INTERNATIONAL ASSOCIATION OF
INSURANCE SUPERVISORS

Public

Supervisory issues associated with benchmark transition from an insurance perspective

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About the IAIS

The International Association of Insurance Supervisors (IAIS) is a voluntary membership organisation of insurance supervisors and regulators from more than 200 jurisdictions. The mission of the IAIS is to promote effective and globally consistent supervision of the insurance industry in order to develop and maintain fair, safe and stable insurance markets for the benefit and protection of policyholders and to contribute to global financial stability.

Established in 1994, the IAIS is the international standard setting body responsible for developing principles, standards and other supporting material for the supervision of the insurance sector and assisting in their implementation. The IAIS also provides a forum for Members to share their experiences and understanding of insurance supervision and insurance markets.

The IAIS coordinates its work with other international financial policymakers and associations of supervisors or regulators, and assists in shaping financial systems globally. In particular, the IAIS is a member of the Financial Stability Board (FSB), member of the Standards Advisory Council of the International Accounting Standards Board (IASB), and partner in the Access to Insurance Initiative (A2ii). In recognition of its collective expertise, the IAIS also is routinely called upon by the G20 leaders and other international standard setting bodies for input on insurance issues as well as on issues related to the regulation and supervision of the global financial sector.

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This document was prepared by the IAIS Secretariat in consultation with IAIS Members and approved by the Executive Committee in June 2020. The IAIS report was developed in close cooperation with the Financial Stability Board (FSB) and Basel Committee on Banking Supervision (BCBS); it is a complement to the FSB-BCBS report and supports its recommendations for LIBOR transition.

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Contents

1. Executive summary

This report presents to the G20[1] the findings from the survey on supervisory issues related to LIBOR transition distributed to IAIS members[2], similar to the survey distributed to BCBS and FSB members and to non-FSB members in FSB Regional Consultative Groups (RCGs) (FSB Report). The key findings and recommendations identified from the survey responses provided by insurance supervisors are largely consistent with those of the FSB Report, albeit with a few points specific to the insurance sector. Findings that are specific to the insurance sector arise particularly from the fact that insurers are exposed to transition risks on both sides of the balance sheet (for example, through the valuation of both their assets and liabilities).

The aim of the IAIS survey, similar to the FSB-BCBS survey, was to improve collective understanding of progress made so far with LIBOR transition and to increase awareness of the importance of ensuring timely transition.

The focus of the IAIS Report is on LIBOR transition, given its predominant global role and the short remaining period for transition, as also pointed out in the FSB Report. The FSB Report however recognises that the use of alternative reference rates should be encouraged across global interest rates markets were appropriate, and its recommendations may also be considered by jurisdictions in reducing reliance on other IBORs. This is supported by IAIS members.

Both the survey and the initial analysis were undertaken before the Covid-19 pandemic and therefore do not reflect any potential issues linked to its impact. In its statement responding to the impacts of Covid-19 on financial stability, the FSB has noted that LIBOR transition is a G20 priority and remains an essential task that will strengthen the global financial system. The FSB recognises that some aspects of firms' transition plans are likely to be temporarily disrupted or delayed by Covid-19, while others can continue. Covid-19 has highlighted that the underlying markets LIBOR seeks to measure are no longer sufficiently active. The FSB maintains its view that financial and non-financial sector firms across all jurisdictions should continue their efforts in making wider use of alternative reference rates in order to reduce reliance on IBORs where appropriate and in particular to remove remaining dependencies on LIBOR by the end of 2021. In this light, authorities may need to fundamentally review their readiness to implement some of the recommendations in this report, and, if necessary, revise their plans accordingly to be prepared to work on an even more compressed timeline when the pandemic situation has stabilised.

Similar to the FSB-BCBS survey, based on the responses received, the IAIS has identified a number of recommendations adopted by authorities to address LIBOR transition challenges.

[1] This report is submitted to the July 2020 G20 Finance Ministers and Central Bank Governors meeting.
[2] Respondents to the IAIS survey have reviewed the IAIS Report and commented on the characterisation of their responses. The IAIS Executive Committee approved the IAIS Report on 11 June 2020.

Some of these recommendations have already been adopted by authorities that are more progressed in LIBOR transition. A wider implementation of these recommendations by jurisdictions could facilitate a more effective and coordinated transition globally.

This report recommends that insurance supervisors, SSBs, international bodies or other relevant stakeholders adopt or strengthen these recommendations in order to make further progress in transitioning away from LIBOR. While the recommendations should generally be applicable to all jurisdictions with LIBOR exposures, a proportionate and risk-based approach should be pursued in practice.

Recommendations are grouped under three areas: (i) identification of LIBOR exposures and transition challenges; (ii) transition facilitation; and (iii) supervisory cooperation and coordination.

