital regimes*

Insurance markets around the world are marked by a wide variety in demographics, legal requirements, insurance and other financial product offerings, consumer risk preferences, and potential government-provided social security, and corresponding differences in approach among jurisdictions' supervisory regimes reflecting these fundamentals.

Members of the IIF/GA unanimously agree that the current ICS standard method including valuation, discount rate and calibration approach do not appropriately reflect these important differences and consequent assessments of exposure to risk. The standard method must be amended to capture these fundamental differences in version 1.0. This could be pursued in a number of ways including more appropriate calibrations and less prescription to reflect geographic diversity or the use of (full or partial) internal models in jurisdictions, where permitted.

The IIF/GA have concerns that the ICS in its current form could be inconsistent with existing and developing insurance capital regimes. In fact, this past year has seen a renewed commitment by several IAIS member jurisdictions to the development or maintenance of their own insurance capital regimes.[1] It is not yet clear how, in such circumstances, the ICS could increase convergence and comparability across regimes, and contribute to greater supervisory and compliance efficiency for supervisors and IAIGs respectively. We call on the IAIS to develop an ICS with appropriate flexibility to

[1] *See* Governor D.N. Tarullo, "Insurance companies and the role of the Federal Reserve," Speech at the NAIC International Insurance Forum, Washington DC, May 20, 2016. *See also* letter from EU Commission DG Guersent to FSB chair, Mark Carney (Bank of England) (Politico report - July 2016); 2018 planned review of Solvency II.

work within local, national, and regional regimes and circumstances, resulting in comparable outcomes across jurisdictions.

2. *Interplay of the ICS and other modules and elements of ComFrame*

There is a fundamental question about the interplay of the ICS and other modules and elements of ComFrame which still needs to be addressed. While we understand that module 2 element 5 acts as a placeholder for the ICS, we note that (a) the developing ICS is not truly embedded in ComFrame and (b) the ICS' prescriptive nature goes beyond functioning as "a basis for comparability of IAIG regulation and supervisory processes."[2] Indeed, several aspects of the ICS go beyond the aim of comparable capital adequacy measurement and cross into other prudential concerns, including liquidity risk.[3] We emphasize the need for a more integrated approach in which capital is viewed in the context of the broader supervisory framework of ComFrame. Numerous quantitative and qualitative tools and requirements currently help guide both supervisors and companies, including corporate governance and ERM standards, ORSA and stress testing. As a result, the ICS capital standard should not be viewed as an all-inclusive solution to all supervisory matters; rather it should be a complement to the range of other available tools.

In today's economic environment, we also consider it critical that the ICS be designed and calibrated in a manner that will allow the insurance sector to continue to provide certain products and services to customers. Excessive risk aversion may lead to a deterioration of the sustainability of the insurance business, thus dampening economic growth and the expansion of insurance in all global markets. Therefore, it is essential to strike a balance between capital, risk and the continued provision by insurers of certain products and services to customers, together with investments associated to support these products and services.

3. *Valuation*

The ICS should be based on a valuation framework that, through a coherent treatment of assets and liabilities, is tailored to the insurance business model. This includes recognition of buy-and-hold investment strategies. The framework should lead to more stable and comparable - substantially the same - valuation outcomes across jurisdictions in accordance with ICS Principle 1. This would support key prudential objectives such as mitigating pro-cyclicality, incentivizing prudent ALM, and providing appropriate risk signaling. It also would increase the ICS' compatibility with local supervisory regimes and risk management practices. Below, we provide recommendations on how to improve the Market-Adjusted Valuation (MAV) and GAAP with Adjustments Valuation (GAAP+) approaches in more detail. We do note that building such a valuation standard is likely to take a long time to accomplish, notably beyond the current timeframe the IAIS has currently set for the ICS.

II. The ICS must respect local and regional differences

[2] IAIS, "Common Framework for the Supervision of Internationally Active Insurance Groups," Revised draft, September 2014, p. 2.

[3] For example, applying an application ratio to liability buckets as currently proposed would double count the liquidity risk.

