

## Insurance Europe response to EIOPA IRRD consultation on Guidelines on criteria for the identification of critical functions

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### General comments

**Q1.** *Do you have general comments on the consultation document?*

Insurance Europe welcomes the opportunity to provide comments to the consultation on guidelines on the criteria to identify critical functions. The industry **welcomes that the methodology for National Resolution Authorities (NRAs) to identify critical functions for their respective insurance markets in the proposed guidelines is high level with national discretion and flexibility.**

This discretion and flexibility are needed to cater to national features and differences such as the role of insurance in society and financial markets. Industry strongly agrees that what is classified as a critical function in one Member State should not by default be classified as a critical function in other Member States. It is **also important that the guidelines allow NRAs the discretion to conclude that there are no critical functions** performed by insurers in their market, based on the characteristics of the national insurance sector.

Article 2(25) of the Directive defines critical functions as insurance activities, services or operations whose default would likely have a significant impact on the financial system, the well-being of a large number of policyholders or lead to a loss of general confidence. Having this in mind, the industry expects that only a few central activities of insurance undertakings need to be covered in order to fulfil the purpose of Article 2(25) of the Directive.

Industry is concerned that the proposed requirement to consider all functions provided to a third party implies that contrary to the above assessment that **very few of an insurer's activities will be excluded from the scope** of potential critical functions. In this context, the industry notes that the draft Guidelines appear to go beyond the mandate provided in Article 9(9) of the Insurance Recovery and Resolution Directive (IRRD), which foresees the specification of clear criteria for the identification of critical functions. By potentially including any function provided to third parties, the Guidelines risk creating uncertainty about the intended scope. As such, industry supports more clarity in the Guidelines and closer relation to Article 2(25) of the IRRD.

Industry agrees that it is **appropriate to consider the extent to which changes in third-party contracts, backup plans, and product mix adjustments could reduce vulnerabilities**. The emphasis on partial cessation or substitution is also very relevant and should therefore be addressed in more detail.

The assessment of critical functions should be carried out at the level of the individual undertaking. References to market-wide impact should be interpreted with caution, to avoid overstating the systemic relevance of a single entity. The Guidelines should clarify this to ensure a proportionate and objective approach. At the same time, the Guidelines should acknowledge that certain market-wide considerations may be relevant when determining the criticality of a function, particularly in relation to broader financial stability. This is in line with the Financial Stability Board's Recovery and Resolution Planning Guidance, which highlights that criticality is often linked to systemic relevance, including factors such as size and market share. While this concept originates from the banking sector, the underlying principle is also relevant for insurance. Therefore, while the primary assessment should remain at undertaking level, the Guidelines could clarify that market-wide factors can provide useful context when evaluating whether the failure of a function at entity level could have wider implications. While industry recognises that the concept of "important and critical functions" under the Digital Operational Resilience Act (DORA) is distinct from "critical functions" under the IRRD — with different objectives and scopes — it would be helpful for the Guidelines to clearly state that no equivalence is intended between the two frameworks. This would avoid confusion and ensure that resolution planning under IRRD remains focused on functions whose discontinuation would have a systemic impact at market level, and not inadvertently extend to all ICT-related or operational functions defined under DORA. Moreover, the Recital 70 of DORA mentions a Bank Recovery and Resolution Directive (BRRD) definition of critical functions, which raises questions around the consistency between the two frameworks.

The **impact assessment contains no quantitative cost assessment**. Without understanding the impact of regulations, it is very difficult to successfully reduce their burden, in line with the Commission's simplification agenda to reduce operational and reporting burdens on firms.

In general, the **Guideline should refer to "parents" rather than "ultimate parents"** as entities that are not subject to the SII framework as stated in the Level 1 text should not be in scope of Level 2 and 3.

## Guidelines

### Q3a. Do you have comments on Section 'Introduction'?

Para 1.3: The Financial Stability Board (FSB) 2023 paper "Identification of Critical Functions of Insurers" does not identify reinsurance as a critical function for insurers. In particular, section 3.2.6 of this paper specifies that none of the case studies evaluated assessed reinsurance as a critical function. Industry suggests that this paragraph is reworded to reflect this.

