

Public interest assessment in the resolution of insurance and reinsurance undertakings

Warsaw, April 2024



Definition and regulations regarding public interest

Assessment of public interest – regulations in the proposal for IRRD (1)

→ According to the Article 19(4) of the proposal for IRRD **a resolution action shall be in the public interest where**

1. such action is **necessary for the achievement of one or more** of the resolution objectives listed in Article 18(2)
2. and is **proportionate** to them and **winding up** the undertaking under normal insolvency proceedings **would not meet those objectives to the same extent.**

→ The assessment of the public interest rationale therefore refers to two aspects (areas of assessment):

1. assessment of the fulfilment of individual objectives in resolution and in standard insolvency proceedings,
2. proportionality assessment (undefined - possible approach: comprehensive assessment of the fulfilment of all objectives and burdens of the stakeholders).



Assessment of public interest – regulations in the proposal for IRRD (2)

The definition of the public interest in Article 19 of the IRR Directive proposal refers to the need to achieve resolution objectives. These objectives are defined in Article 18 of the IRR Directive proposal as follows:

1. **protecting** the collective interest of policy holders, beneficiaries and claimants;
2. maintaining **financial stability**, in particular, by preventing contagion and by maintaining market discipline;
3. ensuring the continuity of **critical functions**;
4. **protecting public funds** by minimising reliance on extraordinary public financial support.



Assessment of public interest – regulations in the proposal for IRRD (3)

The public interest is also referred to in Article 9(2) of the IRR Directive, which sets out the conditions for the preparation of resolution plans as follows:

"Resolution authorities shall **draw up resolution plans for** insurance and reinsurance **undertakings for which they assess that it is more likely**, relative to other undertakings under their remit, **that resolution action would be in the public interest (...).**"

Possible approaches to assessing the fulfilment of resolution objectives in a public interest assessment

Objective 1 - protecting the collective interests of policyholders, beneficiaries and claimants

The degree of protection of policyholders, beneficiaries and claimants can be verified by comparing the financial situation of those in the scenario of triggering resolution against the undertaking and in the scenario of winding up the undertaking under standard insolvency proceedings.

Measures of financial impact can be:

1. **the extent** to which claims are **settled**, and
2. **the possibility to conclude new insurance contracts** if existing contracts expire in a bankruptcy scenario, and **their terms** (amount of new premiums due to, for example, the age of the insured, possibility to obtain a refund of premiums for the unused coverage period, coverage during the transition period).

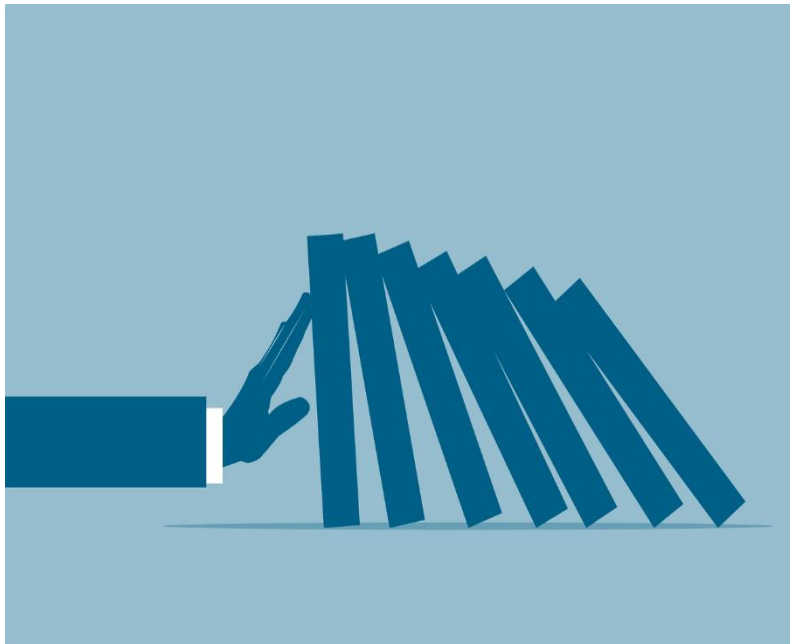


Objective 2 - maintaining financial stability

Verification of whether resolution in a given scenario would ensure the maintenance of financial stability could be made by **comparing the consequences of triggering resolution against an undertaking with a scenario of winding up of that undertaking** under standard insolvency proceedings in the area of possible destabilisation's transmission channels.

