THE GENEVA ASSOCIATION

The Geneva Association Response to the FSB Consultation, 12 August 2013

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The Geneva Association

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Introduction

The Geneva Association appreciates the opportunity to comment on the Financial Stability Board's consultative document *Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions* issued 12 August 2013.

Over the last four years, The Geneva Association has issued a series of research reports and has contributed widely to the global discussion on financial stability in insurance. Over this period, The Geneva Association and the insurance industry have supported the Group of Twenty Finance Ministers and Central Bank Governors (G20) ongoing regulatory initiatives to increase the resilience of the global financial system. We believe that the development and promotion of effective supervisory and regulatory policies to reduce systemic risk and encourage transparency will benefit the global financial system, including the insurance sector, which plays an important role as an investor in the financial markets and as a risk absorber for society.

The Geneva Association submits the following consultation response to support the development of appropriate and effective regulatory and supervisory measures designed to create greater financial stability. Solid recovery and resolution measures are fundamental in achieving this.

From the outset, the position developed by The Geneva Association and the wider insurance industry has been that the insurance sector requires regulatory standards that reflect its business model and that this effort should be focused on identifying activities that are potentially systemically risky. Once these potentially systemically risky activities are identified, appropriate and adequate regulatory responses can be applied to maintain a strong and resilient insurance industry.

The fundamental principle of insurance is the law of large numbers: insurers reduce the relative risk of loss by insuring a large number of independent units of risks. Many insurers further reduce risk and volatility of loss by writing several lines of business, and across several countries. The larger the number of units, and the more diversified by line of business and geography, the more stable is the business. Thus, intuitively, a designation based on size would be against the basic insurance concept of the law of large numbers and the benefits of the diversification of risks.

FSB Consultation: *Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions.* The Geneva Association Position

Introductory comments

The Geneva Association welcomes the opportunity to respond to this consultation and have set out our comments for each of the consultations questions below. In addition we would highlight the following points:

- **A focused activity-based methodology is required.** The objective of any resolution regime should enable non-viable insurers to exit the market in an orderly manner without causing systemic risk to the wider economy. The scope of Financial Stability Board (FSB) resolution measures should apply to only those systemically relevant activities on a scale that poses a potential threat to the continuing viability of an insurer and therefore, the capacity to resolve these activities in an orderly manner. In light of this, the G-SII methodology should focus on the context of activities within the group rather than solely benchmarking between groups on absolute values. The objective and scope of the draft guidance are also difficult to reconcile with the FSB's intention to deal with the potential failure of G-SIIs. For example, the Annex to the Key Attributes lists the objectives of resolution regimes simultaneously as (i) preventing systemic disruption, (ii) avoiding taxpayer losses and (iii) policyholder protection. The draft guidance therefore seems to apply to all insurance activities, irrespective of whether their failure could give risk to a systemic event.
- **A clearly defined scope is needed.** The fact that criticality is separated from the assessment of systemic risk and added as a separate consideration in this guidance potentially extends the scope of the recommendations to all insurance activities, irrespective of whether their failure could give rise to a systemic event. Insurers do not provide critical functions to the financial system or wider economy in the same way as banks. Whilst the insurance industry does provide important services to their policyholders and the broader economy, substitutability within the sector and the availability of appropriate resolution measures ensures continuity of cover for existing policyholders. The FSB should therefore make it clear that this special regime should only apply to those rare cases where systemically relevant activities undertaken by an insurance company might threaten the rest of the group and the rest of the financial system.
- **Legislative and legal challenges.** Implementing many of the proposals will require extensive legislative change across many jurisdictions. Certain of the proposed changes touch fundamental rights of creditors and principles of contract law and, as such, will be controversial in a number of countries. The "technical" implementation process is likely to be a very long process.
- **Viability in insurance must be clearly defined in order to differentiate recovery and resolution planning requirements.** Given the timing characteristics of insurance business, there are many management and supervisory actions that can be taken to stabilise a viable insurer that is experiencing difficulty. It should also be noted that recovery actions may be spread over a long period and would not necessarily be a response to a single event, rather, an assessment of the likely trend given the long-term nature of insurance business. Therefore, resolution plans should trigger only at the point when all other stabilisation actions have been exhausted. A clear focus in this respect will prevent overlap between recovery and resolution plans and associated actions.
- **Diversification of risk is a core insurance benefit to society.** The fungibility of capital is necessary to support diversification across an insurance group. This should be explicitly recognised within the guidance and national supervisors should be discouraged from further ring-fencing. However, the measures barely mention this important implicit requirement, other than requiring the potential for ring-fencing to be considered as part of the resolvability

assessment. We are concerned that overly prescriptive requirements may encourage national authorities to ring-fence, thereby impacting risk diversification within insurance groups. There is a danger that an inappropriately applied policy could negatively impact insurer's diversification and possibly threaten the rationale for the existence of insurance groups. Therefore policymakers should consider carefully the unintended consequences that may arise in applying measures that do not appropriately take account of the nature of insurance groups.

