

Response to IAIS consultation on its draft application paper on macroprudential supervision

Q1. General comments

GFIA appreciates the opportunity to comment on the application paper on macroprudential supervision. The insurance industry welcomes the reference to and the application of the overarching concept of proportionality in macroprudential supervision .

The Holistic Framework for Systemic Risk, which the paper builds upon, represents an achievement in relation to the management of potential systemic risk.

The framework includes a number of enhancements to micro prudential measures to mitigate certain risk exposures and increase the resilience of the insurance sector and/or decrease the probability and magnitude of a negative systemic impact where risk does materialise. Therefore, the guidance on the application of ICP 24 should reflect this reduced risk and approach the elements of the ICP with appropriate proportionality.

In addition, ICP 24.0.3, in describing macroprudential supervision, notes that it involves the identification, monitoring and assessment of sector-wide vulnerabilities and common exposures in the insurance sector and the risk of amplification and transmission of shocks to the financial system and real economy caused by the size, complexity, lack of substitutability and/or interconnectedness of a distressed or failing insurer; or collective actions or distress of a sufficiently large number of insurers undertaking similar activities and thus exposed to common risks. In line with this guidance, GFIA takes the view that monitoring and assessment of sector-wide vulnerabilities should be the prime focus, thus enabling supervisors to focus on vulnerabilities of distressed or failing insurers, where relevant. Currently the application paper seems to place more emphasis on the assessment of the potential systemic importance of individual insurers, rather than the assessment of sector wide vulnerabilities.

In this respect, GFIA is concerned that the paper's focus on the assessment and systemic relevance of individual insurers departs from the identification, monitoring and assessment of insurance sector-wide vulnerabilities and common exposures, and the risk of distressed or failing insurers or the collective actions or distress of a sufficiently large number of insurers, as noted above.

While the framework includes the establishment of a supervisory process to assess the potential systemic importance of individual insurers and the wider insurance sector, these must be balanced in the context of the framework as a whole, which enhances micro-prudential measures to mitigate certain risk exposures and increase the resilience of the sector, together with a focus on the monitoring and assessment of sector-wide vulnerabilities. The paper in contrast seems to have shifted back toward more emphasis on an entity-based approach.

GFIA therefore suggests to de-emphasize the entity-based elements of this paper in favor of a stronger initial focus on the monitoring and assessment of sector-wide vulnerabilities and common exposures on the insurance sector.

GFIA would also like to highlight that the potential use of stress testing within individual insurers' own risk and solvency assessment (ORSA) reports is an inappropriate use of the ORSA concept. The ORSA is owned and managed by firms themselves, representing an "own view" of risk and so it would be inappropriate for supervisors to seek to specify stresses that insurers should apply in the ORSA.

The application paper should also encourage greater flexibility for supervisors in the manner in which they assess systemic risk, both at a sectoral level and with respect to individual insurers, given the differences across markets. Supervisors should be able to base their assessments on their knowledge of insurers, the markets they are responsible for and the data they already have access to. In this respect, the focus should be on outcomes in terms of the questions supervisors are seeking to answer.

In addition, the application paper appears largely silent on involving the insurer in the supervisors findings. ICP 24.3.4 notes that the supervisor should communicate the findings of its assessment, as appropriate. The guidance would be improved if it covered the interaction between the supervisor and insurers in this respect, particularly in the need for supervisors to clearly articulate and quantify the scale of any potential systemic risk and to discuss this with the insurer to ensure that there is a common understanding, and where so to provide insurers with the opportunity to set out how such risk can be managed.

Q6. Comment on paragraph 4

GFIA appreciates the clear recognition in paragraph 4 that the paper does not establish new standards or expectations, and should not be considered as an exhaustive guide to macroprudential supervision. This is especially important for jurisdictions that have well-developed systems of macroprudential supervision.

Q13. Comment on section 1.3 Proportionality

The insurance sector appreciates the paper's clear statement that the proportionality principle must be consistently applied to macroprudential supervision, and that nothing in the paper supersedes this principle.

