The Insurance Receiver

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International Association of Insurance Receivers

Promoting Professionalism and Ethics in the Administration of Insurance Receiverships

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FEATURED ARTICLES

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Dear IAIR Members and Colleagues:

With the coming of Spring (I can dream as I stare at the 13.5 inches of snow on my driveway), comes new beginnings, for me personally and, most importantly, for IAIR. As I take my professional career to new heights as a Partner with the Nelson Levine de Luca & Horst law firm, I also take pride in the continued growth and expanding direction of IAIR.

Francine L. Semaya, Esq.

First and foremost, it is my pleasure to welcome our newest Board members: Mary Cannon Veed, Phil Curley, Doug Hartz, Paula Keyes and Ken Weine. Their contributions have already had a positive influence on the mission and goals of IAIR and the benefits afforded to our members.

January started off with our successful Post-Inaugural Insolvency Workshop in Tampa, Florida, in spite of the cold weather. My very personal thanks and acknowledgements to my co-chairs Dennis LaGory and Jenny Jeffers, along with the assistance of Jim Stinston, Ken Wylie and David Spector. Special recognition goes to the Beaumont Group, Maria Sclafani and Susan Barros, and their staff, who tirelessly worked before, during and after to make this our most successful program to date. Our speakers were not only instructive but stimulating and challenging and, in IAIR's usual fashion, the educational value of each session and the materials presented will continue to be invaluable to the attendees. The positive feedback we have received has been overwhelming. If you missed the "Insolvency Feud" you missed the best session. Special thanks to Patrick Cantilo not only for the concept, but for pulling it off so successfully. When do you recall a seminar with a packed room at 6:00 pm? Next year's workshop will be bigger and better and I hope all of you will attend.

Although we were hopeful that the declining economic climate would stabilize after the historic inauguration of President Obama, we continue to see the "black hole" deepen, which inevitably impacts the insurance industry. Several long-term care insurers have recently been placed in rehabilitation and, I expect, this is only the beginning. Life insurers keep reaching for a life-line and AIG's holding company required yet another federal bailout. The big question remains on whether the solvent insurers will be able to survive the ever deepening storm.

In such trying times, it is not always possible to stay one step ahead. As we continue to move forward in this time of uncertainty, we are faced with unpre-

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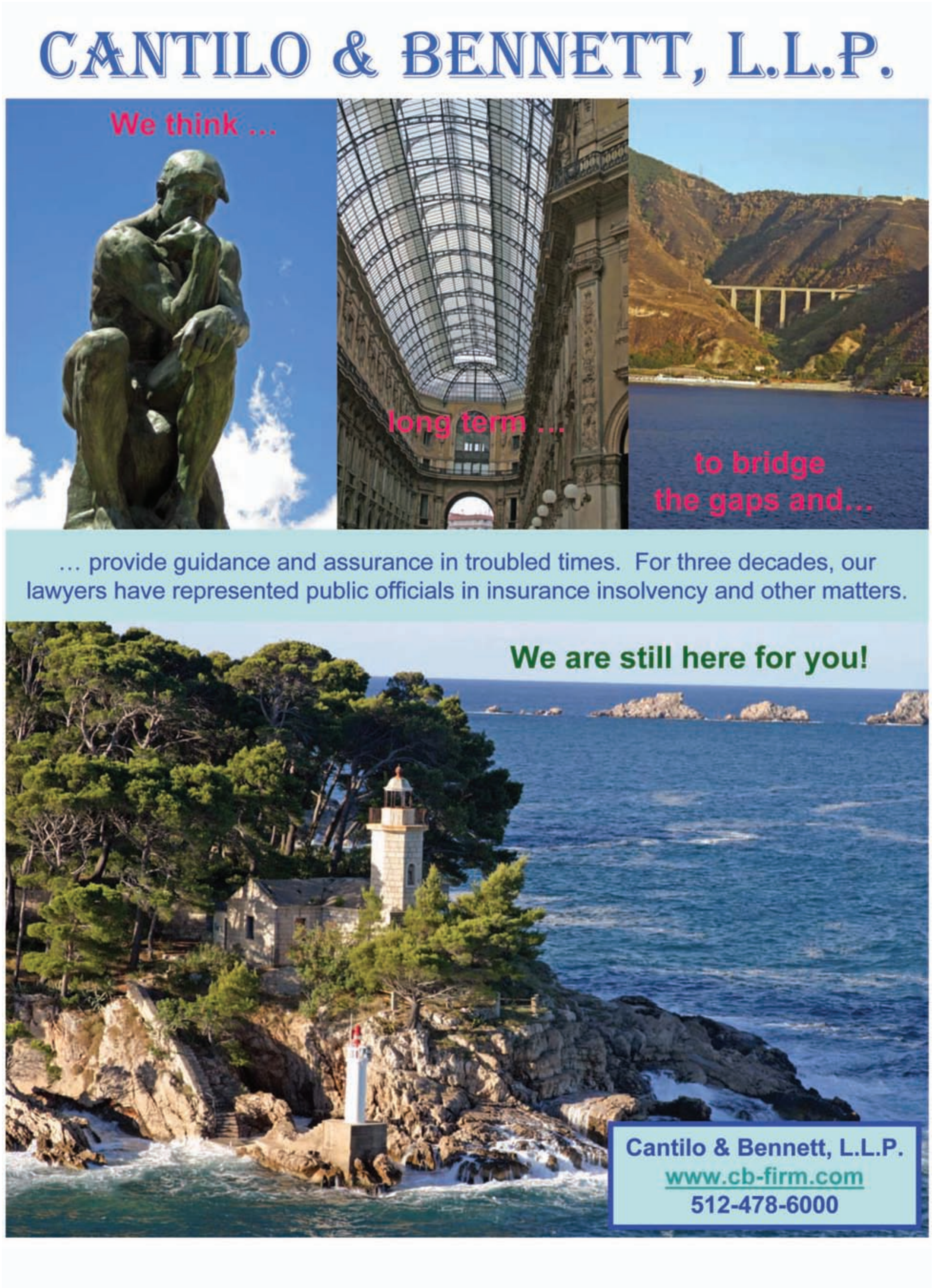
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IAIR's President's Message (Continued)

cedented legislation ever-changing regulations. Is there a Messiah for the insurance industry?

With this in mind, IAIR offers its members forums to network with other industry professionals and to establish new business contacts while sharing experiences and ideas. It is an honor to publicly recognize at each program, and in "The Receiver," our continued supporters and to share IAIR's accomplishments with our members. The benefits generated from your membership in IAIR flows not only to you as an insurance professional, but to each of your clients.

Lastly, IAIR extends our gratitude to Phil Curley who has successfully chaired our Issues Forums for 2008 and welcome Mike Cass as our 2009 Issues Forums Chair.

On behalf of the Board of Directors, please know that IAIR is committed to doing everything it can to ensure that this Association continues to provide programs and opportunities that reflect the members interests in the industry. Don't forget, it is up to each one of us to keep IAIR vital and strong. If we each strive to bring in one new member, IAIR will continue to grow and maintain its reputation as being the preeminent insurance receivership association, valuable not only to the receivership community but also to the regulatory community.

I look forward to greeting you at our upcoming meetings and workshops.

Very truly yours,
Francine L. Semaya
flsemaya@nldhlaw.com

Board Talk

By Michelle Avery & Jamie Saylor

Phil Curley was elected at the winter meeting in December 2008 to a three-year term to the IAIR Board. However, Phil is not a newcomer to IAIR. He joined IAIR in the mid-1980's under its prior name, SIR (Society of Insurance Receivers).

Phil Curley

Phil is a founding partner of the law firm Robinson Curley & Clayton. He spends a substantial portion of his practice dedicated to insurance insolvencies and related litigation; specifically receivership work, asset recovery, reinsurance, and litigation involving claims against management and outside professionals that may have contributed to the demise of insurance companies. Phil estimates that he and his firm have recovered over $300 million in assets stemming from insurance insolvency related litigation. Robinson Curley & Clayton also litigates cases that cover a broad range of commercial disputes and issues, including securities class actions, professional malpractice and employment law.

