INTERNATIONAL ASSOCIATION OF
INSURANCE SUPERVISORS

Public

Global Systemically Important Insurers: Proposed Updated Assessment Methodology

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About the IAIS

The International Association of Insurance Supervisors (IAIS) is a voluntary membership organization 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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Preface

In July 2013, the IAIS developed an initial assessment methodology (the 2013 Methodology) to identify insurance-dominated financial conglomerates whose distress or disorderly failure, because of their size, complexity and interconnectedness, would cause significant disruption to the global financial system and economic activity.[1]

As stated in the 2013 Methodology, the IAIS plans to evaluate every three years whether and, if so, the ways and extent to which the assessment methodology should be reviewed and revised. This public consultation document outlines proposed revisions to the 2013 Methodology for global systemically important insurers (G-SIIs) and invites public comment on these revisions and related issues (Proposed Methodology).

The IAIS acknowledges the need to monitor developments and make changes to the assessment methodology as necessary. In the near term, the ongoing and related IAIS work on the definition of Non-traditional Non-insurance (NTNI) activities and the Higher Loss Absorbency (HLA) requirement will be closely monitored and evaluated in the context of the Proposed Methodology. Any changes to the NTNI definition and the HLA may well lead to a change in the Proposed Methodology. Additionally, the work streams on the NTNI definition and the Proposed Methodology are interlinked with the HLA and, therefore, any change in either the NTNI definition or the Proposed Methodology will be considered in future versions of the HLA.

[1] *See* Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

Glossary of abbreviations

BCBS	Basel Committee on Banking Supervision (also Basel Committee)
BIS	Bank for International Settlements
CDS	Credit Default Swap
FSB	Financial Stability Board
G-SIBs	Global Systemically Important Banks
G-SIFIs	Global Systemically Important Financial Institutions
G-SIIs	Global Systemically Important Insurers
G20	Group of Twenty Countries
HLA	Higher Loss Absorbency
IAIS	International Association of Insurance Supervisors
NTNI	Non-traditional Non-insurance Activities
SIFIs	Systemically Important Financial Institutions

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I. Introduction

1. The International Association of Insurance Supervisors (IAIS) is participating in a global initiative, along with other standard setters, central banks and financial sector supervisors, and under the purview of the Financial Stability Board (FSB) and G20, to identify global systemically important financial institutions (G-SIFIs).[2] The focus of the IAIS' analysis is in relation to potential global systemically important insurers (G-SIIs).[3] To this end, in 2013 the IAIS developed an initial assessment methodology (the 2013 Methodology) to identify any insurers whose distress or disorderly failure, because of size, complexity and interconnectedness, would cause significant disruption to the global financial system and economic activity. Any such insurers have been regarded as systemically important on a global basis.

2. As stated in the 2013 Methodology, the assessment methodology is to be reviewed every three years in order to capture improvements noted by IAIS Members, developments in the insurance sector, changes in insurers, growth in the global insurance markets, and any progress in methods and approaches for measuring systemic importance in the insurance sector and the broader financial sector. On 6 November 2014, the FSB stated that, "by November 2015, the IAIS will further develop the G-SII assessment methodology as needed to ensure, among other things, that it appropriately addresses all types of insurance and reinsurance, and other financial activities of global insurers."[4]

3. The methodology proposed in this consultation document (the Proposed Methodology) integrates a structured use of both quantitative and qualitative factors and will be applied beginning in 2016. While the majority of the Proposed Methodology will be based on quantitative outputs, these will be complemented by an important additional assessment phase, where additional information, including qualitative and quantitative considerations, will be taken into account. Recognizing the heterogeneity of insurers across the global financial system, the Proposed Methodology will include a rigorous, robust, and structured use of quantitative and qualitative components and both will be combined into an overall assessment. The results of the Proposed Methodology will be driven by robust in-depth factual analysis and supporting documentation.

4. Below is a summary of the main proposed changes relative to the 2013 Methodology. These changes reflect the improvements and refinements learned from applying the 2013 Methodology and from data submitted by insurers to the IAIS as of financial year-end 2011, 2013, and 2014.

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[2] G-SIFIs are defined by the FSB as "institutions of such size, market importance, and global interconnectedness that their distress or failure would cause significant dislocation in the global financial system and adverse economic consequences across a range of countries." Global systemically important insurers (G-SIIs) are one class of G-SIFIs. See the FSB SIFI Framework, 2010 (http://www.financialstabilityboard.org/publications/r_101111a.htm).

[3] The term "insurers" includes both primary insurers and reinsurers.

[4] Financial Stability Board, 2014 update of list of global systemically important insurers (G-SIIs), November 6, 2014, (http://www.financialstabilityboard.org/wp-content/uploads/r_141106a.pdf).

5. The Proposed Methodology outlines a five-phase approach to the assessment process that includes both qualitative and quantitative elements. The IAIS is also proposing changes to certain indicators in the 2013 Methodology to address issues related to indicator responsiveness and data quality, including reliability (across both insurers and jurisdictions).

6. First, the IAIS proposes to adopt absolute reference values for certain indicators, including the derivatives trading indicator (CDS protection sold) in the NTNI category, the financial guarantees indicator in the NTNI category, and reinsurance in the interconnectedness category. Second, the IAIS proposes to remove both the large exposures and intra-group commitments indicators from the quantitative assessment in Phase II of the Proposed Methodology and, instead, to use those data points in the Phase III analysis. These indicators capture information relevant to the Proposed Methodology; however, the IAIS proposes that it is more appropriate to consider these indicators in the qualitative analysis of Phase III. Third, the IAIS has not used derivatives trading (excluding hedging and replication) in economic terms as an indicator during the quantitative part of the 2013 Methodology in prior years because of data reliability concerns. Recognizing its high degree of potential systemic relevance, the IAIS proposes to consider how information regarding the degree of speculative derivatives trading can be used as part of Phase III of the Proposed Methodology.

