



**IAIS** 25  
YEARS

INTERNATIONAL ASSOCIATION OF  
INSURANCE SUPERVISORS

Public

# **Holistic Framework for Systemic Risk in the Insurance Sector**

**November 2019**

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## About the IAIS

The International Association of Insurance Supervisors (IAIS) is a voluntary membership organisation of insurance supervisors and regulators from more than 200 jurisdictions. The mission of the IAIS is to promote effective and globally consistent supervision of the insurance industry in order to develop and maintain fair, safe and stable insurance markets for the benefit and protection of policyholders and to contribute to global financial stability.

Established in 1994, the IAIS is the international standard setting body responsible for developing principles, standards and other supporting material for the supervision of the insurance sector and assisting in their implementation. The IAIS also provides a forum for Members to share their experiences and understanding of insurance supervision and insurance markets.

The IAIS coordinates its work with other international financial policymakers and associations of supervisors or regulators, and assists in shaping financial systems globally. In particular, the IAIS is a member of the Financial Stability Board (FSB), member of the Standards Advisory Council of the International Accounting Standards Board (IASB), and partner in the Access to Insurance Initiative (A2ii). In recognition of its collective expertise, the IAIS also is routinely called upon by the G20 leaders and other international standard setting bodies for input on insurance issues as well as on issues related to the regulation and supervision of the global financial sector.

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## Executive summary

1. To support its mission of effective and globally consistent supervision to protect policyholders and to contribute to global financial stability, the IAIS adopted in November 2019 the holistic framework for the assessment and mitigation of systemic risk in the global insurance sector (“holistic framework”). The key elements of the holistic framework are:

### Supervisory material:

2. An enhanced set of supervisory policy measures for macroprudential purposes, designed to increase the overall resilience of the insurance sector and help prevent insurance sector vulnerabilities and exposures from developing into systemic risk, through on-going supervisory requirements applied to insurers, enhanced macroprudential supervision and crisis management and planning; and

3. Where a potential systemic risk is detected, supervisory powers of intervention that enable a prompt and appropriate response. Supervisors are required to have at their disposal a sufficiently broad set of preventive and corrective measures to be able to respond appropriately based on the nature of the macroprudential concern.

### Global monitoring exercise:

4. A global monitoring exercise by the IAIS designed to assess global insurance market trends and developments and detect the possible build-up of systemic risk in the global insurance sector. This includes an annual assessment by the IAIS of potential systemic risk arising from sector-wide trends with regard to specific activities and exposures, but also the possible concentration of systemic risks at an individual insurer level (using an updated assessment methodology) arising from these activities and exposures; and

5. Mechanisms to allow for a collective assessment of potential global systemic risk and a coordinated supervisory response when needed. Recognising that the application of supervisory policy measures is ultimately the responsibility of the supervisor, these mechanisms are designed to help increase awareness and understanding of potential global systemic risk and ensure a more consistent response to such risk. This involves, at an individual insurer and sector-wide level:

- A collective discussion at IAIS level on the assessment of potential systemic risks and appropriate supervisory responses; and
- Reporting to the Financial Stability Board (FSB) on the outcomes of the global monitoring exercise, including the IAIS assessment of global systemic risk and the supervisory response to identified risks (if any).

### Implementation assessment:

6. An assessment by the IAIS of the consistent implementation of enhanced on-going supervisory policy measures and powers of intervention.

7. While each key element represents an essential building block in itself, the overall effectiveness of the holistic framework will depend on an integrated approach. As highlighted in the IAIS 2020-2024 Strategic Plan<sup>1</sup>, these core functions reflect a mutually reinforcing cycle of activities in support of the IAIS Mission – starting with the monitoring of global insurance market trends and developments, collective discussion on an appropriate response to the

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<sup>1</sup> See <https://www.iaisweb.org/page/about-the-iais/strategic-plan/>

potential build-up of global systemic risk, through to the assessment of, and support for, implementation of these standards and good supervisory practices. Lastly, the outcomes of the assessment of implementation are expected to feed back into the global monitoring and collective discussion and, where necessary, standard setting and supervisory practices work.

8. The comprehensive and consistent implementation of the holistic framework will support an effective approach to the assessment and mitigation of systemic risk in the global insurance sector, and hence remove the need for an (annual) global systemically important insurers (G-SII) identification by the FSB and national authorities.

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## Acronyms

<b>BCBS</b>	Basel Committee on Banking Supervision
<b>BIS</b>	Bank for International Settlements
<b>ComFrame</b>	Common Framework for the Supervision of IAIGs
<b>ERM</b>	Enterprise Risk Management
<b>FSB</b>	Financial Stability Board
<b>GIMAR</b>	Global Insurance Market Report
<b>(G-)SIFI</b>	(Global) Systemically Important Financial Institution
<b>(G-)SII</b>	(Global) Systemically Important Insurer
<b>G20</b>	Group of Twenty
<b>GIMAR</b>	Global Insurance Market Report
<b>IAIG</b>	Internationally Active Insurance Group
<b>IAIS</b>	International Association of Insurance Supervisors
<b>ICP</b>	Insurance Core Principle
<b>IIM</b>	Individual Insurer Monitoring
<b>ORSA</b>	Own Risk and Solvency Assessment
<b>RCAP</b>	Regulatory Consistency Assessment Programme
<b>SSB</b>	Standard Setting Body
<b>SWM</b>	Sector-wide Monitoring

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## Introduction

9. Following the 2007-2008 global financial crisis, the G20 launched a comprehensive programme of financial reforms to increase the resilience of the global financial system. The IAIS has contributed to these post-crisis reforms including by participating in a global initiative to address systemic risk in the financial sector, under the purview of the FSB and G20. Part of this initiative is the identification of, and setting supervisory policy measures for, global systemically important financial institutions (G-SIFIs): institutions whose distress or disorderly failure would cause significant disruption to the global financial system and economic activity. In 2013, the IAIS adopted an assessment methodology to support recommendations on the identification of G-SIFIs and policy measures to apply to these institutions (“G-SII policy measures”).

