INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS

Public

Draft Application Paper on Recovery Planning

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Application Papers provide additional material related to one or more ICPs, ComFrame or G-SII policy measures, including actual examples or case studies that help practical application of supervisory material. Application Papers could be provided in circumstances where the practical application of principles and standards may vary or where their interpretation and implementation may pose challenges. Application Papers can provide further advice, illustrations, recommendations or examples of good practice to supervisors on how supervisory material may be implemented.

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Acronyms

ComFrame	Common Framework for the Supervision of Internationally Active Insurance Groups
ERM	Enterprise Risk Management
FSB	Financial Stability Board
G-SII	Global Systemically Important Insurer
IAIS	International Association of Insurance Supervisors
IAIG	Internationally Active Insurance Group
ICP	Insurance Core Principle
MIS	Management Information System
ORSA	Own Risk and Solvency Assessment
PCR	Prescribed Capital Requirement

1 Introduction

1. This Application Paper on Recovery Planning provides guidance with respect to draft supervisory material related to recovery planning in the Insurance Core Principles (ICPs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame). In particular, it is related to the draft revised material in ICP 16.13 and ComFrame 16.13 (ICP 16 Enterprise Risk Management for Solvency Purposes), and is also relevant to supervisory cooperation and coordination arrangements set out in ICP 23 (The Group-wide Supervisor) and draft revised ICP 25 (Supervisory Cooperation and Coordination).[1]

2. The Application Paper addresses issues that were identified in the development of this material, including feedback received from members and stakeholders during public consultations. The issues involved both the nature of a recovery plan, and the roles of the supervisor and insurer with respect to the plan. Subjects that were identified included:

- The relationship between recovery plans and enterprise risk management (ERM) tools, including Own Risk and Solvency Assessment (ORSA), contingency plans and other preventive or corrective measures;
- The circumstances in which it is appropriate for the supervisor to require a recovery plan; and
- Implementing the proportionality principle with respect to a recovery plan.

3. In this Paper, terms have the same meaning as set out in the IAIS Glossary. The IAIS Glossary defines a "recovery plan" as a plan that identifies in advance options to restore financial strength and viability if the insurer comes under severe stress. A recovery plan includes three elements: (i) credible options to cope with a range of severe stress scenarios, including both idiosyncratic and market-wide stress; (ii) scenarios that address capital shortfall and liquidity pressures; and (iii) processes to ensure timely implementation of recovery options in a range of severe stress situations.

4. This Application Paper should be read in the context of the proportionality principle, which provides supervisors the flexibility to tailor their implementation of supervisory requirements and their application of insurance supervision to achieve the outcomes stipulated in the Principle Statements and Standards, as described in the Introduction to ICPs and ComFrame.

1.1 Purpose

5. The purpose of this Paper is to:

- Provide recommendations and guidance to supervisors regarding recovery planning, and cooperation and coordination between supervisors;
- Provide additional information for insurers with regard to recovery planning; and

[1] Draft revised ICPs are available on the IAIS website: https://www.iaisweb.org/page/supervisory-material/insurance-core-principles. The draft revised ICPs, endorsed by the Executive Committee and released for information purposes only, may be subject to further changes before being presented for adoption by the general membership at the 2019 Annual General Meeting.

- Provide examples to illustrate the application of principles, standards and guidance relevant to recovery planning.

6. This Paper does not establish standards or expectations for requiring, creating or implementing recovery plans. It provides guidance to supervisors when considering whether to implement recovery planning in their jurisdiction, and if so, how such recovery planning could be constructed to prove useful to the relevant supervisors. It should not be considered an exhaustive compilation with respect to recovery planning. The examples in this Paper are provided only to illustrate recovery planning concepts.

1.2 Scope

7. This Paper and its concepts are relevant to all insurers (i.e. insurance legal entities and insurance groups including insurance-led financial conglomerates), and its recommendations are applicable across supervisory approaches among jurisdictions. Generally, the concepts described in the Paper are equally applicable to the business of insurers and reinsurers. For further background for supervisors in taking into account the nature of reinsurance business when supervising reinsurers, see ICP 13 Reinsurance and Other Forms of Risk Transfer. It is intended to be particularly useful for the supervisors of insurance groups with more complex structures or larger business operations that may benefit from prior planning for recovery from severe stress scenarios.

8. The FSB *Key Attributes for Effective Resolution* (Key Attributes) and related materials contain information regarding recovery planning for G-SIIs. This Paper is not intended to provide specific guidance for G-SII recovery planning although supervisors may find this Paper helpful when addressing G-SII recovery planning. The Paper has been informed by the Key Attributes and to the extent appropriate to provide background information and explain recovery planning concepts.

9. This Paper does not address resolution planning. Development of an Application Paper on resolution planning and other resolution-related matters is expected to commence in 2019.

1.3 Inputs for the Application Paper

10. This Application Paper relies on existing public and non-public[2] documentation on recovery planning and supervisory practices, including material from the FSB, IAIS and supervisory practices of IAIS members. For the latter, this Application Paper draws upon the results of a survey of ReWG members launched in February 2018, to which 11 jurisdictions responded with descriptions of supervisory practices on recovery planning. Where appropriate, practices of recovery planning in the banking sector are used as a source as well. The Application Paper also benefited from inputs received from stakeholders during a stakeholder event held in September 2018.

1.4 Structure of the Application Paper

11. The Paper covers the following topics related to recovery planning:

- Objectives and concepts of recovery planning (Section 2);
- Requirements for recovery plans, and the application of the proportionality principle to recovery planning (Section 3);

[2] Such as supervisory guidance.

- Governance-related matters in recovery planning, including the development and approval process of a recovery plan and how it relates to overall risk management of an insurer (Section 4);
- Key elements of a recovery plan, and examples of how these can be addressed in a recovery plan (Section 5); and
- The role of the supervisor (or supervisors in a cross-border group) with regard to recovery planning (Section 6).

