

## **GFIA position on the FSB's Consultation on identification of critical functions and critical shared services**

### **General comments**

The GFIA welcomes the opportunity to respond to this consultation by the FSB on the identification of critical functions and critical shared services in the context of recovery and resolution planning for systemically important insurers. We support the FSB's encouragement of cross-border supervisory co-operation on resolution and trying to develop a common understanding of critical services.

We also welcome the recognition by the FSB that critical functions would differ according to jurisdiction and to particular market conditions and the implication that a one-size fits-all approach would therefore not be appropriate.

The GFIA agrees with the FSB's conclusion that, after applying the proposed methodology, very few critical functions are likely to be identified. We concur and would therefore question whether this approach is proportional to the outcome envisaged.

### **Answers to consultation questions**

*1. Are the definitions of "critical functions" and "critical shared services" appropriate for the insurance sector?*

The term "critical functions" is defined in the guidance using two elements: (1) critical functions are provided by an insurer to third parties not affiliated with the firm and (2) the sudden failure to provide that function would be likely to have a material impact on the financial system and the real economy, give rise to contagion, or undermine the general confidence of market participants.

The circumstances when sudden failure to provide a function may lead to a material impact on third parties are then set out as: (a) if no mechanism is in place to ensure the function's continuity and (b) the impact falls into one of the listed categories, such as: where the insurance coverage is vital for third parties to carry out economic activity or go about their daily lives; or policyholders are dependent on insurance payments being made to them; or where it may cause the insurer to dispose of large quantities of assets.

Given that this guidance relates to policy measures designed to address systemic risk, it is important that the focus of the assessment of critical functions is clearly based on their potential ability to materially affect the stability of the financial system and the real economy, as reflected in the FSB's definition of critical functions. We are concerned that, in discussing point (b) above, it is not sufficiently clear that these categories must be considered as part of the financial stability and real economy analysis, and may be read instead as inappropriately extending the potential scope of what may be a critical function beyond those activities that can be material to the financial system.

We therefore consider that the discussion of the categories should be amended to clarify that these must be read within the wider context of a likely material impact on the stability of the financial system and the real economy.

*2. Should critical functions be identified based on whether the disruption of the activity would adversely impact the stability of the financial system or the functioning of the real economy, or both?*

In the GFIA's opinion, the FSB's focus should exclusively be on identifying risks to the global financial system. We note that the guidance primarily focuses on G-SIIs but also that the examples of critical functions are characteristic of traditional insurance.

In the GFIA's view, the guidance drifts into dealing with domestic insurance markets, because it attempts to identify where a large market share in a product area may lead to significant negative externalities if the product is suddenly withdrawn. The GFIA would point out this type of domestic competition analysis falls under the remit of competition authorities, and remedies to address these types of issues require careful analysis and should not be taken lightly.

All insurance is critical to those who buy it, as well as for the functioning of the economy. The GFIA doesn't see why regulators would attempt to decide which insurance lines are more critical than others.

*3. Is the methodology for identifying critical functions laid out in the paper appropriate for the insurance sector? If not, what aspects are missing or need to be changed?*

The GFIA regrets to see that the differences between the insurance and banking business models are still not fully taken into account in this proposal. This is an important concern which we have repeatedly raised in our previous responses. Even if in the new annex to the *Key Attributes* (dealing with the resolution of insurers) more recognition is given to this issue (a fact which we welcome), this document makes a number of confusions (e.g. regarding the interconnectedness of insurers and reinsurers, the potential knock-on effect of an insurer's failure, the focus on sudden failure).

On several occasions, the FSB speaks about the consequences of an insurer's failure and emphasises the subsequent contraction in insurance supply. In the GFIA's view, the FSB fails to take into account the natural equilibrium in the insurance business which means that, when markets contract, prices automatically rise to reflect the lower supply. New capital will then flow in to satisfy the excess demand for insurance products (which are highly substitutable).

*8. Are there any other issues in relation to the identification of critical functions and critical shared services that it would be helpful for the FSB to clarify in further guidance?*

The consequences of identifying critical functions are unclear. Given that the list provided in the annex includes almost all insurance activities and products (most of which are traditional in nature), we fear that the criticality assessment risks being disproportionate to the few critical functions that are expected to be identified as a result.

In particular, an insurer should not be deemed to be "systemically important", if it is found to undertake "critical" activities, especially if those activities are traditional in nature.

#### About the GFIA

Through its 38 member associations, the Global Federation of Insurance Associations (GFIA) represents the interests of insurers and reinsurers in 58 countries. These companies account for around 87% of total insurance premiums worldwide. The GFIA is incorporated in Switzerland and its secretariat is based in Brussels.