

# Solvency regulation of insurance companies and risk management of pension funds: U.S. Framework and Processes

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**PENSION SYSTEMS: CHALLENGES AND PERSPECTIVES THE ROLE OF INSURANCE COMPANIES AND PENSION FUND ADMINISTRATORS**

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# Overview

- U.S. Solvency Framework Overview
- Summary of U.S. Risk-Focused Surveillance
- Summary of Group Supervision/Oversight
- Questions

# U.S. Solvency Framework

## US Insurance Regulatory Mission:

To protect the interests of the policyholder and those who rely on the insurance coverage provided to the policyholder first and foremost, while also facilitating an effective and efficient market place for insurance products.

- Flexibility is important in our system
  - Different insurance group structures, products, etc.
  - Allow management freedom unless trouble occurs

# U.S. Solvency Framework

## Solvency Core Principles

1. Regulatory Reporting, Disclosure and Transparency
2. Off-Site Monitoring and Analysis
3. On-Site Risk-Focused Examinations
4. Reserves, Capital Adequacy and Solvency
5. Regulatory Control of Significant, Broad-based Risk-related Transactions/Activities
6. Preventive and Corrective Measures, Including Enforcement
7. Exiting the Market and Receivership

# U.S. Solvency Framework

## 1. Regulatory Reporting, Disclosure and Transparency

- Heavy emphasis on reporting and disclosure
- Used in the continual assessment of risk
- Standardized reporting allows comparability
- Drive offsite and onsite monitoring
- More information requested when needed
- Used with internal company information

# U.S. Solvency Framework

## 2. Off-Site Monitoring and Analysis

- Assess on an on-going basis the financial condition of the insurer (quarterly)
  - Identify/assess current and prospective risks
  - Automated financial analysis tools
  - Use any information to help understand the company and its actions (SEC filings, market conduct reports, rate and policy form filings, consumer complaints, rating agency reports, media)
  - Used to determine need for, and scope of, targeted exams
  - Continual loop between analysis and exam

# U.S. Solvency Framework

## 3. On-Site Risk-Focused Examinations

- Full scope exam performed at least once every 5 years
- Focus on the ability of company controls and processes to limit current and prospective solvency risk
- Include a review of corporate governance and ERM processes
- Develop detailed findings and recommendations to communicate to company and to assist in ongoing analysis process
- If issues exist, more frequent full scope or targeted exams occur

# U.S. Solvency Framework

## 4. Reserves, Capital Adequacy and Solvency

- Requirements in place for insurers to utilize credentialed actuaries to issue an opinion on the company's reported reserves
- Risk-Based Capital (RBC) requires capital based upon the specific risks of the insurer (asset, underwriting, reserving) as opposed to fixed dollar amounts (which still exist as minimum start-up capital)



# U.S. Solvency Framework

## 4. Reserves, Capital Adequacy and Solvency

<b>RBC Ratio</b>	<b>Action Level</b>	<b>Description</b>
>301%	No Action Required	N/A
201% - 300%	Trend Test Level	Act as if CAL triggered
151% - 200%	Company Action Level (CAL)	Company submits an RBC Action Plan
101% - 150%	Regulatory Action Level	Commissioner may order specific corrective actions
71% - 100%	Authorized Control Level	May place insurer under regulatory control
≤70%	Mandatory Control Level	Must place insurer under regulatory control

# U.S. Solvency Framework

## 5. Regulatory Control of Significant, Broad-based Risk-related Transactions/Activities

- Certain significant broad-based transactions require separate treatment
  - Licensing Requirements – Gateway to business
  - Investment Limitations – Risk to company's assets
  - Change in Control - Can impact strategy & direction
  - Extraordinary Dividends – Release of capital
  - Transactions with Affiliates – Subject to abuse
  - Reinsurance – Often material and subject to abuse

# U.S. Solvency Framework

## 6. Preventive and Corrective Measures, Including Enforcement

- In addition to authority granted through RBC, U.S. supervisors have broad authority to require corrective action when a hazardous condition is identified
- Corrective examples include:
  - Requiring the insurer to file interim financial reports
  - Reducing, suspending or restricting the volume of business being accepted or renewed by the insurer
  - Limiting or withdrawing the insurer from certain investments or investment practices