II. 2013 Methodology for Global Systemically Important Insurers

7. The IAIS developed the 2013 Methodology using year-end 2011 data collected from selected insurers in 2012 and applied the 2013 Methodology in its past designation exercises. The 2013 Methodology involved three steps: collection of data,[5] methodological assessment, and the supervisory judgment and validation phase.[6]

8. The 2013 Methodology was indicator-based and premised upon the BCBS's G-SIB methodology. However, the specific nature of the insurance sector has influenced the selection, grouping, and weights assigned to certain indicators. Table 1 in the Appendix contains the Proposed Methodology's refinements to the initial indicator-based 2013 Methodology. Table 2 in the Appendix lists the weights given to each category and individual indicator under the 2013 Methodology.

9. The 2013 Methodology grouped indicators into five categories:

    a. Size: The importance of a single component for the working of the financial system generally increases with the amount of financial services that the component provides. It should be recognized; however, that in an insurance context size is a prerequisite for the effective pooling and diversification of risks.

[5] The BIS collaborated with the IAIS by providing secured transmission channels for the collection of confidential data.
[6] *See* Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

b. Global activity: The methodology is aimed at identifying components of the financial system whose failure can have large negative externalities on a global scale.

c. Interconnectedness: Systemic risk can arise through direct and indirect inter-linkages between the components of the financial system so that individual failure or distress has repercussions around the financial system, leading to a reduction in the aggregate amount of services.

d. Non-traditional and non-insurance (NTNI) activities: As described in *Insurance and Financial Stability*, non-traditional insurance activities and non-insurance financial activities are potential drivers of the systemic importance of insurers and thus have the greatest impact upon failure.

e. Substitutability: The systemic importance of a single component increases in cases where it is difficult for the components of the system to provide the same or similar services in the event of failure.

10. Under the 2013 Methodology, the two most important categories for assessing the systemic importance of insurers were the NTNI category and the interconnectedness category. Consequently, the size, global activity and substitutability categories were given lower weights. The weighting for the NTNI category was 45%, the weighting for the interconnectedness category was 40%, and the weighting for each of the three remaining categories was 5%.[7]

11. The 2013 Methodology also recognized the importance of supervisory judgment and validation of the results flowing from the indicator approach. This supervisory judgment and validation process included additional qualitative and quantitative assessments, including the selection of candidates for the assessment process.[8]

III. Proposed Methodology for G-SIIs

12. Built on the three-step approach from the 2013 Methodology (collection of data, methodological assessment, and supervisory judgment and validation phase), the Proposed Methodology integrates a structured use of both quantitative and qualitative factors. The Proposed Methodology will incorporate changes to certain indicators to address issues related to indicator responsiveness and data quality, including reliability. These revisions and improvements to indicators are discussed in Section IV.

13. While the majority of the Proposed Methodology will be based on quantitative outputs, these will be complemented by an important additional assessment phase, where additional information, including qualitative and quantitative considerations, will be taken into account. Recognizing the heterogeneity of insurers across the global financial system, the Proposed Methodology will include a rigorous, robust, and structured use of

[7] *See* Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.
[8] *Id.* The IFS assessment approach described in Annex 1 of the 2013 Methodology was not used by the IAIS in prior designation exercises, and it will not be used in the Proposed Methodology.

quantitative and qualitative components and both will be combined to produce an overall assessment.

14. The Proposed Methodology proposes to adopt a five-phase approach to the G-SII assessment process. Phases I and II (see discussion below) incorporate the quantitative component of the Proposed Methodology. Phases III and IV (see discussion below) comprise qualitative and quantitative elements of the Proposed Methodology, including engagement with prospective G-SIIs. These phases will consider important additional factors and other objective factors not adequately incorporated in the quantitative component of Phases I and II. Phase V combines the rigorous, robust, and structured use of both quantitative and qualitative components in Phases I through IV to produce an overall assessment that leads to the IAIS recommendation to the FSB. Section V describes the five-phase approach to the G-SII assessment process.

IV. Revisions and Improvements to Indicators under the Proposed Methodology

Use of Absolute Reference Values

15. The IAIS proposes to use absolute reference values for a limited number of indicators to address the issue of normalization for these indicators. Using absolute reference values for certain indicators means that the score for these indicators will not be calculated solely as the relative importance of an insurer in the sample; rather, an insurer's score also will take into account market developments and/or market size. For example, under the 2013 Methodology, each insurer's score for a particular indicator is calculated by dividing the individual insurer amount by the aggregate amount summed across all insurers in the sample.[9] For indicators with absolute reference values, the absolute reference value will either replace the sum of responses from the sample insurers in the denominator of the indicator score calculation or add a factor to the indicator score calculation that reflects market developments.

16. The use of absolute reference values is motivated by several considerations. Absolute reference values recognize changes in certain areas in the systemic risk of the sample insurers over time. For example, the underlying markets for both the derivatives trading and financial guarantee indicators have seen large drops in volume since the financial crisis. The relative methodology does not adequately capture this and without adjustment these indicators would increase the score of an insurer with a constant amount of this activity.