10. Since 2013, the IAIS approach to assessing and mitigating systemic risk in the insurance sector has evolved, recognising that systemic risk may arise not only from the distress or disorderly failure of individual insurers but also from the collective exposures of insurers at a sector-wide level.<sup>2</sup> The holistic framework, set out in this document, is an integrated set of key elements aimed at assessing and mitigating both of these potential sources of systemic risk. The IAIS adopted the holistic framework for systemic risk in November 2019, to take effect from 2020.

11. Throughout the development of the holistic framework, since early 2017, the IAIS benefited from cross-sectoral work undertaken in conjunction with the Basel Committee on Banking Supervision (BCBS). Stakeholders have also provided valuable inputs, including via three public consultations as well as via various stakeholder events. This document builds on these previous consultations.<sup>3</sup>

12. The purpose of this document is to set out the holistic framework and its key elements and provide references to other relevant IAIS material. These relevant materials, that constitute the holistic framework, are available on the IAIS website and include:

- as adopted by the IAIS Annual General Meeting:
  - this document, describing the holistic framework in an overarching manner; and
  - the Insurance Core Principles (ICPs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame), setting out the supervisory policy measures and powers of intervention.
- as approved by the IAIS Executive Committee:
  - the global monitoring exercise, describing in more detail its objectives and process; and
  - Application Papers providing supporting material for:<sup>4</sup>
    - Liquidity Risk Management; and

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<sup>2</sup> The term “insurer” includes insurance legal entities, insurance groups and insurance-led financial conglomerates. “Insurance business” refers to the business of insurers and reinsurers, including captives.

<sup>3</sup> The three consultation documents related to the development of the holistic framework, can be found here: <https://www.iaisweb.org/page/consultations/closed-consultations>

<sup>4</sup> The Application Papers are at the moment of publication still in development and are expected to be presented for adoption in 2020 and 2021. The IAIS may decide to develop other supporting material at a later stage.

- Macroprudential Supervision.

13. The structure of this document is as follows:

- Section 1 provides a description of the sources of systemic risk;
- Section 2 provides a description of the supervisory material related to the holistic framework, as contained in the ICPs and ComFrame;
- Section 3 describes the IAIS global monitoring exercise, which includes individual insurer and sector-wide monitoring; and
- Section 4 outlines of the IAIS implementation assessment activities, aimed at ensuring a globally consistent application of the supervisory material.

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## 1 Sources of systemic risk

15. This section summarises the IAIS' view on what are the potential sources of systemic risk relevant for the insurance sector. This summary is intended to provide the context for the holistic framework and its key elements as described in Sections 2 to 4. For more detail, see the global monitoring exercise document as well as previous IAIS publications.<sup>5</sup> This section takes a broad perspective by looking at both how insurers may be vulnerable to systemic risks, as well as how the common activities of insurers, or a distress or disorderly default of a single insurer, might be the source of, or exacerbate, financial instability. While the focus is on potential risks, it is important to emphasise that the insurance business model inherently contributes to financial stability, including by providing long-term sources of funding to other institutions and by promoting risk management through the pooling and diversification of risk.

### 1.1 Concepts

16. Systemic risk, as defined by the International Monetary Fund (IMF), Bank for International Settlements (BIS) and FSB in 2009,<sup>6</sup> refers to a risk of disruption to financial services that is caused by an impairment of all or parts of the financial system and has the potential to have serious negative consequences for the real economy. Fundamental to this definition is the notion of negative externalities from a disruption or failure of a financial institution, market or instrument.

17. Systemic risk may stem from either an individual financial institution or a group of institutions. Related to the former is the concept of systemically important financial institutions (SIFIs), whose distress or failure, because of the size, complexity, lack of substitutability and interconnectedness, could cause or amplify significant disruption to the wider financial system and real economy. In contrast, when examining systemic risk stemming from a group of institutions, the focus is on collective actions or distress of institutions that operate in the same markets or are active in the same financial instruments, and thus are jointly exposed to certain risks. It is based on an assessment across firms of the risk transmission of activities that either in themselves or as a result of common behaviours of firms cause significant disruption to the wider financial system and economic activity.

18. As also acknowledged in the 2009 IMF, BIS and FSB report, the assessment of systemic risk is likely to be time-varying depending on, for instance, the economic environment, the financial infrastructure and crisis management arrangements. While some components of the financial system, such as the banking sector, may be consistently assessed as highly systemic, the significance of other sectors like the insurance sector may vary depending on a number of factors, including the state of the overall economy, the relative size of the activities or the overall resilience of financial markets.

19. Of equal importance is the cross-sectoral dimension of systemic risk. The assessment of systemic risk in the insurance sector would be incomplete if undertaken in isolation. Insurers are an integral part of the financial system, and hence need to be assessed in this broader

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<sup>5</sup> For previous related publications of the IAIS, including the November 2018 Consultation Document on the Holistic Framework, see <https://www.iaisweb.org/page/supervisory-material/financial-stability/archive> and <https://www.iaisweb.org/page/consultations/closed-consultations>.

<sup>6</sup> See IMF, BIS, FSB (2009): *Guidance to Assess the Systemic Importance of Financial Institutions, Markets and Instruments: Initial Considerations Report to the G-20 Finance Ministers and Central Bank Governors*. <https://www.imf.org/external/np/g20/pdf/100109.pdf>

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context. A cross-sectoral view helps to bring conclusions drawn on systemic risk in the insurance sector into perspective, proportionate to the actual risk.

20. The IAIS approach aims to be holistic by taking into account both systemic risk stemming from individual insurers and from collective exposures or activities while acknowledging its time-varying nature and considering cross-sectoral aspects.

## 1.2 Key potential systemic exposures

21. The IAIS has identified the following key exposures in the insurance sector that may lead to a systemic impact:

### Liquidity risk:

22. Liquidity risk is defined as the risk that an insurer is unable to realise its investments and other assets in a timely manner in order to meet its financial obligations, including collateral needs, as they fall due.