The ICS aims to provide a comparable capital regime for IAIGs against a background of existing solvency regimes that are primarily focused on solo entities. In order to support this convergence process, the IIF/GA stress the importance of ensuring sufficient flexibility to allow implementation that is tailored to the specific markets and address local and regional issues.

The prescriptive one-size-fits-all approach to the ICS adopts a rather narrow perspective that may seem natural to achieve comparability, but in our view will not succeed.

It is vital that local and regional differences in relation to, among others, available assets, products, strategies or legal environments are accounted for in the ICS framework to appropriately reflect the risks applicable to IAIGs and avoid conflicting with existing, legally binding jurisdictional capital requirements.

As mentioned above, members of the IIF/GA unanimously agree that the current ICS standard method including valuation, discount rate and calibration approach do not appropriately reflect these important differences and consequent assessments of exposure to risk. The standard method must reflect appropriate improvements to capture these fundamental differences in version 1.0. Members suggest this could be pursued in a number of ways, including more appropriate calibrations and less prescription to reflect geographic diversity or the use of (full or partial) internal models in jurisdictions where permitted.

Two examples illustrate the insensitivity of the standard model and the valuation methods to local differences.

- In the standard model, the impact of various risks (i.e. morbidity, mortality, longevity) will differ by region and among insurers within regions (e.g. based on their products, size of portfolio, type of policyholders). Adding additional granularity could better reflect the diversity and yet create comparable results.
- For MAV valuation discount rates, the appropriate approach should reflect the nature of liabilities and the ALM practices of insurers.[4]

We are keen to work with the IAIS to develop strategies for respecting local and regional differences while maintaining meaningful comparability between different regimes in the longer run.

[4] ALM is fundamental to the insurance business model, whereby insurers perform liability-driven investing, using the premiums received from policyholders to invest in diversified portfolios of generally long-term, high-quality assets to support their generally long-term and illiquid liabilities, and managing these assets to support liabilities within reasonable cash flow and duration target ranges.

III. Building valuation approaches with comparable outcomes is a long-term endeavor

A key feature of the proposed ICS version 1.0 is the inclusion of two valuation approaches, the MAV and GAAP+.[5] This reflects existing differences in valuation standards in IAIS member jurisdictions. However, the IAIS' stated ultimate goal is to build a single ICS with a common valuation approach through which the ICS achieves comparable outcomes across jurisdictions. Reaching such an ambitious goal will require a significant amount of time and technical expertise, but could ultimately produce a more informative, globally-consistent, and meaningful ICS that both reflects and incentivizes the prudent asset-liability management that is at the heart of insurance risk management. There are also steps the IAIS can take as an expedient to improve the consistency between the different valuation approaches currently proposed in the ICS. In the interim, with more than one approach existing for the ICS, IAIGs should have a choice on which approach to apply.

The ICS should be based on a valuation framework that, through a coherent treatment of assets and liabilities, is tailored to the insurance business model. The framework should lead to more stable and comparable - that is, substantially the same - valuation outcomes across jurisdictions in accordance with ICS Principle 1. This would support key prudential objectives such as mitigating pro-cyclicality, incentivizing prudent ALM, and providing appropriate risk signaling. It would also increase the ICS' compatibility with local supervisory regimes and risk management practices.

1. *Countering excessive short term volatility and recognizing buy-and-hold strategies*

According to the overwhelming majority of member companies, including all of the G-SIIs, dealing with the problem of excessive short term volatility should be a key objective of the ICS' valuation approach. Under the MAV, volatility arises in particular when spreads increase compared to the reference interest rate, and valuations of assets and liabilities adjust differently if the appropriate liability discount rate is not adopted. This may give rise to movements in available capital in the short term even though the longer term outlook is more stable. Under the GAAP+ approach, the volatility arises because the valuation of liabilities is more or less locked (based on book/expected yield), while that of the assets fluctuates more with the market.