Phil was born and raised in Boston. He attended Northwestern University and received his law degree from George Washington University Law School. Phil worked during law school in Washington, D.C. and considered remaining in the nation's capital to pursue a career in government. The "hot" air in D.C. was too much for him though, and he quickly returned to the "Windy City" of Chicago. Phil and his wife Judy are recent empty nesters with their daughter, Samantha, having graduated from Northwestern last year and their son, Spencer, a freshman at Carthage College in Wisconsin.

Phil believes his greatest professional accomplishments to date have been successfully litigating the first "deepening insolvency" case involving an insurance insolvency way back in the 1980's, and founding and helping to build Robinson Curley & Clayton into a firm that is

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Board Talk (Continued)

highly regarded in the complex commercial litigation and insurance insolvency communities. A small shop by Chicago standards with 12 lawyers, Robinson Curley & Clayton is a boutique firm that prides itself in its superior work product, commitment to value, and the highest standards of client service.

Phil planned and chaired IAIR's quarterly Issues Forums in 2008. His interest in running for IAIR's Board was prompted by his desire to improve its educational programming and help expand its membership base.

On the lighter side of things, Phil was glad to address some of our more hard-hitting questions.

Q. What is your favorite sports team?

A. Growing up in Boston, naturally the Boston Red Sox followed closely by the New England Patriots and Boston Celtics. Phil has also adopted the Chicago Blackhawks as his new "hometown" sports team.

Q. What is the last fiction book you read?

A. Although Phil prefers non-fiction and is an avid history reader of the Civil War era and classical Rome and Greece, he is currently reading Irving Stone's *The Agony and Ecstasy*, a biographical novel about the life and times of Michelangelo.

Q. Where is the last place you vacationed?

A. Flying into Venice, Phil and his wife took a cruise of the Greek islands before returning to Venice for four days. While he enjoyed his recent visit to Venice immensely, Phil's all-time favorite places to vacation are Florence and Tuscany.

Q. What is your favorite leisure activity?

A. Golf. Those of you that have had contact with Phil know that he's an avid golfer and is always trying to recruit IAIR members for the golf outing at the Annual Insolvency Workshop.

Q. What is your favorite NAIC/IAIR conference location?

A. While pushing for a future meeting to be held in Florence, Italy, Phil's favorite spot from the recent meeting rotation is San Francisco.

Q. If you could have dinner with any three people in the world, dead or alive, fictional or non-fictional, who would they be and why?

A. Second only to dinner with the two authors of this piece, Phil would combine his political passion and interest in classical and Civil War history to dine with President Barack Obama, the Greek philosopher Plato, and Robert E. Lee.

Q. Give us one piece of personal information that your business acquaintances might not know about you?

A. "While a freshman at Northwestern, some of my fraternity brothers and I, convinced we were going to flunk our first final exams and become bums, dressed up as bums and traveled the campus Christmas caroling during final exam week in December." The tradition was carried on for many years by others (until the drinking age was raised).

Thanks to Phil for his time and cooperation on this article.

The Insurance Receiver is intended to provide readers with information on and provide a forum for opinions and discussions of insurance insolvency topics. The views expressed by the authors in the Insurance Receiver are their own and not necessarily those of the IAIR Board, Publications Committee or IAIR Executive Director. No article or other feature should be considered as legal advise.

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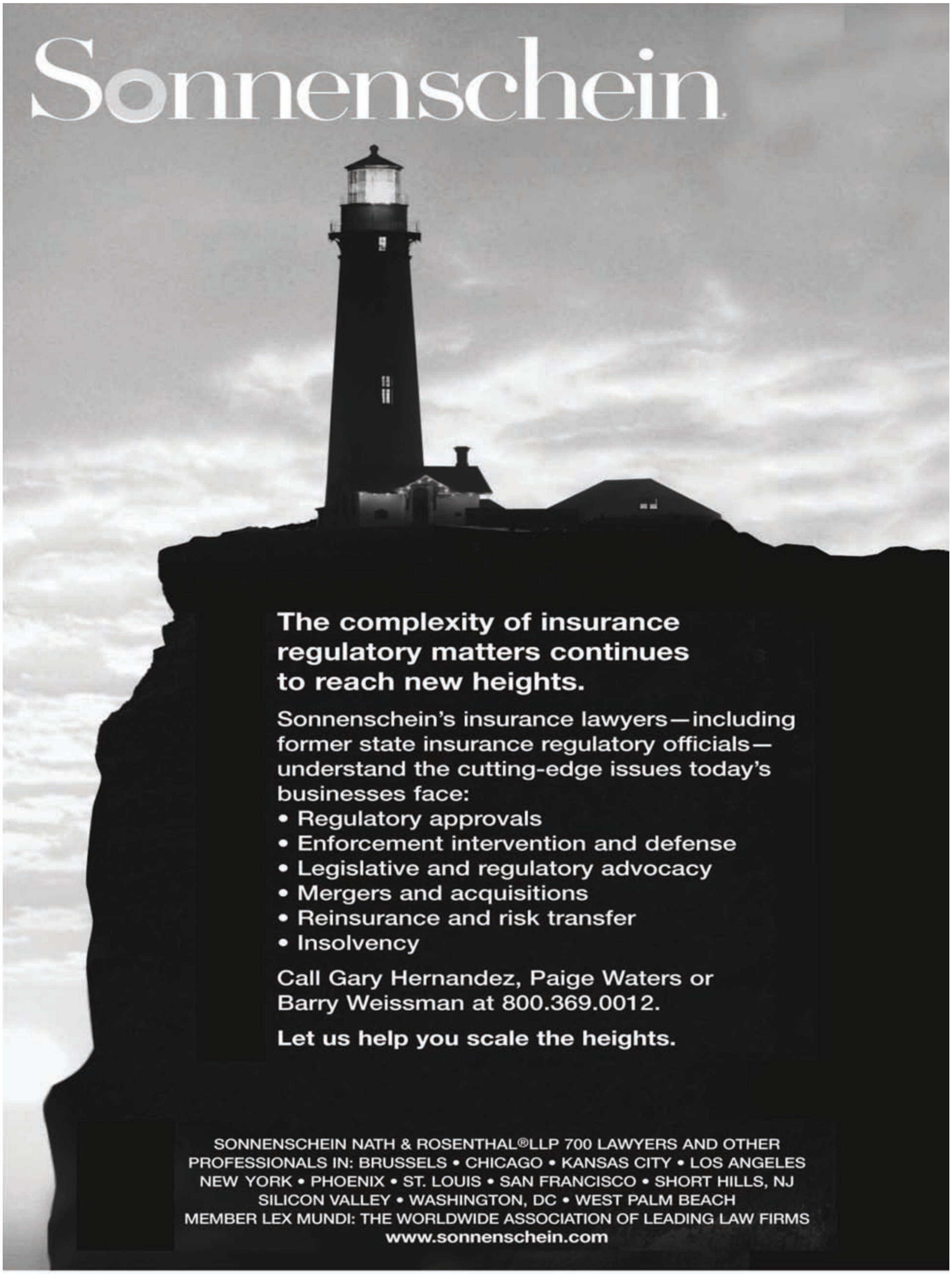
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Largest Reinsurance Pool Solvent Scheme for London Market

By Vivien Tyrell

The London run-off market witnessed an important event this summer when the scheme of arrangement for the largest reinsurance pool so far was sanctioned by the High Court on 17 July.

Eighty two companies participating on the EW Payne Pools numbered 1, 2, 3 and the X account ("Payne Pools") schemed the business which they had written in these pools. The business comprised mainly long tail APH exposures written in various periods from 1960 to 1985 and it held within it the prospect of a complex and labour intensive run-off continuing for a further 20 years or more. Although there are technically 82 separate schemes, the terms of each are either identical or very similar.

