

# **SOLVENCY ADVISORY COMMITTEE**

**QUÉBEC CHARTERED LIFE INSURERS**

March 2008 – volume 4

## **FRAMEWORK FOR A NEW STANDARD APPROACH TO SETTING CAPITAL REQUIREMENTS**



**AUTORITÉ  
DES MARCHÉS  
FINANCIERS**

## SOLVENCY ADVISORY COMMITTEE

Recently, a working group consisting of representatives from the Autorité des marchés financiers (AMF), the Office of the Superintendent of Financial Institutions (OSFI) and Assuris has been formed to update the current solvency framework that would form the Standard Approach in the new solvency framework. This update is required by the expected adoption of the International Financial Reporting Standards (IFRS) by Canadian financial institutions (i.e. including all insurance companies). The proposed new accounting method for insurance contracts ("IFRS Insurance Contracts Phase II") will require a significant change in the way insurance obligations are valued and provided for in the capital requirements. It will also require modifications to the regulatory credit and market capital requirements.

The working group has prepared the attached discussion paper which proposes a new standard approach to determine how much capital a Canadian life insurance company should be required to have on hand in order to be able to meet its obligations to policy holders. The proposed framework is consistent with the "[Canadian Vision for Life Insurer Solvency Assessment](#)", endorsed by the AMF and OSFI. It uses a target asset requirement approach, meaning that insurance companies would be required to hold assets equal to the best estimate of their insurance obligations plus a solvency buffer.

This discussion document is not intended to be a final statement of the position of the AMF, OSFI or Assuris. The methods described in the document are preliminary views. We believe it is vital to engage in an open and constructive dialogue with the industry. This may lead to changes in the suggested approaches.

We hope to finalize the framework by June 2008. We will then prepare more detailed papers on each of the risk categories. We will ask the industry for further comments on each risk category paper and for participation in quantitative impact studies.

The AMF welcomes comments you may have on the attached document. Please send your comments no later than April 25, 2008 to Sylvain St-Georges at:

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**Framework for a  
New Standard Approach to Setting Capital Requirements  
Joint Committee of OSFI, AMF, and Assuris  
January 2008**

**DRAFT FOR COMMENT**

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## Table of Contents

<b>Background .....</b>	<b>3</b>
Minimum Continuing Capital and Surplus Requirements (MCCSR) .....	3
Pressure for Reform .....	3
International Financial Reporting Standards (IFRS) .....	3
New Areas.....	4
Evolution.....	4
The Process .....	5
<b>Overview of the Standard Approach Framework .....</b>	<b>6</b>
Approach.....	6
Risk Categories & Solvency Buffer.....	6
Future Developments .....	8
<b>Framework Details.....</b>	<b>9</b>
Target Asset Requirement .....	9
Harmonization with the Advanced Modeling Approach.....	10
Comparability with Capital Standards for Banks and Insurance Companies in the USA and Europe.....	10
Target and Minimum Capital.....	10
Risk Horizon .....	11
Confidence Level.....	12
Approach to Credit Risk .....	12
Approach to Market Risk.....	12
Approach to Insurance Risk.....	14
Approach to Operational Risk .....	14
Diversification and Concentration .....	15
Refining and Calibrating.....	15
Available Capital .....	15
<b>Glossary of Terms .....</b>	<b>16</b>

### Figures in this Report:

Figure 1. Milestones in the Development and Implementation of the Framework .....	5
Figure 2. Four Categories of Risk.....	7
Figure 3. Factors Used to Determine the Target Asset Requirement .....	9
Figure 4. Factors Used to Determine Target Capital and Minimum Capital.....	11

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## Background

This discussion paper proposes a new standard approach to determine how much capital a Canadian life insurance company should be required to have on hand in order to be able to meet its obligations to policy holders. The proposed framework is consistent with the “Canadian Vision for Life Insurer Solvency Assessment,” endorsed by the Office of the Superintendent of Financial Institutions (OSFI) and *Autorité des marchés financiers* (AMF). It uses a *target asset requirement* approach, meaning that insurance companies would be required to hold assets equal to the best estimate of their insurance obligations plus a *solvency buffer*.<sup>\*</sup> This paper was prepared by a joint committee of OSFI, AMF, and Assuris. It is being distributed to the industry and to the Canadian Life and Health Insurance Association (CLHIA) for discussion and feedback.

