



Reserve Bank of New Zealand
Financial System Policy and Analysis - Financial Policy
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Via email: insurancesolvency@rbnz.govt.nz

17 February 2021

To whom it may concern

Re: Public Consultation on the Structure of the Solvency Standards for Insurers

Thank you for the opportunity to comment on your November 2020 consultation document relating to the structure of the solvency standards for insurers. The consultation document was well thought through with broad questions and it is important to maintain the current momentum to give insurers and their Appointed Actuaries confidence about the capital calculations as they transition to NZ IFRS 17 over the next three years.

The New Zealand Society of Actuaries (NZSA) is the professional body for actuaries practicing in New Zealand. Most of the Appointed Actuaries to New Zealand's licenced insurers are members. The Appointed Actuary regime was enacted through the Insurance (Prudential Supervision) Act 2010 and each licenced insurer must have an Appointed Actuary. One of the key obligations of the Appointed Actuary is to review the solvency calculations and solvency return, which means this consultation document is of particular interest to many of our members.

This submission is on behalf of members of the NZSA and focuses on risks that an Appointed Actuary would typically consider in their work. Our aim is to ensure that outcomes are technically accurate from an actuarial perspective, rules are clear and transparent, and there is consistency across insurers. We recognise that some aspects of the solvency calculations would sometimes require input from people with other expertise (for example, technical accounting and tax) and the interpretation of NZ IFRS 17 continues to evolve as insurers progress their implementation efforts.

Our detailed responses to each question in the consultation document are provided in the attachment to this letter. At a high level, we would like to summarise six key points from our submission:

- The Reserve Bank's risk appetite underpinning the solvency standard, and thus for insurer failure, is a complex decision. A lower risk appetite may lead to higher capital or greater intervention, which may reduce the chance of insurer failure but it would also reduce the attractiveness of the sector to overseas investors and affect the cost of insurance. Ultimately the decision is a balancing act and needs to fit with the purpose of IPSA to promote the maintenance of a sound and efficient insurance sector (s3, IPSA) as well as the principles of IPSA (in particular, s4(b), s4(f) and s4(g)). We recommend that the Reserve Bank articulate a



clear risk appetite so that the consultation around the calibration of the standard is as constructive as possible.

- There is a significant risk of duplication with three different tools set out in the consultation document: a ladder of intervention, adjustments for sectorally (or systemically) important insurers, and supervisory adjustments. An insurer with multiple adjustments may end up holding capital well beyond the level that was originally intended. The interaction between all of these aspects need to be considered to ensure the ultimate capital levels are consistent with the Reserve Bank's risk appetite and intention.
- The issues discussed in the 'Dealing with IFRS 17' section cover some of the issues, but not all. It is critical that the Reserve Bank begin consulting on other IFRS 17 issues such as the projection period for yearly renewable life business (contract boundary or require a different projection period), how reinsurance mismatches will be treated and whether the starting point includes or excludes risk adjustments. Some of these concepts may be addressed if Option 3c from paragraph 62 is selected, but others require further thought. APRA have made some good progress in their recent proposals in these areas that provide a useful reference point.
- We support the ladder of intervention framework. While the framework is conceptual at this point, we expect that the practical outcome will be a ladder above the desired regulatory minimum to ensure a graduated level of supervision prior to an insurer reaching the desired regulatory minimum. We recommend that all the rungs on the ladder be statistically determined to ensure the framework is transparent and robust. Appointed actuaries would like a very clear point defined, and agreed in advance, at which the Reserve Bank would step in and take some form of regulatory action.
- The current capital ratio (known as the solvency ratio) is not a suitable measure for comparing solvency positions across life and non-life insurers. Among other things, it is distorted by levels of deferred acquisition costs and differing probabilities of sufficiency. The calculation of the ratio needs to be fixed via adjustments to the actual solvency capital amount before it could be used effectively in comparisons or any ladder of intervention framework.
- For life insurance business, whether YRT (stepped premium) business can be grouped in the same group as level premium business is a significant issue that needs further industry discussion and clarity from the Reserve Bank. Adoption of NZ IFRS 17 is likely to see YRT and level premium business in separate portfolios and, if the portfolio is used for grouping under solvency calculations, then there could be a material increase in capital requirements across the industry. If this were to be the case, the rationale for this decision would need to be made clear and the industry should be given an opportunity to respond and plan for any capital increases. We note that both APRA and Solvency II regulatory capital frameworks allow for cross-subsidies of YRT and level premium business to some extent.

Throughout our attached response, we often refer to the APRA regulatory framework. The APRA framework is familiar to New Zealand insurers given several are part of a group with Australian insurers. Comments within the attachment reflect this higher degree of familiarity rather than a suggestion that the APRA approach is best practice in terms of supervision. Ultimately the capital



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framework needs to be appropriate for New Zealand insurers and be comparable to similar frameworks internationally to promote a sound and efficient sector.

Please get in touch with us if you have any queries on our responses as we would be happy to discuss them. We look forward to working with you throughout the consultation process for updating the solvency standards.

Kind regards

A handwritten signature in black ink, appearing to read 'Ross Simmonds', is written in a cursive style.

Ross Simmonds
President of the New Zealand Society of Actuaries



Attachment: Detailed responses

1. *Principles and purposes*

A. **Would a purpose statement be a useful addition to the solvency standards? Why or why not?**

A purpose statement would be useful to articulate the intention of the solvency calculation. This would then allow any future discussions and submissions to focus on the calibration of the standard to the overall purpose, which should be more constructive and transparent for industry participants.

The purpose statement should be concise and clear, setting out what it is aiming to achieve in respect of:

- Whether the statement applies to the minimum solvency requirement or a higher level or “rung” of solvency under any proposed ladder of intervention or potentially both;
- What level of sufficiency and over what timeframe is envisaged, including the rationale for any exceptions (for example, catastrophe risk charge); and
- Whether the purpose is to ensure capital sufficiency on a going concern basis or on a wind-up basis (or any other basis deemed appropriate).

B. **Please comment on the utility of the purpose statement (“The purpose of capital is to ensure that, in adversity, an insurer’s obligations to policy-holders will continue to be met as they fall due.”) and suggest improvements, if any.**

This purpose statement provides a good starting point, but it lacks specificity. Adversity will mean different things to different people. It is recommended the statement be refined to address the three items mentioned above in our response to question A.

C. **How likely should the fulfilment of obligations by an insurer be (recognising that certainty is an impossibility, and that there is a trade-off with efficiency and competition)?**

The level of sufficiency needs to balance an appropriate level of risk to society against the associated cost of capital factored into insurance pricing.

