October 18, 2013

Chairman Mark Carney
Financial Stability Board
Bank for International Settlements
Centralbahnplatz 2
CH-4002 Basel
Switzerland
Via email: fsb@bis.org

Re: *Comments on Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions*

On behalf of the Financial Regulatory Reform Task Force of the American Academy of Actuaries[1], I am pleased to provide comments on the Financial Stability Board's (FSB's) Consultative Document on the Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions (the Key Attributes). In summary, we believe that the key attributes of an effective resolution regime should:

1. Focus on the orderly resolution of a G-SII in the event of its failure,
2. Respect the policy decisions of local jurisdictions, such as the prioritization of claimants, and
3. Recognize the contractual rights of third parties.

Our specific concern is that some of these Key Attributes could be interpreted to expand the rights of policyholders or rewrite contracts between counterparties, including reinsurers. If so, this could increase financial stress on the company in resolution, or the insurance industry in general, and thereby exacerbate the systemic risk associated with the company. The following are our observations on the Key Attributes as they pertain to insurers (Appendix II):

Draft Implementation Guidance: Resolution of Insurers
Questions for consultation

22. Are the general resolution powers specified in KA 3.2, as elaborated in this draft guidance, together with the insurance-specific powers of portfolio transfer and run-off, as specified in KA 3.7, sufficient for the effective resolution of all insurers that might be systemically important or critical in failure, irrespective of size and the kind of insurance activities (traditional and 'non-traditional, non-insurance' (NTNI)) that they carry out? What additional powers (if any) might be required?

[1] The American Academy of Actuaries is a 17,500-member professional association whose mission is to serve the public and the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

Comment: The powers specified in KA 3.2 appear sufficient for the effective resolution of an insurer. If we have a concern, it is that certain of the powers seem expansive. For instance, the power to unilaterally terminate contracts or write down debt (found in 3.2(iii)) or compel other entities to enter into contracts, (found in 3.2(iv)) may contradict local law and serve to transfer financial stress to other entities. This is the very essence of systemic risk that should be mitigated.

23. Should the draft guidance distinguish between traditional insurers and those that carry out NTNI activities? If yes, please explain where such a distinction would be appropriate (for example, in relation to powers, resolution planning and resolvability assessments) and the implications of that distinction.

Comment: No, it is unnecessary to distinguish between traditional insurers and those that carry out NTNI activities. It is, however, essential that the guidance respect the role of the local resolution authority, and the hierarchy of claims that have been established in the local resolution regime. Such regimes may give priority to traditional insurance policyholders and claimants over customers of the non-traditional activities.

24. Are the additional statutory objectives for the resolution of an insurer (section 1) appropriate? What additional objectives (if any) should be included?

Comment: We generally agree with the additional statutory objectives stated in Section 1, but are concerned with two aspects. First, Section 1.1 provides for preferential treatment of retail policyholders. This is a matter of public policy, which should be decided by the local resolution regime (which may very well be compatible with this objective). Second, Section 1.2. provides for continuity of insurance coverage and payments. It should be clear that that this objective should not extend coverage and payments on a more favorable basis than the terms and provisions of the existing contracts. To do so could increase financial stress on the company and the insurance industry (which may fund the resolution authority) thereby increasing systemic risk.

25. Is the scope of application to insurers appropriately defined (section 2), having regard to the recognition set out in the preamble to the draft guidance that procedures under ordinary insolvency law may be suitable in many insurance failures and resolution tools are likely to be required less frequently for insurers than for other kinds of financial institution (such as banks)?

Comment: No, we strongly believe that the scope should be limited to insurers designated as Globally Systemically Important Insurers (G-SIIs). The inclusion of any insurer that could be significant or critical if it fails is too arbitrary. This contingency was presumably considered in the deliberations to designate G-SIIs.

26. Does the draft guidance (section 4) adequately address the specific considerations in the application to insurers of the resolution powers set out in KA 3.2? What additional considerations regarding the application of other powers set out in KA 3.2 should be addressed in this guidance?