<sup>\*</sup>**Note:** For definitions of key terms, see the Glossary of Terms at the end of this paper.

## Minimum Continuing Capital and Surplus Requirements (MCCSR)

Regulators currently require insurance companies to use a standard approach to calculate the Minimum Continuing Capital and Surplus Requirements (MCCSR) in order to determine how much capital they need. This system has served the industry well. Introduced in 1992, it has been continually updated and refined. However, there has been growing pressure to reform the system.

## Pressure for Reform

Since the early 1990s there have been advances in actuarial and economic capital theory that are difficult to incorporate into the existing system. The increased complexity of products and globalization of insurance products has resulted in some companies adopting internal models for risk and economic capital. The introduction of modeling approaches for setting capital for banks under Basel II has also caused some Canadian life insurance companies to demand similar advanced approaches.

This has led to the creation of the MCCSR Advisory Committee (MAC), whose key focus is the design of an advanced approach. The advanced approach may affect only a small number of companies. However, impending accounting changes will make it necessary to update the standard MCCSR approach. This update to the standard approach for setting capital standards will affect all Canadian life insurance companies.

## International Financial Reporting Standards (IFRS)

January 1, 2011 is the target date for the adoption by all Canadian public companies. It is expected that Canadian financial institutions (i.e. including all insurance companies) will adopt International Financial Reporting Standards (IFRS) at this date.

An important part of IFRS for insurers relates to the accounting standards for insurance contracts and is entitled “IFRS Insurance Contracts Phase II”. An exposure draft of this proposed standard

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is not expected until 2009, but many of the principles of the proposed new standard are clearly laid out in a preliminary views discussion paper that was released in 2007 by the International Standards Accounting Board (IASB). This proposed new accounting method for insurance contracts will require a significant change in the way insurance obligations are valued and provided for in the capital requirements. It will also require modifications to the regulatory credit and market capital requirements.

It is possible that IFRS Insurance Contracts Phase II will not be ready by 2011 and Canada will need to adopt the current insurance contract standard, IFRS 4, as an interim measure. If IFRS 4 is adopted as an interim measure effective January 1, 2011, some contracts currently accounted for as insurance may be treated as financial instruments and some insurance contracts may be unbundled. The extent of the impact on current Canadian GAAP is unclear at this time but certain contracts will be reported outside the actuarial liabilities and will be subject to the financial instrument accounting principles. IFRS 4 would require modifications to be made to the current MCCSR.

This paper has been prepared in readiness for the adoption of IFRS Insurance Contracts Phase II as envisioned in the IASB's 2007 preliminary views discussion paper.

### **New Areas**

The current MCCSR does not adequately account for risk concentration and risk diversification. Nor does it provide explicitly for operational risk. These areas will also need to be considered in the updated standard approach. However, implementation may be later than for credit, market, and insurance requirements.

### **Evolution**

In developing the new capital requirement framework, it is important to build on the existing methods and systems used by the industry and by regulators. These include the current MCCSR, the Canadian Asset and Liability Method (CALM) valuation, and the Dynamic Capital Adequacy Test (DCAT).

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## The Process

This discussion document is not intended to be a final statement of the position of OSFI, AMF or Assuris. The methods described in the document are preliminary views. We believe it is vital to engage in an open and constructive dialogue with the industry. This may lead to changes in the suggested approaches. It will certainly lead to greater clarity and refinement of the approaches.

We hope to finalize the framework by June 2008. We will then prepare more detailed papers on each of the risk categories. We will ask the industry for further comments on each risk category paper and for participation in quantitative impact studies. In order to allow enough time for companies and regulators to adjust their systems, the form of the calculation will be finalized by June 2009. Final decisions on the calibration of the factors and assumptions will be completed by June 2010 for implementation in 2011. (See Figure 1 for key milestones in the process.)