The above mentioned overwhelming majority of IIF/GA members are of the opinion that, in dealing with non-economic short-term volatility, it is key for any valuation approach to recognize the ability of insurers to apply a buy-and-hold investment strategy as part of their ALM. Buy-and-hold strategies are a key feature of the insurance business model. Indeed, paragraph 162 of the consultation document states that "[t]o support long-term liabilities, IAIGs are able to hold long-term fixed income assets with little risk that they must be sold prior to maturity, in order to support a large amount of their long-term insurance liabilities. As long as those assets are held, their projected cash flows do not change (except through defaults), regardless of short-term changes in interest rates."[6] The same holds for other types of assets, including equities and real estate, which can be held for long periods in line with the duration of (long-term) liabilities and the level of free surplus capital.

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[5] Applying appropriate valuation approaches is key to ensure ICS Principle 6 of promoting sound risk management and ICS Principle 7 of minimizing inappropriate pro-cyclical behavior.

[6] IAIS, "Risk-based global insurance standard version 1.0. Public consultation document," Basel, July 19, 2016, p. 56.

Where future cash flows are fairly matched and the default risk is properly accounted for, the need for capital is significantly reduced. We do recognize that mismatch in the duration of assets and liabilities must be accounted for and that it is also vital that the long term nature of the insurance business is recognized (i.e., that insurers should not be unduly penalized for insurance liabilities which extend beyond the investable horizon). Both should be reflected in the appropriately designed and calibrated capital requirements rather than in the discount rate. Most members agree that interest rate stresses are suited to reflect duration mismatches where they exist on an insurer's balance sheet while some question this.

At the same time, buy-and-hold strategies are not always the most effective tool to support asset-liability management, in particular in a context of low rates. Around the world, prudential regimes have considered as well alternative ALM strategies, and have put in place countercyclical measures.

2. *On solutions to volatility in the consultation document*

Solutions to dampen volatility in the MAV as sought in the consultation document relate to a range of options for adjustments of the discount rate term structure for liabilities. However, the overwhelming majority of our members, including all of the G-SIIs, believe that these do not address the issue and think that significant further work is required. In particular, they stress that an option that should be seriously considered and explored further is an expected earned rate with proper guardrails in addition to other options being tested such as a reference portfolio. Such work should take into due consideration the necessity to avoid creating adverse investment incentives. Moreover, in the view of some members, a dampener to short-term equity movements should be examined as well.

A few member companies remain committed to having the option to use unadjusted discount curves for liabilities. Whereas the overwhelming majority of member companies, including all of the G-SIIs, have a totally different view and believe the use of unadjusted rates is completely inappropriate and would be procyclical and lead to unintended consequences for the wider economy.

Under the GAAP approach, the AOCI adjustment is introduced to deal with volatility. Both solutions – adjustments to the discount rate and the AOCI – are possible paths to address the problem of excessive short-term volatility.

Hence, we strongly urge the IAIS, together with industry, to ensure that the valuation approaches pursued under the ICS result in comparable outcomes in normal and stressed conditions, based on consistent principles.

3. *Key issues for further work*

Key issues for proposed joint further work are:

- Both the MAV and GAAP+ valuation approaches may give rise to "noise" that might distort relevant signals about the capital position. Going forward, priority must be given to avoiding such noise in the approaches.
- Buy-and-hold investment strategies should be reflected in the approaches. This implies that, as long as the default risk is properly considered, excessive short-term volatility should not affect solvency ratios. For example, when a bond is held to maturity by an insurer, a temporary increase in spreads would decrease the economic value of the bond on its balance sheet. However, this

unrealized loss would recycle back as an unrealized profit up to the bond's surrender value at maturity.

    - It is important for many of our members that such differences are captured properly through adopting a flexible, broad approach to the liability discount rate and to avoid narrow, restrictive adjustments. Notwithstanding the reflection of buy-and-hold strategies, where cash flows of assets and liabilities are closely matched, the ICS must recognize that the underlying risk to solvency is significantly reduced and in case of partial matching that the risk is partially reduced.

