Insurance & Reinsurance

Contributing editors
William D Torchiana, Mark F Rosenberg and Marion Leydier

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GETTING THE DEAL THROUGH

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Getting the Deal Through is delighted to publish the tenth edition of *Insurance & Reinsurance*, which is available in print, as an e-book and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes China, Ireland and a new article on the GDPR.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, William D Torchiana, Mark F Rosenberg and Marion Leydier, of Sullivan & Cromwell LLP, for their continued assistance with this volume.

GETTING THE DEAL THROUGH

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Introduction

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The regulatory landscape for insurance companies has undergone significant change since the global financial crisis of 2007–2008. In the US, the individual states have begun implementing various regulatory and legislative changes that will continue to fundamentally affect the operations of large international insurance groups. At the US federal level, the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010 (Dodd-Frank Act) introduced a new era of federal regulation of certain areas of insurance in the US, although the future of many aspects of the Dodd-Frank Act remains uncertain under the new Trump administration and the Republican-controlled Congress. The prudential regulation of insurance and reinsurance companies across the EU is undergoing significant change under the Solvency II Directive, which came into effect on 1 January 2016 and affects both European and non-European insurance groups with operations in the EU. It remains to be seen how the UK's exit from the European Union (Brexit) will affect the UK's insurance industry and regulatory environment. In addition, standards and policy measures under development internationally by the Financial Stability Board (FSB) and the International Association of Insurance Supervisors (IAIS), once finalised and implemented, are expected to have significant implications on the regulatory framework applied to international insurance groups. As the legal environment is likely to continue to be in a state of flux for several years to come, it will be critical for practitioners who provide corporate and transactional advice to stay abreast of the latest developments with respect to the US and international insurance regulatory schemes.

Significant developments at the US state level

Historically, the insurance industry in the US has been regulated almost exclusively by the individual states. Every state has a comprehensive body of statutes, regulations, accounting principles and actuarial guidelines that govern virtually every aspect of an insurance company's operations, including licensing, capital and reserve adequacy, permitted investments, transactions with affiliated companies and reinsurance. At its core, the insurance regulatory framework in the US is designed to protect insurers and their policyholders from risk in other parts of the insurer's holding company group by subjecting individual insurers to stand-alone capital requirements based on statutory accounting principles, and imposing significant capital and asset mobility constraints and other regulatory protections. These laws are generally aimed at insulating state-regulated insurers from contagion by affiliates, whether they are domiciled in the US or in foreign jurisdictions.

Beginning in 2008, US insurance regulators, through the National Association of Insurance Commissioners (NAIC), began reviewing lessons learned from the financial crisis and, specifically, studied the case of American International Group (AIG) and the potential impact of non-insurance operations on insurance companies in the same group. At the heart of the lessons learned from the 2007–2008 global financial crisis was the need for insurance regulators to be able to assess the enterprise risk within a holding company system, both nationally and internationally, and its potential impact on insurers within that group.

US states have made significant progress in the past few years in adopting the latest revisions to the NAIC model insurance holding company act, which provides state insurance regulators with new group-wide supervisory tools, including a new enterprise risk report that insurance holding companies will be required to submit at least annually. The enterprise risk report, to be filed with the lead state commissioner of the holding company system, must identify the material risks within the holding company system that could pose enterprise risk. Another new group solvency initiative being implemented at the individual US state level is the own risk and solvency assessment (ORSA), which requires large and medium-sized US insurance groups to conduct at least annually an internal assessment of the material and relevant risks associated with the insurer's or insurance group's current business plan, and the sufficiency of capital resources to support those risks. In addition, many states have adopted legislation authorising the establishment of supervisory colleges. A supervisory college is a convention comprising the principal insurance regulators of a specific insurance group that meets periodically to facilitate cooperation and exchange of information on a group-wide basis among regulators, as a complement to the supervision of individual entities within a group. Requirements to prepare and submit an ORSA and establish supervisory colleges have also been developed under Solvency II and the standards proposed by the IAIS.

The NAIC is also in the process of developing a group capital calculation for US insurance groups. The approach the NAIC has recommended and plans to develop would be an aggregation methodology that utilises existing state-based capital calculations (ie, risk-based capital) for US-domiciled insurance companies; the standards to be used for calculating capital for entities without existing capital requirements remain a topic of debate. In any event, the NAIC has made clear that its intention is to develop a group capital assessment as opposed to any group-level capital requirement.

Notwithstanding the significant state-based developments in the area of group-wide supervision, the NAIC and state regulators are unlikely to completely jettison the solo entity ring-fencing principle, which has been a cornerstone of policyholder protection in the view of the NAIC and state regulators. Rather, the NAIC has advocated for a 'windows and walls' approach, whereby new group-wide supervisory powers will enable state insurance regulators to collect information on activities throughout the holding company system, thereby providing both 'windows' to assess group activity and risks, and the ability to 'wall' off insurance capital from any non-insurance activities of the group that are deemed to be risky. The Solvency II Directive and group-supervision proposals published by the IAIS, however, are premised on mechanisms for direct, consolidated group-level supervision. Debate as to the right approach to group-wide supervision of insurers is likely to continue, creating uncertainty for marketplace participants as to the regulatory landscape that will apply to insurance companies operating in multiple jurisdictions.

The NAIC and US state and federal regulators have continued to focus on the use of captive reinsurance vehicles by insurance companies. In recent decades, US insurers have been using captive reinsurance vehicles and various financing structures with counterparties in order to ease the capital burdens associated with statutory reserve requirements for certain types of life and annuity contracts. In December 2012, the NAIC approved a new valuation manual containing a principle-based approach to life insurance company reserves. Principle-based reserving (PBR) is designed to tailor the reserving process to specific products in an effort to create a principle-based modelling approach to reserving rather than the factor-based approach historically employed. PBR became effective on 1 January 2017. The adoption of PBR, along with other changes to actuarial guidelines and credit for reinsurance regulations adopted by the NAIC, are intended to eventually eliminate, or

at least diminish, the need for insurers to employ captive reinsurance vehicles and other reserve financing structures.

Finally, the states and the NAIC are beginning to address regulatory approaches relating to cybersecurity (an area in which the US federal government is also increasingly involved), and the burgeoning field of so-called Insure-Tech (a subset of FinTech encompassing a variety of emerging technological and other innovations that have begun to disrupt the traditional methods of insurance marketing, underwriting and claims servicing).

Significant developments at the US federal level

At the US federal level, the Dodd-Frank Act established the Federal Insurance Office (FIO) to monitor the insurance industry and identify gaps in regulation that could contribute to a systemic crisis, and granted the Board of Governors of the Federal Reserve System (Federal Reserve) significant regulatory powers over systemically important insurers and other insurers that are affiliated with an insured depository institution. As a result of the Dodd-Frank Act, the insurance holding companies for which the Federal Reserve is the consolidated supervisor hold approximately one-third of US insurance industry assets, according to Congressional testimony by the Federal Reserve. Other provisions of the Dodd-Frank Act have affected, or may affect, the management and operations of insurance groups, including new regulations on swaps, securities laws reforms, and the establishment of a new orderly liquidation authority (which, though generally not available to resolve insurance companies, may be applied to resolve insurance holding companies or their non-insurance subsidiaries). In addition, the promulgation by the Department of Labor (DOL) of new fiduciary investment advice rules in April 2016 would lead to significant changes in the way financial services providers sell financial products (including fixed and variable annuities) and provide investment advice to retirement plans and IRAs. The DOL's fiduciary rule remains controversial and the current US administration has delayed its effective date; the current rule may be replaced or possibly repealed.

Federal Reserve supervision of certain insurance groups

Until the enactment of the Dodd-Frank Act, the Federal Reserve and other federal banking agencies generally only had regulatory authority over insurance groups to the extent an insurance group owned a bank or a savings and loan company, with the parent company qualifying as a bank holding company (BHC) or savings and loan holding company (SLHC) (several insurance groups currently qualify as SLHCs, although there are currently no insurance-based BHCs). The Financial Stability Oversight Council (FSOC), established pursuant to the Dodd-Frank Act and composed of federal financial regulators, state regulators, and an independent insurance expert appointed by the president, has the authority to designate an insurance group as a systemically important financial institution (SIFI) to be subject to enhanced prudential standards and supervision by the Federal Reserve. The FSOC designated two US insurers – AIG and Prudential Financial – as SIFIs in 2013, and designated a third insurer, MetLife, in 2014. As permitted by the Dodd-Frank Act, MetLife challenged its SIFI designation in federal district court. On 30 March 2016, the district court agreed (in part) with MetLife's grounds and rescinded the designation. The FSOC has appealed that decision and the appeal is pending. SIFI designations are subject to an annual re-evaluation process conducted by the FSOC.

Accordingly, insurance-based SIFIs and SLHCs are now subject to supervision and examination by the Federal Reserve, with insurance-based SIFIs being subject to additional 'enhanced prudential standards' for which the Federal Reserve is required to establish regulations pursuant to Title I of the Dodd-Frank Act. The enhanced prudential standards include, or will include, requirements and limitations relating to risk-based capital, leverage, liquidity, stress testing, risk management, resolution planning, early remediation, management interlocks and credit concentration, and may also include additional standards regarding capital, public disclosure, short-term debt limits and other related subjects at the discretion of the Federal Reserve and the FSOC. Many of the enhanced prudential standards would apply to already-existing state insurance statutes that govern the activities of insurance holding companies. For example, acquisitions of insurance companies will require not only the approval of domiciliary state regulators, but, depending on the nature of the transaction, may also require approval by the Federal Reserve and the satisfaction of conditions set forth in the Bank Holding Company Act. Likewise, the investments permitted by insurers under state laws may also need to comply with additional (yet-to-be-promulgated) requirements respecting credit concentration limits.

The Dodd-Frank Act authorises the Federal Reserve to tailor its application of enhanced prudential standards to different companies on an individual basis or by category, and the Federal Reserve has stated that it intends to take into account the differences between bank holding companies and non-bank SIFIs, including insurance companies, when applying the enhanced prudential standards required by the Dodd-Frank Act. How the Federal Reserve might ultimately apply the prudential standards to federally supervised insurance-based groups is unclear. Many in the US insurance industry were initially concerned that the Federal Reserve might apply a 'bank-centric' model with respect to capital and leverage requirements. In response to this concern, in December 2014 Congress enacted the Insurance Capital Standards Clarification Act of 2014, which provides that, in establishing the consolidated minimum leverage and risk-based capital requirements mandated under the Dodd-Frank Act, the federal banking agencies shall not be required to include (including for purposes of consolidation) entities regulated by a state or foreign insurance regulator to the extent such entities are acting in their capacity as regulated insurance entities. This act was an important step in clarifying the Federal Reserve's ability to deviate from a bank-centric capital framework with respect to consolidated risk-based capital and leverage requirements for insurance groups subject to its supervision.

The majority of the enhanced prudential standards have yet to be finalised for insurance-based SIFIs. In June 2016, the Federal Reserve issued proposed rules applicable to insurance-based SIFIs relating to enhanced prudential standards for risk management, corporate governance and liquidity risk management, and issued a conceptual proposal outlining two potential approaches to capital standards: a 'building-block approach' that would be applicable to insurance-based SLHCs and be largely based on existing state and foreign capital rules, and a potentially more onerous 'consolidated approach' that would be applicable to insurance-based SIFIs.

Based on early indications from the Trump administration and Republican proposals in Congress, the current insurance-based SIFIs may be de-designated under the new administration. Moreover, the designation and supervisory powers of the FSOC and Federal Reserve over non-bank financial institutions under the Dodd-Frank Act could be circumscribed and perhaps even repealed. Until such changes occur, and depending on future rule-making by the Federal Reserve and the extent to which the Dodd-Frank Act is replaced or modified, the regulatory landscape applicable to an insurance-based SIFI or SLHC will continue to be significantly different from that applicable to other US insurers, and any transaction that involves such entities will need to be assessed in light of the federal supervisory framework applicable to them.

FIO and the covered agreement

While the FIO has no general supervisory or regulatory authority over the business of insurance, it is authorised to coordinate and develop federal policy on prudential aspects of international insurance matters. In particular, the FIO has taken a primary role in representing the US government within the IAIS. In December 2013, the FIO released its 'modernisation' report, which includes 27 recommendations for modernising insurance regulation in the US, most of which relate to 'near-term' state-based reforms respecting capital adequacy and solvency, reserving requirements and captive reinsurers, as well as marketplace regulation. The FIO modernisation report suggests there may be a basis for federal involvement if the states fail to accomplish reforms in the near term. State insurance departments, through the NAIC, will likely continue to support the creation and implementation of more uniform laws across the states in order to prevent such federal intervention and maintain the current state-based system.

The FIO is authorised under the Dodd-Frank Act to assist the Secretary of the Treasury (Treasury) in negotiating 'covered agreements' with foreign governments and regulators. A 'covered agreement' is a written bilateral or multilateral agreement regarding prudential measures with respect to the business of insurance or reinsurance that: (i) is entered into by the US and one or more non-US governments and (ii) relates to the recognition of insurance prudential

measures that achieves a level of protection for insurance consumers that is substantially equivalent to the level of protection achieved under state insurance regulation. In November 2015, the FIO began working with the US Trade Representative and Treasury to negotiate a 'covered agreement' with the EU intended to address group supervision and reinsurance regulation in connection with achieving 'equivalence' between the US insurance regulatory regime and Solvency II. On 13 January 2017, the US and EU announced they had successfully concluded negotiations on a covered agreement and the agreed text was submitted to the appropriate committees of Congress, starting a 90-day review period required by the Dodd-Frank Act. The 90-day period has expired and it is not clear yet what position the new US administration will take on the agreement, and whether it will take the steps necessary to have the agreement enter into force from the US perspective. Some industry participants and the NAIC are opposed to the agreement in its current form, while other industry participants favour the current agreement.

Subject to certain exceptions and qualifications, the agreement provides that US-based insurance groups will be supervised at the worldwide group level only by their relevant US insurance supervisors, and that such insurance groups will not have to satisfy EU group capital, reporting and governance requirements for the worldwide group. Under the covered agreement, the EU must apply these group supervision terms provisionally until the date of entry into full force of the agreement. The agreement also seeks to impose equal treatment of US and EU-based reinsurers that meet certain financial strength and market conduct conditions. In the US, once fully implemented, the agreement requires US states to lift reinsurance collateral requirements on qualifying EU-based reinsurers and provide them equal treatment with US reinsurers or be subject to federal pre-emption. In the EU, the agreement requires national authorities in the EU to lift local presence requirements that have been recently applied to US-based reinsurers doing business in certain EU member states. The reinsurance provisions of the agreement are subject to various implementation and application timetables in the US and EU.

International insurance regulatory developments

Developments in the US relating to group supervision and regulatory capital requirements for insurance companies are occurring in parallel with the development by the FSB and IAIS of new global standards applicable to such institutions. The standards and policy measures proposed by the IAIS discussed below would, once finalised and to the extent implemented into local law, significantly impact the regulatory framework applicable to international insurance groups. At the present time, however, the manner and timing of implementing the IAIS's insurance regulatory reforms in the US remain uncertain, as does the extent to which the IAIS's capital and other regulatory standards and rules will complement, supplement or otherwise conflict with those developed pursuant to the Dodd-Frank Act and the NAIC's solvency modernisation initiatives. A number of practical issues will also need to be resolved, including how measures applicable to 'global systemically important insurers' (G-SIIs) would apply to an entity supervised by a body that is not a member of the FSB (such as a state insurance regulator, rather than the Federal Reserve), which may become an issue to the extent that insurers or reinsurers that may not be designated as SIFIs under the Dodd-Frank Act are designated as G-SIIs.

Many of the IAIS's proposals for the insurance sector remain controversial among the US insurance industry, members of Congress, state regulators and the NAIC, particularly with respect to proposed regulatory capital standards, which are viewed by some as favouring a European, 'going-concern' approach to solvency issues over the 'gone-concern' approach used by US state regulators. A perceived lack of transparency in the decision-making processes of the IAIS and FSB has also been a source of criticism by members of Congress, the NAIC and industry.

The FSB and IAIS

The FSB consists of representatives of national financial authorities of the G20 nations, various international standard-setting bodies (including the IAIS), as well as the International Monetary Fund (IMF) and the World Bank. The US members of the FSB include the Federal Reserve, the Securities and Exchange Commission and the Treasury Department. The G20, the FSB and related governmental bodies have developed proposals to address issues such as financial group supervision, capital and solvency standards, systemic economic risk, corporate governance, effective resolution regimes, and related issues associated with responses to the financial crisis. FSB member nations agree to undergo periodic peer reviews assessing the soundness and stability of members' financial systems and their implementation of proposed financial regulatory reforms, which are generally conducted by means of the Financial Sector Assessment Program (FSAP) reports prepared by the IMF or World Bank.

The IAIS is a voluntary membership organisation of insurance supervisors and regulators from more than 200 jurisdictions in nearly 140 countries. US members of the IAIS include the FIO, the NAIC, state insurance regulators and the Federal Reserve. While the policy measures and financial reforms promulgated by the IAIS and the FSB have no legal force unless enacted at the national level, the relevant national financial authorities of members' jurisdictions are expected to implement and enact the policy measures and financial reforms agreed by the FSB and IAIS.

IAIS three tiers of supervision

The IAIS has developed three tiers of supervisory requirements and actions applicable to the insurance industry:

- insurance core principles (ICPs): initially published in 2011 and periodically revised since then, the ICPs apply to the supervision of all insurers and insurance groups, regardless of size or systemic importance;
- the common framework (ComFrame): the latest full draft of ComFrame was issued in September 2014 and applies to the cross-border supervision of 'internationally active insurance groups' (IAIGs); and
- G-SII policy measures: published in July 2013, these policy measures only apply to insurance groups designated as G-SIIs.

ICPs

ICPs are structured to allow a wide range of regulatory approaches and supervisory processes to suit different markets, and cover a broad range of topics, encompassing, among many other topics, supervisor responsibilities, confidentiality, licensing, change in control, risk management, enforcement, resolution and capital adequacy. The IMF issued an FSAP report in March 2015 assessing the observance by US regulators of the ICPs, which found a 'reasonable level of observance' of the ICPs in the United States, but criticised a lack of compliance with certain ICPs and recommended more federal government involvement in US insurance regulation.

ComFrame

At the direction of the FSB, the IAIS is developing ComFrame as a model framework for the supervision of IAIGs that contemplates 'group-wide supervision' across national boundaries. The IAIS is seeking to promote the financial stability of IAIGs by endorsing:

- uniform standards for insurer corporate governance and enterprise risk management;
- a framework for group capital adequacy assessment that accounts for group-wide risks;
- additional regulatory and disclosure requirements for insurance groups;
- requirements to conduct group-wide risk and solvency assessments; and
- the establishment of ongoing supervisory colleges.

ComFrame is scheduled to be finalised and adopted in 2019, and will be subject to revision through prior field testing and confidential reporting. ComFrame is concerned primarily with the ongoing supervision of IAIGs, and is not focused on whether an insurance group is systemically important or on how to reduce the systemic risk of insurers (which is the focus of the G-SII Policy Measures and related assessment methodologies). An IAIG is defined as a large, internationally active group that includes at least one sizeable insurance entity. The IAIS does not intend to develop a definitive list of IAIGs, but has proposed quantitative criteria for national supervisors to assess on a regular basis whether they should apply ComFrame to an insurance group. It is estimated that approximately 50 to 60 firms from around the world would qualify as IAIGs under the current proposed criteria, including all designated G-SIIs.

In connection with ComFrame, the IAIS is in the process of developing a risk-based global insurance capital standard (ICS) applicable to all IAIGs. The first public consultation draft for the ICS was published by the IAIS in December 2014. As with ComFrame, the ICS is scheduled to be finalised and adopted by the IAIS in late 2019, although there are indications that the ICS may not be fully developed and implemented by that time.

G-SIIs

G-SIIs are defined by the FSB and the IAIS as insurers whose distress or disorderly failure, because of their size, complexity and interconnectedness, would cause significant disruption to the global financial system and economic activity. The FSB, in consultation with the IAIS and national authorities, designates G-SIIs on an annual basis each November. The most recent set of G-SII designations (in November 2016) includes nine life and composite insurers (three of which are US-based: AIG, Prudential Financial and MetLife). The FSB and the IAIS have yet to designate any reinsurers as G-SIIs, and the FSB has indicated that such designations will be delayed for the near future pending further assessment.

G-SII designations are based on an assessment methodology developed by the IAIS, which is subject to review and revision every three years. The IAIS issued an updated G-SII assessment methodology in June 2016. Drivers of systemic importance under the IAIS's most recent assessment methodology include size, global activity and substitutability (each receiving 5 per cent risk weightings), with 'asset liquidation' (roughly 36 per cent) and interconnectedness (roughly 49 per cent) representing the remaining and primary assessment drivers (each of which contain sub-elements focused on potentially systemic insurance product features, which the IAIS formerly analysed and referred to under the now-abandoned concept of 'non-traditional/non-insurance' (NTNI) activities). In February 2017, the IAIS announced the adoption of a three-year systemic risk assessment and policy workplan expected to be finalised by year-end 2019, which will focus on developing a macroprudential activities-based approach to regulating systemic risk.

The G-SII policy measures promulgated by the IAIS and endorsed by the FSB include:

- enhanced group-wide supervision, with group-wide supervisors to have direct powers over holding companies and the power to impose restrictions and prohibitions on certain activities (eg, to limit or eliminate systemically important activities or limit the use of affiliate reinsurance for NTNI lines of business);
- enhanced capital standards, including basic capital requirements (BCR) and higher loss absorption capacity requirements (HLA), which apply to all group activities, including those of non-insurance subsidiaries; the BCR is intended to serve as the initial foundation for the application of HLA requirements; the various capital standards and requirements are currently expected to be implemented in late 2019, and the IAIS envisages that the ICS will eventually replace the BCR as the foundation for HLA;
- systemic risk management plans: group-wide supervisors are to oversee the development by G-SIIs of plans for managing, mitigating and possibly reducing systemic risk;
- enhanced liquidity planning and management: group-wide supervisors are to require a regular gap analysis of liquidity risks and adequacy of available liquidity resources under normal and stressed conditions; and
- effective resolution regimes: the FSB has developed a document entitled the 'Key Attributes of Effective Resolution for Financial Institutions', which sets forth the key features of resolution regimes that should be applied across jurisdictions to systemically significant financial institutions; the IAIS has developed an annex to this document that outlines the key attributes that are intended to apply to the resolution of G-SIIs.

Under the insurance-sector specific elements of the Key Attributes, G-SIIs will be expected to develop and prepare recovery and resolution plans to be submitted to their group-wide supervisors on an annual basis. In addition, 'crisis management groups' are expected to be established that will include the relevant supervisory authorities, central banks, resolution authorities, finance ministries and guarantee fund authorities of each G-SII, as a forum for relevant regulators to discuss enhancing preparedness for the potential failure of the G-SII. Moreover, resolvability assessments are to be conducted by the home authority and crisis management group of each G-SII to assess the feasibility of the G-SII's resolution strategies. Finally, institution-specific cross-border cooperation agreements are to be developed and entered into among the G-SII's relevant resolution authorities.

Solvency II

Solvency II is a European Union directive (enacted in 2009) that is intended to codify and harmonise EU insurance regulation. Solvency II became effective, and its full implementation began, in January 2016. Solvency II is based on three pillars of enhanced regulation:

- pillar 1 addresses quantitative measures to ensure insurance firms are adequately capitalised with risk-based capital, including requirements relating to technical provisions (ie, reserves) and solvency capital and minimum capital requirements;
- pillar 2 addresses qualitative measures, governance, risk management and supervisory interaction, including a requirement that firms conduct an ORSA; and
- pillar 3 covers enhanced supervisory reporting and public disclosure requirements.

Solvency II also contains provisions designed to strengthen the supervision of insurance groups, including establishment of colleges of supervisors and the imposition of group-based capital requirements in addition to capital requirements for individual insurers. As group supervision may include groups headquartered in non-EU jurisdictions, or include subsidiaries of an EU-based group located in non-EU jurisdictions, Solvency II permits group solvency and capital calculations to take account of local capital standards and requirements in

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relevant non-EU countries where members of the group are domiciled, provided the supervisory regime of the non-EU jurisdiction involved has been assessed as 'equivalent' by the European Commission, or (absent an equivalence assessment by the European Commission) the relevant EU group supervisor has undertaken its own equivalence assessment or has applied 'other methods' to ensure appropriate supervision. In the absence of equivalence, the relevant non-EU insurer will be consolidated with the group's EU operations for purposes of applying the Solvency II minimum capital and solvency requirements. Solvency II also permits equivalence decisions regarding the regulation of reinsurance, ie requirements applicable to non-EU reinsurers reinsuring risks in the EU. Although to date the US supervisory regime has not been assessed as fully equivalent, the European Commission's third country equivalence decisions adopted in June 2015 granted the US insurance regulatory regime, as well as the regimes in certain other countries, provisional equivalency for a period of 10 years with respect to the 'solvency calculation' area of Solvency II (but not the 'group supervision' or 'reinsurance' areas). This provisional equivalence will allow EU insurers with subsidiaries in the US to use local rules, rather than Solvency II rules, to carry out their EU prudential reporting for these subsidiaries. The insurance regulatory regimes of Switzerland and Bermuda have been granted full equivalence in all three equivalence areas. As discussed above, the recently negotiated 'covered agreement' is intended to functionally result in equivalent treatment for the US insurance regulatory regime for both reinsurance and group-supervision purposes. It remains to be seen whether the UK will continue to implement Solvency II in the same manner as it currently does following the finalisation of its exit from the EU, and whether, after its exit, the UK will need to seek an equivalence decision from the EU, and the US equivalent treatment from the UK.

* *Samuel R Woodall and Roderick M Gilman provided valuable assistance in the preparation of this Introduction.*

GDPR

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Italy and the General Data Protection Regulation (GDPR)

Introduction

The right to an individual's data protection is fundamental, being enshrined in article 8 of the Charter of Fundamental Human Rights as well as article 16 of the European Union Treaty. Therefore, all subjects who collect, manage, store, transfer or treat personal data, regardless of whether they are sensitive or not, must adopt a risk management policy in order to ensure that their storage, use and elaboration is made in compliance with the law to ensure the protection of such data and personal information when potentially endangered by computer fraud, technical problems or mistakes of any kind.

Technology has radically changed our way of living and working, expanding the space beyond the boundaries of our homes and businesses. People today interact, thanks to smart phones, tablets and other electronic equipment, with other people, household appliances, computers and production machines, thanks to the exchange of data.

However, such data, despite being intangible, can be violated, stolen and manipulated for criminal purposes, or simply damaged or destroyed through human error or negligence. Data breaches, therefore, consitutes any event where sensitive data and personal, medical, or financial information are, actually or even only potentially, endangered. Sources of data breaches can be cybercrime, but also technical problems and human errors. In any event, the consequences for the victims can be significant and the damages, from loss of profit to the recovery costs or to reputational damage, can be huge and become a source of potential collective actions. Defence costs resulting from violations or loss of data can be very high and include legal fees, consultancy expenses, as well as costs incurred informing customers of what happened and the due corrective measures, before taking into account fines and sanctions provided by the law.

According to the latest Breach Level Index report by Safe NetGemalto, more than 5.3 billion pieces of data have been lost or stolen in the last three years, which is more than 3.8 million pieces per day and 2,600 pieces every minute.

The Center for Strategic and International Studies estimates that computer attacks cost about €500 billion a year, and in Italy alone they have been valued at between €800 and €900 million. However, damage to reputation alone would amount to more than €8 billion in Italy, which is equivalent to about 0.6 per cent of GDP, and the losses owing to system failure would exceed €14 billion.

In order to prevent or limit these losses, the EU dictated precise rules to safeguard the security of personal data with:

- Community Directive 95/46/EC laying down general principles for the free movement of personal data within European territory;
- Community Directives 2002/58/EC and 2009/136/EU concerning the processing of personal data and the protection of privacy in electronic communications, which introduced precise rules about online personal data collection and the use of cookies; and
- General Data Protection Regulation (GDPR) No. 2016/679 of the European Parliament and of the Council of 27 April 2016, which repealed and replaced Directive 95/46/EC.

The GDPR

The new Regulation will become mandatory in all EU member states, two years after its publication in the Official Journal of the European Union, on 25 May 2018.

The GDPR has introduced new principles on the protection of individuals with regard to the processing of personal data and to their free circulation within the European Union; but interestingly, in addition it has extended the efficacy of the rules on personal data processing outside of it, as long as the data processing concerns the supply of goods or services to EU citizens.

This is the first significant change because social networks, web platforms (even in clouds) and search engines will become subject to the Regulation, despite their location, and even if they are managed by companies outside the European Union.

Other important innovations include the following obligations on the holder of the personal data to:

- define the retention times of the data and indicate their source, if used;
- promptly notify the guarantor of any breach of his or her own database;
- draft the Data Protection Impact Assessment (DPIA), a risk assessment document related to data management incorporating the principles of privacy by design and privacy by default introduced by the GDPR; and
- to ensure the accountability of the data privacy officer (DPO) by way of an appropriate organisational chart and human and financial resources.

New roles and responsibilities

The privacy protection required by the GDPR imposes that compliance and governance programmes are accepted and adopted by the entire company.

A report published by the think tank Centre for Information Policy Leadership (CIPL) recommends integrating the data security requirements into all stages of each business process from design to release. Notwithstanding this clear message, confusion reigns over who has the responsibility of setting the rules to comply with the GDPR requirements. The CIPL report stresses that almost one-third (32 per cent) of the respondents believe that the person responsible should be the chief information officer (CIO), 21 per cent the chief information security officer (CISO), 14 per cent the CEO and 10 per cent the chief data officer (CDO). In reality, personal data management is no longer just a fulfilment of a managerial obligation, but it has transformed into a process that impacts the organisation of each company so that all the above figures shall cooperate and play an important role in their specific area of competence.

For example, in the event of a technical accident or data breach, the responsibility for data encryption and permanently secure confidentiality, integrity, availability and flexibility of the processing as well as the timely restoring of access to personal data rests with the CIO and the CISO. Whereas the CDO shall have responsibility to report the accident and manage the client relationship; third parties and the supervisory authority (SA) shall investigate the event. Finally, the CEO shall supervise the entire system and shall provide adequate financial and human resources to meet the need assessed with the DPIA.

The officers shall also ensure that anyone acting under their authority and having access to the processed data is instructed and capable to act in full accordance with the GDPR requirements. According to a Microsoft study on phishing emails, 23 per cent of the electronic messages of this type are regularly opened, 11 per cent of victims open the

link contained within the email giving hackers full access to their systems, and in 60 per cent of cases the attack is successfully completed within minutes.

Therefore, an adequate document management system will be developed through the compulsory establishment of a data processing registry, where all actions carried out, or accidents, can be tracked and documented according to the accounting principles or to the GDPR rules, to ensure that each data operation conforms to the provisions therein.

The Regulation also introduces the DPO as being a new professional figure who can be an employee of the company or an external consultant. This position is not merely that of a manager, but a professional figure whose skills shall vary from legal, informatics and organisational expertise. Besides overseeing the simple formal controls on data processes, the DPO shall support the decision-making process of the personal data holder and shall interact with the SA.

For public authorities and public agencies, as well as for all enterprises that process data of a significant number of people, or data that, by their nature and purpose, is sensitive or at risk, like banking and insurance, it is mandatory to have a DPO whose appointment will normally last for four years.

The national SA and the European Data Protection Board (EDPB)

All EU member states shall apply a single set of rules, but each member state will establish an independent SA to hear complaints, conduct investigations, sanction administrative violations and so on. In Italy, the current SA is called the '*Garante della privacy*'.

The SA in each member state will cooperate with each other providing mutual assistance.

If a company has more establishments throughout the EU, the competent SA shall be the one of the place where the main manage-ment activities take place. The main authority will act as a one-stop shop to oversee all data management activities of that company within the EU.

The EDPB will coordinate and superintend all national SAs including the Italian one.

The Italian SA in this perspective has actively participated with the article 29 Data Protection Working Party that has developed the guidelines for the correct and homogeneous implementation of the GDPR. In particular, the article 29 Data Protection Working Party on 13 December 2016 adopted, as revised on 5 April 2017, the following guidelines:

- on the DPO;
- on the right to data portability:
- for identifying a controller or processor's lead supervising authority; and
- on the DPIA and determining whether processing is likely to result in a high risk for the purposes of Regulation No. 2016/679.

Data breaches and sanctions

To guarantee rule compliance, in case of breaches the GDPR provides that the competent SA can impose heavy sanctions as:

- a warning in writing in cases of first and unintentional breaches or non-compliance;
- regular periodic data protection audits;
- a fine of up to €10 million or up to 2 per cent of the annual worldwide turnover of the preceding financial year in case of an enterprise, whichever is greater; and
- a fine of up to €20 million or up to 4 per cent of the annual worldwide consolidated turnover of the preceding financial year in case of an enterprise part of a group, whichever is greater, depending on the breach or non-compliance and the gravity of the consequences for the owners of the lost or damaged data.

To prevent breach or non-compliance the DPO must make a DPIA. The document should include an analysis of the risks involved, identify any existing risk, an action plan for their resolution and an annual review of the actions taken to ensure their control and risk reduction. By imposing the DPIA, the SA encourages the establishment of risk management mechanisms and certification procedures for data protection. Therefore, adherence to a code of conduct or to an approved quality certification mechanism could become means by which to demonstrate compliance with the Regulation's security requirements.

In the event of a breach, the DPO must notify the event to the SA within 72 hours of the event and, if the violation caused damage to the affected parties, to report it without delay. The strict timing poses major problems. In fact, it is estimated that about 300,000 variants of malware are discovered every day. Such malware typically includes programs designed to carry out specific attacks to destroy data, steal information and even compromise the activity of victims.

According to a Ponemon Institute study, an average of 205 days is necessary to identify a flaw in security systems and, in many instances, the violation was only discovered after the hackers blackmailed the victim. The latter example occurred at the European Central Bank (ECB) in July 2014, when, following an attack, thousands of addresses and pieces of personal data on European citizens were captured, but the attack was discovered only after the attackers contacted the ECB for a redemption. The variety and complexity of malware makes identifying the attackers immediately very difficult and is now a serious danger for the DPO if he or she does not report an attack within the allotted time. In fact, for data loss, fines of up to €20 million are foreseen for individuals and companies not belonging to groups and up to 4 per cent of the consolidated total turnover for corporate groups.

Italy and data protection

At present, IT security in Italy is grossly inadequate to meet the level of sophistication of current cybercrime. In spite of this, a Dell and Dimensional Research report proved that only 9 per cent of IT and business professionals are ready for the GDPR, and a study by the Milan Polytechnic Security and Privacy Observatory confirmed that, less than a year from the GDPR being fully in effect, Italian companies are still late in meeting the new security requirements.

The Ponemon Institute published the results of its 2016 Cost of Data Breach Study revealing that the public sector and the private retail outlets are the most-hacked sectors, probably because of the large amount of sensitive data collected combined with low levels of security.

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According to the Cyber Intelligence and Information Security Center at the Sapienza University in Rome, which conducted national research, found in contrast that despite all the financial organisations having been attacked, breaches were only successful in a mere 17 per cent of cases. This proves the higher degree of security that characterises banks and insurance companies in general. Finally, the industrial sector remains the least likely area to be attacked, but only 29 per cent of enterprises would be able to detect an advanced persistent threat.

Despite the efficiency of the security systems adopted, it is estimated that most of the incidents are not even detected by the victims.

In this context, the GDPR imposes on private companies and public bodies, that they operate with an approach fully integrated for the treatment of personal data, which is no longer based on the simple concept of compliance, but characterised by a pre emptive analysis followed by appropriate risk management and, eventually, the remedial action plan.

To address and improve such a situation, on 13 October 2016, the Italian SA published the Code of Ethics and Conduct in Processing Personal Data for Business Information Purposes, which joined the already available Guidelines on processing personal data in performing debt collection and the Guidelines on data breach notifications.

Following the large-scale implementation of the Guidelines and actions set for May 2018, according to a Veritas survey, nearly 40 per cent of businesses fear that they will not be able to comply with the new regulations, while just under one-third (31 per cent) are worried about brand-reputation damage caused by inadequate data policies.