- **Policyholder protection should be a central focus of resolution.** Resolution of an insurer that is "non-viable" (where viability is properly defined for the insurance sector), should, where practicable, avoid a "wind up" as this would be incompatible with policyholder protection and continuity of cover in most cases. In order to maintain continuity of cover resolution should focus on other tools; such as recapitalisation (either through capital injection, or restructuring liabilities and portfolio transfer and portfolio run-off). As policyholder protection is an objective in resolution, wind-up would be a last-resort option only applicable in exceptional circumstances. Therefore the working focus of resolution plans should be on the continuity of the insurance entity, as this would preserve policies (albeit possibly at reduced values). Resolution assessments and plans should therefore focus on:
  - ◊ sources of support including policyholder protection schemes that can be called on;
  - ◊ ensuring that intra group agreements are written on an arm's length basis and are enforceable by the legal entity that is the subject of the plan;
  - ◊ ensuring that service-level agreements are in place where services are provided or contracted by other parts of the group so that the legal entity that is the subject of the plan can rely on those services if it ceases to be part of the group.
- **Recovery and resolution measures must be legal.** Any of the measures proposed for recovery and resolution must (when implemented) comply with generally recognised principles of mandatorily applicable law. Some of the proposed measures for the restructuring of liabilities (4.4.(v)-(viii)) and the proposed handling of the *pari passu* principle in paragraph 5.2 go beyond what is currently permissible under insurance supervisory law in many jurisdictions and appears to be highly questionable with regard to the principle of proportionality and the protection of ownership rights (e.g. creation of subclasses of existing policyholders). In order to maintain legal certainty and confidence of market participants, any collateral arrangements in place at the time of resolution of an insurer should be strictly respected.
- **The FSB could usefully expand its guidance surrounding restructuring of liabilities to address the impact on ownership structures for the entity being resolved.** There is a need to explore how recapitalisation involving restructuring liabilities would affect ownership, e.g. whether the entity could be transferred to a new holding company owned by the creditors written down, so that once stabilised it can be sold as a going concern and creditors be paid in order of their ranking (as outlined in the BIS paper of June 2013[1]). This perhaps could position the purpose of a bridge institution in an insurance context. As indicated in the FSB guidance, jurisdictions should implement appropriate policyholder protection schemes, however, these should not seek to remove all losses from policyholders but limit them to a level deemed appropriate at a national level.

1 Cf. *A template for recapitalising too-big-to-fail banks*.

Consultation Question Responses

22. Are the general resolution powers specified in KA 3.2, as elaborated in this draft guidance, together with the insurance-specific powers of portfolio transfer and run-off, as specified in KA 3.7, sufficient for the effective resolution of all insurers that might be systemically important or critical in failure, irrespective of size and the kind of insurance activities (traditional and "non-traditional, non-insurance" (NTNI)) that they carry out? What additional powers (if any) might be required?

Below we state comments on specific aspects of the authorities' proposed resolution powers as described in the Annex to the Key Attributes. As a general comment we would like to note that, with respect to the identification of the relevant resolution authority, a clear distinction ought to be made between additional powers to be granted to the insurance regulator acting as an administrative insurance supervisory body on the one hand, and additional instruments that are made available in connection with an insolvency procedure under the control of an insolvency court on the other. So far, the FSB paper does not provide any guidance in this regard.

Entry into resolution

The point at which an insurer is entered into resolution will require careful judgement. Preset triggers are not appropriate, given the continuum of actions that can be taken to address issues over an extended time horizon. Therefore, a decision to enter an insurer into resolution should not be reached until all possible recovery options have been exhausted.

Control, manage and operate the insurer or bridge institution

The paper notes that resolution authorities should have the power to carry on some or all of the insurance business, either within the existing entity or using a bridge institution, with a view to maximising value for policyholders as a whole and providing continuity of insurance coverage.

In the context of resolution powers being exercised in a situation where the insurer is no longer viable, the power to continue to carry on some of the insurers business, for example, making payments to annuitants, would be consistent with policyholder protection. However, the aim should be to establish appropriate adjustments in value, where required, as soon as practicable to prevent conflicts of interests arising between different policyholder groups.

The nature of a bridge institution in an insurance context is not elaborated on within the annex, and this is an area where we would encourage policymakers to consider further in terms of the purpose and ownership structure of such an institution.

Restructuring of liabilities

The paper notes that the resolution authority should have the power to restructure or limit liabilities, including insurance and reinsurance liabilities, and allocate losses to creditors and policyholders in a way consistent with the statutory creditor hierarchy.

We agree that restructuring of liabilities is an appropriate tool where an insurer is no longer viable and all other recovery actions have been exhausted. Writing down benefits to policyholders to enable continuity of their policies (albeit at reduced value) is a preferable outcome to a wind-up scenario.

