

Resolutions of comments for the Public Consultation on Liquidity Metrics (Phase 2)

Introduction

- Between 18 November 2021 and 24 January 2022, the IAIS consulted on Phase 2 of the Liquidity Metrics project. The public consultation built on the Phase 1 outcomes and comments received during the previous consultation. It focused on the two approaches that the IAIS has developed to monitor liquidity risk, namely the:
 - Company Projection Approach (CPA); and
 - Exposure Approach (EA), including the Insurance Liquidity Ratio (ILR).
- In addition to those two approaches, the IAIS consulted on aspects of insurers' own liquidity metrics that are also part of Phase 2.
- The IAIS received numerous comments that provided valuable input for further advancing this work.
- Following the close of the consultation, the IAIS progressed work on the liquidity metrics project during 2022, taking into account feedback collected, and finalised the metrics that will be used as an ancillary indicator for liquidity risk monitoring as part of the Global Monitoring Exercise (GME).
- This document provides high-level resolutions for the comments received during the public consultation.
- Some comments requested recalibrations of the ILR factors for either liquidity sources or liquidity needs. The recalibration was conducted between May and August 2022, using the 2022 Individual Insurer Monitoring (IIM) data.
- The Level 2 Document – *Liquidity Metrics as an ancillary indicator* is published together with this document.

Reference	Summary of comments received	IAIS response
General comments on the liquidity metrics project, its objective, data sources and scope (Q1 – Q4)	There was broad support for the general objective and usage of the liquidity metrics. There was support for both approaches presented in the public consultation. Many respondents emphasise that neither of the proposed approaches would, in their view, be useful for either liquidity risk management or microprudential liquidity risk supervision. Instead, group specific liquidity risk management and local jurisdictional supervision were widely seen as superior to both the EA and CPA. Some respondents added proposals for other liquidity metrics. It was also mentioned that liquidity stresses can differ significantly from other stress scenarios. Liquidity risk of separate accounts is mostly borne by policyholders. The remainder is generally not seen as a macroprudential concern. It should therefore solely be monitored by the local supervisors.	The IAIS welcomes the support for the liquidity metrics project. The liquidity metrics were developed by the IAIS as an IIM ancillary indicator as part of the GME. They are not intended to be used by jurisdictions as a regulatory requirement. Instead of that, the liquidity metrics will serve as a tool to facilitate the IAIS' monitoring of the global insurance industry's liquidity risk and for the IAIS to assess insurers' liquidity exposure from a macroprudential perspective. The other proposed approaches are not focused on liquidity but are generally used for other purposes (eg solvency measurement, accounting). Their inclusion as a liquidity metric is therefore not further considered by the IAIS. The liquidity metrics as part of the GME will focus on the general account. Seen from a microprudential perspective, lapses of separate account products may carry a liquidity risk for the insurer, depending on the legal and contractual requirements. In addition, large scale lapses of separate

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		account products might increase liquidity risk in general through the asset liquidation channel. In order to lower the reporting burden for insurers participating in the IIM, the separate accounts will be not included in the ancillary indicator in 2023-2025. Developments of separate accounts will be monitored through the sector-wide monitoring (SWM).
Fungibility (Q5 – Q6)	Fungible liquidity pools are generally seen as being very important for the management of liquidity in a group as well as for microprudential supervision of said groups. Most respondents nevertheless propose to not include them into the GME. Reasons given are: • That the additional reporting burden outweighs the benefits; • That there is no simple way to aggregate the pool results to an entity level; • That such an approach might underestimate fungibility between pools; • That a simplified approach is sufficient for macroprudential purposes; and • That any approach could be accompanied by more detailed information from the insurer's own model, where needed.	The IAIS agrees with the assessment of the general importance of fungible liquidity pools. The IAIS acknowledges the reasons presented by respondents. The liquidity metrics in the 2022 Level 2 document will focus on the group (enterprise) level instead of the level of fungible liquidity pools. Data on fungible liquidity pools will not be collected for the purposes of the ancillary indicator. Information from insurer's own models can be requested by local supervisors, where necessary, for the purpose of the collective discussion.