Pool complexity

A pool is a group of insurers and/or reinsurers (the participants) agreeing amongst themselves to write business together as a unit. The administration of the business is undertaken by a pool manager on behalf of the insurers/reinsurers, all of whom participate in the business in agreed shares.

A significant feature of the Payne Pools was that the business was all London market subscription cover. Under this system a single risk is underwritten by a number of insurance or reinsurance companies by them subscribing a percentage line to the risk (on a several not joint basis). The percentage shares in which the pool participants held the risk changed from year to year as did the type of business. Small percentages of business were written on different contracts over different years. The Payne Pools' percentage was split, in turn, amongst a large number of pool participants year by year. This meant that a pool participant's share of the business written was typically extremely small indeed. The business was originally written by the companies on the introduction of brokers EW Payne. Ultimately the management of the pool business was and continues to be Reinsurance Solutions Limited, a member of the Marsh McLennan Group. Since the commencement of the scheme on 18 July Reinsurance Solutions Limited is the scheme manager operating under the terms of the scheme. The Payne Pools wrote exclusively reinsurance business.

Many of the 82 companies were incorporated and operated outside the UK (in for example the EEA, Switzerland, Australia, USA, Bermuda, Canada, Brazil and Japan). However, because all the business of the pools is London market reinsurance business under contracts subject to English law and jurisdiction, there was no necessity to enforce the scheme in other jurisdictions.

The English court was satisfied that there was sufficient connection with England for the scheme to be implemented.

The scheme of arrangement concept

It may be helpful to recap on what a scheme of arrangement is and how it operates. A scheme of arrangement is a court driven binding agreement under Part 26 of the Companies Act 2006) (the successor to Sections 425-427 of the Companies Act 1985) between a company and (in this case) its creditors. The court is involved in two stages. Firstly, it will order the convening of a creditors' meeting or meetings to vote on the terms of the scheme. Provided the requisite majorities support the scheme (three-quarters by value and a simple majority of those creditors present in person or by proxy and voting at the meeting) it will proceed to the second and final stage at which it must be satisfied as to the fairness of the scheme and if so approve its terms and sanction it. Once the order sanctioning the scheme is filed with the Registrar of Companies, the scheme will

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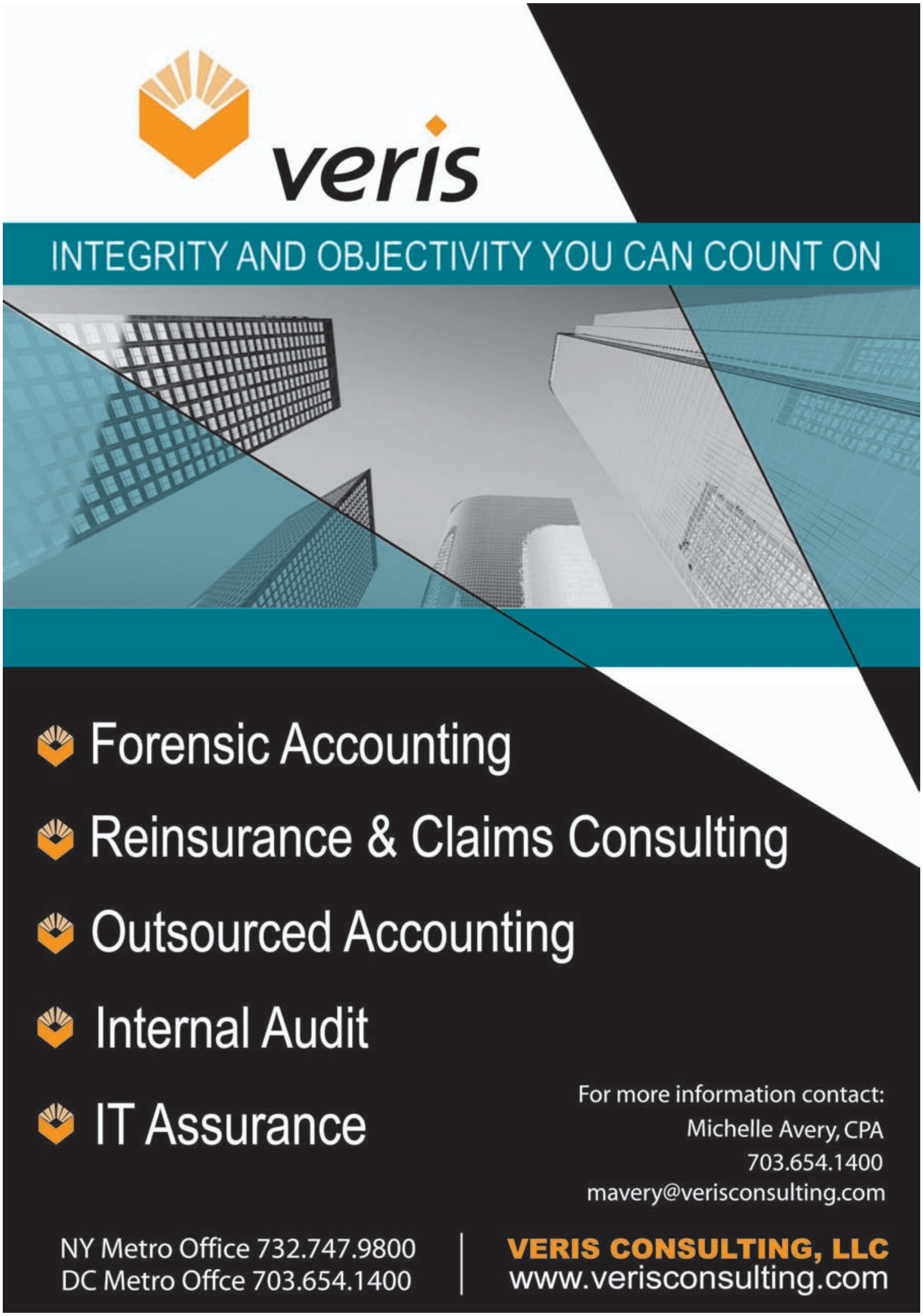
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be effective and will bind all creditors whether or not they voted and whether or not they opposed the scheme. In deciding on whether a scheme is fair, the judge at the sanction hearing must be satisfied that the arrangement is such *"as an intelligent and honest man…acting in respect of his interest, might reasonably approve"* (Plowman J in *Re National Bank Limited* [1966] 1 WLR 819).

There has been recent controversy surrounding solvent schemes of arrangement, in particular the scheme proposed by British Aviation Insurance Company ("BAIC"). A significant aspect of the BAIC scheme (which was defeated in the English court) was that much of the business being schemed was direct insurance business. Significantly, the Payne Pools scheme concerned purely reinsurance business. Since the failure of the BAIC scheme, a number of solvent schemes, all of which have sought to distinguish themselves from the one proposed by BAIC, have been successfully implemented.

The Payne Pools' scheme

The effect of the Payne Pools' scheme is to prevent individual creditors taking proceedings against the companies under their contracts in the normal way and instead it imposes a bar date, 16 December this year, by which such creditors have to lodge their claims including an estimate of their outstanding claims. Creditors will be paid the full amount of their claims within the coming months. The scheme contains a simple method for valuing creditors' future claims. Creditors' Incurred But Not Reported Claims ("IBNR") are valued by applying different multiples to their outstanding loss claims. For example in the case of asbestos losses the multiple is 2; for pollution losses the multiple is .75 and for other long-tail losses it is .25. The claim forms for creditors are pre-populated with the appropriate figures for each scheme creditor which has the opportunity to amend these values if, in its view, they are incorrect, and the scheme includes a mechanism for the agreement or adjudication of disputed claims. If creditors fail to submit their claims by the bar date they will receive the amounts as populated in the forms, with their IBNR entitlement as valued under the scheme.

