EIOPA-CP-16/009
2 December 2016

DISCUSSION PAPER

ON

POTENTIAL HARMONISATION OF RECOVERY AND RESOLUTION FRAMEWORKS FOR INSURERS

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Responding to this paper

EIOPA welcomes comments on the "Discussion paper on Potential harmonisation of recovery and resolution frameworks for insurers".

EIOPA would like stakeholders to focus, in particular, on chapter 4, "Building blocks of recovery and resolution" and the specific questions included in that chapter and in chapter 3 "Rationale for harmonisation".

Comments are most helpful if they:

- respond to the question stated, where applicable;
- contain a clear rationale; and
- describe any alternatives EIOPA should consider.

Please send your comments to EIOPA in the provided Template for Comments, by email **CP-16-009@eiopa.europa.eu**, by **28 February 2017**.

Contributions not provided in the template for comments, or sent to a different email address, or after the deadline will not be considered.

Publication of responses

Contributions received will be published on EIOPA's public website unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.

Please note that EIOPA is subject to Regulation (EC) No 1049/2001 regarding public access to documents and EIOPA's rules on public access to documents.[1]

Contributions will be made available at the end of the public consultation period.

Data protection

Please note that personal contact details (such as name of individuals, email addresses and phone numbers) will not be published. They will only be used to request clarifications if necessary on the information supplied. EIOPA, as a European Authority, will process any personal data in line with Regulation (EC) No 45/2001 on the protection of the individuals with regards to the processing of personal data by the Community institutions and bodies and on the free movement of such data. More information on data protection can be found at https://eiopa.europa.eu/ under the heading 'Legal notice'.

[1] Public Access to Documents (See link: https://eiopa.europa.eu/Pages/SearchResults.aspx?k=filename:Public-Access-(EIOPA-MB-11-051).pdf).

Abbreviations

BRRD	Bank Recovery and Resolution Directive
ESRB	European Systemic Risk Board
IAIG	Internationally Active Insurance Groups
IAIS	International Association of Insurance Supervision
ICP 12	Insurance Core Principle No 12
FSB	Financial Stability Board
G-SIFI	Global Systemically Important Financial Institution
G-SII	Global Systemically Important Insurer
HLA	Higher Loss Absorbency requirement
IGS	Insurance Guarantee Scheme
MCR	Minimum Capital Requirement
NCA	National Competent Authority
NCWO	No Creditor Worse Off
NSA	National Supervisory Authority
ORSA	Own Risk and Solvency Assessment
SCR	Solvency Capital Requirement

Executive summary

1. This discussion paper, which does not constitute a formal proposal by EIOPA, aims at gathering the views of stakeholders. It is composed of four chapters: (i) introduction, (ii) overview of existing national recovery and resolution frameworks in the EU, (iii) rationale for harmonisation, and (iv) possible building blocks of recovery and resolution. The main conclusions of each chapter are summarised below.

Overview of national recovery and resolution frameworks

2. The overview is based on the results of a survey on existing recovery and resolution frameworks conducted by EIOPA in the first half of 2016 and responded to by 30 National Supervisory Authorities (NSAs) of the EU and EEA.

3. EIOPA's survey on existing recovery and resolution frameworks shows that existing frameworks generally do not contain a requirement for the development of **pre-emptive recovery and resolution plans**, including **assessments of resolvability**. Following the designation of five EU insurers as global systemically important insurers (G-SIIs) by the Financial Stability Board (FSB), the relevant NSAs have reported that these G-SIIs are subject to recovery and resolution planning.

4. On the **early intervention powers**, the results of EIOPA's survey show a mixed picture with some of the powers being widely available across Member States (e.g. powers affecting the management and governance of insurers), whereas others are only available in a limited number of Member States and/or are subject to a variety of restrictions (e.g. the power to require the sale of subsidiaries, or the power to require the insurer to transfer its financing operations to the parent company).

5. Most of the NSAs reported that there is no officially designated administrative **resolution authority** for insurers in their Member States at the moment. The NSA and/or relevant ministry, sometimes together with an administrator, usually handle the resolution of insurers.

6. In resolution, authorities in charge of resolution pursue on average three **objectives**, which are usually ranked. In a majority of the Member States the protection of policyholders is the primary objective, followed by financial stability.

7. Existing frameworks usually do not specify clear **conditions for entry into resolution**. A significant breach of Solvency II requirements was often mentioned by NSAs as a trigger for initiating the resolution of insurers.

8. The results for **resolution powers** show that most of the powers listed in the FSB Key Attributes[2] are not widely available at this stage, except for the power to withdraw the authorisation of insurers which is included in Solvency II.

[2] Please see the FSB "Key Attributes of Effective Resolution Regimes for Financial Institutions", 15 October 2015.

9. With respect to **safeguards**, the survey shows that the "no creditor worse off" (NCWO) principle is the most common safeguard and is used in one third of the Member States.

10. The survey also reveals that a majority of the Member States do not have **(formal) crisis management groups or other equivalent arrangements** in place to deal with crisis situations of cross-border insurance groups. This finding does not apply to G-SIIs for which crisis management groups have been or are being established in Member States.

11. A total of twelve NSAs indicated that they have identified **gaps and shortcomings** in their existing framework. NSAs reported gaps and shortcomings, particularly, with respect to early intervention and resolution powers. On the other hand, a total of eight NSAs indicated that they have not identified gaps and shortcomings in their existing framework.

12. As a result of the identified gaps and shortcomings, seven NSAs indicated that there are **plans to reinforce the existing framework**. One NSA mentioned that the reinforcements are already in force, while another indicated that the reinforcements are expected to be in-force in 2018. In addition, one NSA reported that the text introducing the changes is planned to be adopted by legislators in mid-2017.

13. Finally, although Insurance Guarantee Schemes (IGSs) are out of the scope of the current work, the survey sought to obtain an overview of the current situation. Twenty-three Member States have in place one or more **IGSs**, with five Member States having an IGS for motor vehicle insurance only. The survey reveals that there are substantial differences between the IGSs in terms of their funding, mandate and coverage.

Rationale for harmonisation

14. EIOPA has analysed whether there is a need to harmonise national recovery and resolution frameworks for insurers in the EU, whereby the survey results are used as input to the analysis. The conclusion of EIOPA is that a harmonised environment should provide for **minimum harmonisation** only. Minimum harmonisation would benefit policyholders, the insurance sector and more generally the financial stability in the EU. This would also allow Member States to adopt additional measures at the national level, as long as the measures are compatible with the principles and objectives set at the EU level. This approach gives Member States the flexibility to address any national specificities of their insurance market at the national level. In addition, in order to avoid excessive (administrative) burdens for both insurers and national authorities, EIOPA is of the view that a harmonised framework should be applied in a proportionate manner.

15. In its analysis, EIOPA argues that the existing fragmented landscape of national recovery and resolution frameworks could cause significant impediments to the resolution of insurers, particularly of cross-border groups. A minimum degree of harmonisation contributes to avoiding fragmentation in the EU and could facilitate cross-border cooperation and coordination. This is necessary to ensure an orderly resolution of cross-border insurance groups and to avoid any unnecessary economic costs stemming from uncoordinated decision-making processes between national authorities in different Member States.

16. Harmonisation would also ensure that all Member States have in place a recovery and resolution framework for insurers in accordance with the principles set out in the Key Attributes which the FSB considers to be necessary for an effective resolution regime. The survey of EIOPA shows that most existing frameworks do not contain all those core elements. An effective recovery and resolution framework is particularly relevant in fragile market environments, like the current low interest rate environment which poses a risk to insurers.

17. In its analysis, EIOPA has also considered the potential drawbacks of harmonisation. At this stage, it is not demonstrated that in all Member States, normal insolvency procedures would be unsuitable to deal with insurance failures. It is neither demonstrated that in all Member states, existing powers and tools in national frameworks have been inadequate to deal with insurance failures in an orderly manner. It should, however, be noted that there have been no cases of large cross-border insurance group failures in the EU. It could also be argued that national frameworks reflect national specificities in a better way. Furthermore, harmonisation in the field of recovery and resolution could lead to additional administrative burdens and costs for insurers and national authorities. EIOPA is, however, of the view that the proposed approach of minimum harmonisation, in combination with the application of the proportionality principle, should adequately address these potential drawbacks.

Building blocks of recovery and resolution

18. This chapter includes EIOPA's preliminary views of what the main building blocks of a harmonised recovery and resolution framework for insurers could look like (see table 1). The different building blocks could also be considered separately, allowing for a more targeted approach.

19. EIOPA would like to seek stakeholders' views on the different building blocks and has included a set of questions to gather their feedback.

Table 1: Proposed building blocks of a harmonised recovery and resolution framework

Building blocks	Sub-building blocks
Preparation and planning	1) Pre-emptive recovery planning
	2) Pre-emptive resolution planning
	3) Resolvability assessment
Early intervention/ Recovery	4) Early intervention conditions
	5) Early intervention powers
Resolution	6) Resolution authority
	7) Objectives
	8) Conditions
	9) Powers
	10) Safeguards
Cooperation and coordination	11) Cooperation and coordination between national authorities and with third country authorities

1. Introduction

1.1 Legal basis

20. According to Article 8 of EIOPA Regulation[3], which lays down the tasks of EIOPA, the Authority, "*The Authority shall have the following tasks: (…)the development and coordination of recovery and resolution plans, providing a high level of protection to policy holders, to beneficiaries and throughout the Union, in accordance with Articles 21 to 26*;" (cfr. Article 8(1)(i) of EIOPA Regulation).

21. Article 25(2) sets out that "*The Authority may identify best practices aimed at facilitating the resolution of failing institutions and, in particular, cross-border groups, in ways which avoid contagion, ensuring that appropriate tools, including sufficient resources, are available and allow the institution or the group to be resolved in an orderly, cost-efficient and timely manner*."

22. In such context, EIOPA has developed this paper.

1.2 Context

23. Following the past financial crisis and the unprecedented public support to failing financial institutions during the crisis, the adequacy of crisis prevention and crisis management tools of national authorities to deal with crisis situations effectively has gained increasing attention.

24. The G20 and the FSB have developed an extensive agenda for stabilising the financial system and the world economy more broadly. In November 2011, the leaders of the G20 endorsed the recommendations issued by the FSB for a more effective resolution regime for financial institutions: *"Key Attributes of Effective Resolution Regimes for Financial Institutions"* (hereafter referred to as the "Key Attributes").[4]

25. Initially, the focus was primarily on the banking sector and on improving the banking regulation for dealing with crisis situations. In 2014 the European Commission adopted the Bank Recovery and Resolution Directive (BRRD) – a single rulebook for the resolution of banks and large investment firms in the EU. In 2014, the FSB supplemented the Key Attributes with additional guidance on how these should be applied to the insurance sector.[5]

26. Furthermore, the International Association of Insurance Supervision (IAIS) has initiated a number of initiatives in this field. This includes the development of:

    - a methodology for identifying G-SIIs, which has recently been updated.[6] An updated list of G-SIIs was published in 2015 containing five

[3] Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010.

[4] Please see press release of the FSB: http://www.fsb.org/wp-content/uploads/pr_111104dd.pdf?page_moved=1

[5] Please see FSB Key Attributes of an Effective Resolution Regime for Financial Institutions (See link: http://www.fsb.org/what-we-do/policy-development/effective-resolution-regimes-and-policies/key-attributes-of-effective-resolution-regimes-for-financial-institutions/).

[6] Please see IAIS's G-SII Assessment Methodology (See link: http://www.iaisweb.org/page/supervisory-material/financial-stability-and-macroprudential-policy-and-surveillance).

insurance groups located in the EU[7] for which a set of policy measures are applicable, such as recovery and resolution measures in accordance with the FSB Key Attributes but also a potential Higher Loss Absorbency (HLA) requirement[8];

- recovery and resolution standards for Internationally Active Insurance Groups (IAIG) (currently, ComFrame M3E3);
- resolution standards for all insurers and insurance groups (Insurance Core Principle No 12 (ICP 12), which deals with the winding-up and exit from the market of insurers.

27. All these initiatives aim to contribute to the improvement of the powers and tools of national authorities to deal with crisis situations.

28. At the European level, the European Systemic Risk Board (ESRB) has defined in its recent report on systemic risk in the EU insurance sector five sources of systemic risks and argued that *"an insurance recovery and resolution directive and an insurance guarantee scheme directive would form a holistic framework for dealing with insurer failure".*[9] Furthermore, the ESRB is continuing its work on recovery and resolution for insurers.

29. EIOPA, as the European authority for insurance and occupational pensions, has been proactively contributing to this discussion. For instance, EIOPA responded to the consultation papers of the European Commission and the FSB on, respectively, *"A possible recovery and resolution framework for financial institutions other than banks"* and *"Application of the Key Attributes of Effective Resolution Regimes to Non-Bank Financial Institutions*". In its responses, EIOPA emphasised the importance of effective recovery and resolution measures for insurers which take account of the specificities of the insurance sector.[10]

30. In 2013, EIOPA conducted a survey among NSAs in order to obtain a better understanding of the crisis prevention, management and resolution approaches and practices in the different NSAs.[11] The survey contained

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[7] These include Aegon N.V., Allianz SE, Aviva plc, Axa S.A. and Prudential plc. For a full list, please refer to the press release of the IAIS (See link: http://www.fsb.org/wp-content/uploads/FSB-communication-G-SIIs-Final-version.pdf).

[8] IAIS publication of G-SII Policy Measures 18 July 2013 (See link: http://www.fsb.org/wp-content/uploads/FSB-communication-G-SIIs-Final-version.pdf).

[9] ESRB: "Report on systemic risks in the EU insurance sector", December 2015 (incl. Annexes). The five sources of systemic risk identified by the ESRB are: 1) engagement in non-traditional and non-insurance activities, 2) procyclicality in asset allocation, 3) procyclicality in the pricing and writing of insurance, 4) common vulnerability to a double-hit scenario and 5) lack of substitutes in vital lines of insurance business. (See link: http://www.esrb.europa.eu/pub/pdf/other/2015-12-16-esrb_report_systemic_risks_EU_insurance_sector.en.pdf?d171a63f6e1d433f82e477d67416fbd5).

[10] EIOPA's responses to European Commission consultation and FSB consultation papers. (See link: https://eiopa.europa.eu/Publications/Responses/EIOPA_Response-COM_Consultation_on_recovery_and_resolution_for_nonbank_financial_institutions.pdf

and
https://eiopa.europa.eu/Publications/Responses/EIOPA_Response_to_FSB_Consultation_on_application_of_Key_Attributes_to_i.pdf)

[11] EIOPA report on *"Crisis Prevention, Management and Resolution Preparedness of NSAs"*, 29 November 2013 (See link: https://eiopa.europa.eu/Publications/Reports/Report_on_Crisis_Prevention_Management_and_Resolution_Preparedness_of_NSAs.pdfhttps:/eiopa.europa.eu/Publications/Reports/Report_on_Crisis_Prevention_Management_and_Resolution_Preparedness_of_NSAs.pdf).

questions covering crisis prevention, alerts, assessment, management and resolution, including several questions about cross-border cooperation. The survey revealed that there are substantial differences between Member States with respect to all of these aspects.

31. In 2014, EIOPA published an Opinion on *"Sound principles for Crisis Prevention, Management and Resolution preparedness of NCAs"*.[12] The overarching goal of the Opinion was to contribute to the maintenance of the financial stability in the EU, as well the protection of policyholders. The Opinion contains a set of sound principles reflecting prudent practices/references which should be considered when reviewing and further developing national frameworks. Examples are the sound principles on pre-emptive recovery and resolution planning (sound principle 5 and 6), resolution powers (sound principle 11) and cooperation and information sharing with other national authorities (sound principle 14).

1.3 Approach followed by EIOPA

32. In order to develop its view on harmonising recovery and resolution practices for insurers, EIOPA decided to follow a pragmatic and gradual approach by focusing on the main aspects of recovery and resolution which are defined as preparation and planning, early intervention and resolution.

33. Firstly, EIOPA conducted a survey among NSAs gathering information about the existing national recovery and resolution frameworks in Q1 2016. The results of this survey (hereafter referred to as "EIOPA's survey on existing recovery and resolution frameworks" or simply "survey") provided an overview of the current landscape of national frameworks and shed light on the differences between Member States and potential shortcomings in frameworks. Secondly, EIOPA assessed whether there is a need for a certain degree of harmonisation of existing recovery and resolution frameworks, also based on the results of the survey. Finally, the main building blocks of recovery and resolution are shaped in accordance with the FSB Key Attributes. It should be stressed that, at this stage, the building blocks are put forward for discussion and gathering of views of stakeholders and should not be interpreted as a formal proposal by EIOPA.

34. Following this pragmatic and gradual approach and after careful consideration, EIOPA decided not to include IGSs in its analysis. The survey revealed that there are substantial differences between IGSs in terms of their funding, scope, mandate and coverage. EIOPA therefore considered that IGSs should be regarded as a stand-alone topic which requires further assessment and may be addressed at a later stage.

35. It should be noted that the use of the terms "harmonisation" and "harmonised framework" does not prejudge the legal approach of any potential further work by the legislators in this field. In fact, the building blocks set out in this discussion paper could be considered individually,

[12] Please see Opinion on "Sound principles for Crisis Prevention, Management and Resolution preparedness of NCAs", 24 November 2014 (See link: https://eiopa.europa.eu/Publications/Opinions/EIOPA_Opinion_on_Sound_Principles_Crisis_Prevention_Management_and_Reso.pdf).

thereby allowing for a more targeted approach to harmonise national frameworks.