# U.S. Solvency Framework

## 7. Exiting the Market and Receivership

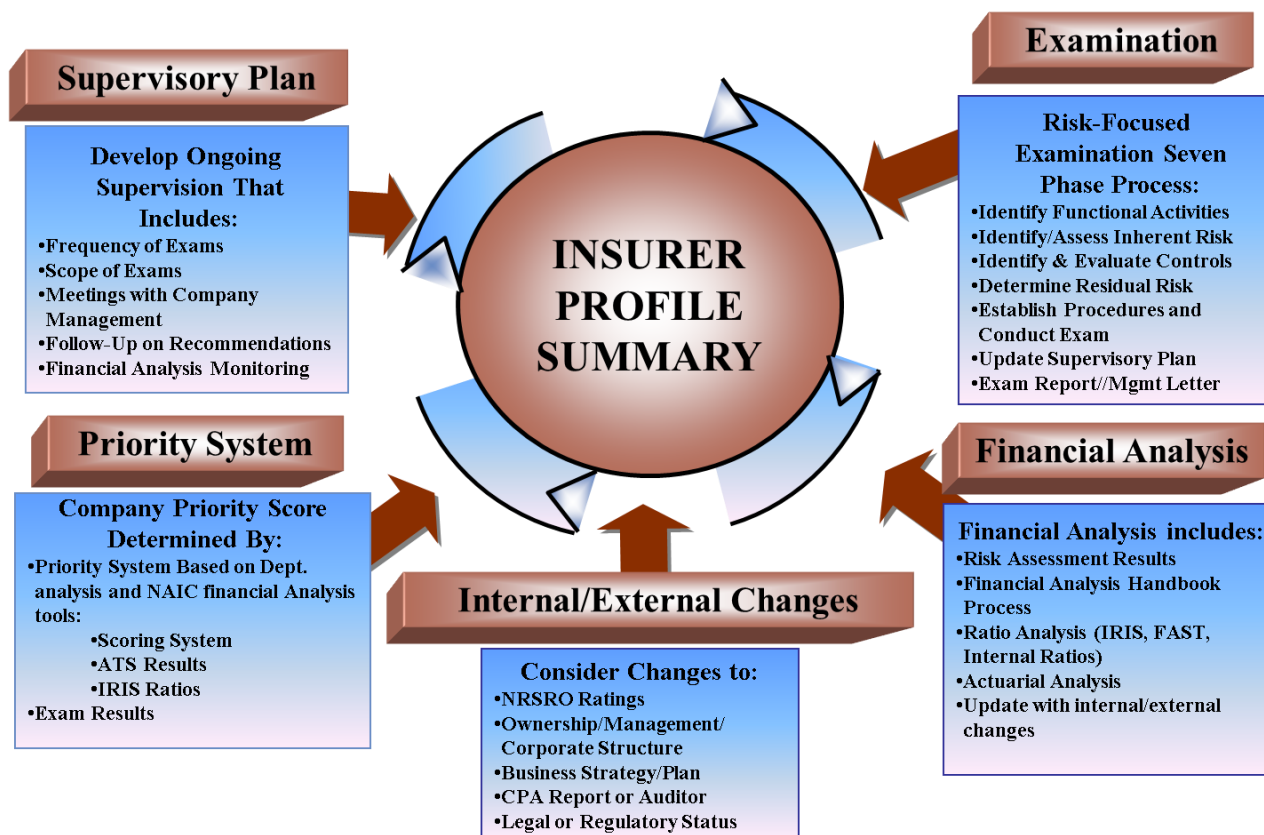
- Receivership law examples include:
  - Mergers, acquisitions, reinsurance
  - Arrangements, non-renewal of part or all of the insurer's book of business
  - Allowing the insurer to be placed in run-off mode under its own management
  - Priority of claims and guaranty funds