Examples of destabilisation's transmission channels are:

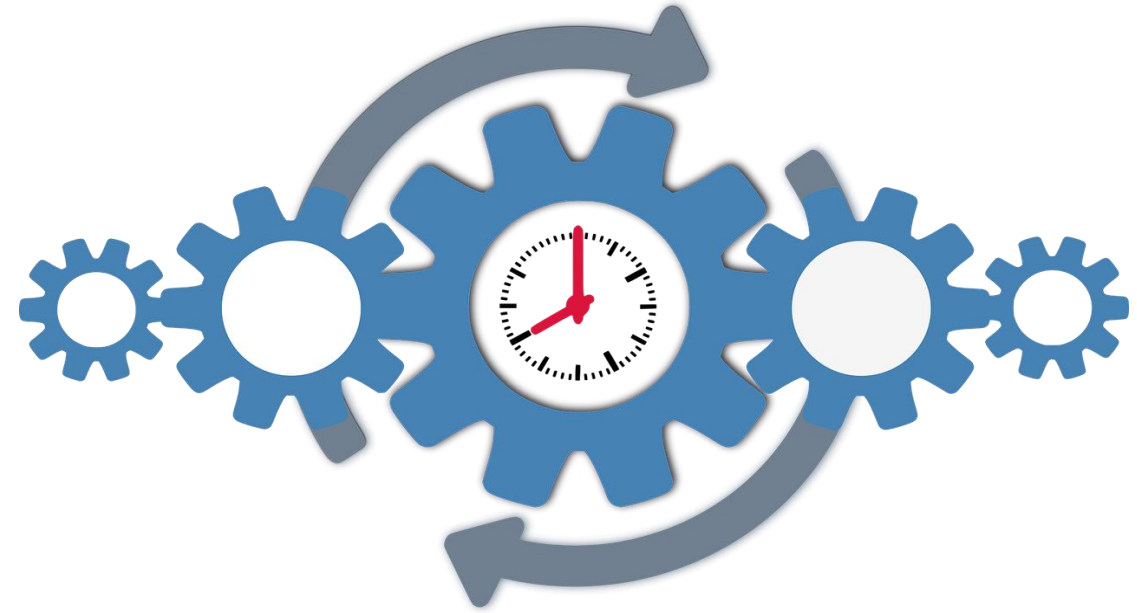
- **Financial markets** (e.g. panic on the stock market following the announcement of the bankruptcy of a listed company and a fall in its stock price),
- **Financial dependencies** (e.g. additional premiums charged by guarantee scheme or resolution fund),
- **Economic dependencies** (e.g. failure to pay significant compensations to large enterprises).



Objective 3 – ensuring the continuity of critical functions

A key step in assessing the objective of ensuring the continuity of critical functions is to determine if and what critical functions the undertaking performs. These functions will be identified according to the methodology adopted by the resolution authority.

In order to assess the continuity of the critical function in the scenario of resolution of an insurance undertaking, **an analysis should be made of the impact of the applied resolution scenario on its continuity (uninterrupted performance) compared to the scenario of the winding-up** of that undertaking under standard insolvency proceedings.



Objective 4 – protecting public funds

Assessment of the fulfilment of the objective of protecting public funds can be made by comparing the amount of use of funds from the sources available in the different proceedings (winding up under standard insolvency proceedings and resolution).

Examples of funding sources considered may include:

- **Undertaking's own resources,**
- **Resolution fund,**
- **Other funds** operating within the financial safety net of undertakings (e.g. guarantee schemes),
- **Budgetary measures (as an absolute last resort).**

The assessment is conditioned by the shape of the implementation of the crisis management system.



