Issues Paper on roles and functioning of policyholder protection schemes (PPSs)

Public Discussion Session

Alex Hart, Chair of the Resolution Working Group (ReWG)
16 January 2024, 14:00-15:30 CET

Background

- Issues Paper on roles and functioning of policyholder protection schemes (PPSs) was published on 14 December 2023.
- The paper was developed as a follow-up to Issues Paper on Policyholder Protection Schemes published in October 2013, in light of subsequent developments such as the adoption of revised Insurance Core Principles (ICPs) and Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame) in November 2019.
- Public consultation took place from February 2023 – April 2023.
- 204 comments were received from external stakeholders and IAIS members. The paper was updated to reflect the comments. All comments received and IAIS' responses are available on the IAIS website.

Objectives of the Issues Paper

- The paper provides an updated overview of global practices regarding PPSs, their roles in insurance resolution, and related activities.

- It is also intended to serve as a guide for jurisdictions considering establishing a PPS or modifying an existing PPS.

- The paper is not meant to set new standards related to PPSs.

Contents of the Issues Paper

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1	Introduction
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3	Coverage
4	Funding
5	Disclosure and communication
6	Cooperation and coordination
7	Other policyholder protection mechanisms
Annex	Consideration of how and whether the existence of PPSs could affect behaviour

Section 1 - Introduction

- Section 1 defines the general objectives of PPSs and offers advice about reading the paper including an explanation of some related terms.

- According to 30 IAIS member answers to an early 2022 survey, PPSs are commonly:
  - Established by legislation;
  - Designed to protect life and/or non-life policyholders – particularly individuals and small businesses;
  - Part of a suite of strategies used to resolve failing insurers; and
  - A mechanism of “last resort”.

Section 2 - Roles of PPSs in recovery and resolution

- Section 2 describes the roles of PPSs in recovery and resolution of insurers, and the difference between PPSs and resolution funds.

- PPSs typically seek to meet commitments a failing insurer has made to its policyholders. This is done by:
  - Paying policyholder claims (by stepping in to support run-off or establishing a bridge institution to facilitate direct payment); or
  - Covering a shortfall in capital or liquidity to aid a compulsory transfer or bail-in.

- PPSs are mostly triggered in insolvency and resolution. In a few jurisdictions, they are also used in recovery.

Section 3 - Coverage

- Section 3 discusses issues of coverage, including considerations relevant to the determination of the scope, limits and other design features of a PPS; as well as issues relating to cross-border cooperation and coverage.
- PPS cover can vary, notably in terms of amounts, eligible policies, eligible policyholders and/or geographical scope. Eligible policies are frequently defined with reference to lines of business (LoBs).
- It is important to calibrate levels & limits of coverage to the importance of classes & vulnerability of policyholders. PPSs should respond quickly to meet immediate expenses, addressing the specific circumstances of the event.
- In the case of cross-border failures, some PPSs employ the home jurisdiction principle, whereas others use the host principle in determining scope of protection.

Section 4 - Funding

- Section 4 discusses practices for PPS funding, such as different sources and methods of funding, and methods to determine levies on insurers.
- It is important that a PPS has adequate and readily available funds. It should have funding mechanisms for prompt settlement of obligations or any assumption of contracts.
- There are several ways to fund a PPS: mainly, collect contributions from insurers and/or apply a surcharge to policyholders. PPSs are most often funded by insurers. Where this is the case, levies on insurers are typically based on the volume of their business, and sometimes on their and/or risk profile. PPS funding can take place before (ex ante), after (ex post), or partly before and partly after an insurer failure.

Section 5 - Disclosure and communication

- Section 5 discusses communication relevant to PPSs, both in business-as-usual conditions, and in crisis. Disclosure and communication about PPSs can promote financial stability and support confidence in the insurance sector.

- Public communication about PPSs should be proportionate to the risk it seeks to manage and explain who is eligible and the extent of cover. It can also list the subscribing insurers. It should build credibility with key stakeholders, including insurers, policyholders and intermediaries.

- Reach is most effective when a range of channels and strategies are used (eg public websites, advertisements, awareness raising campaigns, annual public surveys and social media).

Section 6 - Cooperation and coordination

- Section 6 discusses the need for cross-border cooperation and coordination in crises.
- Cooperation and coordination are essential whether in business-as-usual conditions or in a crisis. This is especially so between PPSs that apply to the same insurer(s), and between PPSs, supervisors and resolution authorities. The PPS’s actions should support the resolution authority’s aim to protect policyholders.
- Jurisdictions particularly report the value of early coordination; clear roles and responsibilities; and formal mechanisms to facilitate sharing and safeguarding of confidential information.

Section 7 - Other policyholder protection mechanisms

- Section 7 discusses other mechanisms to protect policyholders in the event of an insurer failure, including:
  - “preferred claims” (accorded priority payment from the insurer’s assets under the jurisdictions’ applicable law);
  - “tied assets” (where insurers are required to hold assets to cover all technical reserves plus a potential surcharge); and
  - “segregated assets” (where insurers are requested to hold segregated funds for specific types of insurance business or specific policies).

- Distinctions between these mechanisms are not always straightforward as their definitions and features vary across jurisdictions.

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Questions?

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Thank you