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Nordic insurers are strongly against EC's proposal on IRRD

The Nordic insurance industry (Insurance Sweden, Finance Finland, Finance Iceland, Insurance & Pension Denmark and Finance Norway) are strongly against European Commission's (EC's) proposal of Insurance Recovery and Resolution Directive (IRRD). This is an overly burdensome, too extensive, and disproportionate framework for recovery and resolution of (re)insurance companies in the Nordics and the rest of EU/EEA, with no evident benefits for Nordic policyholders nor for the financial stability in the Nordic region. The only consequences for the policyholders of the proposed IRRD will be higher premiums for insurance products and fewer insurance products, risking a reduction in the level of overall insurance protection. Instead of implementing IRRD, the focus should be on creating a more efficient and risk-based supervision within Solvency II, especially of cross-border businesses. As there are great differences between the insurance markets within EU, a large degree of national flexibility to choose the recovery and resolution features that best suit their market should be allowed if IRRD or a similar framework is introduced. There should, therefore, be no requirements of national market coverage for recovery and resolution planning. The fact that some Member states have imposed a similar framework is not a valid argument for IRRD in itself as there are great differences between the insurance markets within EU/EEA that might justify the differences in the national approach between member states.

No need of IRRD from a Nordic perspective

Insurers have limited, if any, impact on the financial stability

EC's proposed IRRD seems to be based on a belief that insurance companies have a significant impact on financial stability. We think this is a misconception. In our view, the rationale behind any recovery and resolution framework is the need to prevent and handle a situation where a disorderly failure of an institution would have an impact on financial stability, and where the prudential rules have been deemed insufficient to deal with the situation. A recovery and resolution framework should therefore be seen as a "regulation of last resort".

Nordic and other EU insurance companies played no part in the global financial crises 2008 – 2009 and the European insurance sector have exhibited resilience during the COVID-19 pandemic crisis. This can also be seen in EIOPA's recent stress test that indicates that the sector even under a severe scenario proves to be able to meet its' promises to the policyholders. Furthermore, insurers' MCR-ratios in the Nordic countries are much higher than the required 100 per cent.[1] This shows the strength and resilience of the Nordic insurance companies.

Insurers rather contribute to stability of the financial system

Failures of insurance companies and groups are very rare and, given the general lack of interconnectedness among insurers, such failures do not affect other insurers, the payment system or other parts of the financial system. Thereby, in contrast to banks there are very limited, if any, financial stability risks of failing insurers. It is rather the opposite since the insurance companies have supported the financial system and the society during e.g. the global financial crises and during the COVID-19 pandemic.

With stable governance, responsibility and long-term perspective, Nordic insurance companies have been a stabilizing factor during these turbulent periods. At the same time, the companies have ensured that Nordic policyholders have access to good insurance policies. Should an insurer fail, there is also no evidence of a lack of substitutability of products that would justify the introduction of the proposed IRRD in the Nordics.

[1] According to EIOPA's Insurance statistics the average MCR-ratio by the end of 2021 was for Danish insurers 669 per cent, for Finnish 776 per cent, for Norwegian 507, and for Swedish 906 per cent.

IRRD neglects the fundamental differences between insurance and banking

It is problematic that IRRD in large parts is merely a copy of BRRD where the fundamental differences between banks and insurance companies have not been considered, for example in respect of systemic risks they impose, the risks for the financial stability in the event of failure of an institution, insurers' low liquidity risk, and the long-tailed nature of insurance claims. That IRRD is to a very large extent a copy of BRRD will lead to unnecessary cost and operational burden for the insurance companies, without any benefits in the Nordics for the financial stability or for the society as a whole. Thus, even if recovery and resolution frameworks have been introduced for the banks and central counterparties (CCPs) it does not mean that such a framework is appropriate for the insurance sector.

There are more efficient ways to improve policyholder protection than IRRD

One of the stated reasons for the IRRD by EC is the need to increase policyholder protection within EU. However, policyholder protection is the very purpose of prudential regulation and the current level of protection offered by Solvency II and national insolvency law already provides sufficient safeguards for Nordic policyholders (prudential rules, rules on winding-up and right of priority). The introduction of Solvency II as well as other new legislations such as IDD have significantly improved policyholder protection. The 2018 review of Solvency II, e.g. through new LAC DT requirements, have introduced even stricter regulatory requirements. That will also probably be the outcome of the current review of the Solvency II Directive, which includes EC's proposal to introduce macroprudential tools also for insurance.

