

Final - Guidelines to specify further the qualitative and quantitative indicators in pre-emptive recovery planning

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General Comments

Q1. Do you have general comments on the consultation paper?

- Insurance Europe welcomes the opportunity to engage in discussion and provide feedback on these draft Guidelines, both here in writing and via the series of webinars EIOPA has hosted. We look forward to continuing to support EIOPA's work as the implementation of the IRRD progresses, with the aim of ensuring the objectives of stronger policyholder protection and enhanced financial system stability are met in a proportionate and streamlined manner for supervisors, resolution authorities and (re)insurance undertakings.
- The implementation of indicators within the recovery plan is in addition to the comprehensive risk appetite framework already in place under Solvency II. The proposed guidelines should explicitly take into account that insurers already have ERM systems in place, including sophisticated monitoring systems. While reference is made to this in Paragraph 1.4, this fact should underly the guidelines throughout. Most often, existing KPIs can be used and only the thresholds have to be adapted to the purpose of the IRRD.
- We believe it is appropriate to limit the framework to targeted indicators—fewer than those used in the risk appetite framework—but capable of flagging major crisis situations that could ultimately lead to the undertaking being designated as failing or likely to fail (e.g. liquidity and solvency indicators). Introducing too many additional indicators will increase the administrative burden, add unwarranted noise to the identification framework and make data analysis more complex. EIOPA should recognize that the IRRD provides **flexibility in the choice and number of indicators**, and the Guidelines should not goldplate the Directive.

- Most of the indicators other than those related to liquidity and capital, such as profitability, asset quality, market conditions and macroeconomic indicators are neither forward looking nor reliable. Indicators that cannot forecast a market correction reliably are not relevant for assessing an entity's viability. One would not expect the activation of a recovery or resolution plan to be solely triggered by changes in market conditions or macroeconomic indicators.
- The guidelines should distinguish between early warning indicators (EWIs) and recovery triggers. EWIs will alert and direct attention to a potentially developing adverse situation but would not require the immediate execution of countermeasures. Recovery triggers would indicate a more imminent adverse situation and would require strong consideration of countermeasures. Many of the examples stated in the guideline (e.g. market condition and macro-economic indicators) would serve well as an EWI. Capital indicators (e.g. SII ratio) are better suited as recovery triggers. Recovery triggers could also be applied in a staged approach with each level requiring stronger management reaction (the SCR could serve as final level requiring immediate and sizeable remedial actions). As such, only the indicators **that are directly linked to the company's viability (e.g. liquidity, solvency) should remain and be used as recovery triggers.**
- Where indicators are used, it is crucial that they are **aligned to existing risk monitoring and reporting.** In particular, to avoid duplication of work it should be clearly stated in the guidelines that analyses and assessments already in place in the existing ORSA, liquidity risk management and stress testing processes can be reused for the indicators in the pre-emptive recovery plan.

Consultation paper overview and next steps

Q2. *Do you have comments on the section 'Consultation paper overview and next steps'?*

Draft Guidelines to specify further the qualitative and quantitative indicators in pre-emptive recovery planning

Q3a. *Do you have comments on the Introduction?*

- The linkage to governance and consistency with internal risk management frameworks appropriately reflects IRRD principles. However, the wide range of indicators envisaged goes beyond minimum harmonisation. When supervising insurance groups, a broadly consistent and coordinated application of these Guidelines across Member States is beneficial. Alignment in supervisory practices regarding the indicators can support legal certainty, help reduce unnecessary divergences, and contribute to effective and efficient supervision within the Member States. However, flexibility across Member States in the application of these Guidelines is also necessary to reflect differences between the insurance markets within the EU.

Q3b. *Do you have comments on Guideline 1 – Requirements for the calibration of recovery plan indicators?*

- **Paragraphs 1.9-1.11:** Early-warning calibration expectations extend the IRRD by prescribing indicator sensitivity and timing. Supervisory acceptance of undertaking-specific approaches is essential.

Q3c. Do you have comments on Guideline 2 – Capital indicators?

- **Paragraphs 1.12 – 1.14:** The mandatory inclusion of SCR breach indicators aligns with IRRD. However, layering multiple capital metrics may add limited value. As Solvency II and IRRD apply to the same entities, the relevant capital indicator is the SII capital ratio. This is by design forward looking, and reflects quality and quantity of own funds. Using the MCR as an indicator is unnecessary as a breach of the SCR already requires immediate countermeasures and a separate (i.e. not pre-emptive) recovery plan under SII. In addition, transitional measures add complexity to the design of the indicators
- **Paragraph 1.12:** “significant” should be changed to “material”.

Q3d. Do you have comments on Guideline 3 – Liquidity indicators?

