



IAIS

INTERNATIONAL ASSOCIATION OF
INSURANCE SUPERVISORS

Activities-Based Approach to Systemic Risk

Presentation at stakeholder meeting in London
1 February 2018



Agenda of the meeting

1. Short presentation of the 8 December consultation paper
2. Interaction on main aspects of the document, in particular
 - A. General approach (definition of ABA)
 - B. Identification of activities
 - C. Steps 3 and 4 of the conceptual approach (gap analysis and potential policy measures)
3. Next steps in the process

Background IAIS systemic risk work

2011	Publication of “Insurance and Financial Stability”
2012	Publication of “Reinsurance and Financial Stability”
2013	<ul style="list-style-type: none">• Identification of first cohort of G-SIIs• Publication of G-SII Policy Measures document• Publication of Report on Macroprudential Policy and Surveillance in Insurance• Guidance for Systemic Risk Management Plan
2014	Guidance on Liquidity Management and Planning
2015	Development first version of BCR and HLA
2016	<ul style="list-style-type: none">• Three – yearly review of G-SII Assessment Methodology• Publication of document on Systemic Risk from Insurance Product Features to clarify original concept of Non-Traditional, Non-Insurance (NTNI) activities
2017	<ul style="list-style-type: none">• Creation of Systemic Risk Assessment Task Force

Project mandate and timeline

Project plan

- Developing an approach to assess and mitigate systemic risk in the insurance sector through an activities-based approach (ABA);
- Addressing cross-sectoral aspects in systemic risk assessment; and
- Revising the G-SIIs Assessment Methodology.

Timeline

- This interim consultation paper has the purpose to get early stakeholders' feed back on the direction of IAIS work and does not include conclusive proposals
- Final consultation expected by end 2018
- Project is to be finalised by end 2019 and implemented in 2020

ABA concept

- Approach to mitigate systemic risk through broadly applicable policy measures addressing potential systemically risky activities across institutions
- It potentially includes insurance, reinsurance and non-insurance activities
- The focus is on risk exposures, transmission channels and potential systemic impact

Comparison ABA and EBA

The table provides a brief comparison of the different approaches in assessing and mitigating systemic risk:

	Entity- based Approach	Activities-based Approach
Type of assessment	Assessment of impact of failure of single institution. The focal point is the failed institution and the repercussion that failure could have on the financial sector and eventually on the real economy.	Includes assessment of impact of many failures, sector-wide distress and synchronised responses. The failure of an institution is not a prerequisite. The focal point is the activity or exposure that can lead to negative externalities to the financial sector and the real economy, independent of the failure of a single institution.
Type of impact	The failure of an institution causes shocks to propagate to broader financial system.	Common exposure causes correlated actions that creates externalities
Scope of application of policy measures	Additional policies specifically apply to companies that are identified as systemic.	In principle, any policies related to mitigate systemic risk stemming from a particular activity, are independent of the institution undertaking the respective activity. Restrictions may apply, for instance due to proportionality and de minimis considerations.

Conceptual approach to develop ABA Policy Measures

Four-step process

- **Step 1:** Identification of activities that insurers engage in that could potentially threaten global financial stability
- **Step 2:** Evaluation of the existing IAIS policy measures that may help mitigate the potential systemic risk stemming from the identified activities
- **Step 3:** Its purpose is to identify risks associated with an activity that are not sufficiently mitigated by any existing policy measure. This involves a gap analysis, which looks to determine whether there are any insufficiencies in the relevant supervisory tools.
- **Step 4:** subject to findings in previous steps, development of new or enhancement of existing policy measures to address any residual systemic risk. It also covers scope of application and proportionality considerations.

Identification of activities (Step 1)

- The IAIS proposes to define the activities in terms of the risk exposures associated with them rather than in terms of their legal form. This allows:
 - **capturing the sources** of potential systemic risk associated with the activity, considering as far as possible the interaction between assets and liabilities (systemic assessment is not binary)
 - **recognising risk mitigating** practices, and
 - **reducing** the potential for regulatory **arbitrage** driven by classification differences.
- Work is still on going. At this stage, the following main exposures have been focussed on:
 - **Liquidity risk**
 - **Macroeconomic risk**
- In addition, the IAIS is also **investigating** the systemic relevance of **other aspects** that go beyond or are not directly linked to the two aforementioned risk exposures.

Those risks will be assessed against **existing mitigants in IAIS's suite of supervisory materials** (including those that have mainly a micro purpose)

Gap analysis (Step 2 and 3)

Identification of (residual) risks associated with an activity that are not sufficiently mitigated by any existing policy measure.

- This gap analysis includes a comparison of the systemic vulnerabilities against the policy measures the IAIS already has in its toolkit
- Other international standards, specifically those related to the capital market (e.g. FSB's over the counter (OTC) derivatives market reforms) will be considered as well in the analysis.
- Any **material remaining gap**, after this assessment, is an **indication** that the existing IAIS or international framework may **need** some **refinement or integration** to address the residual risk in an ABA perspective.

Specific national requirements are not part of the gap assessment, but they become **relevant at the stage of the design and implementation** of standards.

Potential policy measures (Step 4)

1. The gap analysis determines the need for any new or amended policy measures and will be an important part of the IAIS work over the following months.
2. Any such measure needs to be proportional.

Hence:

- the application of policy measures may vary across firms and may be subject to individual circumstances and
- not all companies would be affected by those policy measures. Companies may be excluded because
 - 1) they do not undertake activities that expose them to the noted risk exposures, or
 - 2) they are deemed too small and the imposition of the policy would not be practicable or beneficial for financial stability purposes.