Figure 1. Milestones in the Development and Implementation of the Framework

Formation of the working group for standard capital requirements	Nov 14, 2007
Draft discussion paper issued to OSFI, AMF and Assuris	Nov 30, 2007
Discussion paper issued to industry for comment	Feb 2008
Meetings with CLHIA Capital Adequacy Committee	Jan – March 2008
CICA confirms its intentions regarding the use of IFRS	March 2008
Framework paper finalized and issued by OSFI and AMF	June 2008
Detailed paper on capital requirements for credit risk	July 2008
Detailed paper on capital requirements for market risk	July 2008
Detailed paper on capital requirements for insurance risk	December 2008
Detailed paper on capital requirements for operational risk	March 2009
Quantitative impact studies	June 2008 – June 2009
OSFI and AMF issue the form of calculation	June 2009
Further quantitative impact studies	June 2009 – June 2010
Expected IASB release on Insurance Contracts Phase II exposure draft	Sept-December 2009
OSFI and AMF issue factors and assumptions to be used for 2011	June 2010
Expected implementation of the Framework	January 1, 2011

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## Overview of the Standard Approach Framework

	<b>Approach</b>
<b>Target Asset Requirement</b>	The new standard approach is consistent with the “Canadian Vision for Life Insurer Solvency Assessment,” and will use the target asset requirement. This requires the company to hold assets equal to the best estimate of its insurance obligations plus a solvency buffer (described below).
<b>Harmonization with the Advanced Modeling Approach</b>	The standard approach will incorporate the same target asset requirement, risk categories and calibration information as the advanced modeling approach. For credit risk, the Canadian system will be similar to that used by banks under the Basel II rules. For all risk categories, account will be taken of the systems in the other countries.
<b>Comparability of Capital Standards</b>	
<b>Target and Minimum Capital</b>	When <i>available capital</i> is below <i>target required capital</i> , the regulator will require the company to take corrective action. When available capital is below <i>minimum required capital</i> , the regulator may take additional actions consistent with its intervention tools.
	<b>Risk Categories &amp; Solvency Buffer</b>
<b>Risk Horizon</b>	The solvency buffer will be calculated for all risks that could have a negative financial impact on a life insurance company. It will be calculated to cover risks over the expected term of the assets and liabilities. The preliminary assumption we are using is that the solvency margin will be calibrated so that a company can withstand adverse conditions and have enough assets to sell or run off the business 39 times out of 40. This is a confidence level of 97.5%.
<b>Confidence Level</b>	The framework identifies four categories of risk: credit, market, insurance, and operational. Figure 2 shows how the categories of risk are defined, and how the solvency buffer is expected to be calculated for each category of risk.



Figure 2. Four Categories of Risk

	Risk Category	Solvency Buffer
Approach to Credit Risk	<b>Credit risk</b> is the risk of default by counterparties on loans, debt instruments, derivatives, and reinsurance.	The solvency buffer for credit risk will use factors developed from the best available information, and be similar to the method currently used in the MCCSR.
Approach to Market Risk	<b>Market risk</b> is the risk that changes in the financial markets will affect the value of assets and liabilities. This includes interest rate, spread, equity, and currency risks.	The solvency buffer for market risk will use modifications of the existing CALM models for interest rate risk and <i>deterministic shock calculations</i> for equity, real estate, and currency risks.
Approach to Insurance Risk	<b>Insurance risk</b> is the risk of adverse future experience in mortality, morbidity, and policyholder behaviour, including lapse rates.	The solvency buffer for insurance risk will be calculated using a more conservative integrated combination of mortality, morbidity and lapse assumptions than are used in calculating best-estimate insurance obligations. This integrated approach may take the form of a second more conservative valuation.
Approach to Operational Risk	<b>Operational risk</b> is the risk that the company's business processes will fail, or that the company will fail to comply with laws and regulations. The financial impact of loss of reputation is also included in operational risk.	The solvency buffer for operational risk will be calculated by applying a factor to gross revenue. In addition, the solvency buffer will also contain a margin for future expenses that exceed those assumed in the calculation of the best-estimate insurance obligations.

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**Diversification and  
Concentration**

**Future Developments**

The framework will be adapted in the future to explicitly respond to concentration or diversification of risk.

