Insurance Europe response to IAIS consultation on Issues Paper on roles and functioning of PPS

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Consultation questions

1	General comments on the Issues Paper Insurance Europe welcomes the opportunity to provide comments on the IAIS' Issues Paper on roles and functioning of Policyholder Protection Schemes (PPSs). Insurance Europe would like to underline that PPS which are currently in place vary significantly across Europe but work generally well within their local context and laws. Some EU member states currently have arrangements equivalent to an insurance guarantee scheme (IGS), whereas other EU member states do not have an IGS but consider policyholder protection to be sufficient. Insurance Europe appreciates that the fact that the IAIS does not require jurisdictions to have PPSs in place. This should remain the case given that the appropriate level of policyholder protection is a question better addressed by each jurisdiction, taking into account national market features and specificities. The paper describes some of the roles that PPS could play in recovery and resolution phases of an insurance failure. Recognising the jurisdictional differences that exist, an important point that should be brought out in the paper is the need for a clear delineation of roles and responsibilities between supervisors, resolution authorities and PPS. Overlapping or unclear roles will create uncertainty and could exacerbate any potential problems which arise from a failing insurer. Finally, Insurance Europe wishes to stress that decisions related to IGS funding, as with decisions on resolution financing, should be left to individual member states' consideration, in consultation with local stakeholders.

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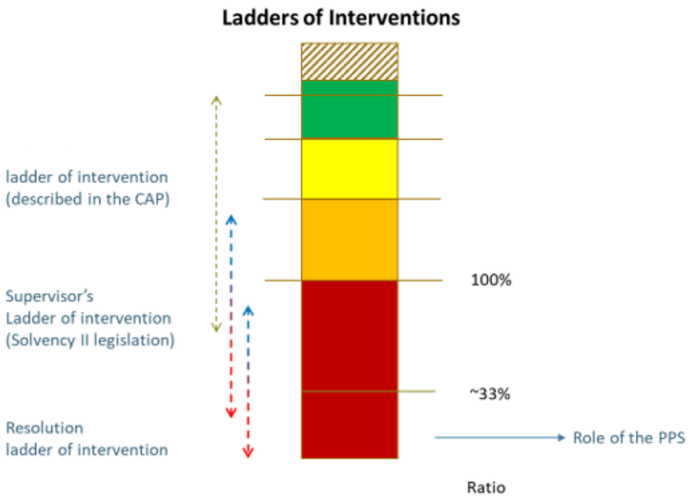
2	General comments on Section 1 Introduction
3	General comments on Section 1.1 Objectives and background
4	Comments on Paragraph 1
5	Comments on Paragraph 2
6	Comments on Paragraph 3
7	Comments on Paragraph 4 The text should recognise the fact that an effective regulatory system, such as Solvency II, combined with effective supervision, as well as a proportionate and effective recovery and resolution framework, can reduce the probability and impact of an insurance failure. It is not necessarily the case that PPS should not bear the cost of resolution (eg PPSs may also provide a mechanism to ensure that resolution costs are borne by the industry). The main objective of PPS should be to provide compensation to policyholders in the case of an insurer failure.
8	Comments on Paragraph 5 Insurance Europe supports the fact that the Insurance Core Principles (ICPs) and Comframe do not require jurisdictions to have policyholder protection mechanisms, and that instead this is a policy question to be addressed by each jurisdiction.
9	Comments on Paragraph 6
10	General comments on Section 1.2 Terminology A graphical overview of the stages of recovery would be beneficial for all readers. The role of the PPS can be easily seen from a graphical representation. For example: 
11	Comments on Paragraph 7
12	Comments on Paragraph 8
13	Comments on Paragraph 9