17. The use of absolute reference values could also make the Proposed Methodology more responsive to changes in the insurance industry's systemic profile in certain areas. For example, if insurers resumed writing credit default swaps at levels undertaken during the global financial crisis of 2007-08, scores would now increase accordingly. The use of absolute reference values could also help adjust for sample bias. The IAIS requests data from approximately fifty insurers as part of the yearly designation exercise. These insurers

[9] See Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

in the data collection exercise may not be representative of certain aspects of the larger global insurance market, particularly for some areas such as reinsurance.

18. The absolute reference values being explored for this limited number of indicators will be based on historical experience (i.e. the size of the particular market during a prior year) and/or industry market share (i.e. expanding the denominator from the share of the activity of the sample insurer pool to the activity of the entire market of the indicator).

19. At the next scheduled three-year review, the Proposed Methodology may move toward using more absolute reference values, where appropriate, to assure that the indicators adequately capture changes in the industry's systemic footprint and the potential threat to global financial stability posed by insurers as compared to other financial firms.

> **Question 1**: Is the use of absolute reference values appropriate for the indicators for reinsurance, financial guarantees, and derivatives trading (CDS sold)?

> **Question 2**: Should the IAIS consider measuring other indicators by absolute reference values? If yes, identify the indicator, explain the absolute reference value that can be used and explain why the use of the absolute reference value would improve the Proposed Methodology in the future.

Financial Guarantees Indicator

20. This financial guarantees indicator in the NTNI category is intended to measure an insurer's financial guarantee and mortgage guarantee products.[10] The IAIS proposes to use an absolute reference value for this indicator in order to take into account market developments and its reduced market size. For example, this indicator could measure the stock of the total gross amount of debt issued at year-end. An in-depth investigation by the IAIS for potential absolute reference values showed that gathering relevant data on financial guarantees is a challenge. To overcome this, the IAIS proposes to use the ratio between structured finance bonds insured and the total bonds insured by the financial guarantors in the sample. This information is publicly available in insurers' annual reports.

> **Question 3**: What information or data could be used as an absolute reference value for the financial guarantees indicator?

> **Question 4:** Is structured finance bonds insured an appropriate denominator or should the denominator reflect the notional value of bonds guaranteed by the broader financial sector via non insurance products?

Derivatives Trading (CDS sold) Indicator

21. The derivatives trading (CDS sold) indicator in the NTNI category is intended to indicate the scale of CDS protection sold which links an insurer with other parts of the financial

[10] See Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

system.[11] The IAIS proposes to use an absolute reference value for this indicator that will take into account market developments and the reduced size of the CDS market. For example, data from the BIS statistics on the overall global CDS market could be used as an absolute reference value.

> **Question 5**: Are BIS statistics on the overall global CDS market an appropriate absolute reference value for the derivatives trading (CDS sold) indicator? If so, how should this absolute reference value be used by the IAIS? What other information or data could be used as an absolute reference value for the derivatives trading (CDS sold) indicator?

Reinsurance Indicator

22. The reinsurance indicator in the interconnectedness category measures the degree of interconnectedness with the insurance sector through reinsurance transactions.[12] The IAIS proposes to use an absolute reference value for this indicator because the approximately fifty insurers in the IAIS annual data collection may not be representative of the reinsurance market and their actual market share in the global reinsurance market may change over time (for example, as alternative capital sources potentially emerge). For example, total global reinsurance premiums written could be used as an absolute reference value to estimate the size of the global reinsurance market. Such information can be collected using multiple sources, which would avoid relying on a unique private data provider. These sources could include, among other items, reports from rating agencies and publically available annual reports.

> **Question 6**: Are total global reinsurance premiums written an appropriate absolute reference value for the reinsurance indicator? If so, how should this absolute reference value be used by the IAIS? What other information or data could be used as an absolute reference value for the reinsurance indicator?

Indicators that will be considered in Phase III of the Proposed Methodology

23. The IAIS proposes to remove the large exposures indicator, the intra-group commitments indicator, and the derivatives trading (excluding hedging and replication) in economic terms indicator from the quantitative indicator-based component in Phase II and to add those indicators to the Phase III analysis.

Large Exposures Indicator

24. The large exposures indicator in the 2013 Methodology was intended to measure the degree of interconnectedness, focusing on concentrations in asset exposures to major counterparties.[13] The 2013 Methodology stated that this indicator would be reviewed by the IAIS in future years. After reviewing the data received regarding this indicator, the IAIS proposes to remove the large exposures indicator from the interconnectedness category of the Proposed Methodology. The data on large exposures that were previously collected

[11] *Id.*
[12] *Id.*
[13] See Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

may largely reflect incoming risks that affect the probability that an insurer will be in distress, rather than the systemic risk from an insurer's failure (impact upon failure) as the indicator is supposed to measure. However, an insurer's large exposures potentially could provide relevant information on an insurer's interconnectedness with external counterparties. Therefore, information from this indicator will be used during Phase III of the Proposed Methodology

> **Question 7**: To what extent are large exposures an appropriate indicator of an insurer's interconnectedness with the financial system? What is the appropriate way to measure or understand the interconnections between an insurer's large exposures and the financial system?