In light of the expected cessation of LIBOR after end-2021, insurance supervisors should strengthen their efforts in facilitating insurers to transition away from LIBOR. Given that benchmark transition would have significant cross-border implications, there is a greater need to step up the coordination and monitoring effort at an international level. In this regard, the next steps of the FSB, which are supported by IAIS members, are:

- Further assessing transition progress by applying a simple set of key indicators and qualitative questions to monitor implementation of the below recommendations; and
- Monitoring the evolving impact of the Covid-19 pandemic on on-going benchmark transition.

2. Summary of key findings

In terms of coverage, the analysis is based on the 22 responses that were received from IAIS members, which provide an insurance perspective on supervisory issues associated with benchmark transition. The completeness and level of detail of the submitted responses vary across jurisdictions. For jurisdictions that have not identified any significant risks due to LIBOR transition, this may be due to insufficient information being available to support a definitive judgment.

Insurance sector exposures to LIBOR

- In terms of exposures, insurers' exposures to LIBOR are overall limited, but might be more concentrated in certain insurers depending on their geographical location, balance sheet structure, business model, products and size. A distinction needs to be made between the insurance sector asset- and liability-side exposures to benchmarks.[3]

- On the asset side, insurers are exposed through their investments in instruments linked to LIBOR (and alternative reference rates such as SONIA, SOFR, TONAR, SARON[4]). For insurers, various types of exposures to LIBOR are linked to cash products, bonds and loans, issuance of bonds and loans, derivatives (interest-rate swaps), floating rate notes, collateralised loan obligations (CLOs), and securitised transactions.
- Insurance sector asset-side exposures in jurisdictions with LIBOR currencies (USD, GBP, EUR, CHF and JPY) are in general found to be higher than those in non-LIBOR currency jurisdictions. In Europe, most of the concentration with respect to LIBOR-related assets is in one jurisdiction.
- On the insurance liability side, no material exposures to LIBOR was identified by insurance supervisors, except in one jurisdiction where close to all of the insurance liabilities are exposed to LIBOR, due to the valuation methodology.

Transition strategy and monitoring

- Approximately half of the responding jurisdictions indicated that there is no material exposure to LIBOR in their insurance markets and hence did not report to have a transition strategy in place. Other jurisdictions are still in the process of executing a work plan to analyse the LIBOR exposures. Reported transition plans, particularly from LIBOR currency jurisdictions, typically include improving awareness and providing guidance to market participants, monitoring transition progress via surveys and information requests to the insurance markets, outlining responsibilities and expectations with insurers, coordination of national working groups (NWGs), and coordination with other domestic and international bodies.

Major challenges and risks for insurers with LIBOR transition

- From a micro-prudential perspective, similarly to the findings from the FSB-BCBS survey, transition risks may arise from the operational, legal, prudential, conduct, hedging and accounting perspectives.
- Key transition challenges that have been identified include the need to develop further cash products, not linked to LIBOR, and concerns about lack of liquidity in alternative reference rates, complexities in adopting fallback language, and the dependence on

[3] This is based on the qualitative responses from insurance supervisors. In the BCBS-FSB survey, while some jurisdictions provided an additional level of breakdowns on exposures, this was mainly for different types of banks and differentiating between FIs and Non-FIs. No split was provided for the insurance sector.

[4] Sterling Over Night Index Average (SONIA), Secured Overnight Financing Rate (SOFR), Tokyo Overnight Average Rate (TONAR), Swiss Average Rate Overnight (SARON)

concrete alternatives offered by financial intermediaries and clients' willingness to adjust.

- A major benchmark transition challenge identified was around the difficulties in developing fallback provisions; the lack of standardised fallbacks for cash products (e.g. bonds, loans) means that these may need to be renegotiated individually. This could potentially result in a heavy legal workload to adjust contracts and financial documents that use LIBOR as a reference rate, involving significant operational and legal risks. Other key benchmark transition risks include the increased market risk and a negative impact on product pricing if hedging strategies result in more basis risk, for example should the loan and derivative markets adopt different approaches for new reference rates. Potential further basis risk could be introduced on insurers' balance sheets when their assets transition to a benchmark that would be different from the benchmark used to value their liabilities.
- Other risks mentioned include:
  - uncertainty and possible effects on the eligibility of capital instruments and capital requirements;
  - an insufficient rate of transition in certain benchmark rates, which could form a barrier to transitioning cross-currency positions and certain futures contracts (market not deep enough);
  - the lack of liquidity in alternative reference rates
  - the lack of term rates for alternative reference rates; and
  - concerns about increased lapses of insurance contracts during the challenging process of agreeing contract amendments and negotiating new contracts under the new rates.

