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Svein Andresen
Secretary General
Financial Stability Board
Centralbahnplatz 2
CH-4002 Basel
Switzerland

Anna Maria D'Hulster

Secretary General
The Geneva Association

Re: Developing Effective Resolution Strategies and Plans for Systemically Important Insurers

Dear Mr. Andresen,

The Geneva Association (GA) and the Institute of International Finance (IIF) are pleased to submit our joint response to the FSB's Consultative Document (CD) on "*Developing Effective Resolution Strategies and Plans for Systemically Important Insurers*" which was released on 3 November 2015. Our response reflects a joint effort of the members of our organizations. Together we represent a wide variety of insurers with representation across all geographies, product lines, and organizational structures, including all insurance groups which have been identified as Global Systemically Important Insurers (G-SIIs).

Our response follows up on our joint response in 2014 to the FSB consultation on the identification of critical insurance functions¹. While we are pleased to note that the new CD reflects that many of our comments have been evaluated and considered by the Financial Stability Board (FSB) we believe a number of issues require further consideration.

We note that the CD is aimed at regulators, supervisors and resolution authorities. As is set out in the 2014 Key Attributes document, resolution assessments should be conducted by home authorities and coordinated with the firm's Crisis Management Groups (CMGs).

¹ <https://www.iif.com/publication/regulatory-comment-letter/joint-ga-fsb-consultation-recovery-and-resolution-planning>

We are committed to continuing to work with the FSB – and the International Association of Insurance Supervisors (IAIS) and other stakeholders – in order to develop an effective and reliable resolution framework, which pays respect to the dual needs of preserving financial stability and strong policyholder protection.

Sincerely,

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Andres Portilla

A handwritten signature in black ink, appearing to read 'Anna Maria D'Hulster'.

Anna Maria D'Hulster

General comments

Before responding to the eight specific questions raised by the FSB in the CD, we would like to make some important comments of more general relevance:

- It is imperative that resolution strategies reflect the business model of insurance. Our comments are to be seen in this light.
- We recognize and appreciate that the CD proposes development of resolution strategies that serve as a guide for authorities, rather than setting prescriptive requirements. Given the heterogeneity of insurers, such a guide must take into account the boundaries set by the jurisdictional laws governing the financial contracts of insurers.
- In addition to working closely with the insurer and stakeholders, it is important for regulators and resolution authorities to liaise with each other to ensure a common understanding of the resolution strategy. For this purpose, we fully support the development of cross-border cooperation agreements.
- We acknowledge and appreciate the degree of flexibility included in the CD regarding the identification of points of entry into resolution and reiterate that given the heterogeneity of insurers and jurisdictional laws governing the financial contracts of insurers across the global financial system such flexibility is essential. In respect of resolving subsidiary-based insurance groups with many or all of the characteristics set out in Section II.1.b, we welcome the suggestion that an “opco” approach may be the more suitable resolution strategy.
- The principle of proportionality should inform resolution guidance and related measures, recognizing that failure of individual firms will have specific characteristics.
- An a-priori restructuring of existing legal and business structures would require an appropriate legal basis. Further, it is questionable whether such an action would provide sufficient benefit to justify the costs, including opportunity costs. Such costs must be borne by market participants, including policyholders – not just in monetary terms, but also, potentially, in the form of reduced product offerings by the industry. We therefore believe it is important that a resolution framework and tools be in line with prudential regulation policies and goals (particularly the level of protection offered to policyholders at a specified confidence level) as this will ultimately determine the threshold between the solvency and insolvency of individual firms.
- We continue to believe very few, if any, critical functions might be relevant in insurance. We interpret the CD as supporting this understanding. As such, we acknowledge that the FSB has endeavored to narrow the critical function definition to better account for this understanding of the insurance business model. In order to ensure consistent implementation of the FSB policies, it is important that the objectives of the Critical Functions concept are unambiguously defined.
- In the context of this central argument on Critical Functions, we would like to underline the link to the topic of Critical Shared Services. Critical Shared Services, or operational continuity, has its own definition and place in the CD. However, it is inevitably connected to the definition of Critical Functions. We emphasize that it is the identification of Critical Functions which defines the range of possible Critical Shared Services in insurance, as opposed to “regular” shared services.

Detailed Questions

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?

- We support institution-specific resolution objectives and encourage regulators to use the flexibility provided in the CD in seeking the most appropriate, proportionate and tailored approach.

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

- We welcome that specific terminology for the insurance business was chosen to reflect the specificities of the insurance sector. We believe the group structure of the firm and the way that its activities are organized within that structure must be considered in determining points of entry into resolution. A feasible and credible resolution strategy must take account of the jurisdictional laws governing the financial contracts of the insurer and offer flexibility to leverage the tools available rather than those that may be preferred by the authorities.
- The development of a preferred resolution strategy that best achieves the resolution objectives may depend on many factors such as the existing structure and business model, the need for recapitalization, the necessity for preservation of diversification, or the degree of internal interconnectedness within the group.
- In respect of resolving subsidiary-based insurance groups with many or all of the characteristics set out in Section II.1.b, we welcome the suggestion that an “opco” approach may be the more suitable resolution strategy.

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?

- The progression from a viable, fully solvent insurer to a non-viable, insolvent insurer is slow and timely recovery action would make an insolvent run-off unlikely. In this respect it should be noted that even in fast moving stress scenarios insurance resolution is still a long process.
- We disagree with the statement that "in some cases, the highly specialized nature of the primary business means that very limited reinsurance alternatives are available" (page 16, part of second last paragraph). In the event of the failure of a reinsurer operating in highly- specialized business lines, expertise is not lost and capacity will still be present in the market so that coverage can be substituted within a reasonable timeframe. The two examples in section III.1.c of how failure of a reinsurer could give rise to contagion to the extent that it materially weakens other insurers or reinsurers if needed, do not properly reflect the reinsurance market. In the case of an isolated reinsurance failure, expertise and capacity will remain in the market giving continued reinsurance options for primary writers. At an industry wide level, major catastrophes lead to premium increases (a hard reinsurance market) with the consequent attraction of additional capital and

reinsurance capacity.