Promoting a sound and efficient sector is a purpose of IPSA. Minimising the impact of insurer failure may ensure soundness of the sector, but it may result in a small and inefficient sector due to limited availability of international capital if capital requirements are too high on an international scale. It is important not to discourage international investment into the sector to ensure the efficiency of the sector is upheld. Many insurers operating in New Zealand have overseas parents (often domiciled in Australia) and a sufficiency level of 99.5% over a one-year period would ensure consistency with Australia, which is a logical starting point. It would also help consistency with branches of Australian companies operating in New Zealand.

When setting the level of sufficiency, it is important to consider this when introducing a ladder of intervention as this may shift the minimum level of capital targeted by insurers to be the top “rung” of the ladder as they look to avoid additional regulatory scrutiny. This results in “capital buffers upon capital buffers”, resulting in an increase in the total capital held across the industry that may be much higher than required in other countries. Investors will then require higher returns to maintain



the same return on capital, which is likely to result in premium increases for New Zealand policyholders. This is against the IPSA principles of avoiding unnecessary compliance costs and these costs will ultimately be borne by policyholders, not insurers.

D. Should the solvency risks be assumed to crystallise immediately, in the short-term (say one year) or over the long-term?

During times of adversity, the financial impacts for an insurer will typically manifest themselves within a short timeframe (that is, one year). Longer term stresses that manifest themselves more gradually tend to be mitigated by management actions, divestment and/or recapitalisation.

The APRA approach of targeting a 99.5% level of sufficiency with an ultimate view at the end of one year takes account of the short-term stresses that will have an impact on the long-term ultimate view of assets and liabilities. This is a reasonable and practical approach.

Implementing a framework where the solvency calculations are based on up to three years may be possible as that is consistent with the obligations under section 24 of IPSA. However, a longer-term view of solvency risks (that is, beyond 5 years) would be both practically and technically difficult because:

- It would be beyond the usual planning or budgeting period for most insurers, so it becomes impractical to implement without significant cost, especially given the need to project solvency out three years under section 24 of IPSA; and
- The further out the calculations go, the more judgement is required due to the increasing level of uncertainty of events many years into the future and the additional risks in the long-term (for example, the impact of increased exposure from climate change). This is likely to lead to more divergence of approaches and less consistency across the industry.

E. Should a “total balance sheet approach” be adopted for solvency calculations?

Conceptually, the “total balance sheet approach” would allow for all second-order or consequential impacts of a particular stress and be more tailored to each insurer. However, such an approach will require significantly more judgement by the practitioner, significantly more variability in interpretation between insurers and is likely to lead to a significant increase in the costs of implementation. Therefore, we do not recommend moving to a total balance sheet approach.

The current solvency approach of applying all stresses at once is simple, easy to apply and provides a level of consistency across insurers. It potentially results in a more conservative solvency position than a total balance sheet approach as it allows for all stresses to occur at once, rather than separately with consequential impacts.

Another potential way of achieving a similar outcome to the total balance sheet approach is to apply all stresses at once (like the existing solvency standards) then include an appropriate diversification benefit to allow for the fact that all stresses are unlikely to occur at the same time. See question NN.

F. Do you think there are insurers that are “sectorally-important”? If so, what would be the advantages and disadvantages of imposing higher capital requirements on them, relative to those that are considered not sectorally-important? Please provide your reasons.



As noted in the consultation document, the IAIS' assessment of systemically importance is based on five broad indicators - size, global activity, interconnectedness, asset liquidation and substitutability. New Zealand insurers lack the relative size, global activity and interconnectedness to be considered systemically important on a global scale. As a result, we do not view New Zealand as being big enough to warrant a two-tiered structure based on how big they are. Such a structure may lead to unintended consequences due to competition issues – for example, an insurer may downsize or split their businesses to avoid additional capital, which is not in the interests of the general public as smaller businesses have less ability to pool risk.

One of the more important risk aspects of larger multinational insurers, or insurers part of a large non-insurance entity, is the reliance on group operations for support that improves their financial position relative to other insurers that operate on a standalone basis. While assets related to the group would be classified as due from a related party (with a capital charge of up to 100%), there can be a lot of support provided through expense subsidies, internal reinsurance arrangements and reliance on group-wide processes or systems. An important consideration is how local insurers could operate if their parent entity became financially distressed and could not fulfil their intra-group obligations. This is an aspect being considered as part of the IPSA consultation more broadly, but from a solvency standard perspective this risk could be addressed by considering the level of group support implied within the capital charges themselves and the impact on the insurer if that group support was no longer able to support them.

We caution against making blanket rules for overseas-owned insurers without the context of how each operates within its own group, as this may contribute significantly to the overall risk profile (positively or negatively).

There are a number of small specialist insurers where failure may be disruptive to significant portions of the sections of the market that they operate in. For example, there are a limited number of underwriters for marine cargo or some credit risks. While not large, they may be considered sectorally important as their demise could severely disrupt trade in the New Zealand economy.

In general, the insurance landscape in New Zealand is a competitive one, policies across main lines of business could be substituted with policies from another insurer (even where there have been changes in circumstances of the insured as this would simply affect the price paid by the new insurer to take on the risk).

Overall we believe it would be difficult to define “sectorally-important” and we do not support creating a two-tiered system with regards to capital. A better way would be to ensure the solvency standard is appropriate for the full range of New Zealand insurers and use the ladder of intervention or supervisory adjustments to ensure capital levels are appropriate in these circumstances.



2. Application of the Solvency Standards

G. Please comment on how effectively existing solvency standards address particular sectors and subsectors of the industry.

For the asset risks, the existing solvency standards are reasonably consistent across all insurers and sectors. While there may be gaps or a lack of clarity in terms of classification of certain types of assets for solvency purposes (for example, in respect of composite insurers), the solvency standards are largely effective in respect of asset risks.

In respect of liabilities, different sectors are exposed to different risks. These risks continue to change and evolve. For example, APRA have recently proposed to expand their product grouping to split prudential reporting of life insurance business into more granular classes while they are proposing to add Cyber and D&O classes of insurance to the non-life framework. It is good practice to periodically review the classes of business within the insurance risk capital charge to ensure it appropriately addresses the evolving risks.

Other than health insurance, which is discussed below, Consumer Credit or Payment Protection insurance contracts may also be treated as life or non-life for the purposes of IFRS reporting and solvency calculations. This subsector may therefore experience similar issues as health insurance and there may be different outcomes for largely the same product.

