

NAIC's Symposium on Supervision of Internationally Active Insurance Groups

Atlanta, Georgia

July 15-16, 2010

On July 15-16, 2010, the NAIC sponsored a symposium on supervision of internationally active insurance groups (IAIGs), which was held in Atlanta, Georgia. The symposium had 46 attendees consisting of U.S. insurance regulators, industry representatives from internationally active insurance groups, three participants representing the jurisdictions of Canada, Bermuda, and Switzerland, and NAIC staff.

The symposium was designed to promote the free exchange of thoughts and ideas on how internationally active insurance groups manage group-wide risk, how regulators currently regulate internationally active insurance groups, and what best practices could be identified based on the exchange of thoughts and ideas between panel members and audience participants.

Two panels were established as part of the symposium: an industry panel consisting of four representatives (four different internationally active insurance groups) and a regulator panel consisting of two U.S. regulators and two regulators representing Canada and Bermuda. Each panel was presented with a set of prepared questions that was followed by questions from audience participants. After the panel discussions, four breakout groups were assembled that focused on specific themes regarding supervision of internationally active insurance groups. The moderators were Terri Vaughan (CEO of the NAIC) and George Brady (Manager, International Division).

Industry Panel

The industry panel members expressed diverse views on how group-wide risks are managed in their companies. Some of the comments expressed included:

1. The only risk manager is the CEO. The responsibility of risk management is placed on the CEO of each business group within the whole group.
2. While risk management is centralized in the home office of the parent company, each company is still locally accountable.
3. To eliminate differences in accounting standards, the group uses a market or economic valuation approach to their business.
4. There are firm limitations on the extent of exposure that can be written.
5. In developing a common framework, actuarial dashboards have been created.
6. The Board can override the CEO (e.g., if the board doesn't want to write a new product).
7. The Board establishes the risk appetite of the firm. The Board establishes limits not dependent on modeling. Static limits are reset every 3-5 years. The Board sets the minimum amount of economic capital necessary to obtain a certain rate of return.
8. The group risk manager is responsible for establishing the framework. The group actuary sets the reserves and reviews the work of the business unit actuary.
9. The Chief ERM officer reports to the CEO. The Chief ERM officer leads the ERM committee (who reviews the risk at the holding company level).
10. The insurer has a decentralized risk management function.
11. Asset management and international operations have their own risk management functions.
12. Rate of return (profit) is not the role of the ERM officer.
13. The Board meets with key managers once a year and they also meet with the audit committee.
14. The Board members have their own staff which are the experts.

15. The Board consists of 50% US members and 50% Europeans. There is an annual education requirement.
16. Twice a year the risk managers go through the top risks with the board members. Key managers are delegated to educate boards on certain risks.
17. On models:
 - We don't create models, but we perform actuarial studies and over the years have more and more data. You have to understand your book of business.
 - Models during the financial crisis worked well on the life side. Management knew where they were, and if X happened, where they would be tomorrow. Mistakes made were in how models were used and relied upon.
 - We use models, but don't rely on it for total risk management.
 - There is no one model...but the use of multiple models brings a better perspective.

Regulator Panel

The regulator panel also expressed different views on how IAIGs are supervised. Some of the comments made by regulators/supervisors included:

1. One supervisor commented that a framework for insurance group supervision was adopted a few years ago, and were now developing legislation on corporate governance.
2. Another supervisor commented that its life companies are supervised at the holding company level.
3. Supervisors generally agreed that its legal structure for supervision is at the solo entity basis. Holding company laws have generally worked well in regulating transactions among affiliated parties.
4. The U.S. has a national system for solvency regulation, but enforcement is conducted at the state level.
5. There should be a focus on outcomes, and not on how we get there. Commonality and differences among supervisory systems are good.
6. We shouldn't say that everything we do (from a supervisory perspective) is the best; there are aspects of supervision that are done better by others, and we should be willing to consider adopting some of those practices to make our supervisory system better.
7. We should consider the group supervisory framework being adopted by Australia.
8. Supervision of IAIGs is not a "one size fits all" approach.
9. The U.S. system of insurance regulation is evolutionary; Europe's system of insurance regulation is revolutionary. The U.S. needs to better communicate its evolutionary perspective.
10. Reliance on capital strength and availability outside of the insurance group has not always been dependable.
11. There is significant value in the appropriate use of supervisory colleges. It forces communication, understanding the company, and understanding what/why supervisors are doing.
12. We have to make sure that whatever group supervision framework we create is realistic and relevant to the risks that we face. It's important that we not create a group supervision framework that goes well beyond the risks that are present.

Breakout Groups

The four breakout groups dealt with the following themes:

- 1) Breakout group #1: What are some of the “best practices” that could be developed for supervision of IAIGs?
- 2) Breakout group #2: What are some of the jurisdictional issues and challenges facing supervision of IAIGs?
- 3) Breakout group #3: What should be the role of an Own Risk and Solvency Assessment (ORSA) in the supervision of IAIGs, and what would an ORSA include?
- 4) Breakout group #4: What should be the role of corporate governance and enterprise risk management in the supervision of IAIGs?

