Position paper

Insurance Europe response to a proposed application of numerical haircut floors to non-bank-to-non-bank transactions

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Contact person:	Alexandru Ciungu, Policy Advisor, Macro-Economics & Life	E-mail:	Ciungu@insuranceeurope.eu
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Insurance Europe welcomes the opportunity to respond to the Financial Stability Board's consultation on a proposed application of numerical haircut floors to non-bank-to-non-bank transactions.

Answers to consultation questions

1. Do you agree that the application of the framework of numerical haircut floors as described in Section 3.3 to non-bank-to-non-bank transactions will help to reduce the risk of regulatory arbitrage and would maintain a level playing field?

Insurance Europe agrees that the proposed measures will help reduce the risk of regulatory arbitrage. However, Insurance Europe concurs with the report's conclusion that the value of non-bank to non-bank transactions is small and would only pose risks if market practices were to change in the future or if regulatory arbitrage activities were to occur.

While Insurance Europe supports the application of numerical haircut floors to non-bank to non-bank transactions where potential for risk is present, it is concerned that the implementation could result in excessive regulation.

Therefore, Insurance Europe believes that at least the following transactions should be exempted:

- Intra-group transactions;
- Transactions in which financing is received by regulated entities subject to regulatory capital and liquidity requirements such as insurance companies.

In Insurance Europe's view, these transactions do not pose any significant risk.

Insurance Europe aisbl
Rue Montoyer 51, B-1000 Brussels
Tel: +32 2 894 30 00 • Fax: +32 2 894 30 01
E-mail : info@insuranceeurope.eu
www.insuranceeurope.eu

Insurance Europe understands that transactions between banks are not affected by the FSB's proposed framework. In order to preserve a level playing field, it must be ensured that transactions between non-banks of the same type (which are subject to similar capital and liquidity regulation) are not unfairly penalized.

2. In your view, how significant is the current level of non-bank-to-non-bank transactions? Do you expect that level to increase going forward and why? What types of non-bank entities are, or could be, involved in such transactions?

As Insurance Europe doesn not have any empirical evidence available, it is not in a position to answer this question. However, in Insurance Europe's opinion it is unlikely that regulated non-bank financial entities such as insurance companies (which are subject to regulatory capital and liquidity requirement), are or will be significantly involved in non-bank to non-bank transactions other than for yield enhancement purposes.

3. Do the approaches set out above cover all potential approaches in applying numerical haircut floors to non-bank-to-non-bank transactions? Are there any other approaches? If so, please describe.

See response to question 2.

4. Please provide any comments you have on the strengths and weaknesses of the approaches set out above, as well as any other approaches you believe the FSB should consider. What issues do you see affecting the effective implementation of numerical haircut floors for non-bank-to-non-bank transactions?

The examples show clearly that the hybrid approach is the only one which is sufficiently flexible to allow an effective but not excessive application of haircut floors. Insurance Europe also feels that the hybrid approach will best allow to prudently and mindfully put into practice the objectives envisaged with necessary carve outs (as those suggested in the answer to question 1).

5. What forms of avoidance of the numerical haircut floors are most likely be employed for non-bank-to-non-bank transactions? Which of the proposed implementation approaches is likely to be most effective in preventing such avoidance?

Insurance Europe feels that applying the hybrid approach should provide the best route to prevent any potential avoidance strategies.

6. If different entity-type regulations are used, do you see the need to ensure comparative incentives across different entity types? If so, please describe any potential mechanisms that may help ensure comparative incentives across entity types?

Insurance Europe believes that different entity-type regulations will need to very carefully consider ensuring a level playing field across and within entity types. Insurance Europe would also strongly recommend appropriate carve outs for:

- Intra-group transactions ;
- Transactions in which financing is received by regulated entities subject to regulatory capital and liquidity requirements such as insurance companies.

7. If market regulation is used, should the FSB consider setting a materiality threshold of activity below which entities do not need to register? If so, what could be an appropriate level for such a threshold?

In the case of both market regulation and hybrid approach, Insurance Europe supports the introduction of materiality thresholds.

8. Do you see the need for a phase-in period in applying numerical haircut floors to nonbank-to-non-bank transactions, and if so how long should it be and why? Does the appropriate phase-in period vary depending on which approach is followed? Should it vary by jurisdiction based on the size and importance of the non-bank-to-non bank sector or should it be consistent across jurisdictions?

Insurance Europe would support a phase-in period. The definition of such a period should reflect the diversity of the infrastructures that are used by the broad types of entities which would be affected.