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Consideration of capital (Q7 – Q8)	Strong support to include capital instruments in the CPA and EA metrics calculations, as described in the public consultation document 2021, with a preference for the simpler method.	Capital instrument will be considered in the CPA and EA. For EA, the simpler method (that is preferred by stakeholders) will be used.
	Dividends should be analysed separately as their payment depends on insurers' discretion.	Paid dividends will be analysed separately, considering that their payments depend on insurers' discretion.

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Company Projection Approach – description, categories of cash flows, haircuts, pros and cons (Q9 – Q16, Q28)	Support for the proposed CPA process with some reservations with regards to the EA-like haircuts, support for three categories of cash flows. Majority of responses agreed with proposed baseline cash flow projection. Various opinions on the granularity of the CPA. Some stakeholders raised reservations on haircuts for assets, but recognised that there is a lower reporting burden if ILR haircuts and liquidity sources are used. Even split between calculation at a group level or a legal entity level, but recognised that the group level is more efficient. Almost all responses agreed with a list of benefits and limitations related to cash flow approach. There were suggestions to add separate banking, insurance, and asset management cash flows into the CPA calculation.	The IAIS decided to apply (at least in the beginning) the CPA with the lowest granularity of required cash flows: • Aggregate cash inflows and outflows will be collected for three categories of cash flows (ie operating, investing and financing); • More granular cash flows may be requested on an ad hoc basis; and • EA-like haircuts will be utilised to lower the reporting burden. Although consolidated group-wide projections would be preferable, the IAIS recognises that some firms may do these projections on an entity level basis and therefore, not have access to consolidated projections. In such circumstances, firms may submit the cash flows for the largest insurance entity (or a group of entities), that comprise preferably at least 70% of the insurer's consolidated total assets.
Company Projection Approach – Liquidity Stress Test for Insurers (Q17 – Q27)	There was broad support for several aspects of the CPA Liquidity Stress test for insurers. More specifically, stakeholders expressed support for:	The IAIS proposes to use three time horizons for the CPA: 1-month (1M), 3M and 1Y and will retain the stress on all three types of cash flows.

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	- The longer time horizons, especially one year (1Y) but also three months (3M); - Stressing all three proposed types of cash flows (including detailed suggestions); - Inclusion of stress parameters for insurance liabilities (including detailed suggestions); and - A single stress scenario. Areas without consensus are primarily: - The adverse liquidity stress scenario; and - The proposed gross domestic product (GDP) and market parameters. Several respondents highlighted the issues around stressing insurer liquidity cash flows: - There is a fundamental difference between the profiles of both assets and liabilities for insurers compared to banks; - Some respondents find it difficult to calibrate a liquidity stress from the given parameters without detailed guidance; - Detailed liquidity stresses are likely to be more beneficial but involve an additional burden on firms and may not be that useful for the reporting firm;	The IAIS will include a stress on insurance liabilities in the CPA and apply a single stress scenario, aggregating the relevant cash flows. The limitations of the metrics are noted. Any single metric will have limitations if applied globally on the level of individual insurance firms. The IAIS will balance the potential additional information from more complex calculations against the additional burden on firms. The adverse liquidity stress scenario consists of adverse macroeconomic, market related and other parameters (eg mass lapse ratios for liabilities). A detailed setting of the liquidity stress test, including its parametrisation will be described in a Level 3 document that will be updated annually and shared with participating insurers (as a part of the annual IIM data collection package). The IAIS acknowledges that the CPA data was collected only once, during Phase 2 in 2022 (in comparison to the ILR data that was collected in over five data collections).

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	- Asset liquidations may impact the size of policyholder liabilities for companies with Asset Liability Management (ALM); and - A simultaneous stress of assets and liabilities may be too onerous and not realistic. On the adverse liquidity scenario, market parameters and GDP, some respondents considered the scenario and parameters plausible as a downturn scenario. Others highlighted perceived issues, including: - Amount of parameters was excessive; - Difficult to translate the parameters into a liquidity scenario; - Not reflecting the most stressed conditions for insurers; - Targeted to bank stresses; - US focused; - Credit focused; - Ignoring specific derivatives; - Should be applied to product lines; - Stresses should be aligned with Solvency 2/Own Risk Solvency Assessment (ORSA);	The parametrisation of the liquidity stress test may be further refined annually and its parametrisation adjusted if needed. Moreover, the IAIS will be able to quickly react and use other adverse stress scenarios that reflect actual macroeconomic developments. The IAIS will also provide further guidance on how to calibrate a liquidity cash flow stress, based on the given parameters. Following the 2021 public consultation feedback, the liquidity stress will be applied to all three categories of cash flows. Insurers will, in the short- to medium-term, have a choice between: - Applying any existing and currently available internal liquidity stress (with parameters, calibrations and any assumptions clearly outlined in the annual IIM Explanatory Statement); or - Applying the IAIS prescribed liquidity stress with the relevant variables as defined by the IAIS. Should any insurer be unable to apply the liquidity stress test, the IAIS will apply a