- **Guideline 3:** It needs to be noted that the liquidity position and liquidity risk in insurance - unlike in banks - is often managed on entity or even portfolio level. A group view is thus often not available and not meaningful. Flexibility regarding individual approaches to liquidity indicators is therefore essential. It should also be clarified that indicators referring to long-term liquidity and funding needs are only required for those undertakings/groups that have a long-term risk management plan in accordance with Article 144a 2. in 2009/138/EC.
- **Guideline 3:** We welcome that the long-term liquidity plans are only required “where relevant”. However, it should be clear that this “relevance” is referring to the fact that long-term liquidity and funding indicators are only required for undertakings and groups that have a long-term risk management plan in accordance with Article 144a(2) of Directive 2009/138/EC.
- **Paragraphs 1.15 – 1.19:** Liquidity indicators significantly deepen IRRD requirements. Alignment with liquidity risk management plans is welcome. However, data availability and stress calibration challenges remain. Simplified liquidity proxies should be permitted.
- **Paragraph 1.15:** “material” should be added, i.e. “actual *material* deterioration”. The indicators are only relevant for material changes, not all.
- **Paragraph 1.18:** EIOPA refers to “Article 1(3) of Commission Delegated Regulation (EU) No xyz/xyz on liquidity risk management plans”. However, the draft RTS submitted to the EC does not have an article 1(3). It is assumed that EIOPA wishes to refer to art. 7(1) of the RTS.
- **Paragraph 1.19:** In the RTS on LRMPs EIOPA writes: “The common indicator, relying on the ratio between liquid assets and (stressed) liquidity needs, was relinquished, while the added condition for undertakings’ own liquidity risk indicators is specified in general terms of “liquidity resources and needs”” For consistency between the RTS on LRMPs and these guidelines, Insurance Europe proposes to delete the words “and could include the liquid assets ratio (% Total assets).”.

Q3e. Do you have comments on Guideline 4 – Asset quality indicators?

- **Paragraphs 1.20– 1.22:** Asset quality indicators may overlap with existing risk monitoring. Asset quality indicators are not forward-looking (e.g AAA ratings for subprime products), are already embedded in the solvency ratio and will add significant noise to the identification framework. As this indicator seems to be replicated from the BRRD approach, one should highlight that the financial sustainability of a credit institution is significantly influenced by the share of Non-Profitable Loans (NPL) or likewise, by the amount of bucket 2/bucket 3 IFRS9 provisions. Such influence does not apply to insurance companies. Therefore, to reflect appropriately the business model of insurance companies, indicators relative to asset quality should remain optional.
- **Paragraph 1.20:** “material” should be added, i.e. “future *material* asset”. The indicators are only relevant for material changes, not all.

Q3f. Do you have comments on Guideline 5 – Profitability indicators?

- **Paragraphs 1.23-1.28:** This guideline seems overly detailed and in essence only states part of what an insurer's ERM system already does. It therefore significantly interferes with the business-as-usual (risk) management, controlling and reporting. Indicators under the IRRD should relate to significant adverse developments. The framework of indicators required under the IRRD does not exist in isolation and additions to the regular KPIs under the ERM system should only be requested when necessary and meaningful. Most often, existing KPIs can be used and only the thresholds have to be adapted to the purpose of the IRRD.
- **Profitability** needs to be looked at with a long-term horizon. In particular:
 - profitability may be seasonal and fluctuates in line with insurers' business models. For example, natural disasters do not occur every year, but when they do, they have a significant impact on profitability, and
 - Market risks are generally reflected in the economic balance sheet before feeding into profitability.
- As profitability indicators are already embedded into Solvency II through the ORSA process, requiring additional or specific profitability metrics for the recovery plan leads to unnecessary and irrelevant burden, The range of suggested metrics risks over-specification. Undertakings should retain discretion to focus on key drivers. For instance, a negative outlook on profitability is not a direct survival threat to an insurer if it holds sufficient capital to sustain the negative trend. This rationale can be backed by the fact that the Article 138 of Solvency 294 does not put a significant emphasize on the profitability forecasts but rather focuses on the ability of the insurer to rebuild its short-term capital position. Focusing on profitability in the context of a pre-emptive recovery plan will add a going concern component that is not relevant with the ultimate target, which is avoiding the prospect of failure. Therefore, the monitoring of such indicators should be optional instead of mandatory and so we propose deleting the section regarding profitability, since it holds a significant overlap with the liquidity and solvency indicators..
- **Paragraph 1.23:** "material" should be added, i.e. "actual *material* deterioration". The indicators are only relevant for material changes, not all.
- **Paragraph 1.25:** Measuring the "deterioration of the adequacy of technical provisions" is not meaningful under Solvency II. The value of technical provisions is based on the best estimate of liabilities and is thus by definition always adequate for the respective liabilities. Observing the impact of changes in valuation assumptions on the technical provisions is more useful, but the guidelines should not prescribe too many possible drivers so undertakings can focus on those factors most material to their business. Undertakings should retain discretion to focus on key drivers.

Q3g. Do you have comments on Guideline 6 – Market conditions indicators?