In addition, Insurance Europe recommends adding the following paragraph to acknowledge the specificities of the reinsurance business model based on the diversification of cross-border geographies and business lines:

*"When assessing whether a reinsurance undertaking carries critical functions, the national competent authorities should give due consideration to the fact that reinsurance is a business-to-business activity between highly skilled reinsurance professionals, including reinsurance brokers. Consequently, the reinsurance activity has no direct implications for retail policyholders."*

*Furthermore, national competent authorities should give due consideration to the fact that the reinsurance business model is inherently cross-border."*

*The diversification of risks achieved through such cross-border operations is a fundamental component of the reinsurance value proposition, enhancing both its efficiency and resilience. In this context, the cross-border activity of reinsurance undertakings should not be misunderstood as an indicator of heightened risk."*

**Q3b.** Do you have comments on Guideline 1 – Scope of potential critical functions?

**Guideline (GL) 1 covers an extensive set of activities to be deemed critical.** In particular, the resolution authority's need to consider all functions provided to a third party implies that very few of an insurer's activities will be excluded from the scope of potential critical functions. This approach seems to be at odds with the underlying principle of the Directive which is to address failure situations, which requires to develop a more specific and tailored approach in the identification of critical functions, to avoid identifying the entirety of an insurer's activities as critical functions.

Industry proposes that the Guidelines should relate more closely to the text of Article 2(25) of the Directive and respecting the principle of proportionality. It should be made clear in the Guideline that **all the criteria stated in the Directive's definition must be met in order for a function to be considered critical. Resolution authorities should focus on the impact that a discontinuation of the function and inability to replace it would cause** and if the function *"cannot be substituted easily within a reasonable timeframe, or at a reasonable cost for policy holders"*.

Para 1.13: Industry **does not support the inclusion of investing in and lending to the real economy**, as well as non-insurance-specific activities such as repo transactions, securities lending and the pooling of risks, as potentially critical functions. This is in line with the case studies in the FSB practices paper (2023): *"Critical functions in relation to investment and lending to the real economy and to acting as a counterparty in derivatives, repo and securities lending markets appear to be of less relevance or seem to be limited to the Chinese example."* Critical functions of insurers should be limited to (re)insurance activities.

**While (re)insurers do play an important role as institutional investors, these activities are not considered a critical function within the meaning of Article 2(25) of the IRRD.** Designating it as such would imply that its continuity must be supported through resolution tools such as bail-in. It is also unclear how their resolvability could be assessed ex ante in a meaningful way.

Furthermore, such investment and financing activities are carried out for the undertaking's own account and balance sheet, in order to meet (re)insurance obligations. As such, they do not meet the definition of a critical function under Article 2(25), which refers to functions performed for third parties.

Given the atomicity of financial markets, it is difficult to imagine investment activities of an insurer qualifying as critical. Existing safeguards — such as concentration risk frameworks and liquidity management tools (e.g. targets on low market footprints to mitigate fire sale risks)— already mitigate systemic risks. Therefore, the Regulation could clarify that such assessments are only required if there is a strong presumption that specific investments could be critical.

Finally, designating investment or lending roles as critical functions risks distorting competition with other institutional investors that are not subject to resolution planning, thereby undermining the level playing field.

**Industry does not support the classification of reinsurance as a non-insurance function in this guideline.** Para 1.13 rewrites the FSB list of the types of economic function of insurance, including a reference to reinsurance, each time there is a reference to insurance (e.g., "Insurance / reinsurance coverage as a precondition for individuals to go about their daily lives; Insurance / reinsurance payments that are vital to individuals' financial security").

Reinsurance is a Business-to-Business activity which does not provide direct coverage to individual customers. **Applying criteria designed for primary insurers may overstate the systemic relevance of certain reinsurance functions.** Instead, resolution authorities should take account of the specificities of the reinsurance model, which enhances market resilience rather than posing contagion risks. Therefore, the wording of the FSB's Practices paper should be reflected in Para 1.13.

**Q3c.** *Do you have comments on Guideline 2 – Geographical Level?*

Industry does not support that the impact assessment on the effects of discontinuation/non-substitutability must be carried out separately for each Member State. A requirement to assess impact separately for each Member State may result in artificial fragmentation of otherwise integrated markets, particularly for cross-border or group-level undertakings. A flexible, proportionate approach is needed.

The industry suggests the term 'Significant impact' and the following paragraphs which are rather vague and risk heterogeneous interpretation by the NSAs.

**Q3d.** *Do you have comments on Guideline 3 - Consideration of an insurance guarantee scheme, measures under normal insolvency proceedings, and use of public funds in the identification of critical functions?*

Industry would appreciate further clarity on why insurance guarantee schemes should not be considered when the authority makes an assessment of the criticality. Guarantee schemes differ from Member State to Member State, but that is why they should be taken into account when determining the critical functions in each Member State.

**Q3e.** *Do you have comments on Guideline 4 - Inability to provide the function?*

The proposal to "use the assumption that these activities and operations cease completely and that the services are no longer provided" is not in line with the impact assessment. The assumption should be a partial stop, for the same reasons (see comments on Q5).

The assessment is made at the level of an individual insurance undertaking. For example, the inability of one insurer to underwrite new business for certain risks may not be critical if other undertakings in the market continue to offer coverage for those same risks. This should be made clear by inserting the following clarification: "1.18. When assessing whether the inability of the insurance or reinsurance undertaking to provide a function that consists of certain activities, services or operations results in a significant impact, the resolution authority should use the assumption that these activities and operations cease completely and that the services are no longer provided **at the level of this undertaking**".

