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Regulatory developments in the global insurance sector

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Executive summary[1]

Region	No	Organisation(s)	Date	Regulatory developments
Global	1	Financial Stability Board (FSB)	7 October 2021	■ **The FSB released a progress report on global stablecoin arrangements** that discusses key developments since the publication of the FSB high-level recommendations in October 2020. Regulatory developments highlighted in the report include the following. ➢ While stablecoins are not being used for mainstream payments on a significant scale, vulnerabilities in this space have grown over the past year. Increased participation by retail investors could give rise to broader financial stability issues and the emergence of global stable coin (GSC) would pose greater risks to financial stability. ➢ The implementation of the FSB recommendations is still at an early stage. Approaches (to be) taken towards the implementation are different among jurisdictions, which could lead to the risk of regulatory arbitrage. ➢ Jurisdictional authorities have identified several issues that may warrant further consideration in the implementation, which include (i) conditions for qualifying a stable coin as GSC and (ii) prudential requirements for issuers, custodians and providers of GSC functions.
	2	International Monetary Fund (IMF)	6 October 2021	■ **The IMF published the Global Financial Stability Report 'COVID-19, Crypto, and Climate: Navigating Challenging Transitions'**. Key messages in the report relating to the financial sector include the following. ➢ Financial vulnerabilities continue to be elevated in many sectors. Warning signs, such as increased financial risk-taking and rising fragilities in the nonbank financial institutions sector, point to a deterioration in the underlying financial stability foundations. ➢ Asset valuation appears to be stretched in some market segments. Equity price misalignments have remained elevated in most markets, credit spreads have narrowed to below pre-pandemic levels, and house prices have risen rapidly in many countries. ➢ Vulnerabilities in investment funds remain and risks are rising at some nonbank financial institutions as they reach for yield to meet nominal return targets. For example, US and European life insurers have increased their investment in lower-quality bonds, seeking to enhance their

[1] Volumes 1 to 12 of the report 'Regulatory developments in the global insurance sector' are available only in Japanese. This executive summary is a summary of the Japanese version of the Volume 15 report. It is advised that you refer to the respective original materials for accurate information.

				return on investments. ➢ Policymakers should (i) address vulnerabilities in investment funds through enhanced prudential supervision and regulation, (ii) develop adequate frameworks for crypto asset service providers and (iii) strengthen the global climate information architecture (data, disclosures and sustainable finance classification).
	3	Financial Stability Board (FSB)	30 September 2021	■ **The FSB revealed its framework to assess vulnerabilities affecting the global financial system**. ➢ The framework is developed based on key principles, e.g. (i) to scan vulnerabilities systematically and with a forward-looking perspective, while preserving flexibility and (ii) to recognise differences among countries. ➢ Under the framework, gross vulnerabilities are first identified and then they are compared with an appraisal of resilience to identify the net vulnerabilities. ➢ Types of vulnerabilities in the financial sector in the framework include asset prices, asset quality, funding/liquidity and leverage.
	4	Basel Committee on Banking Supervision	20 September 2021	■ **Basel Committee issued a newsletter on cyber security**. Key messages in the newsletter include the following. ➢ Concerns over cyber threats and incidents have heightened due to, e.g., remote working arrangements and increased provision of financial services using digital channels. ➢ Banks are encouraged to adopt tools, effective practices and frameworks for cyber risk management that are aligned with widely accepted industry standards. ➢ Banks must continually strive to improve their resilience to cyber security threats and incidents.
Asia Pacific	-	-	-	-
Europe	5	European Insurance and Occupational Pensions Authority (EIOPA)	8 October 2021	■ **EIOPA published its second report on recovery and resolution of insurers**. Key information in the report includes the following. ➢ Most common measures taken include (i) cash injection, reinforcement of internal governance and risk management and additional provisioning in the recovery phase and (ii) discontinuation of the writing of new businesses, liquidation and sale of all or part of businesses in the resolution phase. ➢ Policyholders suffered losses in around 30% of the cases of resolution. External funds (such as

				public funds and funds from Insurance Guarantee Schemes) were used in 33% of the failure cases. ➢ Due to the lack of harmonised Insurance Guarantee Schemes in the EU, policyholders could be treated differently jurisdiction by jurisdiction. It is now decisive to have a minimum harmonised IGS framework in place in the EU.
	6	EIOPA	5 October 2021	■ **EIOPA set out its strategic priorities for 2022**. ➢ Priority areas highlighted include (i) integrating sustainable finance considerations across all areas of work, (ii) supporting the market and supervisory community through digital transformation and (iii) monitoring risks to the financial stability and conduct of business. ➢ Items to be addressed in the context of 'integrating sustainable finance consideration' above include (a) re-assessment of capital charges for the NatCat risk in the standard formula, (b) assessment prudential treatment for assets and liabilities associated substantially with environmental and social objectives and (c) development of guidance on the supervision of the use of climate change risk scenarios in ORSA.
	7	EIOPA	1 October 2021	■ **EIOPA expressed its views on the proposals of the European Commission on the review of Solvency II**. EIOPA's key messages are as follows. ➢ EIOPA welcomes the proposals; the proposals largely share EIOPA's opinions. Those include (i) the development of Insurance Recovery and Resolution Directive, (ii) inclusion of macro-prudential perspectives in Solvency II and (iii) the new extrapolation methodology of the risk-free curve. ➢ On the other hand, EIOPA expresses regret for the Commission's decision on a minimum harmonisation of Insurance Guarantee Schemes in the EU. EIOPA also is of the view that the removal of illiquidity considerations for the purpose of volatility adjustment calculations and relaxations regarding the calibration on the risk margin and interest risk capital charge could pose potential risks.
	8	European Commission	22 September 2021	■ **The Commission adopted (a) proposals to amend the Solvency II Directive and (b) a proposal for a new Insurance Recovery and Resolution Directive.** ■ Proposed amendments to the Solvency II Directive include the following. Proportionality: • To increase the size thresholds for the exclusions of small insurers from the