GFIA encourages the IAIS to continue to stress the importance of the proportionality concept where there could be ambiguity in sections of the paper about the need for proportionality in the application of macroprudential supervisory measures.

The framework includes a number of enhancements to micro-prudential measures to mitigate certain risk exposures and to increase the resilience of the insurance sector and/or decrease the probability and magnitude of a negative systemic impact where risk does materialise. (Paragraph 48 of the framework).

Therefore, the guidance on ICP 24 should be drafted in this context and reflect that other measures in the wider framework result in reduced risk: ie the guidance surrounding the assessments of the systemic impact of individual insurers should not be as prescriptive or overly engineered as currently drafted. ICP 24 requires assessment of systemic risk in the context of both individual insurers and the sector and these should have at least equal weighting in the guidance, which currently gives more prominence to the assessment of individual insurers.

Q15. Comment on paragraph 10

It is GFIA's view that proportionality is not only required with respect to "the nature, scale and complexity of (the) insurance sector's exposures and activities", but also with respect to individual insurers' exposures and activities. Therefore this should be added explicitly.

Q20. Comment on section 2.1 Consideration of data to collect

The focus appears to be on building a separate monitoring framework with bespoke reports, rather than first considering how supervisors can build on their existing understanding of insurers and information that they already have access to.

The potential benefit for supervisors to have additional data that might provide additional valuable insight into the state of the sector needs to always be balanced with the resource demands that expansive data calls place on both insurers and supervisors. In addition, it should be stressed that supervisors should collect data in the least-burdensome way possible, in light of the cost of data collections to both the insurers and supervisors.

GFIA therefore urges the IAIS to amend the paper in such a way that explicitly recognizes that data collections should have a specific link to supervisory needs and not be overly broad, in line with ICP 24.1.1.

GFIA would suggest that this paragraph is amended to include a line which states that: "In line with the objective of proportionality, existing data already provided by the insurer(s) should be leveraged, and where possible reconstituted for other metrics, before additional, bespoke information is required from the group or legal entity".

The IAIS and supervisors should coordinate jurisdictional data calls and IAIS data collections to avoid duplication and burden. Such an approach should be noted in the paper.

Furthermore, the paper should state explicitly that supervisors must consider the sensitivity of some insurer information (even in the aggregate) and determine the decision-usefulness and potential for misinterpretation of that information to investors and other users of the information before publishing it.

Q23. Comment on paragraph 15

GFIA recognizes that the framework does not preclude macroprudential supervision of individual insurers, and agrees that macroprudential supervision depends on good quality data.

However, the emphasis in the paper on data collection from individual insurers appears to be a symptom of the shift back towards the macroprudential supervision of entities rather than the appropriate balance between the supervision of activities and entities that was presented in the framework.

In many jurisdictions, reporting and disclosure requirements for the insurance industry are already very extensive. In order to ensure efficiency and proportionality of data collection for macroprudential purposes, it should be stated that supervisory authorities should primarily make use of the data sets that are already available, as stated in ICP 24.1.1. Further, the supervisor should examine costs and benefits when considering data collection. Additional reporting requirements should be avoided wherever possible in order to avoid repeated, redundant collection of the same or materially similar data point and therefore prevent unnecessary burden on insurers.

The paragraph refers to the transparency of data collections. Transparency also includes the responsibility of the data collector to inform about the purpose and results of a data collection.

The efficiency of data collections should be emphasized, for instance highlighting that data collections should focus on the key necessary data points only and collection of unnecessary (ie nice to have, not needed for any supervisory purpose) data or data that is not further analyzed should be avoided at all cost.

GFIA suggests to make this explicit in the first bullet point by rephrasing it to add "Data collected should be aligned with supervisory needs and serve one or several specific supervisory purposes".

The reference to climate-related risk in the fifth bullet point appears too specific and could be understood in a prescriptive way.