Good internal governance and control, appropriate capital requirements and effective supervision are much more important to good policyholder protection than harmonization of recovery and resolution within EU. In fact, if these elements are in place, the need for a recovery and resolution framework is, if any, limited. Thus, risk-based and efficient supervision (especially cross-border) would be the most efficient way to improve policyholder protection.

Rather than implementing IRRD, existing tools and powers should be fully used and resources adequately assigned towards a proper enforcement of Solvency II. Many Nordic insurers already include many of the elements of EC's proposal of pre-emptive recovery plans in their Own Risk and Solvency Assessment (ORSA), including remedial actions if the financial position deteriorate. It could, therefore, be considered to incorporate in Solvency II that some parts of the recovery planning proposed in IRRD could be in the ORSA. Thereby, large (unnecessary) costs and other negative consequences of IRRD for the Nordic insurance market, that will in the end have negative implications for Nordic policyholders, will be to a large extent avoided.

EC also states problems with policyholder protection when insurance companies operate cross-border as a motive for IRRD (see e.g. recital (6)). Rather than implementing IRRD existing supervisory measures could be used to examine characteristics of cross-border business that give rise to excessive risks. Main risk factors indicating future problems of cross-border business usually include fast growth, considerably low prices, unusual terms and a narrow range of products. In addition, there are efficient solutions how to tackle those problems at a much earlier stage, for example by strengthening the Colleges of Supervisors.

IRRD may lead to weakened insurance protection for Nordic households and companies

The costs of IRRD, especially the costs for more administration for pre-emptive recovery and resolution plans, will in the end lead to higher premiums for insurance products. Higher premiums could make financially vulnerable households less inclined to buy insurance policies. In this sense, the proposed IRRD could reduce the overall level of insurance protection in the society, which in the end could imply higher costs for the government.

The requirement of resolvability in IRRD may also make insurers not able to offer certain insurance products , for example, becauseit will be unclear how the resolution authority will treat these products in their assessment of resolvability. Thus, this could have a negative impact for those companies and other policyholders that demand or need those insurance products. We also think there are great unclearity in EC's proposal on how policy holders in mutual and other insurance companies will be treated in the case of resolution. Therefore, we believe IRRD will rather result in weakened policyholder protection and not increased as EC claim.

Need for a more thorough and extensive impact assessment

EC's impact assessment on IRRD is in our view not accurate and sufficient.[2] The IRRD imposes significant administrative burdens and costs on the national competent authorities and the industry. The consequential costs imposed will necessarily and eventually be passed on to the policy holders. We, therefore, don't agree with EC's impact assessment, for example that IRRD is cost effective and has positive implications for the financial stability. Furthermore, Nordic insurers are already aware of and prepared for adverse situations from their ORSA etc. Thus, IRRD will not change how insurers "take informed and timely remedial actions when needed" as the EC impact assessment claim will weigh up the administrative costs of IRRD.

In addition, EC's impact assessment does not take into consideration how the preventive measures that entered into force with Solvency II affects the risks of failures in the insurance sector. We would, therefore, have found it appropriate that analysis was performed in the impact assessment of the bankruptcies in the European insurance sector since Solvency II entered into force 2016 and of how or to which extent the suggested measurers in IRRD could have prevented these bankruptcies or mitigated their effects.

Large differences between EEA insurance markets calls for large degree of national flexibility

There are important differences between EEA Member states and insurance markets within EEA regarding, e.g. the social welfare system, type of insurance companies (mutuals etc.), insurance products lines and the extent to which insurance companies provide critical functions. These differences can to a large extent explain why the winding-up process, i.e. resolution, for insurers differ. The many differences probably explain to a large extent why some Member states have already imposed a framework similar to EC's IRRD proposal and some have not. That some Member states already have a national recovery and resolution framework is, therefore, not a valid argument to implement IRRD. In addition, these national differences call for a large degree of national flexibility when it comes to implementing a "regulation of last resort" in the form of a possible recovery and resolution framework, i.e. IRRD.

The negative consequences arise as IRRD for example gives national authorities far-reaching, intrusive, and arbitrary powers, especially the alternative measures in article 15. These measures include that the undertaking must divest specific assets or restructure liabilities, restrict or prevent the development of new or existing business lines as well as the sale of new or existing products. Another example is requirements to change legal or operational structures of the undertaking, which could imply large costs and other negative consequences. The resolution authority can require these measures also in situations where the undertaking have a very strong financial position and there is no material risk of economic failure. It could therefore be questioned if IRRD is proportional and how it will benefit e.g. policyholders.