**Refining and  
Calibrating**

Once the new system is in place, there will be regular review and study to refine the methodology and calibrate the factors and assumptions.

**Available Capital**

There will be a review of the current regulations governing available capital. However no significant changes are expected.

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## Framework Details

### Target Asset Requirement

The new standard approach is consistent with the “Canadian Vision for Life Insurer Solvency Assessment,” and will use the target asset requirement. This requires the company to hold assets equal to the best estimate of its insurance obligations plus a solvency buffer.

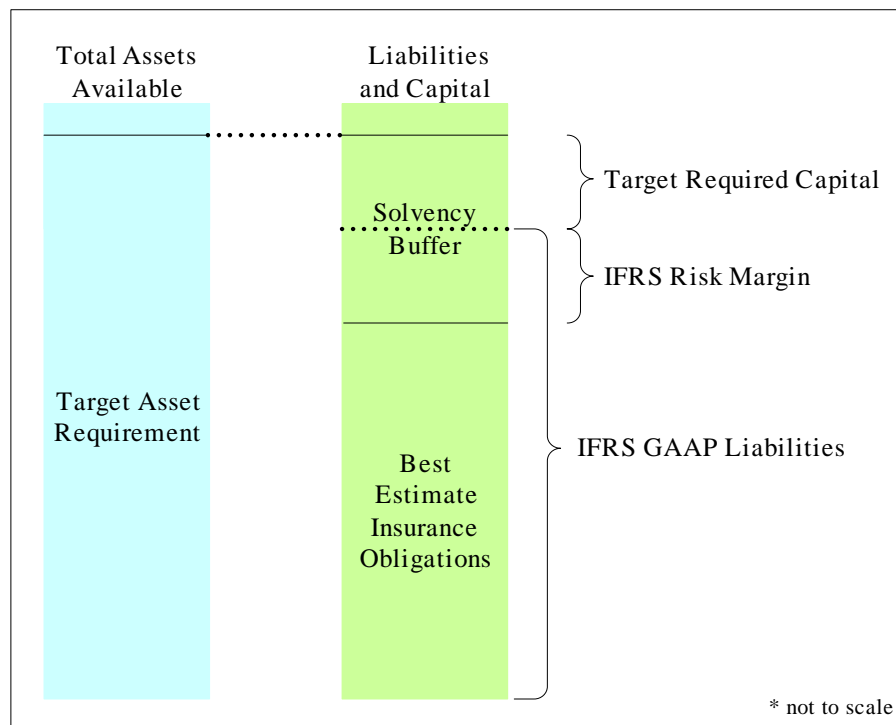
The solvency buffer is the amount of assets a life insurance company must hold in addition to those needed to cover best-estimate life insurance obligations so that the company has a high degree of confidence that it can withstand adverse conditions over the expected term of its assets and liabilities.

Phase II IFRS GAAP liabilities will be calculated starting with the same best estimate of insurance obligations, but adding a risk margin.

The IFRS GAAP risk margin is the amount of assets a buyer needs, in addition to those needed to cover the best estimate of insurance obligations, to assume the risk of acquiring a block of business. This risk margin will likely be calculated using a cost-of-capital method.

Under this approach, the *required capital* is defined as the *target asset requirement* less IFRS GAAP liabilities.

Figure 3. Factors Used to Determine the Target Asset Requirement



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## **Harmonization with the Advanced Modeling Approach**

The standard approach will incorporate the same target asset requirement, risk categories, and calibration information as the advanced modeling approach

The different results obtained by the two approaches will be monitored, which may result in modifications to the advanced approach or recalibration of the standard approach. In some cases the approaches may be different enough that a direct comparison of results will not be meaningful.

## **Comparability with Capital Standards for Banks and Insurance Companies in the USA and Europe**

For credit risk, the Canadian system will be similar to that used by banks under the Basel II rules. For all risk categories the Canadian system will take into account the systems in other countries.

To minimize competitive differences within Canada, the solvency buffer for credit risk will consider the Basel II requirements for banks as well as other relevant information.