The breakout groups were led by facilitators and each breakout group had a mixture of insurance representatives and insurance regulators. Each breakout group gave a brief presentation at the end of their session. The following represents a summary of the key thoughts and ideas presented by individuals participating in the breakout group sessions.

Breakout group #1: What are some of the “best practices” that could be developed for supervision of IAIGs:

- 1) The use of supervisory colleges:
 - They need to be working meetings; they should include presentations on the entities and how they are regulated; identifying regulatory gaps, develop strategies, and identifying who would be involved going forward. There should be a sense of knowing who/what is going to be done going forward.
 - Responsibilities need to be assigned. On a long-term basis, there should be some sort of peer review.
 - Supervisory colleges can be structured using a multi-tier approach with different levels of involvement and distribution of information.
 - The host jurisdiction needs to be sufficiently prepared.
 - Invited participants should be given appropriate guidance before attending the college.
 - There should be a website that provides the point of contact and other relevant information.
 - The hurdles regarding the use of supervisory colleges are logistics and budget (financing). While the first meeting(s) should be face-to-face, subsequent meetings can be conducted via video conferencing or other technology.
- 2) The creation of a centralized group financials database:
 - Focus on creating financial analytical tools, including both quantitative and qualitative.
 - Focus on intercompany transactions and relationships.
 - Use financial information to identify risks to give supervisors a starting point.
 - Building a financial database is somewhat dependent on having common accounting, but even without common accounting, it’s critical that information be captured on a group-wide basis regardless of the accounting basis.
 - The evolution is towards developing best practices, common accounting and common rules and regulations.
- 3) Understand jurisdictions’ legislation and regulatory practices:
 - Develop a database of key information for regulators to use.
 - We need to better understand Europe’s supervisory process.
- 4) Group supervision is evolutionary, not revolutionary:
 - We do not need to scrap the current regulatory solvency framework.
 - We (jurisdictions) need to understand each other.
 - This entire process needs to provide “value added”.
 - Best practices should be a “minimum standard”.

- We need to develop a common database to identify outliers and risks so that regulators can ask the right questions.
 - This process can develop into a “FAWG-like” peer review.
- 5) We should hold multi-jurisdictional exams:
- Exams can be structured as “targeted” exams.
 - There should be a focus on intercompany agreements and transactions.
 - We should be cognizant of exam costs and strive for efficiency: exams can be partly conducted remotely; we should promote joint discussions to eliminate duplication of effort.
 - There should be information sharing of examination findings among jurisdictions.
- 6) Memoranda of Understandings
- Serious consideration should be given to entering into these agreements.
 - Do the states have the ability to hold sensitive international data confidential?

Breakout group #2: What are some of the jurisdictional issues and challenges facing supervision of IAIGs?

- 1) In conducting oversight of an IAIG, there was considerable discussion as to a group supervisor: should there be one, how do you determine who should be the group supervisor, and what should its role be (legal or otherwise).
- In some cases, the determination of who should be the group supervisor is fairly straight forward; it is determined by the place of incorporation/principal place of business, or premium level. In other cases, it is more complicated than a simple analysis that could result in multiple group supervisors. A practical approach to determining who should be the group supervisor would be to consider combining a mix of circumstances, such as location, headquarters, principal place of business, premium, management, location of capital, and other major aspects.
 - What should be the role/legal authority of the group supervisor? Is it a collaborated coordination function or something that is legally mandated?
 - Under a collaborated coordination: 1) U.S. regulators are extremely familiar with this approach; 2) enforcement is operationalized through group consensus and then from group consensus, enforcement is effected at the local level; 3) review interconnectedness (guarantees and indemnities) and reach consensus for risk decision making; 4) joint exams are also contemplated; 5) better coordination of supervisory colleges and crisis management communication; 6) building trust with other regulators; and 7) is there a level of deference to the group supervisor, or only a deference to delegation of tasks.
 - Under a legally mandated role: 1) should the group supervisor assess corporate governance and if the circumstances warrant it, take action on corporate governance issues; 2) should the group supervisor have the legal authority to act on non-regulated entities?; 3) will the Holding Company act be revised to allow for the expanded role of a group supervisor; 4) will enforcement issues be the responsibility of the group supervisor; 5) will the group supervisor be responsible for reviewing the extent of interconnectedness?; 6) some regulators were in favor of incorporating the lead regulator concept (already in practice) into the Model Holding Company Act; 7) some discussed using some sort of full faith and credit/equivalence and supervisory recognition; and 8) will the group supervisor be responsible for coordinating supervisory colleges and crisis management communication?
- 2) Information sharing and exchange of information:
- This is clearly the starting point for international coordination and cooperation. Regulators discussed the value of MoUs to address some of these issues and some of the challenges to

building a sufficient network of Memorandums of Understanding and other challenges such as state public access laws.