The point at which an insurer enters resolution should not remove all risk from policyholders, as this would create moral hazard. However, potential losses to policyholders should be limited. The authorities may adopt a higher risk appetite in this respect where a minimum level of cover is provided by a policyholder protection scheme. This will require careful judgement taking account of the capacity of the policyholder protection scheme to support an insurer's recapitalisation and to facilitate the continuity of protected insurance contracts at the level provided by the policyholder protection scheme.

It should be noted that a restructuring of liabilities would currently, in many jurisdictions, be a matter requiring court approval. The proposed powers would need to be transposed into national law before being exercised by insurance supervisors. The FSB should set out more clearly whether this is its intention and, if so, the rationale for why change is required.

Funding in resolution

Whilst privately financed policyholder protection schemes will prove useful where insurers have insufficient assets to meet their liabilities as they fall due, as noted earlier, they should not be used to prevent policyholders suffering any loss in the event of the failure of an insurer. It is important that policyholder protection is limited to prevent moral hazard, i.e. policyholders should not be absolved of all responsibility over their choice of insurance company.

The paper notes that policyholder protection schemes can assist in securing continuity of insurance coverage and providing compensation where insurers are being wound up. The guidance should be more explicit in noting that policyholder protection schemes in securing continuity of insurance coverage could contribute to the recapitalisation of an insurer, consistent with the limits of protection provided.

Portfolio transfer

Whilst we agree that portfolio transfer is an appropriate tool to have available for resolution, the inclusion of a pre-agreed mechanism to adjust the value of the contract after the transfer has been effected, as indicated in paragraph 4.7 of the paper, would likely deter insurers from agreeing to such transfers. In any event it would have to be subject to the approval of the courts along with all other powers that involve the confiscation of property.

The inclusion of this provision seems to be based on an assumption that speed is a critical factor in resolution, whereas the timing characteristics of insurance should allow for a valuation to be prepared before a transfer is agreed.

Power to suspend insurance policyholders' surrender rights

The paper notes that to achieve an effective resolution, the power of the resolution authority to suspend creditor rights in resolution should extend to the ability to temporarily restrict or suspend the rights of insurance policyholders to withdraw from or change their insurance contracts.

Again there is a need to be clear on the difference between viability and non-viability when considering such a power and who would be best placed to exercise it.

The introduction of such a power for supervisors for use while an insurer is still viable (as is the case currently in some jurisdictions, e.g. France) is most appropriate. This would provide supervisors with the tool necessary to mitigate the perceived risk relating to the liquidity of insurance liabilities.

Where supervisors hold such a power, the weight given to the assessment of liquidity of insurance liabilities as a measure of systemic importance should be reduced.

Besides, to be more efficient from a systemic risk prevention point of view, the supervisory right to suspend surrenders must not be limited to the resolution of a firm, but be potentially extended to the whole market.

With regard to commercial agreements with counterparties, i.e. reinsurers, the integrity of the commercial agreement should not be undermined to avoid undermining the ordinary course of the going-concern business.

23. Should the draft guidance distinguish between traditional insurers and those that carry out NTNI activities? If yes, please explain where such a distinction would be appropriate (for example, in relation to powers, resolution planning and resolvability assessments) and the implications of that distinction.

The Geneva Association considers the currently existing resolution tools for insurance activities as effective, thus this guidance on recovery and resolution planning should focus on activities that pose a potential threat to the continuing viability of the insurers and the rest of the financial system only. For the time being there has been no definition of non-traditional insurance activities which is objective and specific enough to be workable in a resolution process. We urge the regulators to only identify and define NTNIs as activities which can create or amplify systemic threats to the global economy in case of a failure.

For non-insurance activities the assessment needs to make clear which regulator has to be involved to resolve them, as additional expertise might be required. The lead regulator has to make sure the appropriate bodies are involved. Focus must be given to activities which involve bank-like leverage and maturity transformation.

24. Are the additional statutory objectives for the resolution of an insurer (Section 1) appropriate? What additional objectives (if any) should be included?

We believe the scope of application is too broad (cf. our initial remarks):

- The protection of policyholders should be a statutory objective of a resolution framework, but not the primary objectives of a systemic risk regulation regime.
- The definition of "vital economic functions" in paragraph 1.2 needs further consideration in an insurance context, as there needs to be a focus on activities which might genuinely impact the financial system.

Moreover, we believe that further clarification should be provided to make it clear that "appropriate continuity" does not mean that policyholders should suffer no loss in the event of the failure of an insurer. It is important that policyholder protection is limited to prevent moral hazard, i.e. policyholders should not be absolved of all responsibility over their choice of insurance company.

25. Is the scope of application to insurers appropriately defined (Section 2), having regard to the recognition set out in the preamble to the draft guidance that procedures under ordinary insolvency law may be suitable in many insurance failures and resolution tools are likely to be required less frequently for insurers than for other kinds of financial institution (such as banks)?