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?

- It is important to be very clear on the definition of 'bail in'. In our view, the CD rather loosely refers to a restructuring of liabilities, a write down of liabilities, or conversion into equity. We believe that restructuring policyholder liabilities may be justified (i.e. if deemed so by the authorities). However, other bail-in instruments are not relevant or appropriate for insurers. Further we believe that a bail-in could create legal uncertainty for reinsurance creditors and could undermine good risk management. In addition, some bail-in instruments would unnecessarily increase interconnectedness with other players of the financial service industry.

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?

- We recognize and appreciate that the CD proposes development of resolution strategies that serve as a guide for authorities, rather than setting prescriptive requirements. Given the heterogeneity of insurers, such a guide must take into account the boundaries set by the jurisdictional laws governing the financial contracts of insurers.
- In addition to working closely with the insurer and stakeholders, it is important for regulators to liaise with each other to ensure a common understanding of the resolution strategy. For this purpose, we fully support the development of cross-border cooperation agreements.
- We would appreciate if the need for diversification-preserving resolution strategies could be explicitly mentioned within the description of reinsurance business in section III.1.c.

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?

- While we appreciate the enhancements included in the CD to better account for the insurance business model, the analysis required to identify the critical economic functions is still quite extensive. We believe regulators should discuss with the insurer which areas analysis should focus on. Such analysis should be objective and take the experience of the insurer into consideration.
- In relation to Critical Functions, we note that substitutability should be on the basis of a 'reasonable' rather than 'minimum' amount of time, and we suggest a more precise definition of Critical Functions as follows:

Functions that do not have a significant impact on economic and financial stability or that can be substituted within a reasonable period of time and at a reasonable cost are not considered critical. With respect to all other functions, a function is critical if it has both of the following elements:

- (i) It is provided by an insurer to third parties not affiliated with the firm; and*
- (ii) The sudden failure to provide the function would likely have a material impact on the financial system and the real economy (by giving rise to systemic disruption of the financial system and the real economy or giving rise to systemic contagion).*

This change is consistent with the intent to capture only functions that, if suddenly discontinued, would significantly impact financial stability, and eliminates any confusion caused by the use of the disjunctive in sub-bullet (ii).

- In relation to Critical Shared Services, we stress that a Critical Shared Service is a service that supports a Critical Function, and hence should only be considered where Critical Functions have been identified.

Box 3: Arrangements to support operational continuity

- We welcome the opening statement in Box 3 that the following arrangements ‘could be’ considered to support operational continuity rather than positioning them as mandatory requirements. This implicitly recognizes that judgement will be required depending on the individual circumstances of a systemically important insurer. The points that follow, which are currently expressed as arrangements that ‘should’ rather than ‘could’, support operational continuity, should be amended to be consistent with the introductory statement.
- We agree that clearly documented contractual arrangements and Service Level Agreements should be in place for intra group and third party critical shared services as an element of good practice.
- Regarding financial resources, it is important to recognize that insurers already have provisions for expenses in the calculation of their liabilities and it will be for the administrator to decide immediate funding priorities, e.g. ensuring that the third party provider continues to be paid.
- We are not aware of examples when insurance administrators failed to pay external suppliers.

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?

- Feasible and credible strategies to address resolution of entities across jurisdictional boundaries are reliant upon strong and continuous cooperation among regulators. While we fully support the development of cross-border cooperation agreements for this purpose, we do not support a duplication of efforts or requirements at the home and host country levels. Host supervisors should have input on design of the resolution strategy through their participation in the CMG mechanism. Host supervisors should not require separate plans or data submissions regarding only local subsidiaries, which could potentially contradict strategy developed for the group.

- Pre-agreed resolution triggers should be transparent to the affected companies. All defined triggers for resolution plans should be shared with all involved bodies.
- The interaction between regulatory authorities and the administrators of policyholder protection schemes should be defined in resolution plans.
- It will be difficult to identify policies that are eligible for compensation in advance given that eligibility is defined at the time of resolution. Efforts should be focused instead on improving/facilitating the process that would enable the identification of eligible policyholders in resolution (i.e. contingency actions).

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?

- Under Section III. 1.d. (Strategic analysis underlying the development of the resolution strategy/Financial Market Activities and investment products) reference is made to a short-term liquidity guarantee associated with annuity products. We believe that this section is referring to deferred annuities since most immediate annuities do not contain a surrender value. While we would generally support a recommendation that regulators have the power to impose a temporary stay in certain circumstances, we disagree with the characterization in footnote seventeen of the variable deferred annuity guarantees and the systemic risk that they pose. In regards to the second sentence in the footnote, while the policyholder does have the right to move assets between separate account funds (subject to certain restrictions which vary by product series) which incorporate varying levels of exposure to equities and bonds, most annuity providers have instituted asset allocation requirements which restrict the level of risk that a contract holder can incorporate into their deferred annuity.
- In addition to these asset allocation requirements, annuity providers have also introduced fund of fund and managed volatility options which minimize fund movements by contract holders. These limitations on asset allocations, the addition of managed volatility options and income and withdrawal guarantees should add to the stability of investments during market instability since the policyholder is committed to a certain investment strategy with a focus on retirement income.
- Moreover, we note that in the event of a resolution it is likely that the value of policyholder guarantees will remain high; as a result it will be expensive (and a disinclination) to policyholders to surrender. For this reason insurers are unlikely to face a mass surrender of policies.