The driving force behind the scheme was the desire to bring to an end the very onerous burden on the creditors, the claims administrators and the participant companies of handling such high volume but very small value claims made against a complex web of changing participations in different years and in varying percentages of cover per participant. Further, it allows creditors to have a one-off lump sum payment of their estimated ultimate amount due to them. The scheme gained almost unanimous support at the creditor meeting stage and was unopposed at final stage ie the sanction hearing before the court. This outcome was a testament to the meticulous work of Reinsurance Solutions Limited and the diligence of KPMG, the accountant scheme advisers, in explaining the concept and obtaining feedback from stakeholders over a substantial period of time. Edwards Angell Palmer & Dodge, London office, were the scheme legal advisers.

This article first appeared in AIRROC Magazine (September 2008). It is for guidance only and is not intended to be a substitute for specific legal advice. If you would like any further information please contact: Vivien Tyrell

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Vivien Tyrell

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It is ALL About INFORMATION Systems!

By Jenny L. Jeffers, CISA, AES

When a company experiences insolvency and is taken into either Rehabilitation or Liquidation by the state regulators, everybody wants to know everything about the company all at one time:

- Courts need details regarding financial information in order to determine which order to issue.
- State Receivers want to know the assets, liabilities, amount and collectability of reinsurance, policy holders, amount of exposure, outstanding policy holder claims and claims from other stakeholders.
- Guaranty Funds and Associations need to know the claim count and dollar amounts that will be coming their way when and if the ax falls.

All of this information can be supplied – by the databases that are maintained by the company for policy and claim administration, as well as general ledger and reporting systems. The decisions that will be made in the early stages of the rehabilitation/liquidation are crucial to the direction that the process takes. Thus, the reliance on the data provided by the company systems is dependent upon the accuracy and completeness of the data. Not surprisingly, companies that are in financial difficulty do not put high priority on improving, updating or refining Information Systems. Often cuts are made in Information Systems ("IS") personnel; new and needed changes to systems are postponed. All in all, in a non prosperous company, Information Technology ("IT") is considered to be a drain on the funds – a cost center - not a revenue producing resource. In another article, this can be argued by illustrating the cost savings that can be attained by streamlining processes and maximizing automation of processes and controls. For this article, the focus will be placed on the importance of appropriate handling of the Information Systems and Information Technology departments during the Rehabilitation and Liquidation Process. This fact was introduced to point out that MOST often the data that is available in a company being placed into receivership is not of the highest quality. Additional sources of information may be required.

Regulators are required to perform Statutory Financial Examinations every three to five years. In general, the determination to categorize the company as a troubled company is the result of such an exam. Each financial exam includes an Information Systems Questionnaire and evaluation – Exhibit C in the NAIC Examiners Handbook. Included in the Information Systems Review should be:

- A description of the major systems utilized by the company for administration of:
  - Policies
  - Premiums
  - Claims
  - Reinsurance
  - Commissions
  - General Ledger

The risk analysis section of the review should indicate the materiality of each system and the risk level associated with it. These include:

- An evaluation of controls around the procedures performed on each system;
- Description of Security Policies in place;
- The Organization Chart of the IT Department;
- Topographical layouts of the Network and Mainframe environments;
- Backup Schedule and Retention Policy;
- Description of External Access to the systems and the controls around it;

It is ALL About INFORMATION Systems! (Continued)

- A list of all Outside Service Providers for information Systems;
- E-Business being transacted by the company – financially significant transactions accepted and processed over the internet; and
- Electronic Data Transmissions received and sent and the dependency on them.

This information can be a wonderful resource for the liquidation team IS Specialist in the initial analysis of actions to be taken. The IS Report is not always included in the final report to the company but should be available in the TeamMate project that contains the electronic workpapers for the exam. Workpapers in TeamMate can be exported to their native application (MS Word, Excel, PowerPoint, etc) for review by the liquidation team IS Specialist if the TeamMate software is not available. The Liquidation team should always contact the state regulator and ask for this information for the most recent financial examination.

If there is even a possibility that criminal or negligence charges will be brought against the Officers and Directors or any employee of the company, IMMEDIATE attention must be given to the protection of the data and to ensure that the chain of custody is tracked from the beginning of the proceedings. Court cases will require proof of illegal, fraudulent and/or inappropriate business practices. Often the proof will lie in the data and/or email and calendar records. These can be destroyed by company personnel at the earliest indication of the company being placed in receivership. Data can be destroyed quickly. Usually, the data that is deleted can be restored by a computer forensic specialist. A computer forensic specialist must be involved to assure appropriate treatment of all data storage devices – computer systems, images, web content, backups, Blackberries, cell phones, external hard drives, digital cameras, as well as any type of personal storage devices. The inclusion of a computer forensic specialist will maximize the appropriate preservation of all data that can contribute to or comprise the evidence needed to prove a case in court. During this process, a change of custody of all data objects should be maintained to preclude alteration or deletion by any person or persons. Many cases are lost due to the liquidator's inability to provide proof of the accuracy and completeness of the data used to validate accusations of wrongdoing.

Protecting the data integrity is the first priority. With or without the information from the regulator and the assistance of a computer forensic specialist, the data must be protected from being compromised. The most current backup should be put in a safe place, accessible only by the Receivership Team. A new complete backup must be taken of all systems at the earliest possible convenience and secured. External access to the systems should be evaluated and eliminated to the degree pos-

Another high priority activity is the evaluation of Information Systems personnel.

sible. If elimination of external access will jeopardize the continuation of processing, then monitoring of all external activity should be put in place as early as possible. An inventory of all equipment should be done as soon as possible to prevent the transfer of information via external storage devices, which can be taken outside the company and improperly used.

Another high priority activity is the evaluation of Information Systems personnel. IS personnel can contribute greatly to the success of the rehabilitation or liquidation. The company personnel know the systems and the data, the way the systems fit together, what data is stored in each system and any eccentricities of the systems. However, sometimes the systems people are angry that the company is being taken over and that the systems they have so devotedly perfected may become obsolete. Although it is not the fault of the Receivership Team, they are the ones who are there and who can be blamed for the current situation. IS professionals take their work very seriously

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and are proud of their achievements. Some react adversely to the possible impending "putting to bed" of the systems over which they have ownership. Angry IS/IT personnel are VERY dangerous. The Receivership Team should evaluate the personnel utilizing the input of an IS Specialist. The critical personnel should be interviewed and every effort made to retain their services. If instability or anger are exhibited, these personnel should be relieved of duty, regardless of how essential they may appear to be. A good IS Specialist can evaluate and analyze the systems and data and take on the duties of any personnel who appear to be a potential threat. IS/IT personnel have been known to delete critical data, destroy equipment, remove critical information from the building and otherwise undermine the work being done by the Receivership Team. Immediate attention should be given to the evaluation of IS/IT Personnel and appropriate action taken. The team IS Specialist should work closely with the retained IS/IT personnel to secure the systems and data and perform the processes required.

The final step that will be discussed in this article is the need to prepare for the liquidation process if it is required. Primary in this process is the production of data for the various entities involved. These include, but are not limited to:

Sending Proofs of Claim ("POCs") to all potential claimants if required by the state performing the liquidation

Estimating the number of open claims and the associated reserves

Providing a file of all policy holders including the effective, expiration and possible cancellation dates to be utilized in calculating return premium due

Evaluating data for completeness or missing data to fulfill the requirements for transmission of UDS data files to Guaranty Associations and Guaranty Funds. Uniform Data Standard ("UDS ") is the format approved by NAIC to be used by all Guaranty Funds and Associations ("GAs") and Receivers to transmit data back and forth. The data is initially transmitted from the Receiver to the GAs to allow them to upload the claims into their systems and begin processing and paying claims. Claim and expense payments made are then transmitted back to the Receiver for submission to reinsurers and to enter a claim on the part of the GAs for repayment by the Receiver. The UDS Format has been in place since 1995 with updates approved with changing requirements for all related entities. The prompt transmission of data between entities is necessary to assure timely and appropriate handling of claims covered by the GAs as well as to optimize the collection of reinsurance as one of the primary assets of the company in liquidation.

