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Report on the Role of Insurance Guarantee Schemes in the Winding-Up Procedures of Insolvent Insurance Undertakings in the EU/EEA

1. Introduction

This report is prepared as part of EIOPA's input to the European Commission's policy making on Insurance Guarantee Schemes (IGSs) and as specified in the mandate of the Task Force on Insurance Guarantee Schemes. The purpose of the report is to summarise the findings of a mapping exercise on the role of the IGS in the winding-up procedures of insolvent insurance undertakings across the EU/EEA.

A questionnaire was used for the purpose of this exercise and sent to 30 EU/EEA states. 24 Member States responded. Where references are made to the majority or minority of Member States, this refers to the number of respondents rather than the full membership of the EU/EEA.

For the purpose of this report, an IGS is a body that provides last-resort protection to consumers when insurance undertakings are unable to fulfil their contractual commitments. Motor insurance guarantee schemes are covered in this report only to the extent that they provide cover in such winding-up situations. An IGS may have a wide ranging scope, covering life, non-life or both types of insurance contracts. In the majority of Member States' jurisdictions, only certain classes of insurance contracts are covered[1].

2. Topics covered

The following areas are covered in this report:

(1) Types of IGSs (the diversity of IGSs in the EU/ EEA, cross border IGS membership and the permanent or ad hoc character of the IGS);

[1] For further details on existing guarantee schemes in place in the EU/EEA, please refer to EIOPA's (CEIOPS) report 30 June 2009 on Insurance Guarantee Schemes with annexes https://eiopa.europa.eu/fileadmin/tx_dam/files/publications/submissionstotheec/CEIOPS-DOC-18-09%20_Input_to_EC_work_on_IGS-approved_clean_.pdf

(2) Role of the IGS prior to insolvency (formal or informal pre-warning systems, free exchange of information between the IGS and the supervisory authority and preventative measures taken by the IGS);

(3) Role of the IGS in the insolvency process (deciding when to intervene, options for exit from insolvency, continuance of coverage, criteria taken into account by an IGS for portfolio transfer, role of the IGS when an insurance undertaking becomes insolvent, cross-border co-operation and co-ordination arrangements);

(4) Role and interaction of other bodies with the IGS (role of the supervisory authority, differences between life and non-life insurance insolvency and their treatment by the supervisory authority);

(5) Role of the court in winding-up proceedings when the insolvency procedures are initiated and/or throughout the insolvency or the winding-up procedures; and

(6) Role of the IGS in the claims process (time limit for claims payments and observed payment times, treatment of unearned premia, funding payment of claims, rights of policyholders to take the IGS to court, payment of claims upfront and reimbursement, subrogation rights of the IGS, other rights and rights of creditors).

3. Summary of findings

3.1 Types of IGSs

3.1.1 Diversity of IGSs in the EU/EEA

Only two respondents (IS and SE) reported having no IGS at all.

Two Member States have a dedicated IGS for accidents at work (in certain jurisdictions this risk is covered by a public social security scheme).

Seven respondents have a life insurance IGS and five have a non-life insurance IGS. Five have IGSs which cover both sectors. This sample of Member States is not representative and cannot lead to an obvious conclusion concerning Member States' appetite to have separate or common IGSs. The conclusion to be drawn from this is that although nearly all Member States provide some form of coverage, comprehensive protection is scarce and cover is often limited to the motor insurance sector.

18 respondents reported having an IGS which covers motor insurance. Of these 18 countries, nine have reported that the IGS covering motor insurance is the only IGS in their country. Motor insurance guarantee schemes are well developed throughout Member States and some of these countries have extended the scope of their "guarantee funds" set up under the EU Motor Directives to include insolvency cases.

3.1.2 IGS membership – cross border

Member States were asked whether a foreign insurance undertaking (3rd country insurance undertakings or insurance undertakings established in Member States or

both) with branches could become a member of an IGS in their jurisdiction (either on a voluntary or compulsory basis).