2 Objectives and concepts of recovery planning

12. A "recovery plan" is a plan developed and maintained by the insurer that "identifies in advance options to restore financial strength and viability if the insurer comes under severe stress". The goal of a recovery plan is twofold: to aid the insurer in understanding its own risks from severe stress scenarios, and to be better prepared to provide an effective response. The focus is on situations that pose a serious risk to the viability of the insurer or any material part of its business.

13. In the context of this Application Paper, the development of a recovery plan is pre-emptive in nature and should not be considered as a preventive or corrective measure (as defined in draft revised ICP 10 Preventive Measures, Corrective Measures and Sanctions). Although an insurer may be required by the supervisor to provide a type of "recovery plan" following a breach of its Prescribed Capital Requirement (PCR, See ICP 17 Capital Adequacy), a recovery plan in that context would probably be highly dependent on the environment and circumstances that led to the insurer's PCR breach.

14. To be effective, recovery planning should be integrated in the risk management framework of the insurer and be developed in advance of any severe stress scenario. By evaluating risks and recovery options in advance of any severe stress materialising, it:

- Creates awareness and preparedness for possible adverse situations;
- Enables the insurer to consider and evaluate the most appropriate and effective mitigation without the resulting pressures of actual severe stress; and
- Enables the insurer to make more effective, comprehensive and thoughtful plans to ensure their timely implementation.

15. While recovery planning is intended to serve the insurer as an aid to sound ERM, it also helps the supervisor better understand the insurer in general and how certain adverse situations may be addressed by the insurer. A recovery plan may also serve as additional input for the supervisor to evaluate the insurer's preparedness for severe stress and possible necessary or helpful supervisory measures.

16. The existing tools within an insurer's ERM framework may serve as a source of input when drafting and developing the recovery plan; this may include, but is not limited to, the ORSA, contingency planning and the capital and liquidity management plan. Potential benefits of using these tools as input are to ensure alignment with existing ERM tools and to allow the insurer to use its resources efficiently. For example, an insurer may consider that governance arrangements and reporting lines identified in existing planning arrangements may also be

appropriate for its recovery plan. An insurer should carefully consider the appropriateness of using aspects of existing ERM tools, and should not simply look to replicate existing documentation.

17. Recovery plans differ from an ORSA both in perspective and objective. The ORSA is performed regularly by insurers to assess the adequacy of its risk management and capital to support current and anticipated business operations as a going concern. It encompasses all reasonably foreseeable and relevant material risks, and identifies the relationship between management of those risks and the level and quality of financial resources that are needed and available to support those risks. The objective of the ORSA is to prevent an insurer from coming under severe stress. In contrast, a recovery plan envisions the insurer being confronted with severe stress, and contemplates actions needed to mitigate stress and restore financial strength and viability.

3 Scope of application and proportionality

Location	***Requirements (Standards)***	***Recommendations (Guidance)***
ICP 16.13 (all insurers)	The supervisor requires, as necessary, insurers to evaluate in advance their specific risks and options in possible recovery scenarios.	The decision to require a recovery plan and its *form, content and level of detail* should be proportionate, taking into account, for example, the insurer's *complexity, systemic importance, risk profile and business model*
ComFrame CF 16.13a (IAIGs)	The group-wide supervisor requires the Head of the IAIG to: (i) develop a recovery plan that identifies in advance options to restore financial strength and viability; (ii) review and update the recovery plan on a regular basis and when there are material changes; and (iii) take actions for recovery if the IAIG comes under severe stress.	The supervisor should consider the IAIG's *nature, scale, and complexity* when setting recovery plan requirements, including its *form, content and level of detail*, and the frequency for reviewing and updating the plan.
FSB Key Attributes for Effective Resolution KA 11.5 (SIIs)	Jurisdictions should require that robust and credible RRPs are in place for all G-SIFIs and for any other firm that its home authority assesses could have an impact on financial stability in the event of its failure.	A recovery plan for a firm should take account of its specific circumstances and reflect its *nature, complexity, interconnectedness, level of substitutability and size*.

Figure 1. Overview of varying requirements on recovery planning

18. This section is intended to provide guidance to assist supervisors in making a determination about whether to require a particular insurer to engage in recovery planning,

and if determined to be appropriate, what form, content and level of detail that recovery planning should take, based on the proportionality principle. The appropriateness of requiring a recovery plan depends upon many factors, such as an insurer's size, the nature of its business, and its importance in the marketplace. Therefore, as shown in Figure 1 above, the ICPs, ComFrame and the Key Attributes provide direction to supervisors regarding the development and implementation of recovery plans.

3.1 Proportional application of requirements

19. ICP standard 16.13 provides that insurers evaluate in advance their risks and options in recovery scenarios, as necessary, but does not specify that supervisors require a recovery plan for all insurers. When the supervisor does not require a recovery plan, an insurer may still be required to evaluate its specific risks and options in possible recovery scenarios, as necessary. The supervisor may consider whether the written identification of a trigger framework and recovery options, would be beneficial for an insurer to engage in and should assess the appropriate method and form of the insurer's evaluation, as well as the form of summary reporting to the supervisor on the outcomes of its evaluation.

20. The guidance material under ICP 16.13 provides that the supervisor may require an insurer to develop a recovery plan and explicitly refers to the proportionality principle. A supervisor may implement the requirement based on either micro- or macroprudential grounds. For instance, such a requirement could be related to microprudential considerations such as an insurer's risk profile, legal form, nature or structure of business, or scope and complexity of activities. Also, from a macroprudential perspective, it may be based on the (relative) systemic importance of an insurer or its activities or exposures that may lead to potential systemic risk. Criteria to take into account may be related to size, complexity, cross-border operations or interconnectedness to other financial institutions or to the financial system or economy more broadly. In practice, it is expected that standalone, comprehensive recovery plans will mainly be required for those insurers that are larger and/or more complex in nature, or whose activities, or potential failure, have the potential of having broader systemic impacts. It is recognised that the costs of developing a recovery plan might be relatively high for some smaller, less complex insurers in relation to the prospective benefits.

