

Higher Loss Absorbency Capacity for Global Systemically Important Insurers (G-SIIs)

HLA Public Background Session
IAIS Secretariat
8 July 2015



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Purpose of this Public Background Session

1. The primary purposes of this public background session regarding the HLA Consultation are to:
 - Provide background information on the project;
 - Describe the subject matter being presented for public consultation;
 - Describe specific issues on which the IAIS is seeking targeted input.
2. We will also address questions of content, interpretation or clarification of the Consultation Document, with a focus on questions submitted in advance.
3. Responses will only be provided to comments submitted through the IAIS Consultation Tool.

Background

1. In July 2013, the IAIS published its assessment methodology and policy measures for global systemically important insurers (G-SIIs). These policy measures consist of three main types of measures: enhanced supervision, effective resolution, and Higher Loss Absorption (HLA) capacity.
2. The primary purpose of the HLA requirement is to help reduce the probability and impact on the financial system of the distress or failure of a G-SII. It is to be delivered to the G20 for endorsement in November 2015 and will apply to G-SIIs from 2019.
3. As a foundation for HLA requirements, the Basic Capital Requirements (BCR) for G-SIIs was developed by the IAIS in October 2014, and endorsed by the Financial Stability Board (FSB) and G20 in November 2014.
4. On 22 September 2014, the IAIS published a set of Principles (Annex C of the Consultation Document) to guide the development of the HLA requirements. The IAIS is now issuing for public consultation several options of a draft HLA. Comments are due by 21 August 2015.

HLA timeframe

Key Dates	Milestones
25 June – 21 August 2015	Public Consultation on HLA requirement for GSIIIs
Sept/Oct 2015	HLA proposal to be finalized and approved by IAIS
Oct /Nov 2015	Expected endorsement of HLA by FSB and G20
2016-2018	Confidential reporting of HLA and BCR with access by the IAIS; On-going refinement of BCR and HLA; On-going broader IAIS field testing program to support the development of ComFrame (applicable to all IAIGs), including the ICS
From January 2019	BCR and HLA requirements to be applied to all G-SIIIs designated in November 2017 and in future years
Late-2019	ComFrame, including ICS, to be adopted by IAIS
Post 2019	Implementation of ComFrame, including the ICS, by IAIS members to commence; HLA reviewed so an HLA based on the ICS may be developed

Consultation process

1. Consultation opens: 25 June 2015
2. Public background session: 8 July at 14:00 CEST (teleconference)
3. End of consultation: 21 August 2015 (close of business, CEST)
4. How to respond: Submit comments via the IAIS consultation tool
 - See <http://iaisweb.org/> -> News -> Consultations
 - Note that draft comments are automatically saved in the tool, to permit continuing working on a submission at a later date. Only one submission per person is accepted (only the latest submission submitted by each persons will be retained).
5. All comments will be published on the IAIS website unless a specific request is made (in the tool) for comments to remain confidential
6. Review of comments will be completed by end 2015 and responses published

Structure of Consultation Document

The body of the Consultation Document is structured as follows:

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| Section 3 | Background to the development of the HLA requirement |
| Section 4 | Structure of the BCR + HLA components and proposed approach in determining the Uplifts for Insurance and NI |
| Section 5 | Main issues to be consulted on with regard to the HLA required capital: structure of possible HLA formula is presented, with illustrative examples to highlight the potential impact of some choices of formulas |
| Section 6 | Capital resources needed to support the HLA required capital |
| Section 7 | Some operational matters: HLA interaction with G-SII designation process, field testing, HLA reporting process, etc. |

Key HLA consultation points

1. The public consultation does not focus on specific formulas but rather seeks feedback on a structure designed to address the key objectives of risk sensitivity, robustness and simplicity.

2. Key HLA consultation points - three main issues to consider when specifying HLA required capital formulas:
 - Bucketing - to specify which factor to apply to which G-SII, a choice of how many buckets to have
 - Choice of HLA formulas - to specify the exposure, a choice regarding the increased emphasis to be placed on Non-Traditional Insurance (NT) and NI activities
 - Calibration of outcomes - to specify the size of the factors, a choice of the extent of the impact that the HLA is to have on G-SIIs, both on average and in particular, recognising there are differences in G-SII business models

IAIS position on systemic risk

Definition of Systemic Risk:

“Systemic risk is the risk of disruption of financial services that is caused by impairment of all or parts of the financial system and has the potential for serious negative consequences for the real economy.”

The IAIS position on systemic risk in the G-SII Policy Measures can be summarised as:

- There is little evidence of traditional insurance either generating or amplifying systemic risk.
- Non-Traditional Insurance (NT) and Non-Insurance (NI) activities within insurance firms or groups may generate or amplify systemic risk.
- Differences between the traditional insurance business model and the banking business model need to be considered when assessing the systemic importance of insurance.
- The time dimension is important in insurance (both in respect of business model and regulatory action) as runs on insurers are uncommon.
- The insurance sector is susceptible to systemic risk generated in (or transmitted through) other parts of the financial sector.