H. Should health insurance have its own specific solvency standard? Please provide your reasoning.

Under the current solvency framework, the life solvency standard is applied to insurers reporting under Appendix C of NZ IFRS 4 while the non-life solvency standard is applied to insurers reporting under Appendix D of NZ IFRS 4. Health insurance may fall in either category, depending on whether the core business is life insurance or pure health insurance.

Going forward, there will be a single financial reporting standard, NZ IFRS 17, that all insurers must comply with. The distinction between life and non-life will be less obvious and financial reporting will be classified into short-term and long-term contracts.

Health insurance contracts are guaranteed renewable and insure risks relating to a human life. However, most health insurance contracts have the ability to vary premiums and/or benefits at short notice and can impose significant excesses or co-payments on policyholders. This results in a contract that is very short-term in nature with a short tail on the claim payments. There would be practical issues of requiring all health insurers to use the life solvency standard as pure health insurers would not produce long-term cashflow projections given their businesses are cashflow businesses that are highly sensitive to medical cost inflation.

Our preference, discussed in question I below, is to rationalise the existing standards, but we do not recommend a separate solvency standard for health insurance business as it could be treated as a product class under the non-life solvency standard.

I. Please discuss your preferences with respect to how the standards should apply to industry sectors.



Life and non-life risks have different underlying risk profiles and the NZSA is likely to maintain separate professional standards for the Financial Condition Reports relating to life and non-life businesses. The recent APRA proposals have indicated that their APRA standards will also remain separate for life and non-life business with different approaches taken to the calculations (for example, in respect to risk adjustments). Life and non-life risks have different needs when determining the insurance risk and catastrophe risk capital charges. Therefore, it remains important to retain the distinction between life and non-life business for solvency calculations.

Rationalisation of the existing standards is preferred as the differences for variable annuity, life, non-life, captive and run-off are minor variations that could be dealt with in one standard, possibly with appendices for the less used variable annuity, captive and run-off variants. An alternative to this would be to issue the solvency requirements in components - Standard X01 for calculating capital, Standard X11 for Asset Risks, Standard X21 for Insurance risk relating to life insurance business, Standard X22 for Insurance risk relating to non-life insurance business, etc. This is more consistent with the APRA framework and provides flexibility for upgrading one component without unintentionally affecting other components.

J. Please comment on how effectively existing solvency standards address statutory and other funds.

The statutory fund concept is only relevant for life insurers. The large majority of life insurers maintain only one statutory fund, so the framework does not require ring-fencing assets backing certain types of policies from assets backing other policies (participating versus non-participating, for example). Some life insurers may go beyond the regulations with sub-funds or hypothecation of assets, but generally the implementation of statutory funds in New Zealand does not offer additional policyholder security and the statutory fund concept has not been effective.

We recommend that the Reserve Bank articulate a purpose statement for the statutory fund concept before reviewing the regulations. A purpose statement will make it clear on the objectives of statutory funds and we can then support you in how to achieve the objectives in practical terms.

From an actuarial perspective, the Appointed Actuary has specific responsibilities in relation to distributions from the statutory fund. The insurer must obtain written advice from the Appointed Actuary for each distribution from a statutory fund. There is no such requirement on general insurers to obtain the written advice of their Appointed Actuary on distributions up to a parent. We recommend that the obligations on Appointed Actuaries in respect to reviewing distributions from statutory funds (and insurance companies more broadly) be considered and also clarified through a purpose statement. We think it is important for the Appointed Actuary to be involved and consulted on decisions to pay dividends.

K. Should solvency standards applied to statutory funds apply a floor to assets based on the provisions of Sections 82-119?

Consistent with our response to question J, above, the statutory fund concept would benefit from a purpose statement articulating the intended objectives. Until such time, it is not possible to comment on this question.



L. Please discuss your preferences with respect to how the standards should apply to statutory and other funds.

Consistent with our response to question K, we cannot comment on this question without a purpose statement for statutory funds.

Irrespective of statutory funds, we recommend monitoring business at a granular level (insurance fund or a class of business level) but applying solvency requirements at an insurer level. Our understanding is that the administrative burden of doing this would be minimal as most affected insurers monitor the financial position at this level already.

M. In your view, is the current treatment of insurance and non-insurance subsidiaries in the solvency standards appropriate? Please provide your reasons.

For insurance subsidiaries, the current standard measures the solvency of the licenced insurance subsidiary separately and then incorporated with the parent entity included if the parent is also a licenced insurer. The assessment of the insurer individually considers any lending between the entities as well as any diversification benefits in terms of risk margins when consolidating non-life insurance entities. This appears reasonable and appropriate.

For non-insurance subsidiaries, the equity held in those subsidiaries is treated as a related party for solvency, which becomes a full capital deduction. This may be conservative in some cases as there may be value in the subsidiaries that could be used to support the insurer in stressed situations. It also discourages the use of any non-insurance subsidiaries, as there are no capital advantages of holding retained earnings in the subsidiaries. As a result, the number of insurers with non-insurance subsidiaries in New Zealand is limited as most have either consolidated these entities into the parent or moved them to another part of their group, which makes this issue difficult to quantify.

N. If your answer to the previous question was “No”, what do you feel would be a better treatment of insurance and non-insurance subsidiaries?

For non-insurance subsidiaries, an alternative treatment would be to consider the group upon consolidation and look-through to the underlying assets and liabilities of the non-insurance subsidiary to give appropriate credit for any equity within those subsidiaries on a prescribed solvency basis. Consideration would also be given to any legal impediments for the subsidiary to provide capital up to the insurer in a distressed scenario.

It is noted that if a look through approach was taken to non-insurance subsidiaries, there may be additional operational risk considerations given a wide range of risks within potential subsidiaries that require further thought (related to question MM on operational risk charges).



3. Dealing with the impacts of IFRS 17

- O. In the context of solvency requirements, which of the options [presented in the consultation document] do you consider to be the most appropriate for New Zealand? Please give your reasons.**

Overall we agree with the Reserve Bank's preferences to consider Options 3b and 3c, in order to standardise the balance sheet prior to applying prescribed solvency stresses. This would help address differences in accounting judgements and policy choices under NZ IFRS 17, reduce dual accounting and fix issues with solvency ratio comparability under the current solvency standards.

IFRS 17 includes a range of accounting judgements and policy choices. Across the industry, this is likely to lead to a divergence in approaches to valuing insurance liabilities under NZ IFRS 17, even for products that are otherwise similar. The divergence in approaches in New Zealand is likely to be greater than under NZ IFRS 4 currently - this is, in part, a compromise to achieve less divergence in approaches globally. With a greater divergence in approaches to IFRS 17 valuations, standardising the IFRS 17 balance sheet items in terms of the valuation method is reasonable to achieve a consistent starting point prior to the application of the prescribed solvency stresses.