This situation opens a few important scenarios for the insurance market because new forms of liability will emerge posing serious problems. Are the GDPR sanctions insurable or not? Is the DPO liability falling within the scope of the existing directors' and officers' insurance or will a totally new liability policy be necessary? How does one quote a risk for which there are no statistics? How can damages to clients and third parties be insured and is there any insurer that can provide capacity, hence cover for the damage to the company or stockholders if a fine of 4 per cent of the consolidated total turnover for corporate groups were to be imposed?

Despite the difficulties the GDPR will pose in Italy, it will be an opportunity for prudent but capable insurers to benefit from the opportunities that this new regulation will introduce to Italy, Europe and the wider world, having expanded its operation well beyond EU member states.

Austria

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Austrian Financial Market Authority (FMA) is the responsible authority for, inter alia, the supervision of the insurance and reinsurance market. The FMA is an autonomous and independent institution under public law and is supervised by the Federal Ministry of Finance.

Within the FMA, the Department of Insurance and Pension Fund Companies Supervision is the responsible body. The activities of the FMA in respect of the insurance market include, in particular, the ongoing supervision of all business activities of insurance companies and pension fund companies, including on-site inspections, proposals for the continued development of legislation regarding the insurance business, as well as licensing issues and legal supervision.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Apart from the specific statutory exceptions, only companies that have been granted a licence by the FMA may conduct contractual business insurance in Austria. The requirements for the formation and licensing of insurance and reinsurance companies are set out in the Insurance Supervision Act (VAG).

Pursuant to article 8 of the VAG, a company may only conduct contractual business insurance, provided that the company's legal form is one of the following:

- a joint-stock company;
- a European company;
- a mutual association; or
- an equivalent and respectively comparable foreign company.

The administrative headquarters of the company must be located in Austria.

The requirements for obtaining the licence further include:

- professional qualifications of the directors and officers pursuant to article 120 et seq of the VAG (see question 4);
- insurance and reinsurance undertakings shall hold eligible basic own funds in order to cover the minimum capital requirement pursuant to article 193; and
- the submission of a business plan.

The business plan to be submitted with the application must contain the following information and documents:

- the type of risk the company intends to cover, and also, in the case of a reinsurance business, the type of reinsurance contracts that the company intends to conclude with the primary insurers;
- the main features of the reinsurance policy;
- the composition of the equity capital;
- estimates relating to the expenses of installing the administrative services and the operation of the company, and proof that the necessary funds are available;
- estimates of the commission expenses and the operating expenditures (for the first three years of operation);
- estimates relating to the premium income and insurance payments (for the first three years of operation);
- budgeted balance sheets and profit and loss statements (for the first three years of operation);
- estimates of the financial resources intended to cover liabilities and equity capital requirements (for the first three years of operation); and
- the articles of association.

The additional documented information must be submitted when a foreign insurance company applies for a licence (articles 16 to 19 of the VAG).

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Other than the licence from the FMA, no other licences are required from companies in order to conduct contractual business insurance in Austria. However, it should be noted that, as a general rule, separate licences have to be obtained for each insurance line (the VAG distinguishes 23 lines of insurance). Nevertheless, annex B of the VAG provides for exceptions, allowing companies to apply for shared licences valid for multiple insurance lines.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

In general, the VAG provides that, the professional qualification, knowledge and experience of members of the board of directors or of the management board, or the managing directors, must be adequate to enable sound and prudent management. Furthermore, they have to be of good repute and integrity. The personal reliability is deemed not to be met if a person has been convicted of certain criminal or fiscal offences, or when the person's assets or the assets of an entity – over which the person has had significant influence – have been subject to an insolvency procedure.

At least two managing directors must have sufficient theoretical and practical knowledge in insurance business and management experience. These criteria are considered to be met provided a person has at least three years of managing experience in an insurance company of a comparable size and type of business.

In addition, at least one of the managing directors must be fluent in German.

The managing directors may not engage in a principal employment in a field other than the insurance or banking sector.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

At the time of commencement of business operations, there must be sufficient original own funds in the amount of the absolute floor of

the minimum capital requirement pursuant to article 193, paragraph 2, namely:

- for non-life insurance, not including indemnity insurance, credit insurance and fidelity insurance: €2.5 million;
- for non-life insurance, including indemnity insurance, credit insurance and fidelity insurance: €3.7 million;
- for life insurance: €3.7 million;
- for exclusive operation of reinsurance: €3.6 million in case of proprietary companies (captives): €1.2 million, as well as the necessary funds to cover the estimated expenditures with respect to the establishment of the management of the undertaking.

For the future, proof must be furnished that the company will have:

- sufficient funds to cover the technical provisions shown in the solvency balance sheet (article 10, paragraph 3 no 4);
- sufficient eligible own funds (article 174) to cover the solvency capital requirement (article 8, paragraph 2 no 4); and
- sufficient original own funds to cover the minimum capital requirement (article 8, paragraph 2 no 5).

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

The VAG provides for several types of technical reserves to be built in by insurance and reinsurance companies. These, depending on the insurance line of business, include:

- an ageing reserve in health insurance;
- a reserve for outstanding insurance claims;
- a reserve for profit-dependent premium refunds; and
- provisions for deferred profit participation, among others.

Furthermore, article 45 of the VAG provides for a statutory hedge reserve aimed at covering losses arising from the business operation.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

A company applying for an insurance licence must inform the FMA which type of risks the company intends to cover. In Austria, the principle of separation of insurance business-lines applies. Article 7 of the VAG sets out that a company offering life insurance may, in addition, only offer health insurance and insurance against accident and reinsurance. However, this principle of separation does not apply for companies that, prior to 2 May 1992, in addition to life insurance, have offered other insurance lines of business.

In respect of insurance products, the general rules of the VAG relating to, inter alia, licensing and reporting, apply to all insurance lines of business and products offered in this connection. However, in respect of certain insurance lines, the VAG provides for special provisions to be adhered to by the insurance company offering such products, that is, unit-linked and index-linked life insurance (a stricter conduct of business regime applies pursuant to article 254 of the VAG), companies offering life insurance must appoint an actuary, etc.

Further, in regard to the actual insurance products offered for sale, insurance companies have to comply with the Insurance Contract Act (VersVG). The VersVG provides for explicit regulations on matters including the rights and obligations of the insured person and the insurer, the content of the respective contracts and information requirements.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The FMA's supervisory activities include the continued supervision of all business activities of insurance and reinsurance companies, including but not limited to, on-site inspections and legal supervision. For the purposes of its examinations, the FMA may, at any time, request information concerning the business activities of insurance and reinsurance companies as well as the submission of relevant documents. The VAG does not provide for a minimum or maximum amount of on-site or off-site examinations, nor prescribes a period within which such examinations ought to be conducted.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

There are no specific requirements or restrictions relating to the types and amounts of investments that insurance and reinsurance companies may make. However, the VAG provides for detailed rules on the amount of equity capital that must be maintained by insurance and reinsurance companies at all times, and this may limit the amount of investments that such companies make. In the event that the insurance or reinsurance company acquires or sells its participation in incorporated companies, the FMA needs to notify the VAG when:

- the direct or indirect participation exceeds 50 per cent of the equity capital;
- the purchase price exceeds 10 per cent of the insurance or reinsurance company's equity capital;
- the acquisition creates an affiliation pursuant to article 189a no 8 of the Austrian Company Code (UGB); or
- the sale affects the resolution of an affiliation pursuant to article 189a no 8 of the UGB.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

The intended acquisition of a qualifying holding (ie, a direct or indirect holding in an undertaking, which represents 10 per cent or more of the voting rights or of the capital, or another possibility of exercising a significant influence over the management of that undertaking) in an insurance or reinsurance company, has to be notified and accepted by the FMA. The same applies for acquisitions of shares by persons already being shareholders in the event they intend to increase their participation to 20, 30 or 50 per cent.

The FMA may prohibit the acquisition if, following the assessment of the acquiring party, there are justified reasons to do so. The assessment criteria are set out in article 26 of the VAG and include:

- the reliability of the acquirer;
- the reliability and professional experience of the officers and directors responsible for the management of the insurance company;
- the financial soundness of the acquirer, particularly in respect of the actual transactions and services envisaged by the industry company to be acquired;
- whether the acquirer is and will be able to comply with the supervisory requirements set out in Directives 92/49/EEC (third non-life insurance directive), 98/78/EC, 2002/83/EC, 2002/87/EC and 2005/68/EC; in particular, whether the group of which the acquirer will become a part has a structure that makes it possible to exercise effective supervision, effectively exchange information among the supervisory authorities and to distribute the competences among the competent supervisory authorities; and
- whether there are reasonable grounds to suspect that, in connection with the proposed acquisition, money laundering or terrorist financing within the meaning of article 1 of Directive 2005/60/EC is taking place, has taken place or has been attempted, or that the proposed acquisition could increase the risk thereof.

In the event that a shareholder intends to sell his or her shares, or to decrease his or her shares below 20, 30 or 50 per cent, corresponding notification duties exist.

The acquisition or sale is considered as approved if the FMA does not prohibit such within 60 days following the notification.

As stated above, the VAG explicitly provides that officers and directors responsible for the management of the insurance company will be examined for their reliability and professional experience. There is no specific provision regarding such an inspection in respect of the officers and directors of the acquiring party. However, to a certain extent

this may be the case, as the FMA will examine the reliability of the acquiring party as such.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements or restrictions relating to financing the acquisition of an insurance or reinsurance company. As stated above, in the event of an intended acquisition of an insurance company, the FMA will examine the financial soundness of the acquiring party.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

The regulatory requirements for a qualifying holding in an insurance or reinsurance company are set out in question 10. The acquisition of participations of less than 10 per cent of the share capital or voting rights, and those that do not grant the acquirer's significant influence on the management, are not subject to specific restrictions under the VAG.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

In general, the VAG does not distinguish between national and foreign investors. Both groups are free to invest in Austrian insurance or reinsurance companies. Nevertheless, in the event a foreign investor intends to acquire an Austrian insurance company, the VAG provides for a couple of (mainly technical) provisions. These include the prolongation of the period for the FMA to require additional information from the acquiring party from 20 to 30 days, provided the acquiring party has its registered office outside the EEA or is being supervised by an authority outside the EEA. Further, the VAG provides for close cooperation and exchange of information between the FMA and the responsible foreign authority, if the acquiring party is, inter alia, a foreign credit institution, assurance undertaking, insurance undertaking, reinsurance undertaking, investment company, or the parent undertaking of, or a natural or legal person controlling such an institution.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The supervision of insurance groups includes the supervision of the group's solvency, the risk concentrations and intragroup transactions as well as the governance system at the group level. For example, by contrast with the VAG 1978, the supervision is only to be carried out at the level of highest parent company with its head office in a member state. Additionally, the collaboration between supervisory authorities is intensified through the establishment of colleges of supervisors pursuant to article 228 of the VAG 2016, as well as a closer cooperation and consultation according to articles 229 and 230 of the VAG 2016.

Pursuant to article 222, paragraph 2 of the VAG, extensive requirements exist with respect to the governance system of insurance groups; however, they are largely identical to the requirements applicable at the individual level. In particular, risk management systems, internal control systems and the reporting system shall be implemented evenly throughout all companies of the group in order to be controllable at the group level.

The most important element with respect to group supervision is the calculation of the group solvency. At the group level, the colvency capital requirement of the group shall be calculated; in doing so, the varying financial interrelations between the companies of the group as well as the risks at the group level are taken into consideration. The calculation shall be performed at least once annually.

There is no provision for the calculation of the minimum capital requirement at the group level, since the non-fulfilment of the minimum capital requirement ultimately results in the withdrawal of the licence based on the fact that only the individual companies, but not the group as a whole, can hold a licence.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Austrian law does not provide for any specific regulatory requirements in respect of reinsurance agreements. The Austrian Insurance Contract Act explicitly sets out that the same is not applicable to reinsurance agreements. Therefore, reinsurance agreements are governed by the general contract law.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There is no statutory numerical limit for ceded reinsurance and retention of risk. However, a total or unreasonably high transfer of risk from the insurer to the reinsurer is not admissible.

When deciding on the placement of reinsurance, the feasibility of obligations arising from the insurer's own insurance contracts, the obligations arising from the reinsurer's contracts as well as a proper diversification of risk have to be taken into consideration. The first two points above are deemed to be met provided the ceding insurer has its registered seat in a member state of the EEA or if the reinsurer is in the possession of a domestic licence.

Pursuant to article 17c of the VAG, a small insurance undertaking (Chapter 3 of the VAG) must demonstrably verify if the requirements for conclusion of a reinsurance agreement are met (primarily if the reinsurance company is in possession of a valid licence). Further, the insurer must demonstrably seek (and obtain) information about the assets, financial position and earnings of the reinsurance company in order to reliably assess whether the reinsurer will presumably fulfil his or her duties without delay and in accordance with the contract.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no additional requirements that have to be observed by reinsurance companies conducting reinsurance transactions.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Insurance companies must adhere to the general accounting principles enshrined in the UGB. However, VAG provides for additional accounting rules, which insurance companies must observe when preparing their financial statements. In this regard, article 144 of the VAG stipulates the prescribed balance sheet structure for insurance companies outlining the individual items and the order in which they must be displayed. The item 'receivables from reinsurance business' is illustrated in the 'assets' section (subcategory 'claims'), and must therefore be included in the financial statement of the insurance company.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

As a general rule, the Austrian Insolvency Code, applicable to both natural and legal persons, also applies to insolvent insurance and reinsurance companies. However, articles 307 to 316 of the VAG provide for certain exemptions in respect of such companies, for example:

- the management of the insurance or reinsurance company is obliged to immediately inform the FMA of the existence of bankruptcy requirements (that is, an inability to pay or over-indebtedness). The application for opening the insolvency procedure over an insolvent insurance and reinsurance company has to be filed by the FMA, contrary to the general provision that the debtor him or herself files for bankruptcy; and
- further, VAG enables the FMA to take certain measures instead of filing for bankruptcy, if this will benefit the insured parties. Such measures include the suspension of payments to the insured parties to the extent necessary to overcome the cash flow problems, or to reduce life insurance obligations of the insurer according to the assets available.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The rules contained in the Austrian Insolvency Code also apply in cases of insolvent insurance and reinsurance companies. An explicit exception is made for insurance claims in article 314 of the VAG outlining the priority of insurance claims over any other insolvency claim (excluding claims against the insolvency estate). Further to this, if an insolvent insurance or reinsurance company has an established cover pool, this cover pool constitutes a separate insolvency estate that is used to satisfy only the included insurance claims.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

For the purpose of concluding insurance contracts, insurance companies may only employ employees who have sufficient professional skills for such an activity, or independent insurance agents registered in the insurance intermediary register.

The particular qualification of an insurance agent required by law differs depending on the actual activity of the intermediary. In order to act as an insurance agent, one has to pass the qualification examination (the certificate issued by the Austrian Insurance Industry Training Institute), obtain an academic degree in insurance economics, or have at least two or three consecutive years of experience as an insurance broker or consultant. Comparable licensing requirements apply for insurance brokers and insurance consultants.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Only in exceptional cases does Austrian insurance law provide for a direct right of action of a third party against an insurer.

In practice, the most important element of such cases is the direct right of action of a person who has suffered damage in connection with the use of a vehicle being subject to compulsory motor third-party liability insurance (article 26 of the Act on Liability Insurance for Operating a Vehicle).

Further cases include damages that arise from the operation of an aircraft (article 166 of the Aviation Act), and from ionising radiation of nuclear facilities, nuclear materials or radionuclides (article 24 of the Nuclear Liability Act).

In all the above-mentioned cases, the respective law provides for joint and several liability of the person being liable for damages (insured) and of the liability insurer.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Article 33 of the VersVG constitutes a duty of the insured to immediately notify the insurer of the occurrence of an insurance contingency. Non-compliance with this duty represents a breach of contract on the part of the insured.

Standard policy conditions usually contain a clause providing for the right of the insurer to deny coverage when the insured does not comply with his or her notification duty. However, paragraph 2 of the aforementioned regulation provides that the insurer may not draw on such clause if he or she, by any other means, became aware of the insurance contingency.

Further, pursuant to consistent jurisprudence of the Austrian courts, insurers may not deny coverage owing to a late notice of claim provided the delay occurred not culpably or, if the late notice did not have any influence on the assessment of the insured event or on the insurance payment.

The burden of proof regarding the late notice of claim having no effect on the coverage obligation of the insurer lies with the insured party.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

As a general rule, a wrongful denial of a claim, when established by court, will result in the court awarding the insured party the claim arising from the insured event and interest from the date the payment became due. Provided that the insured party can prove that the additional damages were caused by the delayed payment, these damages may be claimed pursuant to statutory requirements.

However, since Austrian law does not recognise punitive damages, these will not be awarded even if the insurer acts in bad faith or refuses to settle legitimate claims.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

In general, liability insurance embraces the duty of the insurer to satisfy justified claims and to defend unjustified claims. In practice, the insurer, on the basis of the existing facts, will decide whether he or she is willing to acknowledge and thus satisfy the claims of the person affected, or whether he or she will defend the claim. The insurance contract, however, may specify circumstances that trigger a duty of the insurer to defend certain claims.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

As a general rule, the insurer's payment obligation is triggered by the occurrence of the insured event.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

In general, in the event of a misrepresentation in the insurance application that results in the failure to disclose a material circumstance, the insurer may withdraw from the contract. However, in respect of life insurance, article 163 of the VersVG provides that, after the expiry of a period of three years – starting from the conclusion of the contract – such withdrawal is no longer permissible. The latter does not apply if the misrepresentation occurred fraudulently.

28 Punitive damages

Are punitive damages insurable?

The Austrian legal system is not familiar with the legal instrument of punitive damages. Therefore, there are no specific provisions in respect of punitive damages. However, owing to the general rule of contractual freedom, parties are free to agree on the coverage of punitive damages. Nevertheless, we are not aware of punitive damages being subject to insurance contracts in practice. On the contrary, where relevant, in particular, in product liability insurance and prospectus liability insurance, the coverage of punitive damages is excluded in the majority of the insurance contracts.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

There are no regulations relating to excess insurance in Austria. Therefore, parties are, in general, free to agree on the terms and conditions of the particular excess insurance contract. Basically, since the primary insurance contract constitutes an independent contract, the question as to whether or to what extent the excess insurer is obliged to pay a claim under the excess insurance contract has to be assessed solely on the basis of this very contract. In essence, the obligation of an excess insurer to pay a claim when the coverage of the primary insurer is not available depends on whether a drop-down clause has been agreed on. The inclusion of such a drop-down clause will, in general, result in the obligation of the excess insurer to drop down and pay the claim of the insured irrespective of why the coverage of the primary insurer lapsed (eg, because of insolvency or other circumstances on the part of the primary insurer).

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

An insolvency or inability of the insured to pay the self-insured retention or deductible has no effect on the insurer's obligation to provide coverage. Where a self-insured retention has been agreed, the insurer will only be liable for the amount exceeding such a self-insured retention. It should also be noted that within a compulsory liability insurance, no self-insured retention or deductible may be agreed in relation to third parties.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

For liability insurance, article 156, paragraph 3 of the VersVG provides that claims of several third parties that are collectively exceeding the sum insured, shall be satisfied in proportion to their respective amounts. For other insurance lines, there are no explicit regulations. In essence, multiple claims of the insured have to be satisfied in the order of their submission and claims of third persons proportionally.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

The consequences of double or multiple insurances are regulated in articles 58 to 60 of the VersVG. The multiple insurers are jointly liable for the amount that every insurer owes under the respective insurance contract. The payment is, however, limited to the actual loss suffered by the injured party. In practice, the insured party is, in general, free to choose the insurer from which it requests the actual payment. In the relationship between the involved insurers, the insurers are obliged to compensate each other in proportion to the actual payment obligation under the respective insurance contract.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

In the Austrian insurance practice, losses flowing from disgorgement or restitution claims are typically not covered by insurance policies and do not regularly constitute insurable losses.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

To date, the issue of whether a single event that results in multiple claims constitutes more than one occurrence under an insurance policy has not yet been subject to judicial review by the Austrian Supreme Court. There are also no published decisions by lower courts regarding this issue.

Update and trends

On 1 January 2016, the former VAG was been replaced by VAG 2016, which has its main focus on the implementation of Directive 2009/138/EC (Solvency II). The practical impact of the new regulatory framework is yet to be seen. In general, the current Austrian insurance and reinsurance regulation and the corresponding jurisdiction reflect European trends. Currently, there are no official proposals for major reforms to Austrian law concerning insurance and reinsurance regulation.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Pursuant to article 16 et seq of the VersVG, a person seeking insurance must, at the time of filing an application, notify the insurance company of all the facts and circumstances that are relevant for the insurance company's decision to insure the respective risk. Should the insured fail to comply with this obligation or negligently make misstatements in the application, the insurance company will be entitled to rescind from the insurance contract within one month of gaining knowledge of the occurrence of such misstatements. In addition, the insurer may also rescind from an insurance contract for fraudulent misrepresentation, in which case the one-month limitation period does not apply.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Parties involved in a reinsurance dispute usually try to resolve disputes through out-of-court negotiations. Besides the formal proceedings, arbitration is the preferred form of dispute resolution. To the best of our knowledge, there are almost no decisions of the Austrian Supreme Court dealing with reinsurance issues.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Reinsurance disputes most commonly concern performance obligations of the reinsurance company and the valuation of damages.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Pursuant to article 606, paragraph 2 of the Code of Civil Procedure, arbitration awards must state the reasons for the decision unless otherwise agreed by the parties. In practice, parties usually do not waive the reasoning.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Owing to the qualification of arbitration courts as private courts, arbitrators have no power over non-parties to the arbitration; therefore, unless otherwise agreed by the parties, arbitrators may only order interim or, if necessary, protective measures against the parties involved in order to secure the claim, or when the enforcement of the claim would be thwarted or made significantly more difficult or when there would be a risk of major adverse effects.

However, the arbitral tribunal may request from the competent state court the performance of judicial acts that the arbitral tribunal is not empowered to carry out (article 602 of the Code of Civil Procedure).

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Within three months of the arbitration award being served, each party may bring an action for the annulment of the arbitration award before the competent state court. The grounds for the annulment of the award are enumerated in article 611 of the Code of Civil Procedure, and include the absence of a valid arbitration agreement, the violation of each party's right to be heard or the right to a fair trial, defects in the constitution of the arbitral tribunal or violation of public policy.

In general, arbitration awards have the same effects as judgments of state courts; namely, the same principles in respect of legal validity and enforceability apply.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There is no statutory obligation on the reinsurer to follow the cedent's underwriting fortunes and to claim payments or settlements. Such an obligation, its scope and the possible defences have to be regulated in the reinsurance agreement.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

In Austrian law, the duty of good faith is a prevailing principle. Therefore, it is also implied in reinsurance agreements. Nevertheless, there is no notable difference in the interpretation of the principle of good faith in respect of standard commercial agreements and reinsurance agreements.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

No; Austrian law does not provide for a specific set of laws for facultative reinsurance and treaty reinsurance. Both reinsurance types are subject to contractual arrangements of the parties.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

As there is no contractual relationship between the reinsurer and the policyholder or a non-signatory to a reinsurance agreement, such persons cannot, as a general rule, bring a direct action against a reinsurer for coverage. As far as can be ascertained, the Austrian courts have not yet dealt with the issue of a right of direct action of an insured against the reinsurer. Nevertheless, according to the German jurisprudence, in exceptional cases, such direct action may exist. Owing to a comparable legislation in the field of insurance law in Austria and Germany, it is likely that Austrian courts would follow the decisions of German courts and, in exceptional cases, affirm a direct claim of the insured.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

In general, there is no obligation on the reinsurer to make a direct payment of a policyholder's claim, and claims of the insurer against the reinsurer are determined solely on the basis of the reinsurance contract. However, the insured may assert his or her obligations under the insurance contract against the insolvent insurer within the insolvency procedure that has been opened over the insurer's assets. As regards to the insurer, the insolvency administrator will, on the other hand, have the right to assert claims of the insurer against the reinsurer. As soon as the reinsurance makes a payment to the insolvency estate under a reinsurance agreement, such a payment will be subject to a right of separation on the part of the insured.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Austrian law does not provide for any specific regulations relating to the exchange of information between insurer and reinsurer. Usually, these issues are regulated in the reinsurance agreement. It is common to pass on the information that is necessary to assess the claim in question.

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In practice, the reinsurance contract will set out consequences triggered by the insurer's failure to provide timely notice. Although there are no decisions of the Austrian Supreme Court as to whether a reinsurer may deny coverage owing to a late notice of claim, in our opinion the same applies in respect of insurance contracts (see question 23).

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

As there is no statutory law that regulates allocation of the underlying claims, the reinsured has to allocate the claim and settlement payments according to the respective reinsurance agreements. The reinsurance agreements may provide that the allocation of claims has to occur in proportion to the reinsured amounts. However, and more commonly, the reinsurance agreements establish a ranking (eg, layers) between the respective reinsurance policies. In such a case, the reinsured – before turning to the second-ranked or subsequent reinsurance policies – must exhaust the first-ranked policy.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Austrian statutory law does not provide for any specific type of review rights in favour of the reinsurer. In practice, such right of the reinsurer will be regulated in the reinsurance agreement, and will, most commonly, include the submission of information or documents proving the occurrence of the loss or the fact that the allocation has been made in accordance with the reinsurance contract.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

The 'follow-the-settlement' principle is common in reinsurance agreements. As far as the insurer complies with his or her due diligence duty while making payments, the reinsurer is obliged to reimburse all payments made by the insurer that are subject to the reinsurance contract.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

As stated above, it is a general rule of reinsurance that the reinsurer is bound by coverage decisions of the cedent and must therefore follow the cedent's settlements. Actions and decisions made by the cedent are thus generally binding for the reinsurer. However, the reinsurer is not obliged to reimburse the cedent for obligations that go beyond the risks and losses covered by the reinsurance policy, for payments or settlements made as a gesture of goodwill, and for fraudulent or collusive conduct on the part of the cedent.

Bermuda

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Bermuda Monetary Authority (BMA) has been responsible for regulating all Bermudian financial services industries, including insurance and reinsurance companies, since 2002 when this responsibility was transferred to the BMA from the minister of finance. In practice, the day-to-day functions of the BMA are delegated to the supervisor of insurance, who is appointed by the BMA and sits as an ex officio member of the board of directors of the BMA

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

The process of establishing a Bermuda insurance company requires both the incorporation of the company and that its registration as an insurer, as there are two pieces of legislation which govern the operations of the insurance company: the Companies Act 1981, as amended (the Companies Act) and the Insurance Act 1978, as amended (the Insurance Act). However, approval of a company for incorporation under the Companies Act is not an indication that an application for the registration of the company as an insurer under the Insurance Act will also be approved.

The application package for licensing of the insurance company will typically include details of the ownership structure, evidence supporting that the shareholder and directors are 'fit and proper', a business plan detailing the viability of the business objective, the insurance programme and pro forma financials.

The Assessment and Licensing Committee (ALC) is made up of BMA representatives and plays a crucial role in the licensing process for insurance and reinsurance companies in Bermuda. The ALC hears all applications to establish new insurers and reinsurers at its weekly meeting. In addition, members of the Technical Advisory Group (TAG) (composed of experienced insurance professionals, actuaries and accountants with the requisite experience to evaluate the variety of proposed insurance companies that want to enter the Bermuda insurance market) may be invited to meetings of the ALC for certain insurance company applications. The ALC and TAG may recommend that the BMA approve the application unconditionally or, subject to conditions (which may be set out in the licence), defer the application pending clarification of certain matters or reject the application if it considers the business case simply cannot be substantiated.

The application package will, therefore, be scrutinised carefully by the ALC, TAG and the BMA with careful attention being paid to the viability of the proposed insurance programme and the financial resources to support that programme. If the application is approved at this meeting the company can generally be incorporated the following week (although there is nothing to prohibit the company being incorporated prior to submitting the licensing application).

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

The Insurance Act sets out the legal framework for insurance regulation in Bermuda together with the related regulations, mainly, in the case of commercial (re)insurers, the Insurance Accounts Rules 2016 (as amended) and various prudential standards rules and regulations applicable to each class of (re)insurer and, for limited purpose (re) insurers, the Insurance Accounts Regulations 1980 (as amended) and the Insurance Returns and Solvency Regulations 1980 (as amended). The Insurance Act provides that no person may carry on insurance business 'in or from within Bermuda' unless the person is registered as an insurer under the Insurance Act. In addition, an insurance company that is not incorporated in Bermuda but in another domicile may, in exceptional circumstances, be licensed to do business in Bermuda under section 134 of the Companies Act.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

As noted above, directors and officers must satisfy a 'fit and proper' test and evidence supporting that this test is met by the directors must be submitted at the time of application for licensing. As regards residency requirements, a Bermuda 'exempted company' which, by definition, is incorporated in Bermuda by non-Bermudians for the purpose of conducting business outside Bermuda, need no longer have two Bermuda resident directors as long as it has at least one representative ordinarily resident in Bermuda. This requirement is satisfied by appointing a director or a secretary who is ordinarily resident in Bermuda or a resident representative.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

The Insurance Amendment Act 1995 introduced a four-class licensing system for general insurance and reinsurance companies to take account of the diversity and volume of business carried on by insurers in Bermuda. The Insurance Amendment Act 2008 subsequently reclassified the class 3 insurers into three sub-categories: classes 3, 3A and 3B (see below). The multi-class system permits a graduated approach in relation, for example, to the ongoing compliance regime to which all insurance companies are subject, so that, although there are certain irreducible minimum requirements (for example, capital and solvency margin requirements) applicable to all insurance companies, the requirements for class 4 insurers are correspondingly greater than for class 1 'pure captives'.

The multi-class system classified general insurance companies into the following classes:

- class 1: single-parent or 'pure' captives writing risks of the parent and its affiliates only;
- class 2: multi-owner captives and single-parent captives writing up to 20 per cent unrelated business;

- classes: 3, 3A and 3B – all other companies not falling into class 1, 2 or 4, including insurers writing direct policies with third parties, finite reinsurers and insurers that are segregated account companies. (Class 3 includes insurers writing more than 20 per cent but less than 50 per cent of unrelated business; class 3A includes insurers writing more than 50 per cent of unrelated business but the unrelated business premium does not or is not projected to exceed US$50 million; class 3B includes insurers writing more than 50 per cent of unrelated business and the unrelated business premium exceeds or is expected to exceed US$50 million); and
- class 4: a special category of (re)insurer that writes excess liability or property catastrophe insurance risks (or both).

The Insurance Act requires that insurance companies must satisfy prescribed paid up share capital as well as minimum capital and surplus requirements, which vary, depending on the class of the insurance company. Class 1, class 2, class 3, class 3A or class 3B insurers must maintain a minimum paid-up share capital of US$120,000. Class 4 (re)insurers must maintain a minimum paid-up share capital of US$1 million. In the case of composite insurers, the minimum paid up share capital required is the aggregate amount of paid-up share capital required for each class for which is registered, namely, that required under the general business classification (classes 1, 2, 3, 3A, 3B or 4) plus the minimum amount required under the long-term business classification (classes A to E – see below). The minimum capital and surplus for a class 1 insurer is US$120,000. For a class 2 insurer the minimum capital and surplus requirement is US$250,000. A class 3, class 3A and class 3B insurer is required to have a minimum of US$1 million in capital and surplus. The minimum capital and surplus requirement for a class 4 insurer is US$100 million. These minimum requirements must be maintained at all times.

The solvency capital requirements must be maintained by the insurer at all times, this being a standard condition imposed on the licence of every insurer. These are the minimum standards required and may need to be adjusted upwards depending on the actual net written premium of the insurer. Classes 1, 2 and 3 must maintain a solvency margin (namely, capital and surplus) of 20 per cent of net premiums for the first US$6 million of premiums written. If premiums are written above this amount, the solvency margin is US$1.2 million plus 10 per cent of the excess for classes 1 and 2. For class 3, 3A and 3B, the amount is 15 per cent of the excess above US$6 million. Class 4 insurers must maintain a solvency margin of 50 per cent of net premiums written.

If the relevant percentage (being 10 per cent for classes 1 and 2 and 15 per cent for classes 3, 3A, 3B and 4) of the loss and loss expense provision of an insurer is greater than the solvency margin described above, the insurer must have a level of statutory capital, which is the greater of the relevant solvency margin or the relevant percentage of the loss and loss expense provision.

Note, the Insurance Amendment Act 2008 empowered the BMA to make orders that set prudential standards for enhanced capital requirements (ECR) and capital and solvency returns. The prudential standards impose different requirements to be complied with by different classes of insurers, in different situations and in respect of different activities. This provides the primary legislative basis for the adoption of the Bermuda solvency capital requirements (BSCR), which applies to class 3A, 3B and 4 general business insurers (as well as class C, D and E long-term business insurers – see below) as part of Bermuda's Solvency II Equivalence.

In addition, Insurance Amendment (No. 3) Act 2010 (effective 31 December 2010) classified long-term insurance companies into several sub-categories, to create an enhanced solvency framework for these companies, as follows:

- class A, where the insurer is wholly owned by one person and intends to carry on long-term business consisting only of insuring the risks of that person or is an affiliate of a group and intends to carry on long-term business consisting only of insuring the risks of any other affiliates of that group or of its own shareholders;
- class B, where the insurer's body corporate is wholly owned by two or more unrelated persons and intends to carry on long-term business not less than 80 per cent of the premiums and other considerations written in respect of which will be written for the purpose of insuring the risks of any of those persons or of any affiliates of any of those persons or insuring risks which, that in the opinion of the authority, arise out of the business or operations of those persons or any affiliates of any of those persons;
- class C, where the insurer has total assets of less than US$250 million (and is not registrable as a class A or class B insurer);
- class D, where the insurer has total assets of US$250 million or more but less than US$500 million (and is not registrable as a class A or class B insurer); and
- class E, where the insurer has total assets of more than US$500 million and is not registrable as a class A or class B insurer.

This amendment Act also introduced new capital and solvency requirements for insurers carrying on long-term business. The minimum amount paid up on the share capital as a:

- class A insurer is US$120,000;
- class B insurer is US$250,000; or
- class C, D and E insurer is US$250,000.

The minimum capital and surplus for long-term business is:

- class A: US$120,000;
- class B: US$250,000;
- class C: US$500,000;
- class D: US$4 million; and
- class E: US$8 million.

The minimum margin of solvency for long-term business is:

- class A: greater of US$120,000 or 0.5 per cent of assets;
- class B: greater of US$250,000 or 1 per cent of assets;
- class C: greater of US$500,000 or 1.5 per cent of assets;
- class D: greater of US$4 million or 2 per cent of the first US$250 million of assets plus 1.5 per cent of assets above US$250 million; and
- class E: greater of US$8 million or 2 per cent of first US$500 million of assets plus 1.5 per cent of assets above US$500 million.

The Insurance Amendment Act 2008 also introduced a new classification of insurer in response to the growth in special purpose insurance transactions and securitisations: special purpose insurer (SPI). The principal features of this new SPI category are as follows:

- minimum paid up share capital of US$1.00;
- the margin of solvency requirement requires that the assets of the SPI exceed its liabilities at all times;
- an SPI will only be permitted to write 'special purpose business', which is defined in the Insurance Act as insurance business under which an insurer fully funds its liabilities to the persons insured through a debt issuance where the repayment rights of the providers of such debt are subordinated to the rights of the person insured or some other financing mechanism approved by the BMA or through cash or time deposits; and
- the SPI will be restricted from entering into any other business save for ancillary agreements to effect its special purpose business.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Section 18B of the Insurance Act provides that class 2, 3, 3A, 3B and 4 insurers must include the opinion of a loss reserve specialist in its statutory financial return (annually for class 3, 3A, 3B and 4 insurers and every third year for class 2 insurers). Section 27 of the Insurance Act provides that class A, B, C, D and E insurers shall include in the insurer's statutory financial return a certificate prepared by its approved actuary in the prescribed form as to the amount of the insurer's liabilities outstanding on account of its long-term business. In addition, for class C, D and E insurers, the insurer's approved actuary must provide an opinion in its statutory financial return on the long-term business technical provisions of the insurer shown on its statutory economic balance sheet.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

As mentioned above, the Insurance Act, together with its related regulations, sets out the legal framework for insurance regulation. As

regards the types of products offered for sale in Bermuda, the focus of the Bermuda insurance market is directed primarily at reinsurers and captive service providers (very little business in Bermuda is transacted with individual policyholders). With respect to the captive (devised in the 1960s), since the 1990s, Bermuda has enacted private Acts of Parliament to enable insurance companies to operate segregated accounts. Most of these have been established as 'rent a captive' facilities, providing the participants with a legally segregated cell within the company through which to underwrite their insurance programme. In 2000, Bermuda enacted the Segregated Accounts Companies Act (amended in 2002), which permits a company to have legally segregated accounts by registration and sets out rules governing the operation of segregated accounts.

