Canadian Institute of Actuaries / Institut canadien des actuaires

Document 219017

International Association of Insurance Supervisors (IAIS)
Public Consultation: Holistic Framework for Systemic Risk in the Insurance Sector

Note that the CIA did not respond to all the questions in the consultation on the [holistic framework for systemic risk in the insurance sector](). The CIA's comments to questions to which it responded appear below.

Q1 Is the list of key exposures that may lead to a systemic impact and its description appropriate? Please elaborate.

Definition of systemic risk: Systemic risk must be more clearly defined to consistently apply the concepts and approaches that would allow the supervisory regimes to monitor and act, as necessary, when required.

Liquidity was offered as an example, and most practitioners would agree this would meet the definition of systemic risk despite the lack of a clear definition of systemic risk and the analysis of liquidity against this definition. We did struggle to accept the other candidate risks identified in the paper, recognizing that tolerances of these risks may vary by region. A definition of systemic risk would resolve these inconsistent perspectives.

We recommend that (1) a definition of systemic risk be provided including criteria that would cause a candidate risk to be designated a systemic risk, and (2) that each candidate risk be analyzed against these criteria.

Consistent application of approaches for each risk designated a systemic risk: We struggled with some of the approaches defined in the paper, in part because of the inconsistent view of some of the candidate risks and the designation of all these candidate risks as systemic risks. We expect that these inconsistencies will be largely eliminated once the definition of systemic risk and the evaluation criteria are defined.

Comments on candidate risks identified in the paper:

- Liquidity risks: The paper uses references that suggest that liquidity risks in the insurance sector are comparable to liquidity risks in the banking sector. (Annex 2 references "Tier 3 assets", which is a Basel III concept.) We believe that many liabilities in the insurance sector are illiquid and assets backing these liabilities would not be subject to a forced sale. We recommend that the application of the approaches to monitor liquidity risks be refined further in order to be applicable to the insurance sector.
- Macroeconomic risks: We support the consideration of macroeconomic exposures as a source of systemic risk, and we recommend that the consideration of these exposures must clearly account for existing company risk mitigation processes and local jurisdictional supervisory controls. Failure to do so will lead to an inappropriate macroeconomic bias against long-term investment and savings products.

1740-360 Albert, Ottawa, ON K1R 7X7 ☎ 613-236-8196 🖷 613-233-4552
head.office@cia-ica.ca / siege.social@cia-ica.ca **cia-ica.ca**

- Counterparty exposure risks: We support the consideration of counterparty exposures as a source of systemic risk, but we recommend that the consideration of these exposures must clearly account for existing company risk mitigation processes and local jurisdictional supervisory controls.
- Lack of substitutability: This may pose a systemic risk to local markets, but we believe it unlikely that this would constitute a global systemic risk.
- "Others": The paper identified cyber risk, under-reserving of certain liabilities, and climate risk as candidate risks. We would also include future regulatory changes as candidate risks; current examples would include IFRS 17 and ICS 2.0.

In each example, a more precise definition of systemic risk, including the criteria that would cause a candidate risk to be designated a systemic risk, would eliminate this noise and would enable the IAIS members to move forward with this issue.

GAP analysis: We note regional differences in benefit designs and risk mitigation tools and recognize that regional biases for and against each feature may exist. We support the use of a GAP analysis to identify these differences, but we recommend that the paper provide additional commentary regarding assessing the effectiveness of existing risk mitigation processes under the macroeconomic stress environments envisaged by the framework.

Q2 Are there any other key exposures that are missing? Please elaborate.

Response included in response to question 1.

Q6 Do you agree with the proposed scope of application and of the practical application of the proportionality principle as described above? Please elaborate.

The paper correctly introduces the proportionality principle in many of its approaches. We believe the impact of these segments can be improved as follows:

- **Definition of proportionality**: We recognize that different interpretation and application of the proportionality principle exist in different sectors and regions. We believe the paper should include a definition of the proportionality principle for the purposes of systemic risk. Of note, the proportionality principle would be applicable even in large markets, where these markets are highly fragmented such as is the case with the property and casualty insurance market in Canada.
- **Identification of companies to be considered in systemic risk monitoring:** In the simplest of definitions, insurers with very small exposures of the referenced risk may be excluded from any data collection and any analysis; however, these companies may be affected, and they may be less prepared to deal with these risks than others that have recognized and mitigated these risks. The inclusion of these smaller insurers may alter the assessment of exposures of the market in general to the referenced risks. It is difficult to draw conclusions on the impact these smaller insurers can have on the

analysis or the impact of the risk on the smaller insurers without better understanding the approach the IAIS will take on monitoring and supervision.

Q8 Do you agree with the above proposal to amend the Standards and Guidance on supervisory review and reporting framework? Please elaborate.

Central organization to monitor systemic risks: The paper describes a vision where local supervision of insurers is supported by a new, central organization to provide these services. The monitoring process and the centralized supervisory process must be clearly established before we can comment on this segment of the paper.

Q12 Is the development of an Application Paper on macroprudential surveillance deemed useful? Please elaborate.

We support the IAIS recommendation that its approach to a central organization to monitor and supervise systemic risks be further developed in a separate application paper. We believe that further refinement of the approaches defined in the paper would help to define the risks and the approach to monitoring and supervisory action.

We also believe that implementation of the framework should be deferred until these issues have been addressed; specifically, (1) include a definition of systemic risk including criteria that would cause a candidate risk to be designated a systemic risk, (2) include a definition of proportionality principle for the purposes of this paper, and (3) develop an approach to a central organization to monitor and supervise systemic risks.

Should deferral of the implementation timeline not be a practical option, then we recommend that the IAIS provide a commitment to further engage with stakeholders on these issues as part of the implementation communication. This will help ensure that appropriate context is provided regarding the status of the framework development at date of implementation.

Q13 What elements could be addressed in such an Application Paper?

Need for prospective supervisory intervention: We recognize that one risk associated with the concepts described in the paper is the time lag between data collection with analysis and any potential supervisory intervention. It would be desirable for any approach taken to enable supervisors to take appropriate action before the referenced risks reach a crisis level.

Q14 Are the proposals on macroprudential surveillance as described in section 3.2 appropriate? Please elaborate.

Use of ICS as a monitoring tool for systemic risk: We note that Insurance Capital Standard (ICS) will not become a Prescribed Capital Requirement (PCR) until 2025 at the earliest. As such, ICS should not be used as a monitoring tool for systemic risk prior to that date.

Use of data in the monitoring process: As has been seen in comments on the ICS 2.0 papers, there are significant challenges in aggregating data across jurisdictions, and in ensuring a level playing field in terms of supervisory powers and intervention. These issues must be addressed within this context and are fundamental to the overall integrity of the holistic framework, and they must be clearly defined prior to the implementation of this framework.