ACLI
Financial Security...for Life.

February 23, 2018

Financial Stability Board
c/o Bank of International Settlements
CH-4002 Basel
Switzerland

The American Council of Life Insurers ("ACLI")[1] appreciates this opportunity to comment on the Financial Stability Board's ("FSB") Consultation Document entitled *Key Attributes Assessment Methodology for the Insurance Sector* ("2017 Consultation") that was released on December 21, 2017.

The ACLI previously submitted comments to the FSB on two other related Consultation Documents. The first set of comments was submitted on October 15, 2013 in response to the *Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions* dated August 12, 2013. The second set was submitted on October 31, 2013 in response to the *Assessment Methodology for the Key Attributes of Effective Resolution Regimes for Financial Institutions*.

We have the following comments and concerns with the 2017 Consultation, many of which are similar to those we conveyed in 2013:

General Comments:

We strongly recommend that the Key Attributes ("KAs") and its Essential Criteria ("ECs") serve as illustrative guidance, rather than prescriptive standards. Flexible application of the KAs and ECs would: (1) avoid unnecessary changes to the time-tested supervisory and resolution frameworks that exist in many jurisdictions, such as the U.S. state-based insurance supervision and insolvency regimes; and (2) the potential disruption of well-developed insurance markets without commensurate benefits to enhancing financial stability.

We also propose that the KAs and insurance-related ECs ultimately be aligned with the IAIS' Insurance Core Principles ("ICPs") and ComFrame as they relate to the contours of a resolution regime. The ICPs, ComFrame, KAs and ECs should all focus on desired outcomes and broad objectives, not strict compliance with defined requirements, and they must be sufficiently flexible to accommodate multiple jurisdictions' supervisory and resolution frameworks.

[1] The American Council of Life Insurers (ACLI) is a Washington, D.C.-based trade association with 290 member companies operating in the United States and abroad. ACLI advocates in federal, state, and international forums for public policy that supports the industry marketplace and the 75 million American families that rely on life insurers' products for financial and retirement security. ACLI members offer life insurance, annuities, retirement plans, long-term care and disability income insurance, and reinsurance, representing 94 percent of industry assets, 93% of life insurance premiums and 98% of annuity consideration in the United States. Learn more at www.acli.com.

In addition, the resolution regime and its KAs and ECs should be applied on an activities-based approach ("ABA") rather than on an entities-based approach, as an ABA can more effectively identify potential systemic risk than entity-based designations (e.g., G-SIIs, non-G-SIIs). This is consistent with what is being proposed by the IAIS in its consultation document on *Activities-Based Approach to Systemic Risk* dated February 15, 2018.

Moreover, we suggest that the assessment of a jurisdiction's compliance with the KAs and ECs be viewed in the context of: (1) the principles of proportional and risk-based supervision, so that the nature of any required recovery or resolution planning efforts are based on a cost-benefit analysis; and (2) the need for flexible guidance in the areas of recovery and resolution planning is predicated on the fact that actual stress events are inherently unpredictable.

Scope of the Document:

The scope of application of the resolution regime and its KAs to insurers is stated in EC 1.1 as follows: "*The resolution regime covers any insurer that could be systemically significant or critical in the event of failure*".

In addition, there are several KAs and related ECs that specifically apply to global systemically important insurers ("G-SIIs") – KA 8 (Crisis Management Groups), KA 9 (Institution-Specific Cross-Border Cooperation Agreements), KA 10 (Resolvability Assessments) and KA 11 (Recovery and Resolution Planning).

ACLI believes that the resolution regime and its KAs and ECs:

(1) Should not apply to insurers who "could be systemically significant or critical in the event of failure" since such a determination is very subjective and could ensnare many insurers who should not be covered under such a regime; and

(2) Should not distinguish between G-SIIs and non-G-SIIs since resolution measures should not be based solely on the size of an insurer.

Instead, the resolution regime should only apply to those insurers who are currently involved in activities that have been identified as systemically risky, regardless of size, when the ABA is developed. Accordingly, the ACLI urges that the resolution regime and its KAs and ECs only apply to those insurers, regardless of whether or not they have been designated as G-SIIs, who have undertaken, on a material scale, activities that have been identified as those that would pose systemic risk to the global financial markets and/or the global economy in the event of failure.

Furthermore, the resolution regime should only be used as a back-up to a jurisdiction's existing resolution framework upon the determination that an insurer(s) could not be properly resolved under the existing framework without the likelihood of a material risk to the global financial system.

Resolution Tools and Safeguards:

We would encourage greater flexibility with the KAs, with a focus on desired outcomes and broad objectives, rather than strict compliance with defined requirements. Given the nature and design of insurance products and the long-term duration of traditional insurance liabilities, run-offs and portfolio transfers are generally sufficient to deal with the vast majority of insurance failures.

In addition, it must be kept in mind that the various measures and tools that are being proposed for recovery and resolution must comply with domestic and local laws. Unfortunately, some of the KAs go beyond what is currently permissible under the insurance supervisory laws in many jurisdictions, and they may also violate to the principle of proportionality and the protection of ownership rights.

<u>Recovery and Resolution Plans:</u>

The requirement for insurers to develop recovery and resolution plans ("RRPs") is stated in EC 11.1 as follows: "*The resolution regime requires the development and maintenance of RRPs for all G-SIIs for which the jurisdiction is the home country and for any other insurer that could be systemically significant or critical if it fails*".

Consistent with our comments in the Scope section above, ultimately, the requirement for insurers to develop RRPs should only apply to those insurers, regardless of whether or not they have been designated as G-SIIs, who have undertaken, on a material scale, activities that have been identified as those that would pose systemic risk to the global financial markets and/or the global economy in the event of failure.