Supervisory actions and other initiatives

- Similar to non-insurance supervisors, most insurance supervisors have not set targets and deadlines for insurers to transition from LIBOR to alternative reference rates. However, several jurisdictions reported supporting the private sector to develop their own targets. Authorities in LIBOR currency jurisdictions are relatively more advanced in taking initiatives to facilitate and monitor benchmark transition, which include sending "Dear CEO" letters, requesting or encouraging insurers to set internal targets and deadlines for transition to LIBOR alternatives and carrying out desktop reviews or on-site examinations.
- On-site examinations to assess individual insurers' preparedness for benchmark transition typically focus on the largest insurers and are aimed at identifying exposures and assessing the readiness to use alternative benchmark rates.

Need for strengthened supervisory actions and in particular cross-border supervisory coordination

- Similar to the findings from the FSB-BCBS survey, the IAIS survey points out that insurance supervisors are likewise concerned about potential inconsistencies with the implementation of benchmark reforms domestically and across international markets, in terms of timing and approach. Examples of particular concerns are multi-currency products such as cross-currency swaps and balance sheet hedges.
- Insurance supervisors therefore see the need for international coordination around the expectations and timings of LIBOR transition. By directing financial institutions away from LIBOR in a coordinated manner, insurance supervisors expect to increase transition effectiveness (avoiding any further strain on resources, modelling complexity and bilateral negotiations) as well as to preserve the international level playing field.

3. Recommendations to support benchmark transition in the insurance sector

Similar to the FSB-BCBS survey, based on the responses received, the IAIS has identified a number of recommendations to address LIBOR transition challenges. Some of these recommendations have already been adopted by authorities that are more progressed in LIBOR transition. A wider implementation of these recommendations by jurisdictions could facilitate a more effective as well as a more coordinated transition globally. This report recommends that insurance supervisors, SSBs, international bodies or other relevant stakeholders adopt or strengthen these recommendations in order to make further progress in transitioning away from LIBOR. While the recommendations should generally be applicable to all jurisdictions with LIBOR exposures, a proportionate and risk-based approach should be pursued in practice.

Recommendations are grouped under three areas: (i) identification of LIBOR exposures and transition challenges; (ii) transition facilitation; and (iii) supervisory cooperation and coordination.

Finally, a common theme identified, also in line with BCBS-FSB, is the deployment of sufficient resources to LIBOR transition: Supervisory authorities in the financial sector are encouraged to dedicate adequate resources and capacity to identify, monitor and facilitate the transition where necessary.

3.1 Identification of LIBOR exposures and remaining transition challenges in the insurance sector

- Insurance supervisors closely monitor LIBOR transition and actively reach out to the sector based on a risk-based approach, given LIBOR exposures seem to be more concentrated in certain insurers depending on their geographical location, balance sheet structure, business model and size.

- Insurance supervisors issue public statements as well as letters and/or follow-up letters to CEOs to promote awareness of LIBOR cessation and associated risks, both within insurers and across the financial system. In particular, further efforts are needed to enhance awareness and preparedness among smaller insurers.
- Insurers' risk management includes the identification of LIBOR-referenced contracts and an assessment of the impact on infrastructure and operations in an appropriate manner.
- Supervisory authorities in a jurisdiction jointly establish a formal integrated LIBOR transition strategy across the domestic financial sector, including evaluating the need and then undertaking regular surveys to monitor financial institutions' exposure to LIBOR, including insurers, and to identify possible areas of risk concentration.
- Insurance supervisors request, as part of insurers' risk management and reporting, a board-level summary of key risks and action plans related to LIBOR transition, steps already taken and designated senior management responsible for transition.
- Insurance supervisors particularly expect exposed insurers to regularly monitor and report major LIBOR-transition related risks, such as
  - lack of liquidity in alternative benchmark rates;
  - lack of term rates for alternative benchmarks and challenges in agreeing contract amendments;
  - exposures linked to underlying funds referenced to LIBOR in unit-linked insurance products; and
  - increased lapses of insurance contracts during the process of negotiating new contracts under the new rates.
- Supervisory authorities in the financial sector, the IAIS and other relevant SSBs jointly engage with industry and professional associations to raise awareness on the potential impact of LIBOR discontinuation, including potentially affected non-financial sector institutions, and provide information that may help the transition as well as identifying transition risks.

3.2 Facilitation of LIBOR transition

- Insurance supervisors communicate clearly to insurers on the timing of the change for new contracts from LIBORs to alternative reference rates.
- Insurance supervisors provide further regulatory clarifications or supervisory guidance to facilitate the transition, for instance, on legacy contracts that are difficult to be actively converted (e.g. due to a lack of robust fallbacks), the transition roadmap and

conduct-related issues. This could include setting out milestones to facilitate the transition and clarify actions market participants should take within the roadmap. Standardised fallbacks, such as those developed by industry associations in cooperation with SSBs, for cash products (e.g. bonds, loans) could help avoid individual renegotiations, which would not only involve a heavy workload but also expose insurers to significant operational and legal risks.