23. Insurers may be more or less vulnerable to liquidity risk, depending particularly on the activities in which they are engaged. For instance, liquidity risk may be lower for certain general insurers that can rely on rather stable cash flows from premiums. Liquidity risk vulnerability may increase for instance through securities lending, derivatives, or backing liquid liabilities with illiquid assets.

### Interconnectedness:

24. Interconnectedness refers to interlinkages with other parts of the financial system and the real economy, of which two types can be identified:

- **Macroeconomic exposure:** exposure of an insurer or the insurance sector as a whole to macroeconomic risk factors, resulting in their financial position being highly correlated with the broader financial markets and real economy and with each other, thereby limiting the potential to diversify through the pooling of idiosyncratic risks. Macroeconomic exposure can accumulate through some types of insurance liabilities or may be created through non-insurance activities.
- **Counterparty exposure:** mutual exposure of an individual insurer to counterparties in the broader financial system and real economy resulting from asset-side interconnectedness and liability-side exposures, which leads to both parties being vulnerable to distress or failure of the other.

25. While interconnectedness makes insurers more vulnerable to non-insurance related shocks, it may also cause an initial shock to an insurer to spread to other financial sector participants or markets. The systemic impact of such transmission of losses will depend on the overall state of the financial cycle and the extent to which other counterparties also have diminished capacity to bear losses. Also, when financial markets are already under stress, liquidity will be reduced.

### Limited substitutability:

26. This refers to the difficulty for other components in the financial system to ensure the continuation of supply of insurance coverage after a failure or distress of an individual insurer. However, the category can also apply to groups of insurers that perform a specialised function. 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

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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.

27. The exposures described here are analogous to those described in previous systemic risk publications by the IAIS. There is a range of other risks that cannot easily be classified but that may have a systemic impact. The IAIS will continue to monitor these types of risks. Given the time-varying and fluid nature of systemic risk, there may be current trends whose potential systemic risk have yet to be fully assessed as well as new risks that may emerge in the future. Examples of potential emerging risks that deserve further investigation before concrete systemic risk scenarios can be identified include cyber risk, wide-spread under-reserving without the possibility to re-price the risk, and climate risk.

28. It should be noted that size and global activity are not separately mentioned as a source of risk. However, this does not mean that these factors are irrelevant in the determination of systemic risk in the insurance sector. In fact, they may work as risk amplifiers.

### 1.3 Transmission channels

29. For the above mentioned exposures within the insurance sector to have a wider systemic impact on the financial system, they must propagate to other market participants or the real economy. The IAIS identified as the main transmission channels: asset liquidation, exposure channel and critical functions. Potential systemic risk may propagate simultaneously through more than one of these channels. Even if certain transmission channels dominate for a particular vulnerability (eg asset liquidation for liquidity risk), they are not mutually exclusive and could work as an exacerbating factor to one another.

#### Asset liquidation:

30. Asset liquidation refers to the sudden sale of assets on a large scale, by a large insurer or a sufficiently large number of smaller insurers, which could trigger a decrease in asset prices and significantly disrupt trading or funding in key financial markets or cause significant losses or funding problems for other firms with similar holdings. Such behaviour may have a more significant impact for smaller, less liquid markets or in a stressed environment.

#### Exposure channel:

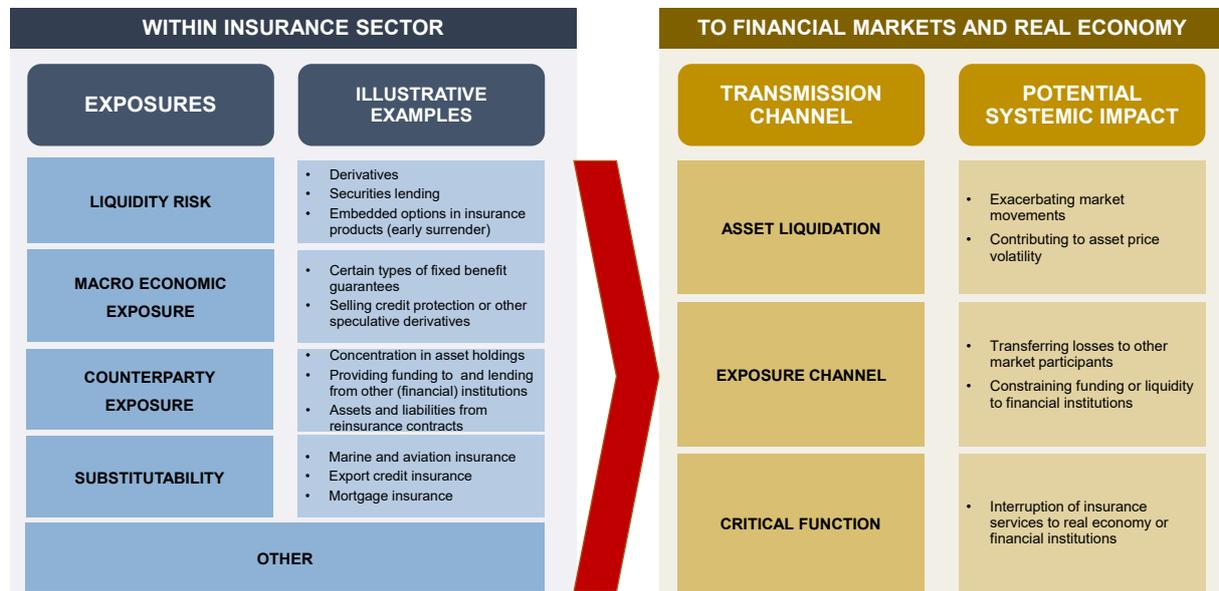
31. The exposure channel includes the following two elements:

- Indirect exposure stemming from macroeconomic exposures, because institutions are exposed to the same or similar asset classes or because their exposures are highly correlated with the financial market; and
- Direct exposure, in case of direct interlinkages between institutions. Distress at the level of an individual insurer may then propagate through transferring directly or indirectly losses to the rest of the financial system.

