FINANCIAL STABILITY BOARD

Scope of Insurers Subject to the Recovery and Resolution Planning Requirements in the FSB Key Attributes: Consultation report

Response to Consultation

American Council of Life Insurers

In general

1. **Are the Draft Guidance and comments on the Draft Guidance clear? Where would commenters seek further discussion?**

   ACLI appreciates the opportunity to provide comments. We suggest several clarifications below.

   As a general comment, the IAIS differentiates between recovery planning and resolution planning by both objectives and ownership. Recovery planning is a preventive, firm-led exercise focused on restoring a distressed insurer to financial health, whereas resolution planning is an authority-led strategy designed to manage an orderly market exit and protect policyholders once a firm is no longer viable. Consequently, their scopes of application diverge based on the level of systemic risk posed. While the framework mandates recovery plans for all Internationally Active Insurance Groups (IAIGs) and other large entities as a core risk management practice, resolution planning is more selectively applied, targeting only those insurers whose failure is deemed to have a significant impact on financial stability or the continuity of critical economic functions.

   Section 2: Draft Guidance

   Regarding Paragraph 4 (Specific Circumstances): The mandate that RRP requirements apply notwithstanding the other criteria effectively creates a "strict liability" standard for application and overrides the nuanced analysis intended in Paragraph 3. An insurer deemed to provide a "critical function," is automatically designated.

   Section 3: Explanatory Comments

   Regarding Section 3.3 (Assessment Criteria - General): The explanatory text states that RRP requirements may be appropriate "even if only a subset of the six criteria" are met. This statement suggests that a firm with zero cross-border activity and high substitutability could still be subject to RRP if an authority subjectively views its "nature" as risky. This creates a regulatory environment where no insurer can reasonably predict its status.

Regarding Section 3.3.1 (Nature): The Guidance suggests assessing nature based on "non-traditional" activities and the "use of derivatives." The text fails to clearly distinguish between derivatives used for hedging (risk reduction) versus speculation (risk creation). As ACLI has indicated in past comments to the FSB on Nonbank Financial Institution Leverage, insurers use derivatives to asset match and hedge risks. In the US, insurers use derivatives in three ways: 1) fair value hedges to offset assets or liabilities, 2) cash flow hedges to offset variability in future cash flows, and 3) hedges to offset FX (currency) risk. These activities are risk mitigation strategies and should not be discouraged. Further, those derivatives insurers are permitted to use for asset replication (e.g., CDS paired with a highly rated fixed income security) and income generation (e.g., covered calls on owned securities) need to be backed with cash. At the state level, insurers are precluded from taking significant leverage per NAIC model code (Models #280 and #282) on derivatives which is widely adopted across the U.S.

Because insurers utilize derivatives for important risk mitigation activities that the FSB should not discourage, the Guidance should explicitly state that the use of derivatives for hedging purposes is not an indicator of systemic risk or a "risky nature."

Regarding Section 3.3.6 (Interconnectedness): The Guidance cites "Reinsurance exposure" as an indicator of interconnectedness.

Characterizing reinsurance as "interconnected", without recognizing its purpose to reduce concentrated risks, strikes against the very purpose of reinsurance; to reduce concentrated risks. Reinsurance is a fundamental, traditional tool for pooling and diversification of risk. Penalizing insurers for reinsurance could perversely discourage risk transfer. The Guidance should clarify that "Interconnectedness" resulting from reinsurance arrangements by dissipating concentration of risk may often be systemically beneficial.

Further, the Global Reinsurance Forum discusses in its 2021 report "Understanding the Economic and Societal Value of Reinsurance" why reinsurance is intrinsically a global industry, relying on diversification of risks across the globe, a wide spectrum of business lines and geographies. This reduces the cost of risk and benefits insurance policyholders.

Section 4: Proposed Revision to Critical Functions

Almost all insurance activity impacts the "real economy" (e.g., paying claims to homeowners, businesses, or auto accident victims). By changing the conjunction to "or," the FSB risks capturing regional or niche insurers that are vital to their specific customers but irrelevant to global financial stability.

Paragraph 3: Assessment criteria

2. How well-suited are the criteria in the Draft Guidance (nature, scale, complexity, substitutability, cross-border activities, interconnectedness) to determining which insurers should be subject to RRP requirements?

ACLI generally agrees that supervisors should consider the nature, scale, complexity, substitutability, cross-border activities, and interconnectedness of insurers when determining the application of resolution and recovery planning requirements.

Local supervisors are best positioned to determine when planning is appropriate. They have tools available such as Enterprise Risk Management (ERM) frameworks, Own Risk Solvncy Assessments (ORSA), capital and liquidity regimes, and more. These tools support an activities-based risk assessment approach rather than one based on predetermined criteria that may trigger unnecessary and costly planning for an expanded list of insurers.

3. **What other criteria, if any, should be in the Draft Guidance for determining which insurers should be subject to RRP requirements? Discuss why any additional criteria should be added and the advantages and disadvantages of doing so.**

   No comments.

4. **What other indicators could be provided as examples of ways that authorities could assess the criteria in the Draft Guidance?**

   No comments.