Currently, there are major differences among the capital requirements in Canada, the USA, and Europe. If this is not corrected it may lead to an increase in international regulatory arbitrage. The emergence of Solvency II standards in Europe presents us with an opportunity to reduce the discrepancies. However, the capital rules will have to establish a prudent level of capital to absorb unexpected losses. In developing the new Canadian requirements, we will compare our approach with the approaches emerging in Europe.

## **Target and Minimum Capital**

When available capital is below target required capital, the regulator will require the company to take corrective action. When available capital is below minimum required capital, the regulator will take additional action consistent with its intervention tools.

Available capital is the difference between total assets available and assets required for IFRS GAAP liabilities.

*Target required capital* is the difference between *the target asset requirement* and assets required for IFRS GAAP liabilities.

*Minimum required capital* will be periodically set by the regulator as a percentage of target required capital. The initial percentage may be set at 80%.

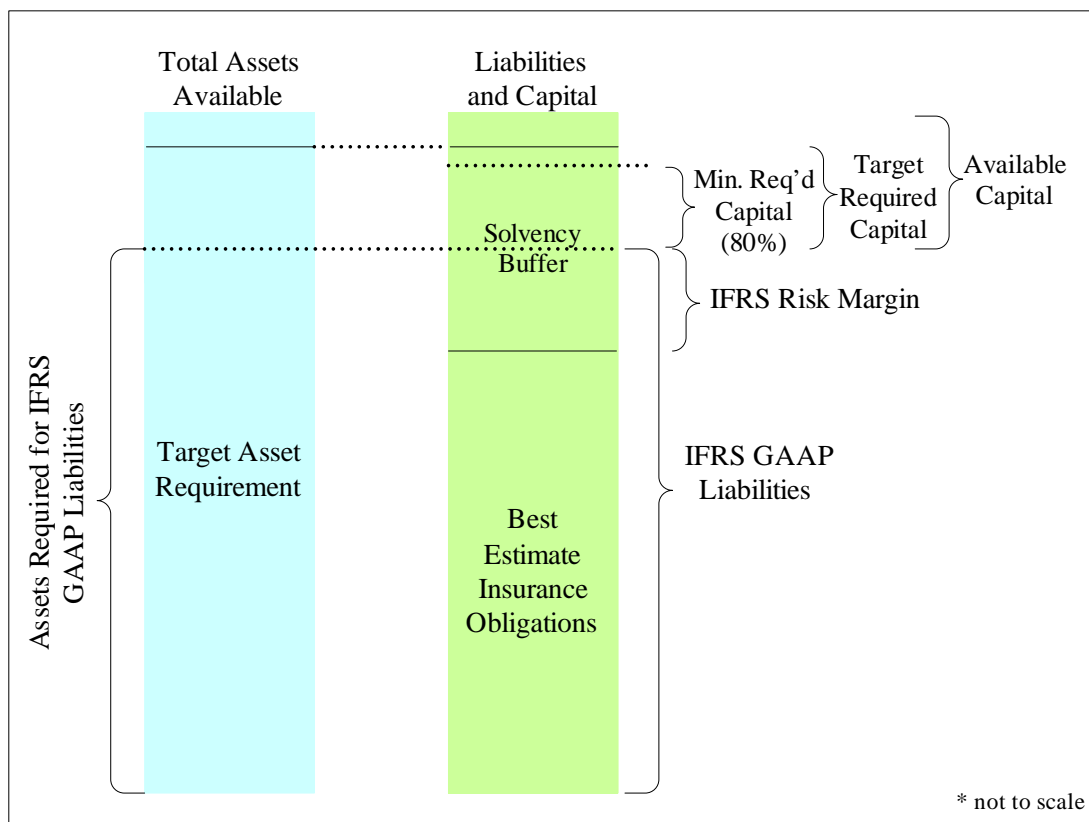
Capital is only one criterion that the regulator might use to determine if some form of intervention with a life insurance company is necessary. The regulators have various tools at their disposal and can be expected to escalate the severity of their intervention depending on the particular situation. At the limit, the regulators have the authority to take control of an insurance company which meets one or more conditions set down in the relevant insurance company

legislation. These conditions include, for example, the failure to comply with a formal capital order issued by the regulator to the company.