For life and non-life IGS (11 respondents), the answers can be divided into two groups, for branches from third-countries and for branches from EU/EEA Member States:

- For branches from non EEA third-countries, eight respondents reported that these insurance undertakings can (sometimes subject to certain conditions) become a member of an IGS, either on a voluntary or mandatory basis.
- For branches from EU/EEA Member States:
  - four reported that such insurance undertakings cannot become a member of their IGS;
  - three answered that they can become a member of their IGS (either on a compulsory or voluntary basis); and
  - in a few Member States, branches of insurance undertakings established in other Member States are required to become members of the host state IGS only where the IGS in the home state does not provide equivalent protection to policyholders established in the host Member States.

These answers may reflect the principle (home or host state principle) chosen by the countries.

For motor IGS, 13 respondents (of 18 Member States concerned) answered that foreign companies must become members of their IGS.

In summary, it appears that where cross-border operations from third countries have been addressed (eight respondents), Member States are more likely to require mandatory membership for third countries insurance undertakings operating in their jurisdictions, whereas for operations from other Member States, membership is often on a voluntary basis.

3.1.3 Permanent or ad hoc character of the IGS

Almost all IGSs are "active" at all times. However, there seems to be a variety of definitions of what "active" means, ranging from being fully operational permanent institutions to a more reduced presence (that is to say only the legal framework exists without the administrative functions in place).

All life insurance IGSs are operational at all times. Five out of six non-life IGSs are also operational at all times.

3.2 Role of the IGS prior to insolvency

3.2.1 Formal or informal pre-warning systems when an insurance undertaking will soon be subjected to liquidation proceedings

(a) Pre-warning an IGS

Pre-warning an IGS that an insurance undertaking will soon be subjected to liquidation proceedings is important for organisational and financial reasons. Keeping

the IGS informed of any potential insolvency enables them to be better prepared to perform their function.

Although only FR reported the existence of a legal provision between the supervisors and the IGS, various Member States:

- suggested the existence (or potential existence if needed) of an informal flow of information between the supervisor and the IGS before the decision to wind up the insurance undertaking (four Member States);
- emphasized the absence of legal constraints to such flow of information, or the empowerment of the supervisor to deliver such information (four Member States).

Eight Member States reported an absence of a pre-warning system. Two Member States noted that the supervisory authority shall warn the IGS of the withdrawal of the insurance undertaking's authorisation.

Overall, Member States reported that such pre-warning systems are not as widely used as in the US, where there is a very active but informal system of pre-warning between guaranty associations (GA) of probable insolvencies of insurance undertakings which could affect multiple states.

(b) Pre-warning of the supervisory authority

Besides the supervisor's regular monitoring of the insurance undertaking, (and the insurance undertaking's obligation to inform the supervisor of non-compliance with financial requirements), in general the insurance undertaking's decision to liquidate itself (voluntary dissolution or petition to the court) is subject to authorisation/non-opposition by the supervisor.

3.2.2 Free exchange of information between IGSs and the supervisory authority

Member States were asked whether an IGS and the supervisory authority could freely exchange information necessary to perform their duties, particularly when the supervisory authority detects problems with an insurance undertaking which is likely to result in intervention by the scheme.

12 Member States reported the existence of a free exchange of information (without legal or other barriers) between the supervisory authority and the IGS. In some Member States such exchange is due to institutional aspects – the fact that the supervisory authority is the manager of the IGS (noted by two Member States), or the supervisor of the IGS (observed by three Member States).

Three Member States emphasized that such flow is not blocked by professional secrecy norms because the need to comply with the secrecy regime would have been communicated to the entity which receives the information. Only one Member State reported that such flow of information is based on a formal agreement.

3.2.3 Preventative measures taken by the IGS

Although no Member State reported that their IGS has powers to act on a preventative basis, a few noted that their IGS can take certain measures to enable

insurance undertakings to continue to meet their contractual obligations under certain conditions:

In IE, if the non-life insurance undertaking averaged over 70% of their business in IE, (over the three years prior to the appointment of the administrator) the Accountant of the High Court can sanction payments from the IGS to enable an administrator to carry on the business of the non-life insurance undertaking and run the business as a going concern.

