U.S. CHAMBER OF COMMERCE

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October 19, 2016

To Whom It May Concern
International Association of Insurance Supervisors
c/o Bank for International Settlements
CH-4002 Basel
Switzerland

Re: 2016 Risk-based Global Insurance Capital Standard ("ICS") Consultation Document

To Whom It May Concern:

The U.S. Chamber of Commerce is the world's large business federation, representing the interest of more than three million businesses and organizations of every size, sector, and region. Our members include insurance companies that operate only in the United States as well as internationally active insurance groups ("IAIGs") headquartered both in and outside of the United States. Perhaps more importantly, our membership includes non-financial companies that rely on insurance products, and we are mindful of the larger role insurance plays as an investor in a globally interconnected economy.

The Chamber appreciates the opportunity to comment on the Risk-Based Global Insurance Capital Standard ("ICS") Consultation Document issued by the International Association of Insurance Supervisors ("IAIS") in July 2016. Our concerns highlighted in our 2015 submission persist, particularly as an ill-designed ICS will impact the traditional role of insurance as investors, ultimately harming capital formation. In addition to our earlier comments, the Chamber through this comment letter wishes to raise the following concerns:

- Accommodation for and respect of jurisdictional differences through a principles-based approach.

- Need for alternative valuation approaches.

- Lack of consideration of impact of derivatives reform on capital standards.

- The impact of poorly-designed capital standards on bond markets.

Accommodation For and Respect of Jurisdictional Differences Through Principles-Based Approach

The IAIS importantly notes that although the ICS is

> a group-wide, consolidated insurance capital standard, it is neither intended as a legal entity requirement nor to affect or replace existing arrangements or capital standards for legal entity supervision in any jurisdiction. Any jurisdiction choosing to reference the ICS in the development of its domestic solvency framework for insurance legal entities does so at its sole discretion.[1]

However, this statement ignores the fact that insurers, particularly IAIGs, operate across borders and will likely have to comply with more rules than that of their home country. In this respect, the ICS is likely to be restrictive and have a direct impact on the ability of an insurer to grow or meet the needs of its policyholders. The IAIS' development of an ICS should facilitate insurance companies doing business across jurisdictions, and at all costs avoid becoming an impediment to cross-border competition.

As a result, we recommend that the IAIS adopt a principles-based approach to any ICS that respects different jurisdictional approaches to meeting important insurance capital requirements. For example, in the United States, the Federal Reserve is moving forward with different capital approaches for savings and loan holding companies ("SLHCs") and insurers designated as systemically important insurance companies ("SIICs"). One approach, referred to as the building block approach ("BBA"), aggregates the insurance capital requirements of each entity, and

[1] Pgs. 12-13, Consultation on Risk-based Global Insurance Capital Standard (ICS) Version 1.0 Public Consultation Document, International Association of Insurance Supervisors (Jul. 29. 2016).

could be used for both SLHCs and SIICs. Such an approach is modeled on the concept that insurance regulation in the United States should not be "monolithic" and that capital standards need to reflect the differences of the companies found in U.S. insurance market. The currently envisioned ICS, as a group-wide standard, reflects the opposite viewpoint and is inflexible in accommodating the various existing regulatory frameworks that exist globally today, including the planned U.S. approach.

Moreover, other jurisdictions are similarly in varying stages of calibrating their own insurance standards. For example, Solvency II will be coming under review in the European Union at the end of next year. There will likely be untold modifications to Solvency II. Consequently, for the ICS to be useful it must be complementary to rather than attempting to replace the various regulatory frameworks put into place by different jurisdictions, while also facilitating the ability to compare capital levels between insurance companies. A principles-based approach is best suited to achieve such a desirable outcome.

Need for Alternative Valuation Approaches

The Chamber is also concerned with the impact of potentially only adopting a market adjusted valuation ("MAV") approach for the ICS. In particular, we believe that a MAV approach does not measure assets and liabilities appropriately, may not be auditable, and tends to be "procyclical" over the normal course of economic expansions and contractions, meaning that potential funding mismatches can be exaggerated. This "procyclicality" is a tool often used in banking regulation to prevent excessive credit bubbles.

Furthermore, we stress that insurers have fundamentally different product risks than banks and should not be treated in the same manner. Indeed, for the insurance industry, this type of treatment is distortive, particularly because some insurers match assets and liabilities over a long-term horizon. This makes insurance fundamentally different from banking and argues against the MAV approach.

Therefore, we are encouraged that the IAIS is pursuing development of the alternative GAAP plus adjustments approach to valuation and urge the IAIS to continue to flesh out this approach and adjustments that are appropriately designed to avoid introduction of levels of non-economic volatility similar to the MAV approach.

At this stage of ICS development, we suggest the IAIS permit use of different valuation alternatives, such as either a GAAP+ approach or the MAV approach.

In addition, the IAIS should consider allowing the BBA as another alternative—or at least as an interim measure—because it incorporates the capital standards of the local regulatory regime and provides greater transparency into the capital adequacy of both the group and the insurance entity.

Lack of Consideration of Impact of Derivatives Reform on Capital Standards

The IAIS approach to the ICS also fails to appropriately support risk mitigation strategies. We believe the ICS needs to award full credit for hedging activities that support capital requirements. Limited credit under the ICS acts as a disincentive to market participants to mitigate their risks, and ignores the recent global implementation of derivatives reforms.

Reforms undertaken in the United States and around the world have made the financial system more transparent, resilient and stable. Reporting of swap data has also helped market participants and the public understand the extent of each participant's derivatives exposures. But, failure to fully credit hedging practices, such as dynamic hedging, may result in a perverse incentive not to mitigate these risks in the markets whatsoever. Such an effect clearly would undermine the stability of our financial system, an objective counter to the stated goals of the ICS.

The Impact of Poorly-Designed Capital Standards on Bond Markets

Businesses rely on the corporate bond markets to raise capital. While not as liquid as equity markets, the bond markets provide a stable form of financing, benefiting businesses and investors alike. As insurers are significant investors in the bond markets, the implementation of poorly designed capital standards could reduce funds available for investment in the corporate bond markets. Equally important, local governments and communities rely on financing provided by infrastructure investments that help those communities fund improvements to transportation systems, communication, sewage, water and electric systems, providing a benefit to both the residents in those areas as well as the businesses that operate there.

The Chamber's concern is that the ICS, combined with the impact of other global financial regulatory initiatives such as the enhanced prudential standards that will be applicable to SIICs, may have a significant impact on the ability of many businesses to raise capital and local governments to access needed financing. In part, the Federal Reserve has recognized this in its plans to design separate capital standards for SLHC insurers and SIICs.

While recognizing that differences in major product lines may justify a different approach and strict comparability may not be possible, the IAIS ICS should seek to "level the playing field" among similarly situated insurers by insuring similar outcomes.. Providing for such flexibility is yet another reason to the IAIS should seek to adopt an ICS that is principle based.

Conclusion

The Chamber appreciates the difficulty IAIS has in convening the global discussion regarding capital standards for insurance given the number of regulators and stakeholders involved. However, for the IAIS' work to be effective, it must result in an ICS that is complementary to and adaptable for multiple jurisdictions, not only to ensure that insurance companies are adequately capitalized, but also to ensure that it promotes capital formation for economic growth. Accordingly, the Chamber urges IAIS to undertake careful deliberation, avoid completion of an ICS on any artificial timetable, and most importantly develop an ICS that is principle based, providing the necessary flexibility to accommodate different jurisdictions.

Sincerely,

Andres Gil
Director
Center for Capital Markets Competitiveness
U.S. Chamber of Commerce