The Insurance Amendment Act 1998 was introduced, among other things, to recognise the convergence of the insurance and capital markets and it permits the BMA to recognise certain contracts (for example, swaps and derivatives) as 'designated investment contracts'. As a result, so-called 'transformer companies' may offer both insurance and capital markets products without the need to obtain a separate insurance licence in respect of products qualifying as 'designated investment contracts'.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

All classes of insurer are required to file with the BMA annual statutory financial statements, an annual statutory financial return and an annual declaration that the insurer is in compliance with the requirements of the Insurance Act and its related regulations. Class 3A, 3B, 4, C, D and E insurers are also required to file with the BMA, annually, additional generally accepted accounting principles or IFRS financial statements and a capital and solvency return, which includes the insurer's BSCR or internal capital model approved by the BMA. Class 3B and 4 insurers (where the insurer is not part of an insurance group supervised by the BMA) are required to submit quarterly financial returns to the BMA.

Under the Companies Act, insurance and reinsurance companies are required to lay before the company in annual general meeting audited financial statements of the company (unless such requirement is waived by all directors and shareholders of the company).

In addition to such requirements, the BMA has extensive intervention powers under the Insurance Act and conducts regular on-site reviews, coupled with off-site analysis, of insurers.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

There are no restrictions on what investments may be made, but certain investments (unquoted equities, investments in or loans to affiliates, real estate and collateral loans) will not qualify as relevant assets for the purposes of calculating a general insurer's required minimum liquidity ratio, unless the BMA designates such assets as relevant assets. Class 3A, 3B, 4, C, D and E insurers are required to maintain a minimum proportion of their ECR as assets qualifying as eligible capital (tier 1, tier 2 and tier 3 capital) under the Insurance (Eligible Capital) Rules 2012, as amended.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

The Insurance Amendment Act 2006 introduced the concept of a 'controller' and the requirement that any person planning to become a controller of an insurance or reinsurance company must give notice to the BMA. A 'controller' includes a managing director or chief executive of an entity registered under the Insurance Act. It also includes a shareholder holding or entitlement to exercise at least 10 per cent of the voting shares at a general meeting. The BMA ensures that the controller meets the 'fit and proper' test – in the same way that it ensures that shareholders and directors meet the same test at the time of licensing (see question 2).

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no particular requirements regarding the financing of an acquisition of an insurance or reinsurance company.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

The definition of controller under the Insurance Act includes a shareholder holding or entitlement to exercise 10 per cent of the voting shares at a general meeting and, therefore, any person seeking to acquire a minority interest in an insurer of 10 per cent or more must give notice to the BMA (see question 10). In addition, an acquirer of any equity securities (voting shares or shares that give rights to appoint one or more directors) in any Bermuda company, including an insurer, must receive the prior approval of the BMA, subject to certain limited general permissions, in accordance with the Exchange Control Act 1972 and its related regulations.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

An insurance or reinsurance company in Bermuda, like any other company in Bermuda, will be incorporated under and subject to the provisions of the Companies Act. Most insurance companies will be established as 'exempted' companies under the Companies Act, meaning that they conduct business primarily with persons outside Bermuda, and, as such, will be exempted from the requirement (applicable to 'local' companies) that at least 60 per cent of the company be owned by Bermudians. Companies that conduct business in and for the island's local economy must be incorporated as local companies and are subject to the 60 per cent ownership rule. The Companies Act therefore allows for an exempted company to be 100 per cent foreign-owned.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The BMA may determine that it is appropriate for the BMA to be the group supervisor of an insurance group. An insurance group is defined as a group of companies that conducts insurance business (which includes reinsurance business). Where the BMA makes such determination, the BMA shall designate a specified insurer within the group as the group's 'designated insurer' and shall give written notice to the designated insurer and other competent authorities of its intention to act as group supervisor. As group supervisor, the BMA performs a number of supervisory functions as set out in section 27E of the Insurance Act. The designated insurer will be responsible for ensuring that the group complies with the requirements of the Insurance Act, as they apply to insurance groups, and its related regulations, including the Insurance (Group Supervision) Rules 2011, as amended, which lays out the framework for group supervision.

Insurance groups supervised by the BMA are required to file annually with the BMA similar financial, capital and solvency information as individual commercial insurers, but on a group wide basis and in addition to that which must be filed by individual insurers within the group. These consist of a group statutory financial return, statutory financial

statements together with additional audited consolidated financial statements of the parent company of the group, and a group capital and solvency return, including the group's BSCR or a group internal capital model approved by the BMA (which the prudential standards applicable to BMA supervised groups require the group's ECR to be calculated on), and the group actuary's opinion on the insurance group's technical provisions. In addition, each insurance group shall file with the BMA quarterly financial returns.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Bermuda regulates reinsurance companies in a similar way to insurance companies. In the Insurance Act, 'insurance business' is defined as: the business of effecting and carrying out contracts – (i) protecting persons against loss or liability to loss in respect of risks to which such persons may be exposed; or (ii) to pay a sum of money or render money's worth upon the happening of an event, and includes reinsurance business.

Indeed, an important feature of the Insurance Act is that the legislation applies to reinsurance companies in Bermuda in much the same way as it applies to insurance companies. The BMA does not, as a matter of course, review or approve reinsurance agreements or require the inclusion of certain provisions. However, the BMA may at times consider the viability of a programme and may review the actuarial valuation of reserves, premium rates, etc.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Insurers are not required to retain any portion of liabilities nor are they restricted from ceding 100 per cent of liabilities to reinsurers. That said, insurers must always maintain the solvency margins set out in question 5.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no regulatory requirements concerning collateral requirements for assuming reinsurance companies in Bermuda. That said, the ceding company may have its own requirements. Under the new SPI regime introduced in 2008 it is a requirement that the SPI vehicle be fully funded and fully collateralised.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Class 3A, 3B, 4, C, D and E insurers are required to file with the BMA, annually, additional GAAP or IFRS financial statements (see question 8), which form the basis for calculation of the insurer's economic balance sheet, which in turn forms the basis for determining the insurer's ECR. Within such financial statements the insurer is required to set out, among other line items, reinsurance balances receivable recorded at fair value in line with GAAP, losses and loss expenses recoverables related thereto and, where such balances are due in more than one year, such balances shall be discounted at the relevant risk-free rate prescribed by the BMA. Class 1, 2, 3A and 3B insurers are required to include in their annual statutory financial return filed with the BMA statutory financial statements setting out, among other line items, reinsurance balances receiveable.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The Companies Act deals with schemes of arrangement, reconstructions, amalgamations and mergers (Part VII). Part XIII of the Companies Act deals with the winding-up of all companies, including the liquidation of insolvent insurance and reinsurance companies.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

All claims of unsecured creditors of an insolvent insurance or reinsurance company whether they be the claims of direct policyholders, reinsureds or ordinary trade creditors rank equally.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The Insurance Act applies to any persons carrying on 'insurance business' in or from within Bermuda, and provides for the registration of all insurers as well as insurance managers, brokers and agents. Apart from the Insurance Act requirement, it is also necessary to make an application to the BMA for permission to incorporate the company and to submit personal declaration forms for each of the proposed individual non-Bermudian beneficial owners. If the beneficial owner is a company, the register of members and financial statements will be required.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Generally, there is no provision for a third party to bring a direct action against an insurer. However, if the insured is bankrupt or insolvent then such an action may be brought.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

An insurer is not required to show prejudice when denying coverage on the grounds of late notice if the notice clause in the policy is a condition precedent.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

An insurer will not be subject to extra-contractual exposure for wrongful denial of a claim.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

An insurer's duty to defend a claim and the trigger for that duty will be determined by the contractual terms set out in the policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

Again, an insurer's duty to indemnify and the trigger for that duty will be determined by the contractual terms and the scope of coverage set out in the policy.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

In general, where a life insurance contract has been in effect for two years during the lifetime of the insured, a failure to disclose (or a misrepresentation of fact) when ordinarily required to be disclosed does not, in the absence of fraud, render the contract voidable.

28 Punitive damages

Are punitive damages insurable?

There are no reported cases in Bermuda dealing with the recovery of punitive damages. In England, the Court of Appeal has held that exemplary damages (punitive damages) were insurable and payable under the indemnity provided by a policy of insurance. See *Lancashire County Council v Municipal Mutual Insurance Ltd* [1997] QB 897. The court commented that contracts should only be unenforceable on public policy grounds in very plain cases and that the courts 'should be wary of minting new rules of public policy when the legislature has not done so'. This authority is not binding, but would be persuasive in Bermuda.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

An excess insurer's obligations with respect to defending and covering a claim are limited to those obligations set out in the terms of the excess policy.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

In such circumstances, if the self-insured retention or deductible is a condition precedent to the insurer upholding the claim the insurer is automatically not liable for the claim or loss to which the condition precedent relates. It is possible in theory that the breach of such term of the policy by the insured could entitle the insurer to repudiate the policy.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

The priority for payment of multiple claims under the same policy may be addressed in specific provisions within the policy. An insurer should be aware of any implications that may arise out of payments made shortly before insolvency.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

The policy wordings may contain specific provisions that address allocation. If more than one policy is triggered, more than one insurer (or set of insurers) may be responsible for the full amount of the insured's loss. However, the insured may not be compensated for more than the full amount of its loss. If full payment is made to the insured under one policy, the insurer that has paid out may bring an action for contribution from other insurers of other policies triggered by the loss.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Yes.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

There are no reported Bermuda cases dealing with the definition of 'occurrence', English case law, which requires common causation, will be persuasive.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The misstatement (misrepresentation) must be material in that it would have affected the decision of hypothetical prudent underwriter and that it must also be shown that it did affect the decision of the actual underwriter.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Arbitration is the most common mechanism for resolving reinsurance disputes as most reinsurance contracts contain agreements to arbitrate. More recently, there has been a re-domestication of the arbitration agreements in reinsurance contracts providing for arbitration in Bermuda. Reinsurance arbitrations in Bermuda are generally subject to the Bermuda International Conciliation and Arbitration Act 1993 (Arbitration Act 1993) that gives effect to the UNCITRAL Model Law on International Commercial Arbitration. This gives the parties broad freedom to agree on rules and, in the absence of agreement, confers broad powers on the arbitral tribunal. A court has very limited powers to interfere with these arbitrations. In the absence of an arbitration clause disputes will be heard by the Bermuda Commercial Court.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Contracts under the 'Bermuda Form' of liability insurance, and some reinsurance contracts, may be governed by New York law even though the seat of the arbitration will be London or Bermuda. A variety of procedural issues can arise in relation to appointment of arbitrators, pleadings, discovery, etc, and common substantive issues include those regarding the scope of a policy or reinsurance contract, late notice, 'follow the settlement', non-disclosure, etc.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Article 31(2) of the Arbitration Act 1993 provides that an award shall state the reasons upon which it is based, unless the parties agree otherwise.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Non-parties to an arbitration agreement cannot be joined as parties to an arbitration without their consent and the consent of the parties. The arbitral tribunal does not have the authority to order discovery from non-parties although they may be compelled to give evidence at the hearing.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

The Bermuda courts give great deference to arbitration clauses and it is, in essence, impossible to appeal an arbitration award based on mistake of fact or mistake of law. As such, there is no case where the courts in Bermuda have overturned an arbitration award.

Article 34 of the Arbitration Act 1993 sets out the grounds upon which an arbitral award may be set aside. The application is made to the Court of Appeal of Bermuda, from whose decision there is no appeal. The grounds on which an award may be set aside include:

- incapacity of a party;
- invalidity of the arbitration agreement;
- lack of notice of appointment of arbitrator or arbitral proceedings or where a party is otherwise unable to present its case;
- the award deals with matters falling outside or beyond the scope of the terms of the submission to arbitration;
- the composition of the arbitral tribunal or the arbitral procedure is not in accordance with the agreement of the parties;
- the subject matter of the dispute is not capable of settlement by arbitration under the law of Bermuda; or
- the award is in conflict with the public policy of Bermuda.

Article 35 of the Arbitration Act 1993 provides that an arbitral award, irrespective of the country in which it was made, shall be recognised as binding and, upon application in writing to the court, it shall be enforced.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Where the reinsurance contract contains a 'follow-the-settlements' clause, the reinsurer is obliged to pay a claim presented by the reinsured, including a claim arguably covered but settled without admission of liability on the part of the reinsured, provided that the claim at face value falls within the underlying insurance contract or has been found by a court or a tribunal to do so, that the claim falls within the reinsurance contract and that the reinsured acted in good faith and in a business-like manner in settling the claim. The reinsurer may not resist payment of the claim by seeking to litigate (or re-litigate) the issue of coverage under the original insurance contract. The burden is on the reinsurer to establish that the reinsured did not act in good faith or in a business-like manner. The reinsurer is entitled to sufficient information from the reinsured to enable it to form a view.

Where there is no 'follow-the-settlements' clause in the reinsurance contract, the burden is generally on the reinsured to prove that the settlement of claim was in respect of a loss that, as a matter of fact and law, was covered under both the original insurance contract and the reinsurance contract. A 'follow-the-settlements' provision will not be implied, absenting express language.

Under Bermuda and English law, the term 'follow the fortunes' is not synonymous with 'follow the settlements', which comes into play when a settlement has been reached without judgment.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Each party to a contract of reinsurance must observe the utmost good faith towards the other throughout the negotiation of the contract and at all times thereafter (unless and until litigation or arbitration commences).

The reinsured and his agent are required to disclose to the reinsurer all material facts relating to the risks that are known (or which ought to be known) at the time the contract was entered into. A fact is 'material' if it would influence the judgement of prudent underwriters in fixing the premium or determining whether they will take the risk or the terms under which they would take it. Material non-disclosure by the reinsured entitles the reinsurer to avoid the contract, provided the reinsurer was induced to enter into the contract by reason of the non-disclosure.

There is no express statutory duty on the reinsurer in relation to non-disclosure of facts to the reinsured. While a deliberate non-disclosure by the reinsurer would be a breach of the duty of utmost good faith and allow the reinsured to avoid the contract, an innocent non-disclosure by the reinsurer may not.

Update and trends

In March 2016, Bermuda obtained full equivalence with Solvency II for its commercial insurers, effective from 1 January 2016, which allows Bermuda's commercial insurers to compete on an equal footing in writing business in the EU. With Brexit looming, and the terms of the UK's exit from the EU uncertain, the anticipated regulatory divergence between the UK and the EU that could result from Brexit may make Bermuda, as a Solvency II equivalent jurisdiction, an even more attractive domicile for insurers and reinsurers currently based in the UK to move to.

Although the duty of utmost good faith continues to apply to the performance of both parties' obligations following the making of the contract, the courts are not willing to imply such a term into the contract, and there is no basis under Bermudian law for awarding damages against an insurer or reinsurer for 'bad faith' handling of claims.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

The same body of law is generally applicable to facultative and treaty reinsurance. While a distinction may certainly be drawn between facultative and treaty reinsurance, categorising reinsurance contracts in such a way is not always straightforward.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

As a matter of common law there is no privity of contract between an insured and a reinsurer. The Contracts (Rights of Third Parties Act) 2016 came into force in Bermuda on 28 March 2016 and applies to any contract which, on or after the commencement date, includes terms that comply with section 4 (section 3(1)). Section 4(1) provides that:

> *'a third party may in its own right enforce a term of a contract if – (a) the third party is expressly identified in the contract – (i) by name; or (ii) as a member of a class; or (iii) as answering a particular description, but the third party need not be in existence when the contract is entered into; and (b) the contract expressly provides in writing that the third party may enforce such term of the contract.'*

Section 9 sets out a list of particular types of contract that are excluded. Thus, third-party rights may not be enforced in respect of bills of exchange, promissory notes or other negotiable instruments, employment contracts, a company's memorandum of association or by-laws, letters of credit, or contracts for the carriage of goods by sea, road or air. Insurance and reinsurance contracts are not excluded and therefore it appears that cut-through clauses that comply with section 4 are enforceable under Bermuda law subject to the question as to whether such a clause is valid if a reinsurer is in liquidation.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The reinsurer has no obligation to pay a policyholder's claim where the insurer is insolvent. The only obligation on the reinsurer is to pay the insurer (or its liquidator) on the terms and conditions of the reinsurance contract.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Reinsurance contracts typically require that the cedent give prompt notice of claims to its reinsurer. The notice provision may form part of the claims cooperation clause. Where strict compliance with such a clause is expressed to be a condition precedent to liability, then breach of the notice condition is sufficient to entitle the reinsurer to deny liability, and it is unnecessary for the reinsurer to show that any prejudice has resulted from the lack of notice. Where the notice provision is not expressed to be a condition precedent, the reinsurer must show that it has suffered prejudice as a result of the lack of notice. However, the degree of prejudice that is required before the reinsurer is entitled to deny liability is unclear.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

In the case of a single reinsurance contract, which is back-to-back with the original insurance contract, a business-like decision by the reinsured to settle a claim will bind the reinsurer under a 'follow-the-settlements' clause. However, where the underlying loss or claim arguably triggers more than one underlying insurance contract, it will be necessary for the reinsured to prove that the reinsurer is liable under the reinsurance contract that reinsures the underlying insurance contract to which the settlement has been allocated. See: *Municipal Mutual v Sea Insurance* [1998] Lloyd's Rep IR 421; *Equitas Ltd v R & Q Reinsurance Co (UK) Ltd* [2009] EWHC 2787 (Comm).

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

As discussed in question 41, where there is no 'follow-the-settlements' clause in the reinsurance contract, the burden is generally on the reinsured to prove that the settlement of claim was in respect of a loss which, as a matter of fact and law, was covered under both the original insurance contract and the reinsurance contract. In addition, it is common for reinsurers to include a provision in the reinsurance contract permitting the reinsurer to inspect the reinsured's file.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Where commutations have apportioned the amounts payable between particular claims made or between claims made and claims outstanding, or between claims made and incurred but not reported losses (IBNR), as between the cedent and the insured, the reinsurers may have an obligation to reimburse the cedent by virtue of a 'follow-the-settlements' clause. That said, the reinsurers may still be entitled to dispute the apportionment and an insurer proposing to enter into a commutation agreement is well advised to obtain the reinsurer's consent before doing so. Where a commutation is agreed in respect of IBNR, the reinsurers may be entitled to stand upon their strict contractual rights and deny liability on the basis that IBNR represents only an estimate of claims and not actual claims.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

In the absence of specific contractual wording imposing an obligation to pay ECOs a reinsurer will not, generally, be liable.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

In Brazil, there are two main bodies for regulating insurance and reinsurance companies: the Superintendence of Private Insurance (SUSEP) and the Private Insurance National Council (CNSP), both created by Decree Law No. 73/1966. SUSEP is a federal agency, established under Industry and Commerce Ministry competence, whose management is under a superintendent nominated by the President of the Republic, after an indication from the Industry and Commerce Minister. CNSP is formed by the Minister of Finance or his or her representative, a representative of the Minister of Social Security, the superintendent of SUSEP, a representative of Brazil's Central Bank and a representative of the Securities and Exchange Commission of Brazil.

Briefly, SUSEP's attributions involve the supervision of the formation, organisation and operation of insurance companies, capitalisation, private equity and reinsurers, executing policies determined by CNSP. Its duties include the protection of the popular savings collection, the defence of consumer interests, the promotion of development institutions aiming for Private Insurance National System improvement and the care of market solvency and stability. CNSP's duties could be summarised as:

- determining guidelines and norms for private insurance policy;
- regulating the formation, organisation and operation of companies subject to the Private Insurance National System;
- to determine general features of insurance, private equity, capitalisation and reinsurance contracts; and
- appreciate appeals from SUSEP's decisions and regulate the acting and profession of brokers and determine general guidelines for reinsurance operations.

It is important to mention that until 2008 reinsurance in Brazil was under the monopoly of IRB Brazil RE, which also possessed a regulatory competence by that time. Since 2008, the reinsurance market was opened after promulgation of Complementary Law No. 126/2007, which avoided the monopolist regime and constituted the main legal mark concerning reinsurance operations from that point forward.

Finally, the National Health Agency is specifically in charge of health insurance.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

To form an insurance company in Brazil, entrepreneurs must observe the provisions of Decree No. 60.459/1967, which regulates Decree Law No. 73/1966. Article 42 et seq provide the conditions for formation and licensing of new insurance companies. It is determined that licensing is conditional upon a ministerial order to be issued by the Industry and Commerce Minister, after a formal requirement signed by entrepreneurs to be sent to CNSP with a previous intermediation of SUSEP. This requirement must be instructed with proofs of the regular constitution of the company attending legal formalities and the deposit to be made in the Bank of Brazil to demonstrate its financial capacity, in addition to copies of its statute.

CNSP will appreciate this requirement considering its convenience and opportunity in light of national insurance policy, saturation of the national market, regularity within the company's constitution, and an assessment on success margins of its planned operations.

In case of approval, the ministerial order that concedes authorisation for the new company will indicate the branches within the company will be allowed to explore, as well as demands eventually presented conditioning its operations, which will be inserted within its statute. Once this ministerial order is published, the new company must present documents to SUSEP within 90 days, proving IRB's stocks capital subscription, registry and publication of all acts legally demanded for its operation, satisfaction of all demands eventually addressed within the ministerial order and the fulfilment of supplementary demands presented by SUSEP. After the fulfilment of all these formalities, a formal letter will be issued to be registered before SUSEP and published in the official journal of the republic, which will then provide the new company with the authorisation of its operations.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Insurance and reinsurance operations are under the strict supervision of the Private Insurance National System, specifically by SUSEP and CNSP. The licences and authorisations issued for the beginning of its operations must be closely followed by insurers and reinsurers, not only regarding the branches within which they are allowed to operate, but also the limits and provisions that must be observed in their daily operations, which are determined by SUSEP. For conducting business, companies must be attached to its original authorisations limits, besides periodical supervision assessments undertaken by SUSEP. Every change in its original formation and authorisation, such as for expanding branches for its operations, merging and acquisitions of other companies, etc, are subject to the previous evaluation and authorisation of SUSEP and CNSP.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

As determined in Circular CNSP 136/2005, the Brazilian insurance regulatory agency requires that officers and directors of insurance companies:

- are not prevented by law, judicial or regulatory decision from performing the job;
- have an unblemished reputation;
- are residents in the country;
- are not defendants in any lawsuits for collection of debts;
- are not insolvent; and
- are not the director or officer of a bankrupt firm.

It is also required that officers and directors of insurance and reinsurance companies are technically qualified for the job.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Minimum capital required is the total capital that insurance and reinsurance companies must maintain in order to operate, equivalent to the higher value between the base capital and the risk capital. Base capital is the sum of the fixed portion corresponding to the authorisation to operate insurance or private pension funds with the variable portion for operation in each one of the regions of the country. The fixed portion of the base capital is 1.2 million reais. The base capital's variable portion will be determined by the region where the insurance company has been authorised to operate. To operate in the whole country it corresponds to 15 million reais. For local reinsurers, the base capital that must be maintained, at all times, is 60 million reais. Risk capital is the variable amount of capital that the supervised body must maintain, at all times, to guarantee the risks inherent in its operations.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Decree Law No. 73/1966 provides that insurance companies must establish reserves, special funds and provisions to guarantee their obligations. In addition they must be in accordance with criteria set out by the CNSP.

CNSP, in turn, provides that insurance companies must establish the following reserves:

- provisions for unearned premiums;
- provision for payable claims (PSL);
- provision for losses incurred but not reported;
- mathematical reserves for current benefits;
- mathematical reserves for future benefits;
- supplementary provision for coverage;
- provisions for related expenses;
- provisions for technical surpluses;
- provisions for financial surpluses; and
- reserves for surrenders or other future policy benefits.

Reinsurers must establish the same reserves, excepting the reserves for surrenders or other future policy benefits.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

As well as all other kinds of contracts, insurance products offered for sale must observe general guidelines and limits imposed by the Brazilian Civil Code and Consumerist Law. Further to that, rules issued by SUSEP and CNSP equally regulate these products. Circular SUSEP 256, issued in 2004, provides contractual wordings and correspondent actuarial features of standardised (identical contractual wording), non-standardised (contractual wording created by insurer) and particular (product created for a specific policy, not for being commercialised with other insureds) products. It is important to state that all these products must be registered by SUSEP, even particular products, for control purposes.

Insurance products that are standardised are:

- performance bonds;
- liability insurance;
- transport insurance;
- logistics operator liability insurance;
- road transport liability insurance for missing cargo;
- real estate rental insurance;
- agricultural warranty insurance;
- popular car insurance;
- port operators' insurance; and
- forest insurance.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

As described in Decree Law No. 73/1966, article 5 of Decree Law, national policy regarding private insurance aims for the promotion of insurance market development and growth, the avoidance of currency evasion by means of a better balance related to commercial business exchange abroad, the defence of the reciprocity principle, conditioning authorisation and licensing of foreign companies to equal conditions as observed in their origin countries, the preservation of insurers' solvency and the coordination with federal government investment policy. In order to execute this policy to achieve these goals, CNSP determines the type and frequency of examinations, which are executed by SUSEP.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

CNSP is in charge of regulating investments that insurance and reinsurance companies may make. Resolution CNSP No. 88/2002 provides that insurance companies must constitute a special fund for financial investments, especially established for this purpose and in accordance with specific regulation from the National Monetary Council about the application of funds, reserves and provisions of insurance companies.

All investments must be registered in the name of the insurance company and assets should be held in custody, registered and maintained in a deposit account before the Special Custodial and Clearing System, entities authorised by the Central Bank of Brazil and the Securities Commission of Brazil. If an insurance company invests in real estate, the property must also be registered in its name. All information about any investments must be disclosed to SUSEP.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Resolution CNSP No. 166/2007 provides the requirements for a change of control of insurance companies. It is important to note that all changes of control of insurance companies must be previously and expressly authorised by SUSEP, who may impose specific conditions such as demonstration of economic and financial capacity compatible with the nature and size of the proposed undertaking and demonstration of the origins of the resources for the undertaking. Only people or companies with this special purpose and authorised by SUSEP can hold control of an insurance company.

Officers, directors and controlling persons of the acquirer are subject to background investigations as they must comply with the same requirements mentioned in question 4.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The acquisition of an insurance or reinsurance company in Brazil must be previously and expressly authorised by SUSEP and must comply with the following requirements:

- publish a statement of purpose;
- present the business plan, the actuarial technical note of the portfolio and the corporate governance standards;
- indicate the composition of the control group of the insurance company;
- demonstrate economical and financial capacity compatible with the nature and size of the proposed project;
- obtain express approval of all members of the control group;
- demonstrate the lack of restriction that can affect the reputation of control holders and qualified shareholders, in this case being

applicable to the same minimum qualification requirements for officers and directors of insurance and reinsurance companies; and
- demonstrate the origins of the resources for the undertaking.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no specific requirements regarding investors acquiring a minority interest in an insurance or reinsurance company, if such minority does not exceed 5 per cent of company's total shares (CNSP Resolution No. 166/2007). In such cases, one acquiring minority interest exceeding 5 per cent may be compelled to demonstrate economical and financial capacity compatible with the nature and size of the proposed undertaking and demonstrate the origins of the resources for the undertaking, as well as obtain approval of all members of the controlling group.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no special requirements or restrictions, with the same rules as for other foreign investments in Brazil being applicable. Foreign investment in an insurance or reinsurance company by foreign citizens, companies or governments is regulated by the same law as all other foreign investments in Brazil: Law No. 4131/62.

According to this law, foreign investors may invest in the same modalities available to resident investors. However, they must hire a representative in Brazil, name a tax representative and hire securities custody services. They are also subject to a series of other requirements such as registration before the Brazilian Central Bank and the Federal Revenue Service and opening an account in Brazil.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

As mentioned in question 10, only people or companies authorised by SUSEP can hold control of an insurance or reinsurance company. As mentioned in question 16, there is a concern in Brazilian law with cession of risk between companies of the same economic group. As such, all risk cessions between companies of the same economic group must be notified to SUSEP. Also, insurance or local reinsurance companies cannot cede to companies of the same economic group more than 20 per cent of the premium of each coverage.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

All of the legal framework applicable to insurance contracts is also applied to reinsurance agreements between insurance and reinsurance companies domiciled in Brazil. Further to that framework, Law No. 126/2007 establishes the main legal provision regarding reinsurance contracts in Brazil, determining several regulatory features for reinsurance agreements. This law provided the same agency responsible for the control of insurance operations (SUSEP) with the powers to control reinsurance and retrocession operations. In parallel, there is a similar provision assigning to the body responsible for regulating insurance contracts (CNSP) the powers to regulate reinsurance, retrocession and reinsurance brokers operations.

In addition to the above rules, there is a general rule with relevant effects over reinsurance agreements with insurance companies in Brazil, one that establishes that reinsurers will not respond directly to an insured or beneficiary with its respective share of the amount reinsured. This is considered a duty solely of the cedents that issued the insurance policy.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Complementary Law No. 126/2007 ended the reinsurance monopoly in Brazil and provided that insurers are authorised to freely choose their reinsurers, in accordance with some requirements, as follows:
- 40 per cent of the ceded risk must be contracted with local reinsurers;
- insurance or local reinsurance companies cannot cede to companies of the same economic group more than 20 per cent of the premium of each coverage (this limit is not applicable to performance bonds, export, rural and internal credit insurances and nuclear risks);
- all risk cessions between companies of the same economic group must be notified to SUSEP;
- local insurers and reinsurers cannot cede more than 50 per cent of their insurance and reinsurance operation; and
- life risks have to be exclusively ceded to local reinsurers.

SUSEP can make exceptions to these limits upon technical review.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

As provided for in article 84 of Decree Law No. 73/1966, all insurance and local reinsurance companies must establish technical reserves to guarantee their obligations in accordance with the requirements set out by CNSP. There are no collateral requirements for a specific reinsurance or insurance transaction in Brazil.

For a specific reinsurance transaction, local reinsurers are obliged to maintain a provision for PSL (see question 6). The provision for payable claims is established to cover all amounts to be settled. This reserve must be up to date and it must vary if the claim varies during loss adjustment proceedings.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

This matter is not expressly provided for in Brazilian law as there is no such custom in Brazil.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The most important law governing insolvent or financially troubled insurance and reinsurance companies is Decree Law No. 73/1966, which establishes circumstances when a special control regime can be applied over a specific company facing financial troubles, the conditions and objectives for this special control regime, the consequences of a failure to recover regular financial conditions and proceedings to face an insolvency or bankruptcy of the company.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

A provision determining the priority of claims to be paid by an insurance or reinsurance company in an insolvency proceeding has not been legally set, and so the order of preference of all claims to be paid by the insolvent company tends to be treated equally. According to CNSP Resolution No. 355/2015, which governs the special control regime and extrajudicial insolvency proceeding applicable to insurers and local

reinsurers, the order of credits to be paid might observe the general provisions of Law No. 11.101/2005 (the Bankruptcy Act), as follows:

- labour credits;
- real estate collateral warranted credits;
- tax credits;
- special privileged credits as defined in law;
- general privileged credits as defined in law;
- further credits not specified before;
- contractual penalties;
- subordinated credits as defined in law; and
- partners and officers of the insolvent company.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Brokerage activity is regulated by Decree Law No. 73/1966, Law No. 4.594/1964 and CNSP Rule No. 249/2012, which provide the following requirements for insurance brokers:

- being approved in a specific technical exam;
- being Brazilian or permanently residing in Brazil;
- being up to date with the military and electoral service;
- not having criminal convictions;
- not being bankrupt;
- not holding office at a public company; and
- not holding office at an insurance company.

Reinsurance brokers must be companies authorised by SUSEP, must have professional indemnity insurance and must have a specialised insurance broker as a technical manager.

'Insurance representative' is an activity regulated by CNSP Rule No. 297/2013. It must be performed by a company that does not perform brokerage activities.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Given that the main object of an insurance contract acknowledges that its goal is to guarantee legitimate interests, and regarding the social features affected by this kind of contract, it seems that it clearly protects third-party interest affected by the conduct of an insured, especially considering liability insurance contracts. Therefore, the possibility of a third party bringing a direct action against an insurer should be widely recognised. However, although there is a remarkable movement towards its acceptance, its application in Brazil is still timid, with a few leading case decisions recognising this possibility (ie, Recurso Especial No. 1245618).

On the other hand, there is a strong resistance against it, as seen in Pronunciation 529 issued in 2015 by the Brazilian Higher Court (Federal Court): 'in facultative liability insurance, it is not admitted to a third party to bring an action direct and exclusively against the insurer of the party responsible for the damages'. In accordance with this pronunciation, it could only be accepted if the plaintiff brings an action against both the insured and its insurer at the same time.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

According to the Brazilian Civil Code, subject to losing indemnification rights, the insured must inform a loss to the insurer as soon as it is aware of its occurrence (article 771). This article, however, does not establish a formal deadline to the notice of a claim. Despite this legal gap, there are important jurisprudential precedents stating that only a late notice could not avoid the insured's rights related to coverage and indemnification, imposing insurers to demonstrate direct negative consequences of this late notice (ie, the impossibility of adjusting the loss, obstacles impeding a proper investigation about causes and conditions of the loss, etc) as a condition to allow them to deny a claim.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Wrongful denial of a claim on its own is not sufficient to expose an insurer to extra-contractual payments. In Brazil, it is expected that the insured prove the damages caused, such as loss of profits or indirect damages suffered, as a result of the denial of a claim by the insurers in bad faith. Further, it is expected that insureds prove the causal connection between the wrongful denial and its alleged negative impacts.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The most common trigger is when the insured is summoned to respond to an action proposed by a third party. This trigger, however, depends on the insurer's previous assessment of the insured's rights according to the policy and to the loss, an evaluation that, sometimes, even in bad faith, is made only to dismiss a claim, causing additional difficulties to insureds that might litigate against both the third party and the insurance company.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The trigger is either a favourable conclusion of a loss adjustment process, or, in case of a denial (wrongful or not) a judicial or arbitral decision in favour of the insured.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

There is no legal provision establishing such a period. What rules this kind of situation is the principle of good faith, which determines a detailed assessment of the behaviour of the parties regarding this issue in order to identify, for example:

- if the insured deliberately omitted information, which he or she previously recognised would have impacted the issuance of the policy;
- if the insurer was negligent during the conclusion of the insurance contract and therefore could not deny a claim afterwards; or
- if, based upon the behaviour of the insured, it could not defend that the determined health condition was unknown, etc.

It is important to add that it is up to the insurer to demonstrate and prove that the insured lacked good faith in order to deny a claim, according to majority jurisprudential understanding.

28 Punitive damages

Are punitive damages insurable?

In Brazilian law, there is no concept equivalent to punitive damages, although references to it are commonly observed in Brazilian doctrine as a criterion to measure moral damages indemnification. Applying this most similar concept (moral damages), it is insurable in certain kinds of insurance contracts.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

The excess insurer has an independent relationship to the insured, which is not affected by the primary insurer's fate. If the primary insurer is insolvent or its coverage is unavailable for whatever reason, the excess insurer is still obliged to pay a claim if its value is above primary policy limits.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

If the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it, this situation must be interpreted according to principles applied to insurance contracts. It could be understood as a hard case, nevertheless; it should not be argued as a condition to deny a claim, mostly if considered a total loss with multiple and severe impacts over insured financial conditions. Therefore, considering the good faith principle, applicable to any contracts and, regarding article 765 of the Brazilian Civil Code, with special effects within insurance contracts, it seems that the best solution should implicate insurer payment excluding the amount of the limit to be paid exclusively by the insured.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is no legal provision in Brazil determining the order of priority for payment when there are multiple claims under the same policy. The best way to solve this kind of situation is to look for conditions established within policy wordings with regards to the conditions of the loss to set up the priorities for payment in this hypothesis. In addition, regarding liability insurance, in cases of multiple victims equally affected by the same loss, it is common to establish within loss adjustment criteria the determination of equivalent indemnification for each one of them (in cases of consumption of the total limit of coverage, to divide it equally among the victims).

