

**Opinion**  
**of the European Insurance and Occupational Pensions**  
**Authority of 24 November 2014 on**  
**Sound principles for Crisis Prevention, Management and**  
**Resolution preparedness of NCAs**

**Introduction and Legal Basis**

1. This Opinion is issued under the provisions of Article 29(1) (a) of Regulation (EU) No1094/2010 of the European Parliament and of the Council of 24 November 2010<sup>1</sup> (hereafter the 'Regulation'). As established in this Article, EIOPA shall play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.
2. To this end, EIOPA has decided to provide an Opinion relating to the Crisis Prevention, Management and Resolution preparedness of National Competent Authorities (NCAs) in relation to the insurance sector.
3. This Opinion is addressed to the NCAs represented in EIOPA's Board of Supervisors.

**Context**

4. EIOPA carried out a survey in 2013 with the aim of obtaining a better understanding of the crisis prevention, management and resolution approaches and practices across EU-NCAs with regard to insurance.
5. The outcome of this exercise was presented in the report titled "Crisis Prevention, Management and Resolution Preparedness of National Supervisory Authorities - Survey Results", which was published by EIOPA.<sup>2</sup>

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<sup>1</sup> OJ L 331, 15.12.2010, p. 48–83.

<sup>2</sup> See:

[https://eiopa.europa.eu/fileadmin/tx\\_dam/files/publications/reports/Report\\_on\\_Crisis\\_Prevention\\_Management\\_and\\_Resolution\\_Preparedness\\_of\\_NSAs.pdf](https://eiopa.europa.eu/fileadmin/tx_dam/files/publications/reports/Report_on_Crisis_Prevention_Management_and_Resolution_Preparedness_of_NSAs.pdf)

6. The report showed the average situation in the EU, without assessing whether the average was satisfactory or not. As a next step, a set of Sound Principles has been extracted, which should help NCAs to self-assess their individual situations.
7. The objective of this Opinion is to have a repository of sound principles in the field of crisis prevention, management and resolution with regard to insurance. The Sound Principles should be understood as a set of prudent practices/references to be considered when reviewing and further developing the NCAs' Crisis Prevention, Management and Resolution Frameworks. The overarching goal is twofold, i.e. to contribute to the maintenance of EU financial system stability, as well as the protection of policyholders. Both goals were reported by NCAs as statutory objectives of their respective frameworks.
8. The Sound Principles are based on the conclusions of the above mentioned report, which is consistent with other relevant material in this field, such as:
  - The "Guidelines for the preparation and management of a financial crisis" (CEIOPS-DOC-15/09); and
  - The "Memorandum of Understanding on cooperation between the financial supervisory authorities, central banks and finance ministries of the European Union" (ECFIN/CEFCPE(2008)rep/53106 REV).
  - The "Key Attributes of Effective Resolution Regimes for Financial Institutions", FSB, 15 October 2014, new version with annexes including guidance on resolution.
9. One of the main lessons learned from the survey is the fact that NCAs have been or are currently introducing changes in their Crisis Prevention, Management and Resolution Frameworks as a result of the financial crisis and the international initiatives. It is expected that NCAs take into account the Sound Principles set out in this document.

**Taking the above into consideration, EIOPA is of the opinion that the following Sound Principles provide a good foundation for the Crisis Prevention, Management and Resolution preparedness of NCAs with regard to insurance:**

### **Crisis prevention and preparation**

10. Crisis prevention is focused mainly on specific procedures and actions taken in order to prevent a crisis as well as the necessary processes to manage the crisis when it occurs. It should enable NCAs to act effectively and in a timely manner in such situations.
11. One of the main lessons learned from the current financial crisis is that prevention is the best and most economical way of crisis management. As such, a substantial part of the Sound Principles revolves around crisis prevention.
12. The following Sound Principles can be extracted, with regard to crisis prevention.

#### **➤ Sound Principle 1: Crisis prevention/management groups**

**An effective crisis prevention system includes the existence of an internal group within the supervisory authority focused specifically on crisis prevention and management.**

13. This group should ideally be composed of high-level staff from all relevant areas and have a formal mandate. The mandate should cover both crisis prevention and management responsibilities, main objectives, staff involved, allocation of tasks and organisation of work.

➤ **Sound Principle 2: Emergency plans**

**Comprehensive emergency plans covering the whole crisis management processes are useful tools. They help authorities to be prepared, identify potential weaknesses and address them before the outbreak of a crisis.**

14. Emergency plans should not aim at covering all possible scenarios. Nor should they tie authorities in any way. Instead, they should contain relevant and updated information that needs to be available promptly in a crisis situation.
15. These plans generally include important elements such as:
  - Legal basis for crisis prevention, management and resolution;
  - Organisational structures to deal with a crisis;
  - Process and procedures for crisis alerts, assessment and management;
  - Roles and responsibilities;
  - Contact lists of relevant crisis prevention and management staff; and
  - Procedures for information exchange and cooperation with other authorities and external communication.
16. In order to keep them up to date, plans should be updated on a regular basis (e.g. yearly) or whenever a significant development takes place.

