

EIOPA Consultation Paper on the Opinion on the 2020 review of Solvency II

Recovery and Resolution



In October 2019, EIOPA published a consultation paper on its opinion on the Solvency II 2020 review. This briefing note summarises the section of the consultation paper on Recovery and Resolution. EIOPA has requested stakeholders to provide feedback on this consultation paper by 15 January 2020.

Overview

On 11 February 2019, the European Commission (**EC**) issued a formal Call for Advice¹ to the European Insurance and Occupational Pensions Authority (**EIOPA**) on the review of the Solvency II Directive. This relates to the full review of the Solvency II rules required by the end of 2020 (**2020 Review**) as required by the Solvency II Directive.

On 25 June 2019 EIOPA published a first wave of consultation papers on its proposals for the 2020 Review regarding supervisory reporting and public disclosure and Insurance Guarantee Schemes. Milliman has written briefing notes on each of these papers (available [here](#)).

On 15 October 2019 EIOPA issued a second wave of consultation entitled "Consultation Paper on the Opinion on the 2020 review of Solvency II" (the **CP**). This was accompanied by an impact assessment document including an assessment of the combined impact of the proposed changes. The CP is 878 pages long and covers a wide range of topics as follows:

- Long-Term Guarantee (**LTG**) and equity risk measures
- Technical Provisions
- Own funds
- Solvency Capital Requirement (**SCR**)
- Minimum Capital Requirement (**MCR**)
- Reporting and disclosure
- Proportionality
- Group supervision
- Freedom to provide Services (**FoS**) and Freedom of Establishment (**FoE**)
- Macroprudential policy
- Recovery and resolution
- Fit and proper requirements

Milliman has produced a briefing note giving a summary of EIOPA's proposals in the CP (available [here](#)) and separate briefing notes covering each of these topics in more detail. This briefing note covers Recovery and Resolution.

Recovery and Resolution

Following EIOPA's opinion² regarding the need for a harmonised recovery and resolution framework issued in July 2017, it comes as no surprise that EIOPA remains of the view that a minimum harmonised recovery and resolution framework for (re)insurance undertakings should be established and incorporated into Solvency II.

In particular, EIOPA is of the view that Solvency II should be supplemented with a requirement for undertakings to develop and maintain recovery plans in a pre-emptive manner. EIOPA did not specify the precise scope of companies that would be required to produce a recovery plan but recommend that the requirement should capture a very significant share of each national market in the EU³.

In its consultation paper, EIOPA has reiterated the expected contents of a recovery plan, including a strategic analysis of the group or undertaking, a set of possible recovery options to be used across a range of stress scenarios and a communication strategy. Stress scenarios should combine adverse systemic and idiosyncratic conditions and identify the available recovery options and their feasibility in the stressed scenario.

ENTERING RECOVERY

Interestingly, EIOPA has stated its advice that breach of the Solvency Capital Requirement (SCR) be considered the formal criteria for entry into recovery. However, EIOPA proposes an early intervention window, which it considers as the stage of a deterioration in the financial condition of the Company in accordance with Article 136 of the Solvency II Directive⁴. During the early intervention period, EIOPA advises that regulators should have additional powers, such as to require

¹ Formal request to EIOPA for technical advice on the review of the Solvency II Directive.

² [https://eiopa.europa.eu/Publications/Opinions/EIOPA-BoS-17-148_Opinion_on_recovery_and_resolution_for_\(re\)insurers.pdf](https://eiopa.europa.eu/Publications/Opinions/EIOPA-BoS-17-148_Opinion_on_recovery_and_resolution_for_(re)insurers.pdf)

³ Minimum harmonisation entails the definition of a common approach to the fundamental elements of recovery and resolution, while leaving room for Member States to adopt additional measures at the national level.

⁴ Article 136 requires that undertakings have procedures in place to identify deteriorating financial conditions and shall immediately notify the supervisory authorities when such deterioration occurs.

companies to limit variable remuneration and bonuses. In addition, during the early intervention period, EIOPA proposes that companies could be required to implement recovery options set out in the pre-emptive recovery plan within a specific timeframe (or to update the recovery plan if the situation is materially different to that expected in the plan). Therefore, while formal recovery is defined as a breach of the SCR, companies may be required to implement recovery options from their recovery plans (i.e. invoke their recovery plan) before this time. EIOPA does not plan to define a specific threshold for early intervention, which will be subject to judgement of the supervisory authority regarding the definition of deteriorating financial conditions.

SCOPE

EIOPA has specifically addressed its opinion that reinsurance companies should also be in scope of the recovery and resolution requirements. The advice acknowledges the differing nature of reinsurers and insurers, whilst also highlighting the sometimes large and global nature of reinsurers, as well as the potential for concentration of risks.

As in its 2017 Opinion, EIOPA is of the view that resolution authorities⁵ should be required to develop and maintain resolution plans and conduct resolvability assessments in a pre-emptive manner for undertakings. The scope of companies for which the resolution plans will be developed may not necessarily be the same as the scope of companies required to prepare recovery plans.

RESOLUTION POWERS

Given the current situation where numerous Member States are limited to normal insolvency procedures for failing (re)insurers, EIOPA proposes regulators should at a minimum be equipped with the powers shown in figure 1.

Creditors, including policyholders, should not be worse off following implementation of resolution powers than they would have been under normal insolvency procedures.

Both under recovery and resolution, EIOPA refers to the possibility of restructuring, limiting or writing down insurance liabilities and allocating losses to policyholders. For example, companies could be required on a temporary basis during the early intervention period to suspend or limit the right of policyholders to surrender their contracts. Such measures

would need to be justified from the perspective of financial stability and/or policyholder protection. EIOPA proposes that policyholders be informed of the existence of such powers and the possibility that these powers might be exercised in exceptional circumstances, for example through inclusion of a clause in insurance contracts explaining the risks and financial consequences for policyholders. EIOPA has listed a number of additional safeguards which would have to be followed if implementing such measures or allocating losses to policyholders, for example that this must be a last resort.

FIGURE 1: RESOLUTION POWERS



Given the recent EIOPA consultation paper on insurance guarantee schemes⁶, EIOPA has not revisited this topic as part of this 2020 review consultation paper. This topic has been covered in a separate Milliman briefing note⁷.

⁵ According to EIOPA, Member States should have in place a designated administrative resolution authority for insurers to ensure an orderly resolution process as well as to avoid confusion or potential conflict among various authorities. In the Irish banking industry, for example, the Central Bank of Ireland is also the resolution authority.

⁶ <https://eiopa.europa.eu/Pages/News/Consultation-on-Advice-on-the-harmonisation-of-national-insurance-guarantee-schemes.aspx>

⁷ <http://ie.milliman.com/uploadedFiles/insight/2018/EIOPA-Consultation-National-Insurance-Guarantee-Schemes.pdf>



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