	Insurance Europe agrees that the focus of a PPS should be only on the individual insurer, not on the insurance group. In addition, Insurance Europe believes that compensation should be focused on the policyholder and beneficiary, not on other creditors of the insurer.
14	Comments on Paragraph 10 Insurance Europe agrees with the IAIS' assessment that reinsurers are rarely covered by PPS. This makes sense because, as noted above, compensation from a PPS should be focused on the policyholder and beneficiary, not on other creditors of the insurer. Reinsurance companies should also not have to pay into resolution funds that cover the costs of failures of primary insurers. The business model of reinsurers is based on taking over risks from primary insurers in exchange for a premium, which helps their clients mitigate the risks of failure. Resolution financing arrangements should be restricted to the compensation of individual (and not business) policyholders and to the administration costs of the resolution tools. In addition, reinsurance is different from primary insurance due to its intrinsically cross-border nature.
15	Comments on Paragraph 11 There should be a proper understanding and description of the so called 'ladder of intervention' and the role of the PPS. In the first instance, an insurer that breaches their prudential solvency ratio must outline measures to resolve this breach (this is often called a recovery plan). In this phase, the insurer is still a going concern and subject to the 'normal' supervisory dialogue. Only when a breach of the minimum capital requirement or a predefined other capital limit is breached - and the insurer is not able to recover from this breach - a so called 'recovery phase' in the sense of the PPS would start. The resolution authority would then take over the supervisory tasks. The definition of the term 'run off' is not unambiguous as it could also be used for the so called 'closed book' approaches of insurers.
16	General comments on Section 1.3 Inputs
17	Comments on Paragraph 12
18	General comments on Section 1.4 Structure
19	Comments on Paragraph 13
20	Comments on Paragraph 14
21	General comments on Section 2
22	General comments on Section 2.1 Overview
23	Comments on Paragraph 15 If a PPS has a role in the recovery phase, the role should not distort the competitive landscape of the distressed insurer in relation with the other insurers operating in the market.
24	Comments on Paragraph 16
25	Comments on Paragraph 17

	This paragraph could even lead to more confusion as it seems three types of supervisors could discuss the financial and solvency situation of a distressed insurer: the normal supervisory authority, the resolution authority and the PPS. The role is not to duplicate, but to transfer authority when due and the timely distribution of information to each other.
26	Comments on Paragraph 18 The PPS should not be a measure which could be used as easily as suggested, but is to help if no other measures could prevent policyholders from being negatively affected by the failure of a distressed insurer. If the PPS is a measure which can be accessed too easily, the issue of moral hazard becomes more important.
27	Comments on Paragraph 19
28	General comments on Section 2.2 Functions of PPSs Recognising the jurisdictional differences that exist, an important point to note is the need for a clear delineation of roles and responsibilities between supervisors, resolution authorities and PPS. Overlapping or unclear roles will create uncertainty and could exacerbate any potential problems which arise from a failing insurer. This is acknowledged in respect to PPS/resolution funding in Article 89 of the paper, but wider consideration of this point is also merited.
29	Comments on Paragraph 20 There is a real concern regarding a possible role of the PPS in protecting the financial stability at an early stage, as suggested by the IAIS. Who decides the actual point and is this also not more of a political decision? Why should the PPS be 'liable' for the negative fall out of the recovery while all kinds of other measures are still possible? It seems that this relates to systemically important insurers, if their distress would endanger financial stability. In various jurisdictions, a recovery and resolution scheme is actually initiated or used to avoid the issues with a failure of an (important) insurer which could endanger financial stability. The 'moral hazard' as mentioned is not only a possibility to emerge within the market but should also be addressed from the perspective of the supervisory community.
30	Comments on Paragraph 21
31	Comments on Paragraph 22
32	Comments on Paragraph 23
33	Comments on Paragraph 24 A comment on the sentence "in some jurisdiction the PPS can be used to facilitate specific resolution actions" should be added to reflect the points made in para. 89 (overlapping PPS and resolution funding)
34	General comments on Section 2.3 Intervention by PPSs
35	General comments on Section 2.3.1 Recovery phase The causes described makes it even more important to describe the actual roles of the three types of supervisors related to an insurer in the various stages of the (in)solvency. How would