- The ICS must be able to reflect the valuation of insurance liabilities for a wide range of insurance products across jurisdictions. Many of our members argue that the optimal way forward is to develop an expected earned rate (based on a company's own assets) with proper guardrails. Such an approach is most readily reflective of insurer business and risk management practices and amenable to the desirable regulatory objective of implementing a risk-sensitive framework that both incentivizes prudent asset-liability management and mitigates procyclicality. An expected earned rate with guardrails could also serve as a single methodology across firms, obviating the broader policy challenge of attempting to make two distinct valuation frameworks co-exist in a meaningful way, which is a pre-requisite for the ICS to serve as a truly global standard. We would also be keen to work further with the IAIS on these issues, including how to define and calibrate the expected earned rate.
- Adjustments to AOCI:
    - The current approach identifies the AOCI on the debt securities, but does not consider the AOCI on foreign currency swaps or interest rate swaps hedging the debt security. We believe the AOCI on qualifying hedges on debt securities should be included in the AOCI adjustment calculation.
    - AOCI on assets backing long-term liabilities should be identified, with appropriate reductions to this AOCI balance for instruments where the unrealized gains and losses are more likely than not to be realized. This would include instruments such as callable bonds and RMBS expected to be prepaid. In addition, an adjustment for the AOCI from qualifying hedges on the assets backing long-term liabilities would be necessary.
    - Currently, instructions on how to determine the amount of AOCI included in the AOCI adjustment require exclusion of assets backing non-life insurance liabilities. Members propose that a determination of AOCI based only on the "more likely than not" criterion would provide a more accurate view of what is expected to be realized, and that the determination should not be based on product type. Assets are purchased so that the overall entity's asset portfolio matches the overall entities cash flow needs. By introducing a generalization based on product type the IAIS is incorporating unrealized gains/losses which are not likely to be realized.
- Moreover, in the view of some members, a dampener to short-term equity movements could be examined as well.
- The need for an appropriate calibration level. The targeted level of calibration of the ICS is identical to the calibration of some other regimes, yet stresses and the approach to the discount rate term structure seem to differ on important points. The reasons for such deviations should be explored in the work going forward.

We recognize and appreciate that the IAIS is seeking to address the issue of excessive short-term volatility in the consultation. However, the overwhelming majority of member companies, including all of the G-SIIs, think that more efforts need to be undertaken in order not only to address short-term volatility issues, but also to do it in a way that promotes comparability of valuation approaches and supports the insurance business model. Together, the IAIS and the industry should analyze how, under both approaches, the short-term volatility problems can best and consistently be resolved.

IV. Capital resources should take into account local regimes

Surplus notes should be included in Tier 1 capital resources for all insurance firms, not subject to limitation. This issue is particularly important for U.S. mutual companies where, unlike stock companies, mutuals cannot raise capital through stock issuance. In contrast to companies with a holding company parent (whether a mutual holding company or stock company), mutuals also cannot issue senior debt and downstream proceeds to add to capital at the insurance entity level. So, in order to attract capital, particularly in times of financial distress, mutual insurance companies and their regulators rely on surplus note issuances. Foundation funds (Kikin) in Japan have similar features as surplus notes, and Kikin should also be included in Tier 1 capital. Hence, the IIF/GA support paragraph 264 (including surplus notes and Kikin examples) in the consultation document. This would allow mutual IAIGs to issue Tier 1 capital, but suggest that the suitability criteria may refer to ICP 17.11.2 not to make capital resources for IAIGs too prescriptive.

1. *Restrictions on financial instruments*

Based on the specifications of the field test, it is clear that the capital resource resulting from the current structure does not recognize the strength of balance sheets when compared to existing globally accepted regimes. In particular the restrictions on financial instruments are not in line with instruments currently in place and in particular the procedures for determining tiering, maturity and amortization are still too immature and onerous as they appear to collate the restrictions of all bases rather than selection of a suitable basis. A specific case in point is the approach on subordinated debt raised at the holding company level which is ”structurally subordinated” to policyholders by means of being pushed down to subsidiaries which is currently not deemed eligible within the ICS framework.