36. Furthermore, the term "insurers" is used throughout this discussion paper to refer to insurers, reinsurers and groups, unless stated otherwise.

1.4 Potential next steps

37. Following the consultation process, EIOPA will further develop its view on harmonising recovery and resolution frameworks for insurers and might decide to publish an Opinion addressed to the EU institutions on this topic.

38. Additionally, future work on potential harmonisation of IGSs might be considered by EIOPA as the existence and working of IGSs are highly connected to resolution tool kits. In the current work, IGSs are left out of scope as EIOPA followed a more pragmatic and gradual approach.

1.5 Structure of discussion paper

39. The structure of the discussion paper is in line with the approach followed by EIOPA. Chapter 2 provides an overview of the existing recovery and resolution frameworks for insurers based on the results of the survey. Chapter 3 assesses the need for harmonisation by focusing on the advantages and disadvantages of harmonisation. Finally, Chapter 4 presents EIOPA's preliminary views of what the main building blocks of a harmonised recovery and resolution framework for insurers could be. Throughout this chapter questions for stakeholders are included.

2. Overview of national recovery and resolution frameworks for insurers

2.1 Introduction

40. EIOPA conducted a survey on existing national recovery and resolution frameworks for insurers in the EU. The survey was launched in Q1 2016 and presents the situation in the Member States as of February 2016. In total, 30 NSAs responded to the survey.

41. It should be noted that most of the Member States do not have in place a formal recovery and resolution framework for insurers. In these cases, NSAs were asked to provide information about their current recovery and resolution practices taking into account all powers and tools available in their Member States.

42. The survey covered questions on (i) planning and preparation, (ii) early intervention and (iii) resolution, as well as on existing cross-border cooperation and coordination arrangements for crisis situations. Furthermore, NSAs were asked to report potential deficiencies that they have identified in their national frameworks and to provide information about their national IGS(s).

43. As is the case with other (qualitative) surveys, this exercise relies on the judgement of the respondents and the subsequent interpretation of the responses by EIOPA. Overall, the information provided was quite comprehensive and can be considered as a good representation of the situation in the Member States.

2.2 Preparation and planning

44. In this section, NSAs were asked whether insurers are required to prepare pre-emptive recovery plans (i.e. before the breach of the solvency capital requirement, SCR). Subsequently, NSAs were asked whether national authorities in charge of the resolution of insurers prepare resolution plans and assess the resolvability of insurers.

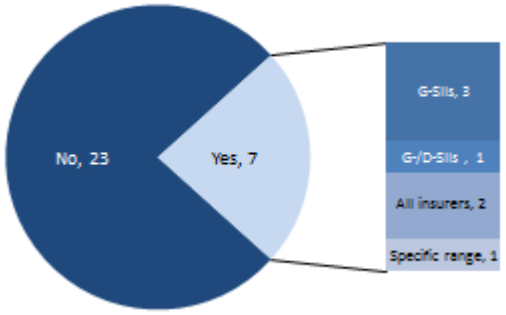
45. Pre-emptive recovery and resolution planning, including resolvability assessments, take place during normal times of business and help to enhance the awareness of and preparedness for stress or crisis situations.

2.2.1 Pre-emptive recovery plans

46. Chart 1 shows that a majority of the NSAs do not require the development of pre-emptive recovery plans by insurers, although three of them indicated that they can require insurers to prepare and submit a recovery or contingency plan before the breach of the SCR, when necessary.

47. Seven NSAs indicated that insurers are required to prepare pre-emptive recovery plans in their Member State. In three of these Member States the requirement is laid down in the law or regulations, whereas in the other four Member States the requirement is based on sound principles and/or international standards set for G-SIIs.

Chart 1: Is there a requirement to develop pre-emptive recovery plans?



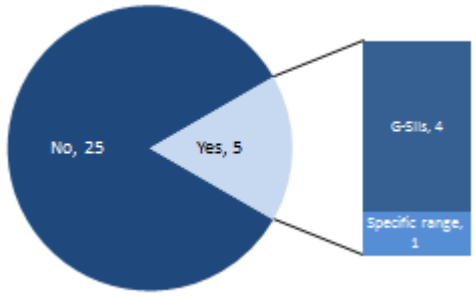
48. With respect to the scope of the requirement for pre-emptive recovery planning, three of these seven NSAs responded that the scope is limited to G-SIIs, while one NSA replied the scope includes insurers which are considered to be of systemic importance for both the global and domestic market. This NSA mentioned that the assessment of the domestic systemic importance is primarily based on the size of the insurer. Two other NSAs indicated that the scope captures all insurers and one NSA responded that the requirement applies to insurers with a significant share in the national insurance market, i.e. all insurers above a certain threshold measured in terms of the percentage of gross technical provisions or market share are included.

49. Finally, five of those seven NSAs mentioned that pre-emptive recovery plans are subject to a review by the NSA. There is, however, no requirement for pre-emptive recovery plans to be approved in any of those seven Member States, although three NSAs indicated that they can request insurers to make changes to the plan.

2.2.2 Pre-emptive resolution plans

50. As shown in chart 2, five NSAs reported that there is a requirement to develop pre-emptive resolution plans by authorities in charge of resolution of insurers in their Member State.

Chart 2: Is there a requirement to develop pre-emptive resolution plans?



51. In four Member States the scope includes G-SIIs only, although two NSAs indicated that there are plans to extent the scope of the requirement. One NSA mentioned that the scope covers insurers with a significant share in the national insurance market, i.e. all insurers above a certain threshold measured in terms of the percentage of gross technical provisions or market share are included.

52. Four other NSAs explained that pre-emptive resolution plans for insurers might be required in their Member State within three years from now or depending on the developments at the global and/or European level.

2.2.3 Resolvability assessments

53. The responses given by NSAs reveal that resolvability assessments are undertaken in those Member States where pre-emptive resolution plans are drafted. Therefore, the outcome is similar to the one above, i.e. five NSAs replied affirmatively to the question whether resolvability assessments are undertaken. The other NSAs replied that such a requirement is not available in their Member State.

54. Two NSAs provided additional information and indicated that they can require the insurer (and/or the group company) to take measures to remove impediments to its effective resolution. For instance, one of these two NSAs mentioned that the designated resolution authority is empowered to require the insurer to revise intragroup financing agreements or to limit or cease specific existing activities.

2.3 Early intervention

55. In this section of the survey, NSAs were asked to identify the powers they have at their disposal to intervene in a troubled insurer at an early stage, i.e. before the breach of the SCR.

56. In response to this question, some NSAs initially referred to Article 141 of the Solvency II Directive.[13] This article empowers NSAs to take all measures necessary to safeguard the interest of policyholders in case the solvency position of an insurer continues to deteriorate after it has breached the SCR. In a second stage, all NSAs were therefore asked to indicate whether the powers can be exercised before or only after the breach of the SCR.

57. Chart 3 shows the outcome for the powers aimed at restoring an insurer's capital adequacy. The chart shows that most of the powers are widely available across Member States, with the exception of the power to require the mandatory conversion of debt instruments. Reason for this might be that the issuance of debt instruments by insurers is not common in all Member States.

58. Despite the fact that most of the powers are widely available, a number of NSAs (see chart 3 for the exact number of NSAs for each of the powers) reported that their availability is subject to restrictions. One of the restrictions, which was often mentioned by NSAs, is the fact that the powers are not explicitly laid down in national regulation and, therefore, are only implicitly available, for instance, via general (direction-making) powers.[14]

59. The figures on the right-hand side of the chart illustrate the percentage of NSAs which have indicated that the powers can be exercised before the breach of the SCR. The results show that a majority of the NSAs can exercise the available powers before the breach of the SCR.

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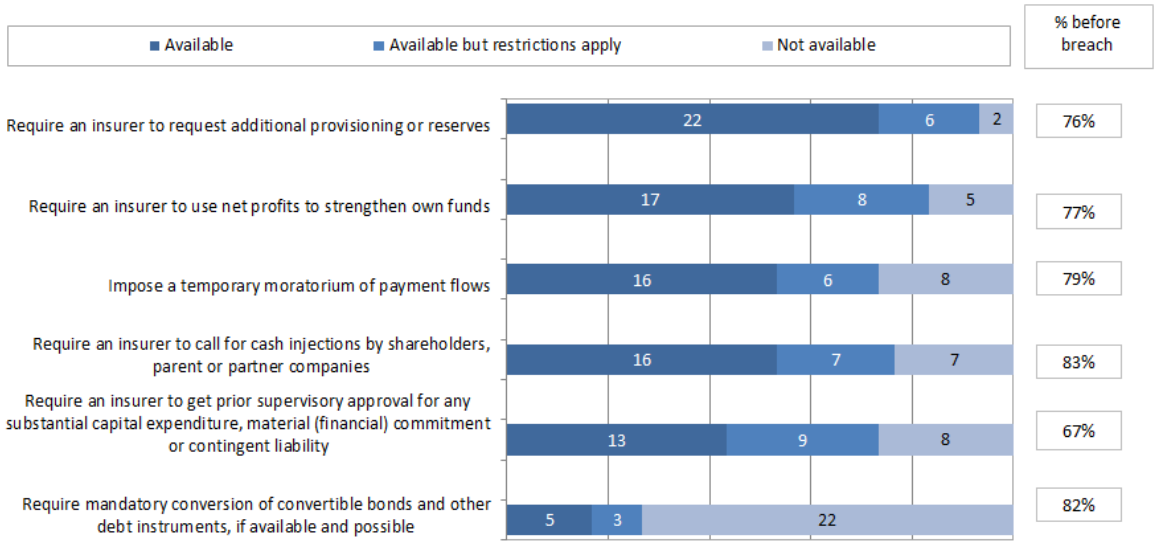
[13] Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), OJ L 335, 17.12.2009, p.1.

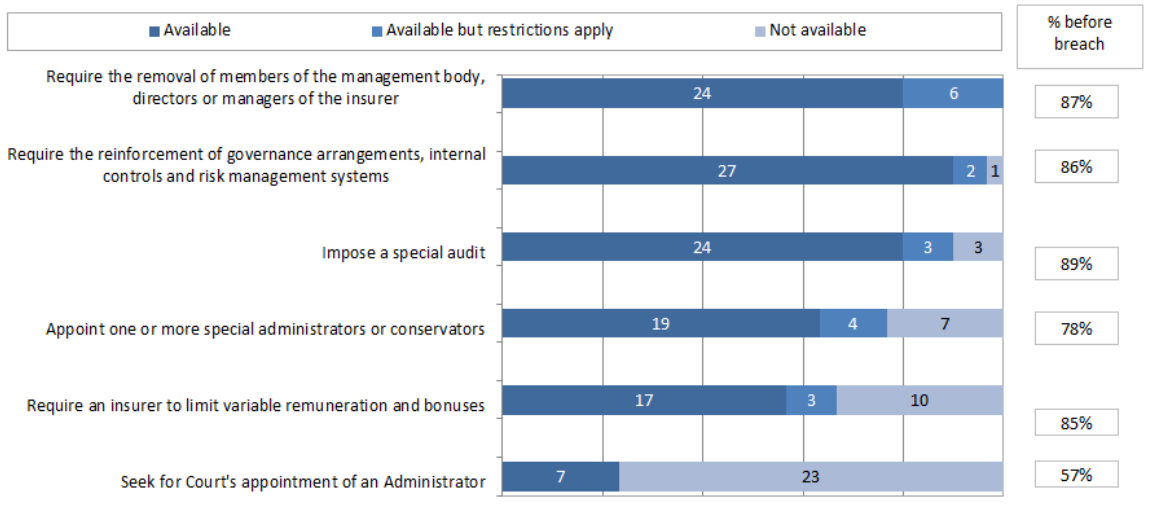
[14] Examples of other restrictions are: one NSA explained that the power to impose a temporary moratorium of payments only applies to certain types of payments. One NSA mentioned that insurers can only be required to use net profits to strengthen own funds in case of a loss exceeding a certain percentage of the insurer's own funds. Another NSA explained that most of the powers available could only be exercised once a "special control measure" has been adopted.

Chart 3: Powers aimed at restoring capital adequacy



60. Chart 4 shows the outcome for the powers affecting the management and governance of insurers. Overall, the chart shows that the powers are available to a majority of the NSAs, except for the power to seek for a court's appointment of an administrator. This might be explained by the fact that a large number of NSAs are themselves empowered to directly appoint an administrator. Only five NSAs replied that neither of the powers is available to them at an early stage. The chart also shows that on average more NSAs are able to use the powers affecting the management and governance of insurers before the breach of the SCR compared to the powers aimed at restoring capital adequacy (see chart 3 above).

Chart 4: Powers affecting management and governance

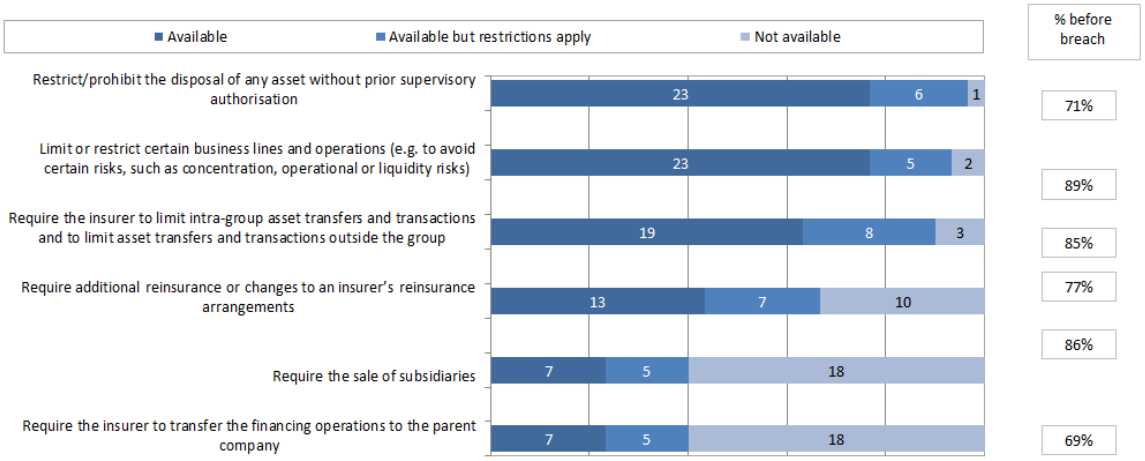


61. Chart 5 shows the outcome for the powers affecting the business and organisation of an insurer. As can be seen, a majority of the NSAs do not have the power to require the transfer of the financing operations to the

parent company, or to require the sale of subsidiaries; these powers might be regarded as rather intrusive measures to be taken at an early stage.

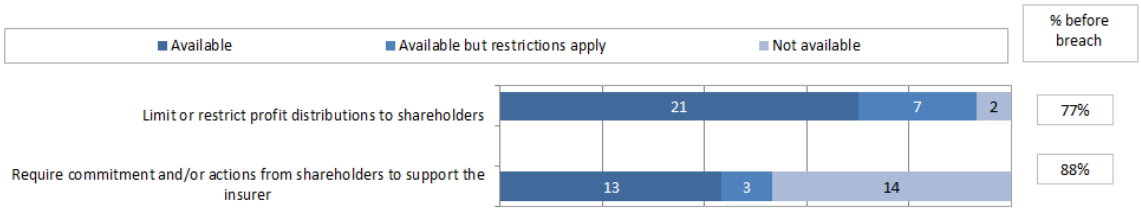
62. On the other hand, measures such as the power to require the insurer to limit intra-group transactions or to require a supervisory approval for the disposal of assets are available across Member States. Again, a diverse range of restrictions were reported by NSAs. For instance, it was reported that only temporary limitations or restrictions could be given.

Chart 5: Powers affecting the business and organisation



63. Chart 6 shows the outcome for the powers affecting the shareholders of an insurer. The chart shows that a majority of the NSAs can limit or restrict the payment of dividends to shareholders, even before the breach of the SCR. A smaller number of NSAs have the power to require shareholders to support an insurer in trouble, although the power is often not explicitly granted to NSAs. One NSA explained that it can summon and participate in shareholder meetings at any time and can propose measures to be approved in such meetings.

Chart 6: Powers affecting the shareholders



64. Finally, some additional early intervention powers not shown in the charts above were reported by a few NSAs, including the requirements:

- To make changes in an insurer's business strategy;
- To establish an obligation for the disclosure of specific data; and
- To prohibit or make subject to conditions the outsourcing of activities.

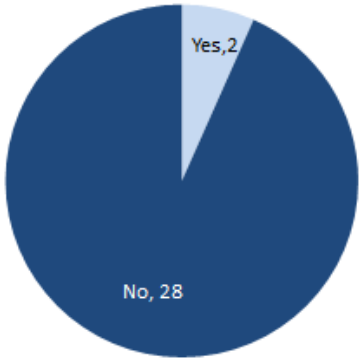
2.4 Resolution

65. This section covers the results of the questions on resolution. In accordance with the elements set out in the FSB Key Attributes, the survey included questions about the existence of a designated administrative resolution authority, the objectives of resolution, the conditions for entry into resolution, the resolution powers and safeguards.