The existing solvency standards tend to adjust for differences in valuation outcomes through the capital charges rather than the actual solvency capital. This can distort the solvency ratios and mean that comparisons cannot be drawn between insurers. It is critical that these distortions are addressed prior to using solvency ratios as a metric for comparing insurers' relative solvency positions. Two examples of these distortions are:

- Negative policy liabilities for life insurers implicitly represent deferred acquisition costs. They increase the actual solvency capital (numerator) and are written off in the calculation of the minimum solvency capital (denominator), which ultimately reduces the solvency ratio. A recent survey conducted by the FSC revealed a large difference in the impact of these negative policy liabilities across life insurers - life insurers with larger acquisition costs are more affected than those with smaller acquisition costs. Adjusting the actual solvency capital for the differences would not only level the playing field, but it also would be an important interim step in standardising the balance sheet to ensure the solvency standard could work efficiently under either NZ IFRS 4 or NZ IFRS 17 for life insurers. This type of adjustment to the policy liabilities is consistent with the approach taken by APRA under the LAGIC framework.
- Non-life insurers have a choice on the probability of sufficiency to adopt for determining outstanding claims reserves on the balance sheet. The solvency standard requires a 75th percentile starting point for solvency purposes, but some insurers choose a probability of sufficiency greater than 75%. The solvency standard allows for this difference by including a negative adjustment within the calculation of the insurance risk capital charge. For those insurers, this means that the actual solvency capital and minimum solvency capital are both lower than if the starting balance sheet was standardised (via an adjustment to the actual solvency capital position for any differences in the probability of sufficiency). The result is that non-life insurers have the same solvency margin irrespective of their probability of sufficiency, but they can increase their solvency ratio by increasing the probability of



sufficiency on their outstanding claims reserves – this is because the numerator and denominator in the calculation of the ratio are both lower with a higher probability of sufficiency.

Standardising the balance sheet prior to applying the prescribed solvency stresses is therefore important. It is also important to ensure this occurs in the calculation of actual solvency capital rather than the minimum solvency capital to enable fair comparisons of solvency ratios, as well as reduce any burden of any dual accounting.

Dual accounting is where insurers would need to continue to prepare insurance liabilities on an IFRS 4 basis for solvency calculations and IFRS 17 basis for financial reporting, which would add significant cost to the industry (particularly the life insurance industry) as there would be two sets of financial positions produced and audited. There are significant complications in continuing to prepare life insurance policy liabilities under NZ IFRS 4 once NZ IFRS 17 has been implemented, yet it adds no value as the policy liabilities are replaced with the higher of a stressed liability or the current termination value within the solvency calculations. Dual accounting should be avoided as much as possible.

P. How do insurers currently treat non-technical insurance assets and liabilities on the balance sheet? Are all assets currently designated as backing insurance liabilities, and hence valued using the fair value approach? Are there any items (other than technical provisions) on the balance sheet that insurers are not currently measured using fair value?

All assets backing insurance liabilities would be accounted for based on the prevailing accounting standards. Our understanding is this currently means most (if not all) assets backing insurance liabilities are valued at fair value.

Exceptions to this may be for insurers in a distressed situation, or discontinued operations, where the assets may be valued at a realisation basis, or alternatively other non-financial assets such as plant and equipment or right-of-use assets measured under NZ IFRS 16. We are not aware of any other significant deviations to this and actuaries would rely on other expertise within an insurer to answer this question.

Q. How, if at all, is the treatment in (P) likely to change after transition to IFRS 17 (and IFRS 9)?

The accounting standards for valuing non-insurance assets is not changing under IFRS 17, so we would expect no change to the treatment. Most insurers have adopted NZ IFRS 9 already and there have not been any significant changes to the capital position. In some circumstances, insurers have seen an immaterial reduction in capital as a result of establishing additional expected credit loss provisions.

R. Is fair value a reasonable approach to value non-technical assets and liabilities? Would an adjustment to bring all assets and liabilities on the balance sheet to fair value for solvency purposes be appropriate?

Fair value would provide a consistent basis across insurers and would also ensure consistent valuation between non-technical assets and liabilities. This would need to be balanced against the effort required to make these adjustments. (Note that separate considerations apply to technical insurance assets and liabilities and are covered in responses to other questions.)



S. Is it necessary to have visibility of insurance receivables, and hence the associated credit risk, from a solvency perspective? If not, how do we ensure that any material credit risk is properly reflected in the solvency standards?

There are two main groups of insurance receivables: premium receivables and reinsurance recoveries. We believe it is important to maintain visibility of both groups to monitor credit risk.

Reinsurance receivables expose the insurer to solvency risk in the situation where the reinsurer fails to fulfil their contractual obligations and the insurer would need to use capital to make the payments due to the insured. It is therefore necessary to understand this exposure for solvency purposes. Insurers will continue to track reinsurance receivables on incurred claims to ensure they receive what it is due to them and therefore it is not unreasonable to expect insurers to isolate these amounts for solvency purposes.

Premium receivables are different. Where the insurer writes business direct to the insured, the premium receivable balances are often smaller and there is less solvency risk for the insurer. Should the insured fail to pay the required premium, the insured is no longer “on risk” for that period and there are limited solvency impacts (potentially only an adjustment to the previously declared profits that are recognised on an “earned” basis).

Where the premium is collected via a third party, particularly a broker, there is more solvency risk from premium receivables. A premium is deemed received by the insurer as soon as a broker has received it and, if the broker fails to pass this money onto the insurer, then the insurer is still exposed to all the risks associated with that insurance contract. Premiums receivable balances represent a material percentage of premium income for intermediated insurers (often 30%) and it is important to understand the ageing of these outstanding premiums to assess the credit risk appropriately.

It is noted that, for property insurers, reinsurance recovery balances have been much larger than premium receivable balances in recent years. This is due to the remaining reinsurance recoveries on significant natural disaster events - namely Canterbury and Kaikoura - and this relativity is not necessarily expected to be a long-term feature of the industry.

T. How do insurers currently measure insurance receivables and payables (premium and reinsurance recovery receivables, claims payable)?

General accounting principles require any receivables to be written off at the point they are no longer likely to be received. The approaches are typically determined by finance professionals rather than actuaries. The exception might be notified but not admitted claims reserves, where actuarial techniques are often employed to estimate the likely payments.

This means that the receivables may allow for some credit risk if the amounts are no longer likely to generate cashflow for the insurer, but the amounts at risk are often not probability weighted so they may mis-state the credit risk.