21. Various approaches have been used or considered to determine the need for a recovery plan. Most supervisors establish a framework with qualitative and/or quantitative factors to assess the need for recovery planning for insurers within their jurisdiction. Factors that may be used include the following:

- The size of an insurer compared to the overall insurance market;
- The importance of an insurer to the broader economy of the jurisdiction;
- The potential systemic activities or exposures of an insurer, for instance exposures to any one investment or investment class that leads to increased vulnerability to common shocks; or
- Whether the insurer offers coverage that cannot be readily replaced, and whether the withdrawal of the insurer from the insurance marketplace would impact policyholders.

22. However, depending also on the level of development of the insurance market, supervisors may choose to decide on a more case-by-case basis.

23. The ICP guidance material does not only relate the proportionality principle to the decision to require a recovery plan, but also to its form, content and level of detail, when

required. This is also true for the ComFrame standard for IAIGs, see Figure 1. When the supervisor decides that a recovery plan is required for a particular insurer, it is expected that the insurer sets up a separate process for the development of the plan to achieve the distinct objective of a recovery plan. As discussed in Section 2, in the preparations of the plan, the insurer may leverage, and should ensure alignment with, existing tools within its ERM framework.

24. Outcomes from the survey indicate that various supervisors require simplified recovery plans, consistent with ICP 16.13. Regarding the **development** of the plan itself, supervisors may apply proportionality, while ensuring that the distinct perspective and objective of recovery planning is maintained in the following ways by:

- Allowing the insurer to use a phased approach for the development of a recovery plan, by drafting the first version of the complete document over a more extended period of time;
- Allowing the insurer to align the timing of the development process with that of existing tools to minimise the needed resources; or
- Varying the level of detail and content requested in the plan, for instance that the insurer may not address all elements of a formal recovery plan as discussed in section 5, or consider detailing fewer recovery options and stress scenarios in the plan.

25. Regarding the **maintenance** of the recovery plan, proportionality could be applied in the following ways, provided that the recovery plan remains usable and effective:

- Varying the frequency for the regular update of the recovery plan, especially when key relevant characteristics have not changed materially year on year; or
- Allowing less frequent monitoring by the insurer of some of the indicators in the recovery plan, such as the status of any non-material entities within a group.

3.2 Matters specific to insurance groups

26. Some matters to consider are specific to group recovery plans, such as supervisory cooperation and coordination, and the scope of application within the group, which (in the case of cross-border groups) is further explained in sub-section 6.2.

27. As the group recovery plan aims to describe how the group as a whole can recover from severe stress, a starting point would be the identification of all group related entities and an assessment of their materiality. This includes the head of the group; the insurance legal entities; the branches; and other regulated entities or non-regulated entities. Those entities that are not material – either financially or operationally - may be excluded from the plan, or the coverage within the plan may be limited to a short description. For material entities, it may be expected that they are covered more extensively in various or all elements of the plan.

28. The following factors may be taken into account when assessing the **materiality** of an entity:

- Its relevance to the group, for instance in terms of revenue, funding, profits or risk profile, but also in terms of the functions that are performed within the entity, like key operational, risk or administrative functions; or
- Its relevance to financial stability and/or the real economy in the jurisdiction in which it operates; and in particular, the extent to which the failure to continue to perform its activities may have a negative impact on either or both.

29. In the case of a cross-border insurance group, a host supervisor may deem it appropriate to require a separate recovery plan for the insurance legal entity in its jurisdiction, particularly in cases where no group recovery plan exists, or the entity in its jurisdiction is not sufficiently covered by a group recovery plan or is particularly important to that jurisdiction. The decision to require a separate recovery plan may be based on factors like size, risk profile and/or level of systemic importance in the host jurisdiction. In such cases, however, it is expected that the host supervisor would cooperate and coordinate with the group-wide supervisor (see section 6).

30. The same process may be applied in the case of financial conglomerates, where the relevant supervisors may deem it necessary to require separate plans for the insurance legal entity or entities, depending on the applicable regulation in the relevant jurisdiction.

4 Governance around recovery planning

31. This section addresses appropriate insurer governance for recovery planning processes. Effective governance for an insurer's recovery planning process should be in written policies and/or procedures that provide a clear and sufficiently detailed description of the operational development process, the approval process, the schedule and process for updating recovery plans, and operational procedures for activation of the recovery plan and any escalation processes.

4.1 Governance – development, approval, review & testing

32. As discussed throughout this Application Paper, recovery planning aims to equip insurers with comprehensive and credible pathways to restoring soundness that are kept up to date and that can be implemented effectively and in a timely manner. To achieve this goal, a formalised governance process around developing, approving and updating the recovery plan will benefit from the participation of the insurer's Board, Senior Management and Key Persons in Control Functions relevant to activation and implementation of the recovery plan. A governance process that includes such active participation in the development of the recovery plan will increase the likelihood that the recovery planning process and the substance of the recovery plans are fully integrated into the insurer's corporate governance arrangements (for supervisory expectations on an insurer's corporate governance arrangements see ICP 7 Corporate Governance) and insurer's ERM.

33. The insurer's governance could benefit from addressing the following elements in policies and procedures regarding **development and approval** of the recovery plan:

- Identification of internal stakeholders, including Board Members, Senior Management and other employees, key to approval, activation and implementation of the recovery plan, and a description of their role and responsibilities. It would be expected that the Board is responsible for the approval of the recovery plan.
- Establishment of development and approval processes with appropriate segregation of duties and controls between those accountable for the development of the plan and those who review and/or approve the plan.