Q25. Comment on section 2.2 Risk dashboard for monitoring key macroprudential indicators

GFIA recognizes that the framework does not preclude macroprudential supervision of individual insurers. However, the emphasis on data collection from individual insurers in the paper appears to be a symptom of the shift back toward the supervision of entities rather than the supervision of activities and entities that was presented in the framework.

Q31. Comment on section 2.2.1 Constructing a risk dashboard

This section presents the risk dashboard as one example of a method for monitoring key macroprudential indicators. However, the facts that (i) no other example next to this is presented, (ii) the risk dashboard method is explained in very much detail over more than two pages and (iii) language is used such as "It is good practice..." (Para 22) and "Jurisdictions should..." (Para 23) could be understood as a push or expectation for supervisors to implement risk dashboards. This clearly goes beyond ICP 24 and the fact that supervisors have the freedom to implement the tools they deem most appropriate for their purposes.

Q45. Comment on paragraph 32

The insurance sector supports the IAIS's approach to provide examples of methods to analyse systemic risk in the insurance sector combined with letting supervisors choose the methods most appropriate for their jurisdictions.

Q49. Comment on paragraph 36

The analysis of second round effects, though in principle desirable, will often be very complex and subject to uncertainties and interpretation difficulties. Therefore, a careful balancing of costs, risks and benefits of such analyses is needed. The limitations of second round-effect analyses should be fully taken into account, and an overloading of the analytical framework should be avoided.

It should be once again stressed that the emphasis on data collection from individual insurers in the paper appears to be a symptom of the shift back toward the supervision of entities rather than the balanced supervision of activities and entities that was presented in the framework.

Q53. Comment on paragraph 40

This paragraph mentions impact analysis without a definition being given and without further reference in the paper. Therefore, GFIA suggests deleting this reference.

Q57. Comment on paragraph 42

This paragraph suggests that analyses of the main historical trends are carried out quarterly, semi-annually or annually depending on the availability of data. Instead of making the decision about an appropriate frequency of analyses dependent on the frequency the underlying data is updated, supervisors should start with what frequency is required for achieving their supervisory objective and a cost/benefit consideration (ie not performing quarterly analyses just because quarterly data is available).

Q61. Comment on section 3.2.2 Stress testing

In some jurisdictions, insurers may be required to recapitalize or reduce their risk exposure to meet specific scenarios, if stress tests are conducted by the supervisors.

Regardless of the situation at national level, scenarios need to be well thought out so that it is neither an excessively large nor long-term event, but a reasonably probable event.

In addition, when forming the scenarios, the basis should be clearly stated: such as whether insurance companies are considered as a going concern, or avoiding resolution.

GFIA proposes to clarify that supervisors should consider and address the above proposals.

Q63. Comment on paragraph 47

The insurance sector welcomes that the stress tests should be fully integrated in a jurisdiction's supervisory framework and not be considered as a stand-alone exercise.

For example, the insurance stress test for European insurers should be in line with Solvency II, and should not be considered as a pass-or-fail exercise for the participating insurers.

Q66. Comment on paragraph 50

While GFIA recognizes that the framework does not preclude macroprudential supervision of individual insurers, the emphasis on stress testing individual insurers here in the "bottom up" and "top down" approaches appears to be a symptom of the shift back toward the supervision of entities rather than the supervision of activities and entities that was presented in the framework.

Q67. Comment on paragraph 51

The insurance sector takes the view that ORSA stress tests must not be used in any sort of horizontal review.

Regarding the following provision: "As discussed above, stress testing is also required to be conducted by insurers as part of their own enterprise risk management (ERM), for instance as part of the own risk solvency assessment (ORSA)." ORSA stress tests are based on the risk assessment of the insurance company itself for microprudential purposes, and it seems inadequate to include stress tests for macroprudential purposes within the ORSA. Therefore, these provisions should be deleted.

In addition, the ORSA is each individual insurer's own risk assessment and, as such, different insurers are likely to use different stresses that are appropriate for their own capital management. It would also be inconsistent with the statement in Annex 4 of the paper, "the insurers would remain free to define the content of the ORSA".

