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Invited Article II

EIOPA's Role in Crisis Prevention, Management and Resolution

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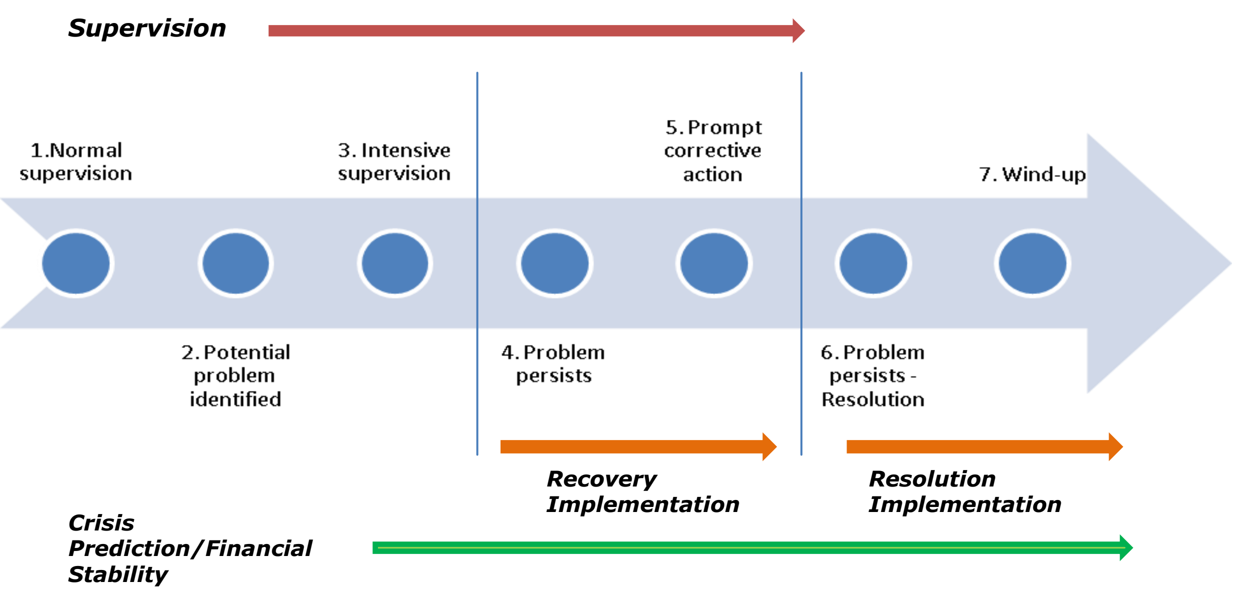
The European Insurance and Occupational Pensions Authority (EIOPA) was created, together with two other European Supervisory Authorities and the European Systemic Risk Board (ESRB), as a direct response to the 2008 financial crisis. One of its key responsibilities is to take an overview of the EU insurance sector in order to identify systemic risks and to coordinate the actions of national supervisory authorities in the face of such risks. These responsibilities are at the core of EIOPA's approach to crisis prevention and management, along with a number of powers and tools that it may use.[1]

Fundamental Approach

EIOPA's fundamental approach to crisis prevention and management is to view them as part of a continuum of supervisory activities, as outlined in Diagram 1. EIOPA considers crisis prevention as the best way to deal with crisis management and resolution, which is reflected in its day-to-day approach. In effect, crisis prevention is one of the most important means of ensuring policyholder protection.

Diagram 1



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1 See Article 18 of Regulation (EU) No 1094/2010 of 24 November 2010 establishing the EIOPA.

In terms of crisis prevention, an essential task carried out by EIOPA is the identification and prediction of “adverse developments” in insurance, financial markets and economic conditions in order to highlight these to national supervisors and facilitate early action. EIOPA has the advantage of being able to take an EU overview and identify patterns emerging across national markets.