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

It is a common condition of policies issued in Brazil to establish, in cases of multiple policies covering the same claim, that a proportional division of the indemnification will occur regarding the calculation, taking into account each one of the limits of the policies which cover the loss.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

In Brazil, there are no specific legal provisions equivalent to disgorgement claims.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

There is a lack of legal provision regarding circumstances where a single event results in multiple claims constituting more than one loss under an insurance policy. Therefore, courts usually apply provisions from the wording of the policies, which commonly define criteria for indemnification of multiple claims arising from a single event. It is a standard provision that the policy limit will not be exceeded if multiple claims emerged from a same event. When the limit is reached, the total amount should be divided among the claims presented to the insured, equally or accordingly to provisions of the contract.

This situation is defined as successive losses (*sinistros em serie*), and establishes different coverage caps for each claim emerging from the same event. Therefore, for instance, it is commonly established that a first claim would be indemnified on a 100 per cent basis of the amount of the loss, the second on an 80 per cent basis, the third on a 60 per cent basis and that those further on would not be covered.

Sometimes in liability insurance policies when multiple injuries or claims emerge from the same event there is an issue related to the calculation of deductibles, considering on one hand the insured's interest in the single application of the deductibles established in contract for each event, and on the other the insurer's interest in its multiplication for the number of claims. Commonly, policies clearly determine what criteria should prevail and, in cases of a gap, the principle 'in dubio pro insured' is given, which determines that if there are any doubts arising from the wording of the policy, these might be interpreted in favour of the insureds, and the most positive definition regarding insured's interests should be applied.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Article 766 of the Brazilian Civil Code provides that deliberate misstatements can be the basis for rescission, even before or after a loss. Despite this rescission, the insured is still obliged to pay the premium. If misstatements are not previously deliberated and intentional, but rather unwilful, the insurer can decide either if it wants to rescind the contract or collect the additional premium. However, in responding to abuse committed by insurers against insureds, Brazilian courts have decided that, if discovered after the loss, unintentional misstatements cannot be used to deny the claim, unless the insurer proves that incorrect information was deliberately given to mislead the insurer and that it implies aggravation of the risk.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Insurers and reinsurers usually prefer business solutions for their disputes, particularly up to 2007 when the reinsurance market was under a monopoly regime operated by IRB, a state-owned reinsurer. However, since 2007 this has started to change, as formal dispute resolutions have become more and more common in Brazil. Although there is a lack of statistics published regarding this issue, it is possible to affirm that reinsurers tend to prefer arbitration as a dispute resolution proceeding. Arbitration in Brazil is regulated by Law No. 9.307/1996 (the Arbitration Act).

There is no body of law that serves as a precedent for issues arising in the litigation of reinsurance disputes in Brazil.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

The most common issues arising are as follows:

- the method of calculation of the reinsurance premium;
- in facultative reinsurance, the refusal of the reinsurer to reimburse the reinsured, alleging that an insurance claim should not have been paid;
- allocation of the loss in different reinsurance policies; or
- failure to provide information (declaration of risk) in the placement of reinsurance business.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Every award in Brazil, judicial or arbitral, must include reasoning. Specifically regarding arbitration, the Arbitration Act provides that all arbitration awards must contain a report of the facts of the dispute, the grounds of the decision, its reasoning and the operative part. If an arbitration award does not include reasoning for the decision, it is void.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

In Brazil, arbitration proceedings are regulated by the Arbitration Act. The provisions of this law, as well as their jurisprudential understanding consolidation, determine that only parties that have signed the arbitration clause, or entered an arbitration agreement, are bound to the arbitration, its decisions and effects of them. Therefore, reinsurance

Update and trends

Brazil lacks a specific law regulating insurance contracts, which is very concerning when contemplated because it means that the two main insurance regulatory milestones could be considered outdated (Decree Law No. 73/1966, from 1966, and the Brazilian Civil Code, which dates from 1975). For this reason, the imminent introduction is expected of the first insurance contracts law in Brazil (Bill No. 8290/2014), which was based on studies developed by a commission of jurists coordinated by Ernesto Tzirulnik, president of the Brazilian Institute of Insurance Law. The relevant features of the Bill have already been academically recognised abroad, inspiring researchers in Latin America and Europe. Once approved, it is expected to stimulate new standards for insurance in Brazil by solving relevant issues, which as yet are not adequately treated, and to improve the grounds for insurance development in the country. In December 2016, the bill was unanimously approved by a special commission of Deputy's House, and was then submitted to the Senate. It is expected to be approved soon.

arbitrators in general do not have powers over non-parties to the arbitration agreement. An exception is made to specific circumstances where the effects of a decision overcome the limits of the dispute, but there is not a priori defined powers over non-parties to the arbitration agreement.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

There is little space for parties to vacate or modify arbitration awards through the judicial system, as the Arbitration Act provides that arbitration awards are not subject to appeals, with extremely strict exceptions. These are, for example, circumstances which determine that an arbitration award is void (article 32). Furthermore, it is important to note that a party is authorised to question through judicial proceedings an additional arbitration award, if the original award had not decided every issue involved in the arbitration. This additional award shall be provided by the same arbitrator panel.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The follow-the-fortunes principle is a consequence of the independence of the contract of reinsurance in relation to the contract of insurance which is established in article 14 of Complementary Law No. 126/2007. A reinsurer can only circumvent the principle by evidencing that an insurance loss allocated in the contract of reinsurance was paid in bad faith as, for instance, an ex gratia insurance payment.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

According to article 5 of Law No. 126/2007, rules applicable to insurers are also applicable to reinsurers. Considering article 765 of the Brazilian Civil Code, which provides that insurer and insured must behave under the principle of utmost good faith, this duty is also implied in reinsurance agreements. In principle, this duty does not differ too much from other commercial agreements, once there are provisions within the Brazilian Civil Code that establish good faith as a general rule that is supposedly binding in all kinds of contracts. A feature that could be considered as a distinctive aspect of reinsurance (and insurance) is that a great part of the agreement is based on unilateral statements of the parties. Therefore, utmost good faith is a requisite to protect, or try to protect, transparency and cooperation through all contractual relationships, from initial conversations through to their execution.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There are no different sets of laws for facultative reinsurance and treaty reinsurance. Both are regulated by Complementary Law No. 126/2007 and CNSP Rule No. 168/2007.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Article 14 of Complementary Law No. 126/2006 provides that reinsurers and retrocessionaires cannot be directly sued by the insured or the beneficiary of a policy. The only legal exception for this rule is when the insurer is insolvent, if it is a facultative reinsurance or if there is a cut-through clause within the insurance policy. This provision is in accordance with jurisprudence and doctrine that unanimously recognise that the insurer is the only one with responsibility for the payment of the insured's claim.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Article 14 of Complementary Law No. 126/2007 provides that the only hypothesis where the reinsurer is responsible for paying a policyholder's claim is when the insurer is insolvent, if it is a facultative reinsurance or if there is a cut-through clause within the insurance policy.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

There is no specific rule in Brazilian law about this matter. Considering the good faith principle, also applicable to reinsurance contracts (see question 42), a claims notice must be made as soon as possible and with sufficient information. However, there is no legal sanction if a claim is made tardily or insufficiently, unless said tardiness or insufficiency affects the reinsurer's defence. In other words, a high level of transparency must be assumed between insurer and reinsurer.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

There is no specific legal provision on this matter in Brazil. As discussed in question 32, it is a common condition of policies issued in Brazil to establish, in case of multiple policies covering the same claim, that a proportional division of the indemnification will occur regarding a calculation that takes into account each one of the limits of the policies that cover the loss.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

As mentioned above, reinsurers cannot review insurer's decisions. Contracts of insurance and reinsurance are independent from each other, as provided for in article 14 of Complementary Law No. 126/2007. A reinsurer can only defend itself from a reimbursement claim from its reinsured by evidencing that an insurance loss allocated in the contract of reinsurance was paid in bad faith, as for instance an ex gratia insurance payment.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

In Brazil there is no room for commutation payments made by the cedent to its policyholders. Therefore, no reimbursements are feasible.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

The reinsurer is not obliged to reimburse a cedent for extra-contractual obligations if they arise from bad faith and fraud. In any other case of extracontractual obligation, the reimbursement is due.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Insurance is regulated in Canada at both the federal and provincial or territorial levels.

The federal government has the constitutional power to regulate the solvency and corporate governance of federally incorporated insurers and the solvency of branch offices of foreign insurers. This regulatory oversight is performed by the Superintendent of Financial Institutions (Superintendent) through the Office of the Superintendent of Financial Institutions (OSFI), pursuant to the provisions of the Insurance Companies Act (ICA), the regulations thereto and guidelines published by OSFI. The ICA also contains consumer protection provisions regulated by the Financial Consumer Agency of Canada.

Canada's 13 provinces and territories have exclusive constitutional jurisdiction to regulate market conduct with respect to the sale of insurance in their jurisdictions, including the types of insurance that may be sold and who may sell insurance. In addition, the provinces regulate the solvency and corporate governance of provincially incorporated insurers. The provinces and territories also regulate insurance agents, brokers and claims adjusters. Reinsurance intermediaries are not regulated in Canada. Each province and territory has its own insurance legislation, administered by an insurance commission or other regulatory body run by a commissioner or superintendent of insurance.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Incorporation of a federal insurer under the ICA is granted at the discretion of the federal Minister of Finance (Minister) upon the recommendation of the Superintendent. In determining whether to approve an application to incorporate an insurer, the Minister must take into account:

- the nature and sufficiency of the financial resources of the applicant;
- the soundness and feasibility of the applicant's plans for the future conduct and development of the insurer;
- the applicant's business record and experience;
- the character and integrity of the applicant;
- the competence and experience of the management;
- the impact of any integration of the operations and businesses of the applicant with those of the insurer on the conduct of those operations and businesses; and
- the best interests of the financial system in Canada.

A government or government agency (whether Canadian or foreign) or an entity controlled by a foreign government (other than an entity that is a foreign financial institution or a subsidiary of a foreign financial institution) is not eligible to apply to incorporate an insurance company under the ICA.

A branch office of a foreign insurer may be registered under the ICA by applying to the Superintendent for an order permitting the foreign insurer to 'insure in Canada risks'.

Every applicant seeking to incorporate an insurance company or register a branch under the ICA must prepare a comprehensive submission that addresses the financial strength and business experience of the owners, and includes a detailed business plan that demonstrates the potential for a successful business operation and compliance with OSFI's minimum capital or asset requirements.

Insurance companies may also be incorporated under provincial law. The application requirements are similar to those under the ICA.

Regardless of its jurisdiction of incorporation or whether it operates as a branch of a foreign insurer, an insurer must be licensed in each province and territory in which it carries on business.

There is no special licensing category under the ICA or provincial or territorial legislation for reinsurers.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Where the applicant for incorporation is a non-resident or a foreign company is applying to register a Canadian branch, the applicant or foreign company must provide evidence that Investment Canada has been notified under the Investment Canada Act (see question 13).

Property and casualty insurers must become members of the Property and Casualty Insurance Compensation Corporation (PACICC) and life insurers must become members of the Canadian Life and Health Compensation Corporation (Assuris). PACCIC and Assuris are industry-run guarantee funds.

Certain provinces and territories require that, in addition to obtaining an insurance licence, insurers be extra-provincially registered in the jurisdiction.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

All proposed directors (or the chief agent in the case of a foreign branch application) and senior officers must submit biographical information to OSFI and undergo to a security background check. OSFI will need to be satisfied that the proposed directors and officers possess the competence, skill and integrity commensurate with the proposed position of the individual within the company. The role and functions of a chief agent closely resemble those of a chief executive officer of a Canadian insurance company.

Persons disqualified from being directors of a company include:

- those under 18 years of age;
- those of unsound mind;
- those who have bankrupt status;
- employees of a Canadian or a foreign government; and
- insurance agents or brokers of the company.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

The capital of an insurance company incorporated under the ICA must, at all times, meet OSFI's minimum capital guidelines. A property and casualty insurer's minimum required capital is the sum of:

- capital required for unpaid claims and premium liabilities;
- catastrophe reserves;
- margin required for reinsurance ceded to unregistered reinsurers;
- capital required for interest rate risk;
- capital required for foreign exchange risk;
- capital required for equity risk;
- capital required for real estate risk;
- capital required for other market risk exposures;
- capital required for counterparty default risk for balance sheet assets;
- capital required for counterparty default risk for off-balance sheet exposures;
- capital required for collateral held for unregistered reinsurance and self-insured retention; and
- capital required for operational risk.

A life insurer's minimum required capital is the sum of the capital requirements for each of the following risk components:

- asset default risk;
- mortality, morbidity or lapse risks;
- changes in interest rate environment;
- segregated fund risk; and
- foreign exchange risk.

New capital and surplus requirements will come into effect on 1 January 2018 for life insurers. Under these new requirements, capital will be required for the following risk components:

- credit risk;
- market risk;
- insurance risk;
- segregated fund guarantee risk; and
- operational risk.

OSFI will start to progressively intervene where an insurer's capital ratio falls below 150 per cent. As a result, OSFI expects the board of an insurance company incorporated under the ICA to establish an internal capital target ratio in excess of 150 per cent. Many such companies currently have internal capital ratio targets in excess of 200 per cent.

Branches of foreign insurers registered under the ICA are subject to similar guidelines. Branches must vest in trust with the Superintendent of assets sufficient to meet its internal capital target ratio.

Provincially incorporated insurance companies must comply with similar capital requirements.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

The liabilities shown in the annual return of a company incorporated under the ICA or of a branch of a foreign insurer registered under the ICA must contain a reserve for the value of the actuarial and other policy liabilities of the company or branch. Such a company or branch must have an appointed actuary who must value the actuarial and other policy liabilities of the company or branch in accordance with Canadian accepted actuarial practice, subject to such changes and additional directions that may be made by OSFI.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance products and market conduct by insurers are exclusively regulated by provincial or territorial insurance regulators. Provincial and territorial insurance legislation contains general provisions with respect to insurance policies (other than life, accident and sickness and marine insurance policies) and specific provisions with respect to fire, motor vehicle, life and accident and sickness policies, including statutory conditions that are deemed to be included in such policies. Those provinces and territories that permit private insurers to underwrite motor vehicle insurance mandate the form of motor vehicle policies. There are no other policy form requirements, and insurers are not required to file their policy forms with insurance regulators, nor to obtain approval of policy forms.

Insurers are not required to file rates or obtain approval for rates, with the exception of motor vehicle insurance rates.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

OSFI's supervision of an insurance or reinsurance company depends on the nature, size, complexity and risk profile of the company, and the potential consequences of its failure. OSFI designates a relationship manager for each company to conduct periodic assessments. OSFI's approach is based on the following principles:

- focus on material risk;
- forward-looking assessments and early intervention;
- sound, predictive judgement;
- understanding the drivers of risk;
- differentiation of inherent risks and management thereof;
- continuous and dynamic adjustment; and
- assessment of the whole institution.

Many insurers and reinsurers are reviewed annually by OSFI. Canadian provinces and territories have exclusive jurisdiction to regulate market conduct with respect to the sale of insurance (see question 1), and the relevant provincial or territorial insurance regulators conduct separate assessments of an insurance company's market conduct in each province or territory in which it sells insurance. Reinsurance companies are not subject to such market conduct assessments.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The ICA permits investments in accordance with written investment and lending policies, standards and procedures that a reasonable and prudent person would apply in respect of a portfolio of investments and loans to avoid undue risk of loss and obtain a reasonable return. This basic standard for investments is limited by express restrictions with respect to commercial and consumer lending, real estate investments, investments in equities and investments in real estate and equities. The ICA provides different restrictions for each of those types of investments for property and casualty insurance companies in Canada, registered branches of foreign property and casualty insurance companies in Canada, life insurance companies in Canada and registered branches of foreign life insurance companies in Canada.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Both the acquisition of more than 10 per cent of any class of shares (a 'significant interest') and the acquisition of control of an insurance company incorporated under the ICA require the approval of the Minister. 'Control' for this purpose includes de jure and de facto control.

An applicant that proposes to acquire control must submit a detailed application to OSFI that includes:

- information concerning the applicant's home regulator and confirmation from the applicant's home regulator that it reports favourably on the applicant (if the applicant is a financial institution);
- the names of all persons owning more than 10 per cent of any class of shares of ownership interests in the applicant;
- a description of how the applicant will fund the acquisition;
- financial information concerning the applicant;

- information on any change the applicant proposes to make to the company's board of directors, senior management, risk management policies or procedures and business plan; and
- a support-principle acknowledgement letter signed by the applicant acknowledging the applicant's responsibility to support the operations and capital needs of the company.

In making a decision on whether to approve an application to acquire a significant interest, the Minister is required to consider, inter alia:

- the business record and experience of the applicant;
- the character and integrity of the applicant;
- whether the applicant has the financial strength to acquire control and to support the ongoing operations of the company;
- whether the transaction will be in the best interests of the Canadian financial services sector; and
- where the applicant is not a WTO member resident, whether the jurisdiction of residence of the applicant provides reciprocal treatment to Canadian financial institutions.

The applicant, including any controlling person (if an individual) and any new individuals who will be appointed to the board of directors or as senior managers will be subject to background investigations by law enforcement and intelligence agencies.

The Competition Tribunal has authority under the Competition Act to block a purchase of shares or assets (a merger) that substantially prevents or lessens, or is likely to prevent or lessen, competition. The Competition Act requires prior notification of substantial mergers to the Commissioner of Competition.

If the applicant proposing to acquire control of an insurance company is a foreign citizen or company, the acquisition may be reviewable under the Investment Canada Act (see question 13).

A change of control of a foreign insurer that has registered a branch under the ICA is not subject to any approvals under the ICA; however, the transaction may be notifiable under the Competition Act (see above) and may be reviewable under the Investment Canada Act (see question 13).

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

OSFI has not issued any explicit guidance with respect to the financing of an acquisition of control of an insurance company incorporated under the ICA. However, such companies are themselves subject to borrowing restrictions. While OSFI will permit a modest amount of debt in a holding company, OSFI will be concerned if the level of debt could impose an unreasonable burden on the insurance company to make distributions to the holding company to service this debt.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

Investments that are considered to be a 'significant interest' in an insurance or reinsurance company require the approval of the Minister (see question 10). Below that threshold, there are no regulatory requirements or restrictions.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

An insurance company incorporated under the ICA is not permitted to register in its securities register or transfer or issue any share of the company to a foreign government or foreign government agency or an entity controlled by a foreign government. There are no other restrictions in the ICA on foreign citizens or companies investing in a Canadian insurance or reinsurance company. However, certain approvals may be required before making the investment (see question 10).

Subject to some exceptions, acquisitions of Canadian businesses above a certain size by a non-resident are reviewable under the Investment Canada Act. The Minister of Industry can block an acquisition if he or she is not satisfied that the acquisition is likely to be of net benefit to Canada. Whether or not an acquisition is reviewable, a non-resident is required to notify Investment Canada under the Investment Canada Act with respect to an investment to establish a new Canadian business.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The supervision of Canadian insurance and reinsurance companies is principles-based (see question 8) and conducted on a consolidated basis, which involves an assessment of all of an insurance or reinsurance company's material entities (including all subsidiaries, branches and joint ventures), both in Canada and internationally. Canada has not adopted the EU's Solvency II framework for the supervision of groups of companies having a head office outside of Canada, but the Canadian model has a number of features similar to Solvency II, such as the three-pillar approach and the own risk and solvency assessment. A number of guidelines issued by OSFI are relevant to group supervision, including those issued in respect of regulatory capital and internal capital targets, own risk and solvency assessments, stress testing and enterprise risk management. No holding company or group capital requirements exist in addition to individual entity capital requirements for insurers and reinsurers.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

OSFI has issued a Guideline on Sound Reinsurance Practices and Procedures (Reinsurance Guideline) that requires insurers and reinsurers to ensure that the terms and conditions of reinsurance contracts provide clarity and certainty on reinsurance coverage. If a final, comprehensive contract cannot be executed prior to the effective date, the parties must have entered into, prior to such date, a binding written slip, cover note or letter of intent that sets out the principal terms and conditions of the reinsurance. The parties are required to enter into a final, comprehensive reinsurance contract within a relatively short time frame that has regard to the nature, complexity and materiality of the agreement.

The Reinsurance Guideline further requires that reinsurance contracts contain an insolvency clause clarifying that the reinsurer must continue to make full payments to an insolvent cedent without any reduction resulting solely from the cedent's insolvency. In addition, 'off-set' and 'cut-through' clauses and the structure of 'funds withheld' arrangements and other such types of terms and conditions must not be used to frustrate the scheme of priorities under the Winding-Up and Restructuring Act (WURA) (see question 19). Finally, the Reinsurance Guideline states that OSFI expects all reinsurance contracts to stipulate a choice of forum and a choice of law.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

The Reinsurance Guideline (see question 15) now requires a cedent to have a sound and comprehensive reinsurance risk management policy (RRMP). OSFI expects the RRMP to document the cedent's approach to managing risks through reinsurance including, inter alia, risk concentration limits and ceding limits. The Reinsurance Guideline states that a cedent generally should not, in the normal course of business, cede 100 per cent or substantially all of its risks in the main areas in which it conducts business. A cedent may, however, occasionally cede a

portion, or even 100 per cent, of a specific line of business or a particular type of risk that is ancillary to its core business.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

A reinsurance company is not required by law to post collateral in a reinsurance transaction. However, a company incorporated under the ICA or a branch of a foreign insurer registered under the ICA is not permitted to take credit for reinsurance ceded to an unregistered reinsurer unless that reinsurer posts collateral. Accordingly, most reinsurance contracts with unregistered reinsurers require that they post collateral. The amount of collateral required is negotiable; however, in order for the cedent to take full credit for the reinsurance, the amount must equal the actuarial value of the ceded liabilities (including reserves for outstanding claims and unearned premium, if any), plus the margin held by the cedent with respect to such ceded liabilities under OSFI's minimum capital guidelines (see question 5).

Where the cedent is an insurance company incorporated under the ICA or the branch of a foreign insurer registered under the ICA, such collateral must be deposited with a custodian in Canada pursuant to a reinsurance security agreement, and the unregistered reinsurer must have granted a security interest in favour of the cedent over the collateral. The cedent must also obtain an opinion from legal counsel that confirms that the security interest in the pledged assets is legally enforceable against all other creditors of the unregistered reinsurer, including in the event of insolvency, and that the security interest over the collateral constitutes a valid, first-ranking security interest.

Alternatively, an unregistered reinsurer may deposit sufficient assets with the ceding company (sometimes referred to as 'funds withheld'). If this option is used, the reinsurance contract must clearly provide that, in the event of the cedent's or reinsurer's insolvency, the funds withheld, less any surplus due back to the reinsurer, must form part of the cedent's general estate.

A letter of credit can only be used to collateralise a maximum of 30 per cent of the liabilities reinsured with an unregistered reinsurer. The letter of credit must adhere strictly to OSFI's requirements.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

See question 17.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The Superintendent may, pursuant to the ICA, take control of an insurer incorporated under the ICA or the assets of a branch of a foreign insurer registered under the ICA where, inter alia, the company or the branch has failed to pay its liabilities or, in the opinion of the Superintendent, will not be able to pay its liabilities as they become due and payable, or the assets of the company or the branch are not, in the opinion of the Superintendent, sufficient to give adequate protection to its policyholders and creditors.

The WURA governs insolvent or financially troubled insurance and reinsurance companies, including branches of foreign insurers registered under the ICA and insurers incorporated under provincial or territorial laws. The WURA provides that, where the Superintendent has taken control of an insurer or the assets of the branch of a foreign insurer pursuant to the ICA, a court may make a winding-up order in respect of the insurer or branch.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The WURA governs insolvency proceedings of insurance and reinsurance companies in Canada. The WURA provides that all costs, charges and expenses properly incurred in the winding-up of a company, including the remuneration of the liquidator, are payable out of the assets of the company, in priority to all other claims. In general, the company must then satisfy certain obligations for unpaid salary and wages to employees in the three months before the commencement of the winding-up, then its obligations to policyholders and to its secured and unsecured creditors, in that order. To the extent any assets remain, they are distributed among the members or shareholders according to their rights and interests in the company. The WURA expressly preserves the law of set-off, at law or equity, with respect to all claims on the estate of a company and to all proceedings for the recovery of debts due or accruing due to a company at the commencement of the winding-up of the company, in the same manner and to the same extent as if the business of the company was not being wound up.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Insurance agents, brokers and claims adjusters must be licensed in each province or territory in which they sell insurance or adjust claims. Managing general agents (MGAs), managing general underwriters (MGUs) and third-party administrators (TPAs) are required to be licensed if their activities cause them to fall within the definition of an insurance agent or broker under the relevant provincial or territorial insurance legislation. Generally, an 'agent' is defined as a person who solicits insurance on behalf of an insurer or transmits an application for, or a policy of, insurance to or from such insurer, or acts in the negotiation of such insurance. As a result of the breadth of this definition, an MGA, MGU or TPA may find that it must obtain provincial or territorial agent licences. When it comes into force, the new Saskatchewan Insurance Act will require MGAs to be licensed.

Currently, reinsurance intermediaries do not need to be licensed, as long as none of their activities would cause them to fall within the definition of an insurance agent or broker within the relevant provincial or territorial insurance legislation.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Insurance statutes in all provinces and territories, except Quebec, provide that a third party may bring an action against a liability insurer (other than a motor vehicle insurer) if the insured under the liability policy is found liable for injury or damage to the person or property of the third party, and fails to satisfy a judgment awarded against the third party in respect of his or her liability. In the case of motor vehicle insurance, insurance statutes in all provinces and territories, except Quebec, provide that a third party has a right of action to recover directly from the motor vehicle insurer.

In Quebec, an injured third party may bring an action directly against the insured or the liability insurer, or against both, under the Civil Code. In Quebec, motor vehicle insurance is dealt with on a first-party, no-fault basis.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Insurance statutes in all provinces and territories, except Quebec, provide for relief from forfeiture in the court's discretion, where there has been imperfect compliance with respect to the notification of loss requirements in the policy, but excluding contracts of life insurance, and in most provinces, marine insurance. Unless the insurer has been prejudiced by late notice, relief from forfeiture will usually be granted to the insured by the court. However, relief from forfeiture on the grounds of lack of prejudice is not available for failure to bring an action against an insurer within an applicable limitation period. In Quebec, the Civil Code provides that if a property and casualty insurer sustains injury because of late notice of a claim, the insurer may invoke any clause of the policy that provides for forfeiture of the right to indemnity.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Punitive damages have been awarded against insurers for wrongful denial of claims where the court has found that the insurer acted in bad faith and engaged in conduct that was high-handed, malicious, arbitrary or highly reprehensible. Aggravated damages have been awarded where wrongful denial of a claim caused foreseeable mental distress to the insured.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Generally speaking, a liability insurer's duty to defend is triggered where the pleadings allege acts or omissions that fall within the policy coverage. Allegations in the pleadings that are not supported by the factual allegations made therein or allegations of negligence that are derivative of the harm caused by intentional conduct do not trigger a duty to defend. A liability insurer is only required to defend those allegations that potentially fall within the scope of the policy, and the insured is responsible for the defence of allegations that clearly fall outside the scope of the policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

An insurer's payment obligations under an indemnity policy are triggered by proof that an insured event has occurred that is within the scope of coverage afforded by the policy, and that the insured has suffered a financial loss as a result. While a claim may include both covered and uncovered claims, only covered claims are indemnifiable.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Insurance statutes in all provinces and territories provide that a life insurer cannot contest coverage based upon non-disclosure or misrepresentation where the policy has been in effect for two years during the lifetime of the person whose life is insured, unless there was fraud. The right to void coverage within this two-year period is limited to non-disclosure or misrepresentation of facts within the applicant's knowledge that are material to the insurance.

28 Punitive damages

Are punitive damages insurable?

This issue has not been extensively considered in Canada. However, in one Ontario case, the court held that insuring punitive damages is contrary to public policy.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

There is jurisprudence in some provinces to the effect that the fact that the primary insurer is insolvent will not, in and of itself, require the excess insurer to 'drop down and defend'. In these cases, the courts held that an obligation on the part of the excess insurer to drop down and defend must be found in the terms of the excess policy, which can in certain cases be broader than the terms of the primary policy.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

There appears to be no Canadian jurisprudence on an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and the insured is insolvent and unable to pay the self-insured retention or deductible. As a result, the court would consider the facts of the case, including the policy wording, and any relevant English and US jurisprudence. Third-party liability insurance policies in Canada usually include a condition that bankruptcy or insolvency of the insured or of the insured's estate will not relieve the insurer from its obligations under the policy.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

With the exception of motor vehicle policies, the general rule adopted by Canadian courts is that, where there are multiple claimants under the same policy, payments are made on a first-come, first-served basis. Owing to specific statutory provisions in provincial and territorial insurance legislation, where there are multiple claimants under motor vehicle policies, payments are made on a pro rata basis.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

There is no established Canadian rule with respect to how indemnity payments should be allocated among multiple policies triggered by the same claim. In deciding how to allocate such payments, the court will consider a number of factors, including the policy wording and the coverage trigger theory or theories adopted by the court in that case. There is some Canadian jurisprudence supporting a pro rata allocation based on policy periods. There has been no judicial consideration of the 'all sums' approach adopted in some US jurisdictions, which allocates responsibility for the full amount of the claim to every insurer who was at risk during the continuous period during which the injury is considered to have occurred, although this approach has been referred to in several cases.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Generally speaking, third-party liability policies issued in Canada only cover the insured's liability to third parties for compensatory damages. Money payable by way of disgorgement or restitution is not normally considered to be damages and, therefore, is not normally covered under such policies.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

Most third-party liability policies issued in Canada define an 'occurrence' as an accident, including continuous or repeated exposure to substantially the same harmful conditions, or in words of similar effect. Where policies contain such a definition, Canadian courts have concluded that all injuries that flow from one cause or event are considered to result from one occurrence. However, where separate injuries result from separate acts, even though the acts may be of the same nature, each act constitutes a separate occurrence.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

In the case of property and casualty insurance, under the common law, a material misrepresentation by the policyholder in the application will render the policy void or voidable. The onus is on the insurer to show that the risk would have been material to a reasonable insurer, and that the insurer would have charged a higher premium or would have refused to underwrite the risk if the misrepresented facts had been correctly or truthfully disclosed to the insurer.

In the case of life insurance and accident and sickness insurance, under provincial insurance legislation, an applicant for insurance and a person to be insured must each disclose to the insurer in the application,

on a medical examination, if any, and in any written statements or answers furnished as evidence of insurability, every fact within the person's knowledge that is material to the insurance. A failure to disclose, or a misrepresentation of, such a fact renders the contract voidable by the insurer. A misstatement of the age of a person insured does not entitle an insurer to void the policy. In addition, where a policy has been in effect for two years, a failure to disclose or a misrepresentation of a fact required to be disclosed does not, in the absence of fraud, render the policy voidable.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Formal reinsurance disputes are not common in Canada. Most such disputes are dealt with by arbitration as opposed to litigation in court. While there is some Canadian jurisprudence with respect to substantive issues involving reinsurance, arbitrators are primarily guided by market practice, supplemented by consideration of English and US reinsurance jurisprudence.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Owing to the small number of reinsurance disputes and the fact that most are resolved by means of private arbitration, it is not possible to identify the most common issues that arise in such disputes. Examples of the issues involved in such disputes include underwriting and claims-related issues, failure to give timely notice of claims, and loss allocation and aggregation issues.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Canadian reinsurance arbitration awards are usually brief and rarely include any reasoning for the decision.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Provincial and territorial arbitration legislation generally provides that arbitrators may, in certain circumstances, issue a notice to a non-party witness to produce documents and to attend and give evidence at the arbitration. Generally, parties or arbitrators may also subpoena witnesses or request the court to subpoena witnesses.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Parties to reinsurance arbitrations can seek to vacate or enforce arbitration awards through the judicial system. The grounds upon which a court may set aside an arbitration award are quite limited. They include situations where:

- the award was beyond the scope of the arbitration agreement;
- the applicant was not treated equally and fairly, was not given an opportunity to present a case or respond to another party's case, or was not given proper notice of the arbitration or the appointment of an arbitrator;
- an arbitrator committed a corrupt or fraudulent act or there was a reasonable apprehension of bias; and
- the award was obtained by fraud.

The arbitration statutes confer upon the arbitration tribunal the right, either on its own initiative or at a party's request, to modify an award, to correct typographical errors, errors of calculation and similar errors, or to amend an award so as to correct an injustice caused by an oversight on the part of the arbitral tribunal. These statutes do not allow a party to apply to the court to modify an arbitration award.

If the arbitration involves a non-Canadian party, the provisions of the UNCITRAL Model Law of International Commercial Arbitration apply.

In addition, where there are no non-Canadian parties, if the arbitration agreement does not deal with appeals on the question of law, a party may appeal an award to a court on a question of law and, if the arbitration agreement so provides, a party may appeal to the court on a question of fact or a question of mixed fact and law. There is no ability to appeal an arbitration award where one of the parties is a non-Canadian.

The courts give a high degree of deference to arbitral awards.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The limited Canadian jurisprudence on follow-the-fortunes and follow-the-settlements obligations indicates that the courts will imply such terms upon satisfactory evidence that they are consistent with the intent of the parties and with market practice. Arbitrators will be primarily guided by the intent of the parties and market practice, supplemented by consideration of the limited Canadian jurisprudence and the much larger body of English and US jurisprudence on these concepts. The limited Canadian jurisprudence that exists indicates that these concepts will not require a reinsurer to pay losses that are outside the contractual scope of the reinsurance contract.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

It is a well-established principle of Canadian insurance law that an insurer owes a duty of good faith to its insured, and this same principle has been applied in the reinsurance context. The duty of good faith requires the cedent to disclose all material facts to the reinsurer. On the other hand, Canadian courts will not generally imply a duty of good faith in other commercial agreements. Where Canadian courts have implied such a duty in commercial contracts, they have done so to ensure that the actions of one party do not nullify the bargain made between the parties after the contract has been entered into. This duty does not require disclosure by one party to a commercial agreement of any material facts to the other party before a commercial agreement has been entered into.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There is no different set of laws for facultative and treaty reinsurance.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Canadian courts have consistently held that a policyholder or non-signatory to a reinsurance agreement cannot bring a direct action against a reinsurer for coverage. There is no Canadian jurisprudence on whether the beneficiary of a 'cut-through' clause could bring a direct action against a reinsurer. In any event, OSFI's Reinsurance Guideline prohibits the use of a cut-through clause in a reinsurance contract if it would frustrate the scheme of priorities under the WURA (see question 15).

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Canadian reinsurance contracts have for many years contained insolvency clauses that require the reinsurer to make full payments to an insolvent cedent without reduction solely from the cedent's insolvency. Insurers regulated by OSFI are now required to include such clauses in their reinsurance contracts (see question 15).

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The type of notice and information that a cedent must give its reinsurer with respect to an underlying claim depends upon the terms of the reinsurance contract. Most proportional treaties deal with claims in a bulk fashion by means of quarterly statements. Few reinsurance treaties nowadays require bordereaux reporting. Market practice with respect to proportional treaties is not to provide detailed information about underlying claims. Market practice with respect to excess of loss claims and facultative claims (both proportional and excess of loss) is to provide the reinsurer with copies of adjusters' reports and pleadings in the case of liability claims. To some extent, the amount of information provided may depend on the complexity or novelty of the claim.

There is no Canadian jurisprudence on the remedies available to a reinsurer where the cedent fails to provide timely or sufficient notice of an underlying claim. However, arbitrators generally apply the same approach as the courts in connection with late notice of claim by an insured, that is, that the cedent will not forfeit its right to recover unless the reinsurer has been prejudiced by the delay, although the language of the reinsurance contract may influence the arbitrators' decision in this respect. It is unclear how a Canadian court or arbitration panel might rule where the delay in giving notice of loss exceeds an applicable statutory limitation period.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

This issue is discussed in question 32. As there is no Canadian jurisprudence on this allocation issue, the policy wordings would need to be considered, and supplemented by market practice (if any) and by any relevant English and US reinsurance jurisprudence.

There is also no Canadian jurisprudence on how a loss or claim that provides for payment under multiple policies should be ceded to multiple reinsurance contracts or whether the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Almost all Canadian reinsurance contracts contain arbitration clauses requiring that disputes with respect to a cedent's claims handling, settlement and allocation decisions be referred to arbitration. As discussed in question 40, the courts give a high degree of deference to arbitral awards, from which the reinsurer may have limited or no rights of appeal (depending on the wording of the arbitration clause), and may have limited grounds to ask a court to set aside the award.