Supervisors should not provide detailed guidance to stress test participants with standardised specifications on how to conduct stress tests to be included in the ORSA, or as part of their own ERM, as this could undermine its purpose and role. ORSA reports should be insurer-specific and should be kept as an instrument tailored to the specific management of individual insurance groups and companies.

Any attempt to standardise ORSAs would greatly reduce the usefulness of this important tool for both supervisors and insurers.

Q70. Comment on paragraph 54

In the event of crises or shocks, firms, particularly those staff managing capital, may not have sufficient resources to allocate to perform stress tests, therefore undertaking additional and more frequent stress tests by companies may not be prudent, whereas supervisors could collect data in crisis/shock scenarios to allow them to conduct their own analyses. The paper should encourage supervisors to think about what frequency is required for achieving their supervisory objective and a cost/benefit consideration.

Q74. Comment on paragraph 58

GFIA believes that regulators should be very careful when it comes to expanding the timeframe of the stress test and moving to a multi-period framework in which the insurer's post-stress solvency position is assessed against a set of risks that evolve over longer periods (eg three or five years). The added value would be limited due to technical limitations and uncertainties, and the implementation cost very high.

Q76. Comment on paragraph 59

The expression "scenario" is used both in the section about stress testing as well as sensitivity analysis hindering the understanding what the difference between the two methods is.

Q77. Comment on paragraph 60

It should be noted that submitting data requests to insurers is no guarantee of homogeneity given that different firms can often have different interpretations of certain instructions and differently derived data points. As such, it should not be assumed, particularly when undertaking a sensitivity analysis which varies one factor out of many, that results are perfectly comparable between insurers.

Q80. Comment on paragraph 62

This paragraph suggests that qualitative vulnerability analyses should be performed on a quarterly, semi-annual or annual basis. Instead of steering supervisors to random frequencies, the paper should encourage supervisors to think about what frequency is required for achieving their supervisory objective and a cost/benefit consideration.

Q83. Comment on paragraph 64

This paragraph suggests that workshops to facilitate qualitative exchanges of views with stakeholders should be performed annually. The paper should, however, encourage supervisors to decide themselves on the most appropriate frequency or ad-hoc organization of such events.

Q84. Comment on paragraph 65

This paragraph suggests that workshops to facilitate qualitative exchanges of views with stakeholders should be performed annually. The paper should, however, encourage supervisors to decide themselves on the most appropriate frequency or ad-hoc organization of such events.

Q87. Comment on paragraph 67

Again, rather than suggesting certain frequencies, the paper should leave it to supervisors to decide whether an ad-hoc approach or an interval approach is most appropriate and, in the case of the latter, what the most appropriate frequency would be to achieve the supervisory objectives.

Q101. Comment on paragraph 78

GFIA agrees that supervisors are required to have "an established process to assess the potential systemic importance of individual insurers and the insurance sector".

In this case, the systemic importance of the insurance sector should not be assessed alone, but rather within the entire financial system, including other sectors, such as banking and securities. In particular, due consideration should be given to the fact that systemic risk of core insurance activities is limited and the scale of potential systemic risk in the insurance sector is much smaller than that of banking.

As such, the supervisory assessment process should begin with a performance of the cross-sectoral analysis described in Section 4.2.5 (paragraphs 143 and 144) to assess the systemic importance of the insurance sector within the financial system. This should therefore be specified in the paper.

Q102. Comment on paragraph 79

As in so many other aspects of the business model, traditional insurers' liquidity risk is fundamentally different from that of banks. Banks face significant liquidity risks since their liabilities are predominantly short-term. They engage in maturity transformation by turning short-term liabilities into long-term assets. In contrast, insurers usually have an opposite position when it comes to maturity and liquidity transformation. Typically, insurers are providing liquidity to the markets by transforming longer-term and less liquid liabilities into shorter-term and more liquid assets. In other words, while banks are often at risk of being "liquidity-short", insurers are liquidity-rich by the nature of their business. Thus, their liquidity risk is very limited. Further, there is no need for supervisors to carry out the analysis of liquidity on an "ordinary basis" with agreed periodicity as described in Annex 3.