	you ensure that the PPS, the resolution authority and the supervisory authority work in harmony? The objectives of the three supervisors could be different: while naturally the overriding objective would be protecting the interest of the policyholder, the manner in which this is achieved is different. See also comment 28.
36	Comments on Paragraph 25
37	Comments on Paragraph 26
38	Comments on Paragraph 27 The moral hazard also resides with the supervisory community. If the fund will pay, why take harsh measures which could have negative publicity, etc? The example "PPS provides funding to recapitalise an insurer" should be removed if it is not based on a specific jurisdiction. The document should not set standards or expectations (para. 1).
39	Comments on Paragraph 28 This paragraph should also reflect the fact that both in resolution and recovery, but certainly in recovery, a PPS intervention could easily distort competition. This is briefly stated in paragraph 28 but could be elaborated on in more detail.
40	General comments on Section 2.3.2 Resolution phase
41	Comments on Paragraph 29
42	Comments on Paragraph 30
43	Comments on Paragraph 31 The interventions of the PPS should be carefully assessed as it should not distort the markets and provide competitive advantages.
44	Comments on Paragraph 32 Not all non-life claims and insurance contracts have a short duration. For example, liability insurance can take many years. There is also an open question: how to tackle a claim which is incurred but not reported which emerges over time. Would a PPS have a role to cover those even of the non-life insurer ceases to exist and all known claims are resolved?
45	Comments on Paragraph 33 Insurance Europe believes it is important that there is an objective justification for a PPS to compensate losses. In many cases the compensation of losses by a PPS results in the attribution of losses to others than those who are responsible for the occurrence of these losses. If a PPS is industry-funded, generally the solvent insurers will bear the losses for a weaker insurer in the market and, while there might be reasons for such a distribution of losses, there should be good and objective reasons why creditors and policyholders should not bear their own losses. Supervisory regimes are generally not designed to be zero-failure regimes.
46	Comments on Paragraph 34

47	General comments on Section 3 When considering coverage, care should be taken to also assess what happens if, for example, several big insurers would fail together: would the PPS be able to withstand this scenario or would the PPS draw the failure of the whole industry?
48	Comments on Paragraph 35
49	Comments on Paragraph 36
50	Comments on Paragraph 37
51	General comments on Section 3.1 Scope of coverage
52	Comments on Paragraph 38
53	Comments on Paragraph 39
54	Comments on Paragraph 40
55	Comments on Paragraph 41
56	Comments on Paragraph 42
57	General comments on Section 3.2 Limits on compensation
58	Comments on Paragraph 43 In this paragraph, only moral hazard with respect to consumers is addressed. However, moral hazard exists for all stakeholders /parties.
59	Comments on Paragraph 44
60	Comments on Paragraph 45
61	Comments on Paragraph 46
62	Comments on Paragraph 47
63	Comments on Paragraph 48
64	Comments on Paragraph 49
65	Comments on Paragraph 50
66	General comments on Section 3.3 Method of compensation
67	Comments on Paragraph 51
68	Comments on Paragraph 52
69	Comments on Paragraph 53 In these instances, the PPS will compete with going concern insurers. Care should be taken not to distort the level playing field, especially if it is being paid by the same insurers on the market being affected by the potential distortion.
70	Comments on Paragraph 54
71	Comments on Paragraph 55

72	General comments on Section 3.4 Eligible policyholders and claimants
73	Comments on Paragraph 56
74	Comments on Paragraph 57
75	Comments on Paragraph 58
76	Comments on Paragraph 59
77	General comments on Section 3.5 Treatment of unearned premiums
78	Comments on Paragraph 60
79	Comments on Paragraph 61
80	General comments on Section 3.6 Cross-border issues of coverage: home- and host-jurisdiction principles If home and host are seen in different jurisdictions and cross border insurance exists, policyholders could always be at risk of not being protected by a PPS. This is unavoidable. There is an issue in home jurisdiction explained on page 17. In 2015, the European Commission (EC) asked France to change the rules of the Mandatory Third-Party Liability Insurance Guarantee Fund (Fonds de Garantie des Assurances Obligatoires de dommages, "FGAO"), taking the view that the IGS was discriminating against insurers based in other EU countries as it only covered insurers headquartered in France.
81	Comments on Paragraph 62
82	Comments on Paragraph 63
83	Comments on Paragraph 64
84	Comments on Paragraph 65
85	Comments on Paragraph 66
86	Comments on Paragraph 67
87	Comments on Paragraph 68
88	Comments on Paragraph 69
89	Comments on Paragraph 70
90	Comments on Paragraph 71
91	General comments on Section 4
92	Comments on Paragraph 72
93	General comments on Section 4.1 Sources for PPS funding Insurance Europe believes that decisions related to IGS funding should be left to individual member states' consideration, in consultation with local stakeholders. Insurance Europe broadly agrees with the pros and cons outlined by the IAIS and wishes to highlight the following elements:

