ITFA IS PLEASED TO SHARE THE LATHAM & WATKINS MEMORANDUM OF ADVICE IN RELATION TO CREDIT RISK INSURANCE, May 2024

The memo was commissioned by the ITFA Insurance Committee to support the EBA with its report to the European Commission on credit risk insurance and the industry's ongoing regulatory advocacy efforts to see a better capital treatment for credit insurance used as eligible credit risk mitigation under Basel III.

The memo details the key characteristics of credit risk insurance. Specifically, it highlights the indemnity nature of the payment obligation provided by the Insurer, which is triggered by the occurrence of a Non-Payment and it is a primary obligation to pay the loss amount sustained by the Lender. In addition, it highlights the following:

> *"(a) Credit Insurance Policies provide Lenders with direct indemnity protection and afford dual recourse rights in respect of the covered losses. The purchase of credit insurance and the receipt of claim payments under credit insurance do not interfere with the bank's rights under the Insured Agreement either by reducing the amount of recourse the bank has to the defaulting borrower or counterparty or by extinguishing the rights of the bank to the defaulting borrower or counterparty under the Insured Agreement;*
>
> b. *the requirements of the Solvency II regime differentiate Solvency II insurers from other types of corporate debtors by materially reducing the risk of non-recovery of claims from such regulated entities in light of the robust regulatory framework provided;*
>
> c. *creditors with claims under products which are insurance policies, or which derive from operations regulated as insurance business (such as Lenders who are insureds under Credit Insurance Policies) enjoy a beneficial statutory priority regime, which provides further protection in the event that a Solvency II insurer does end up in financial difficulties."*

The characteristics highlighted in the L&W memo serve to demonstrate why credit risk insurance as a product provided by certain solvency regulated insurers should attract a more appropriate LGD than 45%.

Click here to view the memo.

Our sincere thanks to Howden, Liberty, WTW and Texel for their involvement in the project.