



AMERICAN ACADEMY *of* ACTUARIES

November 22, 2013

Dave Sandberg, Chair
Insurance Regulation Committee
International Association of Actuaries

Re: IAA Comments on *Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame)*

On behalf of the American Academy of Actuaries'¹ Solvency Committee, I appreciate this opportunity to provide comments on the IAA's Insurance Regulation Committee's proposed comments on the IAIS ComFrame paper.

Sincerely,

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Chairperson, Solvency Committee
American Academy of Actuaries

¹ The American Academy of Actuaries is 17,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policy-makers on all levels by providing leadership, objective expertise and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice and professionalism standards for actuaries in the United States.

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Paragraph Reference	ComFrame text	Proposed IAA Comments	Academy comments
General Comments	General Comments	Different sections require demonstrating or analyzing some aspect of the company’s risk management. The document as written could imply a requirement for voluminous reporting that is duplicative of the ORSA. For example, some items listed that would likely be covered in an ORSA include – p. 46 Guideline M2E3-2-8-2, p. 48 Guideline M2E3-3-2-1, Guideline M2E3-3-6-1 and 2 p. 56 Guide M2E4-4-1-2 (U/Wing policy needs a feedback loop to ensure emerging risks are considered) p. 59 Par. M2E4-7-1 Reinsurance strategy should be in ORSA?	The committee ¹ concurs
General Comments	General Comments	One other unaddressed item that emerges is “What is appropriate and what are the consequences of failure? Some examples include p. 52 Parameter & Guideline M2E4-1-1 What is undue reliance? p. 53 Par. M2E4-1-3 p. 56 Guideline M2E4-4-1-3 How to tell if reinsurance program exposes the balance sheet beyond its risk tolerance levels (actually seems redundant, seems to be written more like a notice to the regulator of what to consider). In any case, this is an area where the use of actuarial standards and the IAIS requirements might be helpful. Also, as indicated in the notes, what will be the regulator tolerance for “failure” or weak compliance? In national jurisdictions, there are specific legal powers linked to instances of failure or weak compliance. But, since the IAIS standards do not have legal authority, the actuarial standards might be written to be more of a dialogue and focused on how to improve the company process no matter where the level of compliance exists.	The committee concurs
General Comments	General Comments	Lastly, the guidance seems silent on the specifics of a diversification credit – How will it be handled? It is referenced on p. 50 Guideline M2E3-4-1-2, but not described elsewhere and if (or how) it is allowed.	The committee concurs
General Comments	General Comments	No relevant IAA reference	The IAIS document still includes

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			items in ComFrame Module 2 that are either already in the Insurance Core Principles (ICPs) or should be in the ICPs. A removal of this overlap would provide focus. The IAIS document contains several incidences of this overlap that the final drafting should remove.
Introductory Remarks - 3. ComFrame Hierarchy	Guidelines illustrate practical approaches to implementing the standards and parameters, provide more detail and show how the requirements might be met.	No relevant IAA reference	The ComFrame wording would imply that guidelines should rarely include the word "should." The subsequent paragraphs are inconsistent in this regard. Some follow the concept of guidelines containing non-binding guidance and illustrations, while some include specific requirements. The document should make a consistent decision of the usage.
Introductory Remarks - 6. Preconditions	To carry out the role of a group-wide supervisor as set out under Module 3, supervisors should have ... powers and responsibilities to undertake group-wide supervision and supervisory cooperation	No relevant IAA reference	While the group-wide supervisory powers currently described in Module 3 do not rise to a level of concern at this time, the potential for legal-entity limitations could become an issue should group supervision be defined to include extra-jurisdictional reach.
ComFrame Standard M1E1-1	Supervisors identify whether or not a group qualifies as an internationally active insurance group (IAIG).	No relevant IAA reference	The committee is unsure how this would apply to a decentralized organization. For example, a company with underwriting operations that are completely decentralized and investment operations are centralized. Is this four groups (some of which may be IAIG and some not IAIGs) with common outsourcing, or one group? There may need to be some direction (via a parameter?) on how to handle this. <i>[The Committee is aware</i>

