

# Client Update

## IAIS Issues Second Consultation on Global Insurance Capital Standard

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On July 19, 2016, the International Association of Insurance Supervisors (the “IAIS”) published its second public consultation document (the “ICS 1.0 Consultation”) on a group-wide, consolidated risk-based Insurance Capital Standard (“ICS”) for internationally active insurance groups (“IAIGs”).<sup>1</sup>

The ICS 1.0 Consultation is a significant step in the multi-year IAIS process to develop global regulatory capital standards for the largest insurance groups: global systemically important insurers (“G-SIIs”) and IAIGs.<sup>2</sup> It follows the publication of the first ICS consultation in December 2014 (the “2014 ICS Consultation”) and subsequent field testing. The document focuses on technical aspects of the ICS, while acknowledging that important strategic and implementation issues will be considered in the next public consultation, which is scheduled to be published in mid-2018. The ICS 1.0 Consultation invites stakeholders to provide feedback on 235 questions by October 19, 2016. In its continuing effort to engage a broad range of stakeholders, the IAIS held a public background call on the ICS 1.0 Consultation on July 27 (the “ICS Call”).

The ICS 1.0 Consultation makes clear that the IAIS is planning to maintain its timetable of finalizing the ICS for effectiveness (subject to adoption by local

<sup>1</sup> IAIS, *Risk-based Global Insurance Capital Standard Version 1.0: Public Consultation Document* (July 19, 2016), available at <http://www.iaisweb.org/page/consultations/current-consultations/risk-based-global-insurance-capital-standard--second-consultation/file/61557/2016-risk-based-global-insurance-capital-standard-ics-consultation-document> [hereinafter ICS Consultation].

<sup>2</sup> Under the IAIS Common Framework for the Supervision of IAIGs (“ComFrame”), an insurance group is an IAIG if it meets the following criteria: (1) international activity – premiums are written in not fewer than three jurisdictions and the percentage of gross premiums written outside the home jurisdiction is not less than 10 percent of the group’s total gross written premium and (2) size – based on a rolling three-year average, total assets are not less than \$50 billion or gross written premiums are not less than \$10 billion.

jurisdictions) in 2019 and continues to give serious consideration to a market-adjusted valuation approach, while noting that most of the U.S. stakeholders commenting on the 2014 ICS Consultation expressed a preference for the alternative, GAAP with adjustments, approach. This latest IAIS consultation overlaps with the exposure by the U.S. Federal Reserve Board of very different proposals for group-wide capital measures for the insurance groups under its jurisdiction. The deadline for comments on the Federal Reserve Board proposals was recently extended to September 16, 2016.

We provide a summary of the key aspects of the ICS 1.0 Consultation and future process below.

## I. CONSULTATION CONTENT

The ICS 1.0 Consultation addresses five primary issues: (i) the approach to valuation of assets and liabilities to be used in the new standard; (ii) the factors to be followed for determining qualifying capital resources; (iii) the nature and composition of the ICS capital requirement, including calculation methodology; (iv) the scope of the group to which the ICS applies; and (v) preliminary considerations for a holistic approach to tax. The ICS 1.0 Consultation closely tracks the approach taken for 2016 field testing. The ICS 1.0 Consultation clarifies that the ICS will serve as a Prescribed Capital Requirement, which is a minimum capital level. The document notes that local regulators may choose to require insurance groups to hold higher levels of capital.

*Valuation Approach.* The IAIS continues to field test two primary valuation approaches: (i) market-adjusted valuation and (ii) GAAP with adjustments. Both approaches will be contained in the ICS that will guide the first round of confidential reporting, in 2017. In addition, the IAIS likely will continue to test alternative approaches for various components of the ICS.

*Capital Resources.* The classification of qualifying capital resources into tiers remains substantially similar to the Basic Capital Requirement's classification scheme for G-SIIs.<sup>3</sup> Issues on which the IAIS seeks comment include (i) the treatment of various items, such as Accumulated Other Comprehensive Income ("AOCI") and net pension plan surplus assets and (ii) how to set appropriate capital composition limits. The ICS 1.0 Consultation notes the challenges

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<sup>3</sup> See IAIS, *Basic Capital Requirement for Global Systemically Important Insurers* (Oct. 23, 2014), available at <http://www.iaisweb.org/page/supervisory-material/financial-stability-and-macroprudential-policy-and-surveillance/file/34540/iais-basic-capital-requirements-for-g-siis>. For a detailed discussion of the final BCR, please see our October 31, 2014 [Client Update](#).

associated with fitting financial instruments, such as surplus notes and foundation funds, issued by mutual insurance groups into the tiered capital resource framework and specifically requests input on the ways in which the framework can account for these instruments.<sup>4</sup>

*Capital Requirement.* As with the 2014 ICS Consultation, the bulk of the ICS 1.0 Consultation and its questions focuses on the nature and composition of the capital requirement component of the ICS, particularly the risks covered and the calibration methodology.

*Scope.* The ICS 1.0 Consultation seeks feedback on whether additional clarification is needed to define the concept of an insurance-led financial conglomerate. Such an entity's consolidated balance sheet forms the basis for the scope of the group.

## II. PROCESS

The IAIS has opened the ICS 1.0 Consultation to public comment until October 19, 2016 and simultaneously intends to engage in field testing, focused on calibration, through October 2016. Forty-two companies are participating in the voluntary 2016 field testing as compared to a cohort of thirty-four companies, predominantly from the life insurance sector, that participated in the 2015 field testing. ICS Version 1.0, which will be based on this consultation document, is scheduled to launch for confidential reporting to group supervisors in mid-2017 with data due in Fall 2017. The ICS Call described this first round of confidential reporting as a "natural extension" of field testing, and the IAIS expects to further refine the ICS based on the experiences of confidential reporters. It was noted on the ICS Call that the IAIS aspires to have full IAIG participation in the upcoming confidential reporting round, thereby allowing the IAIS to "assess the appropriateness of the ICS for different risk profiles."

While the confidential reporting process is underway, the IAIS will work to address key strategic issues omitted from this ICS 1.0 Consultation, including whether internal models will be used, how to implement the ICS and the relationship between the ICS and other local capital requirements at the legal entity and group levels.

Publication of the comprehensive IAIS Common Framework for the Supervision of IAIGs ("ComFrame") consultation, which will include ICS Version 2.0, is scheduled for mid-2018 and coincides with the launch of the 2018 confidential

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<sup>4</sup> ICS Consultation at 81-82.

reporting process. Data from the confidential reporting process and comments on the consultation of ICS Version 2.0 will be due in Fall 2018. ComFrame, including ICS Version 2.0, is expected to become effective beginning in 2019, following adoption by individual jurisdictions.

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Please contact any of the Debevoise lawyers named above if you have any questions.