2. *Encumbrances*

The introduction and description of the charge for encumbrances does not allow for the underlying liquidity/transferability of funds at the balance sheet date and as such does not reflect the level of loss-absorbing capacity of such excess assets. The current ICS proposal requires capital resources to be absent of encumbrances to be deemed eligible (either Tier 1 or Tier 2). The IAIS could undertake improvement on this issue. Members agree that further work needs to be done on encumbrances.

3. *Transitions and timetable*

The ICS proposes restrictions on financial instruments that differ from the current stock of assets in place in the industry in several cases. Existing capital resources should receive grandfathering treatment, and a

clear statement on this would be an essential improvement to aid engagement in this process. We believe that inclusion of transitional measures from existing regimes and grandfathering should be included immediately and the duration for which transition measures apply should be sufficiently long beyond legal implementation of these measures to allow for an orderly run-off of such grandfathered instruments.

V. Other elements of the ICS must be addressed

1. *MOCE*

For the overwhelming majority of IIF/GA members, including all of the G-SIIs, the introduction of the MOCE is a key concern and they question its relevance in the context of the ICS. These members doubt there is an economic rationale for a MOCE to be applied if the current estimates and capital requirements are properly defined. Moreover, these members believe that the MOCE merely acts as another layer of capital in addition to the 99.5% VaR requirement. Not only does this result in significant over-calibration of the ultimate ICS outcome, it could undermine the intention to create comparability of outcomes. These members would recommend that no MOCE provision be developed for inclusion in the ICS.

The above mentioned overwhelming majority consider that, in the ICS, balance sheet valuations should be based on best-estimate assumptions for future liability cash flows, with any potential unexpected losses covered by capital requirements. Consequently, many members believe it should not include a MOCE.

However, a few member companies have a different view and see a rationale for the MOCE, to account for the production cost of the liabilities including the cost of capital.

2. *Calibration*

The ICS is supposedly calibrated on a 99.5% 1-year VaR confidence level, or to target 1-in-200 year events – despite major differences to other regimes applying the same confidence level. The IIF/GA are of the opinion that there is a material risk that the actual calibration level of the standard will be higher than the targeted level. In jurisdictions applying an approach similar to the proposed ICS, a ladder of regulatory intervention will often be used, implying that a "hard regulatory target" would be set significantly below the 1-in-200-year event, leading to the triggering of supervisory intervention if a solvency control level in the ICS is reached.[7] In other words, the 99.5% confidence level would only set a "soft target" for group capital levels.

By way of example of an overly conservative calibration of the ICS, the longevity shocks are excessive since they do not take into account the 1-year horizon (e.g. the changes in the longevity trend are not observable over 1-year horizons and therefore not applicable in a 1-year calibration) and with the trend and level shocks simply added together ignoring diversification. Similarly, the Underwriting Risk modules for P&C businesses do not reflect the portfolio construction of large international companies. Related to this, use of a fully loaded premium basis such as exists under U.S. GAAP will lead to an overstatement of exposure within a common ICS framework.

[7] See ICP 17.3 in IAIS, "Insurance Core Principles," Basel, November 2015.

Also, the magnitude of the U.S. interest rate shock used in the ICS for 2016 Field Testing is calibrated well above a 99.5th percentile instantaneous move. Historical analysis shows this magnitude has never occurred in the U.S. on an instantaneous basis, even when interest rates were at historical highs. Having an interest rate shock applied on an instantaneous basis does not recognize prudent risk management, such as dynamic hedging of interest rates which rebalance positions as interest rates move. The IAIS should revise the interest rate stress approach to make the stress interest rate level dependent and either modify the application to be a stress over a year's time, allowing recognition of risk management practices, or re-calibrate the 99.5th percentile to more appropriately reflect an immediate shift in the yield curve.

It is critical to recognize that, while the ICS is intended to be a minimum standard for group capital requirements, it can be topped up by local decisions. This also raises concerns about the level of calibration.