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			<i>of other situations in which not all the insurance operations within a conglomerate were within the "insurance" division, hence Module 1 should address this issue.]</i>
Parameter M1E2-1-2	The group-wide supervisor documents the reasons for the identification of the group as an IAIG	No relevant IAA reference	Should also require the group-wide supervisor to document the reasons for not identifying a group as an IAIG if it would otherwise qualify based on the objective criteria in Element 1.
Parameter M2E1-1-1	The IAIG Profile provides sufficient information to enable the IAIG to determine whether the legal and management structures give rise to any specific risks and demonstrate how such risks are mitigated.	No relevant IAA reference	The discussion of risks and how they are mitigated would be better placed in M2E3 (ERM).
Guideline M2E1-1-1-3	Matters which could give rise to such risks and need to be considered include: ... the ability to restructure the IAIG during, or in response to, periods of stress.	No relevant IAA reference	The committee agrees that this is a major item for evaluating an IAIG's structure. The more intertwined the affiliate relationships within an IAIG, the fewer the options and the more difficult the rehabilitation in the event of a crisis.
Guideline M2E1-1-1-4	... Whatever structure is adopted, the IAIG should consider risks arising from: ...	No relevant IAA reference	This would be better placed in M2E3 (ERM).
Parameter M2 E1-2-1	The IAIG draws up contingency plans... to achieve a) acceptable financial condition and b) protection of all policyholders	No relevant IAA reference	This requirement as worded could lead to action that detracts from the effective handling of problems. The risk is that detailed plans would be drawn up that would be inoperative in times of crisis (due to implicit assumptions about conditions during crisis that may not exist during such times). In general, the more detailed such plans are, the less useful they are.

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			The focus/guidance should be on clearly identifying authority and responsibility, including backups, and identifying a range or categories of options.
Guideline M2E1-2-2-1	... The IAIG outlines what management actions it would take to manage the potential cash flow implications of a stress scenario ...	No relevant IAA reference	Should change "would" to "could." A contingency plan should not overly restrict management's options nor commit them to a single course of action in a time of crisis, as every crisis is different. It is impossible to predict in advance what the environment will be like.
Parameter M2 E2-11	The supervisor requires that there is an effective actuarial function capable of evaluating and providing advice to the insurer regarding, at a minimum, technical provisions, premium and pricing activities, and compliance with related statutory and regulatory requirements.	What is effective? Link to E4 8 What is the consequence if it is deemed not effective?	The committee concurs
ComFrame Standard M2E1-3	The IAIG takes account of the policyholder protection schemes (PPS) that apply to its insurance entities, and how these schemes affect each of the entities in the IAIG.	No relevant IAA reference	The committee is unsure why this is needed in ComFrame. It does not seem to be material enough to mention separately. It should be in an ICP. If it is material for an IAIG, then it would be applied in the IAIG's ERM (under Module 3).
Parameter M2E2-1-1	The IAIG's group-wide governance framework is well documented and contains adequate measures to: <u>address risks arising from or affecting the IAIG</u>	No relevant IAA reference	This would be better placed in the Element 3 (ERM) rather than Element 2 (Governance).
Guideline M2E2-2-	The Governing Body should	No relevant IAA reference	The only thing that seems to be