In addition, the requirement should only be triggered after a clear, identifiable event or condition of financial stress has occurred, such as the breach of a solvency requirement (e.g., insufficient RBC ratio). Given the substantial amount of time and resources that go into preparing RRPs, an otherwise financially sound insurer that is in full compliance with its regulatory requirements should not have to prepare such plans, unless it chooses to do so as part of its own internal risk management process.

Furthermore, resolution plans should be developed by the group-wide supervisor and/or resolution authority and in consultation with the troubled insurer. Host supervisors and/or resolution authorities can develop their own resolution plans for the legal entities within their jurisdictions if there is a clear demonstrable need, while cooperating with the group-wide supervisor and/or resolution authority to ensure that their plans are as consistent as possible with the resolution plan of the insurance group.

Although RRPs, where required, should be reviewed periodically, we do not believe it necessary to prescribe a set, annual timeframe. Consistent with the proportionality principle, supervisory and resolution authorities should have the flexibility to dictate the timing and contents of the RRPs and to determine the necessity of any new management information system requirements, based on the nature, scale, complexity and activities of the insurer.

<u>Bail-In Powers:</u>

EC 3.11 states that a resolution authority has the power to "*write down equity and cancel shares or other instruments of ownership of the insurer*".

In light of the many differences between the banking and insurance business models, there is limited utility for a "bail-in" tool in the insurance context. Given the structure of most insurers' balance sheets, other loss-absorbing funds (e.g., capital, reserves, non-guaranteed components of policies) are more effective and readily-available sources. Unlike banks, which are funded by depositors and other short-term creditors who expect payment on demand, policyholders pay premiums upfront and contractual payments are generally made only if and when an insured event has occurred. This means that the large majority of insurance contract liabilities are not prone to sudden withdrawals. Furthermore, most insurance policies and other products are generally either not subject to surrender or contain surrender charges and tax penalties which create powerful disincentives to surrender or withdraw early.

Bridge Institutions:

KA 3.2(vii), KA 3.4 and EC 3.8 give a resolution authority the power to establish bridge institution in order to "*take over and continue operating certain critical functions and viable operations of a failed firm*". While such institutions may be practical and viable in the case of bank failures, it may not be so in the case of insurer insolvencies. We, therefore, request that specific language be added to those KAs and ECs that state that a resolution authority would not be required to establish bridge institutions in insurer insolvencies.

Power to Restructure Insurance Liabilities:

EC 3.13 states that "*The resolution authority has powers to restructure insurance liabilities (whether currently due and payable or contingent*" and Explanatory Note ("EN") 3 (s) provide several examples.

In the U.S., state receivership laws do not allow receivers to unilaterally restructure or limit the policy liabilities of an insolvent insurer as it could negatively affect policyholders. While some receivership courts may allow for the restructuring of liabilities when blocks of policies are transferred to a solvent insurer, the affected policyholders would have the right to opt-out of the transfer. We, therefore, request that the following be added at the end of EC 3.13 and at the end of the opening phrase of EN 3 (s): "*, to the extent such powers do not conflict with existing law*".

Departure from the Pari Passu Principle:

EC 5.2 allows for the departure of the principle of equal (pari passu) treatment of creditors of the same class when necessary, while EN 3 (s) states "*The exercise of the powers to restructure insurance liabilities should respect the statutory hierarchy of claims while providing flexibility to depart from the general principle of pari passu treatment of creditors of the same class, in a way that is consistent with KA 5.1*".

In the U.S., state receivership laws generally do not allow or provide for the establishment of different classes of policyholders. While state guaranty association laws provide for different levels of coverage for different products (e.g., $300,000 for life insurance death benefits, $250,000 for annuity benefits), receivers are not permitted to create sub-classes of policyholders and contract holders in order to provide them different treatment. We, therefore, request that language be added to EC 5.2 and EN 3 (s) to state that resolution authorities may not depart from the pari passu principle when it conflicts with existing law.

Funding of Firms in Resolution:

EC 6.1 allows for funding arrangements to assist in the use of resolution powers and achieve the resolution objectives, including a privately funded policyholder protection scheme ("PPS"). EN 6 (a) also states that "*The resolution fund or other funds for resolution purposes may be either privately or publicly administered, provided that the ultimate source of the funding is private*".

In the U.S., many states have laws that permit insurers to offset a portion of their future premium, income and/or franchise tax liabilities by the amount of the guaranty association assessments they have paid (e.g., 20% over 5 years). This, in turn, reduces the tax bases of those states. Jurisdictions should be able to decide whether or not their PPSs are fully or partially publicly funded, therefore, we request that language be added to EC 6.1 and EN 6 (a) to account for this type of arrangement.

Jurisdictional Limits:

We support the FSB's recognition in the KAs, particularly KA 7 (Legal Framework Conditions for Cross-Border Cooperation), that multiple authorities may be responsible for exercising resolution powers under a resolution regime. For example, an insurer's domestic resolution authority may not have direct jurisdiction over its holding company or its non-regulated operational/services entities within the insurance group.

We would urge that, where a robust insolvency framework exists to resolve non-insurance entities within an insurance group, such as the federal bankruptcy court system in the U.S., and where mechanisms exist to promote and facilitate coordination, it is not necessary for such entities to be subject to the operating insurer's domestic resolution regime. This is another example of why flexibility in the application of these principles is critical.

Thank you again for this opportunity to provide comments on the 2017 Consultation. If you have any questions, feel free to contact me at 00-1-202-624-2135 or waynemehlman@acli.com.

Sincerely,

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