- Consideration of how the development and approval processes and the roles and responsibilities of key participants in those processes integrate and interact with the insurer's overall corporate governance framework.
- Review to ensure that recovery plans are consistent with the overall insurer's ERM and risk appetite.
- Consideration of the order in which the roles and responsibilities of Board members, Senior Management and other relevant Key Persons in Control Functions will occur in the policies and procedures addressing development and approval of the recovery plan.

34. The insurer's governance could benefit from addressing the following elements in policies and procedures regarding **review and updating** of the recovery plan:

- Identification of (key) Board members, Senior Management or other relevant Key Persons, and their roles and responsibilities with respect to reviewing and updating the recovery plan.
- Description of the frequency for review and update of the recovery plan as follows:
    - Timing for keeping the plan up to date through regular review and updates;
    - Factors and considerations for when reviews and updates could be triggered by events internal to the insurer (e.g. significant changes in operations) or by events external to the insurer (e.g. significant change in capital markets that impacts insurer's capital management or liquidity plans), because those events could materially affect the insurer or the viability of the plan.
- Ensuring that any changes to the recovery plan are communicated in a timely manner to relevant parties, including the supervisor.
- Ensuring that the insurer's management information system (MIS) and ERM capture events that would trigger the need to update the recovery plan and do so in a timely manner. An insurer should outline its process for regularly monitoring the internal and external events that could trigger a review and update of the plan.

35. The insurer's governance could benefit from addressing the following elements in policies and procedures regarding **testing** of the recovery plan:

- Establishment of regular tests of the recovery plan to ensure that the plan can be implemented in a timely manner in a stress scenario, that the operational procedures and implementation governance of the plan are effective and that any lessons learned are incorporated into the update process.
  This may be achieved through operational testing of the plan. For example, this type of testing could focus on training for internal escalation processes and communication strategies, or engaging in simulation exercises working through the recovery plan in a time accelerated exercise with relevant key persons.
- The insurer's existing stress testing framework can also be an effective way to test the credibility of the recovery plan, particularly in relation to the menu of recovery options and the calibration of the trigger framework.

4.2 Governance – monitoring, escalation and activation processes

36. The recovery plan should also have an embedded governance process for monitoring and escalating breaches of recovery triggers and for activating the recovery plan, which

includes a description of the key roles and responsibilities of the insurer's Board, Senior Management and Key Persons relevant in the plan, and for stakeholders – including supervisors.

37. A critical element in the ability of recovery plans to achieve their aims is timing. As events and stressors may materialise at short notice and/or within short periods of time (e.g. the occurrence of an earthquake), the ability to recognise that an event or stressor has occurred and to implement the recovery plan in a timely manner are essential. As a result, clear governance policies and procedures around **monitoring, escalation and implementation,** and the timing elements relevant to each, are critical.

38. With respect to **monitoring**, policies and procedures should:

- Ensure that the insurer's information system captures the events mentioned above and does so in a timely manner. An insurer should outline its process for regularly monitoring the range of criteria in its trigger framework. Insurers should be able to demonstrate that appropriate management information systems are in place to support this monitoring process.
- Outline the circumstances in which the insurer would consider an increased level of monitoring.
- Form necessary monitoring and governing committees, such as a crisis management team.

39. With respect to **escalation**, policies and procedures should:

- Clearly identify the process and timing for **escalation** to the Board and Senior Management, upon stress events implicating the possibility of recovery actions; this should include the process required when one or more specific criteria in the trigger framework have been breached.

40. In respect to **activation**, policies and procedures should:

- Clearly identify the process for activation of the recovery plan upon severe stress events, including but not limited to occurrence of the specific criteria in the trigger framework as identified in the plan.
- Identify the roles and responsibilities of Board members, Management and other relevant Key Persons in Control Functions.
- Include plans that ensure that any activation of the recovery plan is communicated in a timely manner to all relevant parties, including the supervisor.

41. The points above emphasize the role of the insurer's Board and Senior Management. The activation of a recovery plan is likely to trigger decisions that significantly affect the insurer. Because of this, recovery plans should not commit an insurer to take any action without the Senior Management or Board first evaluating relevant information and deliberating on the best course of action. It can be helpful for Senior Management and the Board to think through their recovery options through development of operational guides or manuals, but this should not bind or limit the actions taken when stress actually occurs.

42. The recovery plan should outline the circumstances and processes for keeping supervisors notified of an emerging stress scenario and for sharing plans on the recovery options contemplated for implementation, including adequate time and governance controls to ensure that any applicable supervisory approvals are obtained (see also section 5.6). This

is particularly important for insurers with significant cross-border operations, in relation to keeping foreign supervisors and local management notified (see also section 6.2).

5 Elements of a recovery plan

43. The key elements of a recovery plan will often include:

- An **executive abstract** of the most important substantive elements of the recovery plan, most notably of the trigger framework and available recovery strategies;
- A **description of the insurer or group** that outlines the insurer's legal structure, its main activities, and key financial and operational characteristics;
- A **trigger framework** that allows the insurer to identify in a timely manner any emerging risks that may have the potential to threaten its viability;
- A description of its **governance** for recovery planning and utilisation of the plan itself, including the alignment of the plan within existing corporate governance and risk management frameworks;
- A menu of **recovery options**, outlining ways in which the insurer could recover from a severe stress scenario;
- A **communication strategy** to keep supervisors informed and involved, and to help manage the expectations, and/or retain (or restore) the confidence, of market participants and policyholders as necessary; and
- A set of **stress scenarios** to assist in assessing the credibility and feasibility of the recovery plan, notably of the trigger framework and recovery options.

44. The guidance provided in this section can be used both by supervisors and insurers. Supervisors may use it as input for developing more detailed guidelines within their jurisdiction. Insurers, on their part, may find it useful background information when developing or assessing their own recovery plan.

5.1 Executive abstract of the recovery plan

45. It may be useful if the insurer develops a high-level substantive abstract of the main operational components of the recovery plan. This should include a summary of the most significant criteria in the trigger framework (i.e. trigger points), key recovery strategies, and the operational plan for implementation.