- Insurance supervisors maintain regular dialogue with insurers to discuss transition plans, and progress against set timelines or milestones as well as the readiness of internal and external systems.
- Insurance supervisors carry out further desktop reviews or on-site examinations, with potential coverage of
  - types and levels of LIBOR exposures;
  - transition plans and milestones;
  - governance over the transition work; and
  - progress of negotiation with counterparties on LIBOR-referenced contracts.

3.3 Supervisory cooperation and international coordination

- Insurance supervisors jointly promote financial sector-wide coordination by sharing latest developments and best practices on transition, for instance, via established or newly created NWGs with a diverse membership of insurers, other financial institutions, non-financial institution corporations and corporate treasuries and industry associations representing various markets (e.g. derivatives, bond and syndicated loan markets).
- Insurance supervisors maintain dialogue with NWGs and/or industry associations (domestically and internationally), particularly focusing on the adoption of fallback language for various products and identifying steps that would facilitate the developments where necessary.
- Insurance supervisors consider working with relevant financial sector supervisors to identify legislative solutions, where necessary, to mitigate exposures of legacy contracts that have no or inappropriate fallbacks, and cannot realistically be renegotiated or amended.
- Insurance supervisors exchange information on best practices and challenges, as well as on progress across jurisdictions through the work of international fora such as the IAIS and/or existing supervisory channels (e.g. supervisory colleges).
- International bodies, SSBs and supervisory authorities encourage financial institutions, including insurers, to maintain a good understanding of wider market developments (in particular the discussion of output of NWGs and international bodies).

4. Next steps

The results of the FSB-BCBS questionnaire have shown gaps in quantifying LIBOR exposures and the status of fallback adoption and therefore it would be difficult to comprehensively assess the impact on financial stability arising from LIBOR transition. On transition progress, the survey results show that a considerable portion of financial institutions including insurance companies across jurisdictions have yet to start or are still planning on the transition. In light of the expected cessation of LIBOR after end-2021, insurance supervisors should strengthen their efforts in facilitating insurance companies to transition away from LIBOR. Given that benchmark transition would have significant cross-border implications, there is a greater need to step up the coordination and monitoring effort at an international level. The next steps of the FSB, supported by IAIS members, are:

- The FSB, in collaboration with the IAIS and other SSBs and international bodies, will design a simple set of key metrics or indicators to update global LIBOR exposures and transition status, and identify a list of qualitative questions to monitor the progress in implementing the above recommendations. The aim is to provide another assessment of the transition progress to SRC by early next year.
- The IAIS will contribute to the FSB's continued monitoring of the evolving impact of the Covid-19 pandemic on ongoing benchmark transition, the findings of which will be incorporated into the FSB's annual progress report on implementation of recommendations to reform major interest rate benchmarks (to be published before the G20 meeting in November).

5. Detailed findings derived from the responses submitted to the survey

The aim of this chapter is to provide a detailed overview of the most important findings extracted from the IAIS survey of insurance supervisors on the prudential and supervisory implications of benchmark rate reforms in the insurance sector. The survey was launched on 20 January 2020 to the IAIS main representatives, with a deadline for completion by 7 February 2020. The responses from 22 IAIS Members and the resulting key findings were discussed in the Policy Development Committee (PDC) and the Executive Committee (ExCo) on 24 and 26 February, respectively.

The aim of the IAIS survey, similar to the FSB-BCBS survey, was to improve collective understanding of progress made so far with LIBOR transition and to increase awareness of the importance of ensuring timely transition.

The limitations of the survey should be considered when interpreting the analysis and its conclusions. The completeness and level of detail of the submitted responses vary across jurisdictions. For jurisdictions that have not identified any significant risks due to LIBOR transition, this may be due to insufficient information being available to support a definitive judgment.

The findings are grouped under the following five areas: (i) insurance sector exposure; (ii) transition progress monitoring by insurance supervisors; (iii) supervisory approach and actions; (iv) cross-border issues and (v) insurance liability valuation.

5.1 Insurance sector exposures to LIBOR

Finding 1: Insurance companies' exposures to LIBOR depend on their location, balance sheet structure, products and size.

Different exposures in different markets

Insurance sector exposures in jurisdictions with **LIBOR currencies** (USD, GBP, EUR, CHF and JPY) **are in general more exposed** to LIBOR than insurance sectors in non-LIBOR currency jurisdictions.[5]

In Europe, most of the concentration with respect to LIBOR-related assets is in the UK. The European Insurance and Occupational Pensions Authority (EIOPA) states that the impact of LIBOR changes on assets in European Union Member States with a large insurance sector are not expected to be material.