Where a reinsurance contract does not contain an arbitration clause, the reinsurer would be able to litigate in court issues involving a cedent's claims handling, and settlement and allocation decisions.

In both venues, arbitration and court, the decider will be guided principally by the reinsurance contract wording, supplemented by market practice and any relevant Canadian, English and US reinsurance jurisprudence.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

There is no Canadian jurisprudence on either of these issues. As a result, an arbitration panel or court would consider the facts of the case, including the reinsurance contract wording, market practice, and any relevant English and US reinsurance jurisprudence.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

The obligation of a reinsurer to reimburse a cedent for ECOs is normally expressly provided for in or excluded from reinsurance agreements. There is no consistency in these provisions – while most reinsurance agreements exclude ECO coverage, some include ECO coverage (usually where the reinsurer has been consulted about, or has expressly agreed to, the cedent's litigation strategy).

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

In Chile, insurance and reinsurance companies, local insurance and reinsurance brokers, and loss adjusters are mainly regulated by the Securities and Insurance Superintendency (SVS).

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Insurance and reinsurance companies can only be stock corporations incorporated in Chile as long as they provide these services only and the complementary activities authorised by the SVS through rules of general application and comply with the special regulations established in Title XIII of the Chilean Corporations Act (companies subject to special regulations).

The selling of insurance in Chile can be undertaken by a general insurance company (first group) or a life insurance company (second group). The former covers the risk of loss or damage of goods or patrimony. Life insurance companies, on the other hand, cover risks of persons or guarantee them within or on termination of a certain term, capital, a paid-off policy or a rent for the insured party or its beneficiaries. Exceptionally, personal risk and health can be covered by both types of companies. Risks related to credit can only be insured by general insurance companies having the sole purpose of covering this type of risk, which could also cover surety and fidelity.

Notwithstanding the above, foreign insurers that are incorporated abroad may commercialise and sell direct insurance cover in Chile relating to international marine transportation, international commercial aviation and cargo in international transit and satellites.

In addition, companies incorporated abroad are allowed to establish branch offices in Chile. These branch offices are subject to the general procedure provided by the Chilean Corporations Act for the incorporation of agencies of foreign companies and must obtain authorisation from the SVS (respectively as per titles XI and XIII of the Chilean Corporations Act). In addition, the branch offices must prove to the SVS that they comply with all requirements established for the authorisation of insurance companies, and need to follow further publication and registration formalities.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

All parties interested in the incorporation of an insurance entity must:

- report the identity of the stockholders and its controllers if they have participation greater than or equal to 10 per cent of the capital and they have the ability to elect at least one member of the board of directors;
- prove that their stockholders and controllers are not affected by the situations referred to in letters a, b and c of article 44-bis of the Insurance Companies Act (also known as DFL 251); and
- prove that their stockholders and controllers own a consolidated net patrimony equal to or greater than their contribution.

The reinsurance of contracts subscribed to in Chile is contracted by insurance and reinsurance companies with the following entities:

- national corporations whose exclusive scope of business is reinsurance;
- national insurance companies that can only reinsure risks from the group they are authorised to operate; and
- foreign reinsurance entities that are classified by two different risks classification agencies approved by the SVS and ranked at least within the BBB risk category or its equivalent. Reinsurance can be provided by the aforementioned foreign reinsurance entities either directly or through reinsurance brokers registered in the Registry of Foreign Reinsurance Brokers, which is managed by the SVS.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

In general, directors of insurance and reinsurance companies must be at least 18 years old and comply with the general requirements that operate in Chile for stock corporations, namely:

- not being a member of a board of directors that was dismissed owing to rejection of the company's balance sheet by shareholders;
- not being accused of or charged with the criminal offences indicated in the Chilean Corporations Act;
- not being a governmental officer or executive for a state-owned company that exercises supervision or control functions; and
- not holding a public position, which applies to members of congress, government ministries or undersecretaries, chiefs of public services, SVS employees and stockbrokers.

Notwithstanding the above, under the Insurance Companies Act there are further requirements for directors and officers of companies relating to the second group.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

The minimum capital of a Chilean insurance company is 90,000 Chilean UF (an indexed unit of account). In the case of Chilean reinsurance companies, this is 120,000 Chilean UF for any of the authorised groups in which they may operate.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

In order to meet the obligations derived from the underwriting of insurance and reinsurance, insurance and reinsurance entities established in the country must constitute technical reserves in accordance with the actuary principles, procedures, mortality charts, interest rates and other technical parameters established by the SVS through general

rules. Their modification or replacement must be communicated to companies at least 120 days in advance.

In this respect, the Insurance Companies Act distinguishes the following types of reserves:

- current risks reserves for obligations of a company with its insureds, derived from premiums of short-term insurance contracts;
- mathematical reserves for obligations of a second group insurance company (life) with its insureds, derived from premiums of long-term insurance contracts;
- claims reserves for obligations to claims that have occurred and are pending payment, and to those that have occurred and not been reported;
- additional reserves for those risks in which the claim rate is not well known, highly fluctuating, cyclical or catastrophic and that, as deemed by the SVS by means of general rules, is necessary to constitute for the normal insurance or reinsurance operations to be carried out;
- discrepancy reserves for risks derived from a discrepancy in the terms, interest rates, currency or investment instruments and between the company's assets and liabilities; and
- fund value reserves corresponding to obligations generated from investment accounts in the second-group insurance (life) that consider them.

The SVS, without prejudice to the compliance with the requirements established for reinsurance and by means of a general rule, shall establish the statutes and minimum requirements for reinsurance transfers in order that they are deducted from the calculation of technical reserves.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance and reinsurance companies must word their contracts using the models of policies and clauses contained in the Register of Policies of the SVS. Exceptionally, they are able to use non-registered models when they relate to general insurance, where the insured or the beneficiary are legal entities, and when the annual premium is higher than 200 Chilean UF. In addition, non-registered models can also be used for cargo, transport, marine or aircraft hulls, or related insurance.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

According to the Insurance Companies Act, the SVS may at any time:

- request from the insurance or reinsurance companies, as well as from the assureds, information related to their business;
- inspect offices;
- examine documents and books;
- issue directives regarding the preparation and presentation of balance sheets and financial statements, and the way companies conduct their accounting systems;
- order the appointment of external auditors for the purpose of informing balance sheets, as well as itself appoint external auditors to perform specific tasks related to such companies; and
- impose sanctions whenever it finds a breach of any directive, general rule or provision under the standing legislation.

These sanctions are of a varied nature, from fines to the termination of the authorisation to operate.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Such rules are mainly contained in the Insurance Companies Act, and refer to the amount and diversification of investments in connection with technical reserves and the overall risk capital. In this respect, they must be secured by investments in the following instruments and assets:

- fixed income investments:
  - instruments issued or guaranteed until their total extinction by the state, or instruments issued by the Chilean Central Bank;
  - fixed-term deposits, mortgage notes of credit, bonds and other credit and debt instruments issued by banks and financial institutions;
  - bonds, promissory notes and other credit and debt instruments issued by public or private companies;
  - participation in credit agreements comprising two or more banks or financial institutions, according to general rules issued by the SVS, which shall contain the debtor's risk rating; and
  - negotiable mortgage-backed loans of the kind indicated in Title V of the Insurance Companies Act;
- equity investments:
  - stocks from publicly traded companies as well as stocks from companies awarded public infrastructure concessions;
  - mutual funds units, the assets of which are invested in securities and national assets; and
  - quotes of investment funds, the assets of which are invested in securities or national assets;
- foreign investment:
  - instruments issued or guaranteed until their total extinction by the state, or instruments issued by the Chilean Central Bank;
  - deposits, bonds, promissory notes and other debt or credit instruments, issued by financial institutions, companies, or foreign or international corporations;
  - stocks of companies or corporations formed under the rules of a foreign country;
  - quotes of mutual or investment funds formed under the rules of a foreign country;
  - quotes of mutual or investment funds formed under local rules, the assets of which are invested in foreign securities; and
- real estate (classified for other purposes other than housing) located in a foreign country;
- real estate whose commercial valuation is performed no less than once every two years, according to general rules set by the SVS;
- other assets:
  - unexpired credits corresponding to premiums not yet earned granted to the insured, deriving from insurance contracts containing a resolution clause for non-payment of premiums, to support the total current risk reserve and up to 10 per cent of risk capital of insurance companies of the first group;
  - unexpired claims, derived from cessions awarded to reinsurers, to support the total claim reserve and up to 10 per cent of risk capital, with the exception of claims deriving from cessions under article 20 of the Insurance Companies Act, which cannot be deducted from the reserve, according the aforementioned article;
  - unexpired credits derived from premiums relating to disability and survival insurance referred to in the New Pension Fund System Act (DL 3500 of 1980), to support the total claim reserve, for companies of the second group;
  - advance payments to life insurance policyholders, up to the amount of the surrender value, provided that the referred policy explicitly states that such loan may be deducted from the amount of the corresponding payment according to the policy or its complements;
  - unexpired credit derived from unearned prime granted to assignor insurance companies of the first group, derived from reinsurance contracts, for the purpose of supporting up to the total of the claim reserve; and
  - unexpired credit derived from earned prime granted to assignor insurance companies of the first group, derived from reinsurance contracts, for the purpose of supporting up to the total of the claim reserve;
- financial derivatives instruments, according to boundaries and conditions established by the SVS through rules of general application. The maximum threshold for investment established by the SVS cannot be lower than 0.5 per cent or higher than 3 per cent of the technical reserves and the company's risk capital; and
- other investments that comply with the requirements, conditions and limits established by the SVS through norms of general

application up to for a maximum threshold investment that cannot be higher than 5 per cent of the technical reserves and the company's risk capital.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

The transfer of business or portfolios, and mergers or divisions of insurance entities require special authorisation from the SVS and must be carried out in conformity with the general rules established by the latter for this purpose.

In every case, the insureds must be informed, and the conditions of the transfer may not encumber their rights or modify their guarantees.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no particular requirements regarding the financing of such a transaction.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

According to the Insurance Companies Act, natural and juridical persons that, individually or as group, are deemed as controllers of a life insurance company (second group) under the Chilean Capital Markets Act, or that own individually more than 10 per cent of its shares must provide the SVS with sound information as to their financial position. In addition, as per the Insurance Companies Act, those interested in constituting an insurance entity must also report to the SVS the identity of their shareholders and their controllers provided that they have a participation equal to 10 per cent or more of the capital or the faculty to elect at least one member of the board of directors. Finally, as per the Insurance Companies Act, insurance entities must report to the SVS any changes relating to ownership comprising shareholders who acquire 10 per cent or more of the capital.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

Except for the general provisions relating to foreign investment, there are no specific requirements and restrictions in this regard.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Generally speaking, this is a matter mainly regulated by Title XV of the Capital Markets Act and the instructions issued by the SVS. The Insurance Companies Act also contains specific provisions applicable to groups of companies in connection with the maximum amounts for investing in instruments or assets representing technical reserves and risk capital. In this respect, it is worth noting that, subject to the line of business of groups of companies, some other authorities may also monitor them.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Except for the requirement that reinsurance can be provided by the entities pointed in question 3, there are no specific requirements in this regard.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

These matters are subject to the margins of indebtedness regulated by the Insurance Companies Act and by the technical reserves. In this respect, it is worth noting that the margins of indebtedness for the first group cannot be more than five times the equity of the relevant company, and in the case of the second group no more than 15 times.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Except for the minimum capital required for national reinsurance companies (120,000 Chilean UF), restrictions relating the groups in which insurance companies may operate (they can reinsured only risks of the same group) and for classification requirements applied to registered foreign reinsurance entities (at least BBB or equal), there are no such collateral requirements. Having said this, reinsurance brokers registered in the Registry of Foreign Reinsurance Brokers must establish a liability insurance policy of no less than 20,000 Chilean UF or one-third of the premium intermediated in the immediately preceding year, whichever is the higher (the policy must not be subject to any deductible).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

This matter is subject to different guidelines issued by the SVS following the implementation of the IFRS.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

This matter is regulated by a specific chapter established in the Insurance Companies Act and the general provisions contained in the Chilean Bankruptcy Law No. 20,720 of 2014.

In general, Chapter IV of the Insurance Companies Act establishes that when an insurance or reinsurance company reduces its capital below the minimum capital mentioned in question 5, it must inform the SVS within two days. The company will then have 40 days to re-establish the minimum capital. Otherwise, the SVS will call an extraordinary shareholders' meeting to approve a capital increase. After this approval, the company will have 80 days to enter the outstanding capital or the company's authorisation to operate will be revoked.

There are similar provisions if the troubled company does not comply with its debt limits, if it has an investment deficit, or if there is both a capital deficit and an excess in indebtedness. If the financial problems are not solved in the context of the aforementioned procedure, the troubled company will have to be liquidated as per the general rules of the Bankruptcy Law.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Generally speaking, in Chile, bankruptcy proceedings and creditors' rights are established by Law 20,720 of 2014 (Bankruptcy Law), the Civil Code and the Code of Civil Procedure. The New Insurance Law (Law No. 20,667 of 9 May 2013) and the Insurance Company Act also contain specific provisions regarding bankruptcy.

According to the New Insurance Law, if the insurer becomes bankrupt, the insured has the right to terminate the contract and request the proportional devolution of premium. On the other hand, the insurer has same option if the insured becomes bankrupt before payment of the entire premium.

As regards priority of claims, creditors are paid in the manner and order of preference established by the Civil Code. The general rule is that creditors are paid pro rata to the amount of their credits unless a legal preference exists. In this respect, under Chilean law there are five groups of credits, and the insured's credits in connection to losses that occurred before the bankruptcy have the same rank as those credits listed as number five of the first-class credits (first group), which refer, inter alia, to workers' wages.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Chilean law regulates the activities of insurance and reinsurance brokers, sales agents of the insurer and loss adjusters. Their licensing requirements can be summarised as follows.

Sales agents

In order to act as a sales agent, the person must first necessarily be registered in the special sales agent registry that will be kept by each insurer, which will contain certain minimum information required by Chilean regulations.

For registration purposes, a natural person must prove that he or she meets the following requirements:

- is a Chilean or a foreigner residing in Chile and of legal age;
- has a good commercial record;
- does not have any disqualifications recorded as established in the Insurance Companies Act; and
- has knowledge of insurance matters, or technical or professional experience as defined by the insurer.

Legal entities must certify that they meet the following requirements: they must not have any disqualification recorded as established in the Insurance Companies Act, and their managers and legal representatives must meet the requirements indicated above. In this respect, insurers must keep an updated list of their sales agents that indicates the dates they started to work and the legal relationships with the insurer. This list must be available at all times to the SVS.

Insurance brokers

Insurance brokers are regulated under both the Insurance Companies Act and the Regulations Applicable to Insurance Industry Officers (DS 1055-2013), which regulate the activities of both insurance brokers and adjusters.

Reinsurance brokers

In addition to provisions contained in the Insurance Companies Act, reinsurance brokers are subject to specific rules contained in SVS General Rule No. 139/2002. In general, they have to be registered in the Special Registry of Reinsurance Brokers kept by the SVS and comply with the following requirements:

- they cannot be registered as insurance brokers as per the preceding section;
- they must establish a liability insurance policy of no less than 20,000 Chilean UF or one-third of the premium intermediated in the immediately preceding year, whichever is the higher (the policy must not be subject to any deductible); and
- foreign reinsurance brokers must be legal entities, and must certify that they have been legally incorporated abroad and are entitled to intermediate risks ceded from abroad. In addition, foreign reinsurance brokers must designate an attorney with a broad range of faculties to act on their behalf in Chile, including the power to serve and be served with court proceedings.

Loss adjusters

Under Chilean regulations, the loss adjuster is appointed to act as an impartial claims specialist who must be licensed and supervised by the SVS. The adjuster's role is to investigate and review the circumstances of the loss or damage and to report on the validity of the policy coverage in respect of the claim. The adjuster's report is released to both the insured and the insurer.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Under the New Insurance Law, the general rule is no. However, in non-marine insurance, the insured may be provided with a direct action against the reinsurer if agreed in the reinsurance contract or if the insurer assigns his or her rights under the reinsurance. In addition, in marine insurance, when the marine liability insurer has issued a guarantee such as a letter of undertaking, the holder of such guarantee can bring a direct action against the marine liability insurer.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The New Insurance Law obliges the insured to notify the insurer as soon as the insured knows about any event that may imply a loss. However, there are no provisions that expressly allow an insurer to deny coverage based on late notice of claim without demonstrating prejudice. This is a matter that has yet to be clarified by the Chilean courts.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

No, unless there is gross negligence or fraud in the claim denial.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The duty to defend a claim is triggered by the existence of coverage under the policy. If the coverage is disputed, under Chilean practice the parties will usually try to reach an agreement on the claim handling; otherwise, the insured will usually carry on with its defence and pursue the insurer's liability once coverage has been determined.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

This obligation is triggered by the following general conditions:

- existence of a valid insurance or reinsurance contract;
- compliance by the insured or reinsured, as the case may be, with his or her obligations and duties;
- losses that occurred within the indemnity period; and
- risks not excluded by the policy.

In this respect, it should be noted that when dealing with a local loss adjustment process, the insurer is required to notify the insured, within five days of the completion of the adjustment process, its final decision on the claim.

The loss or undisputed sum must be paid within six days for registered contracts (ie, those contracts registered with the SVS and that are normally standard form).

If the reinsurance is back-to-back, this provides a very limited period for payment of the loss by reinsurers.

However, this period can be extended where the insurance is a non-registered contract – which is often the case for business facultatively reinsured in the London market. It will therefore be important for reinsurers to identify whether the original insurance is registered or non-registered, and the time for payment under the insurance policy.

Reinsurers may also consider inserting payment provisions within the reinsurance policy as distinct from the insurance policy.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Under Chilean life insurance regulations contained in the New Insurance Law, there is a two-year incontestability period. This period does not apply if the insured's statements for the risks assessment were fraudulent.

28 Punitive damages

Are punitive damages insurable?

Punitive damages are not contemplated under Chilean law.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Unless otherwise agreed, an excess insurer is only liable for the excess coverage.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

The insurer's obligation is to pay indemnity over the deductible or self-insured retention, as the case may be.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There are no specific rules but priority is usually determined by the date of the losses. In this respect, under the New Insurance Law the insured amount constitutes the maximum limit of the indemnity.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Under the New Insurance Law, when there are multiple policies covering the same matter, interests and risks, the insured can claim the loss payment under any of these policies and claim the balance (if any) from the other insurers. In this respect, the insurer that pays the indemnity has a reimbursement action against the other insurers for their respective shares based on the amounts that each policy covers.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

According to Chilean law, an insured would not be allowed to keep the proceeds of wrongful conduct. In this respect, the New Insurance Law establishes that insurance contracts whose objects are illicit are null.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The New Insurance Law does not contain a definition of occurrence. However, 'loss' is defined as the occurrence of the risk or adverse event covered by the insurance contract. As to how the courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy, this depends on the insurance contract terms and factual evidence, including but not limited to the conclusions and findings of the local adjuster that handled the adjustment process.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The New Insurance Law recognises the concept of utmost good faith, and the insured must respond to an insurer's request for information about a risk by honestly disclosing the information requested, to allow insurers to identify the object of the insurance and assess the nature of the risk. For these purposes, it suffices that the insured reports exclusively as per the aforementioned insurer's request.

If the insured provides information that is false, the insurer can avoid the policy and return the premium. The insured must also disclose circumstances that increase the risk during the policy period.

Having said that, if the insurer fails to request information at placement, he or she is prevented from alleging any errors, reticence or inaccuracies by the insured, as well as those facts or circumstances that are not composed of the aforementioned request.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Reinsurance is governed by the principle of freedom of contract but with some restrictions contained in the New Insurance Law. The placing of reinsurance is regulated by the Insurance Companies Act and the complementary regulations issued by the SVS. According to article 29 of the Insurance Companies Act, any dispute arising from insurance and reinsurance contracts governed by Chilean law shall come under the jurisdiction of the Chilean courts. This rule is mandatory and cannot be repealed by agreement of the parties. Therefore, although there is contractual freedom to agree on the applicable law, any dispute must be settled in principle in the Chilean courts. Nevertheless, once a reinsurance dispute effectively arises, the parties to the reinsurance policy are entitled to resolve disputes under Chile's international arbitration rules.

As to the primary means for formal dispute resolution and subject to the parties' stipulations, there is a reasonable balance between litigation in court and arbitration. In the event legal proceedings are commenced before an arbitrator, parties have more freedom to establish the procedural rules to be followed by the arbitrator. In turn, when litigating before ordinary courts, judges and the parties shall abide by the rules contained in the Civil Procedural Code.

In any case, whether litigating before an arbitrator or an ordinary court, the substantive rules of law established in the Code of Commerce, the Insurance Companies Act and the Civil Code (in those rules that are not resolved by the former two) must be followed.

Having said that, most reinsurance disputes are settled out of court. In addition, if agreed by the parties, other alternative dispute resolution mechanisms, such as mediation, may also be considered.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

The most common source of dispute is found in the construction of contracts, including but not limited to issues regarding interpretation, mismatches between the underlying policies and reinsurance slips, differences in legal concepts, and policies or clauses translations.

Regarding claims control or cooperation clauses, these are not expressly regulated, although Chilean practice does recognise them.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Yes; the reasoning for the decision is included in every award as a matter of law.

Update and trends

Definitions
The New Insurance Law now incorporates a new definition of the insurance contract that acknowledges how insurance policies have become more sophisticated since the nineteenth century. The New Insurance Law expressly recognises different classes of insurance and differentiates between damage insurance (for example, fire, theft or civil liability insurance) and individual insurance (for example, life insurance or income protection insurance). Article 513 sets out some limited definitions of common insurance terms such as 'deductible', 'endorsement' and 'insurable interest'.

Reinsurance contracts and dispute resolution
For overseas insurers based in London and elsewhere, the greatest impact of the New Insurance Law may be felt at the reinsurance level. The statutory provisions relating to reinsurance contracts are now more detailed than was the case before the Code was amended. Article 584 of the New Insurance Law appears to provide that reinsurers' obligations will be limited by the policy and will not be triggered until the reinsured incurs an indemnifiable loss. The New Insurance Law now states that international custom and practice regarding reinsurance will influence the interpretation of reinsurance contracts. This states at article 585 that insurers cannot cite their outwards reinsurance as grounds for refusing to make a payment at the direct insurance level.

The changes in the law provide reinsurers with greater certainty as to when insurers can terminate a policy or refuse to indemnify the insured (eg, if the insured provides false information, the loss is triggered by an act of recklessness, the insured fails to pay premium or fails to advise insurers of circumstances that have aggravated the risk). Although the definitions of common insurance concepts are not set out in much detail, we can envisage circumstances where disputes could be resolved by reference to the definitions set out in the New Insurance Law.

The lack of guidance in the regulations prior to the New Insurance Law over reinsurance contracts had created uncertainty for the London market. The new provisions stating that 'international standard practice' will be relevant to interpreting reinsurance contracts may herald an improvement, although there will inevitably be disagreements as to what practice should be followed. Nevertheless, if a reinsurance policy is placed by brokers in London and uses standard London wording, reinsurers will be able to cite the New Insurance Law to argue that evidence of London market practice will be key to resolving disputes at the reinsurance level.

In the past, disputes at the reinsurance level may have been difficult to resolve as there was little case law to provide guidance. While the arbitral awards that will be lodged with the regulator will not bind parties in future disputes, we welcome the initiative to create a bank of arbitral decisions that can be referred to in subsequent proceedings.

Loss adjustment
New loss adjustment regulations came into force on 1 June 2013 (Decree No. 1055). They provide detailed provisions for the registration of brokers and adjusters, as well as their obligations and restrictions, and detailed provisions for the notification and adjustment of losses. The adjustment procedure is consumer-orientated and subject to the principles of promptness and procedural economy, objective and technical reporting and transparency and access. The new regulations increase the Chilean regulator powers to regulate the adjustment process. The new regulations apply to commercial and personal lines of business alike and do not take into account the complexity of the loss (other than an increased adjustment period) or the relevance of reinsurances for the payment of some losses. Adjusters are exposed to various sanctions including fines, suspension and revocation of licence as well as claims in negligence. These are important in that the adjusters are likely to be highly sensitive to any suggestion of a breach of the new regulations and 'guiding principles'.

Adjustment period (article 23)
Article 23 of Decree No. 1055-13 sets out various time limits for the adjustment and provides for the basis on which those periods can be extended:

- the registered adjuster will issue the adjustment report in the 'shortest time possible', not exceeding 45 days from the date of loss, except 180 days for marine (hull or general average) or 90 days where the annual premium exceeds around US$4,700. Specific time periods apply to motor. Ninety days would apply to most non-marine losses that might be facultatively reinsured into the London market;
- an extension of time is provided for under the new regulations, but the reasons for the extension and steps to be taken must be notified to the superintendence and the insured, and recorded. The superintendence can refuse the extension and order the issue of the final report; and
- importantly, 'No extension will be granted where the request for further information could reasonably have been foreseen, unless the reasons that justify the lack of request are indicated.'

The time limits in the adjustment process, restriction on extensions of time, the requirement under article 13 of Decree No. 1055 to request information in a timely manner, and requirement to record all information requested, create a risk that if the information required to properly adjust the claim is not identified early in the adjustment process it may not be obtainable. It therefore becomes very important for reinsurers to become involved in the claim at the earliest opportunity, to identify and request lines of inquiry.

Preliminary report (article 24)
A preliminary report under article 24 of Decree No. 1055-13, which must be issued simultaneously to the insured and insurer, on coverage, can be provided at the adjuster's own initiative or at the request of the insured. The insured and insurer thereafter have five days to comment on the adjusters' findings. The failure on the part of insurers to challenge the findings on liability in the preliminary report may be used in any subsequent dispute against insurers. This article does not change the earlier regulations. It is worth reminding reinsurers, however, that unless they have engaged in the adjustment process through the cedents it is highly unlikely that they will have sufficient information, or receive the adjuster's report early enough, to make any comments within the five-day time limit.

Objections to final adjustment report (article 26)
On receipt of the final adjustment report on both liability and quantum, the insured and insurer have 10 days to object, failing which the parties are taken to have accepted the adjustment – this time period is the same as in the prior regulations. Given the limited time period to comment, the same concerns arise for reinsurers, which is to ensure that they have addressed all issues in advance of the final report being circulated and are able to object within the time limit. If objections are made to the final report the adjuster thereafter has six days to respond (in the previous regulations it was five days), which response is sent to both insured and insurer simultaneously.

Payment of indemnity (article 27)
The insurer is required to notify the insured of its final decision on the claim within five days of the completion of the adjustment process. The loss or undisputed sum must be paid within six days for registered contracts (ie, those contracts registered with the superintendence and which are normally standard form). If the reinsurance is back-to-back, this provides a very limited period for payment of the loss by reinsurers. However, this period can be extended where the insurance is a non-registered contract, which is often the case for business facultatively reinsured in to the London market. It will therefore be important for reinsurers to identify whether the original insurance is registered or non-registered and the time for payment under the insurance policy. Reinsurers may also consider inserting payment provisions within the reinsurance policy as distinct from the insurance policy.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

In Chile, arbitrators do not have powers over non-parties to the arbitration agreement.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

In general, both local and international arbitration awards are usually recognised and enforced by Chilean courts, which give them a high level of deference. This also applies to reinsurance disputes when arbitrated. As to remedies, arbitration awards may be subject to all available remedies unless waived by the parties.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Chilean law has no specific regulations for dealing with this issue. However, if such an obligation is agreed in the reinsurance contract by having a 'follow-the-settlements' clause or wording, the reinsurer may still defend itself by alleging, inter alia, lack of reinsurance coverage or fraud or gross negligence in the claims handling.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

See question 35.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Under Chilean insurance law, there are no specific provisions for facultative reinsurance and treaty reinsurance, and thus these are subject to the general provisions that apply to insurance contracts and also to the general provisions for any sort of contracts.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

See question 22.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Under the New Insurance Law, should the insurer be bankrupted, payments made under reinsurances benefit the insureds, whose credits arising from losses have preference over any other credits against the insurer.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Under the New Insurance Law, the cedent is obliged to notify the reinsurer as soon as the cedent knows about any event that may imply a loss.

As with general insurance, there are no provisions that expressly allow a reinsurer to deny coverage based on late notice of claim without demonstrating prejudice. However, such effect could be achieved by upgrading the notification obligation as an essential term of the reinsurance contract.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

See question 32.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Under Chilean law, there is no specific review. However, this matter can be contractually handled through the application of claims control or cooperation clauses.

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49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

In Chile, this matter is not subject to specific legal provisions, and thus has to be resolved according to the reinsurance terms. For interpretation purposes, international uses and customs can be used.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

In Chile, this matter is not subject to specific legal provisions, and thus has to be resolved according to the reinsurance terms. For interpretation purposes, international uses and customs can be used.

China

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

China's insurance market is principally regulated by the China Insurance Regulatory Commission (the CIRC), a ministerial-level agency of the central government of the People's Republic of China (PRC). Established in 1998, the CIRC is headquartered in Beijing and has 36 provincial and five municipal-level bureaus.

The CIRC is charged with:

- formulating policies and regulations of the insurance industry;
- licensing and supervision of insurance institutions;
- regulation and development of the insurance market; and
- monitoring risks and maintaining insurance market stability.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

The requirements for formation and licensing of new insurance and reinsurance companies are similar and principally grouped into four general categories:

- shareholding percentage;
- shareholder qualifications;
- paid-in capital; and
- CIRC approval.

Shareholding percentage

For any new 'domestic' Chinese insurance or reinsurance company (ie, a company wherein the equity interest held by domestic investors is greater than 75 per cent), a single shareholder may not hold an equity interest in excess of 20 per cent (unless otherwise approved by the CIRC). Another shareholding limitation is that no single limited partnership (LP) may acquire an equity interest in excess of 5 per cent or constitute the single largest shareholder, a controlling shareholder or an actual controller of such company. Moreover, the aggregate equity interest held by all LPs may not exceed 15 per cent. However, for any 'foreign invested' Chinese insurance or reinsurance company (ie, a company wherein the equity interest held by domestic investors is not greater than 75 per cent), the aforementioned limitations do not apply.

Shareholder qualifications

It should be noted that domestic and foreign investors are subject to differing shareholder qualification requirements. (See question 13 for qualification requirements applicable to a foreign investor.)

A domestic investor holding an equity interest in an insurance or reinsurance company of less than 15 per cent must meet the following criteria:

(i) it cannot be a commercial bank, securities institution or a wholly foreign-owned enterprise (unless otherwise approved by the CIRC);
(ii) it must have earned profits in the fiscal year prior to its application;
(iii) the capital to be injected into the company must be in cash and derived from the investor's own equity (unless otherwise approved by the CIRC);
(iv) it must not have materially violated any applicable laws or regulations within the preceding three-year period;
(v) it must have a record of good credit and tax payment;
(vi) if it is a financial institution, it must have met the capital adequacy and other prudential requirements of the relevant regulatory authorities;
(vii) it must have obtained relevant approvals from its shareholders or board of directors;
(viii) it must have obtained approvals from the relevant regulatory authorities, if applicable; and
(ix) its business must operate well and its financial status must be sound and stable.

A domestic investor either holding an equity interest of between 15 and 20 per cent or holding an equity interest of less than 15 per cent but having the power to directly or indirectly exercise control over the company must meet the above criteria in (i) to (ix) and, additionally, must meet the following criteria:

(x) have net assets of not less than 200 million yuan as at the end of the year prior to the application;
(xi) have consecutively earned profits in each of the three preceding fiscal years;
(xii) have the capability to make continuous capital contributions; and
(xiii) have a good reputation and a leading position in its industry.

An LP investing in an insurance or reinsurance company must meet the following criteria:

- the insurance company to be invested in must have a controlling shareholder or actual controller, a reasonable equity structure and sound and stable corporate governance;
- the general executive partners of the LP must have good integrity and have a record of tax payment, have no record of major illegalities or irregularities, must undertake that the sources of funding are not in violation of the provisions on anti-money laundering, and must bear corresponding liabilities for the investment in the insurance and reinsurance company;
- the LP cannot constitute the single largest shareholder, controlling shareholder or actual controller of the company, and the LP cannot participate in the management of the insurance company; and
- the LP must transfer its shares to another qualified holder prior to the expiry of the term of the LP (if any).

Paid-in capital

Paid-in capital requirements are determined by the business engaged in by the particular insurance or reinsurance company (see question 5).

CIRC approval

The CIRC employs a two-stage approval system with respect to the formation and licensing of a new insurance or reinsurance company. In the first stage, an application may be submitted to the CIRC to obtain preliminary approval for establishment of a company. Once the first-stage approval is obtained, a company must complete the preparation for establishment within a period of one year, during which time the company may not engage in any insurance business, and may only conduct activities relating to preparation for the future commencement of business operations. After completion of preparation for establishment,

a company must obtain the second-stage approval from the CIRC prior to commencing business operations.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Insurance and reinsurance companies are licensed to conduct insurance business both at the legal entity-level and at the branch level. The central CIRC has cognisance over administration of legal entity-level and provincial branch-level licensing, and the relevant local CIRC branch has cognisance over administration of lower branch or municipal-level licensing.

With respect to insurance companies, life and non-life insurance business lines are classified into 'basic' or 'extended' categories. Companies newly established after 2 May 2013 (other than an insurance holding company, captive property insurance company, mutual insurance company or specialised insurance company) initially are only approved by the CIRC to conduct one or more specified basic lines of business, and are required to obtain further approval from the CIRC in order to operate a new basic line of business or to expand into any extended line or lines of business.

In addition to the CIRC licensing, insurance and reinsurance companies must also register with the State Administration of Industry and Commerce (SAIC) or its local bureaus to obtain a business licence before engaging in insurance business. Generally speaking, SAIC registration is procedural in nature and, once CIRC licensing is obtained, an enterprise typically would not encounter any significant obstacles in obtaining a SAIC business licence.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

Any prospective member of the board of directors or board of supervisors, or prospective senior officer (including any general manager, deputy general manager, assistant general manager, secretary of the board of directors, chief compliance officer, chief actuary, chief financial officer or chief audit officer) of an insurance company must first satisfy a qualification test and apply to the CIRC for approval of their qualifications for such position. Generally speaking, any such candidate must:

- be familiar with insurance laws and regulations;
- hold a bachelor's degree (or a two- or three-year college degree under certain limited circumstances);
- possess good character; and
- have necessary management capabilities and prescribed years of related work experience.

Additional particular qualification criteria may be applicable according to the specific position.

Additionally, any candidate would be disqualified from a position as a senior officer or director of an insurance or reinsurance company if the candidate:

- is a minor, incompetent or otherwise lacks full civil capacity;
- received specified criminal or administrative penalties (including penalties imposed by Chinese authorities or authorities of other jurisdictions) within a certain period prior to the application;
- is under investigation by the CIRC for serious unlawful conduct;
- received a warning or monetary fine from the CIRC during the year prior to the application;
- served as a director or senior officer for another company and is directly responsible for the failure of such company (including bankruptcy, revocation of business licence or closure by a governmental agency) within a certain period prior to the application;
- served as a director or senior officer for another insurance company, is directly responsible for the distress of such insurance company and such insurance company is under administrative supervision or in receivership;
- is financially troubled; or
- falls under other situations prescribed by the CIRC.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

With respect to an insurance company, the minimum paid-in capital is 200 million yuan. An insurance company (other than an insurance holding company, captive insurance company, mutual insurance company or specialised insurance company) with registered capital of 200 million yuan may only conduct one basic line of property and casualty (P&C) business or one basic line of life business, and is required to increase its paid-in capital in order to expand its business scope; however, that a company established prior to 2 May 2013 with registered capital of 200 million yuan may be permitted by the CIRC to conduct a full scope of business.

With respect to a reinsurance company that conducts only life or non-life reinsurance business, the minimum paid-in capital (or, in the case of a Chinese branch of a foreign reinsurance company, the minimum operating fund) is 200 million yuan. For a reinsurance company that conducts both life and non-life reinsurance business, the minimum paid-in capital (or, in the case of a Chinese branch of a foreign reinsurance company, the minimum operating fund) is 300 million yuan.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance and reinsurance companies are required to calculate solvency in accordance with standards prescribed under China's Risk Oriented Solvency System (C-ROSS). If such a company has a solvency ratio of less than 100 per cent, then the CIRC may elect to:

- order a capital increase or restrict dividend payment;
- restrict compensation of directors and officers;
- restrict advertising;
- restrict new branch establishment, limit business scope, suspend new business or order policy transfer or cession;
- order asset auction or restrict asset acquisition;
- limit fund usage;
- remove officers;
- take over the company; or
- other measures deemed necessary by the CIRC.