U. How are insurers looking at implementing the changes relating to insurance receivables and payables resulting from IFRS 17 from a systems perspective? Are major system changes to collate the receivables/payables system with the valuation system being considered, or will separate systems be maintained, with a high level adjustment being applied to incorporate the receivables/payables into the measurement of insurance contracts?



IFRS17 projects remain in their infancy in New Zealand and it is too early to say what insurers will do from a systems perspective in this regard.

In theory, actuarial models should be changed to have expected cashflows based on when the insurer expects to receive or pay amounts, rather than when premiums are billed and claims or expenses are incurred. However, some insurers may choose to maintain separate systems for administration, claims and debt collection with an adjustment for receivables or payables done at a later stage, potentially at a higher level. Relief was provided to insurers in the June 2020 IFRS 17 amendments to require presentation at a portfolio level rather than a group level, which reduces the operational burden for insurers and may mean there are less system changes required than previously anticipated.

When designing new solvency standards to cater for IFRS 17, it is important to clarify the basis for the cashflows in insurance liabilities. If they are probability weighted and based on when cashflows are expected to be received or paid, then they will implicitly allow for receivables and payables with an allowance for credit risk and claims decline rates. This may make it more difficult to isolate the receivables and payables directly from the valuation output. However, if the cashflows are consistent with current practice (on an accrual basis) with adjustments made to the liabilities for receivables and payables at a later stage, then identifying insurance receivables and payables will be a more straight-forward exercise.

V. If the measurement of insurance receivables under IFRS 4 currently includes an allowance for impairment, how will insurers change the basis to determine the impairment related to insurance receivables after transition to IFRS 17?

NZ IFRS 4 typically results in insurance receivables held at 100% until the receivable becomes unlikely and then the receivable is written off in full - that is, it's usually either all or nothing. NZ IFRS 17 requires a series of probability weighted cashflows, which is more of a graduated scale as the likelihood of receiving an outstanding amount reduces over time.

The impairment assessment included in NZ IFRS 17 is likely to be on a best estimate basis, which may not reflect enough credit risk for solvency purposes.

W. How are the tax items on the balance sheet likely to be impacted by IFRS 17 (and IFRS 9)?

The tax rules for New Zealand insurers are being reviewed by the IRD to ensure they remain appropriate for reporting under NZ IFRS 17. This presents some uncertainty as to the outcomes from a tax perspective.

In general terms, income tax is paid based on billed premiums less incurred claims and expenses with an adjustment for a specific set of tax reserves. There is less of a link to IFRS accounting requirements and therefore the current tax amounts are less likely to be affected by the change to NZ IFRS 17 than they are in other countries (for example, Australia).

Based on current information, it is unlikely insurers will generate any significant tax losses on transition. The impact for current tax calculations are more likely to be a practical one, as amounts currently required for tax purposes may not be included in the income statement with NZ IFRS 17.



There will be other impacts on deferred tax balances, particularly for life insurers. All changes in the deferred tax balances, whether they affected deferred tax assets or liabilities, are removed from the actual solvency capital and therefore do not have any solvency impact under the current standards.

X. Will there be any flow on impacts of tax impacts on other insurance and non-insurance items on the balance sheet?

There may be a second-order impact for some insurers if they move from net of tax discount rates to gross of tax discount rates. NZ IFRS 17 requires all cashflows, and therefore discount rates, to be determined on a gross of income tax basis, while under NZ IFRS 4 some insurers use gross of tax discount rates and others use net of tax discount rates. For the insurers currently using net of tax discount rates, this is likely to reduce the value of any interest rate sensitive insurance liabilities.

It remains unclear under the existing solvency standards whether tax deductions can be claimed for the impacts from the various solvency stresses or not (and, if they are, what the basis for determining the deferred tax asset upon wind up should be). This is a known uncertainty in the industry and it is recommended that the approach to tax, including determining any deferred tax asset upon wind up, be more clearly prescribed to ensure consistency across the industry.



4. Ladder of intervention framework

Y. Should we implement a ladder of intervention approach to solvency? Please give your reasons.

Overall we support a ladder of intervention framework as it will allow insurers to prepare their risk management responses accordingly and should result in a more resilient sector.

We recommend that all the rungs on the ladder be statistically determined to ensure the framework is transparent and robust. However, we recognise that this will inevitably involve a compromise between having a simple, practical framework, and taking the particular risk profile and balance sheet structure of each insurer into account. Appointed actuaries would like a very clear point defined at which the Reserve Bank would take some form of regulatory action, including restrictions on ceasing to write new business. We note that it's likely that the Reserve Bank will wish to retain the ability to act even if the ladder requirements on their own are met, should other circumstances require it.

As outlined in paragraph 105 in the discussion document, the regulator already has a number of intervention tools that can be utilised. These may be based on a quantitative trigger - such as the solvency position - or may be based on other qualitative triggers - such as concerns with the risk management or governance within an organisation. Requests for information and mandatory directions can already be issued to an insurer, along with changes to licence conditions. However, currently there is no guidance as to when or how those intervention tools will be applied so they can be a surprise to insurers. A ladder of intervention framework could be introduced in order to provide this clarity for insurers.

NZSA members have noted that while the reasons for licence condition changes are clear, the methodology for deriving the amounts or ratios in the licence conditions is sometimes unclear and cannot be reconciled to the insurer's own information. There is a limited ability to challenge the methodology and the Reserve Bank's decision is final. Therefore, it is recommended that the rungs on the ladder be set with reference to clear and transparent guidelines that are statistically based, considering the individual insurers' circumstances to avoid the ladder becoming another blunt intervention tool. A 120% solvency ratio as the top rung won't be appropriate for all insurers as their risks and risk management are not all equal and there are comparability issues with the solvency ratio measure currently).

The ladder of intervention should also not discourage capital investment in the sector - for example, to improve systems and processes in order to become a more resilient business. The Reserve Bank's intervention should not curtail a well-run and adequately capitalised insurer if the breach of the upper level is a temporary one to improve the financial position of the business in the long-term.

Currently there is a suggestion that in the event of a breach of the PCR an increased range of 'tools' would be available and the RBNZ would have discretion with regards their application, but when the solvency 'floor' of MCR is breached, intervention will be mandated. Consideration should be given as to whether a mandated response is appropriate, particularly if the breach is a trigger for liquidation (see the response to the next question).



Z. At what point should the insurer's operations be considered to no longer be viable?

We do not believe that it is possible to have a single measure for all insurers that determines whether an insurer's operations are no longer viable.