In the UK, where an insolvency event has occurred or the regulator determines that the insurance undertaking cannot pay claims against it, the IGS can seek to secure continuity of cover. This can include giving assistance to the insurance undertaking to enable it to continue to effect contracts of insurance or to carry out contracts of insurance, if certain criteria are met. The criteria are that it would be generally beneficial to the eligible claims covered by the proposed assistance and, where the cost of providing assistance might exceed the cost of paying compensation, any additional cost is likely to be justified by the benefits. The IGS cannot exercise these powers on a preventative basis to keep an insurance undertaking solvent.

In conclusion, the IGSs appear to be more of a last-resort scheme, intervening only when all other measures have been exhausted, rather than competent to act on a preventative basis.

3.3 Role of the IGS during the insolvency process

3.3.1 Deciding when to intervene

When asked which authority takes the decision on when to intervene when an insurance undertaking becomes insolvent, about half of the respondents reported that this is the responsibility of the supervisory authority. However, the situation is not harmonised throughout Member States and/or sectors.

For life and non-life IGS, seven countries have reported that the supervisory authority generally decides when to intervene, when an insurance undertaking becomes insolvent. In one Member State, only the court can initiate the procedure. In another, the procedure is initiated by its IGS. One Member State also reported that either the court, the supervisory authority or the insurance undertaking can initiate the procedure.

For motor IGS, seven Member States reported that the decision to intervene is the responsibility of the supervisory authority; for five this is the responsibility of the court; for three, it is the IGS and for two Member States, the insurance undertaking[2].

3.3.2 Options for exit from insolvency e.g. schemes of arrangement or transfer of business

Although there appears to be no mechanism for exit from insolvency, six Member States noted that certain remedial measures such as a partial or total portfolio transfer may be possible. One Member State also reported that the terms of the insurance agreements can be amended.

[2] If the initiative comes from the insurance undertaking, this concerns a voluntary liquidation or a petition to the court.

3.3.3 Continuance of insurance cover

Member States were asked whether their IGS provides continued insurance coverage once the winding-up begins.

14 Member States reported that their IGS does not provide for continuance of insurance cover once the winding-up begins although one noted that portfolio transfers may have the similar effect for policyholders as their contracts would still be in place. In other Member States (nine in total), the IGS provides continuance of cover once the winding up of the insurance undertaking begins. This seems to be more prominent in the case of life business (as in the US law model) and compulsory insurance.

3.3.4 Criteria taken into account by an IGS for transferring the portfolio of a failing insurance undertaking

Few Member States reported having criteria for transferring portfolios of business. For some Member States, it falls outside the scope of their IGS to be involved in portfolio transfer. For the five Member States that reported that their IGSs may be involved in portfolio transfer, four Member States noted that various criteria must be met:

In DE, both for the life and health insurance guarantee schemes, the portfolio transfer is the solution of last resort, i.e. it is taken into account when other measures designed to safeguard the interests of the insured are deemed insufficient.

In IE, the court appointed administrator shall have all such powers necessary for their functions in relation to the insurance undertaking. This would extend to powers over portfolio transfers, albeit that any such portfolio transfer would require prior approval from the supervisory authority and the High Court.

In PL, the IGS may grant a loan to the insurance undertaking taking over the compulsory insurance portfolio of the insurance undertaking being wound up, up to the amount of technical provisions calculated in respect of the taken over insurance portfolio.

In the UK, where an insolvency event has occurred or the regulator determines that the insurance undertaking cannot pay claims against it, the IGS has duties and powers to seek to secure portfolio transfer. The objective is to protect consumers rather than insurance undertakings. The courts would exercise oversight. For life insurance undertakings the IGS must, and for general insurance undertakings the IGS may, seek to secure a transfer and also provide funds to support the transfer in cases where:

- it is reasonably practicable to secure a transfer;
- a transfer would be beneficial to policyholders; and
- where the costs exceed the cost of paying compensation, any additional cost is likely to be justified by the benefits.