2.4.1 Resolution authority

66. According to the FSB Key Attributes[15], each jurisdiction should have a designated administrative resolution authority, which should have statutory objectives, functions and operational independence. In the survey, NSAs were asked whether there is a designated administrative resolution authority for insurers in their Member States in accordance with the Key Attributes.

Chart 7: Is there a designated administrative resolution authority for insurers in your Member State?



67. The responses are shown in chart 7, which shows that most of the Member States do not have an officially designated administrative resolution authority equivalent to the description in the Key Attributes. Instead, usually the NSA and/or a relevant ministry, sometimes together with an administrator, handle the resolution of insurers.

68. Only 2 NSAs replied affirmatively to the question, whereas another NSA explained that there is a designated administrative resolution authority for insurers which are considered to be of systemic importance to the national market.

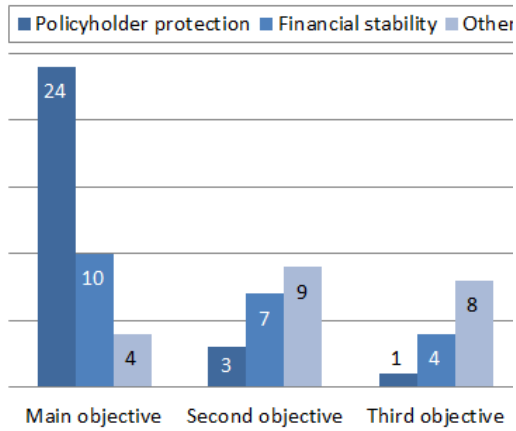
2.4.2 Objectives of resolution

69. The responses to the survey reveal differences in (i) the number of objectives pursued by national authorities in charge of resolution, (ii) the (existence of a) ranking of the objectives and (iii) the objectives. With respect to the number of objectives, the results show that authorities in charge of resolution pursue on average three objectives when resolving insurers, with a maximum of five in one Member State. However, most of the NSAs clarified that the objectives of resolution are not specified in the national framework. The responses are therefore often based on general resolution practices and general supervisory objectives. Chart 8 shows the outcome of the responses.

[15] Please see FSB Key Attributes 2.

70. It can be seen from the chart that there is usually a hierarchy in the objectives pursued by national authorities in charge of resolution. However, two NSAs mentioned that there is no hierarchy in the objectives and explained that the relevant objectives are ranked equally. The objectives are balanced as appropriate to the nature and circumstances of the resolution process in these Member States.

Chart 8: What are the resolution objectives in your Member State?



71. Furthermore, the chart shows that the protection of policyholders is the main objective in a majority of the Member States, followed by financial stability. This is in line with the objectives set out in Solvency II. Other primary objectives reported by NSAs include the protection of public funds, the continuity of functions whose disruption could harm the financial stability and/or real economy and the minimisation of value destruction.

72. The protection of public funds and the continuity of functions whose disruption could harm the financial stability and/or real economy were also often mentioned as secondary and tertiary objectives.

73. NSAs which indicated that several objectives are pursued were also asked to indicate whether they see any potential for conflict or tension between the selected objectives. Seven NSAs answered that there could be a conflict or tension between the protection of policyholders and the protection of public funds, or between policyholder protection and financial stability.

2.4.3 Conditions for entry into resolution

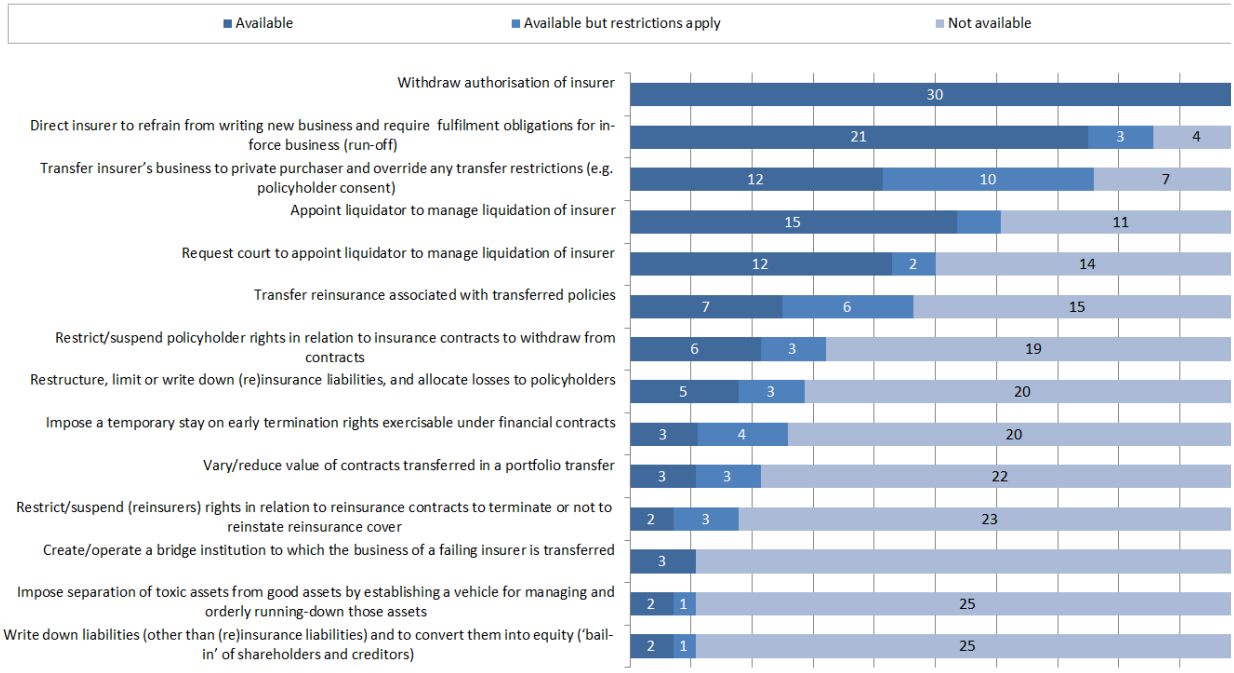
74. In order to find out when resolution processes are initiated in Member States, NSAs were asked what the conditions for entry into resolution are and whether these are different from the conditions for winding-up/liquidation. Winding-up/liquidation usually follows after the insolvency either on a balance sheet basis (the insurer's liabilities are greater than its assets) or cash-flow basis (the insurer is unable to pay its debts as they fall due).

75. The responses to the survey show that the national frameworks usually do not set out specific conditions for entry into resolution, other than the conditions for winding-up/liquidation and/or those related to the breach of Solvency II requirements. Nonetheless, some specific resolution conditions were mentioned, such as "the insurer is failing or likely to fail", "the insurer is likely to be no longer able to meet its obligations towards policyholders", and "a threatening development in an insurer's own funds, liabilities or solvency position has been detected". In addition, one NSA mentioned that resolution actions are subject to a public interest test, meaning resolution action is only taken if the national authority in charge of resolution is of the view that the objectives of resolution cannot be achieved to the same extent if the insurer was liquidated by means of regular insolvency proceedings.

2.4.4 Resolution powers

76. For an orderly resolution of insurers, it is essential that authorities in charge of resolution are granted with a broad set of resolution powers. Chart 9 shows the responses of the NSAs to the question whether the listed resolution powers are available in their Member State. The list of resolution powers was taken from the FSB Key Attributes.

Chart 9: Are these resolution powers available in your Member State?



77. It can be concluded that most of the resolution powers are not widely available in the EU. For instance, only a limited number of authorities in charge of resolution are able to impose a temporary stay on early termination rights in insurance or financial contracts. Similarly, the power to create and operate a bridge institution and the power to allocate losses to shareholders, creditors and policyholders are only available in a limited number of Member States.

78. On the other hand, the power to withdraw the authorisation of an insurer, the power to put an insurer into run-off and the power to transfer the portfolio of an insurer to a private purchaser is widely available. It should be noted that the power to withdraw the authorisation of an insurer is included in Solvency II.[16]

79. With respect to the power to transfer an insurance portfolio, twelve NSAs indicated that the national authority in charge of resolution has the power to transfer the portfolio and the power to override any transfer restrictions. Ten NSAs mentioned that the power is available but is subject to restrictions. For instance, in some Member States the approval of the court or a certain

[16] Please see Article 144 of the Solvency II Directive (2009/138/EC).

threshold of non-objections by policyholders is required before the portfolio can be transferred.

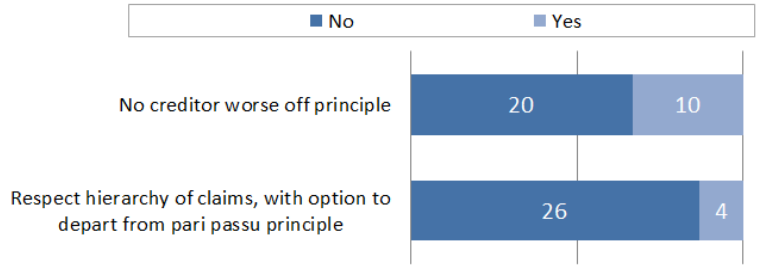
80. Furthermore, some NSAs clarified that the powers are only available in insolvency proceedings or after court approval in their Member State.

2.4.5 Safeguards

81. This section of the survey included questions on whether the exercise of resolution powers is subject to safeguards. NSAs were asked to specify whether the exercise of resolution powers is subject to the NCWO principle. The NCWO principle is a safeguard to ensure that creditors do not suffer a greater loss in resolution than they would have incurred in an insolvency procedure. In addition, NSAs were asked whether authorities in charge of resolution respect the hierarchy of claims while having the flexibility to depart from the general principle of equal (*pari passu*) treatment of creditors of the same class or policyholders of different types of policies (e.g. policyholders covered by an IGS versus those who are not covered) in order to maximise the value for all creditors, including policyholders, or to minimise the potential systemic impact of an insurer's failure.

82. The results are shown in chart 10. As can be seen, in one third of the Member States, the NSA reported that the exercise of resolution powers is subject to the NCWO principle. The chart also shows that the flexibility to depart from the *pari passu* principle is only available in four Member States.

Chart 10: Are these safeguards available in your Member State?



2.5 Cross-border cooperation and coordination

83. In the survey, NSAs were asked whether there are (formal) crisis management groups or equivalent arrangements in place between domestic and foreign authorities to deal with crisis situations of cross-border insurance groups.

84. The responses show that a formal crisis management group has been established or is being established for the G-SIIs headquartered in the EU. In addition, one NSA indicated that it has an equivalent arrangement for cross-border groups headquartered in its jurisdiction. However, the remainder of the NSAs replied that such cross-border cooperation and coordination arrangements do not exist for crisis situations.

85. Furthermore, a number of other NSAs highlighted the fact that they have signed the EIOPA coordination arrangements for the colleges of supervisors,

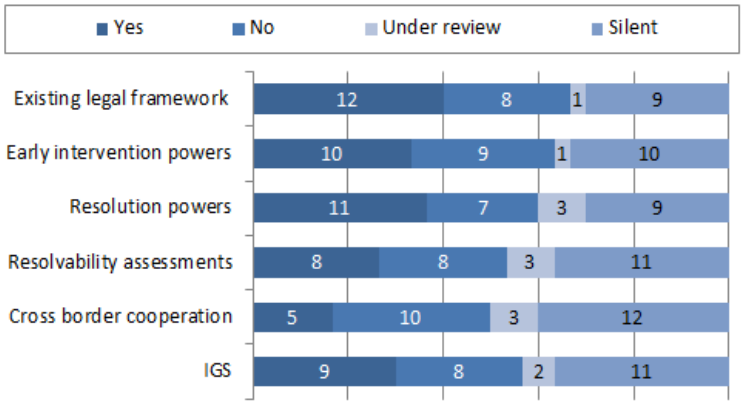
which include a section on coordination and cooperation in emergency situations.

2.6 Gaps and shortcomings

2.6.1 Gaps and shortcomings in existing frameworks

86. NSAs were also asked to report any gaps and shortcomings in their existing framework, focusing on the available powers and tools, cross-border arrangements and IGSs. Chart 11 shows the responses given by NSAs.

Chart 11: Are gaps and shortcomings identified?



87. As can be seen from the responses, a few NSAs explained that the topic is still under consideration; hence, no gaps or shortcomings had been identified so far.

88. With respect to overall deficiencies identified by NSAs in their existing framework, some general comments were made. For instance, several NSAs mentioned that there is no formal administrative resolution framework for insurers with a designated administrative resolution authority, resolution objectives, resolution conditions, resolution powers and safeguards, as set out in the FSB Key Attributes.

89. Looking at responses of the early intervention powers, two NSAs reported that some of the powers are not explicitly provided for in the regulation. Another NSA mentioned that the conditions for exercising the powers could be widened.

90. With respect to the resolution powers, much more gaps and shortcomings were reported. Eleven NSAs indicated that they have identified some deficiencies. For instance, a limited range of available resolution powers was mentioned.

91. Furthermore, the lack of recovery and resolution planning requirements, including resolvability assessments, were reported as shortcomings. Five NSAs also reported shortcoming in the cross-border cooperation with foreign authorities.

92. Finally, nine NSAs reported gaps and shortcomings with respect to the IGSs. In most cases, these relate to the limited scope of the IGSs or the way the IGSs operate and compensate.

2.6.2 Plans to reinforce existing frameworks

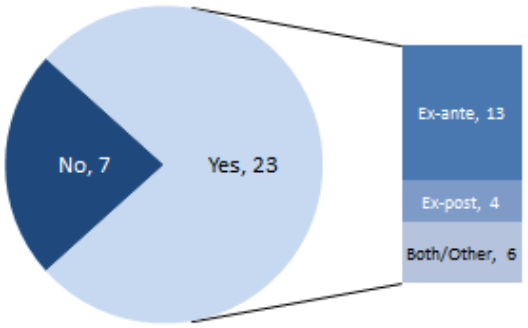
93. Seven NSAs indicated that there are initiatives to reinforce the national framework, although in most cases no concrete plans have been published or issued yet. Nonetheless, one NSA mentioned that the reinforcements are expected to be in-force in 2018, and in another Member State the proposal for a resolution regime for insurers is planned to be adopted in mid-2017.

94. One NSA explained that a comprehensive recovery and resolution framework for insurers had actually already been adopted in response to the identified gaps and shortcomings.

2.7 Insurance guarantee schemes

95. In the final section of the survey, NSAs were asked some questions about their national IGS(s). The results reveal that there are substantial differences between the IGSs in terms of their funding, mandate and coverage.

Chart 12: Is there an IGS in your Member State? If so, how is it funded?

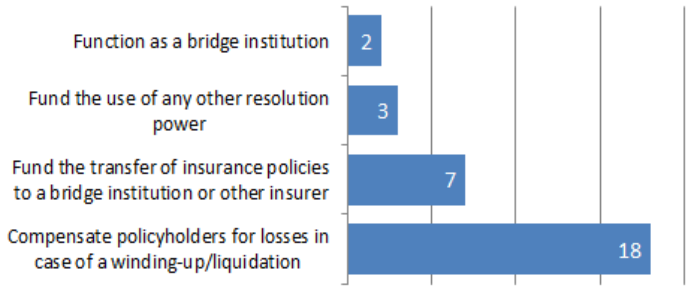


96. Chart 12 shows that twenty-three Member States have in place one or more IGSs. In five Member States the IGS covers only motor liability insurance obligations.

97. More than half of the IGSs are funded on an ex-ante basis and mainly by contributions from insurers determined by the total premiums of insurers.

98. Furthermore, the responses show that the primary function of the IGSs is to compensate policyholders for losses in the event of a winding-up/ liquidation, followed by the function to fund the transfer of an insurer's portfolio to a bridge institution or other insurer (see chart 13). Other functions of IGSs include the (non-mandatory) power to take necessary measures for the purposes of safeguarding the rights of eligible claimants when an insurer is in financial difficulties but before a default is declared, and the mandatory power to make arrangements to secure the continuity of long-term insurance contracts in case of a default.

Chart 13: For what purpose can the IGS be used?