While balance sheet insolvency is a convenient measure to consider as it aligns with requirements under the Companies Act, it may not be suitable as a single measure of viability because:

- It is a matter of opinion involving judgement in the valuation of uncertain insurance liabilities, which may be valued materially higher or lower by another set of independent experts;
- Following the implementation of NZ IFRS 17, the balance sheet may not reflect the economic reality of the assets and liabilities (for example, due to the mismatch between the contract boundaries of underlying and reinsurance contracts);
- As an insurer approaches balance sheet insolvency, the valuation of assets may shift from a fair value basis to a realisation basis and this may change the results significantly; and
- A single quantitative measure does not consider other qualitative factors such as the risk management programme, capability of directors and officers and forward-looking prospects (including any potential recapitalisation).

Each situation involving a distressed insurer should be considered on a case by case basis to determine the long-term future prospects. A key principle of IPSA is to promote confidence in the insurance sector, which should involve minimising the potential ramifications of any insurance failure to policyholders. Liquidation and statutory management should be used as a last resort after close supervision through the ladders of intervention in order to encourage the insurer to first de-risk, recapitalise or divest the business.

AA. Conversely, what point in an insurer's solvency level triggers the need to start increasing the intensity of supervisory intervention from BAU supervision?

As mentioned in our response to question Y, above, we believe that triggers based solely on the solvency ratio or solvency margin are a blunt instrument. There are likely to be qualitative and well as quantitative measures that need to be taken into consideration. It will be a case-by-case decision that should be statistically-based and linked to a probability of breach, defined by the regulator. Insurers should articulate these triggers within a capital management plan (or similar) and the regulator could review any changes in methodology as appropriate. Smaller insurers may have challenges in carrying out such assessments and it may be appropriate in these circumstances to prescribe the trigger levels based on experience and judgement, potentially informed by market intelligence, the regulator could specify a default setting that could be used by insurers that are eligible for an exemption from undertaking this analysis themselves.

We expect that the point where intervention starts would sit above the Reserve Bank's desired minimum level of capital to ensure there can be a gradually increasing level of intensity in supervision. Once the point at which intervention starts is set using a statistically-based approach described above, it is then important for the invention steps considered by the Reserve Bank to be clear and transparent.



BB. Should we adopt an ICAAP/ORSA-type approach alongside the solvency requirements? If so, are either of these frameworks a good starting point for New Zealand? Please provide reasons supporting your statements.

Yes. An ICAAP approach is already used by many Australian-owned insurers. It represents good industry practice as it documents and monitors how capital management is integrated with risk management, which goes beyond a standard capital management plan. We are not as familiar with ORSA, but understand it achieves similar objectives to the ICAAP.

From an actuarial perspective, the Appointed Actuary can rely on the ICAAP for comments in their FCRs as it is a centralised framework and set of documents that cover the risk management framework. In this respect, it should give Appointed Actuaries comfort that the business is being managed appropriately and the concept is likely to be supported by most members.

However, it is also recognised that developing an ICAAP is a significant undertaking, particularly for smaller insurers with limited resources and no Australian parent to rely on. Thus the prioritisation of implementing any similar framework should be considered to ensure there is sufficient time to comply as it can be implemented following the full review of the solvency standards and IPSA.

CC. Are any of the above measures (solvency ratio, assets/stressed liabilities, probability of failure) more or less appropriate to calculate and assess an insurer's solvency position, from the point of view of implementing an effective ladder of intervention framework? Please give your reasons. If not, what measures do you consider would be more appropriate for this purpose?

As discussed in our response to question O, the current solvency ratio is not a measure that is comparable across insurers. Adjustments to the calculation of the current solvency components are needed to ensure the solvency ratio is comparable across insurers with different mixes of business, levels of acquisition costs and probabilities of sufficiency. Subject to these adjustments, a revised calculation of the solvency ratio may be appropriate as it is a standardised measure that could be comparable across insurers of different sizes. It may be useful for smaller insurers where more sophisticated techniques may be impractical.

The stressed assets over stressed liabilities measure is similar to the solvency margin and it is not a standardised measure. It would require more effort and resources to set the various rungs on the ladder. However, this could be an appropriate measure if the solvency ratio was not adjusted to be comparable.

We agree that the probability of failure would be appropriate to calibrate rungs on the ladder (rather than a rung by itself). That is, you may calibrate the top of the rung so that there is a 1 in X year chance of breaching the lower rung but that ultimately translates into a specific regulatory capital ratio or margin that is agreed with the Reserve Bank via the insurer's ICAAP. It is important for Appointed Actuaries to have absolute clarity on the specific levels of capital where intervention begins so a process of agreeing these trigger points on the ladder with the Reserve Bank should be put in place. We accept that judgement is needed to set those trigger points based on both quantitative and qualitative factors, but this should be done in advance to ensure expectations from the Reserve Bank are clear.



DD. What approach would strike the right balance between clarity and discretion when setting out supervisory responses at different levels of the ladder of intervention?

We assume (and expect) that the ladder of intervention is intended to sit above the desired minimum capital requirement. As a result, a breach of the top rung would be expected to occur relatively frequently - perhaps every few years - and intervention should be light touch at first, gradually increasing intensity if the capital position continues to deteriorate.

There is a risk of any ladder of intervention that insurers may increase target capital levels such that they minimise the likelihood of *any* additional supervision from the regulator. This would effectively make the top rung a new minimum capital level, which would result in a buffer on top of the ladder and push overall capital levels across the industry up. This may not be the intention as it may result in uncompetitive levels of capital on a global scale, reducing the maintenance of a sound and efficient insurance sector.

There should be clarity on the range of supervisory responses that could be used and expectations set as to the frequency of breaching each rung, which is consistent with a statistical basis for determining each rung. It should be made clear whether it is reasonable to expect an insurer to breach the top rung, from time to time, and that intensity of supervision will increase gradually as the insurer falls down the ladder. It is appropriate for the Reserve Bank to use discretion in terms of its supervisory responses because each situation will be unique and the Reserve Bank is best placed to take into account the insurer's individual circumstances; however, these trigger points should be agreed in advance so that Appointed Actuaries have absolute clarity when severe intervention measures (such as restrictions on writing new business) are likely to occur.

EE. What should our risk appetite be in relation to insurer failure?

We do not think there should be a risk appetite for insurer failure but there should be a very low risk appetite for adverse policyholder impacts arising from an insurer failure (or a distressed insurer). This is an important distinction.

