

## NAIC's Interpretive Guidance on ICS Comparability Assessment Framework

The International Association of Insurance Supervisors (IAIS) recently agreed on a definition of comparable outcomes and an overarching approach to guide the development of high-level principles and criteria for assessing comparability. The following provides some explanation of each main point under the comparability assessment heading (Part 7) of the IAIS Explanatory Note on the Insurance Capital Standard (ICS) and Comparability Assessment. Initially, the IAIS planned to make public only a definition, so the NAIC appreciates inclusion of the overarching approach, as this provides an important basis for moving into the monitoring period.

### ***Definition of comparable outcomes***

Comparable outcomes to the ICS means that the Aggregation Method (AM) would produce similar, but not necessarily identical, results over time that trigger supervisory action on group capital adequacy grounds.

- Limits the definition to a “trigger” (i.e., binary yes/no, on/off) based on the definition of PCR in ICP 17.4 (*a solvency control level above which the supervisor does not intervene on capital adequacy grounds*).
- Accepts that AM will not necessarily produce identical results (i.e., a ratio) to the ICS. Comparison is between methods of assessing capital adequacy and not IAIG results. Given our concerns about the ICS being an overly volatile benchmark, this looks at the results over business cycles rather than at each and every point in time. Avoids a concept of the “extent of the need” for supervisory intervention, which would have required the comparability assessment to consider not only whether the AM and the ICS both provide a trigger (i.e., binary yes/no, on/off), but also whether the trigger reflects a similar signal of the magnitude of the strain on the group solvency position. Team USA objected to any language relating to the extent, intensity or the magnitude of such a trigger to avoid a quantitative comparison of the amount of the shortfall in group capital.
- There is a common understanding recognizing that supervisory intervention can take varying forms and degrees, appropriate to the circumstances.

The IAIS will develop high-level principles and criteria in such a manner that the AM is neither precluded at the outset as an outcome equivalent approach to the ICS for measuring group capital, nor given a free pass.

- Adopts Team USA's objective of setting “Ground Rules” for the overall process as discussed at the October stakeholder session at Treasury.
- Allows the AM to be considered a viable alternative to the ICS for measuring group capital and confirms that fundamental parts of the AM (including reliance on local valuation and capital requirements) are here to stay. Inclusion of “at the outset” confirms that the intention is not to have principles or criteria that are designed to preclude AM from ever being assessed as outcome equivalent to the ICS. The KL Agreement makes it clear that the AM could be considered comparable, so comparability criteria cannot be designed in a way that makes compliance impossible.

***Developing high-level principles and criteria for the comparability assessment will take into account:***

1. Analysis of the responsiveness of the ICS and AM to changes in conditions over time, including economic and financial market conditions over the business cycle, not short-term market fluctuations.
  - Highlights that the comparability assessment looks at responsiveness of the group solvency approaches over business cycles rather than at each and every point in time. Also acknowledges that the assessment will consider results over time rather than in response to temporary market movements.
  - Rather than refer to “stress situations” and various phrases that would force the AM to recreate the volatility inherent in a market-based valuation (MAV) (e.g., at a point in time), focuses on results over the business cycles, which may include sustained economic or market downturns, but not temporary market movements.
2. Analysis of individual elements of a group solvency approach, ie valuation, capital resources, and capital requirement (including range and level of material risks) to support the assessment of comparable (i.e. substantially the same) outcomes, while recognizing that the decision on comparable outcomes will consider the elements in totality.
  - Rejects a granular approach to a comparability assessment and instead recognizes that the comparability assessment is outcomes-focused, considering the elements in totality rather than individually.
  - Permits other tools/authorities to help demonstrate comparability (i.e., a particular risk component of the ICS is captured elsewhere in the group solvency approach rather than specifically in the AM itself or does not measure the risk in the same way).
  - Use of “group solvency approaches” allows for application of the definition and overarching approach to the outcomes produced by GAAP Plus and Internal Models. The KL Agreement calls for a decision on inclusion of GAAP Plus and Internal Models as viable options for the ICS by the end of the monitoring period, but no decision has yet been made. The outcomes their use produces will be assessed as well because they also do not get a free pass.
3. The prudence of the AM in relation to the ICS, recognizing that the latter will be a minimum standard and other standards could be more but not less prudent than it.
  - Recognizes that the ICS provides minimums, but allows flexibility in how such minimums are achieved, including doing more. Example of how the AM is more prudent: Scaling ensures that the required capital is comparable across legal entities and at an appropriate level, and because there is no diversification when legal entities are aggregated, the final result under AM will be more conservative but still comparable to the ICS.
4. The scope of the group included under AM and ICS, consistent with that set out in ComFrame.
  - Adopts Team USA’s objective of defining “Scope of Group” as discussed at the October stakeholder session at Treasury. Comparability assessment will consider whether the AM and the ICS capture those entities within the corporate structure that could pose material risk to the insurance operations.

5. The extent, quality and scope of information on ICS and AM, required across different business models, that is sufficient to deliver the comparability assessment.
  - Rejects any notion that U.S. IAIGs would be required by the IAIS to participate with the reference ICS during the monitoring period. Also omits reference to “strongly encouraging” IAIGs to participate with the reference ICS. U.S. IAIGs may report on the reference ICS and/or the AM during the monitoring period, based on discussions with the relevant GWS.
  - Removes suggestion of a unilateral and subjective determination by the IAIS as to whether data submitted through participation by IAIGs in the monitoring period is sufficient to deliver the comparability assessment. Team USA rejected any precondition to delivering the comparability assessment (i.e., insufficient data, comparability assessment not completed).
6. The levels of transparency of the group solvency position of the IAIG under the AM and ICS.
  - Adopts Team USA’s objective for transparency in the overall process as discussed at the October stakeholder session at Treasury.
  - Consistent with ICS Principle 9 (*ICS is transparent, particularly with regard to the disclosure of final results*). Having transparency is key to providing mutual understanding and greater confidence, thus it should not be assumed that any form of implementing the ICS (including GAAP Plus, Internal Models, etc.) automatically provides the level of transparency expected.

Additionally, the IAIS will include opportunities for stakeholder engagement through public consultation.

- Adopts Team USA’s objective for transparency in the overall process as discussed at the October stakeholder session at Treasury.

As noted under #2, although the KL Agreement calls for a decision on inclusion of GAAP Plus and Internal Models as viable options for the ICS by the end of the monitoring period, no decision has yet been made. Similar to AM, these should not be precluded but also do not get a free pass. The outcomes their use produces will be assessed following a process laid out in the holistic work plan and timeline. The definition and overarching approach described for the AM seem equally applicable to such an assessment and should be taken into consideration for this process.