**Q3h.** *Do you have comments on Guideline 7 - Impact resulting from effects on the social welfare of a large number of policy holders and from the systemic disruption in the provision of insurance services?*

The assessment is made at the level of the individual insurance undertaking, which should be made very clear. The following amendment to the wording is suggested:

"1.25. When assessing whether there are functions for which the inability of the individual insurance or reinsurance undertaking to provide them is likely to have a significant impact on the real economy or the financial system resulting from the systemic disruption of insurance services the resolution authority should consider, *inter alia*, functions where the inability to provide them **at the level of this individual undertaking** creates a risk to the financial stability, in particular resulting from the systemic relevance of the insurance or reinsurance undertaking that provides the function, according to the criteria in point 1.18(a)."

**Q3i.** Do you have comments on Guideline 8 - Loss of general confidence in the provision of insurance services?

It should be clarified whether the focus of paragraph 1.27(b) is on the actual availability of insurance coverage or on the loss of confidence in its availability. When assessing whether the inability of an individual insurance undertaking to provide certain functions is likely to have significant impact on the real economy or financial system due to a general loss of confidence in the provision of financial services, caution is needed. **This assessment should be made at the level of the individual undertaking, rather than assuming market-wide stress.** The risk of a loss of confidence "for the whole market or for one or more segments", and its potential, should be assessed based on objective criteria, as **the failure of a single undertaking is unlikely to trigger such widespread and major consequences.** This assessment is backed by the fact that the historical insurance failures have not led to significant insurance runs on other insurance companies. The Regulation could be amended to highlight that this analysis should only be performed if there is a strong presumption that the failure of a specific activity would lead to a general loss of confidence.

**Q3i.** Do you have comments on Guideline 11 - Factors to consider when assessing the substitutability of a function within a reasonable time and at a reasonable cost?

The industry fully supports the fact that the substitutability assessment is based on multiple factors and should not be solely based on the market share. Because the list of potential critical functions is very extensive, a more in-depth analysis based on empirical data and case by case review will be needed.

## Annex: Impact assessment

**Q5.** Do you have comments on Policy Issue A: assumptions used for the assessment of the impact of the inability to provide a function?

The impact assessment is based on a purely qualitative assessment performed by EIOPA. A quantitative cost-benefit analysis would allow stakeholders and policymakers to better assess the regulatory burden of the proposed Guidelines, in line with the European Commission's simplification agenda.

In practice, this assessment consists of comparing two policy options. The assumption of a partial rather than a complete stop of the function, recognising that there may be ways to partially continue the function, is realistic. However, this assessment cannot be considered as a full-fledged assessment of impact of the proposed Guideline on criteria for the identification of critical functions.

In addition, in Guideline 4 on specific requirements for the assessment of the likelihood of a significant impact on the financial system or the real economy, the "resolution authority should use the assumption that these activities and operations cease completely and that the services are no longer provided" which is not in line with the impact assessment. Here also, the assumption should be a partial stop, for the same reasons.

## Any other comments

**Q6.** *Do you have any other comments?*

The explanatory text presents a “non-exhaustive list of potential functions”, intended to “serve as a reference for resolution authorities when deciding whether an insurance or reinsurance undertaking provides a critical function”. This list comprises almost every (re)insurance activities and therefore serves limited purpose and should be removed from the Guideline. For instance, this list includes, as far as reinsurance is concerned, “(3) Lines of business and products related to Reinsurance, such as: Facultative or treaty reinsurance / Financial (re)insurance (Insurance of settlements between counterparties)”. Facultative or Treaty reinsurance are types of reinsurance, not products or lines of business. Such an expansive list risks blurring the distinction between ordinary business functions and genuinely critical ones. **A non-exhaustive list should support—not replace—a case-by-case assessment grounded in the Directive’s definition.**

Some groups with BRRD experience raise timing concerns regarding the identification of critical functions under IRRD. Insurance companies and groups are proposed to identify critical functions as part of the **pre-emptive recovery plan, in fact this should not be the case as critical functions must not be part of the PRP** (please refer to our consultation response on content of pre-emptive recovery planning). However, this identification would only challenged later by the NRA in the context of the **resolution plan**. As a result, in the first recovery plan cycle, the identification of critical functions will remain unchallenged.

Insurance Europe therefore asks for **clear guidance from EIOPA and NRAs** on the timing, process, and objectives of identifying critical functions under IRRD.

Insurance Europe is the European insurance and reinsurance federation. Through its 39 member bodies — the national insurance associations — it represents insurance and reinsurance undertakings that account for around 95% of total European premium income.