46. The purpose of the executive abstract is to serve as a roadmap to the recovery plan to enable the Board and Senior Management to quickly understand and assess the governance, trigger framework, recovery options and communication strategies for effectively responding to a severe stress. It may be helpful to use tables and flow charts to summarise these operational details.

47. It may be useful if the insurer documents a record of all material changes incorporated into the recovery plan as it is updated. This can be a useful reference for the Board and Senior Management when reviewing and using the plan.

48. The executive summary can also serve as a useful aid for supervisors when reviewing and assessing recovery plans because it should reflect any material changes made, and outline the operational components for a credible recovery plan.

5.2 Description of the insurer or group

49. The description should summarize the insurer's operational business structure, key jurisdictions in which it is active, entities covered by the plan, functions and/or services that are significant for the continuation of business, key dependencies or inter-dependencies, and any other relevant information. Examples of functions and/or services that are significant for the continuation of business include shared services (if a group), information technology services, management services and necessary outsourced functions. This will enable all decision-makers and supervisors to assess the implications of different recovery actions for the insurer or all entities in a group, and the group as a whole.

5.3 Trigger framework

50. The trigger framework should identify a set of pre-defined criteria which may trigger the implementation of the recovery plan so as to allow the insurer to successfully monitor, escalate and activate the appropriate range of responses for an emerging stress event.

51. The trigger framework should be aligned with other contingency plans and processes in the insurer's ERM, for example, the ORSA and capital and liquidity management policies. For example, supervisors may observe an overlap between the criteria being monitored under existing capital management policies, stress testing and any contingency plans, including risk metrics and limits defined in the risk appetite.

52. The trigger framework should be used to identify any foreseeable risks that may have the potential to threaten the viability of the insurer, and it should be tailored to reflect the insurer's risk profile and operating environment.

53. The trigger framework should include a broad range of criteria, which are pre-determined and well-defined to prompt timely responses from the insurer. It should operate in a cascading manner to reflect the fact that different levels of response will be required, depending on the circumstances and severity of the stress event.

54. An insurer should establish an appropriate process for regularly monitoring the criteria in its trigger framework. An insurer may choose to use certain criteria (such as a share price movement) as 'early warning indicators' to alert it to emerging risk, and determine that these criteria require heightened monitoring.

55. Other criteria (such as a potential breach of the PCR) may be used as 'trigger points' for informing more intensified responses such as instigating escalation procedures and possible activation of the recovery plan.

56. The framework should include quantitative and qualitative criteria and include a forward-looking element, where possible. For example, the survey showed that effective trigger frameworks may include criteria relating to capital, liquidity, asset quality, profitability, market conditions, macro-economic conditions, and the insurer's operational conditions.

By way of illustration, the insurer may consider incorporating the following types of criteria:

- **Capital**: identify deterioration in the insurer's quantity and quality of capital, including metrics which might be sourced from an applicable capital framework;
- **Liquidity**: identify deterioration in the insurer's capacity to meet its liquidity needs (e.g. capital instrument or other debt maturities), including metrics which might be sourced from any existing liquidity management policies;
- **Asset quality:** identify deterioration in the quality of the insurer's asset mix;
- **Profitability**: capture deterioration in the insurer's financial position due to insurance or investment related losses;
- **Market**: capture deterioration in investment performance and market confidence in an insurer's financial condition, such as CDS spreads, share price movements and rating downgrades;
- **Macro-economic**: identify emerging risks in the insurer's operating environment, such as unemployment rates and property prices; and
- **Operational**: capture operational events which could threaten financial viability, such as a fraud, regulatory fine or cyber-attack.

Box 1: Examples of criteria (quantitative or qualitative)

57. Supervisors should evaluate the trigger framework to determine if it is calibrated to provide enough time for the Board and Senior Management to:

- fully evaluate the circumstances of the stress;
- engage in effective decision-making on the appropriate recovery option(s); and
- implement action on the selected recovery option(s) to effectively respond to the emerging stress event.

58. For example, with regard to capital criteria, supervisors may expect an insurer to calibrate trigger points for activation of the recovery plan at a credible distance from any regulatory minimums, such as the PCR.

59. Stress testing and scenario analysis can provide an important feedback loop into the effectiveness of the trigger framework's calibration, by demonstrating that the trigger framework would be breached in a timely manner that enables effective recovery options to be chosen and implemented.

60. Figure 2 illustrates the relationship between viability, the risk appetite and trigger framework and the nature of actions to be taken in a stylised way. It captures the principles discussed in this section, such as alignment with the ERM and the cascading nature of the criteria. The left-hand (green) part is related to an insurer's risk appetite framework, that generally includes target levels in which the insurer is operating "business as usual". The middle (orange) and right-hand (red) parts of the figure relate directly to the recovery plan, in which criteria are set at cascading levels to indicate emerging stress. The part to the right of the point of non-viability is related to the phase of resolution and is not in the scope of this Paper. The thresholds in the figure are added purely for illustrative purposes.