	- The main arguments in favour of ex-post funding are that this will not result in contributions from insurers unless there is a failure, so insurers will have more funds at their disposal. This reduces management costs and avoids investment risks. Contributions to the fund will be computed according to actual need (outstanding claims/policies concerned). With ex-post funding, a certain amount of liquidity is needed on a rather short notice, yet there is no risk that funds are not used exclusively for the defined purposes of the IGS. However, in this case, the failing company will not have contributed to the fund. - Some member states could see ex-ante funding as a more efficient way to ensure speedy pay-outs to policyholders in the case of an insurer's insolvency. With ex-ante funding, contributors can better schedule payments into the fund. In addition, all insurers (including the one that will fail) will have contributed in advance, which seems a fairer outcome. - But ex-ante funding also has a number of disadvantages, especially with regard to financial management. Experience has shown that funding on an ex-ante basis often leads to the multiplication of tasks that the fund needs to run. Ex-ante funding with immediate fund transfer to the IGS also involves greater administrative duties and costs. Unused funds (which become disproportionately large when insurance failures are infrequent or have a limited impact) would block financial resources for a long period of time, exposing them to risks of inefficient use and bad management. - In any case, an IGS should not be expected to guarantee to repay policyholders in full. Therefore, one would expect there to be restrictions (caps and limits) on the amounts that can be reclaimed under this system and IGS funds cannot be expected to be equivalent to the full value of the technical provisions. - In small, concentrated markets, IGS will only be able to protect consumers from the failure of small insurance companies. Any failure of a medium-sized or large company in a small, concentrated market will require state assistance in order to protect consumers effectively. In the absence of state assistance, and should sound companies be required to fill in funding gaps if a large insurance company collapses, interconnectedness between insurance companies operating in such markets would increase and this would give rise to systemic risks concerns.
94	Comments on Paragraph 73
95	Comments on Paragraph 74
96	Comments on Paragraph 75
97	Comments on Paragraph 76
98	Comments on Paragraph 77
99	Comments on Paragraph 78
100	General comments on Section 4.2 Ex-ante, ex-post and hybrid funding
101	Comments on Paragraph 79 A sentence is duplicated: With ex-post funding arrangements, solvent insurers pay assessments after the insolvency has occurred
102	Comments on Paragraph 80

	A possible hybrid approach could be to allow insurers to keep PPS contributions on their own balance sheets, rather than transferring any required ex ante funds to an external fund.
103	General comments on Section 4.3 Determining the levy level for insurers The levy for an insurer should be risk-based and not necessarily be connected to GWP.
104	Comments on Paragraph 81
105	Comments on Paragraph 82
106	Comments on Paragraph 83
107	Comments on Paragraph 84
108	Comments on Paragraph 85
109	General comments on Section 4.4 Differences between resolution funds and PPSs
110	Comments on Paragraph 86
111	Comments on Paragraph 87
112	Comments on Paragraph 88
113	Comments on Paragraph 89
114	General comments on Section 5
115	Comments on Paragraph 90
116	General comments on Section 5.1 ICPs and PPS disclosure
117	Comments on Paragraph 91
118	Comments on Paragraph 92
119	General comments on Section 5.2 Disclosure considerations relevant to PPS
120	Comments on Paragraph 93
121	Comments on Paragraph 94
122	Comments on Paragraph 95
123	Comments on Paragraph 96
124	Comments on Paragraph 97
125	Comments on Paragraph 98
126	Comments on Paragraph 99
127	Comments on Paragraph 100
128	Comments on Paragraph 101
129	Comments on Paragraph 102
130	General comments on Section 6

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<tr><td>132</td><td>Comments on Paragraph 104</td></tr>
<tr><td>133</td><td>General comments on Section 6.1 Cooperation and coordination between PPSs