Clarity of scope for resolution regimes and measuring systemic impact

The introductory remarks to the paper note that traditional tools such as run-off and portfolio transfer may not be able to be relied on, for example, where a sudden deterioration in the viability of a larger, complex insurance group engaging in other non-traditional insurance and non-insurance that may involve some degree of bank-like leverage and maturity transformation. Therefore insurance groups that could be systemically significant or critical if they fail should be subject to resolution regimes that meet the standards of the key attributes.

The traditional insurance business model does not involve maturity transformation and leveraging activities; thus, a sudden deterioration combined with immediate liquidity problems is not a threat. Therefore, focus must be given to material systemically risky activities. It should be noted that it is not the size of NTNI activities that may make an insurer systemically relevant, but the relative size of these activities as a proportion of the insurer's business as a whole. They would need to be of a size sufficient that financial shocks from those activities could pose a risk to the insurer's viability. Even then, the size of the insurer would need to be assessed relative to the financial system to determine if its failure would pose a systemic impact.

The current assessment methodology for the identification of G-SIIs should be improved to consider the relative size of all NTNI activities within a group to establish whether these could pose a destabilising influence, rather than measuring and ranking absolute values.

Definition of systemic risk

The paper refers to the need for resolution regimes to apply to any insurer that could be **systemically significant** or **critical** if it fails. This extends the scope beyond the original definition of systemic risk as set out by the FSB in October 2009. This stressed the critical importance of the continued provision of certain financial services in the context of a systemic event, which was defined as a disruption to the flow of financial services that is (i) caused by an impairment of all or parts of the financial system and (ii) has the potential to have serious negative consequences for the real economy.

We do not consider that criticality should be separated from the assessment of systemic risk and added as an additional consideration, given that it is covered within the definition as an impairment of all or part of the financial system. Separation of critical functions, given the extended definition within the paper, potentially extends the scope to all insurance activities, irrespective of whether their failure could give risk to a systemic event. Whilst insurance activities may be critical to individual policyholders it is unlikely that the failure of an insurer would lead to immediate impairments to parts of the financial system or have serious negative consequences for the real economy.

Vital/essential/critical functions

Section 1 of the paper notes that the objectives of a resolution regime should be to ensure that an insurer can be resolved without severe systemic disruption or exposing taxpayers to loss, while protecting vital economic functions. It goes on to note that vital economic functions include risk transfer, risk pooling and the pooling of savings.

Paragraph 9.2 notes that the chosen resolution strategy should ensure continuity of critical functions, including the continuity of coverage and payment for critical insurance contracts.

Paragraph 10.3 notes that a key component of RRPs is a strategic analysis that identifies the firm's essential and systemically important functions, and goes on to note that such essential functions could include, but are not limited to:

- the provision of critical types of insurance policies, the continuity of which is a priority in resolution for reasons of policyholder protection or financial stability;
- the provision of services (actuarial, claims handling, policy administration, benefit payment, etc.) that are necessary for the continuation of the critical insurance business;
- essential hedging activities that are necessary to the continuation of the insurance business (for example, hedging for variable annuities with complex embedded options and guarantees, or hedging to closely match annuity cash flows);

- liquidity or other funding support provided to other financial institutions, the sudden withdrawal of which could have adverse effects on financial stability;
- intra-group transactions, for example, reinsurance (including captive reinsurance arrangements), funding, liquidity and intra-group support and guarantees, that are essential to the continuation of critical functions elsewhere in a group structure or that could otherwise significantly affect resolution or recovery if they are disrupted or suspended; and
- credit or financial guarantee insurance, or non-insurance (for example, CDS), the withdrawal of which could have adverse effects on financial stability or the broader economy.

This definition of vital economic functions is excessively broad and potentially captures all traditional insurance business functions. This would seem to imply that all insurance contracts are critical. This is inappropriate, as the distinction between what is systemically relevant and what is not has been lost. Current available tools such as run-off or portfolio transfers ensure proper continuation of these relevant insurance functions.

The guidance needs to be revised to focus on those activities that, due to their size and/or market concentration ,could have an impact to the global financial system or real economy. The current descriptions within the annex do not provide this.

It should also be recognised that insurance activities are not critical in the same way as, for example, payment services provided by banks which cannot be readily substituted. The services that support insurance activities are readily substitutable in the market, with portfolios being transferable to alternate providers.

26. Does the draft guidance (Section 4) adequately address the specific considerations in the application to insurers of the resolution powers set out in KA 3.2? What additional considerations regarding the application of other powers set out in KA 3.2 should be addressed in this guidance?

The resolution authority must be entitled to continue to manage derivative portfolios on behalf of the company in resolution without causing a change in control of the company which could trigger additional calls for collaterals or the cancelling of deals. This would avoid breakdowns in hedging programmes and/or unexpected collateral calls. Mandatory bail-in instruments are not effective in insurance due to limited use and volume of third party financing.

Resolution authorities should have the power to stay the exercise of all options under existing contracts of insurance including the surrender or withdrawal of cash-value.