The points discussed are high level information, but are issues that should be dealt with as early as possible in the receivership process. Additional articles will be provided in the Receiver that will go into more detail with regard to the involvement of IS in the process and the importance of and dependence on the data that can be provided by the company.

Jenny L. Jeffers, CISA, AES

Jenny Jeffers, CISA, AES is Managing Member of Jennan Enterprises, LLC in Tallahassee Florida providing IT Services including regulatory IS examinations for states and contracting firms around the country as well as IS services for liquidators and guaranty associations. She is currently serving on the Website Committee of SOFE and is the chair of the AES (Automated Exam Specialist) Committee for SOFE. Jenny is a past Education Committee Chairman for IAIR and is a current member of the Education and Website Committees for IAIR and the ASWG (Audit Software Working Group) for NAIC.

To submit an article, please contact Maria Sclafani at mcs@iair.org.
Deadlines for 2009 submissions are as follows: May 1, August 1 & October 31.

View from Washington

By Charlie Richardson

The new Administration and new Congress are facing immense challenges on the economic front. Financial services, including insurance, are at the center of the discussion as a "systemic regulator" is considered in the short term with more sweeping financial services regulatory reform on the drawing board for the medium term.

What Should Be the Starting Point?

We've talked before about the U.S. Treasury Department's Financial Services Blueprint issued in March of 2008 as being a starting point for how financial services should be regulated in the 21st Century. Two other studies came out in January that the Congress and Administration will be looking at, although both touch on insurance only in passing. The first is a Report by the United States Government Accountability Office, "A Framework for Crafting and Assessing Proposals to Modernize the Outdated U.S. Financial Regulator System." You can access a copy at http://www.gao.gov/?info. The second is "Financial Reform – A Framework for Financial Stability" by the influential Group of Thirty headed by Paul A. Volcker. That report can be obtained at http://www.group30.org.

SEC Takes on Equity-Indexed Annuities

On December 17, the Securities and Exchange Commission ("SEC") approved new Rule 151A, which includes equity-indexed annuities within the SEC's definition of a "security," focusing on the investment risk associated with such products. Parts of this decision were controversial, with key Democrats calling for greater regulation, which could be affected by an SEC with Obama appointees. More than 4,800 comments were filed with the SEC, most, including industry and state insurance regulators, opposing the change. The new definition applies only to equity-indexed annuities issued on or after January 12, 2011.

Health Insurance Changes: A Long and Winding Road

Among the first health care issues in the 111th Congress will be efforts to expand the State Children's Health Insurance Program (SCHIP). With the temporary extension of the federal health care program for lower-income children set to expire in April 2009, Congress is likely to tackle SCHIP early in 2009, possibly as part of the big stimulus bill. Democrats hope to make the income threshold for eligibility 250 percent of poverty, an increase over the current 200 percent level. Notwithstanding the larger Democratic Congressional majorities, significant health insurance changes are rarely done quickly. HHS Secretary Tom Daschle has suggested Congress enact broad principles for health care reform, with specifics filled in later by a regulatory board.

> *Among the first health care issues in the 111th Congress will be efforts to expand the State Children's Health Insurance Program (SCHIP).*

The End of Reinsurance as We Know It?

At its December meeting, the NAIC adopted a new reinsurance framework that will "change reinsurance as we know it." The proposal calls for significant reduction or elimination of collateral requirements for non-U.S. reinsurers. If the regime is implemented, a new department will be established within the NAIC to determine which non-U.S. jurisdictions are entitled to enter into mutual recognition agreements, a single-state regulator for U.S. reinsurers will be authorized to adopt uniform minimum standards, and a single-state regulator for non-U.S. reinsurers will allow access to the U.S. market through a "port-of-entry" jurisdiction. The new framework would also reduce collateral obligations for non-U.S. reinsurers on a sliding scale that could reach zero for highly-rated companies.

Life Insurers Want TARP Coverage

Although the U.S. Treasury Department's $250 billion Capital Purchase Program is open only to federally regulated U.S. controlled banks, savings associations and certain bank and savings and loan holding companies, a number of insurers also submitted applications for relief under the program. To meet eligibility requirements, some insurers filed with the Office of Thrift Supervision to become savings and loan holding companies; others were already eligible by virtue of being organized as bank holding companies. Insurers are seeking shelter under the Troubled Asset Relief Program ("TARP") to increase the capital they have available to cover insurance and annuity costs or gain protection from losses in their investment portfolios. However, not all life insurers are seeking funds under the TARP, as New York Life Insurance Co., Massachusetts Mutual Life Insurance Co. and State Farm have declared that they will not participate. Several major P&C carriers also disclaimed any interest in Federal funding.

Ponzi's Return

Mr. Madoff has likely trumped the successful efforts of years of lobbying by hedge fund and other private equity managers and advisors in fending off federal regulation. Although the SEC should have been regulating Madoff's investment advisory activities, the SEC and Congress may race to see who will act first with new regulations and laws, leaving insurance as the only financial service remaining without comprehensive federal level regulation.

What's All This About International Accounting?

By Rob Esson

Over the past few years, international convergence of accounting standards has been getting more and more attention. A few of the key events have been as follows:

- In September 2002, the International Accounting Standards Board ("IASB") and the US Financial Accounting Standards Board ("FASB") signed the so-called Norwalk Agreement whereby they committed to develop high quality accounting standards on a converged basis. The agreement has been both renewed and extended in the subsequent years, and a number of standards have been promulgated and developed on a joint basis between the two Boards.

International Accounting Standards Board®

What's All This About International Accounting? (Continued)

- In December 2007, the SEC removed the reconciliation requirement for Foreign Private Issuers who prepare their financial statements in accordance with International Financial Reporting Standards ("IFRS"). Prior to this, such issuers would have to reconcile their IFRS statements to US Generally Accepted Accounting Principles ("US GAAP").
- Then, in what was seen as the next big step towards the Nirvana of a single set of worldwide accounting standards, the SEC Commissioners voted unanimously in August 2008 to issue for comment a "Roadmap for the Potential Use of Financial Statements Prepared in Accordance with International Financial Reporting Standards by U.S. Issuers". The "Roadmap" proposed that the US should – if certain key milestones were reached – move to utilize IFRS for all public companies in the middle of the next decade.

Speeches have been made about the desirability of the world moving to one set of accounting standards, with flowery language about accounting being the language of business and the possibility of their being only one such language world-wide.

Importantly for those of us in the insurance industry, the IASB has been working on "Phase II" of its insurance contracts project, with the promise of promulgating a comprehensive international standard for insurance. At present, the international standard for insurance is IFRS4, Insurance Contracts ("IFRS 4"), which is a strange beast indeed. IFRS4 was only ever intended as a temporary stop-gap standard and it does not deal with insurance liabilities in any consistent manner: effectively, with a few exceptions, it says 'continue what you were doing with your local GAAP'.

However, with the move towards adoption of IFRS in the US, the excitement has been palpable: accountants from all walks of life have been ripping off their US GAAP t-shirts and waving their IFRS scarves in the stands, chanting until hoarse: "Convergence", "Transparency", and "Single set of high quality accounting standards". Squadrons of Pigs have been seen banking over the stands leaving little piggy con-trails spelling "Fair Value For Ever."

Well, actually, not really.

And worse than that, the new Chairman of the SEC is threatening to rain on the parade. Mary Schapiro, in her confirmation hearings in the US Senate, made it clear that she would slow down and re-examine her predecessor's commitment to moving the US in the direction of adopting IFRS.