Particular attention should be paid to the position of financial conglomerates, interactions with resolution regimes in both the banking and insurance sectors, compensation of deposit holders by a DGS and resolution strategies applied by the various resolution authorities, in particular when bail-in would be applied.</td></tr>
<tr><td>134</td><td>Comments on Paragraph 105</td></tr>
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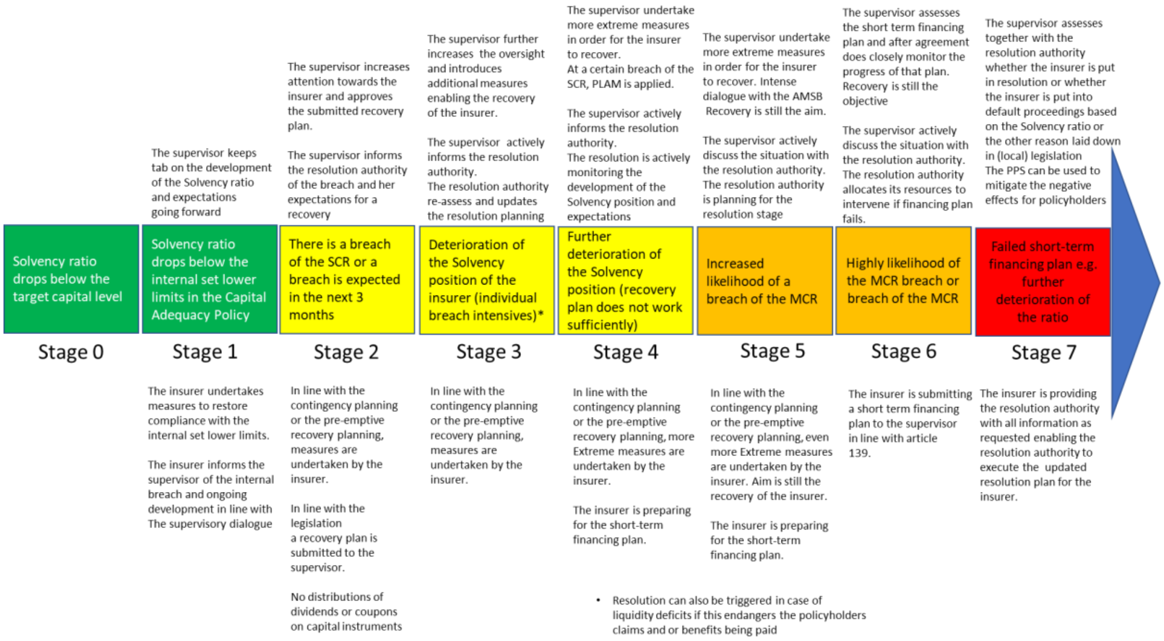
<tr><td>140</td><td>General comments on Section 6.2 Cooperation and coordination between a PPS and a supervisor/resolution authority

The cooperation between the various supervisors should not lead to the duplication of supervision. As mentioned in this section, the supervisory community should assist each other in obtaining clearly set objectives.

An example of the cooperation in different stages is: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<tr><td>141</td><td>Comments on Paragraph 111</td></tr>
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144	Comments on Paragraph 114
145	Comments on Paragraph 115
146	Comments on Paragraph 116
147	Comments on Paragraph 117
148	Comments on Paragraph 118
149	Comments on Paragraph 119
150	Comments on Paragraph 120
151	Comments on Paragraph 121
152	Comments on Paragraph 122
153	Comments on Paragraph 123
154	Comments on Paragraph 124
155	General comments on Section 7
156	General comments on Section 7.1 Other mechanisms aimed at protecting policyholders in the event of an insurer failure An essential mechanism to protect policyholders in the event of an insurer failure is the availability of an orderly resolution regime. Orderly resolution (such as, for example, an orderly run-off in resolution) can help to prevent avoidable losses when an insurer has failed (eg through fire sales of assets, early terminations of policies). Even if an insurer fails there may be sufficient funds available to cover outstanding claims, continue policies, while it may not be possible to continue as going concern insurance company. Orderly resolution can play an important role to mitigate the costs of a PPS, by reducing the risk that losses occur.
157	Comments on Paragraph 125
158	Comments on Paragraph 126
159	General comments on Section 7.1.1 Preferred claims
160	Comments on Paragraph 127
161	General comments on Section 7.1.2 Tied assets
162	Comments on Paragraph 128
163	Comments on Paragraph 129
164	General comments on Section 7.1.3 Segregated assets
165	Comments on Paragraph 130
166	Comments on Paragraph 131
167	Comments on Paragraph 132
168	General comments on Section 7.2 Other protection mechanisms outside of insurers' failure

169	Comments on Paragraph 133
170	General comments on Section 7.2.1 Mechanisms that indemnify the victim when the responsible person is unknown or uninsured
171	Comments on Paragraph 134
172	Comments on Paragraph 135
173	General comments on Section 7.2.2 Mechanisms covering catastrophe risks
174	Comments on Paragraph 136
175	General comments on Annex
176	Comments on Section 1 Moral hazard
177	Comments on Section 2 Safeguards to mitigate moral hazard