Q109. Comment on section 4.1 Assessing systemic importance of an individual insurer

The focus should be on risk exposures or activities that have the greatest potential to propagate systemic risk to the wider global financial system or the real economy through asset liquidation and exposure transmission

channels. It should also recognise the key role that insurers play as providers of liquidity to the financial system which act as 'shock absorbers', as this is overlooked throughout the paper. In addition, while insurers recognise that the framework does not preclude macroprudential supervision of individual insurers, the emphasis on individual insurers here appears to be a symptom of the shift back toward the supervision of entities rather than the balanced supervision of activities and entities that was presented in the framework.

Q111. Comment on section 4.1.1 Indicator-based approach

Despite several indicators to identify systemic risk listed in Section 4.1.1 (Indicator-based approach), the insurance sector has been the cause of very few cases of systemic risk. GFIA believes that the appropriateness and effectiveness of these indicators need to be carefully verified for use within the insurance sector.

Q112. Comment on paragraph 87

The insurance sector is concerned that the indicator-based approach diverges inappropriately from the spirit of the framework and its move toward a balanced activities-and entities-based approach.

GFIA notes that the IAIS has recognized that provision of traditional insurance, including non-life insurance, generates little systemic risk. In fact, insurers believe that it is primarily a systemic risk mitigant, rather than a systemic risk generator.

Q114. Comment on paragraph 89

This paragraph should be extended to better explain the relationship and interplay between the IIM exercise at IAIS level and what is expected at a jurisdictional level. It should be emphasized that data collection on both levels should be looked at in an integrated way rather than duplicating efforts and burden.

Q117. Comment on paragraph 92

While capital interconnectedness may be a valid concept in general, it should not be used to disapply the utility of securities issued by other financial institutions, because financial systemic events do not generally impact insurers in the same way as other parts of the financial system due to the limited correlation with the economic cycle and financial market risks (as evidenced, for example, by the IAIS report on insurance and financial stability, 2011). As such, insurers' liquidity and solvency needs do not automatically increase significantly during financial crises. Consequently, for insurers, the question of the value of different sources of capital is essentially a microprudential question linked to the riskiness of the asset. This is already well catered for by risk-based capital frameworks, such as Solvency II in Europe, and does not have a material, additional systemic angle beyond this.

Q118. Comment on paragraph 93

The use of EBIT as an indicator is not clear.

Profitability would not appear to be a useful indicator of the systemic influence of an insurer in the non-life industry. This is because profitability may be strongly correlated with external events, such as catastrophes, as well as the insurance cycle.

A consistently high EBIT could suggest that an insurer is especially resilient (assuming sound business management) and therefore of less concern from the perspective of financial stability than an insurer which makes less profit, or a loss. As such, it would not appear to make sense to use (high) EBIT to measure the potential systemic impact of an insurer.

Q121. Comment on paragraph 96

Regarding reinsurance recoverables: whilst a cedant relying on a reinsurer does introduce counterparty exposure, and therefore a degree of intra-industry interconnectedness, the IAIS recognises in its 2012 paper, 'Reinsurance and financial stability' that:

- i. The effect of reinsurance is to dampen the propagation of shocks through the insurance market; and
- ii. Although reinsurers can fail, in the past primary insurers have typically absorbed the loss of reinsurance recoverables without a significant detrimental financial impact.

As such, it is arguable that to have reinsurance recoverables available is a net benefit in terms of systemic impact, rather than a risk. The IAIS should avoid any implication that reinsurance introduces net systemic risk given the value of reinsurance as systemic shock absorber.

Q126. Comment on paragraph 101

The guidance in the paper includes indicators to assess the impact to the non-financial sector and public sector. This is welcome as an understanding of materiality is important in determining whether risks are systemic. GFIA would suggest that this approach should also be extended to 'the financial sector' since the current approach in the paper does not appear to provide adequate guidance for the assessment of materiality in this respect.

