

IN BRIEF

# INSURANCE RECOVERY AND RESOLUTION DIRECTIVE (IRRDR)

The EU has put forward an Insurance Recovery and Resolution Directive (IRRDR) to ensure that insurance failures are managed effectively. This legislation aims to establish harmonized recovery and resolution tools and procedures, to ensure that insurers and relevant authorities in the European Union are better prepared for situations of significant financial distress and to facilitate the early and quick intervention of the authorities, especially in cross-border contexts.

## RECOVERY REGULATIONS IN THE INSURANCE SECTOR

Currently, every country has its own rules and practices in the insurance industry, which can create challenges, particularly for insurers operating across borders. This patchwork of national regulations may complicate the orderly resolution of cross-border insurers, and such a situation can lead to legal uncertainties, unequal treatment of policyholders, and potential spillover effects.

The Insurance Recovery and Resolution Directive (IRRDR) establishes tools and mechanisms designed to:

- Reduce the likelihood of an insurance failure and mitigate the impact in case it finally happens.
- Encourage coordination and cooperation among authorities.

The IRRDR complements the regulatory framework for the insurance sector while other topics such as IGS remain on the political agenda.

## 1. OVERVIEW OF IRRDR



A. Preparation and planning



B. Resolution aspects



C. Cooperation and coordination



D. Funding

## 2. CHALLENGES AHEAD



## 3. NEXT STEPS AND TENTATIVE TIMELINE



# 1. OVERVIEW OF IRRD



## A. PREPARATION AND PLANNING

**Pre-emptive recovery plans** are developed in a business-as-usual scenario.

- Supervisors will identify the insurers that are obliged to draw up pre-emptive recovery plans based on several factors, including size, business model, and interconnectedness.
- At least 60% of each Member State market should be subject to pre-emptive recovery planning.
- The pre-emptive recovery plans will be assessed by the supervisory authorities.

**Resolution planning** seeks to prepare for a situation where the company is non-viable, has no prospect to become so and resolution is in the public interest.

- The planning will be managed by the Resolution Authority.
- Insurers will be selected based on certain criteria, taking into account, as a minimum, the necessity to achieve resolution objectives and the undertaking's size, business model, risk profile, interconnectedness, substitutability and in particular its cross-border activity, and ensuring at least 40% coverage of each the Member State.



## B. RESOLUTION ASPECTS

### Objectives of the resolution:

1. Protect the collective interests of policyholders, beneficiaries, and claimants.
2. Maintain financial stability by preventing contagion and ensuring market discipline.
3. Ensure the continuity of critical functions.
4. Protecting public funds by minimizing reliance on extraordinary public financial support.

### Conditions for resolution:

The conditions for resolution are that the insurer is failing or likely to fail, there is no reasonable prospect that any supervisory or private sector measures would prevent the failure within a reasonable timeframe, and resolution is necessary in the public interest.

#### Safeguards

- Independent (or provisional) valuation
- No creditor worse off than in liquidation
- Right of appeal

## TOOLS

### WRITE DOWN AND CONVERSION

- **Write-down:** Reducing the principal amount of capital instruments, debt instruments or other eligible liabilities on the balance sheet.
- **Conversion:** Converting outstanding debts (liabilities) into equity (ownership shares).

Resolution authorities may apply the write-down or conversion tool to meet the resolution objectives for any of the following purposes:

1. Recapitalizing an entity that fulfils the resolution conditions required to apply the solvent run-off tool and maintain its authorization.
2. Converting liabilities to equity or reducing the principal amount of claims that are transferred to a bridge undertaking, or utilized under the asset and liability separation tool, or the sale of business tool.

It is important to note that insurance claims are not exempt from write-downs or conversions; however, this is typically considered a last-resort measure. Additionally, the IRRD includes a list of exceptions and exclusions.

### SOLVENT RUN-OFF

Solvent run-off involves servicing existing policies without writing new business. It is prohibited to underwrite new business and the undertaking is limited to only administering the existing portfolio until its activities are terminated.

## SALE OF BUSINESS

Sale of all or part of the business to a third party/ parties.

The sale of all or part of a business to third parties involves the transfer of ownership. This can include shares or other forms of ownership issued by the business under resolution, as well as any assets, rights, or liabilities associated with that business.

Purchasers must have the appropriate authorization to conduct the business they acquire.

## ASSET AND LIABILITY MANAGEMENT VEHICLE

Impaired or problematic assets and/or liabilities may be transferred to a publicly controlled management vehicle.

- The transfer can include all or any assets, rights, or liabilities of an undertaking that is under resolution. However, there is no possibility of transferring shares or other ownership instruments issued by the undertaking under resolution.
- This management vehicle will be a legal person that is wholly or partially owned by one or more public authorities, which may include the resolution authority, and it will be controlled by the resolution authority.
- The main purpose of this vehicle is to maximize the value of the assets, rights, and liabilities through either the sale of the portfolio or an orderly winding down process.

\*Additionally, the Resolution Authority (RA) have a variety of resolution powers available.

## BRIDGE INSTITUTION

Transfer to a bridge undertaking that temporarily manages assets and liabilities.