This very hesitancy has created considerable uncertainty and people are wondering whether their investments in IFRS are as ephemeral as the value of bank stocks. The answer is no: for insurers, the investment in work on IFRS will return dividends both now and in the future. The reason is relatively simple: although almost all the work on the insurance contracts project has been performed by the IASB, the project itself was run from the beginning as a "modified joint project". Neither the IASB nor the FASB have sufficient staff or resources to work on every project together. Hence, they have introduced the concept of a modified joint project where one Board will take the lead on a project and do the necessary research and work to produce a discussion paper. At that juncture, the other Board will issue the discussion paper with a request for comment from its constituents as to whether the project should be added to its active agenda as a full joint project from that point on, i.e., through the Exposure Draft stage up to and including issuance of the final Standard. Although I will admit that I was personally skeptical as to whether this would happen as expected for insurance, in fact - it has. The IASB issued its Discussion Paper: Preliminary Views on Insurance Contracts (the "Discussion Paper") in May 2007 and the FASB issued it with a wrap-around asking whether it should join the IASB in a joint project on insurance. Almost all commentators said that they should, although there was worry as to whether the project could meet its timetable of to issue a final standard by mid-2011 if the FASB joined.

In fact, the FASB announced in October 2008 that it would join the project, and consequently, the future comprehensive standard on insurance will be produced jointly by the IASB and the FASB. At the time of writing, the FASB is conducting education sessions so that FASB members will be up to speed on the project. Hence, irrespective of what happens here in the US with adoption or otherwise of IFRS, it is likely that a comprehensive new standard on Insurance will be issued by the FASB sometime over the next two to three years, and that new standard will be based on the work to date of the IASB.

Statutory Accounting Principles are based on the framework of GAAP

Statutory Accounting Principles are based on the framework of GAAP and hence, if GAAP for insurers changes, those changes would need to be considered for adoption, modification or rejection into the NAIC Accounting Practices and Procedures manual which codifies SAP. Although I stick my neck out somewhat, I rather doubt that a new US GAAP standard on insurance accounting would be rejected outright for SAP and, consequently, my guess is that it is more likely that such a new standard would either be adopted or modified for SAP.

In summary, therefore, I believe that irrespective of any SEC decision regarding the adoption of IFRS in the US, it is likely that US GAAP will promulgate a comprehensive new standard on insurance within the next two years. There is a political dimension to this timing as well: in June 2011, all the Board Members of the IASB, who have been there since the beginning and have followed the project from its inception, will have left. Cognizant of this, the IASB would like to promulgate the new standard before all the long-term institutional knowledge surrounding the project has gone.

So what's all this insurance contracts stuff all about?

As mentioned before, the IASB issued the Discussion Paper: in May 2007. There were 162 comment letters submitted, including of course, the best one, which - naturally - was the one from the International Association of Insurance Supervisors' ("IAIS") Insurance Contracts Subcommittee that I chair.

Current Exit Value or Fulfillment Value:

The Discussion Paper proposed a measurement attribute for insurance contracts as Current Exit Value. As far as anyone can tell, Current Exit Value is indistinguishable from Fair Value. The IAIS was an early advocate of some form of exit value as the measurement attribute, but many of the Discussion Paper commentators were concerned that an exit value was too theoretical. They argued that almost no insurance liabilities are ever extinguished by way of exiting and the usual route to extinguish a liability is to settle it. However, as the term Settlement Value is used elsewhere in IFRS and does not necessarily mean to settle over time in the normal course of business, a new term "Fulfillment Value" has been coined to imply settlement over time in the normal course of business. The IASB intends to consider within the next few months whether to change the name of the attribute to some form of fulfillment value. It is quite possible that some of the descriptions of fulfillment value would correspond to the type of exit value that the IAIS supported. For example, a fair value attribute would, at present, imply that the liability holder's own credit risk would be a part of the liability measurement. The IAIS has never supported this and had argued that any exit value for insurance liabilities should exclude own credit standing. Additionally, an exit value might, if taken too far, prevent a company from using its own expected expenses estimates in its cash flow estimates. This is because, in theory, an exit value should use the market's expectations of the expenses. While the IAIS supported using the market's expectations of expenses if they were observable, it recognized in its response to the IASB that this would be rare.

Whether the attribute is described as an exit value or a fulfillment value, it is clear that there will be a need to utilize the so-called building blocks approach to measuring the contracts. The three building blocks would be:

1. explicit unbiased and current estimates of the cash flows;
2. a discount for the time value of money; and
3. a margin for bearing risk or uncertainty. The vast majority of comment letters agreed with these building blocks, although it should be noted that the Group of North American Insurance Enterprises has argued that there should be no discount for the time value of money for non-life insurance contracts.

Future Premiums:

There is quite a controversy at the IASB over so-called future premiums. The problem arises for long-term life contracts where the evaluation of the cash flows for the contracts needs to take into account both the outflows due to maturity or death and the concomitant inflows of premiums. Looked at in isolation, the inflows of premiums in the future are not under the absolute control of the insurer as the policyholder can lapse at any time. This leads to a problem related to the definition of an asset as assets must be under the control of the entity. Hence some board members have concerns that the future premiums cannot be measured as assets. However, if you simply evaluate the cash outflows, without the cash inflows, you get an economically silly result. In order to get around the problem, they have postulated that there is a customer relationship intangible asset. The IAIS position is that the measurement of the cash flows should be independent of the process of contract recognition. Once a contract has been recognized, then each of the probability weighted scenarios should be taken into account when evaluating the cash flows. For example, one scenario might be that the policyholder pays all the premiums until the maturity of the policy at which stage, presumably, he or she would receive the proceeds. Another scenario would be that the policyholder lapses after a couple of years. A different one might be that the policyholder dies after six years. Each of these scenarios has a set of both cash inflows and outflows. Indeed, you cannot get the cash outflow for lapse, death or maturity unless the corresponding premium inflows have occurred. The IAIS is providing a paper to the IASB on the boundaries of insurance contracts for the purposes of evaluating cash flows.

Discretionary Participation Features:

Discretionary participation features is the terminology used to describe policies with policyholder dividends where the dividends are not guaranteed. Accordingly, the amount of the policyholder dividends is at the discretion of the insurer. Board members believe that such dividends, if not guaranteed, do not meet the definition of a liability. The IAIS takes a different position, similar to that regarding future premiums. We believe that the cash flows should be based on expected cash flows not expected cash flows less some part which, if evaluated separately, would not meet the definition of the liability. Put a different way, some cash flow scenarios would result in higher policyholder dividends while others would result in lower dividends. If one is going to use probability weighted expected cash flows, then each of those scenarios should be taken into account - not some biased subset.

Universal Life:

Universal life policies are particularly difficult to deal with – their very flexibility makes it hard to know whether policyholders are going to pay the minimum, something more, take premium holidays, etc. In many ways, the problem is one of estimation of the cash flows writ large. However, in considering how to fit these important policies into the measurement methodology, the current (very tentative) view of the IAIS is that the estimates of probability weighted cash flows are surely available to the insurers based on historic experience, modified by current factors. Indeed, we suspect that this is the key. However, and perhaps even more importantly, is the fact that those cash flows will be subject to a greater degree of uncertainty than those for more conventional policies. Hence, we would expect that the risk margin – a measurement of uncertainty – would be correspondingly greater.

Margin calibration and profit on inception:

Of all the arguments about the measurement of insurance contracts, none is more controversial than that of calibration of the risk margin and the resultant possibility of profits on inception. At the IAIS, we split three ways on this. One faction would calibrate the margin based on an exit value estimation and, if a profit on inception arose, then, other than checking the calculations to ensure that it were reasonable, so be it. Another faction would do the same, but then put what would otherwise be profit on inception into another liability that would be run-off like a service provision. A third, and very excellent faction with brilliant minds behind it, would calibrate based on an exit value. If an apparent profit on inception arose, it would be examined in relation to the inherent variability and errors in reserve estimation. Only if the profit on inception was clearly outside any reasonable level of error and variability would it be recognized – otherwise, the margin would be recalibrated to result in a nil profit on inception. Dear Reader – can you guess which faction your author was in? There is at least one other faction, although in the vast majority of times it aligns with the third. This is the view of GNAIE which is that the premium is the only observable price and the margin should be calibrated to this, absent a loss making contract. Naturally, this results in a nil profit on inception. The difference, however, between these last two viewpoints is that in the latter there can never be a profit on inception, irrespective of how large or out of line the premium may be, while in the former, it is possible as long as there is sufficient evidence that it is outside of any reasonable level of error. o me, the difference arises in certain niche markets – think extended warranty, or title insurance, where to keep pushing the margin up over any reasonable expectation of losses is not helpful in providing an accurate economic picture.