# U.S. Risk-Focused Surveillance

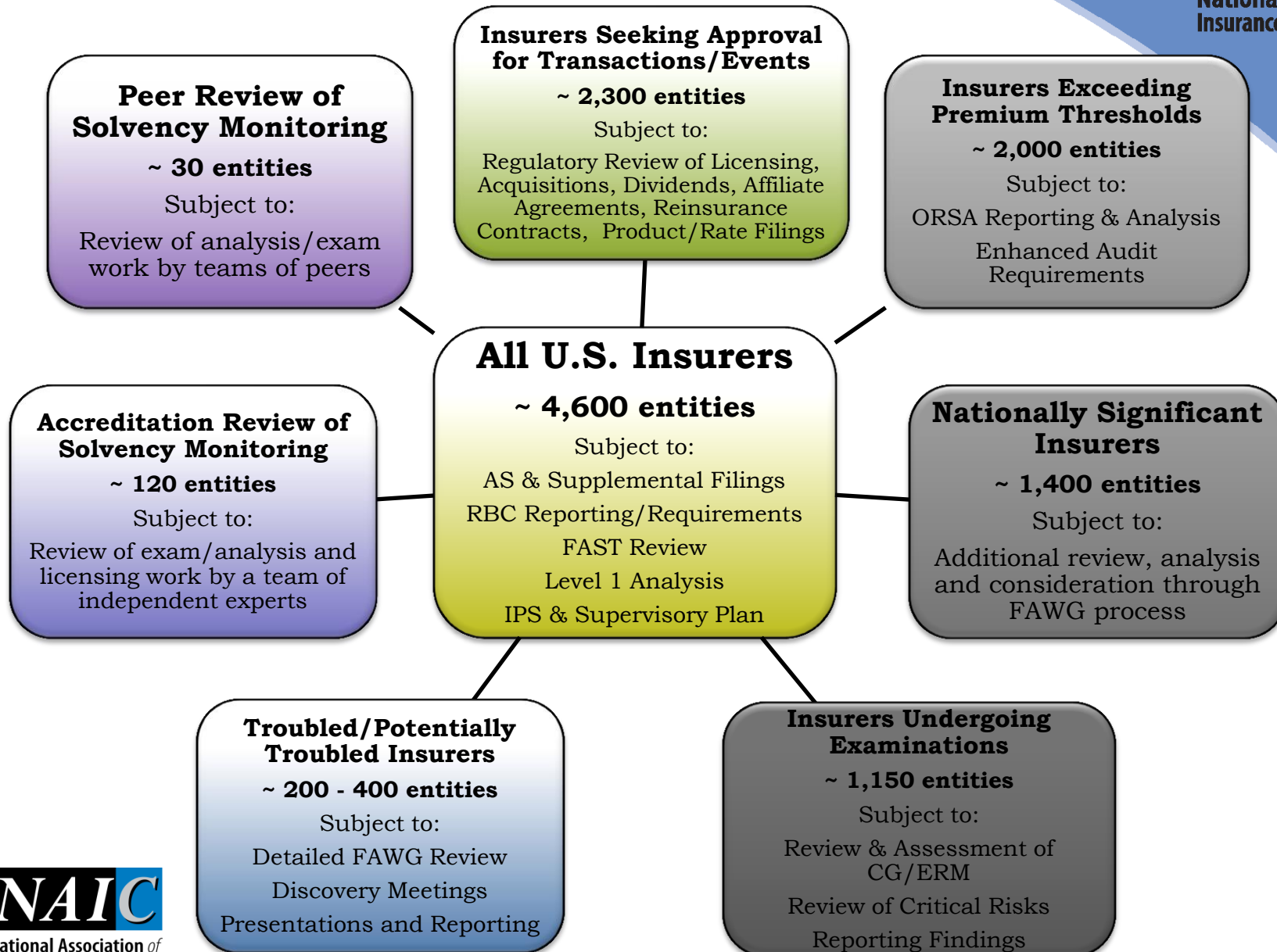
- Primary surveillance activities:
  - Annual and quarterly financial analysis
  - Full scope and targeted on-site examinations
- The intent of risk-focused surveillance is to identify and assess risks in insurers' operations and utilize those assessments to formulate ongoing surveillance plans
  - Assists supervisors in concentrating their efforts on:
    - High risk insurers, and
    - The riskiest areas of an insurer's operations
- Results are documented in the Insurer Profile Summary (continually updated)

# U.S. Risk-Focused Surveillance

- Insurer Profile Summary – Pulls Together Surveillance Process Results



# U.S. Solvency Monitoring Activities



# Overview of Group Supervision in U.S.

- US approach to regulation focuses on solo-entity, but windows allow us to look at group
  - Insurer is usually a cash generator, therefore primary concern is group getting money out of the insurer
    - Authority over transactions with affiliates (e.g., dividends)
    - Significant disclosure - Schedule Y, Part 2
  - Other disclosures spread throughout the annual statement
  - Evaluate financial condition of the group
  - Surveillance results are documented in Group Profile Summary (similar to Insurer Profile Summary)
  - Our insurer focus supports financial stability - financial stability of the group is dependent upon the US insurers





## REGULATORY ENHANCEMENTS (Windows)

- Strengthened review/access to group affiliate information
- Increased cooperation between regulatory jurisdictions
- Expand use of supervisory colleges
- Group financial assessment
- Improve standards across regulatory jurisdictions

## STATE REGULATED U.S. INSURERS

## U.S. SYSTEM OF STATE BASED REGULATION (Walls)

- Insurance Holding Company Model Laws & Regulations
- Quarterly financial analysis
- Conservative statutory accounting practices & principles
- Strong legal entity approach
- Lead state coordination approach
- State financial regulation standards & accreditation program
- Risk-focused examinations

## NON-INSURANCE ENTITIES

- Federal or state regulated financial institutions
- Non-regulated group affiliates

## FUTURE RISKS (Storms)

- Potential federal & international regulatory changes
- Global environmental or economic catastrophe
- Contagion effects of group affiliate/holding company failure

## INTERNATIONAL REGULATORS & ENTITIES

**GROUPS:** More than one business entity and type, controlled by a single holding company. Within each group, entities can be regulated through different jurisdictions.

# Questions