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	- Should be up to the individual firms and a severity level of the stress should be specified; - Does not identify the unique risks faced by a single company; - Stressed VIX levels are within normal bounds; - Is based on the Federal Reserve Board's 2017 Dodd-Frank Stress Test and not the 2012 Dodd-Frank test; and - Insurers will have their own, individual stress scenarios but a single stress scenario, aggregating all cash flows is more suitable for macro prudential supervision. The IAIS could leverage jurisdictional stress scenarios if these were sophisticated and risk sensitive.	general blanket (factor-based) stress to the relevant baseline cash flows. As the CPA is further refined, the IAIS' prescribed stress is likely to change as a more thorough understanding of systemic liquidity stresses is developed. Details regarding the prescribed liquidity stress tests will be provided to participating insurers annually via relevant Level 3 documents. The IAIS is also aiming to harmonise the parameters and the severity of the stress (calibration) across the insurers in the Insurer Pool. Once the CPA calibration is completed, in the final metric, insurers will not be allowed to set their own liquidity stresses, but rather a single liquidity stress scenario will be applied for all participating insurers. The IAIS will simplify the Liquidity Stress Test (LST) setting, including a reduced number of stress variables, leaving more space for insurers' stress considerations.
Exposure Approach – General comments (Q29 – Q31)	Strong support for the refined approach introduced in 2021. Liquidity profiles within the liquidity sector differ greatly, and therefore some sort of segregation in the ILR liquidity needs factors is required to ensure effective monitoring of the industry. The three	Life, non-life and reinsurance business models will be differentiated by the ILR liquidity needs as proposed in the public consultation document 2021.

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	proposed liquidity profiles appear to be reasonable: life insurers, non-life insurers and reinsurers. Majority of stakeholders supported the usage of two time horizons, one main and one supplementary. Both apply to all types of companies. 1Y time horizon remains the main time horizon. Factors for 3M time horizon may be further refined and potentially combined with CFs. Some stakeholders raised reservations against copying the LCR approach as there are fundamental differences between banks and insurers.	The main time horizon remains 1Y. The 3M time horizon will be used as a supplementary metric. Factors for 3M time horizon were refined and recalibrated in 2022. An interplay between the CPA and EA was tested, but the IAIS decided to not create a combined metric in 2022. The factors for the 3M time horizon may be further refined in 2023-2025.
Exposure Approach - Liquidity sources (Q32 – Q42)	Financials: • Include debt and equity instruments issued by financials; • Consider both default risk and credit spread risk for haircuts; • Consider systemic risk (insurers are also part of the larger financial market); • Some participants asked for higher haircuts (ie lower factors) for financials vs non-financials (liquidity of financials is typically correlated with developments in financial markets and the broader economy). Others suggested treating financials with the same weights as non-financials; and	Financials: • Debt and equity instruments issued by financial counterparties will be included into the ILR Liquidity sources; • Based on the recalibration conducted by the IAIS in 2022, the haircuts of exposures to financial counterparties will be slightly higher than haircuts for exposures to non-financials, acknowledging rationale provided by some stakeholders; and