For insurance and reinsurance companies with a solvency ratio between 100 per cent and 150 per cent, the CIRC may require companies to submit and implement a plan for the prevention of inadequate solvency.

In addition to satisfying solvency requirements, the PRC Insurance Law also requires insurance companies to set aside liability reserves necessary to protect customers' interests, and the CIRC has promulgated detailed rules with regard to the calculation of minimum reserves.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

With respect to P&C products, the CIRC requires that certain types be registered for approval by the CIRC prior to offering for sale, while remaining types are permitted to be immediately offered for sale, as long as they are properly filed with the CIRC within 10 days of the offering date. Products prescribed by the CIRC as requiring approval include auto insurance, non-life investment-oriented insurance, bond insurance and credit insurance with a term longer than one year and any mandatory insurance or other insurance concerning the public interest. Products that have been previously approved by the CIRC must again be approved by the CIRC if the product's insurance clause or premium is amended. Products that have been previously registered with the CIRC must again be filed with the CIRC if the insurance coverage or premium is amended. With respect to life insurance products, the CIRC requirements generally follow the same approval or registration procedure as for P&C products. The following life insurance products have been prescribed by the CIRC as requiring approval: life or annuity insurance products other than ordinary, participating, universal and investment-linked products and certain group participating life and annuity products.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

With respect to insurance companies, the CIRC carries out a comprehensive assessment and classification quarterly and will, accordingly, determine applicable regulatory measures, if any. In addition, the CIRC also mandates a system of supplemental periodic reporting, including actuarial reports, financial reports, solvency reports and compliance reports, each of which must respectively be provided to the CIRC within the relevant prescribed time frame. In addition to periodic reports, insurance companies are also obliged to submit a variety of event-based reports. The CIRC also carries out a system of programmed and ad hoc inspections. Originally commenced in 2015, the annual inspection programme is carried out by the CIRC Insurance Consumer Protection Bureau, and aims at combating activities that are deemed to be harmful to customers' legitimate interests. Recently, the CIRC has placed increased emphasis on ad hoc inspections. For example, in early 2017, the CIRC conducted ad hoc onsite inspections of insurance companies that focused on shareholder relationships, corporate governance and insurance company internal control. In future, the CIRC may be expected to continue using ad hoc inspections as a means of testing regulatory compliance with selected topics (eg, capital investment, financial records keeping and compliance with C-ROSS requirements).

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

For the purposes of supervision, the CIRC classifies permissible investment assets into five categories and imposes certain restrictions with respect to the relative proportions of different assets. In terms of classification, the principal asset categories comprise:

(i) current assets;
(ii) fixed-income assets;
(iii) equity assets;
(iv) real estate assets; and
(v) other financial assets.

In terms of investment restrictions, the CIRC requires insurance and reinsurance companies to diversify investment in accordance with respective relative proportions. Generally speaking, the total book balance of investment in items (iii), (iv) and (v) may not exceed 30 per cent, 30 per cent and 25 per cent respectively of the total assets of the company as at the end of the preceding quarter. In addition, aggregate outbound investment may not exceed 15 per cent of the total assets of the company as at the end of the preceding quarter. Subject to certain limitations, the total book balance of a single investment in items (ii), (iii), (iv) and (v) may not exceed 5 per cent of the total assets of the company as at the end of the preceding quarter. In addition, subject to certain limitations, the total book balance of investments in a single legal entity may not exceed 20 per cent of the total assets of the company as at the end of the preceding quarter.

On 24 January 2017, the CIRC promulgated the 'Circular on Further Strengthening Stock Investment by Insurance Funds', pursuant to which, the CIRC classifies investment in mainland China publicly listed companies into the following three categories:

- normal investment: after completion of the acquisition, the investing insurance institution will hold an equity interest in such publicly listed company that is less than 20 per cent, and will not hold controlling power over such company;
- material investment: after completion of the acquisition, the investing insurance institution will hold an equity interest in such publicly listed company that is equal to or more than 20 per cent, but will not hold controlling power over such company; and
- company acquisition: after completion of the acquisition, the investing insurance institution will hold controlling power over such publicly listed company.

With respect to company acquisition, among other requirements, a company may only use funds derived from its own equity to acquire a publicly listed company, and is prohibited either from acquiring such company in concert with any other individual or company not subject to regulation by the CIRC, or from financing such acquisition using publicly listed stock assets as collateral.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Any change of shareholder whose shareholding is equal to or greater than 5 per cent is subject to CIRC review and approval. Specific requirements depend on circumstances, including:

- the nature of the target (domestic or foreign-invested insurance or reinsurance company);
- the identity of the acquirer (domestic or foreign); and
- intended shareholding percentage.

If the investor is not already a shareholder of the target company, the investor must also submit, among other things, information about its shareholders or controlling persons, or both, and a statement with respect to the relationships between its shareholders or controlling persons, or both, and other investors in the company. The CIRC may conduct background investigations of the officers, directors and controlling persons if it deems necessary.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

Generally speaking, an investor in an insurance or reinsurance company may only invest in cash derived from its own equity, which means that it may not use debt to finance its investment. However, the CIRC may authorise an investor to finance a merger or acquisition with loans and other financial instruments up to a maximum of 50 per cent of the cash consideration. For the purposes of this exception, a merger refers to the activities whereby two or more companies merge into one company. An acquisition refers to the acquisition by an investor in one transaction or a series of transactions of greater than one-third of the equity interest in a company, through which the investor becomes the single largest shareholder of the company, or an acquisition that is equal to or less than one-third of the equity interest in a company, through which the investor becomes the single largest shareholder and could exercise control over the company.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

As noted in question 10, any change of shareholder whose shareholding is equal to or greater than 5 per cent is subject to CIRC review and approval. Additionally, in the case of a privately-held insurance or reinsurance company, any change of shareholder whose shareholding is less than 5 per cent must be reported to the CIRC within 15 days of the execution of the relevant share transfer agreement. It should also be noted that different shareholding requirements could be triggered by a minority acquisition depending on the identity of the acquirer and the nature of the target. For example, a domestic company could be converted into a foreign invested company as a consequence of a minority acquisition by a foreign investor.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

The requirements for foreign investment in an insurance or reinsurance company are principally grouped into the following general categories:

- shareholding percentage;
- shareholder qualifications; and
- CIRC approval.

Shareholding percentage
For a life insurance company, the aggregate shareholding of foreign investment is subject to a cap of 50 per cent; however, for a P&C insurance company or a reinsurance company, there are no maximum shareholding limitations.

Shareholder qualifications
It should be noted that foreign and domestic investors are subject to differing shareholder qualification requirements. (See question 2 for qualification requirements applicable to a domestic investor.)

A foreign shareholder holding an equity interest of less than 15 per cent of a domestic insurance or reinsurance company (ie, a company wherein the equity interest held by domestic investors is greater than 75 per cent) must meet the following criteria:

(i) it must be a financial institution in a World Trade Organization (WTO) member and cannot be a natural person or a governmental entity;
(ii) it must have earned profits in each of the three consecutive fiscal years prior to its application;
(iii) it must have total assets of not less than US$2 billion as of the end of the year prior to the application;
(iv) it must have a long-term credit rating issued by an international rating agency greater than 'A' (or its equivalent) for the three consecutive years preceding its application;
(v) it must not have materially violated any applicable laws or regulations within the preceding three-year period;
(vi) it must have met the capital adequacy and other prudential requirements of its home regulator; and
(vii) its financial status must be sound and stable.

A foreign shareholder either holding an equity interest in a domestic insurance or reinsurance company of between 15 per cent and 20 per cent, or holding an equity interest in a domestic insurance or reinsurance company of less than 15 per cent but having the power to directly or indirectly exercise control over the company, must meet the above criteria in (i) to (vii) and, additionally, must meet the following criteria:

(viii) have net assets of not less than 200 million yuan;
(ix) have the capability to make continuous capital contributions; and
(x) have a good reputation and a leading position in its industry.

A foreign shareholder holding an equity interest in a domestic insurance or reinsurance company of greater than 20 per cent but less than 25 per cent must meet the above criteria in (i) to (x) and, additionally, must meet the following criteria:

(xi) have total assets of not less than 10 billion yuan as at the end of the year prior to the application;
(xii) have net assets of not less than 30 per cent of its total assets;
(xiii) have net assets that are not less than its long-term equity investments (including investment in the company);
(xiv) must not have violated any code of conduct for shareholders of insurance companies stipulated in the PRC Insurance Law and other CIRC rules; and
(xv) have maintained an equity interest in the company for three or more years.

A foreign shareholder holding an equity interest in a foreign invested insurance or reinsurance company (ie, a company wherein the equity interest held by domestic investors is not greater than 75 per cent) must meet the following criteria:

- have 30 or more years of relevant experience in a WTO member;
- have maintained a qualifying representative office in China for more than two years;
- have total assets of greater than US$5 billion as at the end of the year prior to application;
- be subject to the effective regulation of the competent authorities of its home jurisdiction, which employs a sound insurance regulatory system;
- meet the solvency requirements of its home jurisdiction;
- the competent authorities of its home jurisdiction must consent to the application; and
- other conditions prescribed by the CIRC.

CIRC approval
As noted in question 10, any change of shareholder whose shareholding is equal to or greater than 5 per cent is subject to CIRC review and approval. Additionally, in the case of a privately-held insurance or reinsurance company, any change of shareholder whose shareholding is less than 5 per cent must be reported to the CIRC within 15 days of the execution of the relevant share transfer agreement. As noted in question 2, the formation of a new insurance or reinsurance company is subject to a two-stage approval process.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

An insurance holding company may be established in order to exercise control over multiple insurance and reinsurance companies, non-insurance financial institutions and non-financial companies that operate insurance-related business within the same group.

The relationship between an insurance holding company and its subsidiaries is governed by the CIRC's Insurance Holding Company Administration Measures (For Trial Implementation), which specify limitations on stock pyramiding, cross shareholding, senior officers holding concurrent positions in different entities within the same group, related transactions and other matters of a similar nature. An insurance holding company is required to closely monitor its subsidiaries with respect to various matters, including human resources, accounting and risk management, and file periodic and event-based reports with the CIRC. An insurance holding company as well as its insurance company subsidiaries must also meet the applicable solvency requirements.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Generally speaking, Chinese law does not regulate the terms included in reinsurance contracts. However, some mandatory restrictions exist with respect to the risk ratios that a reinsurance company may accept under certain types of reinsurance contracts (see question 16).

As opposed to regulation of reinsurance contracts, the CIRC focuses particular attention on the qualifications of the reinsurance companies themselves. The CIRC imposes different qualification requirements, including solvency, rating, financial strength and similar criteria, on reinsurance treaty leaders, reinsurance treaty followers and facultative reinsurers, with the strictest standards being imposed on reinsurance treaty leaders. In addition, any reinsurance company engaging in reinsurance transactions with a Chinese insurance company (domestic or foreign invested) must first register in a specialised system sponsored and maintained by the CIRC, providing required information with regard to solvency, credit rating, financial strength and other relevant matters, whereupon each reinsurance company will be classified according to its assessed qualifications (eg, treaty leader, treaty follower or facultative business).

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Each insurer is obliged to retain risk within parameters that are commensurate with its financial strength and business volume. The PRC Insurance Law requires that the maximum insured amount for each risk unit that is to be retained by the insurer may not exceed 10 per cent of the total of its actual capital and its capital reserves, and any liabilities exceeding this threshold must be ceded to reinsurers. In addition, the PRC Insurance Law and other CIRC rules require that the total insurance premiums retained by a P&C insurer for all of its business may not exceed a value that is four times the total of its actual capital and its capital reserves.

In addition, the Administrative Measures on Reinsurance Business require that, other than insurance involving nuclear, aviation, petroleum or credit insurance, in the case of proportional reinsurance, the proportion for each risk unit ceded out by the direct insurer to a single reinsurer must not exceed 80 per cent of the insured amount or covered liabilities assumed by the insurer. In the case of facultative reinsurance to affiliates, the ratio ceded out by one insurer to its affiliates may not exceed 20 per cent of the insured amount or covered liabilities amount encompassed by each such facultative reinsurance contract.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Chinese law does not require a reinsurer to post collateral in a reinsurance transaction. However, according to the CIRC's requirements under C-ROSS, if business is ceded by a Chinese insurer to an overseas reinsurer that is not licensed in China, the insurer in China will receive solvency credit less than such credit it may otherwise receive if its business were ceded to a reinsurer licensed in China, unless collateral is posted by the overseas reinsurer. An overseas reinsurer may provide a bank deposit or a standby letter of credit (SLOC) as collateral to guarantee the correlating reinsurance premiums receivable or reinsurance reserves receivable on the request of the insurer. With respect to bank deposit collateral, the funds must be deposited in an eligible Chinese commercial bank and must be available at the disposal of the ceding company. The funds cannot be returned to the reinsurer's bank account within one quarter of the date of deposit unless the underlying reinsurance contract has previously been settled. With respect to SLOC collateral, the SLOC must be issued by a bank meeting certain criteria specified by the CIRC, or confirmed by such bank (meaning that the confirmation bank undertakes to honour or negotiate the SLOC supplemental to the undertakings of the issuing bank).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Cedents must adhere to generally accepted accounting principles in connection with reinsurance business as well as the requirements under C-ROSS to classify assets and liabilities in its financial statements. The PRC Accounting Standards for Enterprises No. 26 – Reinsurance Contracts set out the rules governing accounting for reinsurance contracts.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

An insolvent insurance or reinsurance company is subject to the PRC Bankruptcy Law as well as the PRC Insurance Law. According to the PRC Insurance Law, when an insurance company or reinsurance company becomes insolvent, such company or any of its creditors may, on the CIRC's approval, apply to a competent court for restructuring, reconciliation or bankruptcy liquidation of the company. Alternatively, the CIRC may apply to a competent court for restructuring or bankruptcy liquidation of the company. However, as of the date hereof, no Chinese insurance or reinsurance company has ever been subject to a formal bankruptcy proceeding as described by the PRC Bankruptcy Law and the PRC Insurance Law, and, accordingly, the rule has not yet been tested.

In order to minimise the risk of insolvency, the CIRC may impose a series of supervisory measures on any financially troubled insurance or reinsurance company (see question 6).

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

According to the PRC Insurance Law, when an insurance company is declared bankrupt, after the payment of administrative expenses and debts incurred for the common benefit of the creditors, the remaining assets of the company will be applied in the following order:

(i) wages and salaries, as well as certain prescribed employee benefits;
(ii) indemnity or payment of insurance benefits;
(iii) social insurance fees other than those prescribed in item (i) and unpaid taxes; and
(iv) claims of general creditors.

A class of creditors will not be paid unless the creditors of higher priority classes have been paid in full. In the case where the remaining assets are insufficient to pay a certain class of creditors in full, those assets will be distributed on a pro rata basis to the members of that class. Claims against an insurance or reinsurance company are typically classified as the claims of general creditors.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Insurance intermediaries in China comprise the following:

- insurance agency companies (including professional insurance agency companies and part-time insurance agency companies);
- insurance brokerage companies; and
- insurance adjustors.

Insurance intermediaries conducting business in China must be approved and licensed by the CIRC; however, that an overseas insurer broker in a WTO member without a licence from the CIRC is also allowed to conduct cross-border reinsurance brokerage transactions with Chinese insurance companies. Pursuant to CIRC regulations, an insurance intermediary may be granted a licence for a fixed period of three years, which is renewable for additional three-year terms subject to the approval of the CIRC. In addition, a broker engaging in reinsurance transactions with a Chinese insurance company, whether licensed by the CIRC or not, must also register in a specialised system sponsored and maintained by the CIRC.

Insurance agency companies

Insurance agency companies distribute insurance products, collect insurance premiums and conduct insurance claim investigations on behalf of insurance companies. Among other licensing requirements, a professional insurance agency company must have a minimum paid-in capital of 50 million yuan (unless otherwise approved by the CIRC). Such paid-in capital must be derived from its own equity and must be placed under the supervision of a qualified bank. A professional insurance agency company intending to conduct business beyond the territorial limits of its domicile first must establish a branch in each relevant province. However, with respect to a professional insurance agency company established prior to 27 April 2013 with a paid-in capital of less than 50 million yuan, such company will only be permitted to establish a branch within its domiciliary province or in a province where it has a previously established branch, unless its registered capital is increased to 50 million yuan or more. The status of regulatory guidance governing part-time insurance agency companies is relatively fluid, as compared with the regulations governing professional insurance agency companies, with respect to the licence holders, licence renewal requirements and related matters.

Insurance brokerage companies

Insurance brokerage companies provide insurance broking services for the benefit of policyholders under direct insurance contracts, or for the benefit of direct insurance companies under reinsurance contracts. Among other licensing requirements, an insurance brokerage company must have a minimum paid-in capital of 50 million yuan (unless otherwise approved by the CIRC). Such paid-in capital must be derived from its own equity and must be placed under the supervision of a qualified bank. The CIRC licences insurance brokerage companies on a nationwide basis. However, with respect to an insurance brokerage company established prior to 27 April 2013 with a paid-in capital of less than 50 million yuan, such company will only be permitted to conduct business where it has established branches unless its registered capital is increased to 50 million yuan or more.

Insurance adjustors

There are no requirements as to the minimum capital of an insurance adjustor, and the capital of an insurance adjustor is not required to be paid-in on the commencement of operations. The CIRC licences insurance adjustor companies on a nationwide basis.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

A third party can bring a direct action against an insurer for liability insurance coverage if the insured's liability has been finally determined (either through admission by the insurer or through final adjudication by a competent court or arbitration) and the insured has failed to actively request the insurer to indemnify the third party.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The PRC Insurance Law provides that a policyholder, an insured or a beneficiary shall notify an insurer of the occurrence of an insured loss in a timely manner. If notification of the occurrence of such loss is delayed, either intentionally or as the result of gross negligence, and such delay prejudices the ability of the insurer to ascertain the nature, cause or extent of a claimed loss, then the insurer may deny such uncertain part of the loss, so long as the insurer did not have actual or constructive knowledge of the occurrence of the loss.

The PRC Insurance Law also requires that the right to claim for insurance payment must be exercised within two years (for non-life insurance) or five years (for life insurance), from the date when an insured or a beneficiary knew or should have known of the occurrence of the loss.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

In the case of wrongful denial of a claim, a claimant may file a complaint with the CIRC, which may investigate and impose administrative penalties. The PRC Insurance Law provides that if an insurer wrongfully denies an indemnity obligation as agreed in an insurance contract, the CIRC may order the insurer to rectify and impose a fine ranging from 50,000 yuan to 300,000 yuan. If the circumstances are found to be serious, the CIRC may impose certain restrictions on the permissible scope of business for the insurer, order the insurer to cease accepting new business or even suspend its insurance business licence. The CIRC may also issue a warning to responsible persons within the insurer, impose fines ranging from 10,000 yuan to 100,000 yuan and revoke approval of such persons' qualifications.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

A liability insurer does not have a duty to defend a claim unless it is provided for in the insurance contract. Pursuant to the PRC Insurance Law, unless otherwise provided in the insurance contract, if a third party claims for damages against an insured of a liability insurance contract for a matter falling within the scope of insurance coverage by means of arbitration or litigation, and loss or damage has been suffered by such third party, then the insurer must reimburse the costs of such proceedings and other necessary and reasonable expenses paid by the insured.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

An insurer's indemnification obligation is determined by the effective terms and conditions of an insurance contract. Pursuant to the PRC Insurance Law, an insurer must examine claims in a timely manner and determine whether the claims are allowable. If the insurer determines that any portion of a claim falls within the scope of coverage, it must notify the claimant and seek to reach an agreement with the claimant on the allowable payment. Unless otherwise provided in the insurance contract, within 10 days from the date of the contract, the insurer must make the payment. However, if the insurer determines that no portion of the claim falls within the scope of coverage, then within three days it must notify the insured or beneficiary. The PRC Insurance Law also provides that, if the total loss cannot be determined by existing evidence, an insurer remains obliged to effect such primary payment as can be determined within 60 days of receipt of the substantiating evidence, and the insurer is obliged to pay the outstanding payments after they are determined.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Pursuant to the PRC Insurance Law, an insurer may not contest coverage based on a misrepresentation in the insurance application:

- after 30 days from the date when the insurer has actual or constructive knowledge that the insured made an intentional or grossly negligent misstatement of fact that is material to the insurer's underwriting decisions; or
- after two years from the date of the insurance contract that included such material misrepresentation.

28 Punitive damages

Are punitive damages insurable?

Punitive damages have been adopted in China in a limited way, and only for certain subjects. There is no statutory rule on whether punitive damages are insurable; however, in the current market, punitive damages are usually excluded from the coverage of an insurance contract.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

The obligation of an excess insurer in the context of insolvency or other circumstances, when primary insurer coverage is unavailable, has not received meaningful attention with respect to legislation, litigation or judicial interpretation in China.

With respect to an insolvency scenario in the case of a life insurance company, pursuant to the PRC Insurance Law, if a life insurer declares bankruptcy, then it has an obligation to assign its life insurance contracts and liability reserve funds to another qualified life insurer. If such life insurer is unable to reach an agreement with another qualified life insurer, then the CIRC may designate a life insurer to assume the relevant life insurance contracts and liability reserve funds. Accordingly, an excess insurer of a life insurer would have no obligation to 'drop down and defend', even if the original primary insurer is insolvent, because another life insurer will have assumed the liability. However, as of the date hereof, no Chinese insurance or reinsurance company has ever been subject to a formal bankruptcy proceeding as described by the PRC Bankruptcy Law and the PRC Insurance Law, and, accordingly, the rule has not yet been tested.

With respect to an insolvency situation in the case of non-life insurance company and with respect to other scenarios, Chinese courts will enforce the effective agreement of the parties to a contract. Accordingly, the courts will likely enforce the express terms of a contract, which provides for an obligation for an excess insurer to 'drop down and defend', regardless of whether or not a primary insurer pays to the full extent of the primary coverage. In the absence of such express contractual provisions, the outcome would be uncertain.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

This question only becomes relevant where insurance coverage is granted in relation to a third party, namely, where the policyholder or

the insured is liable for damages suffered by another party. Where the policyholder or the insured's own risk is insured, the insurer will provide indemnification for an amount exceeding the deductible or self-insured retention according to the terms of the insurance contract, regardless of whether the policyholder or insured is insolvent or not.

In liability insurance, where the insurer covers the third party's claim against the policyholder or insured, if the policyholder or the insured is unable to pay the claim, the third party has the right to enforce against the insurer, but the insurer's obligation should be limited to pay indemnity above the deductible and self-retention as provided in the insurance contract. However, with respect to other insurance, if the policy provides that the insured has a self-insured retention or deductible but is unable to pay it, the obligation of the insurer will depend on the terms of the insurance contract.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

The order of priority for payment when there are multiple claims under the same contract has not received meaningful attention with respect to legislation, litigation or judicial interpretation in China. Chinese courts will enforce the effective agreement of the parties to a contract. In the absence of such contractual provisions, the outcome would be uncertain.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

If a loss or claim is covered by multiple policies, the principle for the allocation among the insurers is different subject to whether the policies are life policies or P&C policies. If a loss or claim is covered by different life policies, each insurer needs to pay indemnification according to the terms and conditions of the policies, and there are no restrictions under Chinese law as to the total amount that the different insurers would pay for such loss or claim. However, if a loss or claim is covered by different P&C policies, the actual total insurance payment by multiple insurers may not exceed the total loss amount. Accordingly, if the total insurance coverage under multiple P&C insurance contracts does not exceed the total loss, then each insurer needs to pay indemnification according to the terms and conditions of the policies. However, if the total insurance coverage under multiple P&C insurance contracts exceeds the total loss, then unless otherwise provided in the insurance contract, an insurer's liability for indemnification is calculated in proportion to its respective insurance coverage as a percentage of the total coverage amount.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Whether disgorgement claims are insurable has not received meaningful attention with respect to legislation, litigation or judicial interpretation in China; however, Chinese courts will enforce the effective agreement of the parties to a contract.

With respect to restitution claims, pursuant to the PRC Insurance Law, to the extent that restitution constitutes compensation for a third party's losses, then liability insurance may provide indemnification when the losses are recognised by an insurer or a court. With respect to other restitution claims, whether they are insurable also has not received meaningful attention with respect to legislation, litigation or judicial interpretation.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

Chinese law does not specify in what circumstances a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance contract. Accordingly, consistent with the PRC Contract Law, courts are likely to interpret the scope of 'occurrence' with reference to its definition and the express usage within the insurance contract.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Pursuant to the PRC Insurance Law, a policyholder must truthfully disclose information in connection with the insured subject or the insured on the request from the insurer, and, if a policyholder intentionally, or out of gross negligence, makes a misstatement that is material to an insurer's underwriting, the insurer may rescind the insurance contract. As an example, the PRC Insurance Law expressly provides that if a policyholder of a life insurance contract falsely states an insured's age and that age does not fall within the age limits specified by the contract, then the insurer may rescind the insurance contract. In such circumstances, the insurer has 30 days from the date when it has actual or constructive knowledge of such misstatement to rescind the contract. Regardless of knowledge, an insurer may not contest coverage based on such a misrepresentation after two years from the date when such an insurance contract has been entered into. However, the PRC Insurance Law also provides that if an insurer has actual or constructive knowledge that an insured has made an intentional or grossly negligent misstatement of the information requested by the insurer at the time when parties enter into an insurance contract, then an insurer may not rescind the insurance contract for such misstatement.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Formal reinsurance disputes are uncommon. Insurers and reinsurers in China generally prefer business solutions as the primary means to resolve their disputes, without resorting to litigation or arbitration. As a civil law jurisdiction, decisions of Chinese courts generally do not have precedential effect. However, insurers and reinsurers may consult published court decisions as a general reference on substantive issues (see question 37).

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

To the extent that reinsurance disputes have been adjudicated in the Chinese court system, common issues that have arisen typically involved contractual terms such as:

- a reinsurer's liability under a reinsurance contract for interest in the event of a delayed payment to an insured;
- allocation of liability as between insurer and reinsurer;
- late notice of claims; and
- other major contractual terms.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Pursuant to the PRC Arbitration Law, unless the parties to an arbitral award agree otherwise, an arbitral award must state the reasoning for the decision. This rule applies to any arbitral award, including reinsurance arbitral awards issued by a tribunal located within China (eg, the China International Economic and Trade Arbitration Commission).

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Generally speaking, under Chinese law, arbitrators do not have power over non-parties to an arbitration agreement. However, pursuant to the PRC Arbitration Law, an arbitral tribunal may independently gather evidence, and may request witnesses to provide relevant materials and to attend arbitration proceedings.

Update and trends

Recent key developments include:
- implementation of C-ROSS;
- enhanced oversight of insurance companies; and
- the introduction of new provisions regulating the use of information technology.

C-ROSS, China's second-generation solvency regulation system, was formally launched in the first quarter of 2016. On 25 October 2016, the CIRC announced, via a media release posted on its official website, that the industry Integrated Risk Rating (IRR) process for the second quarter of 2016 had been completed, marking full implementation of C-ROSS. The IRR results demonstrate that, as of the end of June 2016, 98 per cent of all insurance companies (including reinsurance companies) in the Chinese market were in compliance with applicable solvency requirements, earning an IRR rating of Class A or Class B, reflecting operations in a solvency condition of relatively low risk. With respect to the remaining 2 per cent of insurance companies whose solvency ratio or IRR rate fell short of applicable standards, the CIRC has implemented supervisory measures, including imposing restrictions on investment portfolios, suspending approval for new branch establishment and suspending approval for business line expansion. The CIRC also released a series of C-ROSS implementing rules and standards, among which are the qualification requirements for collateral posted by overseas reinsurers (see question 17). Recently, the CIRC announced that the second stage of C-ROSS implementation is planned to commence in the near future, and that the CIRC will promulgate additional detailed implementing measures.

The CIRC recently increased oversight of insurance companies, as reflected in a series of measures. With respect to corporate governance, the CIRC has promulgated several rules governing insurance company investor conduct. Additionally, the CIRC recently released the draft Equity Measures for Insurance Companies, which proposed certain shareholder restrictions to constrain the ability of an investor to establish control over an insurance company. With respect to product regulation, the CIRC has introduced new restrictions on short or mid-term life products (ie, certain life products with an expected duration period of less than five years are subject to greater scrutiny by the CIRC). With respect to insurance company investment, the CIRC has promulgated new requirements aiming to curb risk and encourage prudent investment by insurance companies, especially in the stock market (see question 9). With respect to policy sales, in order to encourage customer satisfaction and confidence in the China insurance industry, the CIRC has strengthened scrutiny of pre-sale and claims-related services.

Regulation of internet-related matters relevant to the insurance industry remains highly active. The Cyber Security Law, promulgated in November 2016, is effective from 1 June 2017, and establishes an overarching cyber security framework. Within that framework, supporting measures to provide relatively more detailed implementation guidance are under development. For example, the draft Measures for the Security Assessment of Outbound Transfer of Personal Information and Important Data (Cross-Border Data Transfer Measures) were released for public comment in April 2017, and are intended to govern outbound data transfers, encompassing personal information and important data that is generated in the course of business operations in China, and transferred overseas. In May 2017, the Cross-Border Data Transfer Measures were followed by publication of the draft Information Security Technology – Guidelines for Data Cross-Border Transfer Security Assessment, proposing more detailed guidance. Also, earlier, in 2015, the CIRC published the draft Provisions on Insurance System Informatization (the Draft Informatization Measures) for public comment, which would regulate the use of information technology in the insurance sector, including broadened applicability, new corporate governance obligations, reporting requirements and technology standards, as well as mandating the establishment of a senior-level chief information officer to oversee company informatisation plans and operations. Certain aspects of the aforementioned laws and regulations are unclear and subject to further clarification by relevant authorities. But the evident trend of regulation will likely impact many foreign and Chinese insurance and reinsurance companies, whose compliance burden is likely to be increased.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Pursuant to the PRC Arbitration Law, an arbitral award will be legally effective as of the date on which it is made. However, within six months of the date of receipt of the award, any party to the arbitration may petition the intermediate people's court where the arbitration commission is located to vacate the award. To prevail, such party must demonstrate that:
(i) there was no arbitration agreement between the parties;
(ii) the matters in question fall outside of the arbitration agreement or beyond the power of the arbitration commission;
(iii) the composition of the members of the arbitral tribunal or the procedure of the arbitration violates required legal procedure;
(iv) the evidence on which the award was based has been forged;
(v) the counterparty concealed evidence that could materially affect fair arbitration; or
(vi) the arbitrators solicited or accepted bribes, committed illegalities for personal gain or perverted the law.

The Chinese judiciary will give substantial deference to arbitral awards. Although Chinese courts may vacate or confirm arbitral awards, neither the PRC Arbitration Law nor the record of court decisions reflects an obvious inclination or capacity to modify an arbitral award. However, pursuant to the PRC Arbitration Law, the arbitral tribunal itself has the right to modify an award in the case of an error in calculation or wording, or an omission.

With respect to a foreign-related arbitration (ie, an arbitration in China that has a foreign nexus), pursuant to the PRC Civil Procedure Law, the competent court may vacate an arbitral award under specified circumstances. As an example, if the enforcement target can demonstrate that it either has not been provided notice with respect to the appointment of an arbitrator or for the inception of the arbitration proceedings, or was unable to present its case owing to causes for which it is not responsible, then the court typically would vacate the arbitral award. Additionally, the court would also vacate the arbitral award for the same reasons as noted in items (i), (ii) and (iii) above.

Additionally, with respect to an award by a non-Chinese arbitral tribunal, the PRC Civil Procedure Law provides that if any party to an arbitration by a foreign arbitral tribunal requires recognition and enforcement by a Chinese court, such party may petition the intermediate people's court with territorial jurisdiction over the target party or, where such party's property is located, to enforce the award. The Chinese judiciary will give substantial deference to an arbitral award and enforce a non-Chinese arbitral award in accordance with international treaties concluded or acceded to by China or in accordance with the principle of reciprocity. It should be noted that China is a signatory to New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The Administrative Regulations on Reinsurance by P&C Insurers provide that a claim payment should follow the principle of 'follow-the-fortunes', meaning that as long as the claim falls within the coverage of the reinsurance contract, the cedent's decisions on claims will apply to the reinsurer. Other than the above, there are no statutory requirements under Chinese law. However, unless otherwise provided in the insurance contract, market practice is to follow the cedent's underwriting fortunes for claims payments or settlements to the extent that the claims fall within the scope of the reinsurance contract and the cedent has handled the claims and settlements in good faith.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The PRC Insurance Law requires that all parties to an insurance activity must act in good faith during the performance of their rights and obligations. The PRC Contract Law also requires that parties to a contract act in good faith during the performance of their rights and obligations. The duty of good faith therefore is implied in all contracts, including reinsurance contracts; however, the duty of utmost good faith is not a well-recognised concept under relevant Chinese law.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There are no separate sets of laws in China governing facultative and treaty reinsurance; however, recipients in facultative and treaty reinsurance arrangements are subject to different rating, capital and other qualification requirements.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

The PRC Insurance Law provides that a policyholder or beneficiary is precluded from bringing a direct action against a reinsurer for indemnity or insurance benefits.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The PRC Insurance Law provides that a policyholder or beneficiary is precluded from bringing a direct action against a reinsurer for indemnity or insurance benefits. Accordingly, even if a cedent is insolvent and cannot pay, a policyholder may not raise a claim against the reinsurer. On the approval of the CIRC, in accordance with the PRC Bankruptcy Law, such cedent may petition the competent PRC court for a declaration of bankruptcy. If a cedent is declared bankrupt, then the reinsurance coverage to be provided by the reinsurer will become part of the cedent's bankruptcy estate, and the insured or the beneficiary may become an unsecured creditor of the cedent pursuant to the bankruptcy process. However, as of the date hereof, no Chinese insurance or reinsurance company has ever been subject to a formal bankruptcy proceeding as described by the PRC Bankruptcy Law and the PRC Insurance Law, and, accordingly, the rule has not yet been tested.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

There are no specific requirements under Chinese law applicable to the notice and information to be provided by a cedent to its reinsurer under a reinsurance contract. Accordingly, the type and information that a cedent must provide to a reinsurer with respect to an underlying claim, and the available remedies, will be subject to the terms and conditions of the reinsurance contract. A reinsurance contract typically may require timely delivery of all material claim-related information, including the facts, claim, loss assessment or estimated amount of loss, as well as relevant supporting documentation. Accordingly, pursuant to the agreed terms of the reinsurance contract, a reinsurer may have a basis to deny indemnification to a cedent under specified circumstances.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

For the principle of payment allocation in the case of multiple direct insurance policies, see question 32. Chinese law does not require a reinsurance contract to mirror the above allocation principle. Reinsurers bear liabilities with respect to the insurers based on the terms of the reinsurance contracts.

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48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Chinese law does not provide for a general right of review of a cedent's claims handling, or settlement and allocation decisions. However, a reinsurance contract may provide for such review rights.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

There are no statutory requirements imposing an obligation on a reinsurer to reimburse a cedent for commutation payments made to the cedent's policyholders. Accordingly, the obligation would be governed by the terms and conditions of the reinsurance contract.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

There are no statutory requirements imposing an obligation on a reinsurer to reimburse a cedent for ECOs. Accordingly, such obligation would be governed by the terms and conditions of the reinsurance contract. It is not unusual that reinsurance contracts expressly relieve reinsurers from obligations to reimburse cedents for ECOs.ç

Germany

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Federal Financial Supervisory Authority (BaFin) supervises all insurance and reinsurance companies, guarantee funds and pension funds having their registered seat in Germany (at present this is approximately 538 insurance companies (life, health and property insurance) and 31 pension funds), with the exception of, inter alia, the social insurance carriers and several hundred small mutual insurance companies supervised by the respective state. The BaFin acts on behalf of the federal government and only in the public interest on the basis of the rules set out in the German Insurance Supervision Act (VAG). For companies domiciled within the European Union or the EEA carrying out business in Germany, responsibility for functional and financial supervision remains with the home member state, while the BaFin exercises a complementary supervisory role with regard to legal compliance unless the insurance activities are confined to railways, aviation, shipping and transport insurance. Companies domiciled outside the EU or the EEA acting in Germany are subject to the full supervision of the BaFin.