27. Does the draft guidance deal appropriately with the application of powers to write down and restructure liabilities of insurers (paragraphs 4.4 to 4.6)? What additional considerations regarding the application of "bail-in" to insurers (if any) should be addressed in the draft guidance?

Insurance portfolios are composed by long-term liabilities backed by assets matching the pay-out pattern of the liabilities (ALM). The bail-in tool is a banking concept yet untested. However, its objective can be achieved in many jurisdictions under existing corporate restructuring laws with court and creditor approval. Given the extended time horizon over which issues at insurers can be addressed, the time impediments that make a specific bail-in tool desirable for the recapitalisation of banks are not present for insurers. Therefore, where jurisdictions have a legal framework in place that facilitates corporate restructuring, there would seem little rationale for introducing new resolution tools in this respect. In addition, financing through bonds represents a useful option for an insurer by offering some degree of financial flexibility. It represents a much smaller slice of an insurer's balance sheet than the typical bank's. Bailing in bondholders would thus make a very small contribution to the resolution of an insurer. It would however make it more expensive for all insurers to issue bonds. Further, imposing bail-in instruments to insurers would unnecessarily increase the balance sheet with no positive effect to financial stability

More effective is that companies develop strong risk management procedures with focus on ALM strategies.

Restructuring liabilities including partial reduction of policyholder liabilities may be a preferable outcome to winding up of an insurer where all other options have been exhausted. This would enable the insurer to continue to provide its services. However, we do not believe that the power to restructure liabilities should fall to regulators alone, as this involves confiscation of property from individuals requiring court approval.

Moreover, we do not understand what conferring the ability to convert an annuity into a lump sum payment (paragraph 4.4(v)) aims to achieve. If it is clear that the company will not be able to make future payments, but not clear what level of haircut needs to be applied to achieve sustainability, then it will not be clear what level of lump sum would be appropriate either. All that conversion to a lump sum achieves is the crystallisation of the liability.

Finally, any departure from the *pari passu* principle will deter bondholders from investment in insurers. Therefore, it needs to be restricted and should be taken only in circumstances where adherence to the *pari passu* principle would produce perverse or blatantly unfair results.

The proposals in paragraph 4.4 on "Restructuring Liabilities" go well beyond existing powers of insurance regulatory authorities in many jurisdictions and would require fundamental revisions to bankruptcy laws and other laws protecting creditors' rights because the proposals would effectively give broad restructuring powers to insurance regulators that today, in many jurisdictions, lie within the powers of bankruptcy courts.

28. Is it necessary or desirable for resolution authorities to have the power to temporarily restrict or suspend the exercise of rights by policyholders to withdraw from or change their insurance contracts in order to achieve an effective resolution (paragraph 4.9)?

Yes, the option to be in a position to use such tools would mitigate the theoretical risk of runs, where policymakers appear to have concerns. It has also to be noted that surrenders can improve the solvency position of an insurer due to reducing insurance risk like longevity or mortality risk therefore discretion is needed in the use of such powers.

29. Are there any additional considerations or safeguards that are relevant to the treatment of reinsurers of a failing insurer or reinsurer, in particular to: (i) the power to transfer reinsurance cover associated with a portfolio transfer (paragraphs 4.7 and 4.8); and (ii) the power to stay rights of reinsurers to terminate cover (paragraph 4.10)?

As already mentioned above, with regard to commercial agreements with counterparties, i.e. reinsurers, the integrity of the commercial agreement should not be undermined. A retroactive change in contract terms could destabilise the ordinary course of the going concern business.

In particular the measures proposed under paragraphs 4.4 (viii) and 4.8 in respect of inward reinsurance contracts could have a systemic impact on the reinsurance industry. Moreover, paragraph 4.10 proposes that the resolution authority should have the power to "stay any right to no longer reinstate reinsurance cover upon payment of a premium". This concept would require that, as a general rule, reinsurers do have the obligation to reinstate reinsurance against payment of a premium, which is not the case. Therefore we do not consider the power set out in paragraph 4.10 necessary.

Overall the position should be that a change in control brought about through resolution measures does not trigger contractual clauses that enable counterparties to cancel or step down from contracts. This is particularly important for derivative portfolios.

30. What additional factors or considerations (if any) are relevant to the resolvability of insurers or insurers that carry out particular kinds of business (Section 8)?

In respect to entry into resolution, paragraph 4.1 notes that the resolution regime should set out clear standards or suitable indicators of non-viability to guide the decision as to whether an insurer meets the conditions for entry into resolution. It goes on to note that the standards should allow for early entry into resolution before an insurer is balance sheet insolvent.

This potentially confuses recovery and resolution options. While an insurer is balance-sheet solvent, it should be possible to address it as a viable concern. Appropriate recovery actions (including run-off/portfolio transfer) can be taken by the firm as a viable concern, with the encouragement of its supervisor where necessary.