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	Haircuts on liquid assets should be used only under stressed conditions.	Instruments without sufficient liquidity continue to be excluded.
	Investment funds: - Include a more detailed definition of the funds; - Factors are perceived as being too low by a number of stakeholders; - Distinguish mutual funds vs segregated funds; and - Differentiate between general money market funds (MMFs) and ones that can only invest in government securities.	Investment funds: - Investment funds will be included into the ILR Liquidity sources. - Factors for various types of liquid investment funds were recalibrated in 2022 and increased by 5%. - More detailed definitions of the funds are provided in the Level 2 document, including description of their differences.
	Sovereign/ Public sector entities (PSE) /Government-sponsored Enterprise (GSE) debt instruments: - PSE exposures should be treated similarly to sovereign bonds if these exposures are part of the governmental structure in a jurisdiction. The liquidity will depend on the liquidity of the country where the PSE is localised. - Sovereign bonds with a lower rating should be allowed as liquidity sources, providing these bonds are on the balance sheet of the entity, are located in the same country and the market is liquid.	Sovereign/PSE/GSE debt instruments: - The IAIS conducted a recalibration of liquidity sources in 2022 and agreed to make no changes to sovereign/PSE/GSE debt instruments. - The IAIS acknowledges limitations of the proposed factor-based approach, however, thinks that these limitations are outweighed by its simplicity and low reporting burden.

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	- The local currency sovereign securities, regardless of rating, are rarely illiquid and can be considered the highest quality fixed income instruments in each of those markets. - A factor-based approach does not reflect asset duration, nor the dynamic between position, size, market capacity and time to liquidate institutional-sized positions.	
	Common equity (both financials and non-financials): Use higher factors for both of the proposed time horizons (especially for the 1Y time horizon) as asset prices are less sensitive to sudden market movements.	Common equity (both financials and non-financials): The IAIS conducted a recalibration of liquidity sources in 2022 and agreed to make no changes to common equity factors of non-financials. In addition, as described above, the IAIS decided to slightly lower factors for equities emitted by financial counterparties.
	Non-life premiums: - Be consistent across life and non-life and thus also consider life premiums. - Inconsistency between EA/ILR (balance sheet approach) and non-life premiums, claims and expenses (P&L elements).	Non-life premiums: The IAIS conducted a recalibration of liquidity sources in 2022 and agreed to make no changes to non-life premiums, which represent a material liquidity source for non-life and composite insurers.

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		The IAIS agreed that life premiums, claims and expenses will not be included in the ILR design due to following reasons: (a) combined ratio, net earned premiums and net incurred losses are measures predominantly used in non-life and these data elements reported by life insurers proved to be very volatile; (b) to avoid double-counting as the main sources of liquidity risk related to life policies are already covered by different liquidity needs.
	Certificates of deposit and undrawn committed lines: Factors are far too low according to some stakeholders.	Certificates of deposit and undrawn committed lines: The IAIS conducted a recalibration of the ILR factors in 2022 and agreed to make no changes to factors of certificates of deposit. In addition, the IAIS agreed to lower the factor for undrawn committed lines by 5%.
	Differentiation between 3M and 1Y time horizons:	

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	Rationale should be provided on differences between 3M and 1Y ILR time horizons.	Differentiation between 3M and 1Y time horizons: The shorter 3M time horizon includes slightly lower factors (and thus higher haircuts) for some liquidity sources, reflecting the shorter time available for liquidation of these liquidity sources (without incurring material losses) and also the higher sensitivity of asset prices to sudden market movements (that would normally recover in the longer run) in comparison to the longer 1Y time horizon.
	Additional relevant liquidity sources may be considered in the ILR calculation: - Convertible bonds and insurance asset management products; - Portfolio insurance asset management products; - Reinsurance recoverables; - Securitisations; - Commodities such as gold; - Some direct investments (with appropriate factors); - Less liquid tangible assets (for example Equity Release Mortgages (ERMs) in the UK) ;	Additional relevant liquidity sources may be considered in the ILR calculation: The IAIS conducted a recalibration of the ILR factors in 2022 and agreed to add no types of liquidity sources as they may lead to an increase of ILR complexity, an increase in reporting burden for insurers and to worse comparability across the globe.

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	• Pledged assets to ceding companies when claims arise (in the (re)insurance business model); and • Other assets proven to be liquid and low risk, possessing quality characteristics according to national discretion.	
Exposure Approach: Insurance Liquidity Needs (Q43 – Q51)	Surrender values: • Some stakeholders proposed to recalibrate and lower factors for retail and institutional surrenders; • Rationale was requested on why factors for retail and institutional surrenders differ; • A majority of responses rejected the proposal to conduct a detailed recalibration of factors for surrender values based on historical surrender rates of participating insurers. The main arguments for this rejection relate to the potential substantial reporting burden that this would imply; and • Support for the proposed 3M time horizon factors. Some respondents suggested its recalibration.	Surrender values: • The IAIS acknowledged some limitations of the current approach to surrenders, eg that the ILR calculation does not include or take into account any potential tax penalties or other tax implications occurring in some jurisdictions when life insurance contracts are surrendered by policyholders within a certain time period; • The IAIS noted stakeholders' preference to not conduct a recalibration of factors for surrender values;

