Article Title: ARCHIVE | Criteria | Insurance | General: Testing Of Enhanced Insurer Capital Model Completed Data: (EDITOR'S NOTE: —This article is no longer current. It has been superseded by "Analysis Of Insurer Capital Adequacy," which was published on April 22, 2009.) Standard & Poor's Ratings Services has completed its side-by-side testing of its enhanced insurer capital model and the prior model. (For details on the new model, see "New Risk-Based Insurance Capital Model," published May 31, 2007, on RatingsDirect, the real-time, Web-based source for Standard & Poor's credit ratings, research, and risk analysis.) As a result, from now on, we will focus our risk-based capital analysis on the enhanced model and will retire the old model. Frequently Asked Questions What changes have occurred since the details about the new model were published in May 2007? We have made few changes to the model since we introduced it last year. However, one significant change that we will implement shortly affects the calculation of total adjusted capital (TAC) for nonlife insurance enterprises. Standard & Poor's plans to recognize the emergence of investment income through discounting unearned premium reserves (UPR). It plans to do so by calculating the time value of money of UPR for the time frame of the capital captured by our capital model and the relevant 10-year government bond yield (a weighted average for companies with reserves denominated in more than one currency). The UPR discount would be computed as: 50% multiplied by UPR reserves multiplied by (1-(1/(1+r)^n)) Where: r = applicable long term government bond yield n = time frame for the capital captured by Standard & Poor's capital model in years (average of two years) The 50% haircut is a prudent adjustment to allow a margin for adverse experience and expenses. This adjustment is consistent with the one we currently make to life insurance deferred acquisition costs or embedded value. Are other changes to the model expected? Standard & Poor's might adjust the model from time to time as new information emerges. However, we are considering few significant changes. One change that is under review could modify asset/liability risk charges on a company-specific basis, primarily for companies in Continental Europe. The enhanced model uses capital charges for asset/liability risk in Continental Europe that are significantly greater than those applied in the U.S. and the U.K. We are currently considering proposals that could reduce those charges, depending on our assessment of the quality a given insurer's asset/liability risk management. We will publish the details of this approach shortly once we define them more fully. What is the ratings impact of the transition to the new model? We will not be changing any ratings because of the shift to the new model. However, there is some impact on our assessment of capital because of the shift. For life insurers, the enhanced model generally results in higher capital charges, particularly because of charges for asset risk being assessed at higher confidence levels than in the prior model. This means that many companies that were assessed as having 'AAA' level capital under the prior model are viewed as having 'AA' or 'A' capital adequacy under the enhanced model. In general, this brings our view of capital adequacy closer to the actual ratings on the companies, so we don't anticipate any ratings changes because of it. For nonlife insurers, results vary, with some lines of business (notably, longer-tail casualty lines) receiving higher charges, while shorter-tail property lines are generally assessed lower required capital. For health insurers, the impact of the new capital charges was generally minor, though revised rules around credit for double leverage have negatively affected the capital assessments of a number of highly levered insurers. Will S&P; publish an updated model explanation reflecting the changes? Yes. We anticipate republishing the full capital model criteria to reflect the latest updates sometime in June.