Intra-group Commitments Indicator

25. The intra-group commitments indicator in the 2013 Methodology was intended to indicate significant NTNI activities and/or lack of self-sufficiency of NTNI activities.[14] The IAIS proposes to remove the intra-group commitments indicator from the NTNI category in the Proposed Methodology because of data responsiveness and data quality (including reliability) concerns caused by inconsistent reporting and calculations of the indicator across the sample insurers. However, an insurer's intra-group commitments potentially could provide relevant information on an insurer's NTNI activities. Therefore, information from this indicator will be used during Phase III of the Proposed Methodology

> **Question 8**: To what extent, if any, are intra-group commitments an appropriate measure of a potential G-SII's systemic relevance?

Derivatives trading (excluding hedging and replication) in economic terms indicator

26. The 2013 Methodology included both a derivatives trading (CDS sold) indicator and a derivatives trading (excluding hedging and replication) in economic terms indicator in the NTNI category. The derivatives trading (excluding hedging and replication) in economic terms indicator was intended to indicate the degree of speculative derivatives trading by insurers, which has a high degree of potential systemic relevance. However, the IAIS has not used this indicator in prior designation exercises because of concerns regarding data responsiveness and data reliability with respect to information reported by the insurers. Therefore, the IAIS proposes to remove this indicator from Phase II of the Proposed Methodology. Instead, information about speculative derivatives trading will be used and evaluated during Phase III.

> **Question 9**: To what extent is the derivatives trading (excluding hedging and replication) in economic terms indicator an appropriate indicator of NTNI activities? What is the appropriate way to measure or understand the systemic importance of speculative derivatives trading?

See Table 1 for the revised indicator-based assessment under the Proposed Methodology.

[14] *Id.*

Table 1. Proposed Methodology: weights given to each category and individual indicators

Category	*Category weighting*	*Individual indicator*	*Indicator weighting*
Size	5%	Total assets	2.5%
		Total revenues	2.5%
Global activity	5%	Revenues derived outside of home country	2.5%
		Number of countries	2.5%
Interconnectedness	40%	Intra-financial assets	6.7%
		Intra-financial liabilities	6.7%
		Reinsurance*	6.7%
		Derivatives	6.7%
		Turnover	6.7%
		Level 3 assets	6.7%
Non-traditional insurance and noninsurance activities	45%	Non-policy holder liabilities and non-insurance revenues	7.5%
		Derivatives trading*	7.5%
		Short term funding	7.5%
		Financial guarantees*	7.5%
		Minimum guarantee on variable insurance products	7.5%
		Liability liquidity	7.5%
Substitutability	5%	Premiums for specific business lines	5%

*The IAIS proposes to use absolute reference values for these indicators

+The respective indicator weights do not sum to 100.0 percent because of rounding.

27. The IAIS proposes to maintain the relative weightings of the five categories in the Proposed Methodology. Under the Proposed Methodology, the large exposures and intra-group commitments indicators will be moved from Phase II to Phase III.[15] With the respective category weighting percentages remaining constant in the Proposed Methodology, the weighting of the two removed indicators (large exposures and intra-group commitments) will be distributed evenly to the remaining indicators in each category. Therefore, each remaining indicator in the interconnectedness category increased in weight from 5.7% to 6.7%, and each remaining indicator in the NTNI category increased in weight from 6.4% to 7.5%.

> **Question 10**: The weightings in Phase II of the Proposed Methodology emphasize the insurer's NTNI activities (45%) and its interconnectedness (40%). Are there any developments or trends in the global insurance market that warrant further refinements to the 2013 Methodology, potentially including changes to the category weightings? Please explain your answer.

Revisions and Improvements to other Indicators in the Proposed Methodology

Derivatives Trading Indicator (Interconnectedness Category)

28. The derivatives trading indicator in the interconnectedness category of the 2013 Methodology was intended to indicate the degree of interconnectedness with the financial system through derivatives transactions. The data input used for this indicator in the 2013 Methodology is gross notional value.[16] This measurement was chosen because it provides a common basis in all accounting frameworks. However, the actual net exposures emanating from derivatives in both the amount and structure may differ from gross notional value.

> **Question 11**: Will the responsiveness of the derivatives indicator in the interconnectedness category be improved by using other data such as an appropriate net fair value figure (either positive or negative)? If so, what are more appropriate data and what is the appropriate way to use such data to measure or understand the interconnectedness caused by derivatives transactions? Should the IAIS measure interconnectedness with respect to derivatives transactions in the same manner as the BCBS? Please explain your answer.

[15] The 2013 Methodology included both a derivatives trading (CDS sold) indicator and a derivatives trading (excluding hedging and replication) in economic terms indicator. However, the derivatives trading (excluding hedging and replication) in economic terms indicator was not used by the IAIS in prior designation exercises because of data responsiveness and data reliability concerns.

[16] See Global Systemically Important Insurers: Initial Assessment Methodology, 18 July 2013.

Other Indicators

29. The IAIS seeks public comment on whether, and if so, how, to further improve the reliability and responsiveness of the other indicators and data measures used in the Proposed Methodology, including but not limited to the:

- minimum guarantees indicator
- liability liquidity indicator
- level 3 assets indicator
- short-term funding indicator.

> **Question 12**: How can the reliability and responsiveness of any indicator, including those mentioned above, be further improved, modified or revised for the Proposed Methodology?

V. Phases of Assessment Process under the Proposed Methodology

30. This section describes the five-phase approach to the assessment of G-SIIs that will be followed by the IAIS under the Proposed Methodology. The G-SII identification process focuses on how an insurer's failure or distress would impact the global financial system, not the probability that an insurer will experience failure or distress. Additionally, the analysis in the G-SII identification process does not consider the quality of the resolution or policy framework within a jurisdiction.