➤ **Sound Principle 3: Secure means of communication**

**Communication is key in a crisis situation. Adequate and timely information enables decision makers to take the best course of action.**

17. Considering that the information to be exchanged is usually sensitive, secure means of communication should ideally be in place, not only for a crisis situation, but also on a day-to-day basis. At a minimum, it seems reasonable to set up an email service with encrypted features for secure transmission of sensitive information.

➤ **Sound Principle 4: Crisis exercises**

**Crisis exercises carried out by NCAs seek to enhance their crisis management preparedness by testing the decision-making processes and, eventually, highlighting areas for improvement.**

18. It is important to have a strategy in place that comprises a variety of exercises and a timeline to carry them out, ranging from the simplest (e.g. a communication test), to more demanding exercises (e.g. walkthrough or simulation exercises). Crisis exercises should ideally be performed on a regular basis.

➤ **Sound Principle 5: Recovery plans**

**Two relevant tools that help authorities to gain a better insight into how entities plan for crisis situations and are better prepared in case they finally occur are recovery and resolution plans of insurers.**

19. NCAs should make sure that undertakings (at least, those considered to be systemically important) draft recovery plans<sup>3</sup> in a pre-emptive and proportionate way, to identify options to restore financial strength and viability when the undertaking comes under stress. In this regard, NCAs may also consider issuing guidelines or recommendations with regard to the content and structure of these plans.

➤ **Sound Principle 6: Resolution plans**

**Resolution plans provide for the resolution actions which the authority responsible for resolution may take where an undertaking faces certain problems that cannot be overcome through recovery actions.**

20. Resolution plans should be drafted in cooperation with undertakings and in a pre-emptive and proportionate way, at least for systemically important institutions. Resolvability assessments to evaluate the feasibility of resolution strategies should also be undertaken.

## **Crisis alert and assessment**

21. NCAs need to have crisis alert and assessment mechanisms in place to become aware as soon as possible of a potentially serious financial disturbance or of facts or events that may give rise to significant problems for an insurance group or the functioning of financial markets.
22. The following Sound Principles have been extracted from the EIOPA survey, with regard to crisis alert and assessment.<sup>4</sup>

➤ **Sound Principle 7: Early warning systems**

**Early warning systems may help NCAs to recognise adverse developments at an early stage, which may, in turn, facilitate supervisory interventions and ensure that adequate and proportionate actions are taken.**

23. An early warning system should be designed in a way that supports the supervisory ladder of intervention. Early warning indicators should specify certain benchmarks that prompt the consideration of different actions according to the severity of the situation. In this regard, they should provide the necessary information regarding the transition from intensified supervision to recovery and resolution of institutions.
24. Early warning systems are usually composed of a wide variety of quantitative and/or qualitative early warning indicators. Among others, the following can be considered: solvency, liquidity and profitability position of undertakings, investment exposures, claim evolution, bonus and remuneration structure, significant intra-group transactions, business model, governance structure,

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<sup>3</sup> Recovery plans in this context refer to plans envisaged in the "FSB Key Attributes of Effective Resolution Regimes for Financial Institutions" (15 October 2014) and should not be confused with Recovery Plans as specifically defined in Art. 142 of Directive 2009/138/EC on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II).

<sup>4</sup> Both Sound Principles 7 and SP 8 are aligned with the Solvency II Directive and the Supervisory Review Process.

enterprise risk management systems, adverse reports from auditors/actuaries, failure to implement regulatory/supervisory requirements.

➤ **Sound Principle 8: Structured risk based approach to supervision**

**A structured risk based approach to supervision enables the identification, analysis, and assessment of risks on the basis of micro- and macro prudential information.**

25. The aim is to make supervision more efficient and effective by focusing more closely on the potential sources of risks and by adequately managing the resources available. For example, a risk based approach should allow the classification of supervised undertakings according to their risk profile and systemic relevance, thereby allocating more resources where they are actually needed.

## **Crisis management and resolution**

26. Crisis prevention, management and resolution should be seen as part of a continuum of supervisory activities. After NCAs become aware of a potential problem, and in case their assessment reveals a significant risk, supervision is usually intensified and other measures are taken to maintain the viability of the undertaking.
27. Resolution is usually a last resort option if problems persist and the recovery actions prove not to be sufficient. As stated in the Insurance Annex to the Key Attributes, resolution should make it feasible to resolve an insurer without severe systemic disruption or exposing taxpayers to loss, while protecting vital economic functions through mechanisms which make it possible for shareholders and unsecured creditors to absorb losses in a manner that respects the hierarchy of claims in liquidation.<sup>5</sup> The resolution of an insurance company is different to that of a bank, and these differences should also be taken into account in the resolution framework. The business model of insurers, as opposed to banks, typically does not require rapid liquidation of assets to meet short-term liabilities. As such they are run-off and wound up over a period of time, sometimes several years.
28. The following Sound Principles can be extracted, with regard to crisis management and resolution.