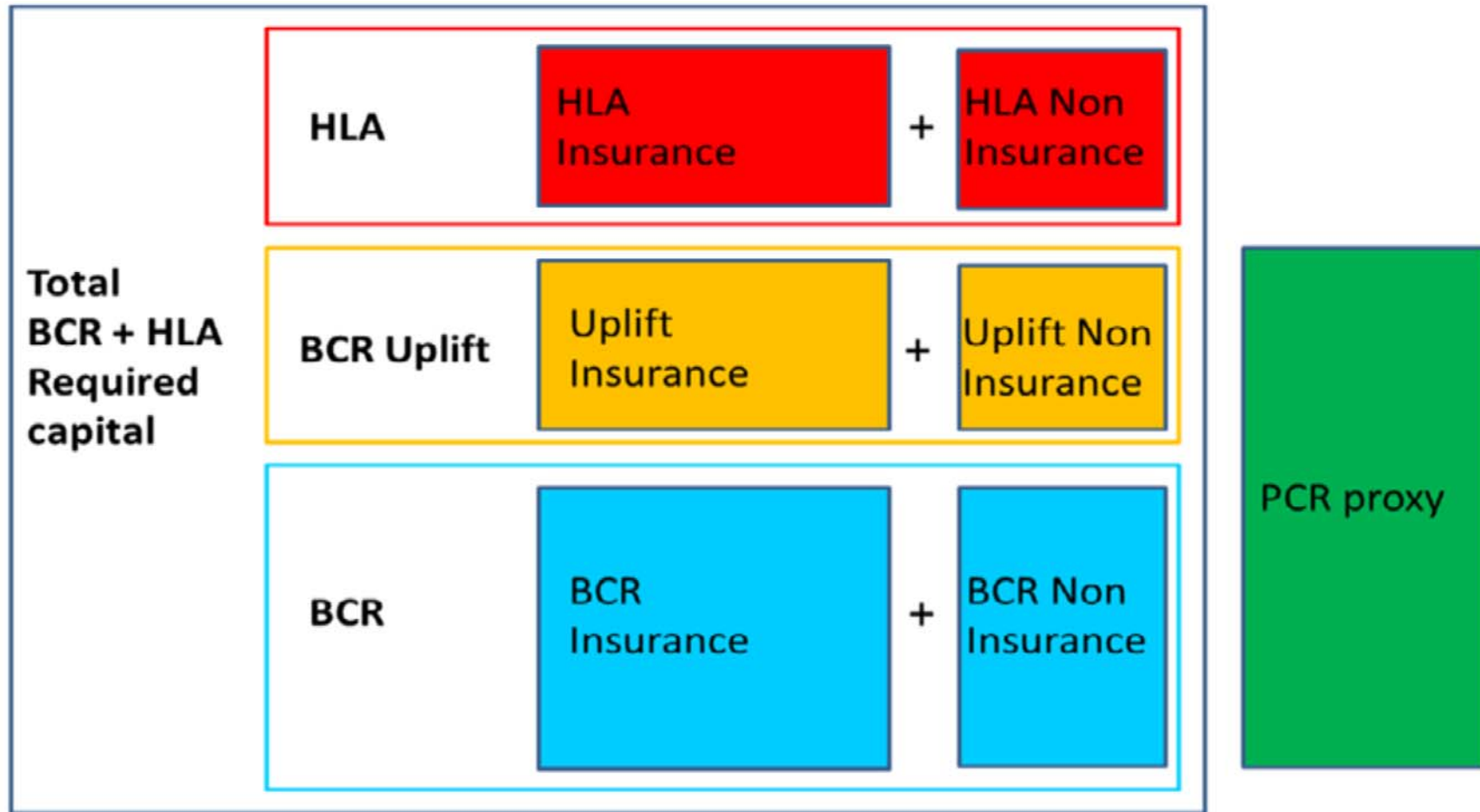
Key considerations in HLA design

1. G-SIIs should be required by their group-wide supervisors to hold higher levels of regulatory capital than would be the case if they were not designated as G-SIIs.
2. The HLA will be a globally comparable group capital requirement that applies to all G-SIIs. The HLA will apply to all group activities, including non-insurance subsidiaries, taking a going concern approach.
3. Meeting the policy objectives for the HLA as outlined in the IAIS G-SII Policy Measures document of July 2013. The development of the HLA is guided by the 10 HLA principles published by the IAIS in October 2014. The first two principles are noted:
 - Principle 1: Outcomes should be comparable across jurisdictions
 - Principle 2: The HLA should reflect drivers (but is not restricted to only these drivers) of the assessment of G-SII status
4. An appropriate trade-off in construction between risk sensitivity, robustness and simplicity will be addressed.

Key considerations in HLA design (cont)

5. Disincentives will be built into the HLA formulas to encourage G-SIIs to reduce potential systemic activities.
6. The construction process for the HLA separates Insurance and NI business aspects so that existing global regulatory requirements in non-insurance sectors may be reflected.
7. The HLA required capital amounts (Insurance & NI) will increase the sum of the BCR and Uplift by amount does not exceed 20%, on average, for G-SIIs. The HLA NI required capital relating to regulated banking activities will not exceed the relevant regulated banking requirements for those activities.
8. The HLA will initially build on the foundation of the globally comparable BCR. When the globally comparable ICS is developed, the HLA will then be reviewed as the ICS will replace the BCR in its role as the foundation for HLA and apply.

Total BCR + HLA required capital



Summary of Total HLA, Uplift, and BCR

1. HLA Insurance: Applies percentages from choices to exposure of (BCR Insurance + Uplift Insurance)
2. HLA Non-Insurance: Applies HLA Insurance percentages from choices to exposure of (BCR Non-Insurance + Uplift Non-Insurance)
3. Uplift Insurance: $33\% * \text{BCR Insurance}$ (working assumption)
4. Uplift Non-Insurance: $33\% * \text{BCR Non-Insurance}$ (working assumption)
5. BCR Insurance and BCR Non-Insurance are as specified in the approved October 2014 document.
6. Data reflects field testing data from 2014.



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Thank you! Questions?



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