If IRRD were to be introduced each country should therefore be allowed large degree of flexibility to choose the recovery and resolution features that best suit their market. Only with sufficient national flexibility can IRRD be proportionate. In addition, it should not go beyond international standards originating from the International Association of Insurance Supervisors (IAIS). Thus, there should no goldplating of these standards in order to not detriment the competitiveness of European insurers.

No requirement for national market coverage for recovery and resolution planning

One example on the need to have a national flexibility if IRRD were to be introduced is the proposed scope of the requirement of pre-emptive recovery and resolution plans. We strongly oppose having any requirement of national market coverage for pre-emptive recovery and resolution plans. Some of the Nordic non-life companies that would be in the scope with EC's proposed market coverage are small, with gross written premiums just around 100 million €. Given the costs and operational burden for the insurers of pre-emptive recovery and resolution plans it is not proportionate to have such scope for these requirements. Furthermore, insurance groups should not automatically and by default be in the scope for pre-emptive recovery and resolution planning as they are in EC's proposed IRRD.

[2] See Commission staff working document impact assessment report (SWD(2021) 260 final).

Any requirement of pre-emptive recovery and resolution plans shall only apply for those undertakings and insurance groups that provide critical functions and be based on the risk profile, complexity including cross-border activity, level of interconnectedness, substitutability, and potential impact on financial stability of a failure of the undertaking or group. The relevant national supervisory authority should make assessments of the need for pre-emptive recovery plans based only on a joint consideration of these criteria.

If sufficient national flexibility is not introduced for the scope of companies obliged to draw up pre-emptive plans, at least it should be a very large national flexibility in how to implement such simplified obligations in IRRD. However, we don't consider this as an alternative that can make the requirements fully proportionate, mainly due to large uncertainty how the simplified obligations will be applied by each country.

IRRD neglects a large part of the insurance market, namely mutual insurance companies

Many Nordic and other EU insurers are mutual insurance undertakings and have no external owners, i.e. shareholders. Thus, for mutuals there are no shareholders that can bear first losses, only policyholders. This is also true for other legal forms of undertakings without shareholders. That imply, for example, that actions under resolution that require sale of shares or converting debt to equity are not possible to apply on a mutual insurance company.

The requirements and especially the resolution tools in IRRD are not suitable for mutual insurance undertakings. One of the resolution objectives is to protect policyholders, beneficiaries and claimants. We strongly question how policyholders in a mutual insurance undertaking would in EC's proposal be protected in a resolution. Furthermore, when resolution authorities assess the resolvability of mutual insurance undertakings, they have to respect the characteristics of the legal form of the company and should not be able to demand any kind of demutualisation.

Treatment of group companies need clarification, especially in regards of BRRD

We agree that a group perspective should be applied in IRRD if IRRD were to be introduced. However, it is not clear in the proposed directive if and how to apply resolution tools and powers to other group companies, that are not insurance companies or holding companies, whether regulated or not. The same goes for the resolution authorities' resolvability assessments and resolution planning.

EC's proposal of IRRD does not consider the fact that several Nordic and other European insurance companies are part of financial conglomerates or other company groups that also include banks. In accordance with BRRD, i.e. banks' equivalent to IRRD, these banks have to draw up recovery plans and the resolution authority has to draw up resolution plans. BRRD also stipulates how a resolution of these banks would be conducted.

Many of the insurance companies that are part of the same group as a bank would according to EC's proposed IRRD also have to draw up recovery plans and the resolution authority would also have to draw up resolution plans for the insurance company. Thus, these financial conglomerates and similar business groups will need to have two different recovery plans within the group and the resolution authority will need to establish two different resolution plans, for each part of the group.

We think there are several different issues and possible conflicts between the regulations that must be sorted out regarding how IRRD would work in relation to BRRD before any decision on IRRD can be made. For example, it should be possible for financial conglomarets and other company groups that are under both BRRD and IRRD to just have one recovery and resolution plan including both banking and insurance. Otherwise, there will be unnecessary costs and other negative consequences for these groups that includes both banks and insurers. This will in the end also have negative effects for policyholders of Nordic and other European insurance companies