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	Non-life and life claims and expenses: - Stakeholders expressed mixed views on the non-life claims and expenses. Some respondents pointed to the lack of rationality of the proposed factors, some noted inconsistencies concerning the proposal in the paper, and one comment disagreed with the use of incurred claims for the determination of non-life liquidity needs; and - There was broad support for the proposal that life premiums, claims and expenses should not be included in the ILR.	- It was agreed to make no changes to surrender value factors for both tested time horizons; and - In the IIM 2022 data collection, more than 16% of the sample experienced a surrender rate higher than 10% for policies held by institutional investors, while only more than 9% of the sample experienced severe lapse rates for retail insurance products. Non-life and life claims and expenses: - Non-life claims and expenses will be included in the ILR with factors as proposed in the Level 2 document. The IAIS acknowledged limitations mentioned by stakeholders and lower the factors from 85% to 40%. - Life premiums, claims and expenses will not be included in the ILR. Many life insurers mentioned in the previous IAIS data collections that loss and combined ratios are not metrics usually used in life insurance. Moreover, life business is already captured mainly by surrender values.

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	Reserving risk: - Some stakeholders agreed with the proposed approach to reserving risk; - The majority of respondents did not agree with the proposal claiming that reserving risk is not a primary liquidity topic; and - The proposed factor for life reserves seems to be more extreme compared to the factor applied for non-life.	Reserving risk: - The IAIS conducted a recalibration of the ILR factors in 2022 and agreed to lower the factor for life reserving from 2.5% to 0%. - The 2.5% factor tested in 2022 overstated the potential cash outflows for life insurers. Any changes to the life insurers reserves are more than likely not to impact next year cash outflows, but rather to affect future cash flows given the long-term nature of the business.
	Unearned premiums: - There were mixed views on the proposed approach. The main argument for the negative answers was the absence of a clear rationale for the factors; - Some respondents disagreed with the calculation of the percentage of unearned premiums included in liquidity needs based on the assumption that policies will be cancelled in the future, given that the cancellation impact is small in non-life insurance, for which products are mainly 1Y policies.	Unearned premiums: The IAIS acknowledges limitations of the current approach to unearned premiums but prefers to continue with the current proposal as it provides a good compromise between simplicity and accuracy.

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	And finally, one comment mentioned that the factors are too high for non-life insurers, since the cancellation rate is about 5%-10% for insurers of a specific country (Mainland China).	
	Reinsurance recoveries: - Respondents expressed mixed views on the proposal. A slight majority of collected responses rejected the proposed approach; - Some commented that the factors for reinsurance recoverable should be related to the rating quality of the reinsurer(s), as many insurance undertakings have strategic reinsurance partners with strong credit ratings; and - Some comments considered that the factors are too severe when assuming that a 1Y default probability for reinsurers is significantly lower than the proposed 50%, given also that there are reinsurers with high credit ratings. Furthermore, three to six months is the normal cycle for reinsurance recoveries.	Reinsurance recoveries: The IAIS noted reservations and conducted a recalibration of related ILR factors in 2022, agreeing to lower the factor for reinsurance recoveries from 50% to 25%.
	Catastrophe risk: A slight majority of responses did not agree with the proposed approach and the 1/250 probable maximum loss (PML);	Catastrophe risk: The IAIS acknowledged stakeholder comments regarding the use of a standardised 1/250 PML scenario;

