ABSTRACT

Surplus Requirements for Life Insurers in Canada

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A proposal for a minimum continuing capital and surplus requirement for life insurers has recently been circulated by the Department of Insurance Canada for comment by the life insurance industry and the actuarial profession in Canada. This talk describes some of the reasoning and methodology underlying this proposal.

A capital and surplus requirement is intended as a supplement to policy reserves in ensuring the insurer's solvency. The determination of this requirement should be consistent with the valuation standards used to fix policy reserves. Since 1978, the setting of reserve assumptions and the calculation of reserves has been the responsibility of the Valuation Actuary. A description of this valuation system preceeded development of the surplus requirement.

The proposed surplus requirement is in the form of factors to be applied to various elements of risk in a company's portfolio. Classical ruin theory can be used to develop factors associated with mortality and incidence of disability risks. The financial risks associated with changes in interest rates are developed by means of computer simulation models. These require assumptions with respect to investment policy and the sensitivity of lapses and expenses, among other factors, to changes in interest rates.

Finally, it should be noted the proposed standard is only intended to protect existing policyholders. It is not intended to provide the vitality surplus required by a healthy and growing insurer.