Distinction between asset and liability side

Asset-side exposures to LIBOR:

- Insurers invest in instruments linked to LIBOR (and alternative reference rates such as SONIA, SOFR, TONA, SARON).
- Different types of exposures to LIBOR by insurers are cash products, bonds and loans, issuance of bonds and loans, derivatives (interest-rate swaps), floating rate notes, CLOs, securitised transactions.

Liability-side exposures to LIBOR: **No material exposures** identified by respondents, **except in the UK** (close to 100% due to reliance on the EIOPA pound sterling risk-free risk curve, which is based on LIBOR).

Distinction between large and smaller insurers

Supervisors monitoring insurance sector exposures to LIBOR differentiated between progress made by:

- **Large insurers**, who in general are observed to be **taking action** to transition away from LIBOR; and

[5] Some risk-free rates in non-LIBOR currencies also rely on LIBOR, and would hence be affected by LIBOR discontinuation.

- **Smaller insurers**, where either:
- No significant exposures have been observed; or
- There is insufficient awareness of LIBOR exposures and/or insufficient capacity to transition away from LIBOR (relating to the costs).

5.2 LIBOR transition progress monitoring work conducted by insurance supervisors

Finding 2: The progress of transition away from LIBOR differs across markets, depending on the observed materiality of the exposures.

Approximately half of the responding jurisdictions indicated that there is **no material exposure** to LIBOR in their insurance markets.

Some jurisdictions are still in the process of executing a work plan to analyse the LIBOR exposures.

Insurance supervisors in other jurisdictions are either taking action or have observed other parties taking action, including:

- Bilateral engagements of supervisors with individual insurers;
- Industry-wide communications and information requests by supervisors, involving industry associations; and
- Setting-up cross-sectoral working groups or task forces at the national level (e.g. £RFRWG[6] in the UK).

Some jurisdictional examples include:

- In the US, the SOFR has been effective since April 2018. Since this date, SOFR-linked transactions have grown significantly.
- In the UK, industry-wide communications and information requests have been sent out; bilateral engagements with the largest insurance firms took place in Q4 2019.
- In Switzerland, the Financial Market Supervisory Authority (FINMA) guidance on LIBOR transition was published in 2018. FINMA also performed a self-assessment survey in 2019 covering more than 60% of the Swiss Life and Non-Life markets and undertook bilateral meetings with insurance entities.
- In Singapore, the Monetary Authority of Singapore (MAS) issued a further survey in early March 2020 to obtain an update on insurers' exposure to LIBOR and the SGD Swap Offer Rate (SOR). MAS will potentially take a targeted approach subsequently to follow up with insurers with significant exposures in order to accelerate transition.

[6] Pound Sterling Risk Free Rate Working Group (£RFRWG)

- In Chinese Taipei, a thematic survey is being carried out across the insurance sector and the relevant analysis is expected to be finished by the end of April 2020.
- In the European Union (EU), EIOPA is seeking to adopt a common approach across the EU to the transition to new benchmark rates and a discussion paper was published on 6 February 2020 in order to address the subject of the ongoing changes to the new benchmark rates (IBOR transitions).
- In Japan, several insurers are working on the identification of systems that need to be updated for purposes of benchmark transition.

Finding 3: Jurisdictions monitoring progress of including fallback provisions under existing LIBOR contracts acknowledge that, for certain cash investment products, the use of fallback provisions is still limited.

Most of the responding jurisdictions had **no detailed observations** in terms of progress by insurers in including fallback provisions under existing LIBOR contracts.

Some jurisdictional examples include:

- In the US, SOFR has been in place since April 2018. However, industry products that rely on LIBOR are different both in nature and in LIBOR fallback approaches (derivatives, floating rate notes, CLOs, securitised transactions and private placements).
  - Fallback triggers exist for new derivatives (ISDA) and certain cash products (either hardwired using SOFR or determined by calculation agents), but the market has not selected a single approach. These differences can give rise to basis risk.
- In Hong-Kong:
  - For loan-related contracts, insurers are managing the transition from LIBOR to alternatives through reference to the steer from the Loan Sales and Trading Organization.
  - For derivatives-related contracts, insurers are staying abreast of fallbacks being proposed by International Swaps and Derivatives Association and anticipate adherence through their future protocol(s).
  - Some insurers expect to rebase to SOFR.
- In the Netherlands, insurers are mostly preparing for a number of scenarios (for example, EURIBOR[7] is replaced by hybrid EURIBOR or €STR[8], or generally the transition to a new reference benchmark).