➤ **Sound Principle 9: Triggers for intervention**

**This sequential process “intensified supervision-recovery-resolution” requires the definition of specific triggers for intervention that result in a series of supervisory actions that –ideally– were previously developed or considered in the crisis prevention phase.**

29. It should be stressed that the governance of the whole process should also be clearly established by making sure that responsibilities are clearly allocated among the different authorities involved and that the right incentives are in place. For example, there should be clear guidance as to when the authority or function responsible for resolution takes over from the supervisor or the supervisory function in the crisis management process.

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<sup>5</sup> See the FSB Key Attributes of Effective Resolution Regimes for Financial Institutions (II-Annex 2: Resolution of Insurers, paragraph 1.1).

30. The triggers for intervention are usually determined by combining a set of financial thresholds and supplementing the latter with expert judgement to provide certain flexibility as to when to intervene. The triggers for intervention should result from the early warning system.

➤ **Sound Principle 10: Triggers for informing the Colleges of Supervisors**

**In a crisis scenario, an adequate sharing of information is key, particularly in the Colleges of Supervisors in case of cross-border groups.**

31. For this reason, it is important that NCAs specify triggers for informing or calling a meeting with the Colleges of Supervisors (for cross-border groups). In case NCAs rely on the agreements reached in the Colleges of Supervisors, they should consider whether these triggers have been adequately internalised with the triggers for intervention.

➤ **Sound Principle 11: Resolution powers**

**A smooth resolution requires authorities to have an array of resolution powers available that enable them to provide a satisfactory answer to the challenges they have to face when resolving an insurance undertaking.**

32. NCAs and/or resolution authorities should be equipped with and be able to use a variety of resolution tools to resolve an undertaking in an orderly manner, without severe systemic disruption or exposing taxpayers to loss, while protecting vital economic functions. For that purpose, NCAs and/or resolution authorities should assess the powers they need against the powers they have and should request to be provided with the necessary additional powers by the relevant legislative body.

➤ **Sound Principle 12: Sources for resolution funding**

**Resolution of one or several undertakings can become costly. Against this background, there is a need to have adequate sources for resolution funding in place.**

33. This may include recourse to an insurance guarantee scheme, disposal of assets or limitation of creditor rights among other options. The use of public money should be restricted to the extent possible and as a last resort.

## **External communications to the public**

34. Handling communications with all stakeholders (e.g. insurance industry, investors, the media and the political sector) may become quite challenging in times of distress. If not properly managed, the level of uncertainty will increase, which will in turn, make any communication action more difficult.
35. The following Sound Principle can be extracted, with regard to external communications.

➤ **Sound Principle 13: Communication agreements**

**External communications need to be properly managed in terms of messages sent and their respective timing.**

36. It is crucial to have clear communication arrangements in place such as crisis communication plans or manuals, agreed messages (templates), or guidance for public communication. Roles and responsibilities, as well as triggers for

external communication should also be defined to avoid confusion in the market.

## **Cooperation on cross-sectorial issues with other national authorities**

37. The different elements of a financial system are not in isolation. The effects of a crisis usually go beyond one institution or sector and tend to spill over to other parts of the financial system. When this is the case, cooperating with other national authorities can contribute to take the right action.
38. The following Sound Principle can be extracted, with regard cooperation with other national authorities.

### **➤ Sound Principle 14: Cooperation and information sharing with other national authorities**

**Cooperation and information sharing with other relevant authorities is key, in particular in case of multiple financial supervisors within the same jurisdiction (i.e. sectorial or twin peaks models).**

39. Integrated supervisors should also make sure that there are procedures in place to ensure cooperation among relevant departments and also with other non-supervisory authorities, such as the ministry of finance.
40. NCAs should have a high degree of cooperation and information sharing with other national authorities to ensure a timely and effectively coordinated action. This is particularly important in those countries where the supervisor and the authorities responsible for resolution are different institutions.
41. Cooperation may imply among other things:
  - Setting up a National Standing Group or, at least, having formal cooperation and information sharing arrangements in place (e.g. Memorandum of Understandings) to enhance the preparedness of the parties in normal times and the management of crisis situations;
  - Developing formal procedures with other national authorities to manage a potential crisis in a coordinated way (e.g. cross-sectorial emergency plans and contact lists of relevant persons);
  - Exploring the implementation of secure means of cross-sectorial communication to share confidential information and avoid undesired leaks or access by unauthorised individuals;
  - Considering the establishment of a common database maintained by all authorities with relevant (common) information for crisis prevention and management that can legally be shared among authorities;
  - Considering the conduct of cross-sectorial simulation exercises in order to test the coordination agreements and the respective decision-making processes; and
  - Coordinating public communication (e.g. by means of regular meetings of the communication teams, agreed terms of references or joint statements) in order to avoid sending contradictory or conflicting messages in a crisis situation.
42. EIOPA considers that its Opinion on Sound Principles is a living document that should be adapted on the basis of the experience gained and the development

in the field of crisis prevention, management and resolution. Furthermore, EIOPA intends to engage in a follow-up exercise with Members in time to explore what actions have been taken in light of this Opinion.

This Opinion will be published on EIOPA's website.

Done at Frankfurt am Main, 24 November 2014

*[signed]*

Gabriel Bernardino

Chairperson

For the Board of Supervisors