5. **How could the comments to the Draft Guidance better explain the difference between any of the six criteria?**

   The current Explanatory Comments (Section 3) acknowledge that the six criteria are "distinct, but not mutually exclusive" and that "some information may be relevant to multiple criteria." While the Draft Guidance warns authorities against using the same information to "solely evaluate multiple criteria," this safeguard is insufficient.

6. **How could the comments on the Draft Guidance be made clearer to explain how the six criteria should be applied, while still allowing authorities the flexibility to consider the criteria in a manner that aligns with the specific characteristics of their jurisdictions?**

   Please see response to question #2.

Paragraph 4: Specific circumstances that should necessitate RRP requirements

7. **Should RRP requirements apply in the two sets of circumstances identified in paragraph 4 of the Draft Guidance, notwithstanding any other facts or circumstances?**

   We do not support the "automatic" application of RRP requirements based solely on the circumstances in Paragraph 4. We strongly urge maintaining the ability for jurisdictional authorities to have supervisory discretion.

   We are concerned with the language that “this paragraph sets forth specific circumstances that, if met, mean an insurer should be subject to RRP requirements notwithstanding any evaluation of the criteria in paragraph 3 of the Draft Guidance.” By providing that the language is subject “notwithstanding” criteria in paragraph 3, this creates prescriptive language without providing jurisdictional flexibility.

   While the circumstances described (providing a critical function or posing a significant impact) are certainly indicators that RRP might be necessary, especially resolution plans that focus avoiding failure in the first place, making them automatic triggers ignores the principle of proportionality and the existence of alternative safety nets such as standard insolvency procedures and/or policyholder protection schemes.

The "notwithstanding" clause is too blunt and too strongly-worded. We recommend amending Paragraph 4 to state that these circumstances create a "presumption" of RRP application, which insurers can rebut by demonstrating that existing mitigants or supervisory measures are sufficient to mitigate the specific risks identified.

Additionally in the United States, existing ERM frameworks, Own Risk Solvency Assessments (ORSA)s, capital and liquidity regimes already create criteria for when recovery and resolution plans are required regardless of insurers' material impact on the financial system and economy.

8. What other circumstances should call for the application of RRP requirements to an insurer, notwithstanding any other facts or circumstances?

We do not support the addition of further "automatic" triggers in Paragraph 4.

The existing two circumstances in Paragraph 4 of (i) providing a Critical Function and (ii) posing a Significant Impact on the financial system/real economy—already capture the entire universe of legitimate systemic risk scenarios. Adding further "notwithstanding" clauses would unnecessarily strip jurisdictional authorities of the flexibility to assess context, potentially forcing benign insurers into burdensome RRP regimes based on technicalities rather than actual risk.

We also strongly oppose language that would expand the application of who should be required to prepare recovery and resolution plans. As mentioned previously, local supervisors have the existing tools to determine when insurers would be required to create RRP's. An expansion of insurers subject to RRP requirements would create an expensive regulatory requirement that a supervisor may not even consider necessary.

9. What are possible quantitative or qualitative thresholds concerning the six criteria or some combination of the six criteria that should necessitate RRP requirements, notwithstanding any other facts or circumstances? For example, should the Draft Guidance call for RRP requirements whenever the cross-border activities of an insurer exceed a certain threshold?

We advise against establishing quantitative or qualitative thresholds that necessitate RRP requirements, including a combination of the six criteria, "notwithstanding any other facts or circumstances."

Applying RRP requirements based solely on a hard threshold (e.g., exceeding $X Billion in assets or operating in Y number of jurisdictions) creates a "blunt instrument" approach that contradicts the Key Attributes' principle of proportionality. While certain thresholds can help guide local supervisory decisions and may be useful for supervisors identifying certain risks, they should never automatically trigger RRP requirements. Such automatic triggers undermine the ability of jurisdictional authorities to use their judgement in determining which insurers, regardless of size, actually pose a risk to the economy.

Proposed revision to FSB guidance on critical functions

10. **What are the advantages and disadvantages of revising the FSB's guidance on the definition of a critical function for insurers by changing the phrase "the sudden failure to provide the function would be likely to have a material impact on the financial system *and* the real economy" to "the sudden failure to provide the function would be likely to have a material impact on the financial system *or* the real economy"?**

    We do not support the proposed change to the definition of a critical function from a material impact on the "financial system and the real economy" to the "financial system or the real economy."

    While the FSB argues this change aligns with banking standards, it ignores the fundamental differences between insurers and banks. The use of the word "or" drastically expands the scope of potential RRP requirements, potentially capturing purely domestic or niche insurers that pose no risk to global financial stability but are merely important to their specific customer base.

    The disadvantages of such a change significantly outweigh any advantages. Although the FSB notes that this change aligns the text with ICP 12.4.4 (which uses "and/or") and banking guidance, automatic alignment of such text is ill-advised since insurers and banks are fundamentally different.

    We invite the FSB to consider review the Global Federation of Insurance Associations (GFIA) report from 2024, "Insurance: A Unique Sector" (https://www.gfiainsurance.org/news/533/gfia-report-insurance-a-unique-sector)

    This report details how the insurance industry is a unique sector that is highly regulated and has a very different risk profile from banks and other financial sectors. Due to the long-term liabilities, risk pooling, and low liquidity risk, the report details how regulations regarding insurers should be treated differently than the regulations that govern other financial institutions.