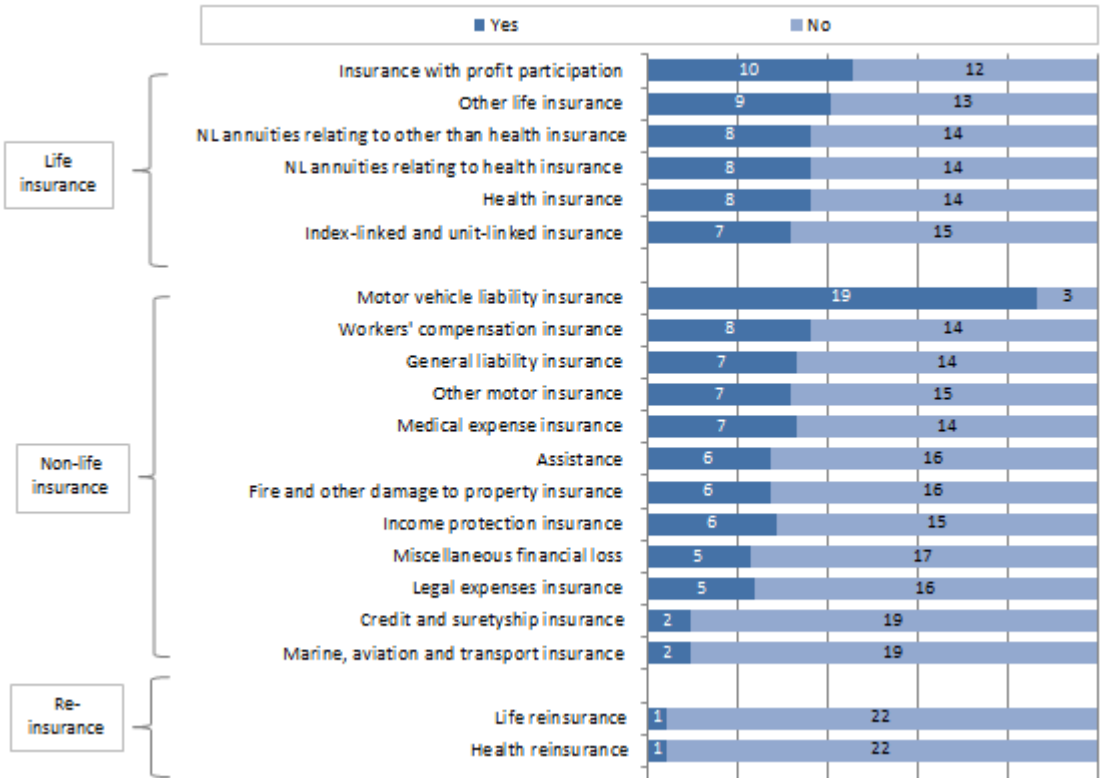


99. With respect to the coverage of the IGSs, the responses reveal that in eighteen Member States the coverage is not limited to policies contracted with insurers whose head office is located in the domestic jurisdiction. This

means that the IGSs provide coverage to branches of insurers whose head office is situated in other Member States. One NSA clarified, however, that this does not apply to motor liability insurance obligations, while another NSA clarified that only branches of non-EEA jurisdictions are covered.[17]

100. Finally, chart 14 provides an overview of the products which are covered by the IGSs across Member States. Obligations from motor vehicle liability insurance products are covered in most of the IGSs, whereas just one IGS covers reinsurance obligations.

Chart 14: Which products are covered by the IGS(s) in your Member State?



[17] In this last case, the NSA explained that the system also covers all insurance contracts issued by the insurer whose head office is located in the jurisdiction, regardless of whether these contracts are sold through a foreign branch or under free provision of services.

3. Rationale for harmonisation

3.1 Introduction

101. One of the lessons learned from the past financial crisis is the need to have adequate recovery and resolution powers and tools in order to be able to handle failing institutions in an effective and orderly manner. In the banking sector, the financial crisis revealed that the existing frameworks were unsuitable to deal with banks in crisis. In response to the banking failures and unprecedented level of public intervention, the European Commission adopted the BRRD, a harmonised recovery and resolution framework for banks and large investment firms, in 2014.[18]

102. Overall, the insurance sector has witnessed fewer failures than the banking sector. Although the introduction of Solvency II, and in particular, the adoption of risk-based capital requirements and forward-looking supervision, should reduce the likelihood of insurance failures in the future, it cannot be prevented that insurers might get into financial difficulties or even fail.[19] It is, therefore, essential that Member States have in place effective frameworks to deal with crisis situations in the insurance sector. The results of EIOPA's survey on existing recovery and resolution frameworks show that there is currently no harmonised recovery and resolution approach for insurers in the EU. Member States have their own national frameworks, which in some cases are limited to normal insolvency procedures.

103. In this chapter, EIOPA analyses whether there is a need for harmonising the elements of recovery and resolution for insurers in the interest of policyholders, financial stability and other resolution objectives. While the insurance sector has its own specific features, it is worthwhile to try to learn from the banking experience, including the experience with the application of the BRRD in Member States, and examine whether harmonisation in the field of recovery and resolution would be needed for insurers.

104. The analysis of EIOPA focuses on the potential advantages and disadvantages of harmonising recovery and resolution practices in the EU. Where available, the analysis is supported with empirical data, case studies and the findings from EIOPA's survey. However, the analysis generally remains at the conceptual level as the insurance sector experienced fewer failures of high profile national or cross-border insurance groups than the banking sector. Table 2 includes a summary of the arguments in favour of and against harmonisation, which are discussed in further detail in this chapter.

105. Before starting the analysis, two preliminary remarks should be made. Firstly, as explained in Chapter 1 "Introduction", EIOPA has followed a gradual approach whereby the potential need for harmonisation of IGSs is

[18] European Commission, EU Bank Recovery and Resolution Directive (BRRD): Frequently Asked Questions, 15 April 2014. (See link: http://europa.eu/rapid/press-release_MEMO-14-297_en.htm?locale=en).

[19] White Paper of the European Commission on Insurance Guarantee Schemes (COM (2010) 370): *Solvency II will not create a zero-failure environment. Neither the current (Solvency I) nor the future (Solvency II) EU solvency regimes create, or can create, a zero-failure environment for insurance companies. (See link: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010DC0370&from=EN)*

not captured in its current work. The issue of IGSs was considered to be a stand-alone topic with broader implications and, hence, needs further assessment.[20] Secondly, any harmonisation in the field of recovery and resolution should be compatible with and take account of other initiatives which are currently ongoing, such as IAIS works on potential HLA requirements for G-SIIs and the European Commission legislative initiative on insolvency proceedings in the EU.

Table 2: Overview of arguments

	Arguments
In favour of harmonisation	(A) Avoidance of fragmentation in the EU
	(B) Enhancement of cross-border cooperation and coordination
	(C) Consistency in reinforcing national frameworks
	(D) Fragile market environment and systemic risk
	(E) Further enhancement of the single market
Against harmonisation	(A) Normal insolvency procedures might be suitable
	(B) No strong evidence for existing powers being ineffective in all Member States
	(C) National frameworks reflect national specificities in a better way
	(D) Administrative burdens and costs for insurers and national authorities

Box 1: The concepts of "recovery" and "resolution"

The concepts of "recovery" and "resolution" are in the recent years often used in crisis management. Although conceptually recovery and resolution refer to different stages of a crisis management process, both terms are associated to insurers experiencing a significant deterioration in their financial situation and should be seen as part of a continuum of supervisory activities. In practice, however, it is difficult to draw a clear line between recovery and resolution, which relate to a situation of, respectively, "going concern" and "gone concern".*

The concept of "non-viability" is useful to shed some light on the transition from recovery to resolution. The FSB Key Attributes state that resolution should be initiated when an insurer is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so (FSB Key Attributes 3.1). It could, therefore, be considered that an insurer experiencing financial problems is in recovery if it is still viable. The FSB Key Attributes also specify that the resolution regime should provide for timely and early entry into resolution before a firm is balance-sheet insolvent and before all equity has been fully wiped out. Furthermore, several examples are provided to determine the non-viability, such as a breach in the minimum capital without reasonable prospects of restoring compliance, a strong likelihood that policyholders or creditors will not receive payments as they fall due or when the recovery measures have failed, or there is a strong likelihood that they will not be sufficient to return the insurer to viability.

[20] The survey conducted by EIOPA revealed that there are also substantial differences in insurance guarantee schemes in the EU, which could lead to a difference in policyholder treatment.

Recovery and resolution, which have become part of the jargon in crisis management together with others such as "early intervention measures", are also difficult to link unequivocally to some of the concepts used in Solvency II such as "reorganisation measures" or "winding-up" (defined in Article 268 of the Solvency II Directive):

- "Reorganisation measures" involve any intervention by the competent authorities which are intended to preserve or restore the financial situation of an insurance undertaking (e.g. suspension of payments or reduction of claims). Although to some extent these could be seen as early intervention measures, reorganisation measures are also linked to some of the elements of resolution as set out in the Key Attributes.
- The term "winding-up" involves the realisation of the assets of an insurer and the distribution of the proceedings among the policyholders, creditors, shareholders or members as appropriate. This term is usually used as synonym for liquidation, and liquidation is acknowledged to be one of the possible outcomes of the resolution process.

In summary, although the concepts of Solvency II and the FSB Key Attributes are somehow interlinked, a mapping exercise to assess similarities and differences has not yet been carried out.

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** It is difficult to find specific definitions of both concepts. As an example, the BRRD indirectly defines "recovery" as the situation when institutions are required to draw up and maintain plans to provide "for measures to be taken by the institution to restore its financial position following a significant deterioration to its financial situation" (Article 5 of the BRRD). The term "resolution" is formally defined in Article 2 of the BRRD as the application of a resolution tool or a tool that the BRRD itself defines in order to achieve one or more of the resolution objectives.*

3.2 Analysis

106. Prior to starting the analysis, it is useful to have a general view on the resolution objectives for insurers, which can be used to assess to what extent a harmonised framework could contribute to better achieving these objectives.

107. For this purpose, the results of EIOPA's survey on existing recovery and resolution frameworks are used. The results revealed four main objectives: (i) adequate protection of policyholders, (ii) maintaining financial stability, (iii) protection of public funds and (iv) continuity of functions whose disruption could harm the financial stability and/or real economy. In addition, according to Solvency II, the main objective for supervision is the protection of policyholders, whereby financial stability should be pursued without undermining policyholder protection.[21]

[21] Please see Recital 16, *"The main objective of insurance and reinsurance regulation and supervision is the adequate protection of policyholders and beneficiaries. Financial stability and fair and stable markets are other objectives of insurance and reinsurance regulation and supervision which should also be taken into account but should not undermine the main objective"*, and Article 27 and Article 28 of the Solvency II Directive (2009/138/EC).

3.2.1 Arguments in favour of harmonisation

(A) Avoidance of fragmentation in the EU

108. The lack of EU legislation governing the process of insurance resolution has resulted in a fragmented landscape of national recovery and resolution frameworks. EIOPA's survey on existing recovery and resolution frameworks revealed that there are substantial differences between national frameworks. Additionally, the survey showed that most of the Member States have not yet implemented the FSB Key Attributes which set out the core elements considered to be necessary for an effective resolution regime by the FSB.[22]

109. Prior to the introduction of the BRRD, the landscape of national recovery and resolution frameworks for banks was likewise fragmented which was seen as a significant impediment to the management of the past financial crisis. The financial crisis "highlighted the lack of arrangements to deal effectively with failing banks that operated in more than one Member State", according to the European Commission.[23] Additionally, the crisis revealed "serious shortcomings in the existing tools available to authorities for preventing or tackling failures of systemic banks".

110. It seems likely that the absence of an effective harmonised recovery and resolution framework would similarly lead to impediments and inefficiency in the resolution process of particularly cross-border insurance groups. Box 2 shows a hypothetical case study of the potential impediments in the resolution process of an insurance group with operations in more than one Member State.

Box 2: Hypothetical case of a cross-border insurance group failure in a fragmented landscape

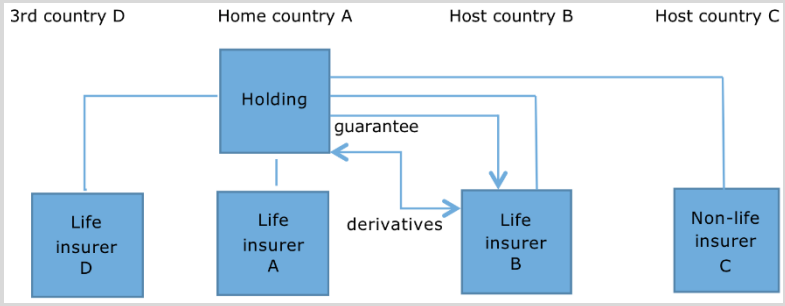
The case study is based on a hypothetical situation where a real-life cross-border insurance group in one of the Member States would fail.

I. Background

Life insurer D outside the EU suffers severe losses. This induces the Holding company headquartered in the EU to move excess capital from EU insurers to life insurer D. A sharp fall in asset prices and a simultaneous decrease in interest rates push the solvency ratios of life insurers A and B below the minimum capital requirement. As a result, the group own funds fall below the required minimum level. Non-life insurer C is in good financial shape; its excess capital is therefore transferred to the Holding company.

[22] Please see FSB "Key Attributes of Effective Resolution Regimes for Financial Institutions", 15 October 2015.

[23] European Commission, EU Bank Recovery and Resolution Directive (BRRD): Frequently Asked Questions, April 2014: "*The crisis also highlighted the lack of arrangements to deal effectively with failing banks that operated in more than one Member State. It was thus agreed that greater EU financial integration and interconnections between institutions needed to be matched by a common framework of intervention powers and rules. The alternative would be fragmentation and inefficiency in EU banking and financial services, something which would harm the single market and would impair its advantages for consumers, investors and businesses*." (See link: http://europa.eu/rapid/press-release_MEMO-14-297_en.htm?locale=en)



The authorities in country A would like to put life insurer A into resolution. In country B, there is no resolution regime in place, other than a regular court-led bankruptcy procedure. There is however an IGS in place, which does not exist in country A.

The group is organised centrally such that human resources and administration issues are centralised at the group level with service agreements between the Holding company and the subsidiaries. Additionally, there are numerous intragroup transactions between both the Holding company and the subsidiaries and between the subsidiaries themselves, such as derivatives positions and a guarantee from the Holding company to life insurer B.

II. Potential problems in a fragmented landscape

a. Authorities in charge of resolution and administrators focus solely on the interests of creditors and policyholders in their own jurisdiction. This may lead to suboptimal outcomes. For instance, the authority in charge of resolution in country A has an incentive to keep the group capital in country A instead of using it to cover capital shortages in other countries.

b. Creditors of life insurer B cannot be bailed-in, unless life insurer B is liquidated. In case liquidation of insurer B is postponed, the potential losses of policyholders of life insurer A might increase.

c. Life insurer B calls in the guarantee issued by the Holding company. This guarantee has to be paid in the end by the creditors of insurers D, A and C, in case the authority in country A cannot impose a moratorium on contractual payments.

d. Resolution of the Holding company stops the service provision of the Holding company to insurers B and C. This results in a halt of the sale of new insurance contracts and pay-outs in countries B and C, which destroys the value of the subsidiaries in these countries.

e. Authority in country A imposes a moratorium on payments following the derivative positions and calls in the termination clause given the failure of life insurer B. This limits the possibility to transfer the portfolio of insurer B.

III. Potential benefits of harmonisation

A harmonised recovery and resolution framework would:

a. Force authorities in charge of resolution to cooperate and coordinate in order to find the optimal resolution strategy for the group as a whole and thereby achieve the optimal solution for all stakeholders.

b. Ensure that a minimum set of resolution powers are available in all Member States in which the insurance group has operations. In that case, groups would have fewer incentives to structure themselves or move capital in order to avoid the use of specific resolution powers (i.e. avoidance of regulatory arbitrage).

c. Make ex-ante visible any intragroup positions and intragroup service contracts which may impede the effective resolution of insurers.

(B) Enhancement of cross-border cooperation and coordination

111. The financial crisis has also highlighted the importance of cross-border cooperation and coordination in times of crisis. Cross-border cooperation and coordination is necessary in order to avoid impediments to the resolution of cross-border insurance groups.[24]

112. Solvency II requires NSAs to cooperate and coordinate with foreign NSAs during normal times of business, which is usually arranged through the establishment of supervisory colleges. These colleges are a platform for cooperation and coordination, including information sharing, between NSAs from all Member States in which entities of an insurance group are located. The aim of these supervisory colleges is to foster a common understanding of the risk profile of the group (entities) and to achieve a more efficient and effective supervision.[25]

113. However, Solvency II does not contain requirements for cooperation and coordination between national authorities during times of crisis. As a result, most of the Member States do not have in place cooperation and coordination arrangement for crisis situations.[26] Only five Member States have currently established a crisis management group or equivalent arrangements to deal with crises of G-SIIs or cross-border groups headquartered in their jurisdiction. A harmonised framework requiring the establishment of cross-border cooperation and coordination arrangements could therefore avoid any future impediments to the resolution of cross-border groups.

114. The importance of cross-border cooperation and coordination in the insurance sector is emphasised by the findings of a recent study on cross-border activity in the insurance sector in the EU (see chart 15 on next page).[27] The results of the study show that the degree of cross-border activity in the insurance sector is relatively higher than in the banking sector. In the insurance sector, 29 percent of the business is written by subsidiaries or branches controlled by foreign entities located in the EU (measured as gross written premiums), whereas in the banking sector this is only 17 percent (measured as the amount of foreign lending).

115. Furthermore, the split between activities coming from subsidiaries and branches in the insurance sector reveals that subsidiaries are the main channel for cross-border activity; on average, about 25 percent of the cross-border activity comes from subsidiaries and only 5 percent from branches. Given that subsidiaries are separate legal entities operating in foreign jurisdictions which are not under the direct supervision of the group supervisor, cross-border cooperation and coordination is even more important in order to ensure an effective and orderly resolution process when required. This is particularly important because the stability of other

[24] Please see European Commission, EU Bank Recovery and Resolution Directive (BRRD): Frequently Asked Questions, April 2014. (See link: http://europa.eu/rapid/press-release_MEMO-14-297_en.htm?locale=en).

[25] Please see Recital 139 Solvency II of the Solvency II Delegated Regulation ((EU) 2015/35).