- 3) Resources:
 - There is a question of adequate resources at the state insurance department level in implementing effective group-wide supervision. There should be some recognition that it is not a mere replication of solo level supervision.
- 4) Lack of common qualitative and quantitative standards:
 - There was a unanimous view that we lack common accounting standards, languages, definitions, and corporate governance. Should an international database for financial and non-financial information be created? Should there be supervisory recognition/convergence of international standards? How should unregulated entities be treated?

Breakout group #3: What should be the role of an Own Risk and Solvency Assessment in the supervision of IAIGs and what would it include?

- 1) Own Risk and Solvency Assessment (ORSA) – what’s in a name?
 - Is this only solvency?
 - “Own” means it’s the insurance company’s view. The requirement for an ORSA should not be prescriptive; no template, and no checkboxes;
 - Should include stress, scenario, and reverse stress tests;
 - Should be forward-looking;
 - Should reflect how an insurer identifies and manages risk;
 - Identify key risks; what’s in the existing model, and
 - Consider some prescribed scenarios for comparability.
- 2) Leverage off the existing process; this is already performed by large companies; all companies need to manage risks.
- 3) Tie ORSA to the regulatory risk-focused exam:
 - Must be part of the examination process;
 - Must be part of the financial analysis process;
 - Regulators need to see an ORSA for all companies, not just those that are poorly managed;
 - There is a question of regulatory resources and the required skill set; will more consultants be engaged, or will there be shared resources (“central risk resources”).
- 4) How do you implement ORSA, and how do you keep it confidential? Law, regulation, exam handbook, or part of the Accounting Practices and Procedures Manual?
- 5) Canada Dynamic Capital Adequacy Testing (DCAT) uses scenarios: three most significant risks.
- 6) Property and casualty – catastrophe exposures, modeled losses, what actions are taken?
- 7) Is ORSA applied to only the group, or the stand-alone legal entity as well?
- 8) Is the concept of proportionality applicable?
- 9) Who signs off?
- 10) The “don’t knows” are important considerations; line of business trends can be good information.
- 11) ORSA should never be a “compliance” exercise.

Breakout group #4: What should be the role of corporate governance and enterprise risk management in the supervision of IAIGs?

- 1) We need to define corporate governance and enterprise risk management, including the relationship between the two:
 - Need to consider international work on this subject matter;

- Need to insert our views into the international work stream;
 - Consider the role of the board and its responsibility versus oversight – concerns were expressed with the ability of board members to be responsible for things when they are not the experts;
 - Incorporate this definition and any specific requirements related to corporate governance and enterprise risk management into the regulatory framework (e.g., new model law/regulation, existing models, and inclusion in Examiners Handbook).
- 2) Include enterprise risk management as initial step in regulatory risk-focused examination:
- Spend the first few days interviewing upper management, getting a sense of how enterprise risk management is handled at the company, determining the extent of management’s participation;
 - What documentation should be required of insurers?
- 3) We need to link this assessment to the regulatory risk-focused examination (how does it impact the assessment of risks and controls for specific functions):
- Companies need to know what it means to be found deficient in enterprise risk management areas – are they just best practices? How does this impact the length/costs/frequency of exams?
- 4) Continue in improving the coordination between analysts and field examiners in improving the risk-focused approach to financial surveillance.
- 5) We need to coordinate review of corporate governance and enterprise risk assessment for insurer groups:
- We need access to upper management; begin by contacting the non-U.S. supervisor; if more is needed, work with the U.S. company, but may need to go to the non-U.S. company;
 - Same process for U.S. and non-U.S. groups, but we may need to develop separate rules or criteria for non-U.S. groups.

Conclusion

In summary, the symposium on supervision of internationally active insurance groups was well attended, and offered a variety of viewpoints and excellent dialogue. The regulators benefited from the symposium, and while there wasn’t complete unanimity in all matters discussed, the following summary statements represent a consensus view from the insurance regulators and are worthy of further consideration by the Solvency Modernization Initiative Task Force.

Regarding the supervision of internationally active insurance groups:

- **The use of well organized supervisory colleges is an integral part of group supervision;**
- **An international database for financial and nonfinancial information should be developed;**
- **Serious consideration should be given to establishing joint international financial examinations;**
- **An international “FAWG-like” peer review process should be developed;**
- **Serious consideration should be given to establishing a group supervisor;**
- **Confidential treatment of documents/processes need to be dealt with;**
- **ORSA should be an integral part of the U.S. regulatory process; it should be included within the regulatory risk-focused examination process;**
- **Principles regarding corporate governance and enterprise risk management should be developed; minimal policies of what constitutes corporate governance and ERM should also be developed; regulators need access to the appropriate level of management staff; and**
- **The question of adequate resources must be addressed in order to have an effective group supervisory framework for IAIGs.**