History has shown that the share of the reinsurance market is not a good indicator for limited substitutability. Past experience has shown that markets work very efficient by attracting new capital into reinsurance at the slightest signs of a supply shortening. Hence this indicator should be deleted from the list of examples.

Q127. Comment on paragraph 102

The 2011 IAIS paper indicates that "insurance markets tend to be competitive" and that substitutability "does not appear to be an issue in most national markets, and probably even less so in global markets". This is echoed in the framework, which states: "For most insurance business lines, competition is high and therefore limited substitutability is not likely to become a global systemic concern. However, there may be (niche) lines of business where only a few insurers dominate the market. In such markets, if the critical and short-term barriers to entry are high, the sudden withdrawal of important insurance coverage could, at a minimum, lead to increasing costs for those entities relying on these key services for their day-to-day business."

Regarding the use of market power as a metric, the IAIS must be very careful in identifying relevant insurance lines / products and market delimitation. For example, without taking into account the criticality of insurance cover, it may be that the supervisor unwarrantedly and inadvertently overstates an insurer's systemic impact.

Q131. Comment on paragraph 105

In light of the limited systemic risk posed by the insurance sector, relative measures of systemic relevance could easily lead to the over-identification of systemic relevance of the insurance sector. In particular, relative scoring risks designation of insurers based on local characteristics, rather than their systemic footprint.

Q136. Comment on section 4.1.3 Reduced-form approach

The industry is concerned about the indicator-based approach, as it also applies to the reduced-form approach, as long as it is directed at identifying individual insurers or groups. It diverges inappropriately from the spirit of the IAIS' holistic framework and its move towards a more balanced approach between scrutinising activities and entities.

Insurers are sceptical about whether this can contribute much to the identification of systemic risk, as assessing the systemic importance of insurers purely relying on statistical relationships has severe limitations and could often lead to misinterpretations.

GFIA also notes that the IAIS has recognised that provision of traditional insurance, including non-life insurance, generates little systemic risk. In fact, GFIA believes that it is primarily a systemic risk mitigant, rather than a systemic risk generator.

Q137. Comment on paragraph 110

The examples of 'reduced form approach' to assessing systemic risk include indicators such as SRISK. This is inconsistent with the guidance in ICP24 which notes that supervisors should take a total balance sheet approach. Hence the large focus on reduced-form approaches clearly goes beyond or even against ICP 24 and therefore should be avoided in the paper.

Q144. Comment on paragraph 117

The examples of 'reduced form approach' to assessing systemic risk include indicators such as SRISK. This is inconsistent with the guidance in ICP24 which notes that supervisors should take a total balance sheet approach.

Q157. Comment on paragraph 129

The paper is largely silent on involving the insurer in the supervisors' findings. ICP 24.3.4 states that "the supervisor should communicate the findings of its assessment as appropriate, to either individual insurers or the sector." This paragraph refers only to communicating the 'assessment methodologies' and 'regular engagements to reduce

systemic footprint', whereas ICP 24.3.4 clearly refers to communicating "findings" to the insurer(s), which is not included in this paragraph or elsewhere in the paper.

This paragraph and others would therefore be improved if amended to include the appropriate interaction between the supervisor and the insurer(s), particularly setting out the need for supervisors to clearly articulate and quantify the scale of any potential systemic risk when communicating with the insurer(s). It would make most sense for this to take place after communicating/discussing assessment methodologies but before engagement to reduce a systemic footprint. Efforts should be taken to ensure there is a common understanding of the risks between the supervisor and the insurers and where so, insurers should be given the opportunity to set out how such risk can be mitigated or managed before any further action, ie actions to reduce systemic risk, is considered.

If there is a formal identification methodology for identifying systemically important insurers, it should include an "off-ramp" whereby insurers know what they must do to de-risk and exit such identification. Failure to include such a mechanism was a significant defect in some of the initial attempts to deal with systemic risk after the global financial crisis.