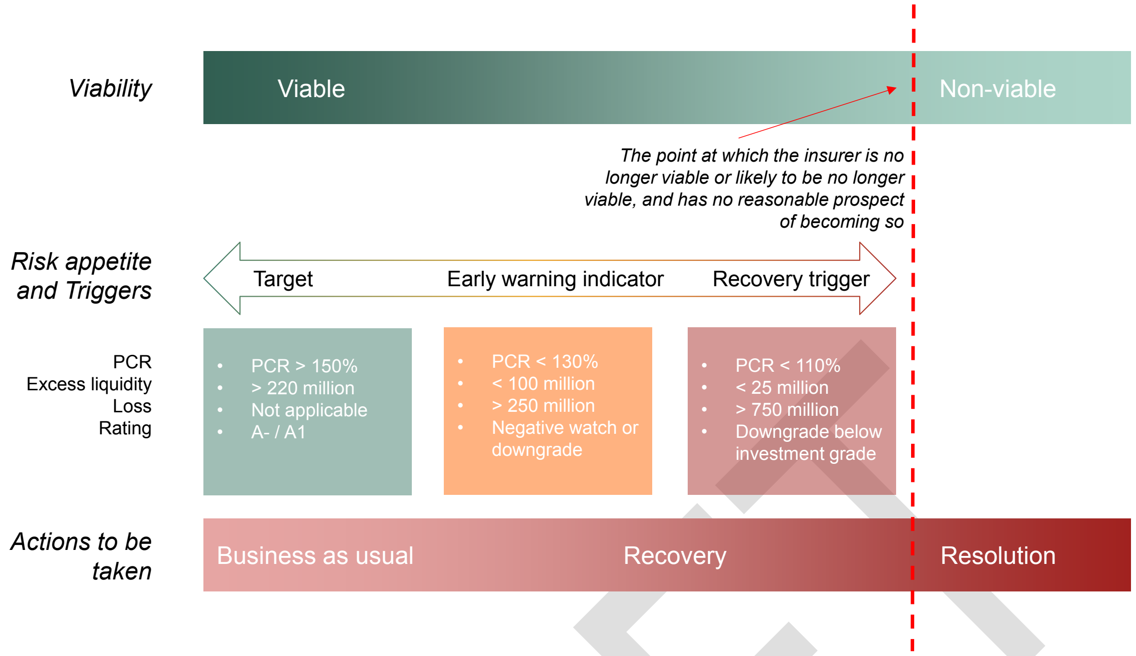

Figure 2. Stylised relationship among recovery triggers, viability and actions to be taken

5.4 Governance

61. The recovery plan should describe the governance for recovery planning and utilisation of the plan itself, including alignment of the plan within existing corporate governance and risk management frameworks, as described in more detail in Section 3. This includes a description of the processes for monitoring, escalating and activating the recovery plan, and a description of the key roles and responsibilities of stakeholders for each part of the governance process.

5.5 Recovery options

62. The core of the recovery plan is the menu of options that an insurer identifies in advance of any stress as potential pathways to effective recovery in the event of a severe stress. This menu of options should be comprehensive, with a focus on options that are able to significantly enhance and restore the capital and/or the liquidity position in times of severe stress. The range of recovery options would usually include acts to: raise capital or other funding, increase liquidity, reduce costs, and enhance risk mitigation. The recovery options may also include options that have permanent structural or strategic implications when necessary. See Box 2 for examples of possible recovery options.

63. The menu of recovery options should be developed without being limited to any specific stress scenario, with the scenario analysis then being used to help assess whether the recovery options provide sufficient recovery capacity across a range of potential stresses.

64. The menu of recovery options should be supported by information required to assess and implement each option, including appropriate strategic, financial and operational analysis. It is important that this analysis is underpinned by realistic assumptions, particularly in relation to pricing and valuation, to properly reflect that the option would be implemented in circumstances of severe stress. Third party evaluations may provide further assurance on the credibility and feasibility of proposed actions.

By way of illustration, the insurer may consider incorporating the following types of recovery options:

- **Strengthening** the insurer's **capital** position: such as recapitalisations, rights issue, institutional or strategic private placements, triggering convertible instruments, inter-fund transfers;
- Actions of **capital conservation**: such as cost containment, suspension of dividends and variable remuneration payments, elimination of major projects;
- **Business strategies**: such as changes to underwriting practices, repricing of insurance contract premiums, re-alignment to reinsurance programmes or other de-risking of the business via e.g. reducing premium volumes;
- **Investment strategies**: such as changes to asset allocation and to hedging programmes;
- Voluntary **restructuring of liabilities**: such as debt-to-equity conversion;
- **Reinsurance** actions: e.g. expanded use of quota share on all or selected business lines or products or whole of account, enhanced adverse development covers;
- **Strategic**: such as run-offs, portfolio transfer arrangements, and sales. These could be solvent run-offs of business lines (particularly those that are non-core), and the sale of strategic investments and of domestic or overseas subsidiaries; and
- **Liquidity**: such as accessing available contingent capital as envisioned in liquidity management plan, more frequent settlement of intra-company balances and deferring or halting unnecessary cash outflows.

Box 2: Examples of recovery options

65. The menu of recovery options should include a **detailed description** for each recovery option identified. Some details that may be considered for inclusion are as follows:

- A summary analysis that reports the essential elements of the option;
- A description of the option;
- Potential adverse consequences arising from the option execution;
- An assessment of the financial impact under business as usual and under stress. For this, it may be appropriate to consider a range of pricing and asset valuation outcomes;
- Speed and timing for the effective execution;
- Any dependency on external counterparties for the effective execution;
- Operational aspects underlying the effective execution, highlighting delegated authorities and approval requirements;
- An assessment of potential impediments and constraints to effective execution, both internal and external; and
- A brief description of any previous experience with applying a certain option, including lessons learned from that experience.

The insurer could utilise a table to summarize this information for ease of use.

66. It may prove helpful to also assess the **compatibility** of recovery options. This will aid the insurer in designing a flexible plan with a wide range of options to respond to different types of stress scenarios. By assessing compatibility, the plan will envision how options can be combined to help the insurer recover from a severe stress. For each option the following aspects are appropriate considerations:

- Whether execution of an option precludes subsequent execution of any other options; and
- Whether execution of an option could potentially impact the scope/full execution of any other options if implemented subsequently.

67. The review of recovery options should be fulsome and wide-ranging, and it may be appropriate to conduct qualitative analyses, and to incorporate expert judgment into this process. In general, options that do not generate material benefits in term of capital or liquidity, or present significant impediments or constraints, are likely to be inappropriate and should be dismissed. Because the insurer is not bound by the recovery options in the plan, it may be helpful for those who would implement the plan to identify any potentially valid options that were considered but dismissed, including a brief explanation of those options and the reason why they were dismissed.