#### Critical functions:

32. Interruption of services of an individual insurer may have a systemic impact if two conditions are met: first, the insurer provides services that are important for the functioning of the financial sector and real economy and, second, there are few, if any, readily available substitutes (ie an insurer has a large market share or even a monopoly). To the extent insurers

fulfil a critical function, lack of substitutability of individual insurers may become an issue in certain markets that are considered to be significant and highly concentrated, such as catastrophe coverage, marine, aviation, export credit or mortgage guarantee. Another factor that influences this channel is the extent to which there are barriers to entry.



**Figure 1: Simplified illustration of the systemic risk transmission mechanism**

33. Figure 1 provides a schematic illustration of how systemic risk may materialise, by looking both at the relevant exposures (left-hand, blue part of the diagram) and at how this may propagate to the rest of the financial system (right-hand, amber part of the diagram). The exposure to one or more vulnerabilities may generate externalities which may propagate through the transmission channels, triggering systemic events as illustrated in the last column of the diagram. For instance, liquidity risk may become a systemic concern if the sudden liquidation of assets happens on a scale that exacerbates market movements and contributes to asset price volatility. Similarly, macroeconomic exposure can turn into a systemic concern if holdings of highly correlated exposures result in similar reactions by insurers (and/or policyholders). Counterparty exposure may lead to direct losses and facilitate the propagation of risks across different market players. Lastly, the failure of an insurer with a large market share in a critical niche market may become a systemic concern if this leads to financial problems for its counterparties, especially if these counterparties are critical financial market participants themselves.

34. The illustrative examples in Figure 1 of activities do not necessarily, on their own, represent systemic concerns. The actual exposure to the mentioned vulnerability depends on how such an activity is managed. The exposure could become a systemic concern only under certain circumstances, for instance depending on the overall state of the financial markets or the manner in which the activity is conducted by an insurer.

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## 2 Supervisory material

### 2.1 Introduction

35. The IAIS supervisory material (ICPs and ComFrame) as a whole aims to protect policyholders and to contribute to global financial stability through the maintenance of consistently high supervisory standards in IAIS Member jurisdictions. The ICPs apply to insurance supervision of all insurers, whereas ComFrame applies to Internationally Active Insurance Groups (IAIGs) only. As indicated in the Introduction to the ICPs: “a sound supervisory system is necessary for the protection of policyholders and promoting the stability of the financial system and should address the broad set of risks within, and posed by, the insurance sector. The IAIS has designed the ICPs as a comprehensive and holistic framework, with each ICP being integral in the creation of a sound supervisory system.”

36. In developing the holistic framework, the IAIS performed a gap analysis of the existing supervisory material that may, in particular, help mitigate potential systemic risk or that provide the necessary foundation for the holistic framework, irrespective of whether those materials are predominantly designed for microprudential purposes. Such material includes for instance a Standard in ICP 1 (Objectives, Powers and Responsibilities of the Supervisor) requiring that primary legislation clearly determines the objectives of insurance supervision to include contributing to financial stability, as well as various Standards in ICP 8 (Risk Management and Internal Controls) that set out the requirements for an effective and documented risk management system.

37. In addition to the existing supervisory material, as part of the holistic framework, the IAIS revised a number of ICPs and ComFrame material integrated therein by enhancing or adding supervisory policy measures specifically designed to assess and mitigate potential systemic risk building up in the insurance sector. The measures are expected to be applied to a broader portion of the insurance sector, in a proportionate manner. A globally consistent implementation by supervisors should contribute to the stability of the global financial system.

38. For the purpose of the holistic framework, the following thematic areas can be identified:

- On-going supervisory policy measures:
  - Macroprudential supervision;
  - Requirements on insurers; and
  - Crisis management and planning.
- Powers of intervention for supervisors.

The enhanced and additional supervisory policy measures are contained in the IAIS supervisory material as Standards<sup>7</sup> (requirements) and Guidance<sup>8</sup> (recommendations and examples). These are further described in Sections 2.2 – 2.5.

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<sup>7</sup> Standards set out key high-level requirements that are fundamental to the implementation of the Principle Statement and should be met for a jurisdiction to demonstrate observance with the particular Principle Statement.

<sup>8</sup> Guidance facilitates the understanding and application of the Principle Statement and/or Standards; it does not represent any requirements.

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### **2.1.1 Scope of application**

39. With the holistic framework, there is a move away from the previous binary approach, which saw a set of pre-determined policy measures applied only to a small group of identified G-SIIs, toward a proportionate application of an enhanced set of policy measures to a broader portion of the insurance sector. Therefore, the material contained in the ICPs and ComFrame has a broader application.

40. The exact scope of application varies. Some material is contained in the ICPs, which are applicable to the supervision of all insurance legal entities and groups, including IAIGs. Other material is contained in ComFrame, which applies only to the supervision of IAIGs. Also, there are some Standards (or a part thereof) that the supervisor is required to apply beyond IAIGs to other insurers “as necessary”, based on the nature, scale and complexity of the insurer’s activities that may lead to increased systemic risk exposure, which in most jurisdictions will only be a subset of the insurance sector. This is to reflect the view that the criteria for being an IAIG (ie size and international activity) may work as a risk amplifier but does not necessarily correspond to whether an insurer is engaged in potential systemic activities or is exposed to certain systemic risks.

### **2.1.2 Proportionality**

41. As described in the Introduction to the ICPs and ComFrame, the principle of proportionality underlies all ICPs and ComFrame material, including those related to the holistic framework. Supervisors have the flexibility to tailor the implementation of supervisory requirements and the application of insurance supervision, as appropriate, to achieve the outcomes stipulated in the Principle Statements and Standards.

42. In terms of implementation, proportionality allows the ICPs to be translated into a jurisdiction’s supervisory framework in a manner appropriate to its legal structure, market conditions and consumers. In terms of application, proportionality allows the supervisor to increase or decrease the intensity of supervision according to the risks inherent to insurers, and the risks posed by insurers to policyholders, the insurance sector or the financial system as a whole.

