NAMIC INTERNATIONAL REGULATION AND ACCOUNTING STANDARDS TASK FORCE

Insurer Solvency Principles
(November 1, 2010)

Sound Supervision For Sound Markets

Toward evaluation of acceptable solvency-regulation measures that exist now and that may be developed or proposed for state regulation by the NAIC and other bodies, the National Association of Mutual Insurance Companies adopts the following principles that should guide analysis and advocacy on behalf of the Association's members.

1) A sound and competitive insurance market benefits from and is made orderly through an efficient and effective solvency-supervision environment.

2) For the benefit of policyholders, regulators, and others with legitimate concern about the insurer's capacity to honor its promises, successful solvency regulation should provide reasonable and practical transparency into the insurer's capital adequacy.

3) The nature of the states' legal systems, and the breadth and complexity of insurance activity in this country suggest that the states' enforcement of capital adequacy should be conducted through application of a uniform regime of measures understood by both regulators and insurers. Individual insurers' internal models of economic capital efficiency or adequacy are not appropriate for judgments on the adequacy of regulatory capital.

Capital Adequacy Measures and Criteria for Assessment

A solvency-assessment system used by the states should be focused on the evaluation of the adequacy of an insurer's financial resources to meet its obligations to policyholders at all times with a reasonable level of assurance.

1) Solvency measures should be based on regulatory minimum solvency levels, rather than market-based solvency levels held for business objectives. Market-based or economic capital measures, while useful for management, are not practical for common application of regulatory sanctions. Even if formulaic, risk-based capital measures, applied with other solvency-maintenance tools, suffice for assessment of capital adequacy and any regulatory action thereon.

2) A solvency assessment system should account for the interaction and correlation among risks, and the use of reinsurance, diversity of risk, and other risk-mitigation strategies of the insurer.

3) All material factors that could influence possible cash flows servicing obligations during the period of assessment should be reflected in that assessment.

4) Accounting valuation of the insurer's resources for general purpose reporting may be different from valuation for solvency purposes (i. e., the amount of capital required to securely meet obligations to policyholders).

5) Solvency assessment by the states should treat domestic, foreign, and alien insurers equally via the same or similar legal requirements.

6) The quality of an insurer's risk-management framework, including its reconciliation of risk with capital adequacy, is relevant in conduct of solvency supervision.

7) A reasonable regime of solvency supervision will carefully observe proportionality, varying the scope and complexity of regulatory measures according to the size and complexity of the insurer.

Setting Standards for the Process

Clear, objective, and, to the extent possible, enduring standards for implementation and supervision of capital adequacy are the objective for regulation of insurers.

1) Standards should be set by supervisors in open and transparent process that includes consultation with sectors of the industry that will be affected by the standards.

2) Standards should be harmonized, where appropriate, across jurisdictions to minimize regulatory arbitrage.

Insurer Groups and Solvency Regulation

Solvency standards for groups may recognize risk diversification and capital mobility to the benefit of members of the group; however, regulatory assessment of capital adequacy must be centered on the legal entity.

1) The supervisor may choose, when assessing an insurer's capital adequacy, to recognize risk diversification among group members or capital resources available from affiliates.

2) Qualitative group-solvency assessment is appropriate in understanding and considering the effects of contagion, reputational, operational, and other species of risk posed by group members. However, quantification of group capital or of group-capital requirements is neither useful nor appropriate for solvency assessment.