[7] Euro Interbank Offered Rate (EURIBOR)
[8] Euro Short-Term Rate (€STR)

- In South Africa, in certain instances, insurers' contracts that contain clauses which assist with an easy transition to alternative reference rates are available. Some insurers indicated that they have LIBOR-linked contracts in their shareholder guaranteed portfolios.
- In Japan, the use of fallback provisions is still limited. The Financial Services Agency (FSA) expects financial institutions, including insurers, to use fallback provisions more widely.
- Korean insurers are in the process of developing fallback provisions in connection with the renewal of existing contracts or entry into new contracts.
- In the UK, the joint Prudential Regulatory Authority (PRA) and Financial Conduct Authority (FCA) outreach to firms should, in the near future, provide data to assess the progress on including fallback provisions; however this is not yet available.

Finding 4: Insurance supervisors observe that larger insurers have generally taken steps to take into account LIBOR transition in their governance framework and organisational structure, including:

- Establishing and documenting internal processes.
- Establishing organisational structures to manage the transition (e.g. dedicated programs and or project teams).
- Keeping executive members continually informed about developments within their organisations.
- Establishing legal teams for the review of the insurer's contractual obligations.
- **Most** insurance supervisors in the responding jurisdictions, however, **have no initial observations** and findings on insurers in terms of the extent to which they have taken into account LIBOR transition in their governance framework and organisational structure.

5.3 Supervisory approach and actions

Finding 5: Insurance supervisors have identified the following key challenges and risks with LIBOR transition:

- Inconsistencies with the implementation of benchmark reforms locally and across international markets, in terms of timing and approach, which adds further strain on resources, modelling complexity and bilateral negotiations.
  - The varied nature of alternative reference rates selected (collateralised vs. uncollateralised) makes migration across products and jurisdictions challenging from a risk management and hedging perspective; and
  - Varied and uncoordinated transition timelines could impact how benchmark discontinuation affects multi-currency products such as cross-currency swaps (for

instance, if the respective legs of the transaction reference different benchmark rates, these could transition at different times), and balance sheet hedges (if assets and liabilities transition at different times).

- **Difficulties in developing fallback provisions**. The lack of standardised fallbacks for cash products (e.g. bonds, loans) means that these may need to be renegotiated individually.
- **Heavy legal workload to adjust contracts and financial documents that use LIBOR as a reference rate,** involving significant **operational and legal risks**, including:
  - Renegotiation of legal contracts, which will **impact resources** and may result in additional costs; and
  - **Conduct risk**, as potential value transfer could occur when amending contracts to reference or fallback to alternative reference rates. This may lead to disputes/litigation. Asymmetry of information available to banks and non-bank entities may also give rise to a perceived risk of collusion and lead to **legal and reputational risk**.
- **Increased market risk** and a negative impact on product pricing if hedging strategies result in more **basis risk,** should the loan and derivative markets adopt different approaches for new reference rates.
- **Insufficient data with respect to alternative reference rates**. For most insurers, this would be an asset management issue primarily in their capacity as institutional investors.
- **Other risks** which were mentioned include:
  - Uncertainty and possible effects on capital instruments (eligibility) and requirements;
  - Insufficient rate of transition in SOFR is a barrier to transitioning cross-currency positions and certain futures contracts (market not deep enough);
  - **Lack of liquidity** in alternative reference rates;
  - **Lack of term rates** for alternative reference rates and challenges in agreeing contract amendments;
  - **Lack of clarity** on a replacement Solvency II discount curve. Potential basis risk between switching to SONIA-based assets whilst holding LIBOR-discounted liabilities;
  - **Lack of clarity** about timelines and the ultimate outcome of the transition exacerbates these risks;
  - Exposures linked to underlying funds referenced to LIBOR in unit-linked insurance products; and

– Concerns about increased **lapses** of insurance contracts during the process of negotiating new contracts under the new rates.

Finding 6: Most supervisors have not set targets and deadlines for insurers to transition from LIBOR to alternative reference rates. While most supervisors are not planning to conduct on-site examinations to assess individual insurers' preparedness for benchmark transition, there are examples of some supervisors who intend to do such assessments through either on-site examinations or regular supervisory activities.

Specific examples of supervisors setting targets and deadlines and carrying out on-site visits or regular supervisory activities for purposes of monitoring benchmark transition preparedness include:

- UK PRA has set a series of targets for 2020. The planning assumption for all UK firms is that LIBOR will cease after end-2021, when LIBOR submissions will no longer be mandated by the FCA.