	scope of the Solvency II. • To establish criteria for the identification of low-risk profile insurers.
Reporting	• To require insurers using internal models to report to the supervisors an estimation of the Solvency Capital Requirement calculated with the standard formula.
Long-term guarantee measures	• To take into account in the extrapolated part of the relevant risk-free interest rates information from financial instruments other than bonds for maturities where the relevant risk-free interest rate term structure is extrapolated and where the markets for those financial instruments are deep liquid and transparent. • To require supervisory authorisation for the use of the volatility adjustment. • To apply a higher percentage (i.e. 85%) of the risk-adjusted spread in the volatility adjustment.
Macro-prudential tools	• To require insurers to assess the impact of plausible macroeconomic and financial developments on their risk profile in ORSA.
European Green Deal-related amendments	• To require insurers to identify material exposures to climate change risks and to assess the impact of long-term climate change scenarios on their business.

- Matters to be addressed in future amendments to the Delegated Regulation include the following.
  - Equity investments: To simplify the conditions for equity investments treated as ‘long-term’, which would expand the scope of equities that are subject to a lower risk factor. This could lead to the reduction in capital requirements by around €10.5 billion.
  - Risk margin: To lower the cost-of-capital rate used in the calculation of risk margin to 5%, which then would reduce the risk margin by more than €50 billion.
- The proposed recovery and resolution directive requires (i) insurers to develop a pre-emptive recovery plan and (ii) resolution authorities to develop a resolution plan. Regarding a recovery plan, it is supposed that at least 80% of the market is subject to the requirement.

				■ With regard to Insurance Guarantee Schemes, the Commission decided not to establish a harmonised scheme at EU level this time.
	9	Federal Financial Supervisory Authority of Germany (BaFin)	21 September 2021	■ **BaFin carried out a second survey for insurers affected by the July 2021 flood disaster**, in which 136 German property and casualty insurers and 28 reinsurers participated. Major findings from the survey include the following. ➢ Gross loss of €8.2 billion is expected for primary insurers as a worst case, around €6.3 billion of which is reinsured. Regarding the reinsurers surveyed, a gross claims expenditure is estimated at around €4 billion in the worst case, part of which is also reinsured. ➢ The impact on insurers' SCR coverage ratio is limited; there is no sign of a threat to their continued existence.
Americas	10	National Association of Insurance Commissioners (NAIC)	7 October 2021	■ **The NAIC performed stress testing on U.S. insurers' exposure to Collateralised Loan Obligations** (CLO). Key findings from the stress test include the following. ➢ Normal tranches rated AA and higher did not experience any losses under the three stress scenarios tested, while normal A-rated tranches experienced losses under Scenario C in 2019 stress testing. ➢ While U.S. insurers exposure to CLOs increased to $193 billion (by around 23%) compared to the previous year, exposure remains small (about 2.6% of total cash and invested assets). 78% of those CLO investments are rated single A or above, which is why the CLO asset class is considered not to present a risk to the industry as a whole. ➢ A few insurers, though, have concentrated investments in Combo Notes and low-rated tranche, which could give rise to significant losses when the environment is stressed.

Sources:

1. FSB ‘Regulation, Supervision and Oversight of “Global Stablecoin” Arrangements: Progress Report on the implementation of the FSB High-Level Recommendations
2. IMF ‘GLOBAL FINANCIAL STABILITY REPORT OCTOBER 2021’
3. FSB ‘FSB Financial Stability Surveillance Framework’
4. BCBS ‘Newsletter on cyber security’
5. EIOPA ‘EIOPA examines further aspects of insurers’ failures and near misses’
6. EIOPA ‘EIOPA sets out its strategic priorities for the coming year’
7. EIOPA ‘EIOPA’s comment on Solvency II proposals from the European Commission’
8. European Commission ‘Insurance rules’ review: encouraging solid and reliable insurers to invest in Europe’s recovery’
9. BaFin ‘Flood claims: Still no threat to companies’ continued existence’
10. NAIC ‘NAIC Releases Stress Testing Report on U.S. Insurers’ Collateralized Loan Obligations Year-End 2020 Exposure’

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