Public interest assessment - summary of the assessment of objectives' achievement

After analysing the extent to which the various objectives have been achieved in resolution and in winding up under standard insolvency proceedings, it is necessary to summarise the results of the analysis to enable verification of the public interest rationale.

- Where, for each of the four resolution objectives, the degree of achievement is equal or higher in the event of the entity's bankruptcy compared to resolution, it should be assumed that the public interest rationale is not met.
- When at least one of the four objectives is achieved to a higher degree in the resolution process, this may indicate that the public interest rationale is met. However, the analysis should be complemented by a **proportionality assessment**.

Proportionality assessment

Public interest assessment – proportionality assessment

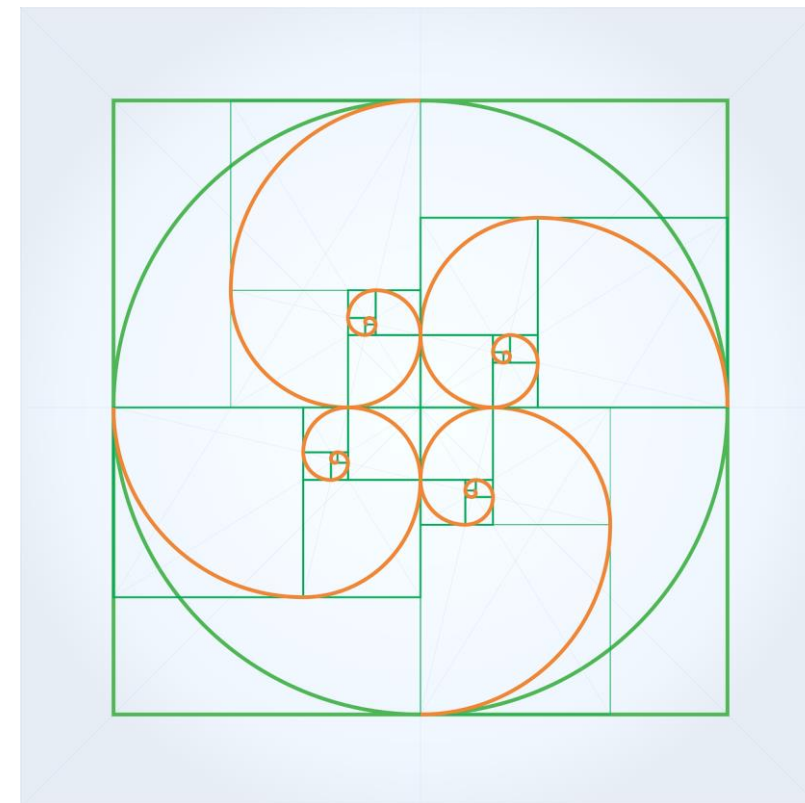
Assessing the proportionality of resolution requires **taking a global view of the achievement of all four objectives** for the individual resolution scenarios and in the option of winding up the undertaking under standard insolvency proceedings and checking whether standard insolvency proceedings would not achieve these objectives to the same extent.

Consideration should also be given to the **burdens** imposed on stakeholders **not explicitly considered** in the analysis of resolution objectives, for example, the **potential inconvenience** to creditors in case of:

- **conversion of the undertaking's debt** into equity instruments,
- **a deferred payment period** or
- possible **problems in handling insurance** shortly after a portfolio transfer.

The **severity of the measures applied to owners** should be also assessed versus the financial situation.

Lastly, it is necessary to compare the global achievement of the objectives with the burdens imposed on the parties to the proceedings and to determine whether there is **proportionality** between them.



Use of the public interest assessment in resolution planning

Public interest assessment vs. the resolution planning process

Verification of the presence of the public interest rationale allows:

- ✓ Identification of entities subject to planning obligations (i.e. preparation of resolution plans),
- ✓ Selection of the **preferred** resolution scenario with the **preferred** resolution tool used,
- ✓ Identification of potential alternative action strategies in the event of a undertaking failure threat,
- ✓ Identifying the impact of different resolution options towards an establishment at risk of bankruptcy.

A proper and pragmatic assessment of the presence of a public interest rationale is an important step that also starts resolution's resolvability assessments.

www.bfg.pl