43. ComFrame itself is an exercise of proportionality in that ComFrame standards are tailored to reflect the nature, scale and complexity of IAIGs. In some cases, this results in IAIGs needing to meet higher standards than other insurers, where the supervision of those insurers is subject only to the ICPs.

Thematic area	High-level description	Location	Scope of application	
			Legal entity / Group	IAIG
Macroprudential supervision	Enhance the link of macroprudential supervision to supervisory review and reporting	Guidance material in ICP 9.1 and 9.2 (Supervisory Review and Reporting) and ComFrame integrated therein	●	●
	Requirements on Macroprudential Supervision	ICP 24 (Macroprudential Supervision)	●	●
Requirements on insurers	Enterprise Risk Management requirements related to: <ul style="list-style-type: none"> <li>• Liquidity risk;</li> <li>• Counterparty exposures; and</li> <li>• Macroeconomic exposure.</li> </ul>	Various Standards and Guidance in ICP 16 (Enterprise Risk Management for Solvency Purposes) and ComFrame integrated therein	○	●
	Public disclosure requirement for liquidity risk	ICP 20.11 (Public Disclosure)	●	●
Crisis management and planning	Coordination of crisis management preparations	ICP 25.7 (Supervisory Cooperation and Coordination) and ComFrame integrated therein	●	●
	including the establishment of crisis management groups			●
	Requirement on recovery planning	ICP 16.15 (Enterprise Risk Management for Solvency Purposes) and ComFrame integrated therein	○	●
	Resolution framework including resolution powers	ICP 12 (Exit from the Market and Resolution) and ComFrame integrated therein	●	●
	Requirement on resolution planning			○
Powers of intervention	Preventive and corrective measures	ICP 10.2 and 10.3 (Preventive Measures, Corrective Measures and Sanctions) and ComFrame integrated therein	○	○

[ ] Not applicable; [○] Applicable / required as necessary only; [●] Applicable / required.

**Table 1 Mapping of Enhanced / additional supervisory material to ICPs and ComFrame**

## 2.2 Macroprudential supervision

44. ICP 9 (Supervisory Review and Reporting) and ComFrame integrated therein sets requirements for the general processes and procedures for supervisors to have in place with respect to supervisory review and reporting. The revised ICP makes explicit that this should include assessments of not only the risks to which insurers are exposed but also the risks which insurers may pose to policyholders, the insurance sector and financial stability, thereby

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referring to risks from both individual insurer failure and the risks stemming from common exposures or activities.

45. ICP 24 (Macroprudential Supervision) deals with the processes and procedures supervisors should have with respect to macroprudential supervision. As stated in its Principle Statement, it requires that “the supervisor identifies, monitors and analyses market and financial developments and other environmental factors that may impact insurers and the insurance sector, uses this information to identify vulnerabilities and address, where necessary, the build-up and transmission of systemic risk at an individual insurer and at the sector-wide level.”

46. ICP 24 details that macroprudential analysis is required to be both quantitative and qualitative, to consider both historical trends and the current risk environment and both inward and outward risks. As part of this, the supervisor should have in place an appropriate form of stress testing, which is applied to the insurance sector as a whole or to a significant sub-sample of insurers, selected according to their exposure to the specific risks to be assessed. Also, supervisors are required to have an established process to assess the potential systemic importance of individual insurers and the insurance sector as a whole.

47. In order to support supervisors in the implementation of ICP 24, the IAIS will develop an Application Paper on Macroprudential Supervision, with adoption scheduled for 2021.

### **2.3 Requirements on insurers**

48. The requirements on insurers are targeted at mitigating the risk exposures described in Section 1: liquidity risk, counterparty exposure and macroeconomic exposure. While these requirements are essentially microprudential in nature, by mitigating certain risk exposures, these also help increase the resilience of the insurance sector as a whole and/or decrease the probability and magnitude of a negative systemic impact when a risk does materialise.

49. ICP 16 (Enterprise Risk Management for Solvency Purposes) and ComFrame integrated therein sets out various requirements on the Enterprise Risk Management (ERM) framework for insurers, including those related to risk identification and measurement, risk appetite statement, asset-liability management, investment, underwriting policies and liquidity risk management, as well as the Own risk and solvency assessment (ORSA). The IAIS enhanced these ERM requirements to explicitly target liquidity risk, macroeconomic exposure and counterparty exposure. The requirements are expected to be applied to IAIGs, and to be extended to other insurers as necessary. Guidance material provides steer for supervisors when making this decision and provides examples on the practical application of the proportionality principle. The IAIS is also developing an Application Paper to provide supervisors with further guidance when implementing the requirements on liquidity risk management and planning, with adoption scheduled for 2020.

50. The requirements include, among others, the following:

- For liquidity risk:
  - The ERM framework to address liquidity risk and to contain strategies, policies and processes to maintain adequate liquidity to meet the insurer’s liabilities as they fall due in normal and stressed conditions;
  - For IAIGs and other insurers as necessary:

- Assessment of the resilience against liquidity stresses, which is recommended to be conducted through stress testing or scenario analysis;
  - Maintenance of a portfolio of unencumbered highly liquid assets;
  - Development of a contingency funding plan; and
  - Submission of a liquidity risk management report to the supervisor;
- For counterparty exposure for IAIGs and other insurers as necessary: a counterparty risk appetite statement and an analysis of stress events on material counterparty exposures through scenario analysis or stress testing;
  - For macroeconomic exposure for IAIGs and other insurers as necessary: stress testing to assess the resilience of an insurer's total balance sheet against macroeconomic stresses.

