Macroprudential Surveillance in Practice

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U.S. Legal Entity Focus

- U.S. Insurance Regulators Regulate Insurance, NOT Financial Markets
  - Macroprudential Surveillance Is Not a Primary Function
    - We Will See It Is Used in Powerful Ways in the Regulation of Legal Entities

- U.S. Legal Environment
  - Insurance Policy Promises Are the Legal Obligations of the Individual Underwriting Entity, not the Entire Group
    - Traditional U.S. Holding Company Review Focused on Transactions with the Insurer
    - AIG Lessons Learned – We Need to Consider Reputational and Contagion Risks of the Entire Group

Macroprudential Surveillance – Aggregation of Data

- Rich Statutory Blank with Detailed Investment Data

- Data Capture ALL financial data and other data as practical
  - Remainder Captured in PDF

- Allows Simple Pull of Data at Various Levels of Aggregation

Aggregated Data Used in Legal Entity Analysis

- Compare Individual Legal Entity Results to those of:
  - Other Insurers in the Group
  - Peer Groups
  - Averages for All Writers of the Line of Business
  - Industry Sector
  - U.S. Insurance Industry as a Whole
  - Worldwide Insurance Data

Aggregated Data Used in Legal Entity Analysis

- Non-Insurance Market Data Used as Well
  - U.S. Employment Data, State Unemployment Data, etc.
    - Assess Future Difficulties in Selling Policies
  - U.S. Investment Markets Data
    - Assess Future Strains on Investment Income
    - Assess Future Losses in Specific Investment Types
    - Compare Insurer Returns to Market Returns to Assess Future Difficulties in Attracting Capital

NAIC Standard Setting

- Aggregated Statutory Financial Statement Data Used to Identify Changes to the NAIC Statutory Blank
  - Add Specific Line to Assets/Liabilities for "Write-Ins" if an Item Becomes Common Across the Industry
- Risk-Based Capital Changes Result from Review of Aggregated Statutory Financial Statement Data and Investment Markets Data
  - Refining the RBC Mortgage Loan Risk Charges
- Concern with Rating Agencies
  - RMBS and CMBS Statutory Process Now Uses Modeled Loss Projections Instead of Rating Agency Ratings

Stress Testing

- Investment Markets Data and Statutory Filings Data Used to Perform Top-Down Stress Testing in 2009
  - Loss Scenarios Were Based on Investment Market Data for Trending Purposes:
    - 28% Loss Scenario for RMBS Subprime
    - 50% Loss Scenario for CMBS Subordinate
    - 40% Loss Scenario for Unaffiliated Common Stock (30% for Affiliated)
    - 30% Loss Scenario for Real Estate
    - 5% Loss Scenario for Mortgage Loans (Investment Market Data Suggested a Higher Loss Scenario, but Analysts View U.S. Insurers as Not Materially Subject to the Reduced Underwriting Standards Issue)
  - Use of Actual NAIC Designation Migrations from 2008 to 2009 for RMBS and CMBS:
    - Used a Duplication of the Actual Designation Migrations (Another Migration Equal to the Actual Migration that Occurred) as the Stress Scenario

Questions?