Additionally, the European Insurance and Occupational Pensions Authority, which is part of the European System of Financial Supervision, monitors and identifies trends, potential risks and vulnerabilities stemming from the micro-prudential level, across borders and across sectors.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Carrying out insurance activities within the German territory requires a licence granted upon application and fulfilment of various criteria, particularly including:

- filing of a detailed business plan setting forth, inter alia, the purpose of the company, the intended classes of insurance offered and the types of risks covered, the financial viability, corporate matters and any agreements on the functional outsourcing of core activities;
- information on assets that cover the minimum capital requirements;
- estimate of the solvency capital requirements and minimum capital requirements envisaged for the following three business years as well as an estimate of the financial assets required to cover these requirements;
- information on the intended reinsurance and on the structure of the administration and distribution;
- details on the management and the supervisory board members as well as other key personnel and their reliability and professional qualifications; and
- details on significant participations in the insurance undertaking.

Additional requirements apply for life and health insurance, which cannot be combined in a single legal entity with other types of insurance. With regard to reinsurance companies, the licensing requirements are somewhat lower; in particular, BaFin may not deny the licence if according to the business plan and other submitted documents the interests of the insured are not sufficiently protected.

Finally, only a few types of corporate entity are admitted to conduct insurance business: the German stock corporation (AG), including its European form (*societas europaea* (SE)), mutual societies, and corporations and institutions under public law.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Once the BaFin has licensed a company to conduct insurance business (see question 2), no further authorisations are required as long as the business is carried out within the scope of the business plan without any alterations or amendments that the BaFin would need to approve. Companies domiciled in other member states of the EU or EEA can conduct business through a branch office or by way of cross-border services after the supervisory authority of their home country has transmitted to the BaFin certain information. Companies domiciled outside the EU or EEA pursuing insurance business in Germany must obtain a licence. Such foreign insurance companies may, however, conduct business by means of correspondence on the intiative of the respective person seeking insurance protection without triggering licence requirements. It also has to be borne in mind that insurance undertakings in Germany are prohibited from conducting non-insurance business.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The VAG provides for detailed rules on the qualifications of the persons responsible for conducting the insurance business. Such persons are: (i) the executive board members and the supervisory board members (German corporate entities that are admitted for conducting insurance business in Germany generally have a two-tier system: namely, an executive board and a supervisory board – an exception to this can be SEs) as well as representatives of a branch of an insurance company; (ii) persons responsible for other key functions such as risk management, compliance, actuarial or internal audit functions; and (iii) other persons who have material influence on business decisions below the management level (if any) (together, the 'managers'). The managers must be reliable and professionally skilled. A person may be regarded as unreliable if he or she has been convicted of a crime or a severe misdemeanour, or if mental or physical disorders could prevent that person from carrying out the orderly performance of the business.

Necessary professional skills require sufficient theoretical and practical knowledge of the insurance business as well as management experience, which will be assumed if the respective person has held a leading position within a comparable insurance business for three years.

While the same reliability standard applies to members of the supervisory board, these need only to be qualified to an extent necessary to perform their supervising function and to assess and control the company's business. Limits also exist with regard to the number of managing or supervisory positions held by an individual as well as with regard to a change from a position in the management board to the supervisory board.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

In order to be in a position to continuously meet their contractual obligations, insurance companies have to maintain eligible capital in the amount of the solvency capital requirement, which can be calculated on the basis of two different models (standard or internal formula) considering the overall volume of the business. Further, insurance companies have to maintain eligible base capital (ie, surplus and subordinated debt) in the amount of a minimum capital requirement, which must not drop below a range of between €2.5 million and €3.7 million for primary insurers and between €1.2 million and €3.6 million for reinsurers (all with certain exceptions), depending on the classes of insurance business conducted as well as on whether the business involves internal insurances. In practice, the BaFin expects insurance companies not only to meet the minimum capital requirement but also to maintain a solid financial basis.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance companies have to build several technical reserves which must be calculated in a prudent, reliable and objective manner to meet their obligations regarding the policyholders and the insured. Such reserves have to equal the amount the insurance company would have to pay if the insurance obligations were to be transferred to another insurance undertaking. The reserves include reserves for unearned premiums, refund of premiums, anticipated losses, claims outstanding and equalisation reserves, as well as, in the case of life insurers, the premium reserve. The technical reserves are established by actuarial methods as set out in the VAG as well as in a special regulation.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance products must comply with the German Insurance Contract Act in the first place, as well as with the laws on general terms and conditions. Additionally, more general laws such as the German Equal Treatment Act have to be observed. Therefore, within the legal framework each insurer is free to design its products in a manner different from its competitors; however, in respect of very common classes of insurance, German insurers often facilitate the respective model terms and conditions issued by the German Insurance Association but amend these according to their business. Except for some cases (as in that of the compulsory insurance where the general terms and conditions are part of the business plan) the product terms and conditions are not subject to prior control by the BaFin. However, the BaFin may review product terms and conditions if it has good cause to do so.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Every year, the BaFin rates the supervised insurance and reinsurance companies with regard to their financial situation, their growth and the quality of their management, in order to determine the required intensiveness of supervision of each company. Moreover, the BaFin conducts on-site inspections, examining in particular solvency, risk management and governance aspects. While the number of insurance companies is decreasing, the BaFin intends to increase its number of routine on-site inspections. The BaFin conducted 105 on-site inspections in 2016, a considerable increase compared to the 72 on-site inspections conducted in 2015. In addition, the BaFin stress tests insurance companies, simulating declines in prices of various asset classes. Finally, the BaFin examines tariffs in order to exclude discrimination and the handling of claims in order to ensure adequate consumer protection.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The VAG provides only for very general investment rules like diversification and the prudent person principle according to which insurers may only invest in assets whose risks the insurance or reinsurance company in question is able to assess, monitor and control. Derivative instruments are only admissible in order to minimise risks and to facilitate an efficient management of the investment portfolio. Unlike in the past, investments are no longer restricted by certain quantitative requirements. However, insurance companies are obliged by law to set down their individual investment principles in internal guidelines, which must contain a list of eligible assets as well as restrictions regarding the quantity of assets.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Any person who intends to acquire a 'significant interest' in an insurance or reinsurance company must notify the BaFin thereof. Any share granting 10 per cent or more of the nominal capital or voting rights of the company or the ability to exercise a significant influence on the management of the company is considered a significant interest. The person holding the significant interest must meet certain requirements in order to ensure a sound and prudent management of the insurance, in particular, the person must be reliable. In the case of a legal entity the same applies to the natural person or persons managing the business and to any personally liable partner. The notification shall indicate the facts regarding the acquisition of the significant interest (eg, amount, transferring person or entity) and the facts required to assess the reliability of the relevant persons as well as the facts that might lead to the prohibition of such acquisition. Further, any increase of the significant interest exceeding the thresholds of 20, 30 or 50 per cent of the voting rights or nominal capital must be notified. Within 60 working days from the submission of all required information, the BaFin may prohibit the intended acquisition or increase of the qualified participation if there is evidence suggesting that:

- the qualifications and requirements set out above are not met or if the acquirer is unable to provide evidence of:
  - suitable and adequate funding for the implementation of its plans for the continuation and development of the business; and
  - that the interests of the insured or reinsured are adequately safeguarded;
- the acquisition would result in the integration of the target insurance company into a group structure, which would hamper effective supervision owing to the ownership structure or poor economic transparency;
- the acquisition would result in the target insurance company becoming a subsidiary of an insurance company domiciled in a non-member state that is not effectively supervised or whose competent supervisory body is not willing to cooperate satisfactorily;
- the future general manager is not reliable or professionally skilled;
- the acquisition or increase of the participation in the insurance undertaking is made in connection with crimes of money laundering or of financing of terrorism, or if such crimes have been attempted or if the intended acquisition or increase of the participation increases the risk of such conduct; or
- the notifying person does not have the financial soundness, in particular with regard to the kind of actual or intended business of the insurance undertaking.

Non-compliance with the notification requirement constitutes an administrative offence and may lead to the obliged person being fined up to €50,000.

The VAG allows the transfer of insurance as well as reinsurance portfolios from one insurer or reinsurer to another with the prior approval of the BaFin. This enables a transfer not only of the rights but also the underlying obligations without the need for the consent of

each individual policyholder or cedent, which is a rare exception under German law.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

Provided that an acquirer can demonstrate its required financial soundness to prevent the BaFin from prohibiting the acquisition (see question 10), the same, not being an insurance company itself, may take up any kind of external finance. However, the acquirer may not use the assets of the target insurance company to facilitate or collateralise its financing and may not push down the debt after the acquisition. The reason for this is that insurance companies may only engage in insurance-related business, whereas taking up third-party finance is, in general, not considered to be insurance-related (with the exception of subordinated capital granted on very specific terms). By the same token, insurance companies may not use third-party finance to acquire any other business or expand their own business activities.

This, however, does not apply to reinsurance companies to the same extent.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

Any person holding, directly or indirectly, at least 10 per cent of the nominal capital or the voting rights in an insurance or reinsurance company (significant interest) must meet certain requirements (see question 10).

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

In principle, foreigners, be they a natural person or a legal entity, are free to invest in insurance or reinsurance companies in Germany. All the same, the BaFin will supervise any acquirer of a qualified participating interest in accordance with the standards set out in question 10. In respect of foreign investors who are subject to financial supervision in their home country, it is necessary that the BaFin would qualify their home supervision as being sufficiently effective and cooperative, as otherwise the BaFin might stop the transaction. If the potential investor resides outside the EEA, the time period in which the BaFin can block the acquisition (see question 10) is extended to 90 working days.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Groups of companies containing an insurer or reinsurer are subject to particular supervision. This comprises the following:

- in cases where an insurance or reinsurance company is a parent company of at least one other insurance or reinsurance company and in some other cases special solvency provisions apply regarding the solvency of the group. Group solvency is usually calculated on the basis of the consolidated financial statements of the group. The minimum consolidated group solvency capital requirement is equal to the minimum capital requirement of the insurance or reinsurance company in addition to the proportional share of the minimum capital requirement of the related insurance and reinsurance company. That minimum consolidated group solvency capital requirement must be covered by eligible basic own funds;
- special reporting obligations apply: the superordinated entity of the group has to inform the competent supervisory authority at least annually of any significant risk concentrations at group level and of all material intra-group transactions, including transactions with persons closely connected with one of the group companies;
- risk management and control mechanisms, including proper reporting systems and accounting standards, must be in place;
- the superordinated entity has to publish annually a report regarding solvency and finance on group level as well as the group structure; and
- with respect to groups of companies with cross-border business activities, the BaFin is part of a college of supervisors to ensure cooperation and consultation as well as the exchange of information between the relevant authorities. The college consists of the competent supervisory authority for the group (ie, the authority competent for the superordinated insurance company of the group), the competent supervisory authorities of the other states in which the group is active as well as the European Insurance and Occupational Pensions Authority.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

The content of reinsurance agreements is generally not subject to regulatory supervision. Even a reinsurance agreement concluded between two non-licensed reinsurers would be valid from a civil law perspective, although the persons acting thereof would be committing a criminal offence. However, the question of whether an agreement qualifies as a reinsurance agreement is, from a regulatory point of view, important in order to assess whether someone is actually conducting reinsurance business, which would require a licence, or another restricted business, which might require another permit (eg, a banking licence).

Note that the German Insurance Contract Act does not apply to reinsurance agreements, so that their substantive terms are governed by the general laws on contracts, and in particular commercial contracts. These sets of rules again do not provide for any particular provisions on reinsurance, but state that the customs and practices of the particular commercial activity shall be taken into account, which in Germany are largely consistent with international reinsurance practices.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

In theory, the insurer or reinsurer is free to cede up to 100 per cent of the covered risks to the reinsurer or retrocessionaire. However, for purposes of calculating the solvency margin, any reinsurance will be taken into account only for up to 50 per cent, namely, the insurer is deemed to retain a minimum of 50 per cent of the risks on its own books.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

A company offering life insurance, health insurance, private compulsory long-term care insurance as well as accident insurance with premium refund must itself retain and administer the assets covering its liabilities in relation to the policyholders, and this also applies to the reinsured part of the business. Otherwise, no specific collateral requirements exist. According to Solvency II the German legislator may not require reinsurers (from member states and from third countries whose solvency regime is equivalent to Solvency II) to pledge assets to cover unearned premiums and outstanding claims provisions.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

There are currently no specific regulatory requirements for cedents to obtain credit for reinsurance on their financial statements.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

If an insurance or reinsurance company should become financially distressed, the BaFin has a range of measures available. In more detail, if the solvency capital requirement is not met or such situation is threatened to arise within the next three months, a recovery plan has to be submitted to the BaFin for approval, setting out the measures to resolve the issue. Within a time period of generally six months, the insurance company has to either increase eligible capital or decrease risk profile to again reach the solvency capital requirement. Further, if the minimum capital required is not reached, a financing plan has to be submitted to the BaFin. The BaFin may further restrict or prohibit the free disposal of the assets of the company or the distribution of bonuses, in particular if the financial situation continues to deteriorate. If the lack of solvency continues, the BaFin may take any appropriate measures to protect the interests of the policyholders, in particular: (i) request a higher amount of eligible capital than required by law; (ii) prohibit or limit withdrawals and distributions; or (iii) prohibit or limit measures for the purpose of balancing a financial loss or show a financial profit. In severe cases, the BaFin can transfer management responsibilities to a special commissioner. If this is to no avail, the BaFin can withdraw the licence to conduct business and file for insolvency on behalf of the company. The particulars of the insolvency proceedings are set out in the German Insolvency Act with certain variations set out in the VAG (eg, the safeguarding and insolvency protection of certain minimum assets to satisfy claims of the policyholders in priority to other third parties).

Additionally, the VAG provides for the compulsory membership of life insurers and substitute health insurers in a guarantee fund that serves to safeguard the claims of policyholders, insured persons, beneficiaries and other persons vested with rights under the insurance contract. The BaFin may, under certain circumstances, order the transfer of the entire portfolio from the insurer concerned (as well as all of the assets required to cover the liabilities under these contracts) to the guarantee fund to the extent that other measures designed to safeguard the interests of the insured are considered insufficient.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The claims of the insured, policyholders, beneficiaries or injured third parties with a direct claim against the insurance company, and premium refund claims resulting from the insurance contract being cancelled before the opening of insolvency proceedings, rank prior to claims of all of other creditors. At present, there is no corresponding rule for insurers having claims against reinsurance companies.

In insolvency proceedings of both insurance and reinsurance companies, creditors having acquired their claims during the insolvency proceedings rank prior to ordinary creditors. Shareholders having granted a shareholder's loan to the insurance or reinsurance company are to be satisfied even after ordinary creditors.

Creditors holding a pledge in an object being part of the insolvency estate are to be satisfied separately from the pledged object.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Insurance companies are required to work only with professional insurance intermediaries (including all kind of agents, underwriters and brokers) who are either authorised in accordance with the German Industrial Code or are exempted from the authorisation requirement pursuant to provisions implementing the Insurance Mediation Directive of the European Commission (2002/92/EC). Anyone intending to act as an insurance intermediary in a professional scope and manner, be it a broker or an agent, needs to obtain an authorisation from the competent chamber of industry and commerce. The authorisation will be denied if the applicant is either not reliable, lives in unstable financial conditions, does not hold the mandatory professional liability insurance or cannot demonstrate sufficient qualifications and expertise by passing a respective test. Lesser requirements apply for intermediaries only distributing insurance as a supplement to other goods or services offered in their principal business if they act on behalf of either an authorised intermediary or an insurance company, maintain a professional liability insurance and are reliable. Intermediaries distributing solely insurance products of a single insurer or non-competing products of several insurers and for which the insurer assumes the unlimited liability resulting from the intermediary's activities do not need an authorisation (but require registration nevertheless), which is a frequently used exception for tied agents. Claims adjusters do not require an authorisation; third-party administrators might need an authorisation if they act as an intermediary.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

While, generally, no third party has a direct claim against an insurer for coverage, such claims are permissible pursuant to statute law in the case of mandatory liability insurance, in particular motor vehicle insurance; where the policyholder's estate is subject to insolvency proceedings; or where the place of the policyholder's residence is unknown.

Additionally, in the substitutive health insurance base tariff, the healthcare provider may claim reimbursement from the insurer directly.

Finally, a policyholder may assign its claim against the liability insurer to a third party, which then may bring direct action against the insurer.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The policyholder or, if different, the insured person in the event he or she is entitled to the insurance cover, has to notify the insurer of an insured event without undue delay immediately upon becoming aware of its occurrence. However, any failure to comply with this notice requirement would not have consequences under the applicable law as such, which is why sanctions must be agreed on in the terms and conditions of the policy. The usual contractual consequence is a denial of cover, which is, however, limited by mandatory law to the extent that cover can be fully denied only in the event of an intentional failure to comply. In the case of non-compliance owing to gross negligence, the cover can be denied pro rata in relation to the severity of the policyholder's fault. A delay caused by simple negligence does not permit even a partial reduction of the cover. Moreover, this defence is not available to the insurer if the delay of the notification had no effect on the insurer's ability to investigate the event and assess the claim unless the policyholder acts in bad faith, namely, tries to hamper the insurer's prospects of investigation by deferring the notification. The insurer may not deny cover if it has learned about the insured event in due time through other sources. Insurance contracts covering 'jumbo risks' may deviate from these provisions. Jumbo risks as defined in the Insurance Contract Act are certain railway, aircraft, ships and goods in transit insurance, motor vehicles operating on land (not automobiles) liability insurance, credit and surety insurance and insurance contracts with policyholders that exceed certain financial thresholds.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Except in very exceptional circumstances, an insurer that wrongfully denies cover does not face any extra-contractual exposure; in particular, punitive damages are not available under German law. If a court has found that the cover was wrongfully denied, the insurer has to settle the claim, including any damages caused by the delayed settlement as well as the policyholder's legal expenses. Undue delay in acknowledgement of the claim can result in the court holding that an excessive delay aggravated the pain and suffering and, therefore, increasing damage payments.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

In the case of liability insurance, the insurer has to indemnify the policyholder against any claims raised by third parties covered by the insurance policy, and has to defend the policyholder against unjustified claims. The insured event as well as the means of defence are set out in the terms and conditions of the liability insurance policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

A liability insurer is obliged to settle a claim if it has finally established the occurrence of an insured event and the amount of the respective losses. Indemnification payments will not become due and payable as long as the policyholder has not provided all information reasonably requested by the insurer regarding the event and needed to assess the claim. If within one month after the notification of the event possible enquiries of the insurer have not been concluded, the policyholder can request a down payment in the amount of the expected damages unless such enquiries could not be concluded because of the fault of the policyholder. Independent from the foregoing, in the case of liability insurance the insurer must indemnify the policyholder within two weeks of the claim being granted by court decision, acknowledgement or settlement agreement.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

An incontestability period does not exist under the Insurance Contract Act. An insurer may always contest cover on the grounds of fraudulent deceit. In the event that a policyholder makes intentional misrepresentations, the insurer can withdraw from the cover, which is important against the background of the policyholder's obligation to provide all information as requested by the insurer and relevant for the insurer to determine whether to issue the policy. In the case of grossly negligent misrepresentations, such withdrawal is only possible if the insurer can demonstrate that it would not have granted cover (not even at different conditions) if it had known of the misrepresented or undisclosed facts beforehand. Any other negligent omissions or misrepresentations do not entitle the insurer to deny the cover with retroactive effect. It is worth noting that the insurer's rights to deny the claim on this basis can only be exercised if the insurer has notified the policyholder of such rights in writing prior to the conclusion of the insurance contract.

28 Punitive damages

Are punitive damages insurable?

Given that punitive damages cannot be awarded under German law and that punitive damage awards are generally unenforceable in Germany, there is only a limited need for a respective insurance, although insurers would be free to cover punitive damages. However, owing to the very nature of punitive damages, the respective cover is commonly excluded, in particular when it is foreseeable that liability could arise in jurisdictions granting punitive damages.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Excess insurance falls under the German Insurance Contract Act, but it is up to the individual terms and conditions to define its trigger. For this reason, there is no general duty to 'drop down and defend' in the case of the primary insurer's insolvency or other unavailability. Unless otherwise agreed in the policy, the excess insurer has the right to provide for its own defence and has to compensate the loss only within what it has covered in the event that the triggers for the excess liability are met, regardless of the primary insurer's insolvency.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

This question only becomes relevant where insurance cover is granted in relation to a third party, that is, where the policyholder or the insured person, if different, is liable for damages suffered by another party. Where the policyholder's own risk is insured, the insurer covers the amount exceeding the deductible or retention only.

In liability insurance where the insurer covers the third party's claim against the policyholder (or insured person) it depends on the nature of the liability insurance, as generally the insurer is only liable for the amount exceeding the deductible or retention. If the policyholder or insured person is unable to pay the amount, the third party has to enforce the amount against the policyholder. This is different in mandatory liability insurance such as motor vehicle liability insurance. Pursuant to section 114, paragraph 2, sentence 3 of the German Insurance Contract Act, such a deductible or retention cannot be held against the third party, but is effective only in the contractual relationship between the insurer and the policyholder. It makes no difference whether a deductible or a self-insured retention has been agreed on.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

In the case of liability insurance where the policyholder is responsible in relation to several affected parties, the insurer has to compensate them equally, but if the claims taken together exceed the cover amount, only a pro rata amount of the respective amount can be claimed.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

In the case of a policyholder obtaining multiple covers for the same risk, the policyholder must notify this to each insurer. Each of the insurers has to compensate a loss to the extent it is covered under the individual policy, but only to the extent that the total compensation payments do not exceed the total loss. Between themselves, the insurers are liable in proportion to the cover they have granted. If the policyholder obtains the cover with the malicious intention of receiving compensation in excess of the loss, an insurer can deny cover. Under German law, a policy covering the consequences of a pollution that has been ongoing over time would only trigger a pro rata indemnification if it only covered a fraction of the time during which the pollution took place.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

There is no case law with regard to this question. Disgorgement claims having a punitive function under German law are generally considered not to be insurable.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

Generally speaking, the definition of occurrence may be determined in the insurance contract. The general liability conditions define as one occurrence all damages resulting from an identical source or an equal source to the extent that they are connected with each other. Such connection is denied by the courts when the different injuries occur over longer periods of time.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Policyholders have to disclose to the insurer the risk factors known to them that are relevant to the insurer's decision to conclude the contract

and that the insurer has requested in writing. If the policyholder breaches this duty of disclosure, the insurer may rescind from the contract within one month after having learned of the breach of the duty of disclosure. In cases where the policyholder breached his or her duty of disclosure neither intentionally nor by acting with gross negligence, the insurer has no such right to rescission, but may terminate the contract subject to a notice period of one month (in which case, the insurer might still be obliged to pay for a damage that had occurred by that time). The insurance company may also avoid the contract in the case of a fraudulent misrepresentation within one year of having discovered the deception.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Parties to a reinsurance agreement subject to German law usually exclude in-court litigation and instead agree on arbitration proceedings to solve any disputes. Because of this and given the confidential nature of arbitration awards, there are hardly any precedents under German law giving guidance to substantive reinsurance issues. Since the German Insurance Contract Act explicitly does not apply to reinsurance agreements, these are governed by the general laws on contracts, in particular commercial contracts. These sets of rules again do not provide for any specifics on reinsurance agreements, but state that the customs and practices of the particular commercial activity shall be taken into account. This means that against the background of the international scope of reinsurance activities one would look, even from a German perspective, to internationally accepted customs and standards of reinsurance. While in the last century formal (arbitral) proceedings were only rarely instigated, the frequency of such proceedings has increased over the past decade (partially as a result of the 9/11 terror attacks), but seem to have been decreasing again.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

A frequent issue arising in reinsurance disputes, particularly in the area of facultative reinsurance, is the scope of the cover, specifically whether the cedent may recover particular claims or risks under the wording of the reinsurance contract. Another frequent issue arising is the reach of the 'follow-the-settlement' principle.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Unless the parties to a reinsurance dispute agree explicitly otherwise, the award must include the reasoning for the decision. As a rule, the parties to arbitration proceedings in Germany will not waive their right to obtain an award with reasoning.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

The arbitrators do not have any direct jurisdiction over non-parties; however, they can request the support of courts in taking evidence. The court, in turn, can make use of its powers and assist the arbitration panel by, for example, compelling non-parties to provide testimony or to produce documents, albeit limited in scope, as German civil procedure does not provide for extensive disclosure or discovery proceedings. Arbitration proceedings are based on an agreement between the parties so that in general these proceedings may not be extended to include non-parties without their consent.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Arbitration awards can be appealed by a motion of one party to the competent court of appeals only in the following very limited circumstances:

- a party was not competent to enter into an arbitration agreement or the agreement was invalid under German law;
- a party was not properly notified of the proceedings or was otherwise hindered from defending itself in an orderly manner;
- the arbitration award was not based on or went beyond the subject matter of the arbitration agreement;
- the arbitration panel or the proceeding did not follow the rules to such an extent that it affected the arbitration award;
- the subject matter of the arbitration is not capable of being settled by arbitration proceedings under German law; and
- the award or its enforcement violates public policy.

A confirmation of an arbitration award is not contemplated under the German Code on Civil Procedure, but in order to enforce an arbitration award the civil courts would have to issue a declaration of enforceability (exequatur) before the prevailing party can make use of coercive enforcement measures.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The reinsurer's obligation to follow the cedent's underwriting fortunes and claims payments or settlements is not set out in statute laws, but is regarded as a well-established custom within the reinsurance industry. It would be taken into account even if the parties do not expressly agree on a follow-the-fortunes or settlements clause in the reinsurance agreement. While the principle to follow-the-fortunes relates to a sharing the fate of the underlying risks accepted by the cedent, the principle to follow-the-settlements provides that the reinsurer must comply with the cedent's decision on claim payments, however, only to the extent that the claim falls within the scope of the reinsurance agreement and the cedent has handled and settled the claim in an orderly and prudent manner.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The duty of utmost good faith governs the entire reinsurance relationship. While under German law the principle of (regular) good faith relates to all contractual relationships, in the case of reinsurance the reinsurer relies to a significant extent on the conduct of the cedent. This concerns, in particular, the information on the reinsured portfolio, the underwriting process and the handling of claims. Therefore, the reinsurer is entitled to the insurer also taking into account its interests to a larger extent than in a normal contractual relationship between two parties pursuing mainly their own interests.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Apart from legal distinctions owing to the different economic aims of facultative and treaty reinsurance, the legal regime for both types of reinsurance is determined by established customs within the reinsurance industry, as no statutory law and only very few court decisions on reinsurance matters exist in Germany.

Update and trends

Currently, the German legislator has initiated the legislative procedure to implement the European Insurance Distribution Directive ((EU) 2016/97). The current legislative proposal as well as recent court decisions will bring various changes to insurance distribution in Germany. Implementation of the legislative proposal is planned for July 2017. As of now, distributors of insurances in particular will face the following changes:

- The legislative proposal includes new rules on when and how an insurance distributor may charge a consulting fee from a potential policyholder. Specifically, the German classification of (i) insurance broker, acting on behalf of the potential policyholder, (ii) insurance agents, acting on behalf of an insurer and (iii) insurance advisers, who may, according to the current legal statutes, only advise potential policyholders, will become relevant on whether or not a consulting fee may be charged. Furthermore, under the current proposal, insurance advisers may also act as an insurance intermediary in the future. If the current proposal is passed, any insurance distributor charging consulting fees ought to ensure that such fees are legally permitted under the new rules.
- Insurance intermediaries as well as insurers will be required to avoid any conflict of interests. The new legislation is in line with a recent decision by the German Federal Court of Justice, prohibiting insurance brokers from managing claims on behalf of an insurer. The decision, as well as the proposed legislation, will lead to restructuring challenges for insurance intermediaries as well as insurers with aspects of corporate, tax, data protection and labour law, as a stricter division of business activities for policyholders and insurers will be required.
- Further changes ought to be made to the internal structures of insurance intermediaries as well as insurers because the necessity of product oversight and information requirements will increase. A recent German District Court decision regarding Check24, an internet aggregator platform comparing insurance contracts, has also put the spotlight on digital insurance distribution. The decision confirmed that information requirements have to be fulfilled equally and transparently for digital insurance distribution. Thus, the decision as well as the proposed legislation, emphasise the necessity for digital insurance distributors to ensure compliance with the legal statutes in place, and especially regarding the specific information requirements.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

The German Federal Court of Justice has confirmed that, unless in the case of exceptional circumstances, neither a policyholder nor any other non-signatory to a reinsurance agreement can bring a direct action against a reinsurer, because the reinsurance agreement is not considered to be an agreement to the benefit of third parties.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

In the case of an insurer's insolvency, any claims of the policyholders would be directed towards the assets under administration secured by a separate fund. Part of these assets would be the insurer's claim against the reinsurer for coverage. However, this claim is based on the reinsurance contract between the insurer and the reinsurer. The reinsurer is under no obligation to pay directly to the policyholder, but must rather compensate the covered losses in relation to the insurer; however, the difference in the insolvency scenario is that the reinsurer must pay to the insolvent cedent (subject to certain defences) before the cedent has made its claim payments to the policyholders. The proceeds from reinsurance are not earmarked for the insureds whose claims have been reinsured, except for claims under life insurance, substitute health insurance, general and motor vehicle liability insurance as well as motor vehicle and accident insurance.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

In the event of a loss, the cedent typically sends through its reinsurance broker preliminary loss advice upon which a reinsurer settles the claim on a provisional basis if the cedent has made respective preliminary settlements. Such preliminary loss advice is updated over time until the final loss is established and adjusted by either a refund or additional payments. Any loss advice usually sets forth the ceded risks affected by the loss and a calculation of the coverage under the respective reinsurance agreement. In the absence of contractual provisions providing otherwise, the loss advice must be provided in due course, while any delay does not necessarily lead to a loss of the cedent's rights. Under statutory law, the cedent's claims become time-barred after the lapse of three full calendar years after its own settlement payments, although, owing to industry usage, arguably the limitation period does not start to lapse before the final amount of the claim has been determined, if the reinsurer was duly advised of the loss on a provisional basis. The parties are free to establish other frequencies of collection in the agreement, for example, on a quarterly basis or by means of a current account, which will then affect the start of the limitation period accordingly.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

This question typically arises in the context of excess of loss reinsurance where the reinsured establishes a scheme of protection by different layers and scopes of reinsurance. The allocation of claims and settlement payments of the reinsured largely depends on the wording of the reinsurance agreement. As an overriding principle, any loss may only be collected once and must fall within the subject matter of the reinsurance, which in individual cases might not always be a clear call. Reinsurance agreements often stipulate a ranking among each other, such as that any other reinsurance cover for the loss in question must be exhausted before claims can be made under the relevant reinsurance agreement. Frequently, the wording defines the scope of the reinsurance in a substantive way by describing the reinsured risks, while other agreements make reference to a specific portfolio. In each case, it might become necessary to look into the information exchanged during the negotiation of the cover to establish whether a particular loss can be collected. Occasionally, reinsurance agreements require the reinsured to make an active decision as to whether individual risks shall be covered, in which case the reinsured is asked to allocate the accepted risks to the reinsured portfolio (eg, by appropriate coding or entering into a bordereaux); the loss or settlement would then follow this allocation. In this context, the reinsured's allocations to the underlying policies may give guidance as to the allocation to the reinsurance agreements; however, the outward reinsurance will in many cases not correspond on a one-on-one basis to the inward business.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

While reinsurance agreements usually provide for an 'inspection of records' clause allowing the reinsurer to verify whether the cedent has handled and settled the claims in compliance with the terms of the reinsurance agreement, German statutory contract law would give the

reinsurer the right to demand detailed accounts. In addition, one would regard the right to inspect the cedent's records as a reinsurance custom.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

To the extent that commutation payments of a cedent are done in compliance with the follow-the-settlement principle, such claims must be honoured. With regard to incurred but unreported losses, these would usually be covered to the extent that cover is finally established under the underlying insurance policies. There is no duty on the part of the reinsurer to indemnify the cedent for incurred but not reported claims, unless the reinsurance agreement provides for an extension of the follow-the-settlement principle to payments beyond the regular liability of the reinsurer.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

The reinsurer's liability towards the cedent is determined by the reinsurance agreement, usually within loss settlements reinsurance clauses. In general, the customary duty to follow-the-settlements stipulates that the reinsurer has to pay for losses of the cedent as long as the cedent's decision to settle a loss was made within the terms of the underlying reinsured policy and the settlement is based on a prudent management of the underlying insurance relationship that took the interests of the reinsurer reasonably into account. Thus, the question is whether it is a loss in this sense or still a question of prudent management. However, we know of reinsurance agreements where reimbursement for certain ECOs is granted and agreements where such reimbursement is excluded. Cases where the reinsurance agreement does not contain a specific provision often end contentiously.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Bank of Greece is responsible for the supervision of private insurance and reinsurance companies in Greece through the Department of Private Insurance Supervision. It is responsible for carrying out the prudential supervision of insurance and reinsurance companies lawfully operating in Greece and of insurance intermediaries.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

In order to provide insurance or reinsurance services in Greece a company must meet a series of criteria set forth in Law No. 4364/2016, which implemented the Solvency II Directive (the Insurance Regulation Act). Among others, it must maintain its registered seat in Greece, operate in the form of a *société anonyme* and have as its exclusive object the provision of insurance activities. The company must evidence that it meets the statutory capital requirements, governance requirements, including any qualifications pertaining to officers and directors, and it must generally comply with all applicable regulatory requirements.

An insurance undertaking may be authorised under its operation licence to conduct either life or non-life insurance activities. By way of exception, insurers authorised on or before 1 January 1981 may retain a single licence for both life and non-life. Finally, it is noted that a licence to undertake insurance activities in a specific business line allows the insurance company to additionally undertake reinsurance undertakings in the respective business line.

In the reinsurance sector, the requirement of a single licence does not apply and therefore reinsurers can be licensed for both life and non-life reinsurance.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Other than the operation licence from the Bank of Greece, there are no additional licences and authorisations for the conduct of insurance. Under the EU passport regime, EU insurance and reinsurance companies are entitled to carry out the respective activities in Greece through a branch or under the Freedom of Services (FOS) regime.

Insurance companies incorporated in non-EU (third) countries, which intend to offer insurance services in Greece, must, in principle, obtain a licence to establish a branch from the Bank of Greece, on the condition of reciprocity.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

All officers and directors of insurance and reinsurance companies and all persons effectively running the undertaking or having key functions must at all times:

- possess adequate professional qualifications, knowledge and experience, in order to ensure sound and prudent management (professionally fit); and
- be of good reputation and integrity (proper).

Reliability is usually evidenced by recent criminal records and non-bankruptcy certificates (or other equivalent documents) on the basis of which it can be ascertained that said individuals have not been sentenced for certain crimes (including embezzlement, usury, fraud, extortion, smuggling, bribery and money laundering) and have not been declared bankrupt.

Furthermore, the board of a Greek insurance company must comprise in its majority Greek or other EU member-state citizens.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Insurance and reinsurance companies must comply with the solvency capital requirements of the Insurance Regulation Act aiming to guarantee that they are in a position to meet any obligations arising from the conduct of business.

Companies must calculate their solvency capital requirement on the assumption that they will carry out business as a going concern. They must also take into account all quantifiable risks (that are exposed to), cover existing business and business to be written in the following 12 months, correspond to the value-at-risk of the basic own funds of an insurance or reinsurance undertaking subject to a confidence level of 99.5 per cent over a one-year period.

As to minimum capital requirements, the Insurance Regulation Act introduces the following minimum thresholds (depending on the type of licence):

- €2.5 million for non-life insurers including captive insurance undertakings (unless such companies insure risks in classes 10 to 15 in which case the minimum capital requirement amounts to €3.7 million);
- €3.7 million for life insurers including captive insurance undertakings;
- €3.6 million for reinsurance companies (with the exception of captive reinsurers for which the amount is limited to €1.2 million); and
- €6.2 million for insurance undertakings with a single licence for both life and non-life authorised on or before 1 January 1981.

The minimum capital requirement shall neither fall below 25 per cent nor exceed 45 per cent of the respective solvency capital requirement including any capital add-on imposed by the Bank of Greece. Minimum capital requirements must be measured and reported to the Bank of Greece at least quarterly.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance and reinsurance companies are under the obligation to form and maintain reserves on a continuous basis and also calculate the amount of such reserves themselves in a prudent, reliable and objective

manner (taking into consideration all relevant financial market and risk underwriting information).

