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Group Capital Calculation

Commissioner David Altmaier
Florida Office of Insurance Regulation

Learning Objectives

At the end of this presentation, you will be able to:

- Objective 1-Describe the basic construct of the NAICs group capital calculation
- Objective 2-identify the material decision points that are ongoing for the Group Capital Calculation Working Group (GCCWG) work
- Objective 3-Explain the drivers for the NAICs group capital work and other group capital related work-streams

Background: Capital Considerations

- In the US, risk-based capital (RBC) requirements currently apply only to legal-entity insurers
  - Provides the commissioner with the authority to take action based on insurer's RBC ratio
- Group capital standards are being developed internationally (ICS) and by the US Federal Reserve Board (BBA)
- There is value in understanding and assessing capital position at the group level

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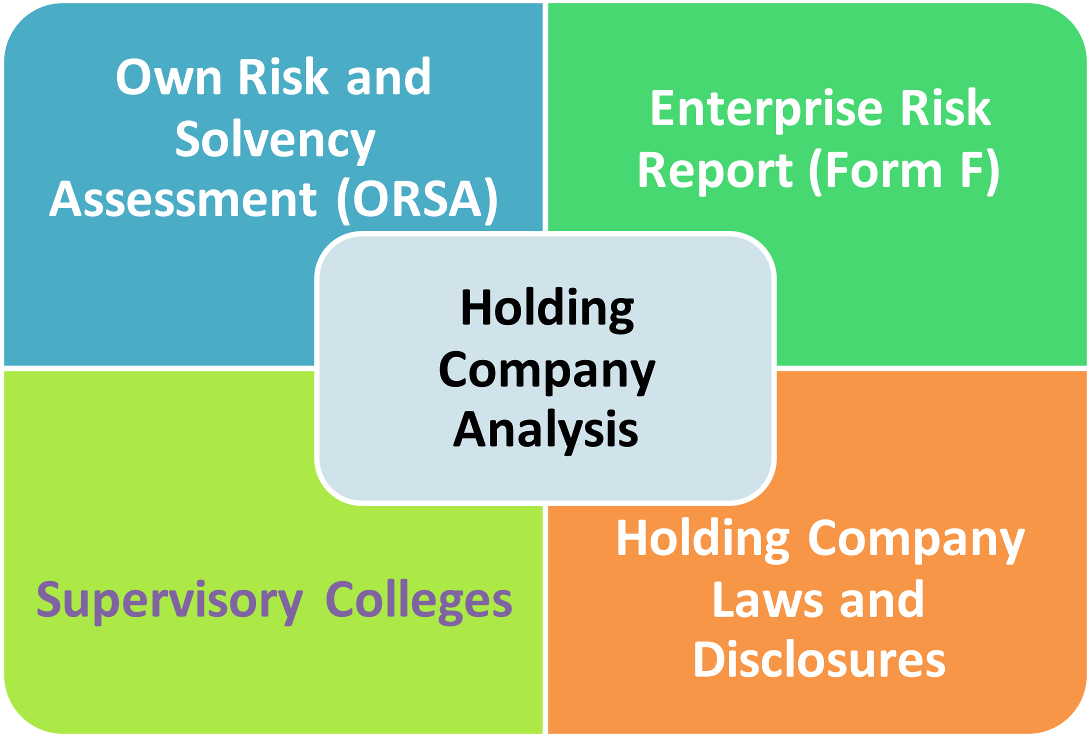
Current US Group Assessment

- US regulators currently have various tools to help them perform group analysis
- Group capital calculation will be a complementary analytical tool



Group Capital Calculation (E) Working Group

- Feb. 2016: NAIC formed the Group Capital Calculation (E) Working Group
  - Chair: Commissioner David Altmaier (FL)
  - Members: CA, CT, DC, IL, MA, MO, NE, NJ, NY, NC, OH, TX and VA

- Working Group's charge:
  - Construct a **group capital** **calculation** using an **RBC aggregation methodology**; liaise as necessary with other groups (federally and internationally) which **may help inform the construction** of a US group capital calculation.

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Key Aspects of WGs Charge

- Group Capital Calculation
  - Not a group capital standard or requirement
  - Additional regulatory assessment tool
- RBC aggregation methodology
  - Where possible, use RBC amounts, eliminate amounts for double-counting, and then aggregate the results
  - This methodology already chosen, as opposed to considering others such as consolidation
- International/FRB developments may help inform the construction
  - NAIC calculation should be developed in the manner most appropriate for use by state insurance regulators

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RBC Aggregation Method

Step 1: Calculate entity-level data, including available capital and required capital, using RBC amounts where available, with adjustments for financial entities with existing capital requirements

Step 2: Eliminate amounts for double-counting for all entities (where applicable)

Step 3: Aggregate the results for all entities, thereby calculating total available capital and total required capital

Step 4: Analyze the results—the group capital ratio

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Ratio: The End Result

For each entity within the group, two amounts must be provided: available capital and required capital

Available Capital (For all entities)

÷ Required Capital (For all entities)*

= Group Capital Ratio

**This will be the most challenging aspect to develop, particularly as there are many types of entities that do not file RBC and/or are not subject to capital requirements.*

Benefits of RBC Aggregation

Relies on RBC, where appropriate

Uses required amounts from the functional regulator

Includes inventory of all entities in the group

Certain financial info. provided for each entity

Allows for greater transparency

Provides for greater analytical capabilities

Identifies adjustments for items such as double-counting

Helps identify entities that are seen as source of strength

Helps identify entities that appear to bear more risk

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Components of the Group Capital Calculation

- Entities within a holding company generally fall within one of six categories
- The Working Group has been discussing each category and determining how each of these groups should be treated in the group capital calculation.