  The UK £RFRWG has set a series of targets for 2020, including to:

  – Enable a further shift of volumes from LIBOR to SONIA in derivative markets, supported by a statement from the Bank of England and FCA encouraging a switch in the convention for sterling interest rate swaps from 2 March 2020;

  – Require lenders to be in a position to offer non-LIBOR linked alternative products to customers by Q3 2020 and require lenders to include contractual arrangements to convert new and re-financed LIBOR-referencing loans ahead of end-2021;

  – Cease issuance of loan products linked to sterling LIBOR by end-Q1 2021; and

  – Significantly reduce the stock of LIBOR-referencing contracts by Q1 2021.

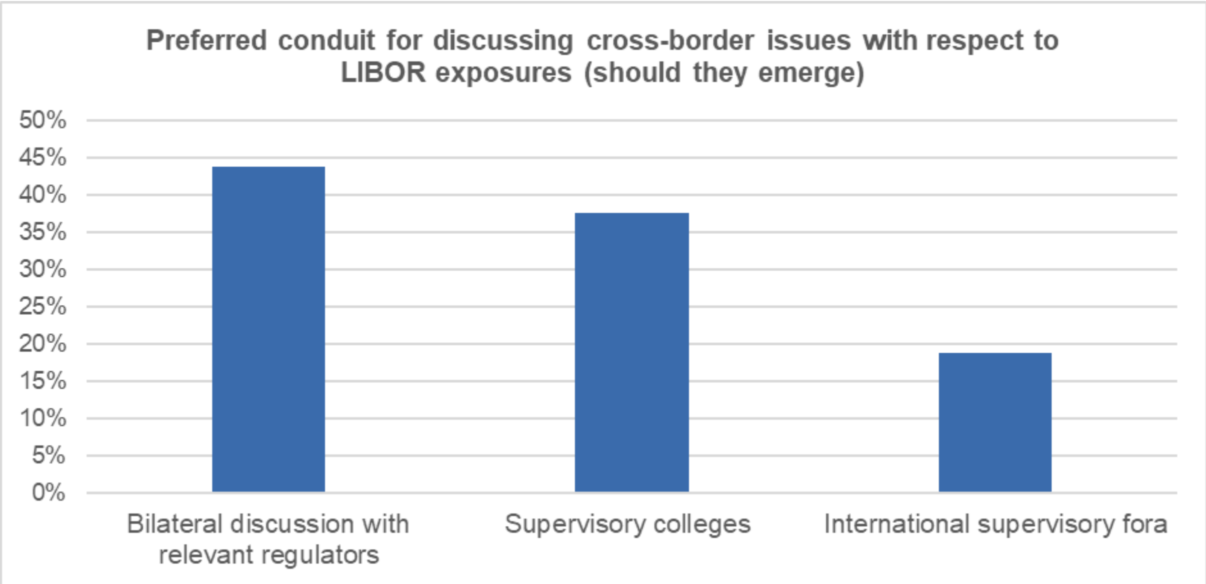
- On-site examinations to assess individual insurers' preparedness for benchmark transition (JP, UK, SA) focus on the largest insurers and are aimed at identifying exposures and assessing the readiness to use alternative reference rates.
- In the US, while some States may perform some work during on-site examinations, most of the work performed by supervisors is expected to be through inquiry, either formally in writing or informally during the analysis process, depending upon the State's sense of preparedness. The Federal Reserve monitors preparedness during the course of regularly scheduled supervisory activities.

5.4 Cross-border issues

Finding 7: Insurance supervisors seeing the need for cross-border supervisory coordination and cooperation state it should target the following objectives:

- **Raising awareness** among all market participants.
- **Coordinating expectations and timings:** Ensuring a consistent implementation of benchmark reforms locally and across international markets, in terms of timing and approach to avoid adding further strain on resources, modelling complexity and bilateral negotiations.
- Removing regulatory barriers to the transition from LIBOR[9].
- Increasing the **effectiveness** and **level-playing field** by directing financial institutions away from LIBOR in a coordinated manner.
- Avoiding challenges that could arise where **one currency is transitioning away from LIBOR at a different rate from the other**.
- In case of cross-border transition failure: Seeking support, advice and potentially corresponding action from relevant micro- and macroprudential authorities in other jurisdictions.

Finding 8: Insurance supervisors prefer the following conduit for discussing cross-border issues with respect to LIBOR exposures, should they emerge:



[9] For example, the lack of clarity on a replacement Solvency II discount curve was cited as a key barrier to transition. Related to this, respondents also noted potential basis risk between switching to SONIA-based assets whilst holding LIBOR-discounted liabilities.

5.5 Insurance liability valuation

Finding 9: Most insurance supervisors report a non-material percentage of insurance liabilities subject to valuation principles set out in regulation that rely on LIBOR, except for the UK, where close to 100% of insurance liabilities rely on LIBOR.

Finding 10: Respondents with clearly identifiable exposure to LIBOR in the valuation of insurance liabilities are actively managing transition away from LIBOR.