3. *Risk mitigation*

- Due account must be taken of tools like rolling hedges. Stresses in the ICS should be applied over a period, as calibration is difficult based on instantaneous stresses. Stresses applied over a period better account for rolling hedges.
- The ICS should take into account the economic benefits of reinsurance contracts. The definition of a reinsurance contract needs to facilitate this.
- As a general principle, the benefit of management actions in section 6.5 should be allowed for where the IAIG has the ability to amend the premium where appropriate. In this context the definition of management actions should be extended to allow for the appropriate premium increases for business on (re)insurance contracts other than health where the features of those contracts allow for such premium increases. Where the premium increases are economically justified in line with the nature of the contract they should not be subject to a cap.
- We support the diversification credit in the ICS proposal, because this would encourage the insurance companies diversifying their product mix and investment portfolios.

4. *Contract boundaries*

- While the IIF/GA recognizes that conservatism in a prudential context is appropriate, the majority of our members have consistently argued against the application of a strict legal definition of contract boundaries to renewable life insurance products, including short-term products, for balance sheets that are designed to be economic in nature, like the ICS balance sheet. Even where contracts are short-term, insurance companies manage this business with an expectation of renewals and the data is deep and credible in considering the likelihood of renewal.

  The ICS MAV approach is an economic approach based on realistic, best estimate assumptions and observable data. The GAAP plus adjustments approach will similarly lead to a valuation of liabilities on a best estimates basis. Applying a strict legal/accounting definition of contract boundaries is inconsistent with this economic approach.
- Most members believe strongly that the current contract boundaries definition should be amended and reflect economic reality based on a current estimate basis in line with all other elements of the current estimate. Such an amendment would avoid that cash flow projections are

artificially cut short and more importantly, that the risk profile is properly reflected (e.g. risks are not hidden). It would also reduce complexity as it would require companies to run additional scenarios to account for the strict contract boundaries definition.

- Other members would not advocate for increasing contracts boundaries as they are a necessity to impose some restrictions to complexity and limits as to what can be envisaged and modelled within reasonable plausible ground. A corollary to that is that the ICS shocks should have exposure remits consistent with those of the prudential balance sheet.

5. *Operational considerations*

The current ICS calls for data mappings that are not established for most undertakings and groups. As such the mapping of exposures to what are granular factors leads to significant scope for measurement error. The alternatives for implementation would appear to be either a move to more simplified buckets and lower calibrations or to a more bespoke basis of exposure measurement as reflective of a company's own mappings and rating factors. There are further operational considerations emerging as we go through each field test, for example the ability to measure encumbrance using an ICS basis of presentation, consideration of how DAC adjustments can flow down to reserves at the level of each capital segment. As these operational considerations mount up it becomes more important to consider the cost-benefit of the regime.

VI. The ICS should avoid creating material unintended consequences

In line with ICP 17.2.4, the ICS should be developed with full consideration of the consequences for the wider economy, society and financial markets. As currently envisioned, the ICS could have material unintended consequences at odds with its stated objectives of increasing comparability of insurance regulatory regimes, strengthening policyholder protection, and contributing to financial stability.

In its current form, the ICS includes redundant layers of conservatism – valuation, MOCE, stress design and calibration – that likely would lead to increased costs for policyholders and/or reduced availability of insurance cover. This will be detailed by some insurance groups in their responses and field testing results.

The current ICS framework also does not appropriately incentivize ALM and diversification. Insurance is often long-term in nature, while the ICS takes a short-term perspective in assessing a group's solvency situation. Many of our members believe that a valuation approach that does not pay due attention to insurer's business models, including by mitigating the impact of short-term volatility in financial markets, could lead to pro-cyclicality and impair the ability of the industry to provide long-term retirement products and stable, long-term investing.

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The Joint IIF/GA ICS Task Force is strongly committed to continuing the constructive dialogue and cooperation with the IAIS. Given the number of critical issues highlighted and given the wide range of views expressed reflecting jurisdictional specificities, the Task Force members believe that a direct

dialogue between policymakers at the IAIS and stakeholders is essential and appreciate the IAIS' willingness to continue these interactions.

The IIF and GA stand ready to provide additional views or clarifications. Should you have any questions on the issues raised in this letter, please contact the undersigned.

Very truly yours,

George Brady　　　　　　　　　　　　　　　　　　　　Anna Maria D'HULSTER