The regulatory requirements could be defined in terms of a minimum asset requirement that could be calculated separately for each of the risk categories, or even each of the sub-risk categories. This has the advantage of precision but the disadvantage of complexity. We have therefore chosen to define the regulatory requirements in terms of total capital required, which is the difference between total assets required for solvency and the total assets required for IFRS GAAP liabilities.

This approach also has the merit of keeping the current terminology of *required capital* and *available capital*, and will ease the transition from the current capital framework.

Figure 4. Factors Used to Determine Target Capital and Minimum Capital



### Risk Horizon

The solvency buffer will be calculated for all risks that could have a negative financial impact on a life insurance company. It will be calculated to cover risks over the expected term of the assets and liabilities. This view is consistent with that used in the determination of the current MCCR capital requirements and also with the MAC Vision which considers risks for their lifetime.

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## **Confidence Level**

The preliminary assumption we are using is that the solvency margin will be calibrated so that a company can withstand adverse conditions and have enough assets to sell or run off the business 39 times out of 40. This is a confidence level of 97.5%. Additional calibration considerations will include current capital levels, the outcome of advanced approach impact studies and a rating of at least a BBB grade security.

The standard approach will use the same level of conservatism as the advanced approach but for simplicity will be expressed in terms of confidence level. This makes it easier to communicate to managements, boards of directors, and other audiences.

## **Approach to Credit Risk**

The solvency buffer for credit risk will use factors developed from the best available information, and be similar to the method currently used in the MCCR.

With the introduction of IFRS GAAP there will no longer be a provision for asset defaults in the liabilities. This would suggest that the solvency buffer for credit risk should be the current capital requirements plus the current asset default provisions in the liabilities. However, it is also anticipated that the new IFRS best estimate liability will discount the liability cash flows using risk-free rates. By itself, this latter change will increase the amount of the insurance liabilities. Together, these two changes work in opposite directions and more work will be required to determine the net change required to the current MCCR factors.

The new factors should also be similar to the credit requirements in Basel II. Preliminary work in this area suggests that the factors give broadly similar results for the same asset classes for banks and insurance companies. More work is needed to confirm and refine this.

Research should also be undertaken to assess the default history of each asset class. The results of this work could then be used to help calibrate the factors.

The current MCCR factors were developed for application to the historic cost value of assets. When the new factors are applied to the market value of assets under the new accounting standards, we need to ensure the credit and market capital standards do not double count or miss risk.

## **Approach to Market Risk**

The solvency buffer for market risk will use modifications of the existing CALM models for interest rate risk and deterministic shock calculations for equity, real estate, and currency risks.

Under the current CALM of valuing liabilities, each company has a system for projecting future cash flows of both assets and liabilities. In this model, the sensitivity of the present value of the cash flows to interest rate changes can be tested using different interest assumptions. This system should be retained and modified to set the solvency margin for interest rate risk.

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The solvency buffer for the market risk of equities and real estate will be calculated using simple *deterministic shocks* to the market value.

We considered, and are still willing to consider, the use of other methods or models for calculating the capital requirement for market risk. However, using systems that already exist should reduce the time and effort it will take for companies to make the transition to the new capital requirements.

Consistent with developments in Europe and internationally, equity risk will be considered within market risk in the new framework (i.e. rather than within credit risk in the current MCCR).

Separate techniques for setting solvency margins for currency risk need to be developed.

Liquidity risk is expected to be addressed through the process of supervisory review.

Additional solvency margins need to be established for product features that provide market-related guarantees to policyholders. The most significant of these are the guarantees on segregated funds, equity indexed annuities, and minimum interest rate guarantees in universal life contracts. The existing methodology should be reviewed, but we anticipate that this methodology will be kept for calculating these solvency buffers.

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## **Approach to Insurance Risk**

The solvency buffer for insurance risk will explore using a more conservative integrated combination of mortality, morbidity and lapse assumptions than are used in calculating best-estimate insurance obligations. Where applicable, other assumptions would be modified to be consistent with the new assumptions. This integrated approach may take the form of a second more conservative valuation.

We anticipate that mortality and morbidity improvements will be allowed in the calculation of best-estimate insurance obligations under IFRS GAAP. The new solvency buffer methodology would likely remove these assumptions.