There are, in fact, a number of other 'open items' in the insurance contracts project, but this should have given you a flavor for some of the ideas. The project, and the joint work of the IASB and the FASB, will be critical in reshaping how insurers are viewed by the financial community in the future. Do you feel the urge to join the cheering throngs of accountants?

Rob Esson

Rob Esson is a Senior International Advisor at the NAIC in the US, and is involved with many of the NAIC initiatives relating to International Accounting and Solvency. At the International Association of Insurance Supervisors (IAIS), he is Chair of the Insurance Contracts Subcommittee and is an active participant on the Solvency & Actuarial Issues Subcommittee. He is also an official IAIS observer member on the IASB's Insurance Working Group and Financial Instruments Working Group, and a member of the joint IASB/FASB Financial Institutions Advisory Group on Financial Statement Presentation.

An International Insurance Regulation Update

By Kent Barrett, CPA, CFE, CLU, ChFC

With all of the talk about change coming out of the new presidential administration in the United States ("US"),

and with the fallout from the financial crisis impacting both the US and international insurance communities, this is a good time to look at possible changes to both US and European Union ("EU") insurance regulation. In the US, the financial crisis has refueled the ever-recurring discussions (and outright arguments) about the creation of a federal insurance oversight entity. In the EU, a centralized risk-based regulatory initiative is already becoming a reality in Solvency II.

The United States

With the primary focus on the current financial crisis, both change and regulation are common themes in current US politics. It is now almost undeniable that the United States' financial system will soon undergo major regulatory reform. The troubles of insurance giant AIG, along with the collapses of countless other financial services institutions, have sparked interest in significant change at the federal level. Even prior to that, in March of 2008, former Secretary of the Treasury, Henry Paulson, proposed a regulatory overhaul plan as a blueprint for future regulatory changes. Consequently, there is little doubt that substantive change will occur in the regulation of US insurance and financial services companies, and insurers should stay abreast of all potential changes

The viability of Paulson's plan has come into question with the election of President Barack Obama and the strong Democratic majority in the Senate and House of Representatives, but any plan that does come to fruition will most likely contain the same themes emphasized by Paulson's plan — consolidation and regulation. The Secretary's plan suggested that recent changes in the insurance marketplace have put an increasing strain on the current state-based regulatory regime and that a more centralized regulatory system is needed. Paulson wanted to establish an Optional Federal Charter to aid the US in gradually distancing itself from a state-based system. These federal insurance charters would be regulated by the Office of National Insurance, which would have regulatory, supervisory, enforcement and rehabilitative powers. The plan would also establish the Office of Insurance Oversight ("OIO") which would work in consultation with the National Association of Insurance Commissioners ("NAIC") to be the lead regulatory voice in the promotion of international insurance regulatory policy for the U.S. as well as to advise the Secretary of Treasury. The OIO would also work to ensure that the NAIC and state regulators achieve uniform implementation of policy goals.

More recently, lawmakers on Capital Hill began a push for more federal oversight of insurance. Shortly after President Obama officially took office, members of Congress asked incoming Treasury Secretary Timothy Geithner "to either create an office within the Treasury Department [to increase federal oversight of insurance companies] or assign a high level Treasury appointee an insurance portfolio." There has been a significant amount of back-and-forth between interest groups within the insurance industry, such as the NAIC, the National Association of Mutual Insurance Companies (both opposed to), and the American Counsel of Life Insurers (in favor of), on the topic of federal oversight. Additionally, a subcommittee of the Group of Thirty – a private, non-profit body comprised of thirty financial experts – headed by Paul Volker (now chairman of the newly-formed Economic Recovery Advisory Board), issued a report on January 15, 2009 on the need for specific regulatory changes brought about by the economic crisis; including regulation at the federal level for "systemically significant" companies including "large internationally active insurance companies."

However, even if the new administration or Congress decides not to centralize insurance regulation, change still appears certain at the state level. As recently as October 17, 2008, US state insurance regulators met with members of international regulatory bodies at the International Association of Insurance Supervisors (IAIS) Annual General Meeting to adopt several supervisory papers addressing risk management. The papers focused on three main issues: the validity of the financial models used by troubled financial institutions; managements' and regulators' understanding of the models; and communication between companies and regulators. In an NAIC news release, the Virginia Insurance Commissioner and chair of the IAIS Technical Committee, Al Gross, stated, "As global pioneers in the application of risk-based solvency standards applied to insurers through the application of risk-based capital laws and standards, the NAIC continues to develop and expand the use of risk-management tools in monitoring the solvency of insurance companies."

Henry Paulson proposed a regulatory overhaul plan as a blueprint for future regulatory changes.

So, while there may be lingering questions about exactly how regulatory changes will occur, US insurers should begin the process of anticipating the change and investing time and resources in developing responsive action plans.

The European Union

Much more detail is available regarding changes in European Union ("EU") insurance regulation because an overhaul is already well underway. Solvency II, a risk-based assessment of an insurance company's overall solvency with both quantitative and qualitative components, has potential global implications that need to be followed by all insurance industry players. In his fall 2005 IAIR article, "Solvency II: Turning Anticipation to Action," David Lightfoot of Guy Carpenter & Company Inc. described the then-pending requirements of the Solvency II framework. The article introduced readers to the inner workings of the directive with an overview of the "three pillar approach," explained the ramifications of such a large scale regulatory overhaul, and emphasized the need for preparation by EU member insurance companies.[1]

Since the article's 2005 publication, the Solvency II initiative has seen a number of developments with the issuance of an initial directive in July 2007 and a subsequent amendment to the directive in February 2008, (collectively referred to as the "directive").[2] The directive is currently in the process of being ratified by the EU parliament, and once this occurs, will go through the process of adoption by the member states. The goal is to have it fully-implemented and enforceable by 2012, although disagreement over the concept of group supervision is currently delaying the process and a push back of the implementation date is likely.

In order to fully understand the implications of the Solvency II directive, it is necessary to have a basic understanding of the Three Pillar approach, as set forth in the amended directive. The Three Pillars are:

1. Quantitative Requirements of Capital Adequacy;
2. Qualitative Requirements of Capital Adequacy and Supervision; and
3. Transparency and Public Disclosure.

It is important to note that a conscious effort was made to keep the interests of small- and medium-sized insurance companies in mind throughout the development of Solvency II, as evidenced by the provision for a simplified Solvency Capital Requirement calculation, where justified. In fact, all elements of the directive incorporate the "principle of proportionality"— a common EU principal that requires laws and regulations to be applied proportionately with regard to nature, complexity and scale, somewhat similar to the concept of materiality. Also, the directive applies to insurance companies and reinsurance companies alike.

1 Mr. Lightfoot's article can be found on the IAIR website at http://www.iair.org/userfiles/image/files/newsletters/2005/The_Insurance_Receiver_-Vol_14_Num_03_Fall_2005.pdf

2 The most recent copy of the directive can be found on the web at http://ec.europa.eu/internal_market/insurance/docs/solvency/proposal_en.pdf

Pillar One – Quantitative Requirements of Capital Adequacy

The goal of the first pillar is to provide uniform capitalization requirements for all insurance companies. To accomplish this, the amended directive defines six elements:

1. Technical provisions based on the current exit value of policyholder obligations;
2. The Solvency Capital Requirement (the "SCR");
3. The Minimum Capital Requirement (the "MCR");
4. Own funds that correspond to financial resources available to stem risks and absorb losses;
5. The basis for the valuation of assets and liabilities; and
6. Guidelines for proper management of investments.