As noted in our high level comments, recovery actions may be spread over a long period and would not necessarily be a response to a single event, rather, an assessment of the likely trend given the long-term nature of insurance business. Therefore resolution plans should focus on non-viability at the point where all other stabilisation actions have been exhausted. A clear focus in this respect will prevent overlap between recovery and resolution plans and associated actions.

If an insurance group is involved in non-insurance activities, (for example through a banking or asset management subsidiary), the resolution framework of those underlying businesses will be applicable.

31. What additional matters (if any) should be covered by recovery plans or resolution plans for insurers or insurers that carry out particular kinds of business (Section 9)?

In considering the application of the FSB's Key Attributes, specifically in respect to recovery and resolution planning, as noted earlier, supervisors need to be clear on the differences between "viability" and "non-viability" and which stage it is seeking to address. This will help distinguish actions that can be taken by an insurer and supervisors as a viable concern and actions that may be taken by the appropriate resolution authority once an insurer is deemed to be no longer viable.

The point at which resolution becomes necessary will require significant judgement, as asset values fluctuate, and so too do liabilities, given that they are best estimates of expected claims/maturities rather than certain amounts. Therefore preset triggers are not appropriate. The process to a point of decision over the probability that an insurer in difficulty requires resolution will take time. Given the long-term nature of insurance business and the continuum of actions that can be taken to address a failing insurer, there should be a clear distinction between the scope and purpose of recovery plans and resolution plans.

The nature of insurers ongoing risk management, including stress and scenario testing, should ensure that all probable risks to the health of an insurer are predicted and planned for. Therefore:

- Recovery planning should be aligned to the management and supervision of an insurance group as a viable concern; and
- Resolution plans should address the remote situation where an unpredictable event has led to the failure of an insurer which cannot be recovered.

Therefore, the question that resolution plans should seek to address is how, in the unlikely event that an insurer reaches the point of non-viability, policyholders interests can be best protected.

The scope of planning should be limited to the insurance group. Recovery planning should consider the impact on the insurance group of the potential failure of non-insurance subsidiaries. However, the resolution of non-insurance subsidiaries will fall under the remit of their relevant sector regulator and should not be duplicated within insurance resolution plans. Consideration should be given to the inclusion of relevant sector regulators within the CMG where these differ. The essential functions as listed are functions which are relevant for a successful processing of a run-off. We do not see them as relevant for the global economic system. Where a firm is in run-off, staff retention may be a relevant consideration.

From a general perspective the requirements on resolution authorities should not produce an outcome that will severely restrict the activities of insurers in the normal course of business, to an extent that is not justified when balanced against the mitigation of damage in the relatively rare event of an insurer's failure (e.g. the requirement in paragraph 9.3(vi) to align business units with legal entities, which reaches deep into the organisation of an insurer, should be a matter for management to determine): The examination of intra-group transactions (paragraph 9.3 (x)) is a key element of any resolvability assessment. However, if carried too far, this analysis risks immobilising the flow of capital around groups and exacerbating the current trend towards capital fragmentation. Consequently, the measures required as a result of this assessment need to be strictly proportionate to the risks identified and weighed against the impact they would have on the availability and cost of insurance.

32. Are the proposed classes of information that insurers should be capable of producing (Section 10) feasible? What additional classes of information (if any) should insurers be capable of producing for the purposes of planning, preparing for or carrying out resolution?

The guidance in paragraph 10 .2 indicates that the specific risks and systemic implications of insurers should be reflected in their recovery and resolution plans. National supervisors therefore need to provide appropriate guidance in a timely manner to insurers on the activities that they undertake that cause them to be regarded as systemically risky.

paragraph 10.3 indicates that a strategic analysis of the firm's essential functions and systemically important functions is a key component of recovery and resolution plans. As noted earlier the guidance surrounding vital/essential/critical functions is too broad, potentially capturing all insurance activity. This therefore needs to be reconsidered to ensure that plans can be appropriately focused, and should focus on those activities that could have a systemic impact due to their size and/or market concentration.

33. Does this draft Annex meet the overall objective of providing sector-specific details for the implementation of the Key Attributes in relation to resolution regimes for insurers? Are there any other issues in relation to the resolution of insurers that it would be helpful for the FSB to clarify in this guidance?

As set out in our introductory comments and our answers to the consultation questions above, there is a need to more clearly focus on the differences between viability and non-viability in the insurance context. The guidance also needs to be more clearly targeted at activities that could be systemically relevant. The current definitions within the paper are too broad to facilitate this.

In addition, we have the following comments on the annex that are not specifically addressed in the questions above.

Resolvability assessments

As noted earlier there is a need to be clear on the differences between viability and non-viability and which stage the resolvability assessment is seeking to address to help identify the actions that will be needed.

The resolvability assessment should consider how policyholders' interests can be best protected in the unlikely situation that an unpredictable event has led an insurer to a point of non-viability, (all other recovery actions having been exhausted).

Where this involves recapitalisation through the restructuring of liabilities, this may necessitate a change of ownership of an insurance entity, i.e. where parental support is either unviable or unavailable.