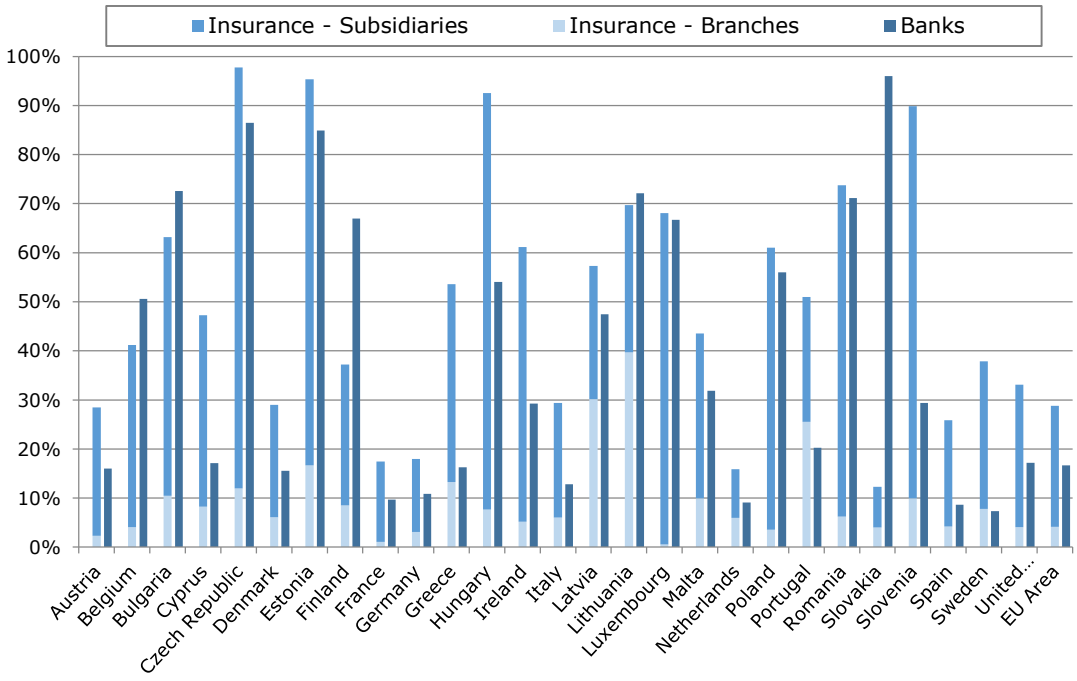
[26] Please see section 2.5 "Cross-border cooperation and coordination".

[27] Dirk Schoenmaker and Jan Sass, "Cross-border Insurance in Europe", November 2014. (See link: https://eiopa.europa.eu/Publications/Speeches%20and%20presentations/DSF%20Policy%20Paper%20No%2045%20Cross-border%20Insurance%20in%20Europe.pdf).

group entities or the group as a whole might be affected by the failure of the parent company or one or more subsidiaries.

116. Even where cross-border activity comes from branches, cooperation and coordination between foreign national authorities is crucial. In its (internal) analysis on the implications of branching-out in the EU, EIOPA concluded that cooperation and coordination, including the exchange of information, between home and host countries are essential elements to reduce the potential negative implications of branches on financial stability and the real economy.

Chart 15: Degree of cross-border activity in insurance and banking in the EU



Data source: *Schoenmaker and Sass (study 2014, data from 2012).*

Notes:

- *Cross-border activity in the insurance sector is as measured as the percentage of gross written premiums written by subsidiaries and branches controlled by foreign enterprises located in the EU. For the banking sector, cross-border activity is measured as the total amount of foreign lending (assets) as percentage of total lending (assets). The chart illustrates the cross-border activity in the EU coming from other EU countries only. Cross-border activity coming from non-EU countries has been removed from the chart.*
- *The Slovenian Insurance Supervision Agency (AZN) reported that the data used for Slovenia is incorrect or inaccurate.*

117. Therefore, it can be concluded that measures to enhance the cross-border cooperation and coordination in the insurance sector are essential to ensure the orderly resolution of cross-border insurance groups. A fragmented landscape which does not provide for a common set of recovery and resolution powers and tools, as well as objectives and conditions for entry into resolution could impede the management of crises and might result in situations where national authorities concentrate on operations in their own jurisdictions. This could lead to inefficient and competing resolution approaches, affecting the functioning of the single market in the EU, and eventually lead to suboptimal results for all affected stakeholders.

118. A common set of resolution powers with consistent design, implementation and enforcement features would facilitate mutual alignment and recognition of resolution actions between foreign national authorities. Harmonisation would therefore contribute to achieving the resolution objectives mentioned by NSAs in EIOPA's survey on existing recovery and resolution frameworks, such as policyholder protection and financial stability.

(C) Consistency in reinforcing national frameworks

119. As stated in the FSB Key Attributes, an effective framework is essential for an effective and orderly resolution of failing institutions. EIOPA's survey on existing recovery and resolution frameworks revealed that most of the national recovery and resolution frameworks do not contain the core elements prescribed in the Key Attributes. Some of the NSAs (twelve in total) also reported to have identified some gaps and shortcomings in their national framework. One of these NSAs provided a real-life case study which illustrates the impediments it faced in the process of managing a failing national insurance group (see Box 3).

Box 3: Anonymised case study of an insurance group in financial distress

This box presents a real life case study of an insurance group in a Member State which faced some serious financial difficulties. Various recovery and resolution scenarios were investigated by both the insurance group and the NSA. Eventually, a solution was found and the insurance group was saved, policyholders were protected and financial stability was maintained. Nevertheless, this case provides an example of the potential impediments to an orderly resolution in the absence of an effective resolution framework.

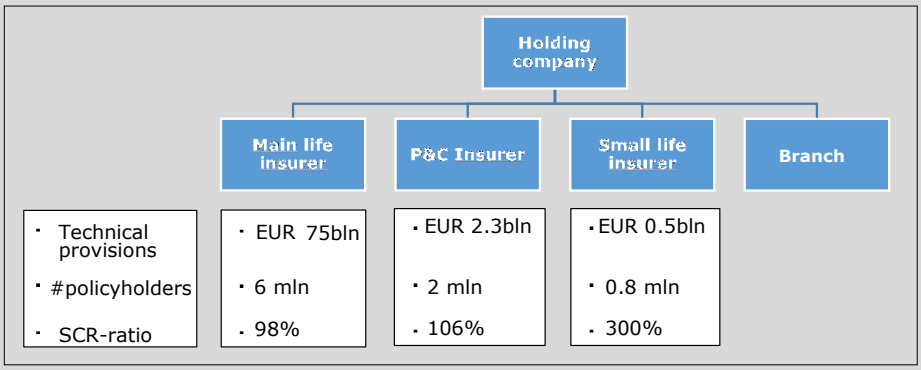
The case study is based on confidential information provided by the NSA. For confidentiality reasons, the figures shown in the text have been slightly adjusted.

I. Background

Figure 1 shows the stylised organisational chart and some basic facts of the insurance group which faced solvency problems. The main cause for the problems was the challenging market conditions; the combination of low interest rates, declining sales in the life insurance market and high competition and low margins in the non-life market put pressure on the business model and solvency position of the insurance group.

In order to restore its solvency position, the insurance group tried to raise capital in the financial markets but was unable to do so. Other options to raise additional capital were investigated, including the option to put the entire insurance group for sale. The number of interested buyers was however limited and a successful outcome of the sale process was highly uncertain. Against this background, the NSA, together with the insurance company, had to prepare for alternative resolution scenarios. The shared opinion was that the scenario of a viable stand-alone going concern was not possible.

Figure 1: Insurance group



II. Impediments to orderly recovery and resolution

When developing alternative resolution strategies, the NSA encountered a number of impediments to the orderly resolution of the insurance group. These impediments include:

- *Defining the conditions for entry into resolution*

The existing framework did not set out clear conditions for resolution. The NSA had to decide when to intervene and what kind of intervention was warranted, as the insurance group was in compliance with the in-force Solvency I-requirements. The minimum capital requirement (MCR) ratio was also far above the threshold of 100%.

- *Cliff-effect between going and gone concern valuation*

There was a discrepancy in the valuation of the insurer's assets and liabilities moving from a going concern to a gone concern assumption. This was caused – among others – by the use of different (market) parameters for the valuation of insurance liabilities and a change in the degree of recognition of deferred tax assets. The cliff-effect further complicated a portfolio transfer to an external party.

- *Lack of transferability of insurance portfolios*

Detailed analysis of the life insurance portfolio showed that more than half of the policies were not transferable or only after adjusting the characteristics of the products (see figure 2). In addition, analysis showed that transferability of the IT systems used to service the products was also problematic and would take several months.

Figure 2: Degree of transferability - life portfolio

High	- Individual life: o Term life products o Traditional life products - Group life: o Unit-linked (Defined Contribution) contracts
Medium	- Individual life: o (Deferred) annuities with high guarantees (economically not profitable) - Group life: o Traditional Defined Benefit contracts with profit sharing
Low	- Group life: o Separate accounts for which other regulatory framework is applicable o Traditional Defined Benefit contracts with certain options and guarantees - Individual life: o Certain unit-linked products

- *Intra group interconnectedness and interdependencies*

Analyses by the insurance group revealed that the entities within the group were highly interconnected and interdependent. For instance, the holding company was responsible for the IT, financial and regulatory reporting, legal, tax, treasury and human resources of the subsidiaries and, hence, crucial for the operational continuity of the subsidiaries in the short-term. In addition, the analysis revealed that a bankruptcy of the holding company might have been triggered if the life insurer was put into run-off.

- *Early termination rights in financial and reinsurance contracts*

The early termination rights in financial derivatives contracts and reinsurance contracts were another impediment to the orderly resolution of the group, as many derivatives and reinsurance contracts contain early termination options which may be triggered when an insurer goes into run-off or when it gets downgraded by the rating agencies.

III. Missing powers and tools

During this process, the NSA identified some gaps and shortcomings in the national framework. The NSA considered that the following powers and tools would have helped to ensure the orderly resolution of the insurance group.

- *Require recovery and resolution planning in a pre-emptive manner*

In this case, recovery and resolution planning was only done after the insurance group came into financial difficulties. Preparing for a potential crisis in a pre-emptive manner would have helped to reveal and remove potential impediments at an early stage.

- *Create possibility to intervene at level of ultimate holding company*

The existing framework in the Member State did not allow the NSA to intervene at the level of the holding company, which complicated the resolution process.

- *Introduce the power to bail-in creditors, shareholders and policyholders*

The resolution planning process revealed that many portfolios would not have been transferable without amending the terms and conditions of the insurance contracts. The power to bail-in policyholders, creditors or shareholders might therefore be necessary. The same applies to the power to put an insurer into run-off.

120. As a result of the inadequacy of existing frameworks, Member States are initiating plans to reinforce national recovery and resolution frameworks.[28] Box 4 shows examples of national initiatives which are aimed to bring national frameworks more in line with the core elements set out in the FSB Key Attributes.

121. The emergence of national initiatives poses a risk that the differences between Member States will increase even further, resulting in a higher degree of fragmentation in the EU. This might have further implications for the effective resolution of a cross-border insurance group. Initiatives to reinforce existing frameworks at the EU level would avoid this fragmentation.

122. An initiative at the EU level would also ensure a consistent implementation of the Key Attributes, which was endorsement by the G20 leaders in 2011[29], and hence strengthen the single market in the EU. Following the

[28] Seven NSAs responded to EIOPA's survey that there are plans to reinforce national recovery and resolution frameworks (please also see section 2.6.2 "Plans to reinforce existing frameworks").

[29] The FSB Key Attributes were endorsed by the G20 leaders at the Cannes Summit in November 2011.

endorsement, Member States are expected to implement the FSB Key Attributes in their national frameworks. Some NSAs explicitly mentioned in EIOPA's survey that actions at the EU level would be welcomed and facilitate this process, particularly, because the implementation of some of the elements included in the FSB Key Attributes might require changes in the EU legislation (e.g. the power to bail-in creditors might only be possible after changing the provisions about shareholder rights under EU company law directives[30]).

Box 4: Examples of national initiatives to reinforce existing recovery and resolution frameworks for insurers

	France	**The Netherlands**	**Romania**
Action	- On 30 March 2016, the Ministry of Finance presented a draft law introducing a recovery & resolution regime for insurers. - When adopted (expected mid-2017), the regime will include: recovery and resolution planning for insurers whose balance sheet size is above a certain threshold; resolvability assessment; and resolution powers, in particular the power to transfer insurance portfolios and to create a bridge institution. The NSA will also have the power to write down life insurance liabilities prior to a portfolio transfer, if needed to facilitate the transfer.	- In the process of adopting reinforcements to the existing framework in accordance with the FSB Key Attributes. - A public consultation of the draft law on recovery and resolution for insurers was launched on 13 July 2016. - Regime includes powers to bail-in shareholders, creditors and policyholders.	- Adopted a recovery and resolution framework for insurers in accordance with the principles set out in the Key Attributes. - The framework includes recovery and resolution planning, early intervention and resolution. - Also, the insurance guarantee fund was changed to enable it to finance resolution actions.
Reason for action	- To introduce a resolution regime in France, more efficient than the current regime (which does not go far beyond (judicial) winding-up). - To foster a dynamic at EU level. - To comply with	- During the financial crisis, some domestic insurers had to be bailed-out. - Aim is to clarify resolution objectives and resolve problems identified in the current system (i.e. recoverability options	- Primarily a response to adverse developments in the Romanian insurance market in 2014. - Aim was to enhance consumer protection, strengthen market conduct and address further adverse

[30] These refer to Directive 2004/25/EC, Directive 2005/56/EC, Directive 2007/36/EC and Directive 2012/30/EU.

	international standards, in particular with the commitment of the G20 to adopt a resolution regime for all financial institutions that could be systemically significant if they fail. However, this was only a trigger to take action, as the intended scope goes beyond insurers which are or could be systemic at the point of failure.	for insurers turned out to be limited and available resolution tools were not sufficient in some cases). - To introduce some missing resolution powers (e.g. the power to bail-in shareholders, creditors and policyholders).	evolutions.
Scope	- All insurers (and insurance groups). - Proportionality applied.	- All insurers (and insurance groups). - Proportionality applied.	- Recovery planning applies to all insurers. - Resolution planning applies to insurers above a certain threshold. - Proportionality applied.
Source: Information is gathered from the respective NSAs.			

(D) Fragile market environment and systemic risk

123. The importance of having in place an effective recovery and resolution framework is notably high in a fragile market environment, like the current environment with prolonged low interest rates combined with a risk of a sharp reversal in asset prices (so-called "double hit scenario"). A double hit scenario is a real risk for insurers and could lead to failures of predominantly life insurers. For instance, the results of the EIOPA stress test conducted in 2014 showed that 44% of European insurers would not meet their capital requirements under the prescribed double hit scenario.[31]

124. The ESRB considers the common vulnerability to such a double hit scenario as one of the main sources of systemic risk that may come from the insurance sector.[32] In this regard, the ESRB is of the view that *"an insurance recovery and resolution directive and an insurance guarantee scheme directive would form a holistic framework for dealing with insurer failure"* and that the application of a resolution regime should be proportionate.

125. It is, therefore, essential to ensure that national authorities are equipped with a broad range of powers which enable them to intervene sufficiently

[31] EIOPA (2014): "Insurance Stress Test 2014", 30 November 2014.

[32] ESRB: "Report on systemic risks in the EU insurance sector", December 2015 (incl. Annexes). The other main sources of systemic risk identified by the ESRB are: 1) engagement in non-traditional and non-insurance activities, 2) procyclicality in asset allocation, 3) procyclicality in the pricing and writing of insurance, and 4) lack of substitutes in vital lines of insurance business. (See link: http://www.esrb.europa.eu/pub/pdf/other/2015-12-16-esrb_report_systemic_risks_EU_insurance_sector.en.pdf?d171a63f6e1d433f82e477d67416fbd5).

early in case of financial distress and to take rapid and effective actions when a failure of an insurer cannot be avoided. Taking account of the reported gaps and shortcomings in national frameworks and the lack of cross-border cooperation and coordination arrangements for insurers other than G-SIIs, existing frameworks might not be adequate to deal effectively with the consequences of a severe stress scenario affecting several insurers and/or jurisdictions. This could be reasonably assumed even though existing frameworks have not been tested in dealing with complex cross-border group failures or with multiple failure events happening simultaneously as there have been no such cases so far.

126. The financial crisis has shown that, where recovery and resolution measures are inadequate, public support to financial institutions may be needed to maintain financial stability in times of severe stress. Over the course of the financial crisis, European insurers received a total of approximately EUR 6.5 billion from public authorities[33], although this is less than the public support received by the banking sector it is still significant.[34] Box 5 includes some examples of insurance and bancassurance groups which received state aid during the financial crisis.

127. Harmonisation of recovery and resolution frameworks could help to minimise the reliance on public support in times of crisis and at the same time encourage market discipline and limit moral hazard by providing for effective recovery and resolution measures, including a clear set of resolution objectives.

Box 5: Examples of public intervention in insurance during financial crisis

Insurer	**Public intervention**	**Reason for intervention**
Ethias Group (Belgium)	In 2008, Ethias received €1.5 billion from the Belgian government.	The state aid was required to enable Ethias to continue its operations and to develop a restructuring plan to ensure its long-term viability, as it experienced a sharp fall in the value of its financial assets and the withdrawal of a large number of investors.
KBC Group (Belgium)	In 2008, the EC approved Belgian authorities' plans to recapitalise KBC with €3.5 billion.	The capital injection was considered to be necessary to maintain the market's confidence in KBC and to ensure its contribution in providing loans to the real economy. The capital injection was, however, mainly aimed at supporting the banking part of the group (financial conglomerate).