Some jurisdictional examples include:

- In the UK close to 100% of insurance liabilities rely on LIBOR (£RFR). The planning assumption for all UK firms is that LIBOR will cease after end-2021, when LIBOR submissions will no longer be mandated by the FCA.
  - As outlined under finding 6, the UK PRA has set a series of targets for 2020. The planning assumption for all UK firms is that LIBOR will cease after end-2021, when LIBOR submissions will no longer be mandated by the FCA.
  - Furthermore, on-site examinations are aimed at identifying exposures and assessing the readiness to use alternative reference rates with focus on the largest insurers.
- In the US: Insurers are already transitioning away from LIBOR. The National Association of Insurance Commissioners (NAIC) will work with the industry to develop appropriate transition language. SOFR is perceived as less volatile than LIBOR, therefore risks should be reduced as a result of the process.
- In the EU, the interest rate swap instruments currently used within the risk-free rate curve, which is used to value insurance liabilities, are based on IBOR benchmark rates. Given that it is expected that LIBOR rates will be replaced by OIS[10] rates, the EIOPA Risk-free Rate (RFR) methodology and the EIOPA RFR production will need to be adjusted. In February 2020, EIOPA published a discussion paper[11] in which three options for switching the term structures to the new OIS rates are proposed:
  - The first option proposes an immediate switch, whereas the other two options consider gradual approaches to the replacement of the term structures to the new OIS-based term structures.
  - EIOPA favours one of the two gradual options, which promotes maximum stability for insurers. The discussion paper considers a "one size fits all" approach, which can be applied to all currencies and rates, including LIBOR.

[10] Overnight indexed swap (OIS)
[11] The paper is addressed to stakeholders, with a request for feedback to EIOPA by the end of June. (https://www.eiopa.europa.eu/content/discussion-paper-ibor-transitions)

- Stakeholders are invited to provide EIOPA with their feedback by end of June 2020. Based on this feedback, EIOPA will produce a consultation paper, which will include specific policy recommendations on the subject of IBOR transitions.

- In Costa Rica: The supervisor has recommended that the transition plan should include a review of regulations that use LIBOR as a reference. The selection of an alternative rate and regulatory changes are expected to be made in the third quarter of 2020.

Most respondents state **no changes** are required, due to the immaterial exposure.

Annex: List of Insurance Supervisors that responded to the IAIS Survey

	Jurisdiction	Supervisory Authority	FSB member jurisdiction	Jurisdiction with LIBOR currency
1	Argentina	Superintendencia de Seguros de la Nacion Argentina	✓	
2	Australia	Australian Prudential Regulation Authority (APRA)	✓	
3	Belgium	National Bank of Belgium (NBB)		✓
4	China, Hong Kong	Insurance Authority (IA)	✓	
5	China, Macao	Autoridade Monetária de Macau		
6	Chinese Taipei	Financial Supervisory Commission		
7	Costa Rica	Superintendencia General de Seguros de Costa Rica		
8	EIOPA	European Insurance and Occupational Pensions Authority (EIOPA)		✓
9	**France**	**Prudential Supervision and Resolution Authority (ACPR)**	✓	✓
10	**Japan**	**Financial Services Agency (FSA)**	✓	✓
11	Korea (Republic of)	Financial Services Commission (FSC) & Financial Supervisory Service (FSS)	✓	
12	Lithuania	Central Bank of Lithuania		
13	Netherlands	De Nederlandsche Bank (DNB)	✓	✓
14	Portugal	Autoridade de Supervisao de Seguros e Fundos de Pensoes (ASF)		✓
15	**Singapore**	**Monetary Authority of Singapore (MAS)**	✓	✓
16	South Africa	Prudential Authority	✓	
17	**Spain**	**Dirección General de Seguros y Fondos de Pensiones**	✓	✓
18	**Switzerland**	**Financial Market Supervisory Authority (FINMA)**	✓	✓
19	Thailand	Office of Insurance Commission		
20	**United Kingdom**	**Prudential Regulation Authority (PRA)**	✓	✓

	Jurisdiction	Supervisory Authority	FSB member jurisdiction	Jurisdiction with LIBOR currency
21	Uruguay	Banco Central del Uruguay (BCU), Superintendencia de Servicios Financieros (SSF)		
22	**USA**	**National Association of Insurance Commissioners (NAIC), Federal Reserve Board (FRB)**	✓	✓

Supervisory authorities/IAIS members highlighted in bold are from a FSB member jurisdiction with a LIBOR currency. For the purpose of this note, LIBOR jurisdictions include the Euro area jurisdictions. It should be noted that for jurisdictions with the Euro as LIBOR currency, the prevalence of the exposure is with EURIBOR or EONIA, which are non-LIBOR reference rates.