

IDENTIFICATION OF CRITICAL FUNCTIONS

Fourth event in IRRD series of online events with stakeholders

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AGENDA

1. Introductory remarks
2. On the identification of critical functions
3. On the assessment of the likelihood of a significant impact
4. On the assessment of substitutability
5. Q&A

1. INTRODUCTORY REMARKS

- The identification of critical functions is an important part of **resolution planning**.
- In essence, critical functions inform the **scope** of resolution planning as well as the outcome of the **Public Interest Assessment (PIA)**
- One of the resolution objectives is **to ensure the continuity of the critical functions** of a failing/likely to fail undertaking, while protecting the collective interest of policyholders, beneficiaries and claimants
- Critical functions are identified in view of the **impact** on the stability of the financial system and the functioning of the real economy as well as of the **substitutability** of the function
- Connection with other aspect of the IRRD elements and planning requirements
- This presentation will provide you with some initial ideas related to EIOPA's work related to these topics

2. ON THE IDENTIFICATION OF CRITICAL FUNCTIONS

- The approach taken builds on the **definition of critical functions** in **Art. 2(25) of the IRRD**.

(25) ‘critical functions’ means activities, services or operations performed by an insurance or reinsurance undertaking for third parties that cannot be substituted within a reasonable time or at a reasonable cost, and where the inability of the insurance or reinsurance undertaking to perform the activities, services or operations would be likely to have a significant impact on the financial system or the real economy in one or more Member States including, in particular, the impact resulting from effects on the social welfare of a large number of policy holders, beneficiaries or injured parties or from a systemic disruption or a loss of general confidence in the provision of insurance services;

2. ON THE IDENTIFICATION OF CRITICAL FUNCTIONS (2)

- Related work of international bodies such as the International Association of Insurance Supervisors (IAIS) and the Financial Stability Board (FSB) is also being considered. **While the approaches are different, they are consistent in defining the same concept.**
 - The identification of critical functions is the responsibility of the resolution authority.
 - The resolution authority performs the assessment of criticality based, inter alia, on national specificities and information provided by the insurance undertakings.
 - Relevant issues to be considered in the criteria for identifying critical functions:
 - *Need to adapt to the **realities of the insurance sector***
 - *Application to **individual** insurance undertakings*
 - *Additional elements: activities, services or operations provided to **third parties***
 - *Geographical dimension: **national, regional, Union level***
- Not to consider:** IGS, national insolvency proceedings and/or Public funds

3. ON THE ASSESSMENT OF THE LIKELIHOOD OF A SIGNIFICANT IMPACT

Specific requirements for the assessment of the likelihood of a significant impact on the financial system or the real economy (impact analysis), in particular:

- This impact would likely be **significant** and would likely be affecting **one or more Member States**
- The impact on the financial system or the real economy is driven by the **inability of the insurance or reinsurance undertaking to perform the function**
- **Concrete aspects include:**
 - No new business is written for certain risks
 - Certain coverage(es) is/are no longer provided
 - No payments are made to certain policyholders, beneficiaries, claimants
 - No new investments and loans into certain entities are made and that existing investments are immediately sold or called in
- **Impact considered as:**
 - Direct impact on third parties: e.g. a reduction in the level of activities and in the ability to meet obligations.
 - Contagion from third parties to which the function is provided to other parties in the financial system or the real economy.

3. ON THE ASSESSMENT OF THE LIKELIHOOD OF A SIGNIFICANT IMPACT (2)

- **Some factors to consider for the assessment whether a significant impact on the real economy or the financial system is likely**
 - The characteristics of the function
 - The type and number of third parties to which the function is provided
 - The geographical level at which the function is provided
 - The impact of the disruption of the function on the third parties to which it is provided
- Furthermore, the impact is identified based on whether it results from:
 - a) *effects on the **social welfare** of a large number of policyholders, beneficiaries or injured parties*
 - b) *a **systemic disruption** or*
 - c) *loss of **general confidence** in the provision of insurance services;*

4. ON THE ASSESSMENT OF SUBSTITUTABILITY

- **Specific requirements for the analysis of the substitutability at a reasonable cost and in a reasonable time:**
 - The reasonability of the costs and of the time are assessed by the resolution authority.
 - Reasonable time for substitution depends on the the speed with which the inability to perform the function impacts the real economy or the financial system and on the magnitude of the impact
- **Factors guiding the assessment of the substitutability of a function (list not exhaustive):**
 - The nature and features of the function and properties of the market for the function
 - Appetite and ability of other market participants to provide the same or similar function to the third parties
 - Obstacles to the provision of activities
 - Nature of the failure of the undertaking impacting the availability of any replacing entities to provide the function
- **Some additional considerations:**
 - Type of product/coverage: e.g. in case savings products
 - Financial strength of the potential counterparty: e.g. non-insurance/non-financial entity, reinsurance etc.

5. Q&As



Your turn...



THANK YOU!

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