Therefore the resolvability assessment should focus on:

- sources of support including policyholder protection schemes;
- enforceability of intra group agreements (these should be arms length);
- transferability of service agreements where services are provided by other parts of the group, or contracted by other parts of the group;
- how ownership would be structured for the entity where it is recapitalised without group support whilst maintaining respect for creditor hierarchy, so that they can be reimbursed for their losses from future gains.

We have the following comments on the points listed in Section 9 of the paper.

- Paragraph 9.3 (iv) notes that in a solvent run-off there is a risk that later maturing policies may not receive their benefits in full. We do not agree that this risk is any greater in an insurer that is in a solvent run-off than in an insurer that is actively taking new business. In both cases the insurers will be subject to prudential regulation as a going concern and will need to be capitalised to meet their obligations to their policyholders as they fall due.
- Paragraph 9.3(vi) notes that the alignment of corporate structures and business units to facilitate sale of different parts of the group should be considered. The important issue is not whether there is alignment between corporate structures and business units, but whether there are appropriate service agreements in place such that services provided to a legal entity could continue if it were separated from the group.
- Paragraph 9.3(viii) notes that the assessment should consider the legal, operational and financial separateness

of traditional insurance from non-traditional insurance. Care is needed in interpreting this point as the IAIS blur the distinction between what is traditional and non-traditional insurance in their G-SII assessment methodology. Given that the aim of the resolution regime is policyholder protection and continuity of insurance, a distinction between insurance and non-insurance will be more relevant.

- Paragraph 9.3(x) notes that the assessment should consider the effect of intra-group transactions in resolution. The focus here should be on the enforceability of intra-group transactions, (the effect of enforcing the transactions should be considered as part of going-concern management actions and recovery scenarios).
- Paragraph 9.3(xiii) notes that the assessment should consider whether surplus assets in other jurisdictions may be ring fenced. We believe the FSB should expand on this point of guidance and specifically state that authorities should not ring fence assets in jurisdictions in a manner that could damage diversification of risk within an insurance group through restricting fungibility

Resolution strategies and plans

Paragraph 10.10 (ii) notes that the plan should include the actuarial assumptions used for calculating insurance liabilities and an independent exit actuarial value of liabilities. Supervisors should have an understanding of the assumptions used in calculating liabilities as part of its "going-concern" oversight of insurers. Therefore, it would seem unnecessary to include this within the scope of the resolution plan. As noted above, the plan should focus on the circumstances where an insurer is a no longer viable, i.e. the assets will be insufficient as valued and monitored on an on-going basis.

Therefore the introduction of the idea that RRPs for insurers must contain "the actuarial assumptions used for calculating insurance liabilities and an independent exit value actuarial valuation of the technical provisions (policyholder liabilities)" is unwarranted. If "exit value" is something different from the "best estimate liability" that is used for accounting/prudential purposes, it would mean "a winding-up gap" between this "exit value" and the audited "best estimate liability". The going-concern principle must not be questioned by the reintroduction of a gone-concern vision.

Paragraph 10.10 (vii) notes that the recovery plan should consider details on ceded reinsurance among the various legal entities and the impact on recovery levels. Reinsurance will be a factor in the valuation of liabilities. However, this is something that should be considered as part of the ongoing management and supervision of an insurer. Contracts of reinsurance between legal insurance entities should not be impacted by resolution if the aim is to provide continuity of insurance through recapitalisation of the entity (preserving its legal identity).

Paragraph 10.10 (viii) notes that the plan should include an estimate of the outcome for each class of policyholder upon winding up the insurance entity. The value would depend on the available assets of the insurer and market conditions that may affect those assets. Therefore, this is something that would be best estimated once a decision has been taken that an insurer should be taken into resolution rather than something that can be planned in advance. Given the objectives of resolution to protect policyholders and provide continuity of cover, wind-up would seem to be an exceptional course of action only for consideration if recapitalisation is not viable. Therefore, this is a matter that should be assessed by the resolution authority once an insurer has entered resolution. The plan should perhaps set out considerations that the resolution authority should take in this respect, rather than trying to predict in advance what uncertain future values may be.

FSB Consultation: *Information Sharing for Resolution Purposes.*
The Geneva Association Position

Introduction

The paper on Information Sharing for Resolution Purposes proposes draft implementation guidance that elaborates on the standards for information sharing, confidentiality requirements, statutory safeguards and information sharing within cross-border crisis management groups (CMGs).

Before commenting in detail we would like to make a general observation: we highly appreciate that the FSB aims to provide for confidentiality requirements in institution-specific, cross-border cooperation agreements. However, they will only be effective if the respective jurisdiction provides for legal certainty. This may not always be ensured in all jurisdictions in which G-SII may undertake business. Therefore, the composition of the CMGs is key to providing confidentiality. We believe that highly confidential information, such as, for example, the measures section of the recovery and resolution plan, may only be shared with such jurisdictions whose markets are material for the G-SII. This is further supported by the fact that in electronic communication, confidentiality is very difficult to achieve, in particular if the diverse parties of the CMGs have different IT systems. Hence, it is of utmost importance that as much data transfer is avoided as possible. A possible solution could be that supervisors of jurisdictions not material for the respective GSII only receive information that is directly related to their markets.