68. Lastly, the insurer may decide to take any preparatory measures to facilitate the implementation of the recovery plan, for instance to overcome any identified impediments to effective execution of a recovery option, or to increase the chance of timely execution of a recovery option. These measures and any progress towards them could be noted in the recovery plan.

5.6 Communication strategy

69. The communication strategy is important for successfully implementing a recovery plan. A communication strategy will ensure effective and clear communications with internal and external stakeholders and will be particularly important in helping to manage external stakeholders' expectations, and retain (or restore) their confidence if necessary.

70. The communication strategy should consider circumstances where confidentiality regarding the impact of the severe stress and implementation of the recovery plan needs to be maintained. There may be circumstances where the implementation of recovery actions should be kept confidential, in consultation with supervisors. When developing the communication strategy, the insurer should be mindful of any legal and regulatory requirements regarding disclosure and confidentiality (see draft revised ICP 20 Public Disclosure).

71. The plan may include tailored communication strategies that recognise the different communication needs depending on the stress scenario and the recovery action(s) being implemented. An effective communication strategy will consider the scope, detail and timing of the disclosures, and the form of communication. The insurer would also need to consider the increased resources (human, facilities, etc) required to support the communication strategy.

72. A communication strategy should consider communication with both internal and external stakeholders, including supervisors, management, staff, key counterparties, policyholders, and investors. Communication with analysts and the press may also be relevant. Depending on the audience and the recovery actions, it may be appropriate to describe the key roles and responsibilities of Board Members, Senior Management, Key Persons in Control Functions as well as relevant business units, such as the communications office, customer service, and supervisors.

73. As part of its communication strategy, the insurer should consider the frequency and detail of updates to the relevant **supervisor(s)**. It would be expected that the insurer informs the supervisor:

- In anticipation of a likely breach of one or more recovery trigger points, including a description of the circumstances leading to the potential activation of the recovery plan;
- Immediately in the event of a breach of one or more recovery trigger points, describing the causes and consequences of such breach. This includes any host supervisors, if relevant (see also section 6.2);
- When a trigger point is breached but the insurer deems that activation of the recovery plan is not necessary, the insurer should fully discuss that decision with the supervisor, explain management's assessment and reasoning for not activating the recovery plan, and advise as to the possible mitigating actions that the insurer intends to execute to restore its position and prevent a further deterioration of the situation. The insurer should also regularly report on the effectiveness of those mitigating actions, and whether further action is required;
- When the recovery plan is activated;
- Periodically after activation of the recovery plan, with updates on the progress and implementation status of the selected recovery options and its effects on the causes of the stress scenario, e.g. the solvency and liquidity positions of the insurer; and
- Finally, once the recovery has been successful and the insurer has moved outside of the recovery zone, it should also give prompt notice to the relevant supervisor(s).

74. The communication strategy with **other external stakeholders**, including investors, analysts, rating agencies and the media, should consider possible options for the detail and timing of information to be provided, and the level and form of communication. These communications may support the effectiveness of certain types of recovery options.

75. Overall, the strategy should address the different tools that the insurer could use, depending on the circumstances and the stakeholder involved, including written notices, press releases, conference calls, and physical meetings. Examples of communication channels for **policyholders** may include:

- Agents and employees who are in direct contact with policyholders (contact centre and customer relationship managers);
- Proactive communication (websites, press releases, email and social networks) in order to ensure real time communication, particularly in the event of an emergency; and
- Reactive communication (inbound calls in Contact Centres, emails, online chats)

76. It is important to recognize that in times of crisis, **employees** may be ambassadors to external stakeholders and will likely need clear and timely updates. Internal and external messages should align, with a fresh and frequent flow of updates to avoid speculation and rumour. These may include establishment of the following:

- Key messages and Q&A for agents and customer-facing employees;
- An insurer message to all employees; and
- Management speaking points for plenary/functional meetings;

5.7 Stress scenarios

77. Recovery plans should include credible options to respond to a range of severe stress scenarios. In this subsection, guidance is given about the stress scenarios primarily based on the experience of various jurisdictions.

78. The use of scenario analysis helps to assess the credibility and feasibility of the recovery plan, including the trigger framework and recovery actions. It also gives insurers and supervisors insights into major risk factors and possible impediments to recovery. Furthermore, scenario analysis may support the decision-making process concerning the recovery actions to be taken after implementation of the recovery plan.

79. It is best for stress scenarios to be severe but plausible, tailored to the risks of the insurer, and result in a serious risk to the viability of the insurer. For example, calibration to represent a near-default scenario, such as a breach of the PCR, would achieve this goal. Additionally, reverse stress testing could be chosen for one or more scenarios.

80. The scenarios should cover clearly defined events that are most relevant to the insurer, taking into account the insurer's risk profile, business model, group structure (if applicable) and other relevant factors, and include:

- Idiosyncratic events, e.g. events that have serious negative consequences for an insurer or group;
- Market-wide or systemic events, i.e. events that may have serious negative consequences for the financial system or real economy; and
- A combination of idiosyncratic and market-wide stress.

The scenarios could include both slow-moving and fast-moving adverse events.

81. Each scenario should calculate the impact on the solvency, capital and liquidity of the insurer and any other relevant entities in the group, as well as what the impact is on the functions and/or services that are significant for the continuation of the insurer. The nature and extent of impacts on the policyholders should also be considered. Other impacts may also be appropriate for consideration/calculation.

82. Furthermore, an effective analysis of the scenario would include an explanation of the criteria in the trigger framework that are breached under each scenario and when this occurred.

83. The insurer should set out which recovery actions it would take in each of the scenarios, taking into account the stressed market conditions in the specific scenarios. This will further the insurer's identification of which recovery actions are less viable in given scenarios. For instance, some recovery actions might be less realistic and viable in a systemic scenario where it is likely that more than one insurer will be seeking to implement similar recovery actions.