[33] European Commission: "Note for discussion by Expert Group on Banking, Payments and Insurance (EGBPI) meeting on 5 March 2015" (See link: https://www.eduskunta.fi/FI/vaski/Liiteasiakirja/Documents/EDK-2015-AK-3427.pdf).

[34] Between October 2008 and December 2012, the Commission approved €591.9 billion or 4.6% of EU 2012 GDP in state aid measures in the form of recapitalisation and asset relief measures. Source: European Commission, EU Bank Recovery and Resolution Directive (BRRD): Frequently Asked Questions, April 2014. (See link: http://europa.eu/rapid/press-release_MEMO-14-297_en.htm?locale=en).

Aegon (Netherlands)	In 2008, the EC approved a plan to recapitalise Aegon with €3 billion through a special type of securities.	The capital injection was considered to be necessary to maintain the markets' confidence in Aegon and to ensure its refinancing.
ING Group (Netherlands)	In 2008, a capital injection of €10 billion to ING Groep by the Dutch government was approved. A total of €2.8 billion was received by ING insurance.	The injection was considered to be necessary as a loss of confidence in a core institution as ING would have led to a further disturbance of the existing situation and harmful spill-over effects to the economy as whole.
SNS Reaal (Netherlands)	In 2008, SNS Reaal received a capital injection of €750 million from the Dutch government.	The capital injection was considered to be necessary to restore the markets' confidence in SNS REAAL and to ensure the contribution in providing loans to the real economy of its bank subsidiary.
Source: European Commission database (See link: http://ec.europa.eu/competition/recovery/cases.html)		

(E) Further enhancement of the single market

128. Furthermore, a harmonised environment promoting convergence of recovery and resolution practices in the EU could increase the willingness of policyholders to contract with insurers from other EU countries which would improve the European competitiveness in the insurance sector. A potential improvement of the level playing field would contribute to a further integration and enhancement of the single market and benefit the ongoing process of the creation of the Capital Markets Union.[35,36]

3.2.2 Arguments against harmonisation

(A) Normal insolvency procedures might be suitable

129. On the banking side, it was argued that normal insolvency procedures are unsuitable to deal with failures of banks which operate on the basis of public trust. Therefore, in order to avoid a run on banks and to maintain the financial stability in the EU, it was agreed that national authorities should be given sufficient powers to respond in a rapid and decisive manner to failing banks. This agreement resulted in the introduction of the BRRD.[37]

130. For the insurance sector, however, it is not demonstrated that in all Member States normal insolvency procedures would be unsuitable to deal with insurance failures across Member States. Furthermore, although fears of financial distress might similarly lead to a run on insurers in the form of

[35] Green Paper of the European Commission on retail financial services, better products, more choice, and greater opportunities for consumers and businesses (COM(2015) 630): *"One of the priorities of the Commission is the achievement of a deeper and fairer Single Market."*

[36] Please also refer to box 3 which illustrates the potential implications in the resolution of national insurance groups.

[37] European Commission, EU Bank Recovery and Resolution Directive (BRRD): Frequently Asked Questions, April 2014. (See link: http://europa.eu/rapid/press-release_MEMO-14-297_en.htm?locale=en).

mass surrenders by policyholders, the likelihood and the potential impact of such a scenario are lower compared to the banking sector.[38] Furthermore, it should be noted that in the insurance sector an insolvency situation materialises over time and failure is usually a "slow burn" process taking several years.

(B) No strong evidence for existing powers being ineffective in all Member States

131. It is also not demonstrated that in all Member States existing powers and tools have been unsuitable to deal with severe stress scenarios. It should, however, be noted that there are no cases of large cross-border insurance group failures in the EU. Furthermore, eight NSAs replied to the survey that they have not identified any gaps and shortcomings in their national framework. In fact, currently existing resolution powers, such as the power to transfer the portfolio of an insurer and the power to put an insurer into (solvent) run-off, have been regularly used in the past and have proven to be adequate in dealing with insurers in financial distress.

132. Any EU action to reinforce national frameworks could, therefore, be unwarranted and lead to undue administrative costs and burdens for those Member States which may already have adequate frameworks.

(C) National frameworks reflect national specificities in a better way

133. In order to initiate a legislative initiative at the EU level, there should be a strong case that EU actions are more effective than actions taken at the national levels.[39] This also applies to any potential initiative of EU legislators to harmonise existing recovery and resolution frameworks for insurers.

134. It could be argued that some of the Member States are better equipped to reinforce their national framework, taking into account the characteristics of their national insurance market. National specificities might not be addressed to the same extent if actions are taken at the EU level.

(D) Administrative burdens and costs for insurers and national authorities

135. Finally, harmonisation in the field of recovery and resolution might lead to additional administrative burden for both insurers and national authorities. In particular, the requirements to develop pre-emptive recovery and resolution plans could be seen as entailing significant administrative burdens for, respectively, insurers, especially small and medium-sized insurers, and national authorities.[40] The requirement for pre-emptive resolution plans might lead to an additional burden for insurers, as national authorities may request information from insurers for drafting the pre-emptive resolution plans. Also, the requirement to have a designated administrative resolution

[38] For instance, the Ethias group experienced a withdrawal of a large number of investors during the financial crisis in 2008, which could be interpreted as a run on the insurer (see box 5).

[39] European Commission "The principle of subsidiarity" (See link: http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=URISERV:ai0017&from=EN).

[40] Please refer to chapter 4 for the building blocks of a harmonised recovery and resolution framework for insurers.

authority, either as a separate authority or established within the NSA, might cause considerable additional costs.

136. The exact level of additional burdens cannot be estimated without an impact assessment, but it can be expected that it will be greater if potential new EU requirements would go beyond what is already in national frameworks.

137. In addition, harmonisation in the EU will require changes in national legislation and potentially a transposition into national legislation. This might create additional burdens and costs for Member States, especially, for those Member States which have already started to reinforce or are in the process of reinforcing their existing framework at the national level.

3.3 Conclusion

138. EIOPA is of the view that a certain degree of harmonisation of recovery and resolution practices in the EU would benefit policyholders, the insurance sector and more generally the financial stability in the EU. The past financial crisis has shown the importance of having in place adequate recovery and resolution measures, including cross-border cooperation and coordination arrangements, in order to ensure an orderly resolution of insurers.

139. Harmonisation would avoid a fragmented landscape of different national recovery and resolution frameworks, which could be a significant impediment to the management of crisis situations. Cross-border cooperation and coordination between national authorities in different Member States are crucial for an orderly resolution of cross-border insurance groups. A harmonised environment with a common set of recovery and resolution measures facilitates cross-border cooperation and coordination, as well as mutual alignment and recognition of resolution actions.

140. Furthermore, harmonisation could ensure a consistent implementation of the FSB Key Attributes and hence ensure that Member States have in place effective recovery and resolution frameworks which are needed to deal with severe stress or crisis situations. Adequate and effective frameworks are particularly essential in fragile market environments where there is a risk of insurance failures, like the current low interest rate environment which poses a significant risk for insurers. In order to protect policyholders and to avoid unnecessary disruption to the financial stability, as well as minimise reliance on public funds, it is essential that national authorities are equipped with the necessary powers and tools to deal effectively with crisis situations.

141. Although there is no strong empirical evidence that all national frameworks, including normal insolvency procedures, are inadequate to deal with insurance failures in an orderly manner, EIOPA's survey showed that most of the existing frameworks are not as comprehensive as the resolution regime prescribed by the FSB in the Key Attributes. In addition, it should be acknowledged that a number of Member States are in the process of reinforcing their national framework after gaps and shortcomings have been identified. Finally, as aforementioned, the absence of a harmonised framework could impede an effective cooperation and coordination process between national authorities in different Member States.

142. Harmonisation of existing recovery and resolution frameworks would therefore be desirable, whereby the drawbacks of harmonisation are fully taken into account. EIOPA is therefore of the view that a harmonised environment should provide for **minimum harmonisation** only. This would allow Member States to introduce additional measures and powers at the national level, as long as these are compatible with the objectives and principles set out at the EU level. This gives Member States the flexibility to address any national specificities of their insurance market at the national level. In addition, in order to avoid excessive (administrative) burdens for both insurers and national authorities, it should be ensured that the requirements in a harmonised framework are applied in a proportionate manner with the possibility to waive some of the requirements by national authorities, where appropriate.

Questions for stakeholders:

Q1) Do you consider the arguments in favour or against a harmonised recovery and resolution framework, as identified and analysed in this chapter, exhaustive?

Q2) In your view, are there any other arguments in favour or against a harmonised recovery and resolution framework which should be considered? If yes, please provide an explanation for the arguments.

4. Building blocks of recovery and resolution

4.1 Introduction

143. This chapter sets out the possible building blocks of a harmonised recovery and resolution framework for insurers in the EU. As aforementioned, the term "harmonised framework" is used to refer to a common minimum approach and does not aim to prejudge on the legal form of any potential work in this field by legislators.

144. In order to develop the building blocks, EIOPA followed a three-step approach. Firstly, EIOPA identified the main building blocks of an effective recovery and resolution framework for insurers (i.e. preparation and planning, early intervention, resolution and cooperation and coordination).

145. Secondly, the main building blocks are further defined and broken into sub-building blocks in accordance with the FSB Key Attributes. The FSB Key Attributes are used as guidance in order to avoid a potential conflict with the measures to which G-SIIs are subject to. Additionally, the current recovery and resolution practices in Member States and the ongoing work of the IAIS in this field are taken into account to the extent possible.

146. Finally, a way to harmonise the current recovery and resolution practices with respect to each of the sub-building blocks is proposed, including a way to apply the proportionality principle to each of the sub-building blocks.

4.2 Overview of building blocks

147. EIOPA chose to define and organise the building blocks of a harmonised recovery and resolution framework along the different stages of a crisis management flow, i.e. normal supervision, early intervention/recovery and resolution. In the context of insurers, the transition between supervision, recovery and resolution is usually a more gradual process compared to banking as a "run on the company" is less likely to happen. A recovery and resolution framework should facilitate an effective transition between these stages.

148. Before defining the building blocks, it should be noted that the aim of a harmonised EU recovery and resolution framework should be minimum harmonisation, as concluded in the chapter "Rationale for harmonisation". A harmonised framework should introduce a common set of powers and tools, while allowing Member States to adopt additional measures at the national level as long as these are compatible with the resolution objectives and principles set out at the EU level.

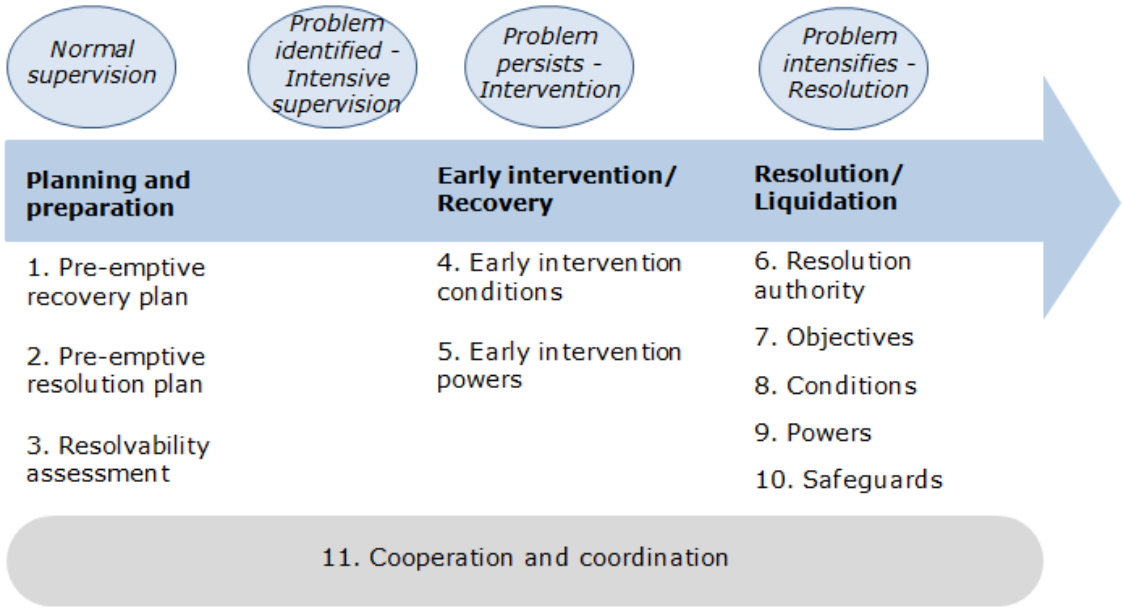
149. Furthermore, although the identified building blocks could form part of a single framework, they could also be considered individually, thereby allowing for a more targeted approach.

Proposal and potential considerations

150. A harmonised recovery and resolution framework should cover the following main building blocks and sub-building blocks (chart 16 provides an illustrative summary):

- **Main building block 1 - Preparation and planning:** Insurers and national authorities should make preparations during normal times of business for situations which might lead to financial stress or the failure of an insurer. The planning and preparation stage covers the building blocks pre-emptive recovery and resolution planning, including resolvability assessments.
- **Main building block 2 - Early intervention:** Early intervention could be regarded as further developing and supplementing Solvency II by granting NSAs a set of powers to intervene at a sufficiently early stage, i.e. before the breach of the SCR, in order to avoid the escalation of financial problems at an insurer. This requires the determination of early intervention conditions and a list of early intervention powers – the two building blocks for early intervention.
- **Main building block 3 - Resolution:** Once an insurer is no longer viable or is likely to be no longer viable, resolution authorities should have at their disposal a broad range of powers to resolve insurers in an orderly manner so as to meet resolution objectives. Resolution, therefore, covers the following building blocks: the designation of a resolution authority, the determination of resolution objectives, resolution conditions, resolution powers and safeguards.
- **Main building block 4 - Cooperation and coordination:** A harmonised framework should facilitate and empower the cooperation and coordination, as well as the exchange of information, between relevant national and foreign authorities.

Chart 16: Overview of main building blocks (4 in total) and sub-building blocks (11 in total) of a harmonised recovery and resolution framework for insurers



Questions for stakeholders:

Q3) What is your view on the proposed building blocks for recovery and resolution?

Q4) Should additional building blocks be considered? If yes, what should these building blocks be?

4.3 General principles

4.3.1 Scope

151. The scope of a resolution regime is defined as follows in the FSB Key Attributes (annex 2, paragraph 2.1): *"Any insurer that could be systemically significant or critical if it fails and, in particular, all insurers designated as Globally Systemically Important Insurers ("G-SIIs"), should be subject to a resolution regime consistent with the Key Attributes"*. This requires an ex-ante assessment of the likely impact of the failure of an insurer on the financial stability in order to determine whether the insurer should be subject to the requirements of a resolution regime. The prescribed scope captures all insurers which could be systemically significant or critical upon failure and is therefore not restricted to include only insurers classified as systemically important insurers in normal times of business, like G-SIIs.

152. The insurance sector serves a number of key economic functions. For instance, it is a facilitative business as it facilitates other economic activities, such as trade credit insurance, public and employers' liability and transport insurance. Furthermore, life insurance allows policyholders to smooth their incomes and is a key savings channel through which funds are invested in capital and debt instruments, as well as other assets.

153. Given this broader economic significance of insurance, it is not adequate to focus solely or primarily on the potential impact of an insurance failure on the financial stability when defining the scope of a recovery and resolution framework for insurers. Other objectives, particularly, the protection of policyholders, but also continuity of certain insurance functions and protection of public funds should be taken into account (see also section 4.5 "Early intervention" and section 4.6.3 "Sub-building block 7: Resolution objectives" for a more detailed description of the recovery and resolution objectives for insurers).

Proposal and potential considerations

154. The scope of a harmonised recovery and resolution framework should cover all insurers, including branches of third-country insurers situated in the EU, subject to the proportionality principle. As aforementioned in paragraph 34, please note that the term "insurers" is used to refer to "insurers, reinsurers and groups".

155. Insurers that are excluded from the scope of Solvency II due to their small size (i.e. annual gross written premium income does not exceed EUR 5 million and technical provisions does not exceed EUR 25 million) could be excluded from the scope of a harmonised recovery and resolution

framework. However, Member States should be given the flexibility to decide to make these insurers subject to the harmonised recovery and resolution framework. In fact, some Member States follow a similar approach for the definition of the scope of Solvency II and have used their national discretion to include small insurers within the scope of Solvency II.

Questions for stakeholders:

Q5) What is your view on the scope of a recovery and resolution framework?

4.3.2 Proportionality principle

Proposal and potential considerations

156. A harmonised recovery and resolution framework should not be too burdensome for insurers and national authorities. The proportionality principle should be applied both to the requirements imposed on insurers and national authorities and to the exercise of powers.

157. This means that national authorities should be allowed to ex-ante limit or exempt requirements imposed on insurers and national authorities. This could, for instance, be based on an insurer's size, complexity and business type as well as the interconnectedness of an insurer with the rest of the system.

158. The exercise of recovery and resolution powers should also be proportionate to the nature, scale and complexity of the situation and/or insurer and, furthermore, be subject to an assessment whether it is in the interest of the public (see also sub-building block "Resolution powers").

159. The specific applicability of the proportionality principle in each sub-building block is discussed further in the relevant sections below.