Implementation question responses

1. The draft guidance is intended to apply in relation to all financial sectors. Do any considerations arise in relation to the exchange of information on particular kinds of financial institution that require sector-specific provisions? If yes, please elaborate.

As there are different policyholder protection schemes in different jurisdictions, there is a concern that this could trigger different agreements per company and jurisdiction

2. Do the provisions on legal gateways for disclosure of non-public information (paragraphs 1.1 to 1.8) outline the key elements that should be included in a jurisdiction's legal framework to allow national authorities to share information for resolution-related purposes with other national and foreign authorities? Please explain any additional elements that should be included.

In addition to the elements provided, we suggest that:

- When establishing legal gateways for disclosure of non-public information it must be clear that this must be restricted to only sharing that information which is absolutely required and to only those authorized personnel for resolution purposes.
- Sharing of non-public information should not be done on an annual basis, but only for resolution purposes.
- It should be made explicit that the G-SII is a necessary party to any cross border cooperation agreement (COAG) and that a COAG must be binding on a liquidator or other party taking control of an institution.
- Generally, legal gateways should permit commercially and sensitive material (e.g. customer or counterparty information) to be disclosed to domestic and foreign authorities if necessary for resolution. However, consideration should be given to how this could occur given that the underlying information with third parties is subject to

confidentiality provisions. Typically there would be a carve-out permitting disclosure where such disclosure is required by applicable laws/regulations, but there might be restrictions on how much of the information can be disclosed.

- Please see response to Question 4 below for further comments.

3. Does the draft guidance (in particular, paragraph 1.4) provide an adequate standard of protection for all the types of information, including supervisory information, that authorities may need to share for resolution purposes? If not, please explain.

The draft guidance is helpful in setting out the principles for preserving the confidentiality of the information to be shared. However, it should be explicit that that the G-SII is a necessary party to any COAG and that a COAG must be binding on a liquidator or other party taking control of an institution. A COAG must be in place and signed by all the G-SII Group's regulators before any information is shared by the G-SII's principal regulator and another regulator of the G-SII Group.

Additionally, the provisions in paragraph 1.13 should apply equally to information shared by the home authority. Additional guidance should be included on the system used to share the information to ensure it is secure and on the system of the authority, where information provided will be held and how it will be held (e.g. a secure private server located in Canada). There should also be appropriate measures in place regarding storage, copying/reproduction and destruction of the information.

4. Are the resolution-related purposes for which authorities should be able to disclose information (paragraph 1.9) sufficiently comprehensive? If not, what additional purposes should be included?

While the purposes listed appear reasonable, it should be made clear when a G-SII's resolution plan should not be shared by the G-SII's principal regulator with other regulators. For example, this should not occur on an annual basis as all of these steps will be highly commercially sensitive information.

It should be noted that during the resolution process, sharing of information[2] should only be shared by the G-SII's principal regulator with another country's regulator as it impacts a particular jurisdiction or where a resolution option has a cross-border impact which the relevant regulator needs to be aware of. The principal regulator should restrict disclosure to the extent absolutely necessary.

If the G-SII regulator has to step in to effect resolution of the G-SII and there is a need to share further information on the resolution plan at that stage with the G-SII group's other regulators, it should only be a summary of the resolution steps which will be taken which should be shared.

5. Are the standards of "adequate confidentiality requirements" set out in the draft principles (paragraphs 1.10 to 1.15, 2.4 and 2.5) sufficient to protect the confidentiality of sensitive information, without being excessively restrictive so as to impede necessary exchange? If not, please explain what more is required or desirable.

It should be clear that authorities are responsible for breaches of confidentiality by third parties to whom they transfer

2 Paragraph 1.9 (i)–(iii) and (vii).

information. Authorities should disclose to the institution when information is shared with an authority that is not a signatory to a COAG.

Paragraph 2.4 0(iv) should be extended to cover off dissemination of information to agents being restricted in the same way. The additional protection for sensitive information set out in the key attributes document is not reflected in the guidance, i.e. that the sharing of this information may be restricted but should be possible among the top officials of the relevant authorities only.

6. Is it appropriate that information received from foreign authorities should be excluded from Freedom of Information regimes or exempt from disclosure under such regimes (paragraph 1.15)? Are there circumstances when information received from foreign authorities for resolution-related purposes should be subject to disclosure requests?

Information received in respect of resolution plans by any authority whether directly from a G-SII or from a foreign authority should be excluded from Freedom of Information or equivalent regimes.

7. What other issues in relation to the exchange of information for resolution-related purposes (if any) would it be helpful for the FSB to clarify in this guidance?

No further comments.