51. ICP 20 (Public Disclosure) lays out public disclosure requirements for insurers, related to a wide range of items like company profile, governance and financial position. Public disclosure is intended to enhance market discipline. As stated in the Introductory Guidance to ICP 20: "The supervisor's application of disclosure requirements will depend on the nature, scale and complexity of insurers. For example, it may be overly burdensome for a small, private insurer to meet the same requirements developed for large, publicly traded insurers. Additionally, the supervisor may decide not to apply disclosure requirements if there is no potential threat to the financial system, no public interest need for disclosure, and no legitimately interested party is prevented from receiving information. It is expected that such situations would be exceptional."

52. The IAIS added an additional Standard in ICP 20 to cover a requirement for insurers to disclose quantitative and qualitative information on liquidity risk. In addition to enhancing market discipline, liquidity disclosures may help prevent or alleviate a loss of confidence caused by the absence of reliable information

#### **2.4 Crisis management and planning**

53. Crisis management and planning tools are aimed at reducing the likelihood and adverse impact of a disorderly failure. The related IAIS supervisory material incorporates elements of the FSB Key Attributes<sup>9</sup> to the extent that these are relevant to the insurance sector and includes the following:

54. ICP 12 (Exit from the Market and Resolution) and ComFrame integrated therein lays out requirements on the resolution framework for insurers, resolution powers, resolution planning and management information systems. Resolution plans are developed to identify, in advance, options for resolving all or part(s) of an insurer to maximise the likelihood of an orderly resolution. These are required for IAIGs as necessary; and in considering the need for resolution plans, the supervisor and/or resolution authority should take into account the activities, lines of business and number of jurisdictions in which the insurer operates, the complexity of the group structure, and the potential impact of failure of the insurer on financial stability. The IAIS is developing an Application Paper on Resolution Powers and Planning to provide further guidance, with adoption scheduled for 2021.

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<sup>9</sup> See FSB (2014): *Key Attributes for Effective Resolution Regimes for Financial Institutions*. [https://www.fsb.org/wp-content/uploads/r\\_141015.pdf](https://www.fsb.org/wp-content/uploads/r_141015.pdf)

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55. Standard ICP 16.15 and ComFrame CF 16.a/b include requirements for recovery planning to identify in advance options to restore the financial position and viability of an insurer should it come under severe stress, which is applicable to IAIGs and other insurers as necessary. The IAIS has developed an Application Paper to provide more background on recovery planning.<sup>10</sup>

56. ICP 25 (Supervisory Cooperation and Coordination) and ComFrame integrated therein contains a section on crisis management and cooperation, including a requirement to have in place crisis management groups for IAIGs with the objective of enhancing preparedness for, and facilitating the recovery and resolution of, an IAIG.

## **2.5 Powers of intervention for supervisors**

57. The supervisory material described in Sections 2.2 – 2.4 is designed to assess and help prevent insurance sector vulnerabilities and exposures from developing into systemic risk. In case systemic risk does materialise, or there are signs of the build-up of systemic risk, the supervisor should have at its disposal a sufficiently broad set of powers. While ultimately the type of action required will depend on the circumstances and the nature of the concern, the supervisor's powers should allow the supervisor to promptly and effectively address and mitigate the build-up of systemic risk.

58. ICP 10 (Preventive Measures, Corrective Measures and Sanctions) puts forward various measures to address supervisory concerns. The supervisor should be able to apply preventive or corrective measures to either prevent a breach of regulatory requirements or respond to a breach of regulatory requirements.

59. The measures listed in ICP 10 may, subject to the existing supervisory framework and due processes as described in ICP 9 (Supervisory Review and Reporting) and ICP 10, also be applied to address a threat to financial stability.

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<sup>10</sup> See IAIS (2019): *Application Paper on Recovery Planning*.  
<https://www.iaisweb.org/page/supervisory-material/application-papers>

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### 3 Global monitoring exercise

60. As a key element of the holistic framework, the annual global monitoring exercise of the IAIS serves to assess global insurance market trends and developments and to determine any potential build-up of systemic risk at a global level.

61. The global monitoring exercise includes the following elements:

- Sector-wide monitoring (SWM);
- Individual insurer monitoring (IIM);
- Data analysis by the IAIS to assess any potential systemic risk stemming from a sector-wide or individual insurer level, considering also broad financial market developments;
- Collective discussion<sup>11</sup> of the results of the assessment within the IAIS. This discussion has the following key aspects:
  - Assessment of trends and any systemic risks identified at a sector-wide level;
  - Consideration of trends in risks and increasing levels arising from potentially systemic activities and exposures concentrated in an individual insurer, that could ultimately have a global systemic impact in case of its distress or disorderly failure; and
  - Consideration of appropriate supervisory responses, including the enhanced supervisory policy measures and/or powers of intervention, taking into account the assessment of those supervisory policy measures and/or powers of intervention that have already been implemented; and
- Reporting to participating insurers, IAIS Members, the FSB and the public.

62. The global monitoring exercise supports the IAIS in its 2020-2024 Strategic Plan, specifically High Level Goal 1: The IAIS assesses global market trends and developments in or relevant to the insurance sector and responds to issues that present opportunities, challenges and risks relevant to its Mission.

63. The holistic framework also allows for the introduction of a feedback loop between the global monitoring by the IAIS and the enhanced macroprudential monitoring and supervision by supervisors, which is, in part, aimed at monitoring and mitigating systemic risks building up within a jurisdiction (see ICP 24 Macroprudential Supervision). For instance, vulnerabilities building up in certain jurisdictions may have cross-jurisdictional implications. Correspondingly, the interpretation of global trends will benefit from having a better understanding of the underlying trends at the jurisdictional or regional level.

64. The global monitoring exercise document provides more detail on these various aspects.

#### 3.1 Categories

65. The global monitoring exercise monitors the following 10 categories:

- Size;
- Interconnectedness – Counterparty exposure;
- Interconnectedness – Macroeconomic exposure;

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<sup>11</sup> This collective discussion will take place in coordination with the relevant supervisor where an individual insurer is involved.

- Asset liquidation;
- Substitutability;
- Global activity;
- Underwriting & Solvency;
- Policyholder behaviour;
- Emerging risks; and
- Economic environment.

