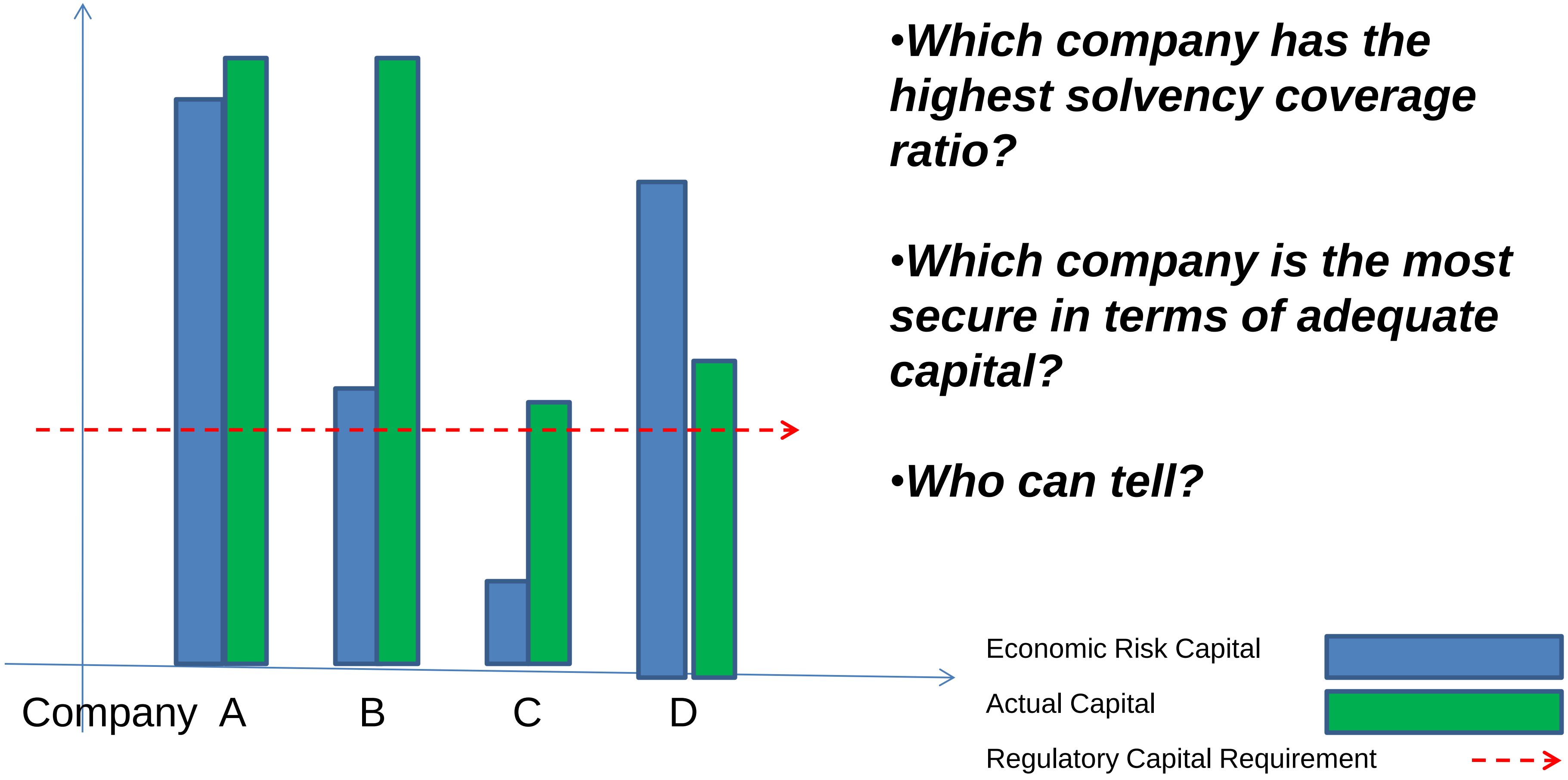
Risk Based Capital Regimes Some experiences of insurers and regulators

Craig Thorburn
Senior Insurance Specialist, The World Bank
cthorburn@worldbank.org
+1 202 473 4932 or +1 202 470 6012
Skype: craig_thorburn

Conceptual Diagram



- ***Which company has the highest solvency coverage ratio?***

- ***Which company is the most secure in terms of adequate capital?***

- ***Who can tell?***

Country Cases

- Australia, Thailand, Papua New Guinea, Sri Lanka, and 5 others
- IAIS Solvency Subcommittee
- Mixture of additive and combinatorial approaches
  - increasingly additive is used
- All moving from a Solvency I system

Advantages / Positive Outcomes

- Strong performance through GFC
- All insurers (not just the best) have a better focus on risk and risk management
  - Especially to include risks associated with assets, reinsurance, and forms of capital
- All insurers make business decisions based on risk and capital considerations that are the same

- Arbitrage driven business initiatives are greatly reduced, some risk activity reduced.
  - People engaged in managing rules are redeployed
  - Boards and Senior Management focus on some material risks more than before
- Supervisor / Insurer discussion is about risk rather than rule oriented
  - Extend beyond minimum requirements

Experiences - In the beginning

- Not all insurers or other stakeholders are at the same level
  - The best risk oriented insurers already agree and want it aligned to their internal approach
  - The least risk oriented insurers think it is a rule change
- Some other stakeholders argue for increased absolute minimum capital
- General nervousness or suspicion with the topic on the table or the potential for inadequate transitions
- Some want a different and specific reform that they consider ‘more important’

Experiences – along the way

- Concrete proposals increase focus
  - Earlier consultations draw focus from technocrats rather than managers and boards
- Some data may not be immediately available
- Some stakeholders start to advocate for more risk sensitivity

Experiences – at the end

- “This is a great system”
- Without these reforms, the GFC would have been a problem
- We have grown up some more
- Increased credibility in consultative approach and reliability of rulemaking intentions among insurers
- Increased respect / credibility of the sector, reduced funding costs, some cases of exit or merger in some but not all countries

Why RBC is worth pursuing

- To better reflect risk, RBC brings incentives into line with economic realities
  - Reduce activity motivated by rules rather than risk (reality)
  - Increase efficiency in insurance markets and the wider economy
- Supporting RBS
  - Align signals to supervisors with reality (or should be) of management
  - Make the solvency coverage ratio comparable for intervention signals

END