3.3.5 Role of the IGS when an insurance undertaking becomes insolvent

Generally the vast majority of Member States' IGSs are either directly responsible for payment of claims (15 Member States) or for supporting or ensuring such payments

are made (two Member States), or both (one Member State). However, payment arrangements as well as other duties of IGSs when an insurance undertaking becomes insolvent vary significantly across Member States. The main differences are:

- some IGSs can either pay compensation or seek portfolio transfer;
- assessment of claims can be the responsibility of:
  - the court or the liquidators appointed by the court;
  - the insurance undertakings of the claimants; or
  - the IGS;
- the IGS may be responsible for auditing claims-assessment processes (to ensure claims are being handled effectively and/or economically);
- the IGS may grant a loan to the insurance undertaking taking over the transferred portfolio; and
- the payment may be possible only after the insurance undertaking's authorisation has been revoked by its supervisory authority.

3.3.6 Cross-border co-operation and co-ordination arrangements

Member States were asked what cross-border dimensions are taken into consideration by their IGS when an insurance undertaking is being wound up. Respondents mostly referred to the European Passport, with situations differing largely with regards to the home state or host state principle adopted.

For life and non-life IGS, most Member States concerned reported no actual or potential cross-border dimensions. Only three countries reported cross-border dimensions such as direct contact between supervisory authorities or the relationship between the IGSs.

For IGS following the host state principle, or mixed home/host principle, cross-border dimensions consist mainly of claims payments.

For motor IGS, seven Member States stated that cross-border dimensions are not taken into account besides what arises from the international nature of the coverage of compulsory motor insurance (obligation of payment irrespective of the accident location).

In its report (CEIOPS-DOC-18/09) "CEIOPS Input to the EC work on Insurance Guarantee Schemes", CEIOPS highlighted the importance of harmonising the geographical scope of an IGS, and expressed a preference for the home state principle, so that insurance undertakings are covered by the IGS in the state where the insurance undertaking was authorised. This includes the insurance undertaking's branch and service businesses throughout the EEA.

3.4 Role and interaction of other bodies with the IGS

3.4.1 Role of the supervisory authority when an insurance undertaking becomes insolvent

Member States were asked whether the supervisory authority was the competent authority for the winding-up of an insolvent insurance undertaking. Under Directive 2001/17/EC on the reorganisation and winding-up of insurance undertakings, "competent authorities" of the Member States are responsible for deciding on the commencement of winding-up proceedings.[3] The competent authorities may be judicial or administrative depending, upon Member State's legislation.

Insolvency laws and in particular insolvency procedures appear to vary quite significantly throughout Member States. Accordingly, Article 9 of the said Directive states that the decision to commence winding-up proceedings for an insurance undertaking shall be governed by the laws, regulation and administrative provisions applicable in its home state.

Responses indicated that the supervisory authority plays a pivotal role when an insurance undertaking becomes insolvent. Nine Member States reported that the supervisory authority has sole responsibility for decisions regarding re-organisational measures (transfer of portfolio, stay in payments, etc). Three Member States reported that the court's authorisation is required.

Most replies however, indicated that the liquidation procedure is judicial and governed by the courts (20 Member States), although four Member States noted that there are cases where the procedure is administrative, with the supervisory authority deciding the timing, nominating the liquidator and monitoring the merit and the legality of the proceedings.

In the case of judicial liquidation:

- in some Member States, winding-up proceedings cannot be initiated without the consent of the supervisory authority;
- the supervisory authority often has the power to advise the court on the nomination of the liquidator (noted by nine Member States);
- two Member States noted that a condition of the court issuing the liquidation decree is the supervisory authority's withdrawal of the insurance undertaking's authorisation.

Most replies also gave prominence to the role of the liquidator (administrator of the insolvency, or bankruptcy) who is responsible for the day-to-day activities of the liquidation procedure. The liquidator is appointed by the competent authorities as referred to above. One Member State emphasized the fact that the liquidation does not prevent the supervisory authority from exercising its general power/duty to supervise the insurance undertaking's activities.

The diversity of regimes across Member States indicates that any future proposal for EU harmonisation regarding IGS should leave the role of the supervisory authority to the individual Member States. However, the diversity of situations also highlights the

[3] (1) Directive 2001/17/EC See whereas clause (8): "A distinction should be made between the competent authorities for the purposes of reorganisation measures and winding-up proceedings and the supervisory authorities of the insurance undertakings. The competent authorities may be administrative or judicial authorities depending on the Member State's legislation."
(2) Note that in the Life and Non-Life directives, the supervisory authority is also referred to as 'competent authority'.

importance of addressing the issue of cross-border communication between supervisory authorities in any future directive.