In a situation of a distressed insurer, it is preferable to help the insurer resolve their issues and ultimately minimise the impacts to policyholders. Resolution may come via recapitalisation initiatives, transfers of policies to another insurer or schemes of arrangement. The distressed insurer may ultimately fail but protecting policyholders should be the primary objective. It should be acceptable to let an insurer fail if policyholders are protected in the long-term. Protecting policyholders should be the primary objective, not minimising insurer failure.

With a ladder of intervention and additional supervisory tools, the likelihood of insurer failure should be less anyway, and this should be taken into consideration as well.



5. ***Solvency calculations***

FF. Would you be comfortable with handling some deductions from capital through the Resilience Risk Capital Charge? Why or why not?

Whether an asset is dis-allowed for solvency purposes by applying a deduction from capital or a 100% capital charge will result in the same solvency margin. However, the solvency ratio will differ depending on what approach is taken.

The current approach in the solvency standards is to have a small number of deductions from capital in order to preserve the consistency with IFRS net assets. This makes checking the solvency calculation easier but reduces comparability across insurers, as noted in our responses to questions O and CC.

As a result of changes to IFRS reporting, the IFRS balance sheet will become less reliable as a starting point for an economic balance sheet (particularly for life insurers). We would expect *more* deductions (or additions) to capital going forward rather than less to ensure that the capital amount in the numerator of the solvency is standardised and closer to an economic measure of capital. This would improve comparability of the solvency ratio across the industry - for example, it would result in equivalent treatment across insurers that chose to expense acquisition costs immediately versus those who carry an asset for acquisition costs allocated to future renewals.

It is reasonable to shift some of the existing deductions from capital to the Resilience Risk Capital Charge where there is a possibility that those items have value on a going concern basis. This includes deferred tax assets and equity investments in related parties.

With regards to deductions (or additions) to capital, there are two other items that result in New Zealand being inconsistent with other jurisdictions. It is recommended that both of these items be considered in the review of the solvency standards:

- The deduction for dividends declared as it currently leads to unintended consequences whereby insurers plan the timing of dividends to avoid any periods between the balance date and when the solvency return is finalised. This may not be the intention and is different to the approach taken by APRA (so may present challenges for Australian owned insurers).
- There is no credit for any surplus arising from the Liability Adequacy Test (which will be replaced by the onerous contract test under IFRS 17). This results in a more stringent solvency requirement for non-life insurers compared to Australia where there is an adjustment for this through the excess technical provisions added to the capital base. It can be a material item.

GG. Do you believe that some value should be allowed for certain deductible items at higher levels on the ladder of intervention? Is it appropriate to assume a 'going-concern' valuation at these levels?

Prior to LAGIC in Australia, there were standards for solvency and for capital adequacy. Solvency was based on a wind-up basis with an expense reserve while capital adequacy was based on a going concern basis with a new business reserve. This has since been replaced by LAGIC with a single minimum capital requirement and an ICAAP to manage capital at reasonable levels above that.



Giving credit to insurers for deductible assets at different levels on the ladder of intervention will require a prescribed set of rules to ensure this is applied consistently across the industry. This adds a practical complexity that should be weighed up against the theoretical benefits.

HH. Is it appropriate for us to adjust insurer solvency calculations?

There are situations where an adjustment to the solvency calculations is an appropriate response. New Zealand is a small country with a diverse range of insurers that continue to change and evolve so it is difficult to create solvency standards that work appropriately in all circumstances. However, we expect that most situations would be resolved by the Reserve Bank issuing additional guidance – for example, to clarify any areas where adjustments may be required. We note that there is a difference between applying licence conditions and adjusting solvency calculations as the former is a requirement above the minimum that may not be disclosed whereas the latter is within the minimum that is disclosed.

However, the scope of the Reserve Bank's ability to adjust solvency calculations should be clear, potentially restricted to certain charges or classifications of assets. There have been instances where the Reserve Bank has directed insurers to value certain assets or liabilities under accounting standards that are inconsistent with other technical accounting opinions or the views of the insurer's auditor. It is noted that the valuation of assets and receivables is not always an actuarial responsibility and insurers should be able to rely on technical accounting opinions if prepared by a suitably qualified accounting professional, similar to insurers relying on an opinion from the Appointed Actuary. If there is a difference of opinion, advice should be sought from an independent third-party with the relevant expertise.

II. Does the list in paragraph 140 cover all circumstances where solvency calculations should be adjusted?

The circumstances in paragraph 140 are very broad and should cover most of the circumstances for when solvency should be adjusted.

Other circumstances requiring adjustments within the solvency calculations arise for small insurers (the fixed minimum capital amount) and in rare situations where the MSC is below zero. Neither situation relates to the insurer's use of judgement but they potentially relate to the third situation in paragraph 140.

JJ. Do you support introducing supervisory adjustments as an integral part of the determination of capital requirements?

Yes, we support this in principle (consistent with our response to question HH).

Consideration should be given to whether supervisory adjustments are disclosed or not. APRA do not allow supervisory adjustments to be disclosed, presumably because this may send negative signals to policyholders and shareholders even though the insurer may be appropriately capitalised for the risks it is exposed to. The NZSA does not have a consensus view on whether supervisory adjustments should be made public.

In determining supervisory adjustments, we recommend having a robust and transparent framework for determining the adjustments. Having a publicly available methodology or a scorecard (for example, APRA's Probability and Impact Rating System, PAIRS, and Supervisory Oversight and



Response System, SOARS) will help in making this process defensible. Comments from NZSA members in the past have noted that the reason for licence condition changes have been clear but the workings to arrive at the numbers selected appear arbitrary at times and lack any supporting calculations because the Reserve Bank does not release their workings. This makes it difficult for an Appointed Actuary to understand the logic or challenge the approach in circumstances where the adjustments may be deemed to be unreasonable or unsupported.

KK. Are there other forms (other than fixed amounts, ratios and valuation instructions) that the supervisory adjustments could take?

In Australia, supervisory adjustments can also be in the form of adjustments to the quality of capital used. While this is less relevant in New Zealand under current solvency standards, this may become more important depending on what the final solvency standards look like. In the review of New Zealand bank capital, there was an overall increase in capital requirements but there were concessions on the quality of capital that could be used to fund the increased capital requirements. A similar concession may be needed for New Zealand insurers.

LL. Should New Zealand adopt a more structured risk hierarchy? Why or why not?

We have no preference as to whether there should be a risk hierarchy or not. The purpose of a hierarchy is unclear and it is less important than the risks addressed by the solvency standard.

MM. Is it necessary to introduce risk charges for risks currently not hypothesised in solvency standards, for example operational risk? Why or why not?