Phase I: Data Collection Phase

31. Approximately 50 insurers that meet the IAIS criteria for data collection will be included in the annual data collection exercise. Subject to the judgment of the IAIS and relevant authorities, the criteria for insurers being included in the data collection phase are:
    - total assets of more than US$ 60 billion and a ratio of premiums from jurisdictions outside the home jurisdiction to total premiums of 5% or more and
    - total assets of more than US$ 200 billion and a ratio of premiums from jurisdictions outside the home jurisdiction to total premiums between 0% and 5%.

> **Question 13**: What criteria, other than those listed above, should the IAIS consider when determining whether to include an insurer in the Phase I data collection?

Phase II A: Quality Control and Scoring Phase

32. During Phase II, the IAIS will validate the completeness and accuracy of data received from insurers, to the extent reasonably possible, and produce a preliminary empirical ranking based on the quantitative indicator-based component of the Proposed Methodology. The IAIS will communicate with supervisors and, through the respective relevant authorities, with insurers to validate data as needed.

Phase II. B: Determination of Quantitative Threshold

33. For purposes of the quantitative component of Phase II of the Proposed Methodology, the IAIS proposes to establish a quantitative threshold that will potentially divide the sample insurers into two groups before the application of supervisory judgment and Phases III, IV and V.[17]

34. The quantitative threshold will divide insurers between potential G-SII status and non-G-SII status. An insurer's score or ranking following Phase II will not indicate or result in G-SII identification. The five phases of the Proposed Methodology will produce a recommendation from the IAIS to the FSB on a recommended G-SII list.

35. The two groups for purposes of the quantitative threshold are:

- Group 1, above the quantitative threshold: This group will contain insurers scoring above the quantitative threshold. Subject to the analysis in the remaining phases of the Proposed Methodology, insurers in this group will be considered for potential identification as a G-SII.

- Group 2, below the quantitative threshold: This group will contain insurers scoring below the quantitative threshold. Insurers below the quantitative threshold will not be recommended for identification as a G-SII unless added by discretion of the relevant authorities.

36. When establishing the quantitative threshold in Phase II, the IAIS proposes to consider the principle of consistency and relative stability in the quantitative threshold year-over-year.

> **Question 14**: What are the strengths and weaknesses of consistency and relative annual stability as a guiding principle for establishing the quantitative threshold in Phase II? For purposes of establishing the quantitative threshold, what other principle(s), if any, should the IAIS consider?

37. The IAIS is considering several approaches to establishing the quantitative threshold. These approaches may include:
- Cross-sectoral analysis, i.e. do potential G-SIIs compare to systemically important firms in other sectors (such as the G-SIBs).
- Natural cliff, i.e. does the score indicate a quantitative distinction between insurers.
- Cluster analysis, i.e. does the score demonstrate that a certain number of highly ranked insurers score within a range.
- Establishing an annual floor for the quantitative threshold.

[17]The quantitative threshold divides insurers between potential G-SII status and non-GSII status, and may not be used for purposes of the HLA grouping allocations.

- Average score of the insurers included in the data collection plus a certain level of standard deviation from the average score.
- Year-to-year and trend comparisons of data points to assess whether the systemic exposure of the sample insurers in the identified areas has increased or decreased, i.e. to evaluate the extent to which potential G-SIIs may retain a high or low score based on the relative nature of the rankings.

> **Question 15**: For purposes of establishing the quantitative threshold in Phase II, what other approaches, if any, should the IAIS consider? What are the strengths and weaknesses of the alternative approaches, as listed above, to determining the quantitative threshold?

Phase III: Discovery Phase

38. The quantitative assessment in Phases I and II will be used to provide an initial ranking of the relative systemic importance of insurers within the Proposed Methodology. This quantitative assessment, however, may not be sufficient to make a determination as to whether this subset of insurers should be identified as potential G-SIIs. Additional information and analyses may be necessary in Phases III, IV, and V.

39. While the majority of the Proposed Methodology will be based on quantitative outputs, these will be complemented by an important additional assessment phase (Phase III), where additional information, including qualitative and quantitative considerations, will be taken into account. The qualitative and quantitative elements in Phase III could be used to better understand and assess the heterogeneity of the insurance industry, differences in business mixes and product attributes across jurisdictions, and differences in data quality reported across insurers and across jurisdictions. Adjustments to potential G-SII status (such as removal from or addition to the G-SII list), will be based on all considerations of the Proposed Methodology, including Phase III and the reinsurance supplemental assessment.

> **Question 16**: While the majority of the Proposed Methodology will be based on quantitative outputs, what specific qualitative aspects of a potential G-SII should be considered in Phase III that are not captured in Phases I and II?

40. During Phase III, the IAIS and the relevant authorities will gather and analyse additional quantitative or qualitative information that is not captured in Phase II. This phase is mandatory for insurers above the G-SII threshold. The level and extent of additional analysis conducted in Phase III for insurers above the G-SII threshold will be determined by the relevant authorities and the IAIS. For insurers below the G-SII threshold, Phase III is subject to the discretion of the IAIS or the relevant authorities. The IAIS has developed the following guiding principles for supervisory judgment:

- Adjustments to the Phase II score will not be made unless the Phase III analysis reveals there are substantive errors in the data submitted by insurers.

- Adjustments to potential G-SII status should be supported by well-documented and verifiable arguments that can be applied consistently to all insurers in the G-SII assessment process.

> **Question 17**: What constraints should be imposed on the use of non-quantitative analysis of the potential systemic importance of insurers in the Proposed Methodology? To what extent, if at all, can qualitative analysis enhance the IAIS's understanding of the systemic importance of a potential G-SII?