3.4.2 Differences between life and non-life insurance insolvency and their treatment by the supervisory authority

Member States were also asked whether there were significant differences between life and non-life insurance undertakings with regards to the winding-up procedures and the role of the supervisory authority.

The majority (15 Member States) stated that no apparent differences existed, with a few indicating minor differences (for example one Member State observed that the court has greater powers over the continuation of life business and the terms of life insurance contracts).

The replies indicated that Member States do not generally treat the insolvency of life or non-life insurance undertakings[4] differently. There is nothing in the winding-up procedures therefore that would prevent a potential directive on IGS from addressing both sectors at the same time, and contributing to the creation of general IGSs for enhancing consumer protection and confidence in financial services.

3.5 Role of the court in winding-up proceedings

3.5.1 During winding-up proceedings

Directive 2001/17/EC on the reorganisation and winding-up of insurance undertakings sets out the provisions which must be followed by insurance undertakings that are being wound up. Article 9 of the said Directive also provides that the winding-up proceedings and their effects shall be governed by the laws, regulations and administrative provisions applicable in each home Member State unless otherwise provided in Articles 19 to 26 of the same directive. In line with this approach, it appears that most Member States referred to the general laws relating to the insolvency of companies when describing the role of the court in this question.

3.5.2 When the insolvency procedures are initiated

In most Member States, the court issues an order initiating the insolvency procedure, unless it is a voluntary winding-up procedure. Most Member States (17) reported that the role of the court is to ensure that orderly and effective insolvency procedures are in place. The court is responsible for initiating liquidation proceedings, issuing a bankruptcy decree and appointing a person responsible for the winding-up of the insurance undertaking, usually referred to in Member States' legislation as a liquidator, receiver, administrator or trustee.

Throughout the winding-up process, the court's role is mainly to monitor and supervise the process, to oversee the actions and arrangements proposed by the trustee, receiver or liquidator and to approve reports relating to the winding up. The court monitors the process and is referred to when there is disagreement or the need for direction.

[4] As recommended in our 2009 report (CEIOPS-DOC-18/09)

We note that the role of the court in winding-up proceedings as reported in the majority of responses, is akin to the US regime, with the distinction that in the US the supervisory authority (the insurance commissioner) is itself the liquidator appointed by the court.

A few Member States (four) stated that the court is not involved in winding-up procedures. One Member State reported that the court plays no role in the IGS tasks as a portfolio transfer takes place before the insurance undertaking becomes insolvent, whilst another noted that, since the process is entirely conducted by the supervisory authority, the role of the court is merely as a last resort to resolve conflicts regarding the verification, valuation, graduation and payment of claims by the liquidation procedure.

3.6 Role of the IGS in the claims process

3.6.1 Time limit for IGS pay-outs and observed payment times

Member States were asked whether there are any specific time limits for the IGS to pay claims.

Only six Member States reported having a prescribed time limit:

- In four Member States the time limit is fixed by law and in two Member States, by the supervisory authority.
- The time limit is triggered by declaration of bankruptcy, request/report of claim or end of calculation (reported by two Member States in each case).
- The time limit varies from 15 days to three months. In some cases the limit can be extended for another two or three months.

One Member State noted that the time period starts from when the liability of the insurance undertaking and the amount of the claim have been established.

Most of the Member States did not provide any information about the payment times observed. Some respondents indicated that they cannot report time limits due to no (or only a small number of) insolvency cases with the involvement of an IGS. One respondent's experience is that the timescales for winding up of insurance undertakings and payments of dividends are lengthy. Only Norway reported observed time limits from one week to three months (from when the individual claim has been regulated/adjusted by the insolvency administrator) in practice.

3.6.2 Treatment of unearned premia

Member States were asked whether their IGS treats unearned premia differently from other insurance claims.