- It may involve shares or other ownership instruments issued by an undertaking that is undergoing resolution, as well as any assets, rights, or liabilities from that undertaking.
- The bridge undertaking must be a legal entity that is wholly or partially owned by one or more public authorities. This may include the Resolution Authority (RA) or, where applicable, an Investor Guarantee Scheme (IGS), and it must be controlled by the RA.

The purpose of creating a bridge undertaking is to receive and hold shares, assets, rights, or liabilities. This arrangement aims to achieve the resolution objectives and facilitate the sale of the undertaking.



## C. COOPERATION AND COORDINATION

A **Resolution Committee** will be established within EIOPA to address resolution-related matters. This committee will be composed of resolution authorities from Member States, which must implement structural arrangements to prevent conflicts of interest between supervisory and resolution functions.

The **Resolution Colleges** will be led by the Resolution Authority of the country where the insurer is based. The purpose of this group is to coordinate preparatory and resolution measures among national authorities. EIOPA plays a significant role in promoting the efficient, effective, and consistent functioning of the Resolution Colleges and in fostering convergence among them.



## D. FUNDING

- Each Member State shall establish one or more financing arrangements.
- The home approach must cover at least the no creditor worse-off (NCWO) than in liquidation claims for insurers authorized in that territory and for third-country undertakings established in that State.
- These arrangements may be utilized to cover the costs associated with resolution tools.
- Funding can be obtained either ex-ante, ex-post, or through a combination of both methods.
- Member States may utilize the same administrative structure for their financing arrangements as they do for their Investor Guarantee Schemes (IGS).

## 2. CHALLENGES AHEAD

### EIOPA and NCAs

- Develop 19 new technical standards and guidelines
- Set up the Resolution Committee
- Other additional tasks such as analysing recovery and resolution plans, participating in Resolution Colleges or other administrative tasks.

### Member States and NCAs

- Transpose the IRRD in national law within 24 months
- Set up Resolution Authorities
- New recovery and resolution planning requirements
- Set up Resolution Colleges.

### Insurers

- Draft pre-emptive recovery plans, if within scope
- Support Resolution Authorities in the preparation of resolution plans (including provision of information)
- Remove impediments to resolution.

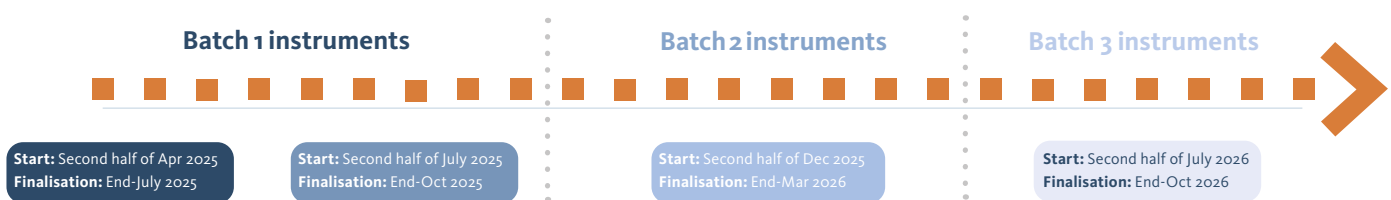
## 3. NEXT STEPS AND TENTATIVE TIMELINE

The primary focus is on developing new instruments, specifically 19 RTS/ITS/guidelines and a framework for a cooperation agreement.

For illustrative purposes, the topics can be categorized into five broad areas: Recovery Planning, Resolution Planning and Resolvability, Valuation, Legal Issues, and Other Operational Topics.

### TENTATIVE TIMELINE

EIOPA has set up the necessary arrangements to develop and deliver the material on time. EIOPA has grouped instruments and will run public consultations on all the instruments.



### Batch 1 instruments (6 instruments)

- RTS on content of pre-emptive recovery plan and remedial action
- RTS on market share for recovery planning
- RTS on contents of the resolution plans (incl. groups)
- Guidelines on the identification of critical functions
- Guidelines on matter and criteria for the assessment of resolvability
- Guidelines on removing impediments to resolvability

### Batch 1 instruments (2 instruments)

- RTS on operational functioning of resolution colleges
- ITS on procedures and information (forms and templates)

### Batch 2 instruments

- Guidelines to specify further scenarios (with ESRB) and the qualitative and quantitative indicators contained in the pre-emptive recovery plans
- Guidelines on how information should be provided in summary or collective form for the purpose of confidentiality requirements
- Guidelines specifying further details on the criteria for application of simplified obligations
- RTS on independence of valuers
- RTS on contents of the contractual term on recognition of resolution stay powers
- RTS, in consultation with ESMA, specifying methodologies and principles on the valuation of liabilities arising from derivatives.

### Batch 3 instruments

- RTS on methodologies for assessing the value of the assets and liabilities of the (re)insurance undertaking in the context of resolution
- RTS on separation of resolution valuation and NCWOL valuation
- RTS on the methodology for assessing the treatment that shareholders, policy holders, beneficiaries, claimants, and other creditors, would have received if the undertaking under resolution had entered insolvency proceedings and the methodology for the estimation of the replacement costs
- RTS on methodology for calculating the buffer for additional losses to be included in provisional valuations