- **Paragraphs 1.29-1.30:** Market-based indicators can provide useful external signals but should already be reflected in the capital and liquidity metrics. For instance, as highlighted by the Merton Credit risk model, CDS protections will be significantly influenced by the solvency headroom. Moreover, the suggested indicators may be volatile and outside management control. Their role as supplementary rather than primary triggers should be clarified.
- **Paragraph 1.29:** "material" should be added, i.e. "the *material* decline". The indicators are only relevant for material changes, not all.

Q3h. Do you have comments on Guideline 7 – Macro-economic conditions indicators?

- **Paragraphs 1.31-1.34:** Macroeconomic indicators extend IRRD by linking external variables to recovery triggers. This guideline in essence only states what is anyway monitored by an insurer's ERM system. It is therefore unnecessary.
- Macro-economic indicators are not forward-looking (e.g. GDP forecasts will fail to identify an inversion of the market cycle), and are not directly linked to insurers' risk of failure (e.g. changes in unemployment rates are extremely tenuously related to insurer failure, if they are linked at all).
- To the extent these indicators seem to be replicated from the BRRD approach, they may not be as relevant for insurers that usually have a more diverse risk profile split across multiple risks (P&C/Life/Market/ Operational) and have a lesser sensitivity to metrics such as GDP¹.
- These indicators should primarily serve as contextual alerts, and macroeconomic conditions should be viewed as a channel through which risks are transmitted to solvency and liquidity indicators. Automatic escalation should not be expected and these indicators should be considered as part of the scenarios.
- The reference to geographical and sectoral concentrations requires clarification.
- **Paragraph 1.31:** "material" should be added, i.e. "identify *material* deterioration". The indicators are only relevant for material changes, not all.

Q3i. Do you have comments on Guideline 8 – Operational events indicators?

- **Paragraphs 1.35-1.36:** Operational indicators appropriately capture non-financial risks beyond IRRD minimums. However, their calibration is inherently qualitative and quantification should not be overemphasised.
- **Paragraphs 1.35 and 1.36:** state that "Operational indicators should capture operational events (...)". We consider that operational indicators should not capture events but operational conditions. Indicators are, by nature, forward-looking signals of emerging vulnerabilities, not records of operational events. As outlined in the IAIS Application Paper on Recovery Planning (section 5.3 on Trigger Framework), operational indicators should reflect the operational conditions of the undertaking (i.e., weaknesses, pressures, or deteriorations in processes, systems, or resources) not the occurrence of the event itself. In addition, a quantitative assessment of the operational dimension should be optional and left to the discretion of the undertaking.
- **Paragraph 1.35:** "material" should be added, i.e. "capture *material* events". The indicators are only relevant for material changes/events, not all.

Compliance and reporting rules

Q4. Do you have comments on the section 'Compliance and reporting rules'?

- Applying comply-or-explain to a detailed indicator framework risks creating de facto binding requirements. Reporting expectations may increase supervisory leverage beyond IRRD. Clear communication and proportional application are essential. Transitional arrangements should be considered, and consistency across NCAs is critical.

¹ The Beta (sensitivity to the market portfolio) of insurers in a CAPM model are usually identified as smaller than the ones of banks.

Annex I: Impact Assessment

Q5. *Do you have comments on Policy Issue A: Inclusion of additional criteria compared to list of criteria provided in the IRRD?*

- The preferred option not to introduce additional criteria beyond IRRD is strongly supported. The minimum list approach preserves flexibility and proportionality. Supervisory focus should remain risk-based.
- It must be ensured that no “shadow supervision” arises that triggers supervisory measures on the basis of informal indicators or above the clearly defined SCR thresholds. Solvency II purposely defines clear, transparent, and quantifiable intervention thresholds with the SCR and the MCR. This system must not be undermined by the IRRD.
- However, from a group perspective a consistent and non-fragmented application of *these Guidelines* across Member States is crucial. Alignment in supervisory practices regarding these indicators can support legal certainty, promote a level playing field, and contribute to effective and efficient supervision within the Member States. However, flexibility across Member States in the application of these Guidelines is also necessary to reflect differences between the insurance markets within the EU.

Q6. *Are there any elements in the proposed Guidelines which could be modified to reduce the administrative burden or improve the (cost) efficiency of the requirements? If so, please provide a (monetary) assessment of the expected efficiency brought by the proposed change.*

- To avoid duplication of work and, thereby reduce administrative burden, it should clearly stated in the guidelines that analyses and assessments already in place in the existing ORSA, liquidity risk management and stress testing processes can be reused for the indicators in the pre-emptive recovery plan.
- Acknowledging existing monitoring carried out under the ERM framework and its application (with thresholds tailored to IRRD requirements) would reduce the danger of duplication of effort greatly.
- Allowing simplified indicator sets for smaller undertakings could materially lower costs.
- Greater tolerance for qualitative indicators would improve efficiency.

Any other comments

Q7. *Do you have any other comments?*