About half of respondents reported that the treatment of unearned premia is not applicable to their IGS, as their scheme provides no cover for unearned premia, or in other cases Member States only have schemes for motor insurance which cover claims but not unearned premia.

A number of Member States treat unearned premia on equal terms with other insurance claims (six Member States) although a few treat them separately (two Member States). Two Member States reported no relevant legal provisions.

3.6.3 Funding payment of claims

Member States were asked what happens if there are insufficient funds in the IGS to pay all claimants.

Some Member States just explained the way the IGS is financed and reported caps for the coverage without giving a precise answer to the question. Others reported a range of solutions, which include a proportionate reduction of claims on a pro rata basis, full payment of all claims with additional ex post contributions by IGS members, loans (with and without state guarantee for the repayment), the ability to request borrowing from the government/other sources and additional public money. The most reported solution is additional contributions by scheme members.

3.6.4 Rights of policyholders to take IGS to court

Most Member States (15) reported that policyholders have only general legal rights to contact the IGS or to take it to court.

Five Member States with only a motor IGS stated that third party claimants/injured party/victims have those rights rather than policyholders.

3.6.5 Payment of claims upfront and reimbursement

The vast majority of IGS have the ability to pay out claims up front:

- In Member States with life, non-life or more general schemes in place, 11 out of 12 IGSs may pay out claims upfront.
- Eight Member States with an IGS exclusively for compulsory motor insurance reported that the scheme has the ability to pay out claims upfront.

However, when intervening in case of the insolvency of an insurance undertaking or in the case of a winding-up, the vast majority of IGSs have powers to pay out claims up front (in the sense that they offer payment to the clients once each claim has been established), which is in the interest of policyholders.

3.6.6 Subrogation rights of the IGS

Providing an IGS with subrogation rights allows the IGS to take over the rights of policyholders against the insurance undertaking and therefore receive recoveries against compensation payments it has made directly. A majority of respondents indicated the existence of subrogation rights (20 Member States) without commenting specifically on whether the IGS is subrogated with the same priority as direct insurance claims.

It seems appropriate for a directive to provide for IGSs to have subrogation rights.

It also appears beneficial to provide IGSs with the right to benefit from the same level of priority as policyholders (i.e. preferential treatment whereby the policyholder's claim is prioritised above most other creditors). Unless the IGS takes over the same creditor priority as held by the policyholder, it will be unlikely for the IGS to recover its compensation payments. This will increase the IGS's funding requirements. This also means that the IGS will effectively be subsidising the payment of other creditors and giving them a greater chance of getting their money back (which should not be the purpose of the IGS).

3.6.7 Other rights of the IGS including apply to the court for a winding-up order

Another important right that some IGSs may have is the right to be a member of the creditors' committee. The majority of respondents stated that their IGSs have no specific rights in this regard (13 Member States). Four Member States reported that this question is not applicable.

One Member State reported that their IGS may appoint a member in the creditors' committee, whilst another noted that the IGS has the expectation, but not the right, to have a representative as a member of the creditors' committee. In another, the IGS or other creditors may be appointed in the committee by the judge commissioner.

Four Member States noted that their IGSs have general/standard rights in their capacity as creditors of an insurance undertaking (e.g. to be a member of the creditors' committee, to present proposals, to file petitions against decisions of creditors meetings, to be heard by the court and to file appeals against court decisions).

3.6.8 Rights of creditors

Six Member States reported that creditors have rights to be heard by the court.

4. Conclusions

The findings of the report highlight the lack of harmonisation in a number of areas such as:

- which authority takes the decision to intervene when an insurance undertaking becomes insolvent;
- the ability to provide for portfolio transfer;
- a lack of pre-warning system when an insurance undertaking is in difficulty; and
- the role of the supervisory authority when an insurance undertaking becomes insolvent.

Overall the report highlights the diversity of regimes across Member States and the importance of cross-border communication between Member States. The report also illustrates how Member States have exercised their discretion in implementing Directive 2001/17/EC on the reorganisation and winding-up of insurance undertakings to fit with their legal and institutional framework. This points to the potential need for any future directive on IGS to provide Member States with sufficient flexibility to adapt the directive's requirements to fit with their national framework.