### 3.2 Sector-wide monitoring

66. The SWM is aimed at assessing sector-wide trends with regard to specific activities and exposures and consists of qualitative and quantitative parts. It is a complement to the IIM and both their outcomes feed into the IAIS assessment of systemic risk as well as the IAIS collective discussions. The SWM includes an annual data collection exercise that contains the following elements:

- Information from IAIS Members, based on:
  - Data collection on quantitative data elements, for the 10 categories mentioned above. This part of the SWM relies on aggregated data from insurance legal entities operating in IAIS Member jurisdictions; and
  - A qualitative information request that covers supervisors' assessments of macroprudential risks, in terms of probability, impact and trends; and
- Additional data collection by the IAIS Secretariat based on public sources.

67. The SWM is a voluntary exercise, open to all IAIS Members. However, for the purpose of monitoring global trends, there needs to be sufficient coverage of the global insurance sector. Therefore, at least those IAIS Members whose insurance or broader financial markets play a significant role in the global financial system should participate in the exercise, providing data based on a representative sample of insurers within their jurisdictions.

### 3.3 Individual insurer monitoring

68. The IIM is aimed at assessing systemic risk stemming from an individual insurer's distress or disorderly failure and is based on an assessment methodology developed by the IAIS. With the adoption of the holistic framework, and in line with the agreed three-year cycle of reviewing and updating the Assessment Methodologies, the IAIS adopted an updated 2019 Methodology, which replaced the 2016 Methodology.<sup>12</sup> The 2019 Methodology will first be applied during the 2020 global monitoring exercise.

69. The IIM is facilitated through individual insurer and Insurer Pool assessment of systemic risk, which includes:

- Individual absolute assessment: scores of individual insurers are calculated based on an absolute indicator-based methodology,<sup>13</sup>

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<sup>12</sup> See IAIS (2016): *Updated G-SII Assessment Methodology*.

<https://www.iaisweb.org/page/supervisory-material/financial-stability/archive>

<sup>13</sup> The absolute methodology means that scores are calculated against a fixed benchmark based on the sample total in a defined base year.

- Individual relative assessment: scores of individual insurers are calculated based on a relative indicator-based methodology;<sup>14</sup>
- Cross-sectoral analysis, comparing the systemic footprint of individual insurers and the Insurer Pool with that of banks;
- Trend developments within the Insurance Pool;
- Ancillary indicators, such as liquidity risk metrics;
- Qualitative assessment of individual insurers and the Insurer Pool; and
- Interplays with the SWM, which is further described in Section 3.4.

### 3.4 Data analysis and interplays

70. The global monitoring exercise supports an integrated and forward-looking assessment of the possible build-up of systemic risk in the global insurance sector. This assessment is based on the outcomes of both the SWM and IIM, inputs received from an annual roundtable with risk managers and investors, and, finally, facilitated by a collective discussion at the level of the IAIS.

71. To allow for an integrated view of the possible build-up of systemic risk, the IAIS has created interplays between SWM and IIM by targeting the same risk categories, so that the IAIS can analyse and compare developments and trends at the sector-wide level and also at the level of individual insurers and of the Insurance Pool. The SWM provides a broad overview of trends in the global insurance sector. However, it offers limited information on the source of a risk, for instance whether it is stemming from certain activities or exposures concentrated in a limited number of insurers or if it is a more widespread behaviour across the sector. The IIM can provide insights into the level of concentration of risks or into potential outliers.

72. To further allow for a forward-looking collective discussion on the possible build-up of systemic risk, the analysis goes beyond a single insurer or a small set of insurers whose distress or disorderly failure may pose a significant threat to global financial stability. Instead, the IAIS also considers significant growth in certain activities or markets based on the outcomes of the SWM, or of a specific insurer (or insurers), that shows significant increases or concentrations in potentially systemic activities and exposures.

73. The following criteria are used to assist the IAIS in the determination of the focus of the IIM assessment as one input to the collective discussion:

- Level: to indicate any insurer(s) whose distress or disorderly failure may pose a significant threat to global financial stability, based on the total score of the individual absolute assessment;
- Trends (subject to a materiality criterion): to monitor significant increases in indicator scores and/or total scores of individual insurers; and
- Outliers (subject to a materiality criterion): to highlight sample outliers when comparing developments of sector-wide and/or Insurance Pool aggregates with individual insurers' scores.

The above criteria are complemented by expert judgement, which may be quantitative or qualitative in nature and include IAIS Members' expert knowledge and insights. Applying

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<sup>14</sup> The relative methodology means that scores are calculated based on the sample total of the relevant exercise year.

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this expert judgement and taking into account other inputs, including from the sector-wide monitoring, the IAIS will determine the scope of the collective discussion.

### 3.5 IAIS collective discussion

74. The collective discussion is a platform for IAIS Members to form a collective view on the assessment of systemic risk in the global insurance sector, detect the build-up of systemic risk and discuss appropriate supervisory responses to systemic risk if it arises.

75. To support the discussion, IAIS Members and relevant supervisors<sup>15</sup> will be asked to provide information on their assessment of the identified risk and on the supervisory response to address the build-up of potential systemic risks as identified through the global monitoring exercise, including supervisory policy measures already applied or under consideration. This discussion will be supported by the outcomes of the IAIS' assessment of the implementation of the holistic framework supervisory material.

76. In the event that potentially systemic activities or exposures become concentrated in an individual insurer such that its distress or failure would pose a serious threat to global financial stability, then the discussion becomes more intensive. Also, the focus is not necessarily on exploring and assessing potential risks, but more so on discussing supervisory responses to address the identified risk. The discussion includes an evaluation of which supervisory policy measures and powers of intervention have already been applied to that insurer and whether the group-wide supervisor plans to take any further action.