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	- Many respondents rejected an usage of a standardised 1/250 PML scenario to be applied for catastrophe claim payments; - Some comments suggested the 1/200 PML scenario would be more consistent with other economic value-based risk metrics; and - Some suggested an approach based on the company's own assessment instead of a standardised approach.	- The IAIS agreed to use the 1/200 PML scenario; - The standardised PML scenario will not be used in the ILR in 2023-2025; and - Treatment of ceded catastrophe risk will be aligned with the treatment of reinsurance recoveries.
Exposure Approach: Non-Insurance Liquidity Needs (Q52 – Q62)	Bank deposits: - Full support to consider deposit guarantee schemes (DGS) in the ILR factors for bank deposits; and - Support for proposed factors as it is consistent with the view that under the stress scenarios, banks may be under additional pressure in the immediate short-term which can delay access to the cash deposits. No change required. Non-financial type of business that some insurance groups may conduct: - Support for the current proposal as long as the corresponding liquidity sources for the non-financial type of business is also excluded. In addition, the insurer should also assess the materiality of the cash flows arising from its	Bank deposits: - DGS will be reflected in the ILR factors for bank deposits. Bank deposits included in the DGS will get lower factors than other bank deposits; and - No further changes will be done with regards to bank deposits. Non-financial type of business that some insurance groups may conduct: - The IAIS decided not to create any new charge for non-financial non-insurance liquidity needs.

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	non-financial type of businesses and consider the need to include, if deemed as material; and • Liquidity sources, for the EA, should be rescaled for companies with significant non-financial business.	
	Derivatives: • Split views on inclusion of non-cash collateral in the ILR design; • Some stakeholders emphasised that also other types of collateral should be considered in the ILR; • Support for the 3M time horizon ILR treatment and factors for derivatives; • Support to consider some form of derivative assets in the ILR design; • Split views regarding the “floor” for insurers that don’t report data on derivatives; and • Support for a level playing field with some disclaimers.	Derivatives: • The IAIS decided to use the floor (for insurers that do not report data rows needed for the ILR liquidity needs) in the ILR calculation in order to maintain a level playing field; • The IAIS agreed not to include derivative assets in the ILR given data collected in 2022. The approach to derivative assets may be reconsidered in 2023-2025; and • Non-cash collateral will be considered in the ILR with a higher haircut.
	Operational, cyber and other risks: • Split views were received on operational and cyber risks; • Support to consider operational and cyber risk, but it is requested to back factors with more historical data and loss evidence;	Operational, cyber and other risks: • Liquidity needs for operational and cyber risks will be included in the ILR; • The IAIS recalibrated factors for operational and cyber risks in 2022

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	- Stakeholders suggested to collect data elements to test the factor levels; and - No other liquidity needs were proposed.	and decided to lower its factor from 5% to 2.5%; and No new liquidity needs are proposed for the ILR.
Other liquidity metrics (Q63 – Q64)	Generally, no disagreement with respect to the description of the several additional aspects that were included in the public consultation document. There is also agreement to not include these aspects in the liquidity metrics for the purpose of the GME.	The additional aspects will not be elaborated on in the Phase 2 document. A shorter summary of these aspects is deemed sufficient. Own liquidity metrics will not be included in the new ancillary indicator.
Next steps (Q65 – Q66)	Different views were expressed. Some stakeholders support one metric approach, others support a set of metrics. If a set of metrics is chosen, the IAIS should specify how it will be used and which metrics will be included. Some support the use of a single liquidity metric for liquidity risk monitoring at a macroprudential level, given the limited amount of liquidity risk inherent in the insurance industry. Others think that both liquidity metrics (ILR and CPA) offer different perspectives of an insurer's liquidity position, hence it would be useful to monitor both approaches and the metrics belonging to them. Some stakeholders emphasised that more metrics are needed to reflect variabilities in insurers' business models and especially in their liquidity needs.	The IAIS agreed to create a new IIM ancillary indicator called "liquidity metrics" that consists of the following metrics: - EA ILR 1Y time horizon; - EA ILR 3M time horizon; - CPA 1Y time horizon; - CPA 3M time horizon; and - CPA 1M time horizon. The IAIS' use of the ancillary indicator "liquidity metrics" in 2023-2025 will focus as much on understanding trends and drivers of liquidity risk for insurers and the industry as the relative level of the liquidity metrics for an insurer in the IIM Insurer Pool.

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		Because of the limitations of different assumptions and approaches, the IAIS developed multiple liquidity metrics for monitoring. The new ancillary indicator enables the IAIS to monitor liquidity using various time horizons and data sources (ie balance sheet and P&L elements, cash flows). The ancillary indicator will be reported and monitored during 2023-2025 and may be further reconsidered as a part of the IIM assessment methodology in its future regular reviews (eg in 2025).