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Dear Felicity,

Insurance Solvency Standards Consultation Paper

The Financial Services Council ("FSC") appreciates the opportunity to comment on your consultation paper *Insurance Solvency Standards: guarantees and off-balance sheet exposures.*

Individual members of the FSC may make their own company-specific submissions on this consultation paper. Our response is based on discussion with members and covers two points in the consultation paper but does not purport to address all of the concerns of all insurers.

Appendix 2 Other off balance sheet exposures
Disputed amounts (paragraph 96)
The proposed paragraph 96 requires that a general charge be held for disputes over claims amounts arising on the portfolio, based on past experience. This appears to allow for both known pending claims that have already occurred but that may end up being disputed, and a contingency for other potential claims arising in the following year that again may end up being disputed (and then paid). Whilst this charge may be reduced by any more specific provisions for known disputed claims, the excess is in addition to the amounts held within the accounts.

In terms of the life insurance solvency standard, we note that an allowance for disputed claims should already be implicitly allowed for in the best estimate assumptions. The actuary will have up-to-date experience analyses and will have based the underlying mortality/morbidity assumptions on such analyses, and this will implicitly include allowance for actual pay-outs on disputed claims. With regard to current pending claims, implicit allowance should also be held with regard to future pay-outs in the 'Reported but Not Accepted' Reserve.

Estimates of legal costs, based on past experience, should similarly have been allowed for in the expense assumption.

We submit that the Appointed Actuary need not make specific allowance for this, but instead suggest that the Appointed Actuary ensures that appropriate general allowance has been made for disputed claims that will be paid in the estimate of future claim amounts in the solvency reserve within the Insurance Risk Capital Charge, and makes appropriate adjustment if this is not believed to be the case.

We further submit that such adjustment should form part of the Insurance Risk Charge (which has a minimum of Current Termination Value), along with all other reserves for future claim payments including pending claims.

Contingent Liabilities (paragraph 95)

The proposal also requests that insurers allow for contingent liabilities not disclosed in the NZ GAAP Financial Statements, "even if remote". It appears (from paragraph 97) that it is expected that the liability is held at full possible value (which is then multiplied by the 20% factor for Off-Balance Sheet exposures). This, we believe, is too extreme a position. Reserving such amounts for events that are unlikely and remote could well put many insurers in an adverse solvency position quite unnecessarily. There is always the possibility of legal threats, for instance, which have no real substance behind them.

We submit that the contingent liability should be assessed on the event of its likelihood of occurrence and allowance only be made if the Appointed Actuary considers, on the balance of probabilities, that there is a reasonable likelihood of such event occurring. Alternatively, the Appointed Actuary could calculate a liability based on a probability weighted assessment of the likely values to be paid.

Yours sincerely,

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EXECUTIVE OFFICER