A unique sector

Insurers should be regulated separately from banks and non-banks

By Angus Scorgie, chair of the GFIA Systemic Risk Working Group

The change in economic conditions over the past two years and the shift away from the ultra-low interest rate environment in many parts of the world has contributed to increasing policymaker attention on the non-bank financial intermediation (NBFI) sector.

The global insurance industry has become concerned by this policymaker focus because insurers are often wrongly included with non-banks and so, despite being a sector that is already highly regulated — or even over-regulated, there is a risk of new, inappropriate or unnecessary regulatory burdens for insurers.

Banks, insurers and non-banks are very different

The financial services industry is often seen by regulators as a single, homogeneous industry. This is an oversimplified view, as the industry consists of different sectors, each with its own objective to fulfil its customers' diverse needs. And this flawed perception that banks, insurers and non-banks are similar leads to the equally flawed assumption that banking regulation needs to be applied to insurance. This very often results in an unsatisfactory outcome for all parties.

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As an industry, we have long advocated that policymakers do not blindly apply banking regulations to the insurance sector, given the different business models and therefore the different risks that they pose to the financial system and the real economy. Similarly, we do not consider it justified that recent concerns about the NBFI sector affect the insurance sector.

The NBFI sector is diverse, encompassing many different types of financial institutions, such as money markets, financial intermediaries, venture capitalists, crypto-currencies and microloan organisations. Policymakers’ concerns are typically centred around the lack of regulation and supervisory oversight in some areas of the sector. Historically, the main concerns have been with money market funds or credit funds, which are often subject to little or no regulatory oversight, despite having grown exponentially in recent years.

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Although there are a few overlapping features with banks and non-banks, insurance is a unique sector. Insurers are exposed to risks that are different in nature, scale and scope to other financial sectors. The important differences are not always well understood by policymakers around the world, which can lead to two wrong assumptions:

- that banking regulations and requirements should also be applied to insurers; and,
- that concerns about the NBFI sector are directly relevant for insurers too.

The insurance sector provides many benefits for citizens, businesses and the wider economy. Poorly designed regulation and excessive requirements can undermine the role it plays by creating higher costs or fewer products, thus having a material, negative impact on the sector and the economy as a whole.

To raise awareness of this issue, GFIA’s Systemic Risk Working Group is developing a booklet on the different risks non-banks, banks and insurers face as a consequence of their activities, the different risks each therefore poses to the financial system and the fact that distinct regulatory approaches are thus needed at company level and that an activity-based approach is the most appropriate at the macroeconomic level.

Other issues on the radar

Engagement with the International Association of Insurance Supervisors (IAIS) has also been important

for GFIA's Systemic Risk Working Group over the last year.

Individual Insurer Monitoring (IIM) assessment methodology

The IAIS has continued to enhance the Holistic Framework for the assessment and mitigation of systemic risk in insurance, which is made up of an integrated set of supervisory policy measures, a Global Monitoring Exercise and implementation assessment activities. The IAIS work includes a triannual review of risk assessment in the Global Monitoring Exercise, in support of which the IAIS conducted a public consultation seeking input on the IIM assessment methodology used to calculate individual insurers' systemic risk scores.

In its February 2023 response, GFIA raised concerns about further potential increases in the data-reporting burden in the next round of data collection, including the expansion of liquidity risk-related data.

In reviewing the IIM methodology, GFIA believes the IAIS should carefully select data that is truly necessary to identify systemic or macroprudential risks. It should also consider using publicly available data to the maximum extent possible, taking into account the overall increase in the burden on insurers.

GFIA also highlighted the following key points:

- Stability and streamlining of data collection is paramount. New data fields and qualitative components have been added every year with little notice before the changes were implemented. Many of the new data fields are not available from the financial statement and must be produced specifically for the IIM.
- IIM data collection should be on a best-effort basis and proportionality should be ensured.
- The need to significantly expand data collection about reinsurance businesses is questionable. The combination of the IIM quantitative template, the IIM qualitative questionnaire and the reinsurance component of the Sector Wide Monitoring provides a lot of information on reinsurance exposures and cross-border reinsurance activities.
- Participants should have more time to complete the IIM. The timeline should also be provided well in advance, along with the data template and technical specifications.

Draft Issues Paper on roles and functioning of Policyholder Protection Schemes (PPS)

GFIA's April 2023 response to this IAIS Draft Issues Paper praised it as a welcome addition to the IAIS's previous work on the topic.

The Paper builds on developments such as the adoption of the revised set of Insurance Core Principles (ICPs) and the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) in November 2019.

In its response, GFIA highlighted four key points:

- The importance of having a jurisdiction-specific approach
- The need for clear roles and responsibilities for supervisors, resolution authorities and PPS
- The overall prudential framework, including any recovery and resolution requirements and PPS, should be balanced and not duplicative
- The importance of appropriate funding requirements

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