Questions for stakeholders:

Q6) What is your view on the approach to the proportionality principle, i.e. defining the specific applicability for each sub-building block separately?

4.4 Preparation and planning

4.4.1 General considerations

160. The aim of preparation and planning measures is to increase the awareness of and preparedness for crisis situations. In line with FSB Key Attributes 10 and 11, preparation and planning measures should include the requirement to develop and maintain pre-emptive recovery and resolution plans and to assess the resolvability of insurers.

161. EIOPA's survey on existing recovery and resolution frameworks shows that preparation and planning measures are currently only required in a limited number of Member States; pre-emptive recovery plans are required in seven Member States and pre-emptive resolution plans and resolvability assessments are required in only five Member States (see also section 2.2 "Preparation and planning").

162. In response to EIOPA's question whether shortcomings in existing national frameworks were identified, the lack of pre-emptive recovery and resolution planning was often mentioned by NSAs. The case study in box 3 (see chapter "Rationale for harmonisation") illustrates the experiences of an NSA which indicated that it would have been better prepared for, and, hence, have been better able to deal with the stated crisis situation in a more efficient manner, if recovery and resolution plans were developed in a pre-emptive manner.

4.4.2 Sub-building block 1: Pre-emptive recovery planning

163. Solvency II requires the development of a recovery plan once an insurer breaches or is likely to breach in the short-term the SCR.[41] From a crisis management perspective, it is however important to be prepared for such scenarios by developing and maintaining recovery plans in a pre-emptive manner, i.e. during normal times of business and before an insurer breaches the SCR. This increases the awareness and preparedness of insurers for adverse situations and allows making rapid and informed decisions in times of crisis. This pre-emptive approach was also taken in the FSB Key Attributes, which consider that *"All insurers that could be systemically significant or critical upon failure, and at a minimum all G-SIIs, should be subject to a requirement for an ongoing process of recovery and resolution planning"* (see Annex 2 - 9.1).[42]

164. In a pre-emptive recovery plan, an insurer sets out the possible options and measures it could or would adopt to restore its financial strength and viability following a (significant) deterioration of its solvency position. This includes a review of its risk profile, operations and funding sources.

165. A pre-emptive recovery plan differs from the own risk and solvency assessment (ORSA) which insurers are required to develop in Solvency II.[43] In the ORSA an insurer makes an assessment of its overall solvency needs taking into account its specific risk profile, approved risk tolerance limits and its business strategy. This does not necessarily include the identification of options to restore the financial strength and viability in case it comes under severe stress. Nevertheless, the ORSA might serve as an input for the development of pre-emptive recovery plans.

166. Other requirements under Solvency II could also be used as input for the pre-emptive recovery plan and, hence, limit the administrative burdens for

[41] Please see Article 138 of the Solvency II Directive (2009/138/EC).

[42] The essential elements of recovery and resolution plans are further detailed in the I-Annex 4 of the FSB Key Attributes and could therefore serve as guidance.

[43] Please see Article 45 of the Solvency II Directive (2009/138/EC).

insurers. This includes, for instance, the requirement to develop a medium-term capital management plan and contingency and emergency plans for colleges, as well as to report significant intragroup transactions and to disclose the group structure, including the legal, governance and organisational structure.[44]

167. Furthermore, the requirements for determining the technical provisions, SCR and MCR could and should be used to the extent possible when developing pre-emptive recovery plans in order to avoid unnecessary burdens for insurers.

Proposal and potential considerations

168. Harmonisation in the field of recovery and resolution should include a requirement for insurers to develop and maintain pre-emptive recovery plans. Pre-emptive recovery plans should be developed by insurance groups and individual insurance entities which are not part of a group. The development of group recovery plans should not, however, prohibit the possibility for host authorities to require the development of recovery plans by individual insurance entities.

169. In line with the FSB Key Attributes, pre-emptive recovery plans should include, at least, a strategic analysis, an operational plan for implementation and an analysis of the preparatory actions which might be needed to ensure that the recovery measures can be implemented in an effective and timely manner. The strategic analysis should include a description of the insurer or insurers covered by the plan, including a detailed description of the legal structure, business model, core business lines and functions whose disruption could harm the financial stability and/or real economy. As part of the strategic analysis, insurers should identify and assess possible recovery options, whereby severe stress scenarios combining adverse systemic and idiosyncratic conditions are taken into account. Insurers should also make an assessment of the necessary steps and time needed to implement the recovery measures, including the risks associated with the implementation.

170. Pre-emptive recovery plans should be submitted to NSAs for a review on their completeness and credibility of the recovery options set out in the plans. In case the NSA identifies material deficiencies in the plan or material impediments in its implementation, it should be able to require changes in the pre-emptive recovery plan.

171. Furthermore, insurers should update their pre-emptive recovery plans at least annually or when there are material changes to the risk profile, business or group structure.

Application of the proportionality principle

172. In order to avoid excessive burdens for insurers, NSAs should be able to apply simplified obligations relating to the content and detail of the pre-emptive recovery plans and the frequency for updating the plans.

[44] Please see Article 41, Article 245 and Article 256a of the Solvency II Directive (2009/138/EC).

Additionally, NSAs should have the power to waive the requirement entirely for certain insurers.

173. A harmonised framework should set out conditions which NSAs should consider in order to determine whether insurers should be subject to simplified obligations or no obligations at all. The conditions should, however, not be prescriptive in setting thresholds. Conditions could, for instance, include the size, complexity and business type as well as the interconnectedness of an insurer with the rest of the system. Further consideration is needed to define appropriate conditions for a harmonised recovery and resolution framework.

Questions for stakeholders:

Q7) Do you agree on the need for pre-emptive recovery planning?
Q8) In your view, what should the conditions be in order to determine the range of insurers for which simplified obligations could apply?
Q9) And what should the conditions be in order to determine the range of insurers which may be exempted from the requirement to develop recovery plans?
Q10) In your view, what should the content of pre-emptive recovery plans include?

4.4.3 Sub-building block 2: Pre-emptive resolution planning

174. As with pre-emptive recovery plans, the development of pre-emptive resolution plans increases the awareness of and preparedness for crisis situations by identifying strategies on how to carry out a potential resolution in the most effective and efficient manner. Pre-emptive resolution plans are the responsibility of national authorities charged with the resolution of insurers.

Proposal and potential considerations

175. Harmonisation in the field of recovery and resolution should include a requirement for resolution authorities to develop and maintain resolution plans in a pre-emptive manner. Pre-emptive resolution plans should be developed for insurance groups and individual insurance entities which are not part of a group. The development of group resolution plans should not, however, prohibit the possibility to develop resolution plans for individual insurance entities.

176. In line with the FSB Key Attributes, resolution authorities should consider various scenarios including the scenario that failure of an insurer might be idiosyncratic or may occur at a time of broader financial crisis or market stress. Pre-emptive resolution plans should therefore set out a range of resolution actions which the resolution authorities may take if an insurer enters into resolution. In these resolution plans resolution authorities will have to identify the potential need for resolution funding, the sources of funding, operational and practical arrangements for ensuring continuity of coverage and payment under insurance policies, and other relevant elements.

177. Pre-emptive resolution plans should be drafted in close cooperation with insurers and other relevant authorities, including the NSA. The resolution plans should be updated at least annually or when there are material changes to an insurer's risk profile, business or group structure.

Application of the proportionality principle

178. In order to avoid excessive burdens for resolution authorities, simplified obligations should apply with respect to the content and detail of the plans and the frequency for updating the plans. Additionally, resolution authorities should have the power to waive the requirement to draft resolution plans for certain insurers entirely.

179. A harmonised framework should set out conditions which NSAs should consider in order to determine whether the development of resolution plans could be subject to simplified obligations or whether the requirement could be waived. The conditions should, however, not be prescriptive in setting thresholds. Conditions could, for instance, include the size, complexity and business type as well as the interconnectedness of an insurer with the rest of the system.

180. Further consideration is needed to define appropriate conditions for waiving the requirement for resolution planning and simplified obligations. The conditions for pre-emptive resolution planning are likely to be set differently from those for pre-emptive recovery planning. This would result in a scope for resolution planning which is narrower compared to the scope for recovery planning.

181. In order to avoid excessive burdens for insurers, resolution authorities should try to limit the information required from insurers to what is essentially needed and cannot be gathered from other sources (e.g. information obtained from the ORSA, medium-term capital management plan, contingency and emergency plan, reporting of intragroup transactions, etc.).

182. Information requested from insurers could be requested in phases to ensure proportionality. For instance, resolution authorities could request i) baseline information to establish a resolution strategy; ii) detailed information to develop the preferred resolution strategy; and iii) additional information if an insurer is experiencing stress and approaching possible resolution.

Questions for stakeholders:

Q11) Do you agree on the need for pre-emptive resolution planning?Should there be any difference in the scope for pre-emptive recovery planning and resolution planning? If yes, what are the reasons for this?

Q12) What should the conditions be in order to determine the range of insurers for which the resolution authorities may waive the requirement to develop pre-emptive resolution plans?

Q13) In your view, what should the conditions be in order to determine the range of insurers for which simplified obligations could apply?

Q14) In your view, what should the content of pre-emptive recovery plans include?

4.4.4 Sub-building block 3: Resolvability assessments

183. FSB Key Attribute 10 states that *"Resolution authorities should regularly undertake, at least for G-SIFIs, resolvability assessments that evaluate the feasibility of resolution strategies and their credibility in light of the likely impact of the firm's failure on the financial system and the overall economy".*

184. Resolvability assessments are part of the resolution planning process and help to identify impediments to the resolvability of an insurer by assessing the feasibility and credibility of the resolution strategies. Impediments to the resolvability could for instance be the complexity of the group structure or a high degree of interconnectedness.

Proposal and potential considerations

185. A harmonised recovery and resolution framework should include a requirement for resolution authorities to assess the resolvability of insurers. The assessment should include an evaluation of the feasibility and credibility of the resolution strategies.

186. In line with the FSB Key Attributes, the feasibility assessment should capture elements such as the likely availability of a transferee or purchaser for an insurer's portfolio, the capacity of an IGS to fund a potential transfer and the availability of human resources to run the resolution process. The credibility assessment involves an evaluation of the impact of the resolution actions on third parties and financial stability. Resolution authorities should, for instance, consider whether the identified resolution strategies could have a material adverse impact on economic activity which may be caused by a disruption to the continuity of insurance cover and payments, a forced sale of distressed assets and/or by a lack of policyholder confidence.

187. In case resolution authorities identify significant impediments to the resolvability of an insurer, they should be able to require the removal of these impediments. However, careful consideration should be given to these impediments before requiring the removal hereof. In principle, only substantive impediments should be considered.

Application of the proportionality principle

188. Resolvability assessments should be done in a proportionate manner and, where relevant, subject to simplified obligations. Additionally, the power to require the removal of impediments should be exercised in a proportionate manner and the insurer should first be given the opportunity to make its own proposal to remove any identified impediments. Finally, resolution authorities would only have to assess the resolvability of insurers for which resolution plans are drafted.

Questions for stakeholders:

Q15) Do you agree that resolution authorities should only have to assess the resolvability of insurers for which a resolution plan is drafted?

Q16) Do you agree that resolution authorities should have the power to require the removal of significant impediments to the resolvability of an insurer? And what type of potential impediments could be considered?

Q17) How could the simplified obligations in assessing the resolvability of insurers be defined?

4.5 Early intervention

4.5.1 General considerations

189. Early intervention, as defined here, could be regarded as further developing or supplementing the existing powers and tools in Solvency II. The aim is, therefore, to supplement Solvency II and not to interfere with the actual supervisory work. Early intervention aims to avoid the escalation of financial problems at an insurer and take place when the insurer is in a going concern situation.

190. The objectives for early intervention are therefore similar to the supervisory objectives as specified in Solvency II: "*The main objective […] is the adequate protection of policyholders and beneficiaries. Financial stability and fair and stable markets are other objectives of insurance and reinsurance regulation and supervision which should also be taken into account but should not undermine the main objective*".[45]

191. According to the supervisory ladder of intervention in Solvency II, NSAs are able to take recovery measures once an insurer is in breach or there is a risk it will be in breach of the regulatory capital requirements.[46] In such a scenario, NSAs could take all necessary measures to safeguard the interest of policyholders if the solvency position of an insurer continues to deteriorate.[47] However, in some situations, intervention by the NSA might be needed before the breach of the regulatory capital requirements in order to avoid the escalation of financial problems. This could be captured by the early intervention stage.

192. In addition, Solvency II does not set out a detailed list of powers. In EIOPA's survey on existing recovery and resolution frameworks, the fact that intervention powers are not explicitly provided for in national frameworks was often mentioned by NSAs as a restriction and shortcoming in existing frameworks. In total, one third of the NSAs indicated that they have identified deficiencies in their early intervention powers. Furthermore, the survey showed that NSAs have at their disposal a different set of early

[45] Please see Article 27 and Article 28 of the Solvency II Directive (2009/138/EC).

[46] According to Article 138 and Article 139 of the Solvency II Directive (2009/138/EC), an insurer is no longer compliant with the SCR/MCR if it is in breach of or where there is a risk it will breach the SCR/MCR in the following three months. If an insurer is in breach of the SCR or MCR, it will have to submit a recovery plan or a short-term finance scheme to the NSA.

[47] Please see Article 141 of the Solvency II Directive (2009/138/EC).

intervention powers which can usually be exercised before the breach of the SCR (see also section 2.3 "Early intervention"). A common set of powers could therefore be beneficial and supplement the powers already included in Solvency II.

Questions for stakeholders:

Q18) Do you think that early intervention should be part of a recovery and resolution framework for insurers?

4.5.2 Sub-building block 4: Early intervention conditions

193. With respect to defining the conditions for the exercise of early intervention powers, two types of conditions can be identified: quantitative and qualitative conditions. It is important to find a proper balance between the two types of triggers which should allow for a sufficient degree of supervisory discretion.

Proposal and potential considerations

194. A harmonised recovery and resolution framework may benefit from setting out effective early intervention conditions. The conditions should be defined in such a way that the criteria allow for a sufficient degree of supervisory judgement and discretion. Hard quantitative criteria should be avoided.

195. Early intervention, as defined here, should be triggered before the Solvency II supervisory ladder of intervention becomes effective (i.e. before the breach of the SCR) and cover the point where the financial situation of an insurer starts to deteriorate and is expected to deteriorate even further if no action is taken.

196. However, further consideration is needed to define adequate conditions and criteria which should allow for a sufficient degree of supervisory judgement and discretion. For instance, the following could be taken into account:

- A notable deterioration in insurer specific financial indicators (e.g. fall in solvency ratio, downgrade of credit rating, material fall in insurer's share price or material rise in insurer's credit spread);
- A notable deterioration in relevant external financial indicators (e.g. a sharp fall in financial markets to which the insurer is exposed to);
- A notable deterioration in relevant non-financial indicators (e.g. increase in life expectancy).

197. Further consideration is also needed in order to find a balance between i) avoiding that the introduction of early intervention conditions creates a new intervention level and, hence, an extra level of solvency requirement and ii) providing for adequate legal security.

Application of the proportionality principle

198. Early intervention conditions should be judgement-based rather than hard and fast rules to allow for the different nature of insurers and changing economic circumstances. NSAs should therefore use supervisory judgement and discretion to decide whether intervention is needed before the breach of the SCR. Early intervention conditions should not lead to a mechanistic decision-making process by the NSA.

Questions for stakeholders:

Q19) What is your view on the approach towards early intervention conditions?

4.5.3 Sub-building block 5: Early intervention powers

Proposal and potential considerations

199. A harmonised recovery and resolution framework could provide for a minimum set of common early intervention powers. The choice and application of the powers should however not be made compulsory. NSAs should have discretion over how to intervene and which power(s) to apply.

200. Table 3 includes a (non-exhaustive) list of early intervention powers which could be considered in a harmonised framework. The list of powers should be regarded as examples of early intervention powers. Other powers could also be considered, including the potential use of powers included in Solvency II. For instance, the development of the Solvency II recovery plan (in Solvency II required after the breach of the SCR) and the finance scheme (in Solvency II required after the breach of the MCR) could possibly be implemented in an early intervention phase.

201. The survey of EIOPA shows that most of the powers listed in table 3 are currently broadly available to NSAs, either explicitly or implicitly via general direction-making powers.

202. It should be noted that these powers are not of exclusive use in the early intervention phase. The powers may also be exercised after the breach of the SCR (in accordance with Article 141 of the Solvency II Directive) and in the resolution process of insurers.

Application of the proportionality principle

203. NSAs should ensure that the use of the early intervention powers is proportionate to the nature, scale and complexity of the insurer. In addition, NSAs could be granted with those powers but should not be imposed to use the proposed powers.

Table 3: Early intervention powers

Powers aimed at restoring compliance, capital adequacy and soundness
• Require an insurer to call for cash injections by shareholders, parent or partner companies

• Require additional provisioning or reserves from an insurer • Require an insurer to get prior supervisory approval for any substantial capital expenditure, material (financial) commitment or contingent liability • Require an insurer to use net profits to strengthen own funds • Limit or restrict profit distributions to shareholders
Measures affecting management and governance • Require the reinforcement of governance arrangements, internal controls and risk management systems • Require the removal of members of the management body, directors or managers of the insurer • Require an insurer to limit variable remuneration and bonuses
Measures affecting the business and organisation • Limit or restrict certain business lines and operations (e.g. to avoid certain risks, such as concentration, operational or liquidity risks) • Require the insurer to limit intra-group asset transfers and transactions and to limit asset transfers and transactions outside the group • Require additional reinsurance or changes to an insurer's reinsurance arrangements • Restrict/prohibit the disposal of any asset without prior supervisory authorisation

Questions for stakeholders:

Q20) Do you have any comments on the early intervention powers listed in the table?

