



The Actuarial Profession  
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# 31<sup>st</sup> ANNUAL GIRO CONVENTION

12-15 October 2004, Hotel Europe, Killarney, Ireland

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# CP190 Update

Alan Spence (Chief Actuary)  
Stefan Claus



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# Overview of today's presentation

- Overview of the regime
- Update on final decisions in PS 04/16
- Future developments
- Process for giving ICG
- Modelling approaches and issues
- Early experiences



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## Some FSA Maths

- CP 190 = PS 04/16
- CP 178 = CP 04/7
- PRU 2.4 = PRU 2.3!

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## Overall aims

- Principle 4
- A firm must maintain adequate financial resources
- Senior management responsibility
- Identify the major sources of risk
  - Credit, market, liquidity, operational, and insurance
- Consider how they will be dealt with
- Stress and scenario test / model

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## Overall approach

- ECR as 'benchmark'
- Individual capital assessment by firm (ICAS regime)
- FSA review
- FSA gives Individual Capital Guidance (ICG)

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## ICAS framework

- We aim to make it practical and be practical
- Proportionate to the nature, scale and complexity of the firm's activities
- Integrated with the RAF process

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## Update on final decisions in PS 04/16 (1)

- Soft test
- Factors for ECR unchanged *except for*
  - Investments in money market funds – charge reduced to 0%
- Rejection of increased granularity for charge for reinsurance debtors; fixed interest investments and pecuniary loss
- Makes clear the confidence level ICA should be prepared to

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## Update on final decisions in PS 04/16 (2)

- Clarification of exclusion of non-directive mutuals
- Derivatives – no intention to act as disincentive to use for risk management
- ECR reporting requirement in public removed
- Increased clarity of our thinking for run-offs
- Some changes in definitions of capital

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## Confidence level

- Because ICG is in effect an intervention level we want a level playing field
- Prudence or otherwise in some assumptions would make this difficult
- So: 99.5% confidence level over one year period OR, IF APPROPRIATE TO THE FIRM'S BUSINESS A LOWER CONFIDENCE LEVEL OVER A LONGER PERIOD

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## Future developments

- Main roll out for companies starting now
- Lloyd's approach still being developed and a lot to do – but managing agents should all be clear that they have to be ready by 2005
- Should complete all firms by end of 2006
- We expect continuous evolution of industry and FSA capabilities as we move forward
- Solvency II – should be clearer by 2006; review of ECR as hard test in 2006

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## The FSA internal ICG Process

- We will write to firms giving at least 3 months notice of when we want to receive a firm's ICA
- Letter states what we expect firm to do and documents we want to receive
- We ask for confirmation that you can meet the timetable, but you should be ready

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## What does the ICA review cover?

- Business Plan
  - Identification of risks
  - Stress & Scenario
  - Economic Capital Modelling
  - Structure & Implementation
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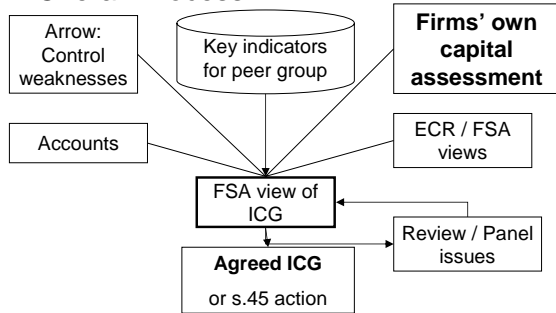
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## Overall Process



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## Internal Resources

- Supervisor
  - General Insurance Actuaries
  - Risk Review Department
  - Capital Specialists
  - Policy
  - Life Actuaries
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## Modelling Issues

- Does senior management understand it?
- Integration with business processes
- Parameterisation and calibration
- Starting position on a level base?
- Correlations in tail different to correlations before tail?
- Use of outside work (e.g. catastrophe models)
- Stress & Scenario used for sense checks

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## Modelling – FSA views

- We do not approve models for ICAS
- It is up to the company to think about the difficult issues and present to us what options you have taken and why
- We realise it takes time and there will be future enhancements to the early work
- We are looking for sound assessments, awareness of risk, and sound capital management – not perfection in mathematical modelling

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## Early Experience

- Good standard of work in the pilots
- Identification of risks and good links to Stress & Scenario tests
- It is taking longer than originally thought!
- Learning process re documentation
- Most are following Annex A
- Parameter risk is key
- ICAS and capital modelling embedded within the organisation
- Sophistication of models varied

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## Industry response to the new regime

- Early consultation reflected some industry resistance to any change to old regime
- Reaction now positive
  - CP190 feedback positive on framework
  - ABI welcomed it
  - Brit issued press release 1/9/04 – “successfully completed the ICAS study with the FSA”
- In discussions, companies are saying they have found the work very useful
- Senior management are engaging with process

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