In addition, supervisors should also be aware that the effect of relying on certain metrics to designate insurers as systemic could incentivise behaviour to exit or avoid such a designation that could have negative consequences on systemic stability itself. For example, substitutability is one of the three factors mentioned in Paragraph 87 as a basis to identify systemically important insurers. The risk of doing so is that insurers are incentivised to reduce their activities in a particular market for which there is limited substitutability, which would in itself cause the impact supervisors were intending to avoid. As such, supervisors must be sure that the potential impact of using such factors is fully considered.

Q158. Comment on paragraph 130

Regarding their assessment of systemically important insurers, the insurance sector very much supports that supervisors should narrow the scope of insurers using proportionality. In this way, overburdening undertakings and supervisors can be avoided, keeping costs and benefits in line.

This chapter explains how individual insurers and the insurance sector as a whole could be assessed for systemic relevance while giving little details on the appropriate frequency of such assessments (Paragraph 130 could be understood in a way that this is to be done on a yearly basis). ICP 24.3 is silent about this point and only requires an established process to be in place. Hence the paper should make it clear that there is no expectation to have such an assessment for individual insurers or the sector as a whole on a yearly basis (or any other given frequency). It should be emphasized in the paper that supervisors are free to conduct such an assessment on an ad-hoc basis when they feel drivers of systemic importance have changed significantly enough for individual insurers or the sector as a whole since the last assessment to justify the costs of a re-assessment.

Q161. Comment on paragraph 132

The statements in Paragraphs 132 and 136 that the sector could be considered systemically risky if one insurer is deemed systemically important are overly broad and does not reflect the fact that a systemically important insurer may be conducting significant non-insurance activities.

Q163. Comment on section 4.2.1 Macroprudential sector-wide stress tests

Sector-wide stress tests can be an important tool for macroprudential surveillance: eg the current stress testing exercises by EIOPA. However, it is important to avoid too much complexity and too far-reaching interpretations.

Q167. Comment on paragraph 136

The statements in Paragraphs 132 and 136 that the sector could be considered systemically risky if one insurer is deemed systemically important are overly broad and does not reflect the fact that a systemically important insurer may be conducting significant non-insurance activities.

Q168. Comment on paragraph 137

GFIA supports the IAIS's approach in that supervisors should use the proportionality principle to decide on the scope of insurers included in the sector-wide systemic risk assessment. The principle of proportionality should consistently be based on the actual level of risks taken in a business model or activity.

Q186. Comment on paragraph 150

Supervisory actions can harm a company and its policyholders and send the wrong signals to other insurers. The paper should reflect that supervisory discretion is essential to crafting appropriate supervisory actions, especially in the case of IAIGs where relevant supervisors in other jurisdictions may need to be brought into the discussion of how to address a particular supervisory issue.

Q187. Comment on section 5.2 Types of supervisory responses

The insurance industry supports the framework and complementing microprudential supervision with a macroprudential perspective.

Effective microprudential supervision and existing microprudential tools already go a very long way in addressing potential systemic risks. With respect to any macroprudential measures, it is crucial that there is a strict and consistent application of the proportionality principle and that measures are clearly targeted to a specific systemic risk identified.

In addition, it is important to note that though some tools can be applied with a micro- or macroprudential perspective, and that not every microprudential tool is suited for macroprudential purposes. For example, for the insurance industry, a blanket ban on distributions is not a suitable macroprudential instrument. Such an extensive intervention seems disproportionate in principle. Even regarding individual undertakings, it should only be used as an ultima ratio. Accordingly, ICP 10.2 requires that the insurer is likely to operate in a manner that is inconsistent with regulatory requirements. This requirement must not be undermined by macroprudential considerations unrelated to the individual situation of an insurer. In addition, potential counterproductive effects need to be taken into account. Dividend distributions are indispensable for an appropriate capital allocation within groups. Therefore, prohibiting dividend distributions within a group instead of enhancing financial stability can even have destabilising effects. Non-availability of dividends to external investors can also be counterproductive from a macroprudential perspective.

With respect to potential macroprudential tools, it is also crucial to ensure consistency and coherence of the supervisory system. For example, in a supervisory system that uses a principle-based prudent person approach, exposure limits for certain assets should be avoided.