Q21) Should other early intervention powers be considered? If yes, what are these powers?

4.6 Resolution

4.6.1 General considerations

204. According to the FSB Key Attributes, it is essential to designate a resolution authority and to define resolution objectives, conditions, powers and safeguards for an orderly resolution of insurers.

205. The results of EIOPA's survey on existing recovery and resolution frameworks reveal that there are substantial differences in existing national frameworks with respect to each of these aspects. These differences could potentially impede the resolution process of cross-border insurance groups (see also section 2.4 "Resolution").

4.6.2 Sub-building block 6: Resolution authority

206. According to FSB Key Attribute 2 *"each jurisdiction should have a designated administrative authority or authorities responsible for exercising the resolution powers over firms within the scope of the resolution regime ("resolution authority")"*.

207. EIOPA's survey on existing recovery and resolution frameworks shows that the vast majority of the Member States do not currently have an officially designated administrative resolution authority for insurers. Usually, the NSA and/or a relevant ministry, where needed in cooperation with an administrator, handle the resolution of insurers.

208. However, for an effective and orderly resolution it is essential to have a designated administrative authority with statutory responsibilities, transparent processes, sound governance and adequate resources. It is however not essential which authority is appointed as the resolution authority as long as its operational independence is ensured. This would avoid any unnecessary interference with the existing institutional framework in Member States.

209. The resolution authority could, for instance, be set up within the NSA or competent ministries. In the former case, appropriate checks and balances should be in place in order to avoid regulatory forbearance, which is driven by concerns that NSAs may procrastinate on putting an insurer into resolution, as it may be likely to suggest to external observers that the insurer has not been monitored properly. In addition to its operational independence, Member States should be ensured that resolution authorities have thorough knowledge of the insurance sector, including its economic and institutional characteristics

Proposal and potential considerations

210. Member States should have an administrative resolution authority for insurers, whereby Member States should be given the flexibility to decide which authority to designate as the resolution authority (e.g. the NSA, competent ministries or a specially appointed authority).

211. Member States should ensure the operational independence of the resolution authority in order to avoid regulatory forbearance. Additionally, it should be ensured that resolution authorities have adequate expertise and resources to manage the resolution of insurers at national and cross-border level.

Questions for stakeholders:

Q22) Do you agree that Member States should consider the designation of an administrative resolution authority for the resolution of insurers?

4.6.3 Sub-building block 7: Resolution objectives

212. With respect to the resolution objectives, the FSB Key Attributes state that *"a resolution regime should make it feasible to resolve an insurer without severe systemic disruption or exposing taxpayers to loss, while protecting vital economic functions through mechanisms that make it possible for shareholders and unsecured creditors to absorb losses in a manner that respects the hierarchy of claims in liquidation. For insurers, the resolution regime should have as specific objective the protection of policyholders, beneficiaries and claimants. This however does not mean that policyholders will be fully protected under all circumstances and does not exclude the*

possibility that losses be absorbed by policyholders to the extent they are not covered by policyholder protection arrangements".[48]

213. An effective recovery and resolution framework should therefore clearly set out the objectives of resolution. The survey of EIOPA revealed that NSAs pursue on average three objectives when resolving insurers. It also showed that the protection of policyholders is the primary objective for resolution in a majority of the Member States, followed by financial stability. Other objectives often mentioned include the protection of public funds and the continuity of critical functions.

Proposal and potential considerations

214. A harmonised recovery and resolution framework should clearly set out the objectives of resolution which should include:
    - Protection of policyholders;
    - Financial stability;
    - Continuity of functions whose disruption could harm the financial stability and/or real economy;
    - Protection of public funds (by minimising reliance on extraordinary public support and enhancing the market discipline).

215. Depending on the situation, resolution authorities should balance these objectives appropriately and try to minimise the cost of resolution by avoiding destruction of value unless necessary to achieve the resolution objectives.

216. The objective of policyholder protection does not mean that policyholders will be fully protected under all circumstances and does not exclude the possibility that losses be absorbed by policyholders, subject to the safeguard that they do not face larger losses than they would have suffered in normal insolvency procedures (see also sub-building block 10 Safeguards and restrictions).

Questions for stakeholders:

Q23) Do you agree with the objectives of resolution? Should other objectives be considered? If yes, what are these objectives?

Q24) Should the objectives be ranked? If yes, how should this look like and which objective should be the primary objective? If no, how could potential conflicts between the objectives be resolved (e.g. between policyholder protection and financial stability)?

4.6.4 Sub-building block 8: Resolution conditions

217. The FSB Key Attributes prescribe that an insurer should be put into resolution if it is *"no longer viable or likely to be no longer viable, and has no*

[48] Key Attributes, Annex 2, paragraph 1.1.

reasonable prospect of becoming so". Furthermore, it also stresses that the resolution regime *"should provide for timely and early entry into resolution before a firm is balance-sheet insolvent and before all equity has been fully wiped out".*[49]

218. EIOPA's survey on existing recovery and resolution frameworks shows that most of the national frameworks do not set out specific conditions for entry into resolution; hence, conditions related to the breach of Solvency II requirements are often used by NSAs to determine whether resolution actions are needed.

Proposal and potential considerations

219. A harmonised recovery and resolution framework should clearly set out the conditions for entry into resolution, whereby the relation with the triggers for insolvency proceedings needs to be assessed and taken into account.

220. In line with the FSB Key Attributes[50], the conditions for entry into resolution could, for instance, be the following:
    - The insurer is no longer viable or likely to be no longer viable ("point of non-viability");
    - Recovery measures have failed, or there is a strong likelihood that proposed recovery measures will not be sufficient, to return the insurer to viability or cannot be implemented in a timely manner (previous measures may include measures implemented by the private sector, including measures within the scope of an IGS, or measures implemented by the NSA and/or the insurer[51]);
    - A resolution action is necessary in the public interest, meaning that the resolution objectives could be achieved to a greater extent if the insurer is put into resolution versus the situation where it is liquidated by means of regular insolvency proceedings (the so-called public interest test).

221. Furthermore, the point of non-viability (i.e. the insurer is no longer viable or likely to be no longer viable) could be further specified as follows:
    - *The insurer is in breach of or likely to be in breach of the MCR, assets backing technical provisions, or other prudential requirements*.
      In practice, this means that the insurer's going concern status is jeopardised.
    - *There is a strong likelihood that policyholders or creditors will not receive payments as they fall due*.
      The implementation of a resolution action is necessary and expedient to realise this and/or resolution objectives.

[49] FSB Key Attributes, 3.1

[50] FSB Key Attributes, II-Annex 2, 4.1.

[51] It should be noted that prior implementation of early intervention and recovery measures is not a precondition for the adoption of resolution actions.

Application of the proportionality principle

222. Resolution authorities should ensure that the decision to initiate a resolution process is based on the judgement that the conditions for resolution are met. A decision-making process based on hard and fast rules should be avoided as this could limit resolution authorities' ability to act.

Questions for stakeholders:

Q25) Do you agree with the conditions for entry into resolution?

Q26) Do you agree with the conditions for determining the point of "non-viability" (i.e. where an insurer is no longer viable or likely to be no longer viable)?

Q27) What other conditions could be used to define the point of "non-viability"?

4.6.5 Sub-building block 9: Resolution powers

223. As stated in FSB Key Attribute 3, it is essential that *"Resolution authorities should have at their disposal a broad range of resolution powers"* to ensure that insurers can be resolved in an effective and orderly manner. EIOPA's survey on existing recovery and resolution frameworks showed that most of the powers listed in the FSB Key Attributes are not widely available in the EU at this stage. As a result, twelve NSAs have replied to the survey that this is a shortcoming of the current framework (while only eight NSAs have stated that they have not identified a shortcoming).

224. The introduction of common resolution powers in the EU should ensure that resolution authorities in all Member States have at their disposal a minimum set of powers to resolve insurers. The choice and application of the powers should however be left to the discretion of resolution authorities, which should have the legal and operational capacity to use one or multiple resolution powers, with resolution actions being either combined or applied sequentially.

Proposal and potential considerations

225. A harmonised recovery and resolution framework should provide for a common set of resolution powers. Table 4 presents a list of resolution powers which could be considered for inclusion in a harmonised framework.[52] These powers are chosen in accordance with the powers listed in the FSB Key Attributes.

226. Some of these powers, however, require further consideration in order to fully assess their impact; particularly, the power to bail-in shareholders, creditors or policyholders needs careful consideration in order to assess its

[52] The resolution powers could also be linked to different resolution scenarios in the respective resolution plans, in order to have a better understanding of their impact on private property and policyholders' rights.

potential negative impact on, for instance, an insurers' access to financial markets, as well as the confidence in the insurance sector.

227. It should also be noted that the list of powers is not exclusive and/or exhaustive; resolution authorities could apply other resolution powers which are available in their Member States. In addition, resolution authorities should have the discretion to apply resolution powers at the level of an individual insurance entity or at the level of an insurance group holding company located within their jurisdiction.

Application of the proportionality principle

228. Resolution authorities in charge of resolution should ensure that the use of resolution powers is proportionate to the nature, scale and complexity of the insurer.

Table 4: List of resolution powers
(based on the powers listed in the FSB Key Attributes)

Resolution authorities should have the power to:

- Withdraw license to write new business and put all or part of the insurance business contracts into run-off (i.e. requirement to fulfil existing contractual policy obligations for in-force business);
- Transfer all or part of the insurer's business to a solvent insurer or third party (including a bridge institution);
- Create and operate a bridge institution to which the business of a failing insurer can be transferred;
- Override any restrictions to the transfer of an insurer's business under applicable law (e.g., requirements for approval by shareholders, policyholders' consent for transfer of insurance contracts or consent of the reinsurer for transfer of reinsurance);
- Transfer any reinsurance associated with transferred insurance policies without the consent of the reinsurer, subject to adequate safeguards;
- Restructure, limit or write down liabilities, including insurance and reinsurance liabilities, and allocate losses to creditors and policyholders,[53] where applicable and in a manner consistent with the statutory creditor hierarchy and jurisdiction's legal framework;
- Temporarily restrict or suspend the policyholders' rights of withdrawing their insurance contracts;
- Stay rights of reinsurers of a cedent insurer to terminate or not to reinstate coverage on the sole ground of the cedent's entry in recovery or resolution;
- Impose a moratorium with a suspension of payments to unsecured creditors and a stay on creditor actions to attach assets or otherwise collect money or property from the firm;
- Stay early termination rights associated with derivatives and securities lending transactions;

[53] Restructure, limit or write down insurance and reinsurance liability and allocate losses to policyholders should be a last resort measure, and subject to adequate safeguards (see sub-building block 10 "Safeguards and restrictions").

- Sell or transfer the shares in the insurer to a third party;
- Initiate the liquidation of the insurer or part of it;
- Ensure continuity of essential services (e.g. IT) and functions by requiring other entities in the same group to continue to provide essential services to the insurer in resolution, any successor or an acquiring entity.

Questions for stakeholders:

Q28) Do you have general comments on the powers listed above?
Q29) Should other powers be considered? If yes, what are these powers?
Q30) Do you have specific comments on the power to bail-in shareholders and creditors?
Q31) In your view, what are the benefits and what could be the potential (wider) implications or side effects of the power to bail-in shareholders and creditors?
Q32) Do you have specific comments on the power to bail-in policyholders?
Q33) In your view, what are the benefits and what could be the potential (wider) implications or side effects of the power to bail-in policyholders?

4.6.6 Sub-building block 10: Safeguards

229. According to FSB Key Attribute 5, the resolution of insurers should be subject to safeguards. The Key Attribute states that resolution authorities should apply the NCWO principle. This principle should ensure that creditors do not incur a loss greater than they would have incurred in a normal insolvency procedure. Additionally, it states that resolution powers should be exercised in a way that respects the hierarchy of claims, while providing flexibility to depart from the general principle of equal (*pari passu*) treatment of creditors of the same class

230. EIOPA's survey on existing recovery and resolution frameworks shows that the NCWO principle is applied in one third of the Member States. The flexibility to depart from the *pari passu* principle appears to be possible in only four Member States.

Proposal and potential considerations

231. The resolution of insurers should be made subject to adequate safeguards, including the safeguard that the exercise of resolution subject be subject to the NCWO principle.

232. Additionally, resolution powers should be exercised in a way that respects the hierarchy of claims, while providing the flexibility to depart from the *pari passu* principle. This means that a differential treatment between creditors in the same class could be possible provided that it is in the interest of the public and complies with the NCWO principle. The aim of such a differential treatment is to maximise the value for creditors, including policyholders, as

a whole. For example, a differential treatment could be made between policyholders covered by an IGS versus those who are not. An overall fair treatment of all creditors and policyholders should however be ensured. For instance, differences between policyholders holding a policy with guaranteed rates versus policyholders with unit-linked products should be taken into account, as well as the differences between policyholders with incurred claims versus policyholders with future claims.

233. For partial property or portfolio transfers additional safeguards may be appropriate; for instance, to protect secured liabilities and to protect set-off and netting arrangements.

Questions for stakeholders:

Q34) Do you think that other safeguards are needed on top of the above mentioned safeguards and restrictions?

4.7 Cooperation and coordination

4.7.1 Sub-building block 11: Cooperation and coordination

234. FSB Key Attribute 12 requires jurisdictions to *"ensure that no legal, regulatory or* policy *impediments exist that hinder the appropriate exchange of information, including firm-specific information, between supervisory authorities, central banks, resolution authorities, finance ministries and the public authorities responsible for guarantee schemes"*.

235. As concluded in the chapter "Rationale for harmonisation", cooperation and coordination between national and foreign authorities is essential to ensure an orderly resolution of (cross-border) insurance groups.

236. EIOPA's survey on existing recovery and resolution frameworks revealed, however, that a majority of Member States do not have in place (formal) crisis management groups or other equivalent arrangements to deal with crisis situations. Furthermore, five NSAs reported that this is a shortcoming in the existing framework (see also section 2.5 "Cross-border cooperation and coordination").

Proposal and potential considerations

237. Cooperation and coordination, including the exchange of information, between resolution authorities is essential for an orderly resolution of cross-border insurance groups (including conglomerates). Member States should establish cooperation and coordination arrangements to facilitate this by, for instance, establishing crisis management groups or equivalent arrangements.

238. The need for cooperation and coordination across Member States starts before a crisis does. Therefore, whilst a crisis management approach is necessary to ensure an orderly resolution, a certain level of cooperation pre-crisis is required. For instance, an insurer regulated by one NSA may be systemically important in another Member State or have an impact on

significantly more policyholders than it does in its home state. Cross-border cooperation is therefore also required at the resolution planning stage in order to ensure that the impacts across all Member States are considered appropriately.

239. Resolution authorities should ensure that they involve all relevant authorities in the resolution process, and not only other (foreign) resolution authorities. For instance, NSAs, ministries, central banks and IGSs should be involved where necessary.

240. In order for cooperation and coordination arrangements to work efficiently, a number of elements need to be agreed upon between Member States. For instance, the agreements should establish the objectives and processes for cooperation through these arrangements, define the roles and responsibilities of the authorities, establish emergency contact lists and set out the process for information sharing and decision-making before and during a crisis.[54] The facilitation of information exchange requires particular consideration as this may be difficult to achieve in practice due to confidentiality issues.

241. Furthermore, when dealing with cross-border failures resolution authorities should ensure that due consideration is given to the interests of each Member States where the parent undertaking, subsidiaries and branches are located. The interests of each Member State should be balanced appropriately.

Application of the proportionality principle

242. Member States should have the flexibility to decide how to set up the cooperation and coordination arrangements. They could, for instance, decide to establish new arrangement or make it part of or an add-on to an already existing Solvency II supervisory college.

243. The participation, role and responsibility of resolution authorities in cooperation and coordination arrangements could depend on the materiality of their insurer belonging to an insurance group.

Questions for stakeholders:

Q35) Do you agree on the need to have cooperation and coordination arrangements (e.g. crisis management groups or equivalent arrangements) in place for cross-border insurance groups?

Q36) How should these cooperation arrangements be organised in order to allow for an efficient decision-making process?

Q37) What other issues need to be considered in order for the cooperation arrangements to work more effectively and efficiently?

Q38) In your view, how and/or to what extent should third countries be involved in these cooperation arrangements?

[54] A detailed list of elements can be found in the Key Attributes: Key Attribute 9 and I-Annex 2.

4.8 Resolution funding & insurance guarantee schemes

244. An important element of resolution is resolution funding which is not covered by the current work of EIOPA. The funding of resolution actions presents elements of complexity and is strictly related to the existence and the functioning of IGSs in a majority of the Member States. As aforementioned, EIOPA decided to follow a pragmatic and gradual approach by which as a first step the main building blocks of a harmonised recovery and resolution framework (as identified in this chapter) are addressed. It was decided that the potential harmonisation of resolution funding and IGSs requires further assessment and needs to be considered as a stand-alone topic. This might be addressed at a later stage.