77. The outcome of the collective discussion is twofold:

- A common IAIS view on the assessment of current and potential future systemic risk in the global insurance sector. Where applicable, this may highlight certain identified risks, which could be at the level of a certain activity, exposure, region or individual insurer.
- Any recommendations for follow-up, which may entail:
  - Recommendations for further analysis at the level of the IAIS, which can be both qualitative and quantitative in nature, to monitor or better understand certain identified trends;
  - Recommendations for developing targeted supervisory or supporting material to help supervisors address specific activities or exposures, or possibly additional supervisory capacity building; and/or
  - Considerations on the application of certain enhanced policy measures or powers of intervention to a specific insurer, while recognising that the application of supervisory policy measures and intervention is ultimately the responsibility of the relevant supervisor itself.

### 3.6 Reporting

78. Outcomes of the global monitoring exercise are shared each year with participants in the global monitoring exercise (participating insurers as well as participating IAIS Members), other IAIS Members, the FSB and the general public.

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<sup>15</sup> In case of insurance groups, the relevant supervisor is the group-wide supervisor.

79. The aim and the level of detail of the reporting is specific to each of the different audience groups.

#### Participating insurers and IAIS Members

80. The IAIS continues to provide all individual participating insurers and their respective group-wide supervisors with insight into how the individual insurer's risk scores relate to the Insurance Pool score and other relevant descriptive statistics.

#### FSB

81. For the FSB, the IAIS reporting feeds into their broader, cross-sectoral assessment of global financial stability. The report to the FSB is comprised of the outcomes of the IAIS collective discussion on the assessment of global systemic risk, the supervisory response, and the outcomes of the SWM and IIM data collection.

#### General public

82. For the general public, the aim of the reporting is to provide insight into the key (systemic) risks and trends in the global insurance sector as assessed by the IAIS, through reporting on the outcomes of the global monitoring exercise. The existing annual Global Insurance Market Report (GIMAR) will be enhanced for this purpose, to not only include a broad overview of the macroeconomic environment and global insurance market developments, but also the IAIS assessment of systemic risk, including disclosures of the outcomes of the SWM and IIM.<sup>16</sup> Additionally, there will be a publication of special topics, covering deep-dives into relevant topics stemming from each year's global monitoring exercise.

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<sup>16</sup> The disclosures on the IIM data collection are similar to those that were in place for the G-SII data collection exercise.

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## 4 Implementation assessment

83. The assessment of consistent implementation of the supervisory material is the final key element of the holistic framework. It is aimed at promoting globally consistent and effective implementation of the relevant supervisory material. This is critical for supporting financial stability – since the potential build-up of systemic risk may be global in nature, so should be the application of policy measures aimed at assessing and mitigating systemic risks. The policy measures are designed to help prevent insurance sector vulnerabilities and exposures from developing into systemic risk in the first place. For this to be effective in practice, it is important that the policy measures are implemented consistently and effectively and applied to a broader portion of the global insurance sector, as described in Section 2.

84. The assessment activities also support the IAIS in its 2020-2024 Strategic Plan, specifically High Level Goal 4: “The IAIS assesses and promotes observance of its supervisory material. As highlighted in the IAIS 2020-2024 Strategic Plan, credible and independent assessment of implementation of the IAIS supervisory material is critically important to supporting effective and globally consistent supervision. Increasing the transparency around implementation gaps and challenges (and whether comparable outcomes are being achieved) is equally important in supporting observance of the supervisory material.”

85. The IAIS’ implementation assessment approach builds on the existing methodology for assessing implementation of ICPs and ComFrame, while taking into account the specific nature of the holistic framework as a subset of ICP and ComFrame material that is relevant to the assessment and mitigation of systemic risk.

### Assessment Focus

86. In line with the IAIS Assessment Methodology for ICPs and ComFrame, the holistic framework implementation assessment determines whether the supervisor has and exercises, when required, the legal authority<sup>17</sup> and supervisory practices to effectively perform and enforce the requirements of the relevant holistic framework supervisory material. Implementation assessments will also assess how the requirements of the holistic framework that should be applied as necessary, and the proportionality principle, are effectively implemented (see Section 2.1.1).

### Jurisdictions Assessed

87. Consistent with the focus of the SWM, the implementation assessment activities prioritise those IAIS Member jurisdictions whose insurance or broader financial markets play a significant role in the global financial system.

### Assessment Approach

88. The implementation assessment of the holistic framework will proceed in phases, beginning with a baseline assessment in 2020 and moving to a more intensive jurisdictional assessments in 2021, which will include peer reviews of the jurisdictional self-assessment and targeted in-depth verification of supervisory practices.

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<sup>17</sup> Legal authority means the supervisor has the power, based in legislation, to perform a particular activity. In the ICPs and ComFrame, the term “legislation” is used to include primary legislation (which generally requires full legislative consent), secondary legislation and legally enforceable rules set by the supervisor.

89. The baseline assessment builds on the current IAIS assessment methodologies, in particular the IAIS' Peer Review Process. IAIS Member jurisdictions participating in the baseline assessment are asked to report on their progress in implementing the holistic framework supervisory material and to share their implementation plans where there are gaps. The baseline assessment will be repeated annually and will be used as the starting point for subsequent in-depth jurisdictional assessments.

90. Jurisdictional assessments will take into account relevant assessments by other Standard Setting Bodies (SSBs), such as the methodology and process developed by the BCBS for its Regulatory Consistency Assessment Programme (RCAP).

#### Transparency

91. The implementation assessment results should be comparable and should facilitate a discussion by the IAIS on consistency, completeness and comprehensiveness of implementation of the holistic framework.

92. The IAIS will publish the operational details of its approach for undertaking the holistic framework implementation assessments, including the assessment handbook and the work plan for the assessments. The IAIS will share the outcomes of the holistic framework implementation assessments with relevant stakeholders, such as the FSB and the general public, taking into consideration the scope and detail of implementation assessment reporting by other SSBs.

#### Feedback loop

93. As with its other implementation assessment activities, the IAIS recognises the value of a strong feedback loop between assessment results and policy development. The IAIS will take into account outcomes of implementation assessments as appropriate when seeking to identify areas that may, over time, require further improvements or refinements.