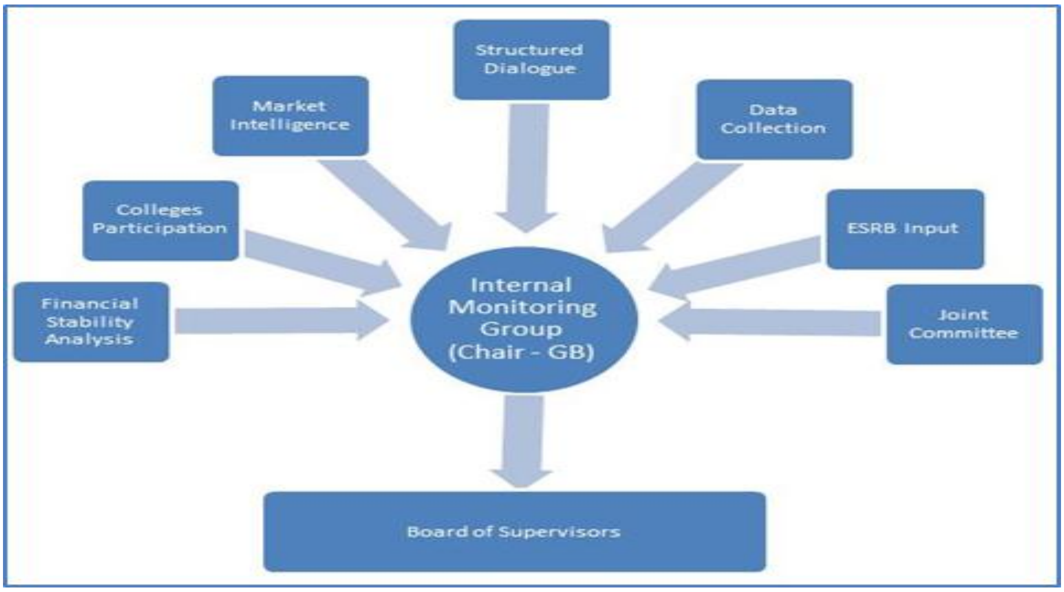
EIOPA also provides a unique forum for national supervisory authorities to share information and experiences on how they are dealing with particular issues. Of itself, this simple act of information sharing is a first step towards achieving greater consistency across jurisdictions.

Crucial in all of this is a successful working relationship between EIOPA and national supervisory authorities and clarity about their respective roles. National supervisory authorities retain their full powers in relation to the supervision of firms, whereas EIOPA’s role is to facilitate and, where necessary, coordinate supervisory actions on an EU basis. It therefore seeks to complement the work of national supervisory authorities rather than to replace them.

Some Organisational Details

So how does EIOPA actually achieve coordination across such a wide membership and make decisions in a timely and effective way? Organisationally, EIOPA has a small “Internal Monitoring Group” (IMG) chaired by the EIOPA Chairman and comprising a small number of EIOPA staff and EIOPA Board of Supervisors members. It is tasked with assessing the need for EIOPA action and making proposals for such action to the EIOPA Board of Supervisors.

Diagram 2



The IMG regularly reviews a range of macro and micro-information ranging from financial stability analysis through intelligence gathered from EIOPA’s participation in supervisory colleges to cross-sectorial input from the Joint Committee[2] (see Diagram 2). This group reflects the variety of perspectives across EU supervisory authorities with membership from large and small jurisdictions, along with those that have more cross-border firms operating in their markets. The proposed policy actions put to the EIOPA Board of Supervisors benefit from the perspective of the IMG in two ways. First, because the IMG focuses on issues which are likely to be of importance to EIOPA’s broader membership, thereby acting as a preliminary filter. Second, because the IMG, by taking this perspective, ensures that proposals put to the EIOPA Board of Supervisors can be processed quickly and efficiently. The provision of mature, well-formed proposals speeds their passage through the EIOPA Board of Supervisors, which is the legal decision-making body for EIOPA.

[2] The Joint Committee brings together the senior management of EIOPA, the European Securities and Markets Authority (ESMA) and the European Banking Authority (EBA) to ensure cross-sectorial coordination and, where necessary, to take joint decisions affecting all financial sectors in their respective remits.

EIOPA's internal procedures also include provision for an emergency group, which would serve as the organisational platform for the active coordination of measures taken by national supervisory authorities to deal with a crisis situation. This group has not been triggered to date.