The first component of Pillar One is an insurer's technical provisions which correspond to a company's insurance liabilities. Technical provisions should be based on current exit value (amount an insurer would expect to pay if it transferred its contractual rights and obligations to another insurer today) and should be consistent with the insurer's obligations to policyholders and/or beneficiaries. The calculation should reflect the best estimate of the present value of future cash flows required to settle all current and future policyholder obligations, including expenses, plus a risk margin.

The next component, the SCR, is essentially a safety net capital requirement that attempts to quantify the target economic capital level required to limit the probability of an insurer's failure to 0.5% (1 in 200 year loss event). The SCR level should allow a company to handle significant unforeseen losses and provide reasonable assurance to policyholders and beneficiaries. If a firm's capital drops below this level, it would act as an early warning sign to regulatory bodies and trigger some level of intervention. It represents an additional level of required capital above an insurer's technical provisions. Companies will be able to use the standard model or their own internal model(s), if approved by supervisory authorities. All models should use a value-at-risk approach and incorporate all quantifiable risks (at a minimum: non-life underwriting risk, life underwriting risk, health underwriting risk, market risk, credit risk, and operational risk), as well as the impact of any risk mitigation. It must be calculated at least once every year and monitored throughout the year.

Much more detail is available regarding changes in European Union ("EU") insurance regulation

The MCR is the absolute minimum capital level allowed in excess of technical provisions before the regulator requires a firm to cease writing business. It must be calculated quarterly, based on a standard formula. As of the date of implementation, companies will have one year to update their MCR from Solvency I levels to Solvency II levels. In an October 2008 press release, the European Parliament Economic and Monetary Affairs Committee stated that the resulting MCR "should be between 25 and 45 percent of the company's SCR, with the exact amount being a calculation based on variables which indicate the company's ability to remain operational."

The fourth component of Pillar One will be a company's own funds, which are determined based on its financial resources, both on-and off-balance sheet (off-balance sheet items would include members' calls, letters of credit, etc.) available to absorb losses. Own funds will cover the company's two capital requirements: the MCR and SCR, and will include all eligible capital in excess of an insurer's technical provisions. Own funds will be identified through a three-step process in which the total amount available is calculated by (1) summing "basic own fund items" (items on the balance sheet) and "ancillary own fund items" (items not on the balance sheet), (2) classifying the summed items into three tiers based on individual quality and ability to absorb losses (Tier 1 funds being the highest quality, and Tier 3 funds the lowest), and (3) designating funds as eligible or ineligible based on their classification. Tier 1 funds should equal at least one third of the SCR and half of the MCR, while Tier 3 funds should equal no more than one third of the SCR and are not eligible with respect to the MCR.

The first pillar also establishes that the valuation of assets and liabilities will be based on fair value, as defined by International Financial Reporting Standards ("IFRS"). The methods for calculating fair value for specific balance sheet items are in the process of being developed with the goal of ensuring consistent valuation amongst all insurance companies over time. The valuation of liabilities will not take into account a company's credit standing, whereas asset valuations will incorporate credit and liquidity measures.

Finally, Pillar One addresses the management and monitoring of an insurer's investments. It sets forth that insurance companies must abide by the "prudent person" principle in its investing activities. This principle, which is described in the directive, mandates that the investing practices of an insurer are carried out in the best interest of policyholders and beneficiaries.

Pillar Two – Qualitative Requirements of Capital Adequacy and Supervision

The second pillar outlines the concepts of qualitative capital requirements and supervision. The main objective of this pillar is to provide adequate policyholder protection through proper risk management, with secondary goals of ensuring financial stability and fair and stable markets. The qualitative nature of the pillar should provide regulators and stakeholders with a better understanding of an insurer's true risk profile by ensuring that all available information is incorporated in the assessment. As Mr. Lightfoot pointed out, it is Pillar Two that drastically changes the regulatory review process in that it requires companies to perform an integrated analysis of their risks and capital adequacy, including both quantitative and qualitative considerations.

Under the second pillar, all insurers will be expected to undertake an Own Risk and Solvency Assessment ("ORSA") which will involve viewing the results of capital requirement calculations from a qualitative standpoint. As part of the assessment, companies will be expected to review their risk profile, risk tolerance, and business strategy in conjunction with one another in an effort to assess their compliance with capital requirements. The SCR calculation output should be incorporated into the ORSA, and any assumptions made should be evaluated. The results should be reported to the appropriate supervisory body and reflected in the company's business strategy. This approach will provide an insurance company with the ability to change its risk profile and, accordingly, its required capital through the use of risk mitigation strategies such as reinsurance, hedging, and proper risk management and governance.

In fact, strong internal controls and risk management programs will be of great benefit to a company trying to lower its capital requirements, and Solvency II will aim to provide guidance for companies in developing an effective system of governance. It will be the responsibility of the company to have written policies in place that are reviewed annually, outlining its governance procedures for internal controls, internal audit, risk management, and outsourcing. Supervisory authorities must have the right to access any information pertaining to duties outlined in the directive that are outsourced. Once Solvency II has been fully-implemented, management will have the final responsibility for compliance.

The second pillar also establishes a Supervisory Review Process ("SRP") for identifying organizations with the potential for having a high risk profile. In situations where weaknesses or deficiencies are identified by an appropriate supervisory authority (in the insurer's home state), the directive provides the supervisory body with the authority to follow-up and monitor the insurer in an effort to remedy any deficiencies. This process requires the supervisory authorities to regularly review each company's internal assessment of its risk-based capital level, in addition to the company's risk management processes, as determined by the supervisory authority. The review should be inclusive of all strategies, processes, and reporting procedures, as well as all known risks and any potential future risks.

Additionally, the supervisory authorities may provide a company with an adjusted SCR (known as a capital add-on) under exceptional circumstances. The directive mandates that the supervisory authorities have the power to take any measures they deem necessary to ensure compliance with regulatory requirements. A European Parliament Economic and Monetary Affairs Committee press release describes this pillar stating, "It shifts the focus of supervisory authorities from merely checking compliance with a tick-the-box approach based on a set of rules to more pro-actively supervising the risk management of individual companies based on a set of principles."

Pillar Three – Transparency and Public Disclosure

The third and final pillar tackles the concept of supervisory reporting and public disclosure. It aims to significantly increase the level of transparency in the insurance industry. The pillar mandates that all information necessary for effective supervision must be disclosed and requires insurers to publish an annual solvency and financial condition report. A temporary exception has been allowed for the disclosure of capital add-ons during a transitional period. Companies are required to have a public disclosure policy as part of their solvency and financial condition report and management must sign-off on the report before it is published.

Unlike insurers in the US, those in the EU have more details in hand in order to prepare for pending regulatory changes. They should note that the original version of the Solvency II directive included an impact assessment discussing the potential for side-effects that could impact the EU insurance industry, including possible reduction in some coverages, increased prices, and modified insurance mixes. Additionally, Standard & Poor's stated in a Spring 2008 report that it predicted Solvency II would prompt "consolidation in the European insurance industry" and that it "could require over 25% of Europe's insurers to re-evaluate their businesses." This would be especially true for small to medium sized insurers. However, much of this is speculation as it is too early to predict the definitive impact of such a major change.

What It All Means Now

As with most change, the outcome of changes in the regulatory environment for insurers across the globe is uncertain. In the US, no one knows who will win the debate over federal regulation of the insurance industry, and what that oversight would look like if implemented. In the EU, even though Solvency II will almost certainly be implemented and the major provisions have been ironed out, the timeline and final details are still to be determined.

In any case, the status quo will not be an option in these challenging economic times; therefore all insurers need to prepare for the implications of potential regulatory changes on both a domestic and international level. While insurers continue to follow the regulatory discussions in the US and the progress of Solvency II in the EU, they should also note that the trend is extending beyond those borders. Canada and Mexico are moving toward regulatory approaches similar to Solvency II, and rating agencies within the U.S. are beginning to promote Solvency II methodologies. Although progress on changes to insurance regulation may appear to have been slow to date, the first steps, both within the US and on an international level, appear to have been taken. Insurers should be ready for the pace to quicken.

Kent Barrett

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