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AAE POSITION ON INSURANCE RECOVERY AND RESOLUTION

The Actuarial Association of Europe, on behalf of the European actuarial profession, supports this initiative to further enhance policyholder security of insurance and reinsurance undertakings across Europe.

The AAE recognises the debate in the funding of insurer failures – whether the costs (not previously met by shareholders or bondholders) should be borne by national governments (thereby all citizens), or by other industry participants (thereby implicitly all policyholders).

We also note the Directive does not reference Insurance Guarantee Schemes or Policyholder Protection Schemes. We believe resolution without clarity on such Schemes can never be complete.

Given the complexity of issues presented, at best a Directive may achieve minimum harmonisation.

The existing Solvency II regime has created powerful tools to monitor the risk position and with the Own Risk and Solvency Assessment (ORSA) undertakings are already asked to inform shareholders and the supervisor about their expectation and possible risks. Since its introduction in 2016, the requirement to install strong holistic risk management within insurers has led to a risk-adequate capitalisation regime and also identification and management of other risks such as liquidity and emerging risks. The parts of the IRRD relating to recovery should not compete with or contradict the existing Solvency II regime.

We have outlined some issues relating to the proposed IRRD below.

1. Recovery plans and pre-emptive recovery planning

The AAE sees recovery planning as a risk management process, and resolution as a legal process. Solvency II already has a well-developed Pillar II framework that requires risk management systems and Pillar III includes material disclosure to shareholders, policyholders and supervisors on those risks. Solvency II Level 3 Guidelines give local supervisors a mechanism to clarify Solvency II requirements, and this has led to prescribed requirements on pre-emptive recovery planning in some countries (e.g. Netherlands, France, Ireland).

A formal requirement to create a recovery plan for in-scope firms might therefore be excluded from the planned IRRD, provided suitable alternative mechanisms were included in the IRRD that allowed the relevant resolution authority to understand how the firm might expect to react to events preceding resolution.

2. Resolution mechanisms

We share the view that a harmonised resolution process could be beneficial for policyholders and could be the preferable solution compared to winding-up under national insolvency proceedings. We support the inclusion within the IRRD toolset of the "solvent run-off" option.

Need to segment the application to policyholders

The main objectives of the IRRD should be the protection of policyholders' interests and fair treatment at a point of failure. We accept that it is important to include financial stability considerations, but these should not override policyholder protection considerations. This brings a lot of segmentation to be considered:

- Cases where a continuation of business by an undertaking is not viable, or where it is unable to maintain sufficient capital (and regulatory compliance).
- Situations where systemic risk results from a failure of an undertaking.
- Group structures and cross-border business models - undertakings (large or small) with significant amount of cross-border business, undertakings (EU or outside EU) with many EU subsidiaries or branches, undertakings with only domestic business (home equals host state), etc.
- Different insurance classes – mandatory insurance, property & casualty, savings and investments, pensions. All have different time horizons and different value/importance to the policyholder. The financial stability characteristics of savings-based insurance also typically differ from those of protection-based insurance.

Two cases we would suggest are emphasised more than in the original proposed Directive text are:

- Mutual insurers. Several parts of the text implicitly assume the existence of shareholders or bondholders distinct from policyholders, who can contribute to a bail-in before policyholders, but these parties may not exist with mutuals. The text also does not explicitly allow for mutuals to remain mutualised or for failed non-mutuals to have benefits reduced and turned into mutuals which would be useful possible resolution mechanisms and which are already allowed in certain member states. In the case of resolution of a mutual, it should be made an explicit option within the IRRD for the re-organised entity to continue as a mutual, if this is what mutual members (i.e. acting as the decision-making body for the entity) prefer. It should also be made explicit that mutual members (again, the decision-making body thereof) may decide to de-mutualise. It would be inappropriate for the IRRD or the new Resolution Authority to remove decision-making power completely from the members of a mutual.
- Insurers that are part of broader financial conglomerates to which both the BRRD and IRRD apply. In such circumstances, it would seem desirable, e.g., to allow / encourage resolution authorities to draft a single pre-emptive resolution plan covering the whole group, to avoid duplication of effort and cost.

Setting the scope of application

We do not agree that Resolution Authorities should provide resolution plans based on a coverage percentage of the market. It should be based on risk factors (of failure, or the impact of failure).

National supervisors are best placed to do this, but the Directive should set down guardrails or criteria to be used.

Some parts of the Directive seem to be copied from the BRRD. This potentially ignores the important fact that insurance risk (and failure) differs significantly from banking risk (and failure). It can generally be said that timescales in insurance are much longer than in banks – both in the visibility in any run-up to failure, and the time to resolve following failure. This means that in insurance, compared to banks, there is generally a much longer time to react to emerging problems, a caveat being that insurers or insurance groups can occasionally have large exposures to activities that have bank-like characteristics (e.g. AIG). We acknowledge that EIOPA has analysed similarities and differences between the BRRD and the proposed IRRD and considers them broadly justified.

Some comments on the IRRD text as proposed

A) Funding of the resolution process - as a result of an impact assessment (IA), the IRRD states on page 6: "*The IA also confirmed EIOPA's assessment that it would not be proportionate to require the financing of a resolution fund by the insurance industry or the building-up of liabilities by individual insurers that could be bailed-in to absorb losses and recapitalise failing insurers. The IA assessed that these measures would inflate the balance sheet of insurers to create a loss-absorbing capacity in proportion to their technical provisions; this would entail higher costs for the industry and impose additional servicing risks on the companies that would not be justified by materially increased benefits.*"

   However, there is no proposal for any Insurance Guarantee Scheme. We therefore see the need to have more clarity on how policyholder detriment would be addressed, and how the resolution process would be funded.

B) We observe extensive empowerment of the Commission / EIOPA to develop delegated acts, regulatory or implementing technical standards to lay down more concrete details (for example Recital 74).

   The lack of such details (at this stage) impedes an assessment of the concrete tasks for undertakings and for the resolution authority.

C) The proposal would require EIOPA to: "*(i) develop ten technical standards and six guidelines; (ii) establish one annual report on the use of simplified obligations; (iii) maintain a database on administrative sanctions reported by national authorities; (iv) take part in resolution colleges, make decisions in case of disagreement between supervisory and resolution authorities and exercise binding mediation."*

   The newly established resolution committee would also prepare the tasks for EIOPA in the areas covered by the proposal. In this context, relevant competent authorities shall be invited to participate, as members, into these developments, thereby maximising use of existing resources.

   These new resolution activities will bring additional workload to EIOPA at a time when EIOPA is still very engaged and active in bringing sufficient supervisory convergence across the EU. With regard to any recovery requirements, the required information

should as far as possible make use of Solvency II requirements (in particular, the supervisory ladder in case SCR is breached).

The administrative burden and costs resulting from the existence of a new authority should be kept as low as possible (in line with Article 67). A trade-off between the cost caused by such an authority and the positive effects is necessary.

D) Identification of causes of failure
The text is rather silent on e.g. the resolution authority having a responsibility for analysing why a specific firm has failed. However, the associated resolution process will often need to rely on such an analysis, e.g., if part of the resolution process involves benefit write-downs.