

Comments

of the German Insurance Association (GDV)

on

Developing Effective Resolution Strategies and Plans for Systemically Important Insurers

Consultative Document

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General Comments

The German Insurance Association (GDV) welcomes the opportunity to comment on this draft, which builds on both the sector-specific guidance to the FSB Key Attributes of Effective Resolution Regimes for Financial Institutions and the guidance on identification of critical insurance functions and would like to make the following observations:

- We acknowledge that the FSB has endeavored to limit the width of the Critical Function's definition to potentially capture fewer functions. However, we are concerned that it is still unclear what (i) amounts to a Critical Function (systemic risk or mere policy holder protection concept?), (ii) what consequences follow therefrom (forced recovery or orderly run-off?) and therefore (iii) whether new book (maintenance of offering of certain insurance products under any circumstances) and/or old book (protection of policyholders) are targeted. This is particularly important as, once a Critical Function has been designated, it may have far reaching consequences from an operational continuity standpoint.
- The Consultation Paper discusses various options for (intra-group) critical shared service providers to safeguard operational continuity (ranging from mere information re-quests and analyses of service level agreements to forced legal structure changes in form of ring-fencing and pre-funding requirements). It is difficult to comment on such wide range of options as insurance undertakings can-not assess what regulators may ultimately require. Any resolution strategy must be established within the parameters set by insurance supervisory and insolvency law.
- We strongly approve that resolution strategies and objectives need to be tailored to the specific environment the insurer is operating in. Due to the variety of business models and group structures a one-size-fits-it-all-resolution strategy will inevitably fail to meet the objective of maintaining financial stability and policyholder protection.
- At the same time, we endorse the admission of the FSB that the authorities need to have flexibility by determining the point of entry into resolution. Focusing on the group structure of the firm and the way that its activities are organized within that structure instead of following abstract definitions of non-viability is the right way to get a grip on this complex issue.

- The requirements on the resolution strategies for reinsurers indicate an increased level of systemic relevance. We reiterate our view that neither the limited degree of interconnectedness with primary insurers nor the substitutability of reinsurance products gives reason for systemic concerns.
- In the overall context of the FSB framework we would strongly recommend to allow best practices, which are used in the European Solvency II regime and are almost adequate to the future FSB-standards. This could be applied when similar practices, criteria or data will be used. With this measure a double effort within the whole European Insurance Industry could be avoided.

Questions for consultation

Question 1

Do you agree that authorities should identify institution-specific resolution objectives as proposed in Section I.? Are there any considerations relevant to that identification, additional to those discussed in this document, that should be covered in the Guidance?

Yes. In addition, we feel that the resolution authorities should closely engage with the insurer in order to ensure transparency and to define realistic objectives.

Question 2

Are the considerations for determining “points of entry into resolution” as discussed in Section I.1 appropriate and relevant for the insurance sector?

Yes. The FSB highlights that the structure of the group prejudices the determination of points of entry. This linkage ensures that authorities have the full spectrum of flexibility to take full account of the business model and structure of the group. Moreover, the variety of possible entry points enables authorities to develop customized strategies in contrast to stick to one predefined script that possibly does not match reality.

Question 3

Do you agree with the considerations in Section II and underlying analysis in Section III for determining a preferred resolution strategy? Are there other relevant factors that should be taken into account?

Basically yes. In detail, we comment as follows:

Section II. 1. states that authorities may require firms to make changes to legal and business structures to improve their resolvability. Influencing the structure of a group is a severe regulatory intervention that needs to be justified in terms of proportionality. Given that crisis situations do not occur overnight and are usually managed over the long term, we believe structure changes should only be envisaged under exceptional circumstances as a measure of last resort.

Section III. 1 b. claims that some P&C policies are complex and unique and it might be more difficult to find a substitute product in some jurisdictions. The GDV would like to point out that lack of substitutability is not an issue in the (re) insurance business. There is no indication that the services provided by a failing (re) insurer could not be absorbed by other

competitors. This was also confirmed by the IAIS report “Insurance and Financial Stability”¹.