In theory, a charge for operational risk in the solvency standards sounds sensible. In practice, they are hard to implement effectively in a market such as New Zealand where there are a lot of small insurers. Constructing operational risk models is more art than science and the results are driven by extreme tail events, which would not give the appropriate credit to insurers with well-managed operational risk management programmes. Applying a fixed percentage based on premium volume would be a blunt instrument that is not sensitive to the underlying risks or the control environment.

We believe capital levels held by an insurer should address any material risks to the insurer. Capital held for risks such as operational risk could be within the minimum solvency capital requirement or it may be more appropriate to be a required feature of the target capital, potentially through a ladder of intervention framework. Any charge within the minimum requirement should be practical to apply, especially for smaller insurers where sophisticated modelling of certain types of risks (including operational) is not feasible.

NN. Should solvency standards allow for a diversification benefit of some form? Is the Solvency II approach to relating risks appropriate for New Zealand conditions?

In principle, we support the introduction of a diversification benefit as risks are not perfectly correlated.

In the interest of transparency and consistency across insurers, it would be best to have a specified matrix of diversification benefits than use a total balance sheet approach. Consideration should be given to:



- Whether the risks included in the diversification benefit are both asset risks and liability risks or liability risks only; and
- The probabilities of sufficiency of starting points - for example, a higher probability of sufficiency for non-life insurers leads to a lower IRCC for outstanding claims, which may understate the diversification benefit if the capital charge is taken directly.

It is noted that general insurers may already factor in some level of diversification when setting their risk margins, potentially including diversification across premium liabilities and outstanding claims. This diversification currently only relates to insurance liability risks, not any other risks in the solvency standard. Life insurers (or single line general insurers, including standalone health insurers) do not have any such diversification, which is a clear difference between the sectors of the industry.

OO. Should the deduction for policy and other liabilities be moved inside the Life IRCC?

In respect of policy liabilities, adjustments should be made to the actual solvency capital to improve comparability of the solvency ratios. By replacing policy liabilities by adjusted policy liabilities in the calculation of the starting capital balance will make the ratio a fairer comparison across insurers with large acquisition costs and those without. It also removes the need to deduct policy liabilities from the Life IRCC.

Other liabilities are added in the Life IRCC then deducted later. There is no solvency effect from other liabilities and it is only presentational. This could be simplified by not adding other liabilities into the Life IRCC then removing them later.

PP. Are any of the following grouping options (Insurer, statutory fund, IFRS 17 portfolio, regulatory groupings, IFRS 17 groups, individual policy) appropriate for solvency purposes? Please provide your reasons.

The choice of grouping depends on the Reserve Bank's intention of the solvency standard. If it is to be determined on a run-off / wind up basis, then that may lead to a different outcome than on a going concern basis.

We recommend that this decision be split into two key decisions:

1. The level of grouping at which the Reserve Bank would like to monitor lines of business and collect data for prudential reporting or industry analysis. This could be similar to the IFRS 17 portfolios, but ideally would be a prescribed list of classes of business (and consistent with that used in insurer data returns). Monitoring performance at this level would give the Reserve Bank and other stakeholders information about trends in profitability at a class of business level. Consideration would need to be given to expense apportionment as often overheads are not allocated down to a granular level (so it might be more practical to monitor profitability after allowance for direct expenses but not overheads).
2. The level at which solvency calculations should be performed and, in particular, the level at which the termination value minimum is applied for life insurers. This may be at a higher level to allow for the natural cross-subsidies between similar products, such as level premium and yearly renewable premium options within the same product line. APRA's approach is to apply a termination value minimum at a participating / non-participating level. The Solvency II approach is to allow for a 50% (or similar) shock lapse, which allows assets on



some lines of business to offset liabilities on others (as opposed to a termination value minimum, which is equivalent to a 100% shock lapse). Both are other options that were not considered in the consultation document.

Without splitting the decision into two parts, the Reserve Bank risks having significant and unintentional consequences for capital requirements for life insurers. NZ IFRS 17 portfolios are likely to be more granular for life insurers with level premium and yearly renewable contracts in separate portfolios. Applying the current termination value (CTV) minimum at the NZ IFRS 17 portfolio level is likely to require significantly more capital across the industry. If this is the intention, the Reserve Bank should communicate their rationale for this early to give insurers time to respond and potentially prepare for significant increases in capital levels.

The NZSA does not have a consensus view on whether YRT stepped life business should be allowed to be combined with level life business within the solvency calculations. Allowing for full cross subsidies in all cases may not appropriately reflect the reality of a distressed situation, but some cross-subsidies may be reasonable in certain circumstances. A framework where YRT and level business is separated, which is where there are no cross-subsidies, would be equivalent to assuming all yearly renewable business lapses immediately but the level premium business remains. This may be unrealistic in a distressed situation as there is likely to still be some value realised for the yearly renewable book if it was sold to support the level premium business. An alternative might be to have a high shock lapse assumption instead of the CTV minimum to recognise that there could be some groups of policies in an asset position after all the stresses are applied that could be used to offset any liabilities - this approach is more consistent with the approach taken under Solvency II. We recognise that there could be a wide range of distressed situations that need to be considered and there needs to be further industry consultation on this issue with a consistent approach applied across the industry to ensure a level playing field.

Also note that policies attaching to IFRS 17 groups can change over time (that is, a group can move in and out of onerous depending on the experience). Furthermore, one of the options where grouping is at an individual policy level so that no policy is an asset is a very impractical solution as assumptions are not set at a policy level so it would have a significant level of spurious accuracy. This suggests that any grouping at the IFRS 17 group or below would not be appropriate.

QQ. Are there any other grouping approaches that you consider would be appropriate for solvency purposes? Please provide your reasons.

See response to question PP, above. We recommend splitting the grouping question into two decisions and considering a participating / non-participating level for applying the CTV minimum for life insurers.

RR. What are your views on our preferred option of specifying regulatory groupings for solvency purposes? What basis do you think should be used to form the regulatory groupings? Please provide your reasons.

In principle, we support the option of specifying regulatory groupings, both for prudential reporting and for solvency calculations or applying termination value minimums for life insurers. This will ensure consistency in the treatment across the industry.

Some NZSA members may wish to use their own groupings for various reasons. There may be a general industry consensus on appropriate groupings over time too. However, the objective of



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ensuring standards are fair and consistent to all insurers should prevail and there should be a process whereby members can share their feedback on any proposed groupings before they are finalised.

Whatever decisions are made in this space it would be helpful if there could be early consultation and communication of the decision in order that insurers can consider any system changes and capital implications resulting from these groupings at the same time that the IFRS changes are being implemented.