US Insurers Subject to RBC	US Insurers Not Subject to RBC (excluding captives)
US Captive Insurers	Non-US Insurers
Non-Insurers Subject to Capital Requirements (e.g., banks)	Non-Regulated Entities (not subject to capital requirements)

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Entities with General Consensus

US Insurers Subject to RBC

- Use current RBC treatment and amounts
- As a general principle, desire to retain and use RBC treatment to the extent possible

US Insurers Not Subject to RBC (excl. captives)

- Applies to title companies, financial guaranty companies, etc.
- Use minimum capital per state law or NAIC model, as applicable.

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Entities with General Consensus

Non-US Insurers

- Apply scalar to recognize difference in conservatism/accounting
- Scalar based on country's average capital ratio compared to US average capital ratio
- Two approaches to be field tested

Non-Insurers Subject to Capital Requirements (e.g., banks)

- Use capital requirements imposed by functional regulator
- These capital requirements are suited to the industry and have been tested over time

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Entities with General Consensus

US Captive Insurers

(Pure Captives)

- Pure captives generally are not required to file RBC reports
- Will be treated in same manner as non-insurers not subject to capital requirements

US Captive Insurers

(excl. Pure and XXX/AXXX Captives)

- This includes all types of captives other than pure captives and XXX/AXXX captives
- Will calculate amounts using an RBC blank with certain adjustments from SSAP No. 97.

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Entities Still Under Discussion

US Captive Insurers (XXX/AXXX Captives)

- Some believe amounts derived via AG 48 (economic for inforce, PBR for new business) and current regulatory requirement appropriate
- Others believe adjustments for captives necessary for comparability

Non-Insurers Not Subject to Capital Requirements

- RBC applies 22.5% factor to book/adjusted carrying value
- Considering other alternatives based on industry proposals
- Definition of material risk

Issues Under Consideration Now

- Surplus/Notes Debt
  – Contractual Subordination
  – Structural Subordination
- Scope of the group
  – To date, assumption has been that the scope of the group follows the NAIC Holding Company Act/Reg, which includes all entities in the group
  – U.S. Insurers with foreign group Supervisors
- Grouping
  – Particularly de-stacking of nonregulated entities
- Stress Testing
  – Should this be included to complete the group capital calculation?

Field Testing

- 2 Rounds of Baseline Exercise Completed
  - 11 Volunteer groups from 9 lead-States
  - Key Takeaways
    - No health groups among volunteers
    - Full inventory approach can result in negative value entities
    - Significant amount of debt issued by some volunteers
- More robust filed testing planned for later this year
  - Data Template to be developed
  - Tentative decisions to be tested
  - Intend to include health groups

THE GCC / The IAIS' ICS / THE FED's BBA

- NAIC is calculating a group capital calculation (GCC) under an aggregation approach for use with groups that include a US insurance company
- IAIS is creating a group insurance capital standard (ICS) under a consolidated approach for use with Internationally Active Insurance Groups (IAIGs)
- IAIS recently agreed to consider field testing an aggregation approach for the ICS as an alternative.
  - NAIC has submitted a proposed data collection template working with Team USA (NAIC, Federal Reserve and the Federal Insurance Office (FIO)
- The Federal Reserve Board is developing a building block method (BBA) for developing a group capital standard for U.S. based insurance led groups that include a depository bank within the group.

Related Issues to be Considered

- Overlap of GCC and Group-wide Insurance Capital Standard (ICS)
  – Approximately 10 -12 IAIGs

- Overlap of GCC Federal Reserve Board’s Building Block Approach (BBA)
  – Approximately 10 - 12 groups

- Reporting Mechanism

- Confidentiality

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Recap Question 1

Final decisions have been reached by the GCCWG for treatment of the following entity types in the GCC:

a. U.S. XXX/AXXX Captives

b. Non-Insurers not Subject to a capital requirement

c. Senior debt as available capital in the GCC

d. None of the above

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Recap Question 2

Which of the following statements is false?

a. The GCC is a complementary financial indicator to other group focused analysis tools
b. The GCCWG is considering ways to maximize consistency between the GCC and the global ICS and the Federal Reserve's building block approach (BBA)
c. Lead-State regulators will be required to take specified actions if the GCC indicates that capital resources are less than capital requirements
d. The numerator of the GCC is total capital available within the defined group.

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