By way of illustration, the insurer may consider using the following types of recovery scenarios:

Systemic events:

- A fall in financial markets which is unforeseen, sharp and steep;
- A persistent low interest rate environment;
- A high-impact catastrophic event, such as a pandemic or climate-related event; or
- A longevity shock following a medical breakthrough

Idiosyncratic events:

- Adverse movements in the prices of assets to which the insurer is predominantly exposed;
- Mass lapse;
- The failure of significant counterparties;
- Severe losses through a rogue trader; or
- A major cyber-security attack.

Box 3 : Examples of recovery scenarios

6 Supervisory considerations

84. Recovery plans are developed, maintained and implemented by the insurer; in short, they are owned by the insurer. Supervisors should assess recovery plans and challenge insurers when these plans do not appear to be effective or suitable for the designed purpose of recovery.

6.1 Assessing recovery plans

85. A first key supervisory consideration is having the ability to require amendments to the plans when necessary, and to require being kept informed by the insurers about any changes to the plans or activation of the plans (see Section 5.6). In addition, the supervisor should consider whether it has sufficient quantity and quality of supervisory capacity (e.g. personnel, technology, etc.) to be able to carry out supervisory duties in respect to recovery plans.

86. Supervisors should assess whether recovery plans are satisfactory, considering among other things, if the plans are complete and align with the insurer's risk profile and risk management. Supervisors should assess the quality of the plan, including whether the plan is clear and comprehensive, contains relevant and complete information, is sufficiently detailed, contains a sufficient range of recovery options and is internally consistent (e.g. aligned with other contingency plans and integrated with the insurer's overall risk management framework). In addition, supervisors should assess the credibility of the plan, whether the recovery options identified are implementable (e.g. if a recovery option involves the sale of a subsidiary, whether this can be done expediently and obstacles to implementation have been identified and addressed). Last, but not least, supervisors should assess whether the recovery plan can be implemented in a timely manner.

87. Supervisors should challenge insurers when they feel the quality of the recovery plan does not meet the desired standard, or is not considered to be credible. For example, supervisors may form the view that:

- The stress scenarios provided in the recovery plan are not sufficiently severe, and do not place the insurer under a stress that actually threatens its viability;
- The trigger framework is inappropriate for the purpose of invoking the recovery plan in a timely manner;
- The menu of recovery options is considered to be insufficient;
- The valuations or anticipated execution timeframes of recovery options are not considered to be feasible; or
- The impediments to the recovery plan and/or recovery options have not been adequately considered.

In case the quality of the plan does not meet the desired standard, the supervisor should have the power to require the insurer to resubmit the recovery plan (see also the powers provided by ICP 10).

88. Recovery plans should not be seen by the insurer as a 'compliance exercise' but instead, they should be embedded in the insurer's risk management framework. In this respect, the supervisor can look for evidence of engagement from the insurer's Senior Management and Board in designing, challenging and testing the plan, and whether the plan has been structured as a usable document. The effectiveness of recovery planning can be enhanced if Board Members and Senior Management have engaged with the development of the plan and where the plan is owned by the most senior people in the organisation.

89. Supervisors may find it helpful to assess recovery plans not only at an insurer-by-insurer basis, but also at comparative and at an aggregate basis. Benchmarking recovery plans from different insurers may help in assessing the quality and credibility of the individual plans, while recognising the difference in business models among insurers. Moreover, by looking across the industry, the supervisor may better understand and be able to compare how insurers would react in a stress scenario. For instance, supervisors may find it helpful to assess how an insurer's recovery actions may impact or be impacted by actions of other insurers in cases of market-wide stress, such as a severe market down-turn. This also includes whether each insurer's recovery strategy makes sense and is feasible compared to peers (comparative level analysis and assessment), and whether multiple insurers trying to take similar actions at the same time could lead to contagion (aggregate level analysis and assessment).

90. Supervisors should also require insurers to keep the recovery plan up to date (see section 3.1), and should encourage them to test its usability in practise (see section 4.1).

6.2 Supervisory cooperation and coordination

91. An insurer's recovery planning may have implications beyond the jurisdiction of the insurer. This is the case at least for IAIGs. Whenever recovery planning concerns more than one supervisor, there should be arrangements in place to enable cooperation and coordination among supervisors. Examples of supervisory cooperation and coordination arrangements are supervisory colleges or Crisis Management Groups (CMGs) (see ICP 23 and 25, and the

ComFrame material integrated in it for details on supervisory colleges and Crisis Management Groups respectively).

92. Supervisory cooperation and coordination arrangements contribute to the effectiveness and efficiency of recovery planning at both group and legal entity levels. Further, they should set out, as appropriate, the scope and modalities for cooperation and coordination among supervisors throughout the various stages of recovery planning and action discussed in this Application Paper. Among other things, it may help to identify and address any cross-border elements that may affect recovery planning and action, for example regulatory approvals needed for the execution of a recovery option.

93. Supervisory cooperation and coordination can also help ensure that the interests of each jurisdiction are given due consideration and are balanced appropriately, for example when recovery options contemplate group level funding of cross-border subsidiaries.

94. If multiple recovery plans are created within a group, e.g. recovery plans on a group-level and on a legal-entity level in certain jurisdictions, supervisory cooperation and coordination arrangements should address alignment between the plans, and contribute to identifying and addressing any elements that may affect the effective and efficient interaction between these plans. Also, the group should ensure the consistency of recovery options, indicator frameworks and governance arrangements between group and legal entity level plans, and be transparent about any interdependencies between group and subsidiary-level.

95. For some insurance groups, there may not be supervisory colleges or CMGs in place. In these cases, other arrangements may be considered, for example, the IAIS Multilateral Memorandum of Understanding.

96. Cooperation and coordination in respect to recovery planning may also affect other bodies in addition to insurance supervisors, for example, resolution authorities or policyholder protection schemes. The supervisor should identify these bodies and, as appropriate, consider the establishment of cooperation arrangements with them.