Q188. Comment on paragraph 151

GFIA appreciates the recognition in this paragraph that appropriate microprudential supervision is a significant systemic risk mitigant. This is illustrated throughout the rest of the paper's discussion of supervisory responses.

Q192. Comment on paragraph 154

It is stated that "If a potentially systemic exposure is identified by trends in certain risks and activities in the macroprudential analysis, supervisors should require insurers to strengthen their ERM framework."

Scenarios must be well thought out so that it is neither an excessively large nor long-term event, but a reasonably probable event.

In addition, when forming the scenarios, the basis should be clearly stated, such as whether insurance companies are considered as a going concern, or avoiding resolution.

GFIA therefore proposes adding the above two points to the paper as matters which supervisors should consider and address.

Q193. Comment on paragraph 155

Further requirements in ERM development should be avoided, as companies must already consider all material risks that have an impact on the risk profile. Thus, the ERM includes those risks with potential systemic impact as well. Therefore, the insurance sector is of the opinion that the potential benefit of adding requirements or further unnecessary specifications does not justify the additional costs this would imply. Further, it would not provide a more detailed picture of the situation on the European insurance market.

Q194. Comment on paragraph 156

Regarding macroprudential analysis, while it is stated that "based on the risks the assessment may highlight, supervisors may require insurers to strengthen their risk appetite statement or to establish a counterparty risk

appetite statement to define more stringent limits”, insurers take the view that risk appetite is set according to each insurer's preference for risk, and correlated with each insurer's strategy. Therefore, the statement should be deleted as it is not appropriate for supervisors to be involved in such decisions.

Supervisors may discuss with insurers the results of the macroprudential analysis and ways to manage identified risks.

Q200. Comment on section 5.2.3 Preventive and corrective measures

When proposing the use of preventive or corrective measures, supervisors must consider the potential impact on policyholders (eg the potential to restrict product availability), as well as on macroprudential risk and financial stability (eg the impact of counterparty exposure limits on insurers' ability to provide market liquidity).

Q201. Comment on paragraph 161

In this paragraph, it is stated that “supervisors should have at their disposal a sufficiently broad set of powers” to address systemic risks. The measures described in ICP 10.2 are also listed as specific examples. However, supervisors should not have excessive powers to deal with systemic risk incommensurate to their purposes. In addition, the legal system in each jurisdiction should be taken into consideration. GFIA proposes adding provisions which describe such points.

A prerequisite to the use of any powers is that the supervisor has clearly articulated the nature and materiality of any systemic risk to the insurers and provided them with an opportunity to discuss this with the supervisor. This will ensure there is a common understanding and allow the insurer to set out a plan for how that risk can be adequately managed or mitigated.

Furthermore, the measures listed include strict contents such as "prohibiting the insurer from issuing new policies or new types of product", which are excessive compared to the situation "in the event that there are" signs "of the build-up of systemic risk". Provisions should be added to the effect that predictability and transparency are ensured in triggers and the operation of each measure so that insurers can take voluntary actions in advance.

Q206. Comment on section 6.1 Importance of transparency

The paper should state explicitly that supervisors must consider the sensitivity of some insurer information (even in the aggregate) and determine the decision-usefulness and potential for misinformations to investors and other users of the information before publishing it.

Q210. Comment on paragraph 167

GFIA agrees that transparency on macroprudential risks has an important role to play: eg with the regular publication of financial stability reports or risk dashboards or insurance statistics. However, the results of macroprudential sector analyses or of stress tests should not be published at individual company level as this could result in counterproductive effects (eg misinterpretations by market participants that lead to market distortions). It should be clarified that this is not required. The respective publications by supervisors should focus on aggregated data and more general aspects regarding market developments and the stability situation.

Q225. Comment on section Annex 4: Example of ORSA analysis

The appendix 4 includes an example of an ORSA analysis. As a microprudential instrument, we feel this is misplaced in an application paper on macroprudential supervision.

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