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3-1	undertake, at least annually, an assessment of how the IAIG, the Governing Body and the Senior Management meet the performance goals and measures adopted.		different here from the ICPs is the requirement for an annual review. According to the hierarchy in the Introductory Remarks, such a requirement should be in the parameter and not in a guideline.
ComFrame Standard M2E2-4	"The supervisor requires the insurer's Board to have, on an on-going basis: an appropriate number and mix of individuals ..., appropriate internal governance practices and procedures ..., adequate powers and resources	No relevant IAA reference	The parameters and guidelines that accompany this standard seem to be rather general and not unique to IAIGs. Therefore, the committee does not see the need for this section in ComFrame.
Guideline M2E2-5-1-1	The group-wide remuneration policy may have a structure which contains elements of group-wide and entity based remuneration policies and practices. ...	No relevant IAA reference	There is no mention in this guideline about conflicts between group-wide versus individual entity incentives, but suggest there probably should be.
Guideline M2E2-11-1-1	The IAIG's group-wide actuarial function <u>should aggregate and review actuarial information at the group level</u> . The form and implementation of a group-wide actuarial function may vary but the outcome is to have an overview of the actuarial activities, functions and risks of the insurers within the IAIG as a whole.	No relevant IAA reference	Suggest modifying: "The IAIG's group-wide actuarial function <u>should include aggregation and review of actuarial information at the group level...</u> "
Guideline M2E2-11-1-2	Further examples of activities that could be carried out by the IAIG's actuarial function include providing advice and opinion on...	No relevant IAA reference	It is clear that these are examples, but would be better if "advice and opinion" were replaced by "advice, opinion, or report." In the U.S., an "opinion" may imply a legal

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			attestation to compliance with legal provisions.
Parameter M2E2-13-1	The IAIG has a consistent group-wide policy for the outsourcing of activities or functions, and <u>retains appropriate documentation for all such outsourcing</u> . It should be accountable at a group level for its outsourcing activities in order to provide control over the process and effectively aggregate the impact they may have on group-wide ERM policy.	No relevant IAA reference	The scope of this parameter is expansive. As worded, it would include outsourcing of the employee cafeteria, grounds maintenance, and other administrative areas with low risk. The committee recommends that it be reworded to require such controls for areas with a potentially material impact on solvency and viability risks. Note: Accompanying guideline also says to "provide for group-wide monitoring and oversight of the outsourced (intra-group or external) activities." This is burdensome for some administrative functions.
Standard M2E3-1	The supervisor requires the insurer's enterprise risk management framework to provide for the identification and quantification of risk under a sufficiently wide range of outcomes using techniques which are appropriate to the nature, scale and complexity of the risks the insurer bears and adequate for risk and capital management and for solvency purposes.	Who decides what is or is not appropriate? Is this defined elsewhere?	The committee recommends the IAA not include in its response a comment on a direct quotation from an ICP.
Standard M2E3-1	The IAIG has a group-wide ERM Framework that addresses all relevant and material risks at both the insurance entity and IAIG	Including that of unknown risks via an emerging risk process.	The committee concurs

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	level and enables the IAIG to assess its solvency requirements.		
Standard M2E3-1	The IAIG has a group-wide ERM Framework that addresses all relevant and material risks at both the insurance entity and IAIG level and enables the IAIG to assess its solvency requirements.	No relevant IAA reference	This document should address how non-insurance entity risk is to be addressed.
Parameter M2E3-1-2	The IAIG comprehensively documents its ERM Framework, emphasizing any differences that may apply to different entities within the IAIG, due to the nature, scale and complexity of the business conducted locally.	No relevant IAA reference	It seems that this would be more appropriate for an ICP itself, as long as an ICP would include a requirement to emphasize the differences between the risks as they apply to entities within an IAIG. While ComFrame may be trying to get additional comparative comments into the ERM documentation, this request might be better appearing in an ICP rather than ComFrame itself.
Parameter M2E3-1-4	The IAIG's ERM Framework is independently reviewed on a regular basis, at least once every three years, in order to ascertain that the ERM Framework itself remains fit for purpose.	What does it mean to be "fit for purpose"? Since the guideline says the review may be carried out by others, how will the reviewers know how to evaluate it?	The committee agrees with the comment and would further pose another question, what are the reviewers independent of?
Guideline M2E3-1-4-1	The review may be carried out by an internal or external body but the independent reviewer should not be responsible for, nor have been actively involved in, the part of the ERM Framework that it reviews.	Is the outcome of the review a "clean bill of health" or a list of red, yellow, green comments or a "What is working well and what needs to be better?"	The committee agrees with the comment and suggests removing the word "independent" here. Since the reviewer may be in the employ of the IAIG, they are not "independent" in the usual context of the word (e.g., "independent auditor").
Parameter M2E3-1-	The IAIG articulates its risk	My highlights – What examples (and professional	The committee concurs