Section III. 1. c. addresses the alleged risks posed by reinsurers on primary insurers and the rest of the financial system. The IAIS report “Reinsurance and Financial Stability”² pointed out that reinsurance is unlikely to cause, or amplify, systemic risk, neither to the broader financial market nor to primary insurers due to the low level of interconnectivity.

Question 4

Are the resolution tools that are described in Section II.2 appropriate for use in a resolution of an insurer? Should other tools be considered?

The GDV welcomes that portfolio transfers are mentioned with a certain preference by the FSB. This goes along with the long term nature of insurance liabilities and their extended run-off profiles providing the time necessary for deliberate and balanced action while serving the interests of policyholders and financial stability.

The Consultation Paper rather loosely refers to a restructuring of liabilities. We believe that re-structuring policyholder liabilities can be a powerful tool in recovering a distressed insurance undertaking. However, besides regulator-ordered restructurings of policyholder liabilities, other bail-in instruments are not appropriate due to the specific structure of insurance balance sheets (90% of liabilities are policyholder reserves, third party debt is at a very low level and the rest is equity).

Question 5

Is the proposed framework for developing effective resolution strategies and plans for systemically important insurers flexible enough to take due account of the different types of business undertaken by systemically important insurers?

Yes, as long as the final guidance continues to preserve the flexibility needed instead of imposing binding requirements.

¹ <http://iaisweb.org/index.cfm?event=getPage&nodeId=25255>

² <http://iaisweb.org/index.cfm?event=getPage&nodeId=25255>

Question 6

Is the proposed approach for identifying (i) critical functions (Section III.2) and critical shared services (Section III.3) appropriate and relevant for supporting the development of effective resolution strategies and plans for systemically important insurers? If not, what aspects, if any, are missing or need to be changed?

Despite the fact that the FSB proposes some important limitations on the concept of critical functions, the regulatory goal which the elaboration on critical functions of insurers is supposed to serve still remains vague.

Section III. 2. c. expects authorities to determine a regulatory objective once a critical function that needs be continued is identified. If continuity of cover for life insurance policies is the main objective it should be noted, that the authorities should focus on whether equivalent products at reasonable prices are available, rather than to assume substitutability only if policyholders could procure replacement coverage under exactly the same contractual terms.

Regarding the extensive list of critical shared services listed in section III. 3., it should be clarified that these services are intertwined with critical functions. Regulatory requirements imposed on critical shared services must be based on a sound legal basis and recognize the policy choices made in the course of prudential regulation. In this context, it is important to realize that no framework can invalidate the inherent risk of failure without harming policyholders.

Question 7

Are there arrangements, in addition to those set out in Section IV of the draft Guidance, that may be needed to ensure that a resolution strategy for an insurer can be implemented and that should be covered by this guidance?

Referring to resolution plans as described in section IV. 1., the GDV would like to emphasize in general terms that plans must be adapted to the specific structure of the insurer and need to recognize that insurers operate quite different in a resolution situation given the long term nature of their business model. At the same time, it is paramount that the authorities are keeping their flexibility. Resolution plans should not constitute a corset obstructing the regulator's objected view on what it is necessary in the concrete situation.

Section IV. 3. illustrates the importance of being flexible by considering all relevant factors when defining the trigger for resolution.

Section IV. 4. specifies the cooperation agreements underpinning the resolution strategy and plan. Aspects of cross-border cooperation are described in the “FSB Guidance on Cooperation and Information Sharing with Host Authorities of Jurisdictions where a G-SIFI has a Systemic Presence that are Not Represented on its CMG” released on November 3, 2015. However, it is understood that any cross-border cooperation must be developed in accordance with the rule of law.

Regarding a review timeframe of “at least annual”, we suggest to update the resolution plan only if there are material changes. This could happen by implementing an additional clause for the most critical adjustments (e.g. material changes in product lines or in risk capital) in the framework. For the regular reviews by “appropriate senior officials” we suggest an adjusted review-period of three years.

Question 8

Are there any other issues in relation to resolution strategies and tools or the resolution of insurers generally that it would be helpful for the FSB to clarify in further guidance?

n.a.

Berlin, 4 January 2016