41. Phase III also will consider additional indicators that may contribute to stability or instability in the global financial system but are not captured by the quantitative assessment in Phase II of the Proposed Methodology. At this time, the IAIS is proposing to remove intra-group commitments, large exposures, and derivatives trading (excluding hedging and replication) in economic terms from the quantitative assessment in Phase II and consider these three indicators in Phase III. These indicators provide relevant information for the Proposed Methodology; however, the IAIS proposes that it is more appropriate to consider these indicators in Phase III. In the future, the IAIS may identify and consider other indicators in Phase III.

> **Question 18**: What other indicators, if any, could be considered by the IAIS to inform the supervisory judgment aspects of the Proposed Methodology?

42. The qualitative elements of Phase III of the Proposed Methodology should be robust, documented, and justifiable. Examples of information and analysis that may be considered in the qualitative aspects of Phase III include the following:

- Enhancing the understanding of the data being evaluated in the indicators and producing a more accurate interpretation of the indicator results.
- Revealing extenuating circumstances that cannot be easily quantified in the form of an indicator.
- Providing for a more in-depth understanding of the nature and extent of the insurer's interconnections with other financial counterparties.
- Providing for a more in-depth understanding of the nature and extent of risks associated with a particular type of non-traditional or non-insurance activities.
- Providing for a more in-depth understanding of the nature and extent of risks associated with insurance activities.
- Providing for an assessment of the liquidity aspects of the insurer's specific products and/or liabilities and whether such liquidity calls might have systemic implications for the global economy.
- Factors that change the potential impact of the insurer's failure on the real economy;
- Characteristics of the insurer's business model; composition and proportion of the group's financial and non-financial activities.
- Cross-sectoral assessments.

- Changes in an insurer's circumstances since the compilation of the data on which the quantitative analysis is based.

Reinsurance Supplemental Assessment

43. The reinsurance supplemental assessment complements the other components of the Proposed Methodology and allows the IAIS to better assess risks associated with an insurer's third-party reinsurance activities. The reinsurance supplemental assessment is not a separate alternative to the Proposed Methodology, rather, it allows for a data and fact-driven analysis of primary insurers and reinsurers with significant third-party reinsurance activities. The reinsurance supplemental assessment will be applied to primary insurers and reinsurers with significant third-party reinsurance activities that are subject to the analysis in the phases following Phase II.

44. The IAIS is developing certain indicators for primary insurers and reinsurers conducting a significant amount of third-party reinsurance business. Adjustments to potential G-SII status (such as removal from or addition to the G-SII list), will be based on all considerations of the Proposed Methodology, including the reinsurance supplemental assessment. For example, it could depend on whether the insurer's third-party reinsurance activities present institutional risk (i.e. an analysis of the extent to which the insurer's reinsurance exposures are dispersed or concentrated) or geographic concentration risk that increases or reduces its systemic footprint.

45. The 2015 G-SII data collection exercise contained supplementary reinsurance questions and a separate reinsurance template that requested certain data relating to the sample insurers' third-party reinsurance activities.[18] The additional data and information requested in the reinsurance templates will help the IAIS better assess the business model and potential risk of third-party reinsurance activities.

46. In particular, the IAIS collected data on a sample insurer's top 10 assumed exposures from ceding insurers. Additionally, the IAIS collected general information and data on a sample insurer's aggregate reinsurance activities (measured by, as appropriate, aggregate gross written premiums, aggregate technical provisions, or aggregate assumed exposures). The IAIS also collected data elements on retrocession activities, including a reinsurer's top five exposures to other reinsurers and an insurer's aggregate retrocession activities for all contracts retroceded. The IAIS also previously received information from certain reinsurers on their gross reinsurance/retrocession premiums assumed that was segmented by region, based on the domicile of the individual ceding insurer. This data was segmented by the following regions of ceding insurer: (1) Europe (Western, Central and Eastern); (2) North American (Canada and the United States); (3) Asia (Central, South, East Asia and Oceania) and Australia; (4) Africa, Near and Middle East; and (5) Latin America and

[18] The IAIS also received more detailed data from all insurers in the sample that have significant third-party reinsurance activities above a certain threshold.

Caribbean. The IAIS also previously collected information on a sample insurer's reinsurance activities in certain business lines in order to better assess concerns regarding substitutability.

47. The reinsurance data elements collected by the IAIS will be used to evaluate whether an insurer's third-party reinsurance activities could present risk to large, interconnected primary insurers and the global financial system. The IAIS is proposing to use data on a reinsurer's top 10 assumed exposures from ceding insurers and its top 5 exposures to other reinsurers to perform a network analysis and better assess the extent to which third-party reinsurance activities disperse or concentrate risk in the broader insurance market.

> **Question 19**: How can the additional information collected in the supplementary reinsurance-specific questions as part of the data collection be relevant to better assess the potential effects of a reinsurer's failure on other reinsurers or primary insurers? Should the IAIS set a threshold amount of third-party reinsurance activities that must be exceeded by an insurer in order to be required to complete the supplementary reinsurance-specific questions in Phase I? If so, what should be the level of the threshold?

> **Question 20**: Are gross written premiums, technical provisions or exposures an appropriate way to measure and/or understand the interconnections between an insurer's third-party reinsurance activities and other primary insurers and reinsurers?

> **Question 21**: How could the information collected be used to evaluate the extent to which an insurer's third-party reinsurance activities disperse or concentrate risk in the global insurance market?