Comment: We have several concerns on Section 4. They are:

a. 4.1 It should be clear that these attributes apply to companies that are in resolution. This is to distinguish from those companies in rehabilitation. In some jurisdictions, prior to resolution, companies enter a period of rehabilitation or recovery that attempt to restore the company to

a viable state. These resolution attributes should only apply to companies that are no longer deemed viable.

b. 4.3 We are concerned that the stated objective to maximize value for policyholders and provide continuity of insurance coverage could be interpreted to introduce policy benefits more favorable than provided for under the contract. As stated earlier, resolution should preserve contractual rights, to the extent provided for or possible under the local resolution regime. These key attributes should not introduce any extra-contractual benefits, the cost of which would be borne by the company or the insurance industry, thereby increasing systemic risk.
c. 4.3(iii) We disagree with the power to enter into new contracts of insurance. It is unclear to us why this power is needed. We do agree with the power to enter into new contracts of reinsurance, for existing contracts.

27. Does the draft guidance deal appropriately with the application of powers to write down and restructure liabilities of insurers (paragraphs 4.4 to 4.6)? What additional considerations regarding the application of 'bail-in' to insurers (if any) should be addressed in the draft guidance?

Comment: The draft guidance provides for a number of effective ways to restructure liabilities. We think it is important that the attributes recognize local resolution regimes. In particular, we recommend that resolution actions respect the rights of current and future claimants (Sections 4.5 and 4.6). The specific treatment of claimants should be as expressed by local resolution regimes. These regimes may give priority to different classes of claimants, such as claimants currently receiving benefits.

28. Is it necessary or desirable for resolution authorities to have the power to temporarily restrict or suspend the exercise of rights by policyholders to withdraw from or change their insurance contracts in order to achieve an effective resolution (paragraph 4.9)?

Comment: Yes, we believe that in order to protect policyholders in certain circumstances, it is necessary for resolution authorities to have the power to temporarily restrict or suspend policyholder liquidity. Without this power, companies in resolution may be forced to sell assets at distressed prices, thereby reducing the amount of proceeds available to policyholders. Limiting policyholder liquidity may better preserve values for policyholders and enable more fair treatment among policyholders. Forced asset sales to pay early withdrawing policyholders may increase losses to remaining policyholders or the insurance industry responsible for funding the resolution authority, thereby increasing systemic risk.

29. Are there any additional considerations or safeguards that are relevant to the treatment of reinsurers of a failing insurer or reinsurer, in particular to: (i) the power to transfer reinsurance cover associated with a portfolio transfer (paragraphs 4.7 and 4.8); and
(ii) the power to stay rights of reinsurers to terminate cover (paragraph 4.10)?

Comment: We disagree that the resolution authority should have the power to stay the rights of reinsurers. The event of a company entering into resolution should not cause reinsurance contracts to be rewritten. This could cause financial stress to the reinsurer, thereby increasing systemic risk. If it is determined that this right should exist in the event of resolution, then it should be made a required contractual provision – not imposed extra-contractually.

30. What additional factors or considerations (if any) are relevant to the resolvability of insurers or insurers that carry out particular kinds of business (section 8)?

Comment: None

31. What additional matters (if any) should be covered by recovery plans or resolution plans for insurers or insurers that carry out particular kinds of business (section 9)?

Comment: We strongly believe that assessments should be limited to insurers designated as G-SIIs. The inclusion of any insurer that could be significant or critical if it fails is too arbitrary. This contingency was presumably considered in the deliberations to designate G-SIIs. The plans should be flexible, as crises rarely unfold as envisioned by a pre-established crisis-resolution plan.

32. Are the proposed classes of information that insurers should be capable of producing (section 11) feasible? What additional classes of information (if any) should insurers be capable of producing for the purposes of planning, preparing for or carrying out resolution?

Comment: It is unnecessary for G-SIIs to produce this information. The actual information needed at the time of resolution may be very different than what is anticipated in advance. The requirement to produce this information on an ongoing basis is speculative and the associated cost would exceed any likely benefit. Moreover, local regulatory regimes normally have existing reporting requirements that have been deemed sufficient.

33. Does this draft Annex meet the overall objective of providing sector-specific details for the implementation of the Key Attributes in relation to resolution regimes for insurers? Are there any other issues in relation to the resolution of insurers that it would be helpful for the FSB to clarify in this guidance?

Comment: None

Thank you for this opportunity to comment. If you have any questions, please contact Tina Getachew, senior policy analyst, Risk Management and Financial Reporting Council, via email (getachew@actuary.org) or phone (202-223-8196).

Sincerely,
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