What Has EIOPA Actually Been Doing in this Area?

In concrete terms, the period since EIOPA's establishment in January 2011 has been very busy in the areas of crisis prevention, management and resolution:

- As a new organisation, much effort had to be put into institution-building. In order to be ready to carry out its responsibilities under Article 18 of the EIOPA Regulation, EIOPA put in place initial basic processes when it was established. Over the course of 2011, the exercise gathered pace and resulted in a comprehensive set of processes and structures to allow EIOPA to discharge its responsibilities. The IMG is a central element of this structure.
- EIOPA also needed to build trust with its members and better understand national conditions as a basis for better facilitation of coordinated actions. EIOPA engaged in a process of so-called "structured dialogue" with national supervisory authorities to better understand the conditions in national markets and also the local supervisory response to the ongoing crisis. Besides completing the EU picture, this work built trust by giving a very clear understanding of the challenges facing national supervisors and the positions they may take on proposed actions.
- EIOPA has sought to better understand the exposure of the EU insurance sector to emerging risks. It has gathered information, drafted reports and shared them among its members, covering issues such as:
    - exposures to sovereign and bank risk, across instrument types and durations;
    - qualitative information on anticipated changes in balance sheets, liquidity positions and cashflows;
    - product types exposed to the impact of a prolonged period of low interest rates, as well as the measures available to firms and national authorities to deal with such risks; and
    - the full range of measures deployed by national supervisory authorities to deal with the financial crisis.
- EIOPA has been able to make informed decisions on the need for specific coordinated supervisory action in response to the crisis. EIOPA members agreed on a "common approach" to dealing with the financial crisis covering the risks that would be the focus of supervisory scrutiny, as well as the preparation of firms to deal with any emerging risks.
- At every EIOPA Board of Supervisors meeting there is a session dedicated to the sharing of information on supervisory developments and the consideration of what actions EIOPA should take. Thankfully, the EU insurance sector continues to weather the financial crisis reasonably well, which has limited the need for heavy action by EIOPA. Nevertheless, a close watch is being kept.

So What About Resolution?

Resolution has deliberately not been mentioned in detail so far, since the resolution of insurance firms is very much a national preserve. While the Directive on reorganisation and winding up of insurance undertakings[3] provides for recognition of reorganisation and winding up proceedings across borders, there is limited scope for coordination.

EIOPA has been working on the theoretical and practical underpinnings for recovery and resolution in insurance, trying to understand the basic rationale and implications. This reflects the work going on in a number of international forums. In parallel, a new development in this area is a consultation by the European Commission on a possible framework for recovery and resolution of non-bank financial institutions. Insurers are explicitly dealt with in this consultation and EIOPA will make a response to the consultation.

[3] Directive 2001/17/EC on reorganisation and winding up of insurance undertakings.

The core issue that the consultation needs to address is whether the recovery and resolution framework developed for banking should be extended to insurance and other financial institutions.

EIOPA has consistently highlighted the specificities of insurance, in particular its differing systemic importance and interconnection with the rest of the financial system. This does not mean that a recovery and resolution framework should not be developed for insurance, but it does raise the question of what the objective of such a framework should be. Is the purpose to minimise upset to the stability of the financial system? Or is the purpose to minimise the economic costs to policyholders and the broader economy of a significant insurance failure? These questions and others remain to be answered fully.

On the practical aspects of recovery and resolution, there is little doubt that large complex insurers or insurance groups with extensive cross-border operations would be very challenging to resolve. There is, therefore, scope to consider measures that would make it easier to achieve recovery or resolution for such entities.

EIOPA looks forward to the development of EU policy in this area, which will enable it to complete the framework for dealing with insurance firms "from cradle to grave".

Looking Ahead

EIOPA will continue to refine its approach to crisis prevention, management and resolution. In particular, it will focus on early warning indicators and further integrating micro and macro-prudential supervision. In the near term, the development of a recovery and resolution framework for insurance will be a challenging project that will ask some very searching questions in terms of the rationale for such a framework. EIOPA looks forward to being at the heart of that debate, where it can put forward a coordinated EU insurance supervisory view on how to proceed.

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