> **Question 22**: Are an insurer's third-party reinsurance activities interconnected with financial markets and, if so, how? What additional data measures could be useful to understand the extent to which an insurer's third-party reinsurance activities are interconnected with other parts of the financial markets (*e.g.* banks or asset managers)?

> **Question 23**: What other data points would be relevant for the IAIS to consider in the Proposed Methodology when evaluating the extent to which the potential geographic risks (*i.e.* the risk that a reinsurer or insurer may be overly concentrated in one area) of the global reinsurance market are dispersed or concentrated among certain reinsurers or insurers?

Phase IV: Exchange with Prospective G-SIIs

48. Following Phase III, the IAIS will reach consensus on a preliminary list of G-SII recommendations based on the rigorous, robust, and structured use of the quantitative and qualitative components of the Proposed Methodology. The IAIS and the relevant authorities will then offer any prospective G-SII the opportunity to present information to the IAIS that may be relevant to the Proposed Methodology, and provide a technical

perspective thereon. The relevant authorities will participate in this exchange of information.

49. In advance of the exchange, the IAIS will provide the prospective G-SII with a summary of the assessment process and analysis that resulted in the insurer being considered as a potential G-SII. During this exchange, the prospective G-SII may ask questions and present additional information relating to any aspect of the Proposed Methodology. During this exchange, the IAIS also will discuss its assessment of the quantitative and qualitative analyses. The prospective G-SII also will have the opportunity to share with the IAIS its perspective and views on the data collection and any accompanying explanatory statements submitted to the IAIS.

> **Question 24**: What types and forms of information exchange with prospective G-SIIs should the IAIS consider?

Phase V: IAIS Recommendation to the FSB

50. Following annual completion of the G-SII designation exercise, the IAIS will recommend a list of identified G-SIIs to the FSB.

51. It is proposed that the list of recommended G-SIIs could be allocated for HLA purposes in a similar manner to the existing allocation process outlined in the HLA paper.

52. The G-SII allocation process for HLA purposes will be based on the quantitative methodology of Phases I and II. Any adjustments made through Phase III will have a corresponding impact on the application of HLA.

> **Question 25:** Is it reasonable for Phase 2 of the Methodology to be the basis for applying HLA to G-SIIs? Please indicate any alternative methods that the IAIS should consider for this allocation process. What constraints, if any, should be applied to Phase III's effect on the allocation of HLA?

VI. Annual G-SII Data Collection and Data Instructions

53. The annual G-SII data collection process and data instructions will be revised to be consistent with the outcomes of this consultation and the NTNI consultation initiated separately.

VII. Entry and Exit from the G-SII List

54. The IAIS is also establishing procedures regarding an insurer's entry and exit from the G-SII list. An insurer not previously identified as a G-SII will be recommended for identification the first year the Proposed Methodology produces that outcome. Identification as a G-SII by the FSB will then create a two-year minimum presumption of G-SII status during which

the IAIS will recommend the identification be maintained even if the insurer's score drops below the threshold after Phases I through V. The IAIS' evaluation of an insurer's continuation as a G-SII will focus on changes in the insurer's risk profile and whether changes in the insurer's qualitative or quantitative assessments are likely to be permanent.

Question 26: What factors, such as stability in the G-SII list, should the IAIS consider when determining the appropriate presumption period for G-SII status?

VIII. Improved Transparency under the Proposed Methodology

55. The IAIS is considering whether and, if so, how to improve transparency with respect to the Proposed Methodology and the data used by the IAIS.

Question 27: How and, if so, to what extent should conceptual aspects of the Proposed Methodology, including , the data instructions, the data template, and the detailed formulas used for the calculation of indicator scores be made publicly available? If made publicly available, who should disseminate this information? What factors should the IAIS consider in this respect?

Question 28: How and, if so, to what extent should the resulting score be communicated to the prospective G-SII?

Question 29: How and, if so, to what extent should the data used for the calculation of the scores and the resulting scores be made transparent to the public? If made publicly available, who should disseminate this information? What factors should the IAIS consider in this respect?

Appendix

Table 1. Five categories of the IAIS indicator-based assessment under the Proposed Methodology.

Category: **Size**		
Indicator	***Content***	***Rationale***
Total assets	Total on balance sheet asset size	Straightforward indicator of size
Total revenues	Sum of insurance gross premium earned, investment income, realised gains and losses, fees and commissions, and other income	Indicates the extent or scale of financial services of an insurer from a different angle (Looking at only asset size may underestimate activities of non-life insurers)

Category: **Global activity**		
Indicator	***Content***	***Rationale***
Revenues derived outside of home country	Sum of the total revenues recognized from jurisdictions outside the home country	Indicates the extent of global activity from a revenue perspective
Number of countries	Number of countries where a group operates with branches and/or subsidiaries outside of the home country	Indicates the extent of global activity from an operational perspective

Category: **Interconnectedness**		
Indicator	***Content***	***Rationale***
Intra-financial assets	Sum of lending to financial institutions and holdings of securities (debt securities, commercial paper, certificates of deposit and equity) issued by other financial institutions	Indicates the potential for failure or distress of an insurer to impact the financial system through fire sales of assets
Intra-financial liabilities	Sum of borrowing from financial institutions and issuance of securities (debt securities, commercial paper and certificates of deposit) owned by other financial institutions	Indicates the degree to which failure or distress of an insurer could impact those with exposures to it