It would be preferable if the new integrated calculation could make use of valuation systems currently in use by companies. However, considerable work needs to be done to establish the appropriate assumptions to be used in the solvency margin valuation. These assumptions will need to take into account catastrophe risk, as well as level and trend uncertainty.

Appropriate assumptions will also need to be developed to account for situations where risk is shared with consumers in participating contracts or through other contractual provisions.

To assist executive management, boards of directors and regulators in assessing the reasonableness of the resulting solvency buffer and to allow comparisons between companies, companies will be required to disclose information in a standard form.

## **Approach to Operational Risk**

The solvency buffer for operational risk will be calculated by applying a factor to a measure of exposure such as gross revenue. In addition, the solvency buffer will also contain a margin for future expenses that exceed those assumed in the calculation of best-estimate insurance obligations.

There are currently no explicit capital requirements for operational risk. However, they are implicitly accounted for by requiring companies to hold more than 100% of the capital required by the MCCR calculation. We recommend that operational risk be explicitly provided for by applying a factor to gross revenue.

Operational risk can be further divided into the sub-categories of process risk, legal and regulatory risk, and fraud and mismanagement risk.

Process risk is the risk of loss due to the accumulation of small process errors. This occurs most often in processing high-volume, low-dollar-value transactions. The risk is best measured by using volume of transactions, but using gross revenue can give reasonable results.

Legal and regulatory risk is the risk of loss due to non-compliance with laws or regulations. This risk increases with the size of a company. Gross revenue is a reasonable measure of company size.



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Fraud and mismanagement risk is the risk of loss due to significant fraudulent or negligent action by people in the organization. A classic example would be the unauthorized derivative trading that caused the failure of Barings bank. This type of risk has many of the same characteristics as catastrophic risk and it is difficult to find a suitable measure. The amount of such risks does tend to increase with company size, and gross revenue is a reasonable measure of size.

Different factors may be required for different lines of business. More study and thought is required in this area.

IFRS best estimates may not include actual expenses, but may instead include standard expenses derived from a reference entity. Where the present value of actual future expenses is expected to be higher than the present value used in the valuation, the excess should be provided for in the solvency buffer.

### **Diversification and Concentration**

The framework will be adapted in the future to explicitly respond to concentration or diversification of risk.

The “Canadian Vision for Life Insurer Solvency Assessment” stated that it was not anticipated that there would be diversification allowances between the categories of risk. We need to do more study on the behaviour of risks in extreme circumstances before we consider introducing explicit allowances for diversification or inclusions for concentration.

There will be some diversification allowance within the risk categories. For example the integrated approach to insurance risk that is recommended here will include a method of taking into consideration the reduction of risk that occurs when risks are aggregated into larger pools.

Diversification and concentration will be considered under Pillar II supervision. Here the regulator may impose conditions on companies that are subject to risk concentrations. These may include the requirement to increase the solvency buffer.

### **Refining and Calibrating**

Once the new framework is in place, there will be a regular schedule for updating both the methods and the calibration of the methods. This will be done based on experience with both the advanced and the standard approaches, and on special experience studies.

### **Available Capital**

There will be a review of the current regulations governing available capital. However no significant changes are expected.

The review should consider if the different treatment of deductions for MCCR and Basel II are appropriate. It should also consider if the current treatment of negative reserves and cash surrender values remain appropriate.

