Preliminary Comments:

IAIS Consultation on a Holistic Approach to Systemic Risk

January 15, 2019

Outline

I. Overarching Comments

II. Supervisory Policy Measures -- Liquidity Annex

III. Intervention Powers

IV. Data Gathering

I. Overarching comments

Better foundation to identify and mitigate potential systemic risk
However, merger with EBA creates inconsistencies

- Overall, the holistic approach is much more consistent with how insurers manage risk
    - More granular focus on role of liquidity and interconnectedness (counterparty risk) as transmission channels
    - Recognition of need for more cross-sectoral analysis, particularly for activities that span multiple industries (i.e. derivatives, repos, etc.)
    - Elimination of a binary approach to identification of systemic risk and relevant policy measures
    - Application of proportionality principle for policy measures

- Recognition that exposures must “propagate to other market participants or the real economy” to have a systemic impact. (Section 2.3)

- Clarification that exposure to vulnerabilities “depends on how such an activity is managed.” (Para 59)

- Continued assumption that ABA fails to address domino-type propagation results in inconsistent analysis

II. Supervisory Policy Measures (1)

Comments focused on Liquidity Policy Measures and Annex

- General support for:
  - Focus on short-term liquidity intensive activities.
  - Enhancements to ICP 16 regarding minimum enterprise-wide process to identify, measure, monitor and control liquidity risk including under stressed conditions.
  - Enhancements to ICP 24 for greater macroprudential surveillance regarding liquidity risk, including appropriate stress tests (but bottom up, not top down).
  - Enhancements to ICP 20 for supervisors to have sufficient quantitative and qualitative disclosure regarding material liquidity risks.
  - Strengthen ORSA requirements to raise the importance of sensitivity or scenario analysis.

II. Supervisory Policy Measures (2)

Comments regarding Liquidity Policy Measures and Annex

- Use of a factor-based approach to liquidity risk measurement
  - A cash flow analysis is more appropriate for IAIGs.
  - Tiering assets by timing of sale and prescribing buffers inconsistent with the consultation's recommendation to have each firm establish its own risk appetite and does not allow for supervisory judgement.
- Use of a top-down approach to liquidity stress testing
  - A bottoms-up approach is needed so that each firm can tailor its liquidity stress testing framework, including stress scenarios, to its specific liquidity risk profile. Top-down approaches typically assume that "one size fits all."

III. Intervention Powers

Concerns regarding section 3.5

- Definition of powers for insurance supervisor “in response to the build-up of systemic risk” is very broad and, as presented, would represent a significant expansion of supervisory powers
- The principles of proportionality and conditionality are referenced, but without any clearly defined “supervisory ladder”
  - More justification is needed for a stay of redemptions than additional reporting on liquidity/systemic risk.
  - More severe measures must be tied to an insurer’s condition, activities or compliance with microprudential requirements.
  - Reference to intervention powers as “state specific” is insufficient and greater conditionality is needed.
  - More generally, some of the powers mentioned are generic and do not articulate how they would address a relevant systemic risk transmission channel.
- Lack of clarity regarding availability of measures could create uncertainty and disrupt well-established market expectations

IV. Macroprudential Surveillance, Global Monitoring and Data Gathering (1 of 2)

Proposed changes to data and analytical process:

Refine approach to macroprudential surveillance and global data gathering consistent with appropriate identification of sources of systemic risk in order to ensure an effective and efficient targeting of risks linked to the agreed systemic risk transmission channels,

- Data gathered should allow for analysis of how it would like to an established systemic risk transmission channel
- Clarification that exposure to vulnerabilities "depends on how such an activity is managed." (Para 59) and whether adequately addressed by existing microprudential regulation
- More analysis needed to understand data in the context of the overall balance sheet and relevant risk management practices – i.e. potential liquidity demand must take into account amount and quality of collateral as well as overall contingency funding and liquidity of assets
- Despite continued recognition for need of more absolute assessment of potential systemic relevance compared to entire market, little progress
- Measurement and analysis should create right incentives by rewarding good risk management and identifying where greater risk is being taken

IV. Macroprudential Surveillance, Global Monitoring and Data Gathering (2 of 2)

Proposed changes to governance process:

Ensure careful planning, guidance and coordination of the several monitoring exercise to avoid multiple demands for similar but slightly different data points given the burden and cost to companies.