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6	<p>appetite by establishing and maintaining a risk tolerance statement for the group which:</p> <ul style="list-style-type: none"> • sets out its overall qualitative and quantitative risk tolerance and • defines risk tolerance limits that take into account all relevant and material risk, both on an insurance entity and group wide basis. 	<p>literature or notes) are there about qualitative risk tolerances? Qualitative is also used on p. 45 in Parameter M2E3-2-8</p>	
Standard M2E3-2	<p>Within the group-wide ERM Framework, the IAIG develops a comprehensive group-wide ERM policy which addresses the risks on both an insurance entity and group-wide basis.</p>	<p>Who decides whether it does or does not address it? What is the consequence if it is not addressed?</p>	<p>It may not be needed as it seems the group-wide supervisor addresses this.</p>
Parameter M2E3-2-1	<p>Through its group-wide ERM policy, the IAIG defines the basis for how it determines the relationship between the IAIG's risk tolerance limits, regulatory capital requirements, economic capital and the processes and methods for monitoring risk.</p>	<p>No relevant IAA reference</p>	<p>This sentence is confusing and we suggest it should be rewritten for greater clarity: "During the development, statement and testing of its group-wide ERM policy, the IAIG both defines the basis for how it determines the relationships among the IAIG's risk tolerance limits, regulatory capital requirements, and economic capital and also formalizes the processes and methods for monitoring risk."</p>
Standard M2E3-3-1	<p>The framework covers at least the following risks: insurance, etc.</p>	<p>No relevant IAA reference</p>	<p>Since this seems to be a comprehensive list, consider adding "counterparty risk". Counterparties are cited in the guideline, M2E3-3-1-2, that follows.</p>
Guideline M2E3-4-	<p>In conducting its ORSA, the</p>	<p>Are these different from, contained within or in addition</p>	<p>"counterparty risk" should be included</p>

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4-1	IAIG should consider risks arising from insurance and other entities, including non-regulated ones. Some other risks that are important to consider are: • liquidity risk • strategic risk • reputational risk	to the operational risks mentioned in the accompanying Parameter	
Guideline M2E4-2-4-1	The IAIG should also have documented procedures on actions to be taken to affect the cross-border transfer of capital and assets in normal and stressed times.	Will this link to Module 3 on the supervisory need to have similar documentation/preapproval already in place? This will be of little value if regulators will not allow the actions in a time of stress.	The committee concurs
Parameter M2E4-8-2	The group-wide actuarial policy requires an annual actuarial opinion (whether certified or not) to be provided to the Governing Body. This actuarial opinion is forward looking and goes beyond the current balance sheet of the IAIG. It covers at least the following subjects: • the reliability and sufficiency of the technical provisions • the adequacy of reinsurance credit for technical provisions	Reliability and sufficiency will need to be defined to be sure they are applied consistently. This will not be the same as local unit statutory sufficiency if only the central estimate is booked in the consolidated balance sheet (without any risk margins).	In addition, the term "opinion" should be replaced with "report."
Parameter M2E4-8-2	The actuarial opinion includes consideration of non-insurance entities and non-regulated entities.	Is this a well-defined, limited role or can they rely on another expert?	In addition, the term "opinion" should be replaced with "report."
Parameter M2E4-8-2	The actuarial opinion includes consideration of non-insurance entities and non-regulated entities.	Will need to distinguish if and how the purpose of an actuarial opinion differs from an accounting opinion. Direction is needed to clarify if desired outcome is a "clean" opinion, or is more like an assessment/report on	The committee concurs

