IAIS Major Projects Update

Macroprudential Committee

Alberto Corinti, Chair of the Macroprudential Committee
IAIS Annual Conference
8-9 November 2018, Luxembourg
Overview of work of the MPC

Systemic Risk Workplan:

• the development of a holistic systemic risk framework

Ongoing macroprudential monitoring and assessment:

• Annual G-SII Assessment Exercise
• Macropudential surveillance
In February 2017, the IAIS announced a work plan to develop a holistic framework for assessing and mitigating systemic risk in the insurance sector at the global level, including three work streams:

- Development of an Activities-Based Approach to mitigate systemic risk in insurance through the identification, and (further) development as needed, of relevant macroprudential policy measures
- Addressing cross-sectoral aspects in systemic risk assessment
- Revising the Entities-Based Approach, namely the Global Systemically Important Insurers (G-SII) assessment methodology

In December 2017, the IAIS launched an interim consultation, focusing on the first work stream only.

In November, the IAIS will launch a next consultation document, which will bring all these strands of work together and propose a holistic framework.
Holistic Framework

Key characteristics (1)

• With the holistic framework, the IAIS proposes to evolve its current approach to systemic risk, by:
  o Taking into account both the EBA and the ABA, the first focusing on the propagation of risk through the failure or distress of an individual insurer, the second stemming from collective risk exposures or activities
  o Addressing cross-sectoral aspects of systemic risk, by comparing the potential systemic risk of insurers with other parts of the financial system, notably the banking sector
  o Introducing a proportionate application of an enhanced set of policy measures for macroprudential purposes, targeted to a broader portion of the insurance sector
Holistic Framework

Key characteristics (2)

• Aim of the framework is to be able to prevent systemic risk from materialising, identify the build-up of potential systemic risks and, lastly, to mitigate these risks should they materialise anyway.

• Some of the key elements of the holistic framework are:
  - An enhanced set of supervisory policy measures for macroprudential purposes
  - A global monitoring exercise by the IAIS designed to detect the possible build-up of systemic risk in the global insurance sector
  - Where a potential systemic risk is detected, supervisory powers of intervention that enable a prompt and appropriate response
  - Implementation assessment and mechanisms to help ensure the global consistent application of the framework
## Sources of systemic risk

<table>
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<tr>
<th>WITHIN INSURANCE SECTOR</th>
<th>ILLUSTRATIVE EXAMPLES</th>
<th>TO FINANCIAL MARKETS AND REAL ECONOMY</th>
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<tr>
<td>EXPOSURES</td>
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<td>LIQUIDITY RISK</td>
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<td>ASSET LIQUIDATION</td>
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<td></td>
<td>• Derivatives</td>
<td>• Exacerbating market movements</td>
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<td>• Securities lending</td>
<td>• Contributing to asset price volatility</td>
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<td>• Embedded options in insurance products (early surrender)</td>
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<td>MACRO ECONOMIC EXPOSURE</td>
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<td>EXPOSURE CHANNEL</td>
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<td>• Certain types of fixed benefit guarantees</td>
<td>• Transferring losses to other market participants</td>
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<td>• Selling credit protection or other speculative derivatives</td>
<td>• Constraining funding or liquidity to financial institutions</td>
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<td>COUNTERPARTY EXPOSURE</td>
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<td>CRITICAL FUNCTION</td>
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<td>• Concentration in asset holdings</td>
<td>• Interruption of insurance services to real economy or financial institutions</td>
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<td>• Providing funding to and lending from other (financial) institutions</td>
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<td>• Assets and liabilities from reinsurance contracts</td>
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<td>SUBSTITUTABILITY</td>
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<td></td>
<td>• Marine and aviation insurance</td>
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<td>• Export credit insurance</td>
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<td>• Mortgage insurance</td>
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<tr>
<td>OTHER</td>
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<td></td>
<td>• Operational risk (e.g. cyber risk)</td>
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<td>• Wide-spread under-reserving without the possibility to re-price</td>
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**ILLUSTRATIVE EXAMPLES**

- Derivatives
- Securities lending
- Embedded options in insurance products (early surrender)
- Certain types of fixed benefit guarantees
- Selling credit protection or other speculative derivatives
- Concentration in asset holdings
- Providing funding to and lending from other (financial) institutions
- Assets and liabilities from reinsurance contracts
- Marine and aviation insurance
- Export credit insurance
- Mortgage insurance
- Operational risk (e.g. cyber risk)
- Wide-spread under-reserving without the possibility to re-price
The policy measures are grouped into two categories:
- On-going supervisory policy measures:
  - Macroprudential surveillance by supervisors;
  - Requirements on insurers; and
  - Crisis management and planning.
- Powers of intervention for supervisors.

Some of the policy measures will be explicitly targeted at a certain identified potential systemic risk, other will have a broader application to assess and/or mitigate potential systemic risks.

The policy measures will be integrated in the IAIS supervisory and supporting material (ICPs, ComFrame, Application Papers)
The global monitoring exercise is a central element of the holistic framework. It consists of:

- An annual data collection from individual insurers building on the current G-SII collection template but based on an updated Assessment Methodology
- A less granular data collection from supervisors that supports the annual assessment of sector-wide trends with regard to specific activities and exposures
- Data analysis by the IAIS to assess any potential systemic risk stemming from a sector-wide or individual insurer level, taking into account general financial market developments
Implementation Assessment

• Robust implementation assessment can be seen as the final step in a mutually reinforcing cycle of activities that consists of monitoring, standard setting and implementation assessment.

• A transparent process of implementation assessment will thus help ensure a globally consistent application of macroprudential policy measures.

• In practice, these activities will build on existing implementation assessment methods for international supervisory material such as the IAIS Peer Review Process (successor of the Self-Assessment and Peer Review).
## Next steps and timeline

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<th>Milestones / activities</th>
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| **November 2018** | • Publication of consultation document on the holistic framework  
                        • Public Background session – via Teleconference                                      |
| **January 2019** | Feedback on consultation document due                                                  |
| **June 2019**   | • Publication of resolution of comments on Section 3 of the November 2018 consultation; and  
                        • Publication of consultation document on further revised ICPs/ComFrame             |
| **November 2019** | Publication of resolution of comments on the complete November 2018 consultation  
                       Adoption by the Annual General Meeting of:  
                        • Holistic framework; and  
                        • Revised ICPs and ComFrame                                                   |
| **2020**        | • Revised systemic risk assessment methodology to be applied; and  
                        • Implementation of revised ICPs and ComFrame                                    |
| **November 2022** | Review of the holistic framework                                                      |