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## Glossary of Terms

Advanced modeling approach	A method of determining the <i>target asset requirement</i> using <i>stochastic modeling</i> techniques.
AMF	<i>Autorité des marchés financiers</i> . A regulatory authority for Quebec's financial sector. It protects consumers by enforcing the laws and regulations governing insurance, securities, deposit institutions (other than federally chartered banks), and the distribution of financial products and services.
Available capital	The difference between <i>total assets available</i> and assets required for <i>IFRS GAAP</i> liabilities.
Basel II	A set of international banking agreements ("the Basel Accords") that helps financial markets run smoothly. These accords coordinate the regulation of global banks. They were created to guard against financial shocks to the economy.
Best-estimate policyholder obligations	The best estimate of the cash needed in the present to meet future obligations to policyholders, without the addition of margins.
CALM model / CALM valuation	Canadian Asset and Liability Method. An actuarial valuation method, using the projected cash flows of the actual assets and liabilities of the company.
Canadian Vision for Life Insurer Solvency Assessment	A paper prepared by the Minimum Continuing Capital and Surplus Requirements (MCCSR) Advisory Committee (or MAC) to outline a vision for new principles-based solvency financial requirements for Canadian life insurers.
Capital	The remaining assets of a business after all liabilities have been deducted. Also see <i>available capital</i> , <i>target required capital</i> , and <i>minimum capital</i> .
CLHIA	Canadian Life and Health Insurance Association.
Confidence level	A level of confidence in financial predictions.
Conditional Tail Expectation (CTE)	The mean of the present value of the highest or lowest results, expressed as a percentile, of a simulation model. For example 95%CTE is the present value of the mean of the highest 5% of results.
Credit risk	The risk of financial loss, despite realization of collateral security or property, resulting from the failure of a debtor to honour its obligations to the company.
DCAT system	Dynamic Capital Adequacy Test. A formal approach to test the financial strength of a company by projecting its future financial condition under various possible sets of consistent scenarios. DCAT is a systematic way to quantify the major business risks faced by an insurance company.
Deterministic shock calculations	A method of determining the change in value of an asset or liability in response to a specific change in a market variable, such as an interest rate.

GAAP	Generally Accepted Accounting Principles. "Canadian GAAP" means generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants. "IFRS GAAP" means generally accepted accounting principles as set out in the International Financial Reporting Standards.
IFRS	International Financial Reporting Standards.
Insurance risk	The risk of adverse changes in mortality, morbidity, and lapse rates.
Lapse rate	The rate at which policyholders stop paying premiums and allow the protection offered by their policies to stop.
Liquidity risk	The risk of a company having insufficient cash to meet current demands for cash.
MAC	MCCSR Advisory Committee.
Market risk	The risk that changes in the financial markets will affect the value of assets and liabilities. This includes interest rate, spread, equity, and currency risks.
MCCSR	Minimum Continuing Capital and Surplus Requirement. The current system for determining required capital. The AMF capital formula name is Capital Adequacy Requirements (CAR).
Minimum assets required	The level of assets below which the regulator will take corrective action that may include taking control of the company.
Minimum capital	The level of capital below which the regulator will take corrective action that may include taking control of the company.
Morbidity rate	The number of policyholders claims for illness or disability, within a certain period of time, divided by the total number of policy holders.
Mortality rate	The number of policyholders who die, within a certain period of time, divided by the total number of policyholders.
Operational risk	The risk that a business will lose money because of the way it operates, or because of its failure to comply with laws and regulations. This includes the financial impact of loss of reputation.
OSFI	Office of the Superintendent of Financial Institutions. A regulatory body that was created to contribute to public confidence in the Canadian financial system.
PfAD	Provisions for Adverse Deviations. An amount set aside or identified in case things go worse than you expect.
Pillar II rules	The rules set by the regulator to cover risks not explicitly dealt with under Capital rules (Pillar I). It includes the regulators response to monitoring and assessing the company's Internal Capital Adequacy Process.
Regulatory arbitrage	"Shopping" for favourable regulations – for example, to find the regulatory regime with the lowest capital requirements.
Risk horizon	The future period over which risk is measured.

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Solvency II standards	European standard approach for the calculation of the available capital of life, non-life and health insurance companies.
Solvency buffer	An estimate of the amount of capital in excess of the best estimate policyholder obligations that a business needs to have on hand to withstand financial problems and have enough assets to sell or run off the business.
Stochastic modeling	A modeling technique that consists of running multiple scenarios from randomly generated variations in the assumptions.
Target asset requirement	Target level of assets required determined as an expected asset requirement plus a solvency buffer.
Target required capital	The difference between the target assets requirement and assets required for <i>IFRS GAAP</i> liabilities.
Terminal provision	A calculation of the assets that would be required to close a business at the end of the <i>risk horizon</i> , either by selling off the business or by putting it into run-off.
Valuation	The process of determining the current worth of an asset or company.

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