Reinsurance	Gross technical provisions for reinsurance assumed business	Indicates the degree of interconnectedness with the insurance sector through reinsurance transactions
Derivatives	Gross notional amounts of derivatives outstanding including some types of embedded derivatives	Indicates the degree of interconnectedness with the financial system through derivatives transactions
Turnover	Two ratios: (a) Ratio of total purchase of invested assets[19] plus total sale of invested assets to total assets, and (b) Ratio of total sales (issuance) of funding liabilities* plus total retirement of funding liabilities to total liabilities	This indicator could point towards insurers that are more active in the capital markets than is normal for a traditional insurance business
Level 3 assets	Combination of: (a) Total level 3 assets, and (b) Ratio of total level 3 assets to sum of level 1, 2 and 3 assets[20]	Indicates the potential scale of fire sales of illiquid assets by an insurer in distressed financial market situations. In its ratio form it could point towards insurers that are more active in markets for complex assets than is normal for a traditional insurance business

[19] In accordance with cash flow statements

[20] Level 1 Assets are based on unadjusted, quoted prices for identical assets in an active market. Level 2 Assets are based on quoted prices in inactive markets, or whose values are based on models - but the inputs to those models are observable either directly or indirectly for substantially the full term of the asset. Level 3 Assets are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

Category: **Non-traditional insurance and non-insurance (NTNI) activities**		
Indicator	***Content***	***Rationale***
Non-policy holder liabilities and non-insurance revenues from financial activities*	Combination of: (a) Total on balance sheet liabilities minus all policyholder liabilities (b) Ratio of (a) to total on balance sheet liabilities, (c) Total revenues from financial activities of non-insurance businesses, and (d) Ratio of (c) to total revenues * all technical provisions held for fulfilling insurance contracts	Indicates the extent to which an insurer conducts NTNI activities using both balance sheet and revenue figures Policyholder liabilities are a proxy for traditional insurance activities: "total liabilities minus policyholder liabilities" indicates NTNI activities In its ratio form it could point towards insurers that do more NTNI activities than is normal for traditional insurers
Derivatives trading	Gross notional amount of CDS protection sold	Indicates the scale of CDS protection sold which links an insurer with other parts of the financial system An insurer's distress or failure could impact financial positions of buyers of CDS protection
Short term funding	Combination of: (a) Absolute sum of: • Short term borrowing, • Commercial paper issued, • Certificates of deposit issued, • Gross value of collateral received from repos, and • Gross value of collateral received from securities lent; and (b) Ratio of sum of the above mentioned items to total assets	Indicates the extent to which an insurer could be involved in maturity transformation A large degree of short-term funding is a feature of financial institutions involved in maturity transformation Ratios pointing to a larger-than normal amount of short-term funding could signal an insurer venturing into this kind of business and assuming the liquidity risks that come with it, including the potential for fire sales of assets
Financial guarantees	Sum of: (a) Gross notional amount of debt securities including structured finance insured for financial guarantee. Not including CDS	Financial guarantee and mortgage guarantee products link an insurer with other parts of the market and are correlated with the economic cycle

	protection sold or surety bonds, and (b) Risk in force for mortgage guarantee insurance, which is the gross mortgage default amount covered by all mortgage insurance policies issued	An insurer's distress and failure could impact the financial positions of guaranteed parties
Minimum guarantee on variable insurance products	Total technical provisions for variable annuities and contingent annuities including additional technical provisions for any guarantees	Variable insurance products (including variable annuities and unit linked products with capital protection) most often include some type of guaranteed levels of payment to policyholders: attempting to pay guaranteed amounts could accelerate asset sales by an insurer and exacerbate already distressed market conditions There is also the possibility that hedging strategies for guarantees could adversely affect markets in times of wider market stress
Extent of liquidity of insurance liabilities	Amount of liabilities that can be surrendered upon request within short time frame with and without penalties.	Indicates the potential for an "insurance run" to occur because the liabilities are more exposed to being "on demand" than traditional insurance liabilities

Category: **Substitutability**		
Indicator	***Content***	***Rationale***
Premiums for specific business lines	Combination of: (a) Direct gross premiums written and assumed premiums for catastrophe coverage (b) Direct gross premiums written and assumed premiums for credit coverage including mortgage guarantee coverage, financial guarantee and export credit coverage, (c) Direct gross premiums written and assumed premiums for aviation coverage, and (d) Direct gross premiums written and assumed premiums for marine coverage	Indicates the degree of lack of substitutability in some specific insurance markets The three markets selected are considered to be significant and highly concentrated markets in a global context

Table 2. Weights given to each category and individual indicator under 2013 Methodology

Category	*Category weighting*	*Individual indicator*	*Indicator weighting [for 2011 data]*
Size	5%	Total assets	2.5%
		Total revenues	2.5%
Global activity	5%	Revenues derived outside of home country	2.5%
		Number of countries	2.5%
Interconnectedness	40%	Intra-financial assets	5.7%
		Intra-financial liabilities	5.7%
		Reinsurance	5.7%
		Derivatives	5.7%
		Turnover	5.7%
		Large exposures	5.7%
		Level 3 assets	5.7%
Non-traditional insurance and noninsurance activities	45%	Non-policy holder liabilities and non-insurance revenues	6.4%
		Derivatives trading	6.4%
		Short term funding	6.4%
		Financial guarantees	6.4%
		Minimum guarantee on variable insurance products	6.4%
		Intra-group commitments	6.4%
		Liability liquidity	6.4%
Substitutability	5%	Premiums for specific business lines	5%