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		green, yellow, red.	
Parameter M2E4-8-2	The actuarial opinion includes consideration of non-insurance entities and non-regulated entities.	Based on US meaning of opinion, the actuary could not opine on non-insurance or non-regulated entities.	The committee concurs
Parameter M2E4-8-2	The actuarial opinion includes consideration of non-insurance entities and non-regulated entities.	ComFrame is insurance only. These are only relevant to SIFI's. Expectation of this topic? Can the actuary point out the issues without needing to evaluate/quantify the risk? Are they advising the board or providing assurance/reliance to the board?	The committee concurs
Guideline M2E4-8-2-1	The IAIG may use the underlying actuarial reports submitted locally by the individual insurance entities as input to its annual actuarial opinion to the Governing Body.	Is the input an opinion as a statement of reliance to the board, or a documentation of current procedures, shortcomings and plans for improvement? How much would be duplicated in the ORSA? Or can be left out of the ORSA if included here?	The committee concurs
Guideline M2E4-8-2-1	the methodologies used to determine the margin over current estimate (MOCE)s by each insurance entity and the consolidation/aggregation method applied at the group level	The MOCE's are not expected to be calculated, used or determined for the ComFrame balance sheet. All of the Margins will be in the capital.	The committee concurs
Guideline M2E4-8-2-1	Suitability and adequacy of reinsurance/risk transfer arrangements taking into account the strategies for underwriting and claims management as well as the overall financial condition of the IAIG and the Governing Body's risk tolerance.	Is this last item meant to include a requirement to opine on the opinions of the other mentioned functions & policies? How likely would this duplicate an ORSA or could be done here vs. the ORSA?	The committee concurs

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Standard M2E5-1	The IAIG assesses its capital adequacy by comparing its qualifying capital resources to the capital benchmark.	Will it also compare fungibility? Via stress testing???	The committee concurs
Standard M2E5-2	For the purposes of the capital adequacy assessment, the IAIG applies a total balance sheet approach to assess all the material risks to which it is exposed.	Next step is more details on total balance sheet approach – Will it include/exclude deferred taxes, etc.?	The committee concurs
Parameter M2E5-5-2	The IAIG's financial instruments that qualify as core capital do not have a fixed maturity.	No relevant IAA reference	Surplus notes should be a component of core capital even though they have a fixed maturity.
Standard M2E5-6	The IAIG assesses the ability of its capital elements, other than financial instruments, to absorb losses on both a going-concern and wind-up basis.	How is this demonstrated?	The committee concurs
Standard M2E5-7	The IAIG's amount of qualifying capital resources is determined after the application of inclusions and exclusions to reflect that some capital elements' basis of valuation or recognition may not be appropriate for capital adequacy assessment.	How is the appropriateness determined?	The committee concurs
Parameter M2E5-7-4	The IAIG includes in its additional capital ... the DTA's... in a winding-up	No relevant IAA reference	We believe this would be an acceptable resource in a going concern test.
Standard M2E5-8	The IAIG determines the amount of its qualifying	What does this mean?	The committee concurs

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	capital resources subject to limits.		
Standard M2E5-11	In determining the group capital benchmark, the IAIG addresses the key categories of risk (including risk concentrations) which are: insurance risk, market risk, credit risk, group risk and operational risk.	How does it demonstrate that these items have been addressed? Is it implicit or explicit that operational risk (and other similar risks) need capital?	The committee concurs
Standard M2E5-12	The IAIG, for the purposes of calculating its group capital benchmark, uses a scenario-based approach.	What is a scenario based approach? Own capital benchmark or regulator defined benchmark? STANDARD NEEDS TO LINK TO THIS AND WILL NEED INPUT TO BE REVIEWED IN FTTF Project.	The committee concurs
Standard M2E5-13	The IAIG combines the results of the different components of the scenario-based approach in line with the target criteria in order to obtain a group-wide capital benchmark.	Company discretion allowed?	The committee concurs
Parameter M3E1-2-6	The group-wide supervisor assesses the valuation and capital adequacy of the IAIG, as well as its leverage and liquidity.	What criteria are used to “assess”? Is leverage based on total capital or free capital? Setting liabilities at central estimates will portray a less leveraged balance sheet even though the risks are unchanged.	The committee concurs