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The general and special terms of insurance policies and reinsurance agreements are neither subject to any prior notification or regulatory approval, nor must they be communicated to any regulator on a systematic basis. On request by the regulator, insurers may have to disclose applicable premiums as part of general price-control systems.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The supervision carried out by the Bank of Greece is based on an investigative and risk-based approach and depends, in particular, on the nature, complexity and volume of the risks undertaken by each company. Its scope is mainly prudential in nature. Among others, the Bank of Greece may carry out on-site and off-site inspections, may request any information and may have full access to the books and records of the supervised entities. It generally retains great discretion with respect to the frequency and type of regulatory examinations that it may carry out.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The Insurance Regulation Act follows the prudent person principle, according to which companies are free to decide how they invest their assets, provided that the interests of insureds are adequately safeguarded. The relevant risks must be properly identified, measured and controlled and all assets must be invested in a manner that ensures security, quality, liquidity and profitability. Assets covering technical provisions must, in addition, be invested in a manner appropriate to cover the nature and duration of the insurance liabilities. Investment decisions are not subject to any kind of limitation or prior approval or systematic notification requirements.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

A prior notification to the Bank of Greece must be filed by a party that intends to acquire, directly or indirectly, a holding as result of which such party would reach or exceed 10, 20, 33.3 or 50 per cent of voting rights or share capital, or would acquire control directly or indirectly. In terms of process, the Bank of Greece has in principle 60 business days to assess the intended acquisition. It may only oppose the proposed acquisition if there are reasonable grounds on the basis of criteria such as:

- the reputation of the proposed acquirer;
- the reputation and experience of any person who will direct the insurance or reinsurance company as a result of the proposed acquisition;
- the financial soundness of the proposed acquirer;
- whether the insurance undertaking will be able, and continue, to comply with the prudential requirements in particular, whether the group of which it will become a part has a structure that makes it possible to exercise effective supervision and effectively exchange information with the Bank of Greece; or
- whether there are reasonable grounds to suspect that, in connection with the proposed acquisition, money laundering or terrorist financing has been committed or attempted, or that the proposed acquisition could increase the risk thereof.

If the Bank of Greece does not oppose the proposed acquisition within the assessment period in writing, the acquisition shall be deemed approved. The Bank of Greece may not impose conditions as to the amount of the participation acquired nor can it carry out a full financial assessment on the basis of market conditions. However, it may impose an obligation to the target company to convert their shares in registered shares with voting rights for purposes of facilitating the supervision of all natural persons with beneficial interests in insurance and reinsurance companies.

In cases of non-compliance with the above obligation, the exercise of the voting rights attached to the holding is rendered ineffective by operation of law. The Bank of Greece also has the power to impose monetary fines up to 10 per cent of the value of the shares transferred without its approval or to prohibit participation in the management of the targeted company.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

Other than the general prudential requirement that the acquirer must be financially sound, no additional requirements or restrictions apply in respect of financing such acquisition.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

To the extent the acquisition of a minority interest amounts to a qualified holding (exceeds 10 per cent of the share capital or votes), the acquisition triggers a notification obligation to the Bank of Greece and is subject to regulatory approval. There are no special regulatory requirements and restrictions for acquisitions of participations falling below the above threshold.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

In general, foreign citizens, companies or governments are free to invest in insurance or reinsurance companies in Greece under the same rules that apply for Greek and EU investors. Where, however, an acquisition by a foreign investor triggers a notification obligation to the Bank of Greece and is subject to regulatory approval, the Bank of Greece has discretion to prolong the period during which it can require additional information for an additional 30 business days.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The Insurance Regulation Act includes detailed provisions for group supervision following closely Directive 2009/138/EC. These rules apply to group level insurance or reinsurance companies subordinated to other insurance, reinsurance, insurance holding or mixed financial holding company, having its registered seat in the EU or a third country. Among others, group supervision comprises the following:

- the group must report to the Bank of Greece any significant risk concentration at least on an annual basis (supervision of risk concentration);
- the group must report to the Bank of Greece any significant intra-group transactions by insurance and reinsurance undertakings within the group, including those performed with a natural person with close links to an undertaking, at least on an annual basis;

furthermore, very significant intra-group transactions must be reported to the competent regulator as soon as practicable (supervision of intra-group transactions); or
- the Bank of Greece ensures that appropriate governance systems (including risk assessment, internal audit and reporting systems) are in place within all companies of the group that are subject to group supervision (supervision of the system of governance).

In addition, the Insurance Regulation Act includes special provisions pertaining to the solvency of the group. Such provisions introduce a system of capital and surplus requirements that are calculated at group level.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Under Greek law, there are no specific regulatory requirements for reinsurance agreements, which are generally viewed as commercial arrangements subject to the contractual freedom of the parties and the provisions of general contract law. The prevailing view is that reinsurance should be considered as a form of non-life insurance and thus provisions of Law No. 2496/1997 (the Insurance Contract Act) also apply on reinsurance agreements by analogy to the extent compatible with the operation of a reinsurance agreement or directly to the extent that the parties expressly subject themselves to such rules.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There are no statutory restrictions as to the amount of ceded reinsurance and retention of risk by insurance companies; therefore, an insurer may in principle cede even 100 per cent of the risk to a reinsurer.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no statutory collateral requirements for reinsurance conducting reinsurance transactions.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

For purposes of calculating technical reserves, the value of recoverables and claims from reinsurance contracts with reinsurers that are not licensed in accordance with Directive 2009/138/EC or are located in a third country whose solvency regime is not deemed equivalent with that of the Directive is considered to be nil unless reinsurers have a high credit rating or they have provided adequate guarantees or commitments or the collateral or pledges are located within the EU.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The Insurance Regulation Act includes specific provisions for insolvent or financially troubled insurance companies. In principle, an insurance company may not be declared bankrupt but instead may be subject to a special winding up regime. In brief, the Bank of Greece issues a decision revoking the operation licence of the insurance company, which is followed by a stage of insurance liquidation. Thirty days following the revocation of the licence, all policies that the latter has issued are terminated by operation of law.

Winding up of insurance companies constitutes a formal process, which is additionally governed by the provisions of the Greek Bankruptcy Code, the Greek Corporate Act and the Greek Code of Civil Procedure (GCCP). The Bank of Greece appoints a special insurance liquidator, who has a wide range of authorities (including, indicatively, the power to dispose assets and to enter into loans) for the purpose of carrying out the winding up process. The product of the liquidation of the company is evenly distributed to all eligible beneficiaries.

In addition, the Insurance Regulation Act provides the Bank of Greece with authority to adopt appropriate reorganisation measures that could be considered as a pre-bankruptcy stage. Such measures include the placement of the insurance company under special administration, the imposition of an obligation on the insurance company to effect a share capital increase, the mandatory transfer of insurance portfolios, the suspension of due and non-due payments to policyholders and beneficiaries for a certain period of time and the reduction of insurance claims.

For reinsurance companies, the general rules of the Greek Bankruptcy Code will apply.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The priority of claims against an insurance company in a winding-up scenario is as follows:
- all expenses arising out of the winding-up procedure (including insurance liquidator's fees) take absolute priority over the assets of the insurance business under liquidation;
- further to payment of all expenses arising out of the winding-up procedure, the following categories of claims take priority:
  - claims by employees arising from employment contracts and employment relationships;
  - tax claims of the Greek State;
  - claims of social security funds; and
  - claims on assets of the company that are subject to in rem rights; and
- all insurance claims from life, non-life and motor liabilities take precedence over any other claims against the insurance business.

The provisions of the Greek Bankruptcy Code and GCCP in respect of priority of claims also apply in insolvency proceedings involving insurance and reinsurance companies, to the extent they are not in conflict with the above.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Intermediaries having the capacity to represent insurance and reinsurance undertakings are insurance and reinsurance agents and tied insurance intermediaries who must be registered with the local Professional Chamber. They must possess adequate professional qualifications, knowledge and experience and they must be in good standing for the conduct of this profession. In order to be qualified, they must submit documentation such as an intermediary's certificate of professional qualification, good-standing certificates, tax clearance and criminal record certificate and professional indemnity mandatory insurance. Third-party administrators and claims adjusters do not require an authorisation, unless they act as intermediaries. Licensed insurance consultants and brokers do not represent insurance and reinsurance companies.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Pursuant to the Insurance Contract Act, a third party may bring a direct action against an insurer only for mandatory liability insurances and up to the defined statutory amount for which the insurance is mandatory. A typical example is the claim of a third party suffering damages from the use of motor vehicles. In case the claims from the insurance policy are assigned to a third party (subject to the rules for a valid assignment), the assignee may also bring a direct claim against the insurer.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The policyholder has a duty to notify the insurer within eight days about the occurrence of the insured risk and provide all necessary information and data relevant to the circumstances. The policyholder cannot claim lack of knowledge of the occurrence of the risk if this is because of its gross negligence.

The breach of this duty does not, however, result in a right of the insurer to deny coverage for late notice of claim. Only for non-life insurances, the insurer may seek restitution of any damage suffered because of such late notice, when this is attributed to the fault of the policyholder (ie, negligence or wilful misconduct). It is accepted that the right of the insurer to seek restitution may be available even before the lapse of the eight-day period, provided that the insurer can prove that the policyholder was aware of the occurrence of the risk, of the damage and the causal link between them and did not notify the insurer because of negligence or wilful misconduct. Deviations from these provisions of the Insurance Contract Act are accepted for large risks and reinsurances.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

The insurer's wrongful and unjustified denial of a claim may, under conditions, substantiate a claim in tort, in which case the insurer may be requested to pay damages (including interest and legal expenses). However, the mere delay or non-payment of the insurance compensation does not per se amount to tort unless the denial of the insurer is found to contradict bonos mores or to be intentional. In cases of tort, moral damages may be adjudicated by the court.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

As a general rule, liability insurances provide that the insurer undertakes to pay compensation for justified third-party claims, thus releasing the policyholder of its liability towards the third-party claimant, and also to defend the policyholder in the conduct of relevant proceedings against unjustified claims. Under common practice, the terms, conditions and circumstances under which the insurer has a duty to defend a claim are defined in the insurance policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

According to the Insurance Contract Act, the insurer must pay the insurance indemnity without undue delay on the occurrence of the insurance risk and notification from the policy holder. In case the assessment of the loss and of the insurance indemnity requires a longer period of time, the insurer is still under obligation to pay any uncontested amount. Deviations are accepted for large risks, where the parties may freely decide the terms under which payment obligations are triggered.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

If the misrepresentation is intentional, then the insurer may terminate the policy with immediate effect within one month as of knowledge thereof. The misrepresentation must refer to a material fact or circumstance, such as the age of the insured. If the misrepresentation is made because of negligence or without default, then insurance coverage is valid and not subject to right of the insurer to terminate. In any case, the policyholder shall be entitled only to the surrender value of the policy.

28 Punitive damages

Are punitive damages insurable?

Although punitive damages are not permitted under Greek law, it should be accepted that insurers would be free to agree on the insurance of punitive damages. However, this is uncommon in practice.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

There is no specific rule of the Insurance Contract Act on such obligation of an excess insurer. This is a matter regulated by agreement of the parties within the insurance policy. Therefore, if the prime insurer is insolvent or coverage is unavailable, this does not entail automatic obligation of the excess insurer to drop down and pay a claim.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

If a retention of risk or deductible has been agreed, the insurer is obliged to pay any amount in excess of the agreed retention or deductible, and this may not be altered by the insolvency of the insurer. However, such retention or deductible may not be agreed for mandatory third-party liability insurance.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

For mandatory liability insurances, the Insurance Contract Act provides that in cases of multiple claims, each party shall be indemnified in proportion to his or her claims. If the insurance indemnification paid to a third party exceeds this proportion, the insurer is released from an obligation for any amount exceeding the insured sum, unless the insurer made the above payment while aware of the existence of these other claims. The remaining claimants shall, however, have a claim against the indemnified third party for the refund of the sums received in excess of the allotted proportion.

In the absence of an explicit statutory provision for other types of insurances, multiple claims of the policyholder shall be satisfied in the order of their notification to the insurer, while third-party claims will be treated proportionally.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Multiple insurance contracts are valid up to the total value of the insured loss. In the absence of agreement between the parties to the contrary, the insurers are severally liable up to the insured sum stipulated in their contracts. It can be agreed (and often this is the case) that in the event of non-disclosure of other insurance policies with the same cover that are existing at the time of conclusion of the policy, the insurance compensation will be limited to the extent not covered by the previous policy. If the policyholder or the insured intentionally fail to disclose this, then the insurer is entitled to terminate the policy with immediate effect within one month after he or she acquired knowledge of the further contract or contracts. In case the insured risk occurs within this period, the insurer shall be released from any obligation to pay the insurance compensation and in addition, the policyholder shall be liable for any loss suffered by the insurer.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Although in principle the parties are free to conclude insurance contracts covering disgorgement or restitution claims, this is uncommon in practice. In the cases of pollution insurance, the insurance cover often

includes restitution of the natural environment from the occurrence of the insured risk.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

There is no reported jurisprudence of Greek courts determining when a single event, resulting in multiple injuries or claims, constitutes more than one occurrence under an insurance policy. This is typically a matter of agreement of the parties within the insurance policy. In the absence of any special agreement, the courts will apply the general principle of reasonable causality between the event and the occurrence of the multiple claims on an ad hoc basis.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The policyholder must disclose to the insurer all information or circumstances that are objectively material for the assessment of risk by the insurer.

In case any misstatements in the application are intentional, the insurer is entitled to terminate the policy with immediate effect within one month after becoming aware of the misstatement. In case the insured risk occurs within this period, the insurer shall be released from the obligation to pay. In addition, the policyholder shall be liable for any loss suffered by the insurer. In cases of life insurance contracts, the policyholder shall be entitled only to the surrender value of the policy.

In case the misstatements are owing to negligence of the policyholder, the insurer may either terminate the contract or propose its variation, within one month after being aware of the misstatement. If the proposal of the insurer is not accepted by the policyholder within one month after its receipt, the contract is considered terminated, effective within 15 days of its receipt by the policyholder or after one month of the receipt of the insurer's proposal for variation. In case the insured risk occurs prior to the variation of the insurance contract or before the effective date of termination, the insurance compensation shall be reduced in proportion to the difference between the premium payable (following the variation) and the premium payable, should no breach of the duty to disclose have occurred. The above provisions on misstatements owing to negligence do not apply to life and health insurances.

Finally, in case the misstatements are not attributed to a party's fault, the insurer may either terminate the contract or propose its variation, within one month after he or she became aware of the misstatement. If the proposal of the insurer is not accepted by the policyholder within one month of its receipt, the contract shall be considered terminated, effective within 15 days of its receipt by the policyholder or within one month after the receipt of the insurer's proposal for variation.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Reinsurance disputes are uncommon in Greece. Insurers and reinsurers would tend to either settle a dispute out of court or through arbitration proceedings, which are often not held in Greece or are not governed by Greek law.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

The most common issues arising in reinsurance disputes are the triggering event of the obligations of the reinsurer, the extent of its obligations and the evaluation of damages. The very limited Greek jurisprudence recognises standard contractual clauses such as the follow-the-fortune or settlement clause, the claims control clause, the cut-through clause and others that have been developed by English case law.

Update and trends

The Insurance Regulation Act has been introduced and is in effect as of 1 January 2016. It provides for the issuance of a series of secondary and regulatory decisions that are expected to be issued and that will clarify and give the tone of the supervision and the regulatory enforcement in the market. Because of both Solvency II requirements and the unprecedented financial crisis in the country, the Greek insurance market is undergoing a serious consolidation, which will take the form of aquisitions, divestitures and portfolio transfers.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Pursuant to the GCCP, arbitral awards must include, inter alia, the reasoning on which the decision is based, unless the parties agree otherwise.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitral tribunals and arbitrators do not, in principle, have any power over non-parties to the arbitration agreement. Arbitrators cannot order, revise or otherwise revoke injunctive relief measures. However, they may request the support of the local court in the taking of evidence, which may result, to a certain extent, in the compelling of non-parties to provide testimony or to produce documents.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Parties to the arbitration agreement as well as any third party having lawful interest may file an appeal for annulment of the arbitral award within three months of the date of the service of the award (on penalty of inadmissibility) before the local court of appeals. The annulment of an award, in whole or in part, may, in accordance with the GCCP, be declared for the following reasons:

- nullity of the arbitration clause;
- issuance of the award after lapse of effect of the arbitration clause;
- appointment of arbitrators was made in breach of the arbitration clause;
- award was issued in excess of the ambit of the arbitration clause or the law;
- a party was not properly notified to participate in breach of principle of equality;
- award was not issued with required majority, nor in writing, nor bearing signatures;
- award did not include the de minimis elements required by law (including arbitration clause, the reasoning, the tenor of the decision);
- award violates public policy or bonos mores; or
- award is not understandable or includes contradictory provisions.

Parties to the arbitration agreement may also request correction or interpretation of an award. Parties may also agree in writing to allow appeal against the award but they must determine in advance the conditions, deadlines and the process for its filing and hearing. An arbitral award generally has the same effect of res judicata (both substantive and procedural) with a court judgment and also constitutes an enforceable title under Greek law.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There is no statutory obligation on the reinsurer to follow its cedent's underwriting fortunes and the claim payments or settlements. However, both in theory and in the limited Greek jurisprudence this is generally accepted as a well-established principle of the treatment of reinsurance agreements and would be taken into primary consideration in the absence of an explicit contractual clause. Possible defences of the reinsurer would be that the claims paid or settled by the reinsured were not covered by the ambit of the reinsurance agreement or that the cedent did not act prudently or in the utmost good faith.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

While there is no specific statutory provision for good faith in reinsurance agreements, it is supported mainly in theory that there is a duty of utmost good faith that must be inherent in both insurance and reinsurance agreements. This was also accepted by a court decision in Greece in the context of marina insurance (pre-contractual disclosures, notice of claim).

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Except for their different business rationale and operation, facultative and treaty reinsurance are not subject to different sets of rules.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Greek law applies the privity of contract principle, according to which a contract confers rights and obligations only on the contracting parties. Therefore, non-signatories to a reinsurance agreement (such as policyholder or insured) are not entitled to and cannot directly seek insurance proceeds or demand on their own direct reinsurance payments. The most significant exception to this rule arises where the reinsurance agreement includes a cut-through or similar provision that gives the right of the policyholder to recourse directly to the reinsurer or in the case of insurer insolvency by permitting funds to pass directly to the policyholder, rather than to the estate of the insolvent reinsured.

Furthermore, GCCP provides that in case a debtor fails to enforce his or her rights against third parties to the detriment of any creditor, the creditor may, under specific conditions, take legal action in court in order to enforce the debtor's rights.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The insolvency of the insurer does not trigger the obligation of the reinsurer to pay directly to the policyholder. Typically, in the event of insolvency of the insurer, the reinsurance proceeds are paid to the insolvency administrator for the benefit of all policyholders, whereas reinsurance agreements usually contain similar insolvency clauses. This rule may be derogated where the reinsurance agreement includes a cut-through or similar provision that, in essence, alters the reinsurer's obligations in the case of insurer insolvency by permitting funds to pass directly to the insured, rather than to the estate of the insolvent reinsured.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

There are no specific rules on notice and information. However, given that reinsurance is generally deemed to constitute a form of non-life insurance, it should be accepted that notice must be given without undue delay in a manner similar to that applicable to insurance policies. Therefore, the issue of notice and information should be specifically regulated in the reinsurance agreement.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

There are no specific provisions on the allocation of underlying claim payments. This is a matter to be regulated by the reinsurance agreement. In practice, reinsurance agreements provide either for an allocation pro rata to the reinsured amounts or for layers among each other in the sense that the reinsured must first exhaust the first policy before going to the subsequent reinsurance.

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48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Greek law does not provide specific rights to reinsurers with respect to a reinsured insurer claim handling, settlement and allocation decisions. Industry practice and customs show that typically reinsurance agreements would include a clause allowing the reinsurer to have a rather extended right of access and audit to the records and accounts of the insurer and its handlings.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

The insurer has to reimburse a cedent insurer for any payments made in accordance with the follow-the-settlement principle provided that the insurer exercises the necessary due diligence in making these payments. As regards incurred but not reported claims, there is no duty to reimburse the cedent, unless this is explicitly provided in the reinsurance agreement.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

There are no specific rules on ECOs and therefore this is subject to agreement between the parties in the reinsurance agreement. Normally, ECOs are expressly excluded from reimbursement.

India

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Insurance and reinsurance companies and insurance intermediaries in India are governed by the Insurance Regulatory and Development Authority of India (IRDAI). The primary legislation regulating the Indian insurance sector comprises of the Insurance Act 1938 (Insurance Act) and the Insurance Regulatory and Development Authority Act 1999 (IRDA Act). Pursuant to the powers granted to it under the IRDA Act, the IRDAI has issued various regulations for governing the licensing and functioning of insurers, reinsurers and insurance intermediaries. The IRDAI has also released the IRDAI (Registration and Operations of Branch Offices of Foreign Reinsurers other than Lloyd's) Regulations 2015 (Branch Office Regulations), which govern the establishment and functioning of branch offices in India set up by foreign reinsurers (foreign reinsurer branch), and has also notified regulations pertaining to the entry of Lloyd's into the Indian market as well.

Although the Insurance Laws (Amendment) Act 2015 (Amendment Act), which was passed in March 2015, introduced a plethora of changes to the Insurance Act and the insurance regulatory framework in general, the primary insurance regulator continues to be the IRDAI. Appeals from orders issued and decisions made by the IRDAI may now be referred before the Securities Appellate Tribunal (SAT). Subsequently, the procedural rules for filing appeals from the IRDAI orders or decisions with the SAT were also notified. As per the publicly available information, appeals against four IRDAI orders (involving insurance intermediaries) have been decided by the SAT and two appeals filed by insurers are pending.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Under the Insurance Act, an Indian insurance company is permitted to carry on insurance business in India. An Indian insurance company is a public limited company formed under the Companies Act 2013 (Companies Act), which exclusively carries on life insurance business or general insurance business or health insurance business or reinsurance business. An entity desirous to carry on insurance business is required to apply for a certificate of registration from the IRDAI in accordance with a three-stage process set out under the IRDA (Registration of Indian Insurance Companies) Regulations 2000 (Registration Regulations). A certificate for registration is required for each category of insurance business (ie, life, general, standalone health and reinsurance). In addition, the Registration Regulations also set out the essential requirements that an applicant applying for registration is required to fulfil, including, but not limited to:

- permissible foreign investment limits;
- minimum capitalisation requirements;
- minimum qualifications of the directors and principal officers;
- planned infrastructure; and
- general track record of conduct and performance of each of the Indian promoters and foreign investors in the business or profession they are engaged in.

The applicant must also provide adequate documentation in support of its application as prescribed under the Registration Regulations.

Further, the Amendment Act permitted the establishment of foreign reinsurer branches and setting up of service companies under the Lloyd's India framework. The Branch Office Regulations prescribes that a foreign reinsurer is required to apply for registration of a foreign reinsurer branch. The Branch Office Regulations specify the eligibility criteria of a foreign reinsurer, such as credit rating, infusion of minimum assigned capital into the foreign reinsurer branch, in-principle clearance from home country regulator, and commitment to meet all liabilities of the foreign reinsurer branch. In addition, syndicates of Lloyd's may now participate under the Lloyd's India framework (Syndicates of Lloyd's India) through a service company set up in India in accordance with the IRDAI (Lloyd's India) Regulations 2016 (Lloyd's India Regulations).

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Other than registration under the Insurance Act and general company law, no additional licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business. Banks that intend to set up insurance joint ventures with equity contributions on a risk participation basis or make investments in insurance companies are required to obtain prior approval of the Reserve Bank of India before engaging in such business.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The Registration Regulations prescribe that the IRDAI will consider the following when considering granting registration to an insurance or reinsurance company:

- the performance record of the directors and persons in the management of the promoter of the applicant and the applicant;
- the level of actuarial and other professional expertise within the management of the applicant company; and
- the academic and professional qualifications, professional experience, reputation and character of the directors and key persons, and whether any censure or disciplinary actions, dismissals and litigations have been instituted against them.

In addition to the foregoing, the application process for registration requires substantial details about the qualifications and professional background of the top management of the applicant.

The Branch Office Regulations, which prescribe similar requirements as above, require the key management persons of the foreign reinsurer branch to be appointed with the prior approval of the IRDAI. Moreover, an executive committee of the foreign reinsurer branch is required to be constituted by the board of directors of the foreign reinsurer to perform the functions of the board with clearly defined delegation from such board of the foreign reinsurer. Lloyd's is required to obtain a prior approval from the IRDAI for the appointment, removal

or managerial remuneration payable to the Chief Executive Officer of Lloyd's India. Further, the details of the key management persons of service companies along with their bio data are required to be submitted at the time of registration with the IRDAI. Any change in the details submitted is required to be intimated to the IRDAI.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Insurance companies are required to have a minimum paid-up equity capital of 1 billion rupees, while a minimum paid-up capital of 2 billion rupees has been prescribed for reinsurance companies. For foreign reinsurer branches, the minimum assigned capital shall be 1 billion rupees. In addition, minimum assigned capital of 1 billion rupees is required to be infused in Lloyd's India by Lloyd's. Syndicates of Lloyd's India are required to maintain an assigned capital of 50 million rupees through their service companies in India.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance and reinsurance companies are required to maintain at all times an excess value of assets over the amount of liabilities of not less than 50 per cent of the amount of the minimum capital requirement of such insurance or reinsurance company. In addition, insurance and reinsurance companies are also mandated to maintain a minimum solvency margin. The required solvency margin is calculated by insurance companies themselves on the basis of their mathematical reserves and the sum at risk. The IRDAI periodically specifies the factors that are considered in the calculation of the required solvency margin. The Branch Office Regulations prescribe that the foreign reinsurer setting up a foreign reinsurer branch shall fully comply with the solvency margin requirements under the home country's regulatory requirements. Moreover, the foreign reinsurer branch and the service companies registered under the Lloyd's India framework are also required to maintain their solvency margin in accordance with the applicable regulations issued by the IRDAI.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The IRDA (Protection of Policyholders' Interests Regulations) 2002 (Policyholders Regulations) prescribe certain terms to be incorporated in both life insurance and general insurance policies. For life insurance policies, the IRDAI requires insurance companies to include, inter alia:

- name of the product;
- whether it is participating in profits and the basis thereof;
- benefits payable and the contingencies on which these are payable;
- details of riders;
- date of commencement of risk;
- maturity date; and
- premium details, including regarding the grace period for premium payment, conditions of non-forfeiture, revival of lapsed policies, exclusions, provisions for nomination, assignment, claim documentation requirements and the communication address of the insurance company.

General insurance companies are required by the Policyholders Regulations to incorporate, inter alia:

- name and address of the insured and banks or other persons financially interested in the subject matter of insurance;
- full description of the property or interest insured;
- location of the property or interest insured;
- period of insurance;
- sums insured;
- perils that are covered and not covered;
- franchise or deductible applicable;
- premium payable and, if adjustable, the basis for the same;
- policy terms and conditions;
- warranties;
- obligations of the insured on occurrence of claim circumstances;
- applicable riders; and
- pro forma of any communication insurance companies may seek from the policyholders.

Under the IRDAI (Health Insurance) Regulations 2016, the IRDAI has specified a number of regulatory requirements and conditions that are required to be incorporated into health insurance policies making such policies highly regulated. The IRDAI has also prescribed a standard set of definitions, standard nomenclature for critical illnesses, and a standard list of excluded expenses in relation to health insurance policies.

It is relevant to note that insurance contract wording is highly regulated. The terms and conditions of property and engineering insurance covers are currently governed by the policy wordings specified by the former Tariff Advisory Committee. Very few modifications to these policy wordings have been permitted. On all other lines of insurance business (except 'mega risks' and other forms of specialised insurance covers), insurance companies are permitted to issue only those policy terms and conditions, endorsements and other ancillary documentation that have been approved by the IRDAI in advance under the relevant product filing procedures. No changes are permitted to be made unless the prior approval of the IRDAI is obtained.

Note that the IRDAI has recently released an exposure draft that proposes to replace the Policyholders Regulations. The exposure draft prescribes, inter alia, the matters to be stated in a health insurance policy and also stipulates that life insurers shall attach a 'key feature document' along with the policy documents. However, the exposure draft is yet to be finalised.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Insurance companies, reinsurance companies and insurance intermediaries are amenable to inspections and investigations by the IRDAI. No specific frequency has been prescribed for such investigations and inspections. With the passing of the Amendment Act, even service providers and contractors to insurance companies or intermediaries are obliged to furnish to the IRDAI, if required, during any investigation or inspection, all such books of account, registers, other documents and databases in their custody or power that relate to the affairs of the insurance company or intermediary. Directors and other officers of such service providers or contractors may also be called on by the IRDAI to furnish statements on oath.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Investments made by insurance and reinsurance companies are governed by the Insurance Act, the IRDAI (Investment) Regulations 2016 (Investment Regulations) and various circulars issued by the IRDAI. The Insurance Act mandates that assets of life insurers should be invested as follows: 25 per cent in government securities, a further sum equal to not less than 25 per cent in government securities or approved securities, and the balance in any other approved investment in accordance with the Investment Regulations. General insurers are required to invest 20 per cent of the assets in government securities, a further sum equal to not less than 10 per cent of the assets in government securities or approved securities, and the balance in any other approved investment in accordance with the Investment Regulations. Reinsurers and foreign reinsurer branches are required to invest and keep invested at all times 20 per cent of the assets in government securities, a further sum equal to not less than 10 per cent of the assets in government securities or approved securities, and the balance in any other approved investment in accordance with the Investment Regulations.

The Investment Regulations, which contain the exposure or prudential norms, set out, inter alia, the limits on investments to be made by insurers or reinsurers on the basis of the investee company, group or industry. In addition, subject to the Investment Regulations, insurers cannot invest more than 5 per cent of their assets in companies

belonging to promoters. Moreover, insurers are also prohibited from investing the funds of policyholders, directly or indirectly, outside India.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Per section 6A of the Insurance Act read with the IRDAI (Transfer of Equity Shares of Insurance Companies) Regulations 2015, prior approval from the IRDAI must be obtained in the event of a change in shareholding of an insurance or reinsurance company where, after the transfer, the total shareholding of the transferee is likely to exceed 5 per cent of the total paid-up capital of the company.

In addition, prior approval of the IRDAI must also be obtained in the event the nominal value of the shares intended to be transferred by any individual, firm, group, constituents of a group or body corporate under the same management, jointly or severally, exceeds 1 per cent of the total paid-up capital of the insurance or reinsurance company.

Note that there are no specific provisions dealing with background investigations of officers and directors of acquirers. However, while obtaining the IRDAI's approval, information regarding whether the directors of the transferee have ever been refused a licence or authorisation in the past to carry on regulated financial business or whether any company, firm or organisation with which such directors have been associated as directors, officers or managers has been investigated by a regulatory or professional body may be required to be submitted.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The Indian insurance regulatory framework does not expressly regulate financing of the acquisition of an Indian insurance or reinsurance company.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no specific provisions or requirements under the Indian insurance regulatory framework on the acquisition of a minority interest in an insurance company or reinsurance company.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

With the passing of the Amendment Act, foreign investment in insurance and reinsurance companies was increased from 26 to 49 per cent of the paid-up equity capital. In order to implement the changes introduced by the Amendment Act, the Ministry of Finance notified the Indian Insurance Companies (Foreign Investment) Rules 2015 (Foreign Investment Rules) on 19 February 2015. The Foreign Investment Rules provided that approval of the Foreign Investment Promotion Board set up under the Ministry of Finance (FIPB) will be required for any foreign investment over 26 per cent and up to the permissible limit of 49 per cent. However, on 16 March 2016, the Foreign Investment Rules were amended to reflect that foreign investment up to 49 per cent of the total paid-up equity capital of an insurance or reinsurance company shall be allowed on the automatic route (ie, without requiring any approval from the FIPB) subject to verification by the IRDAI. Subsequently, the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry notified the Consolidated Foreign Direct Investment Policy on 7 June 2016 to ensure uniformity with the Foreign Investment Rules.

In addition, the Amendment Act also mandated that insurance and reinsurance companies must be 'Indian owned and controlled'. The Foreign Investment Rules read with the Guidelines on 'Indian owned and controlled' of 19 October 2015 (IOC Guidelines) provide that 'Indian ownership' means that more than 50 per cent of the equity capital is beneficially owned by resident Indian citizens or Indian companies, which are owned and controlled by resident Indian citizens. Further, 'Indian control' of an insurance or reinsurance company shall mean control of such company by resident Indian citizens or Indian companies, which are owned and controlled by resident Indian citizens. 'Control' includes the right to appoint a majority of the directors or to control the management or policy decisions by virtue of shareholding, management rights or shareholders agreements or voting agreements.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

In relation to the IRDAI's supervision of the group to which an insurance company, reinsurance company or insurance intermediary belongs, it should be noted that the IRDAI directly regulates only those insurance companies, reinsurance companies and insurance intermediaries operating in the Indian insurance sector, and currently does not regulate the operations of the group entities of such insurance companies or insurance intermediaries. However, there are some restrictions on insurance companies and insurance intermediaries operating in the same group, where the IRDAI has discretion (in some cases) to determine the scope of 'group':

- an Indian corporate group can have an insurance company and an insurance broker within the same group, subject to certain conditions being fulfilled;
- typically, within a group, the IRDAI will grant register to licence only one entity for insurance intermediation unless a case on merits and with no conflict of interest is made before the IRDAI;
- a web aggregator cannot be a related party of an insurance company;
- there is no express restriction on insurance companies and surveyors operating in the same group, but the IRDAI is likely to view this as an inherent conflict of interest;
- there is no express restriction on insurance companies and third-party administrators (TPAs) operating in the same group; and
- an insurance agent or insurance intermediary is not permitted to be a director of an insurance company.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

In relation to reinsurance contracts, the reinsurance regulations issued by the IRDAI define a contract of reinsurance as a legally binding document on all the parties that provides a complete, accurate and definitive record of all the terms and conditions and other provisions of the reinsurance contract. The reinsurance arrangements do not need to be pre-approved by the IRDAI, but they must be documented and filed with the IRDAI within the stipulated time frame.

The overarching regulatory framework for the reinsurance of general insurance risks in India is set out in the IRDAI (General Insurance – Reinsurance) Regulations 2016 (General Reinsurance Regulations), and in the case of life insurance risks, in the IRDA (Life Insurance-Reinsurance) Regulations 2013 (Life Reinsurance Regulations). The guiding principle is maximising retention within India, so each Indian Insurer must maintain the maximum possible retention commensurate with its financial strength and volume of business. An Indian insurer is also strictly prohibited from fronting for a foreign insurer or reinsurer. There is no statutory or regulatory definition of what amounts to fronting, but this will essentially be a question of, inter alia, the extent of control that is exercised by the foreign insurer or reinsurer over functions such as whether to write a risk, the price to quote for the risk, the setting of discretionary limits and the handling of claims.

Further, Indian insurers are required to mandatorily cede a certain percentage (currently 5 per cent) of the sum assured on each policy

for different classes of insurance written in India to the state-owned GIC Re.

In addition, subject to the retention limit and the mandatory cession to GIC Re for reinsuring the remaining insurance risks, every Indian insurer, with effect from 16 January 2017, is required to comply with the 'order of preference for cession' prescribed under R28(9) of the Branch Office Regulations. An Indian insurer is now required to first offer its facultative and treaty surpluses to Indian reinsurers having a minimum credit rating that denotes good financial characteristics for the preceding three years (currently, GIC Re) and thereafter to foreign reinsurer branches that have been registered under Category I of the Branch Office Regulations (ie, where foreign reinsurer branch maintains a minimum retention of 50 per cent of the Indian reinsurance business). The Indian insurer may then proceed to offer the surplus to other Indian reinsurers or to those foreign reinsurer branches registered under Category II of the Branch Office Regulations (ie, where the foreign reinsurer branch maintains a minimum retention of 30 per cent of the Indian reinsurance business), followed by foreign reinsurer branches set up in special economic zones, and the balance, if any, may be offered to other Indian insurers and overseas reinsurers.

Note that Indian insurers are also required to comply with various requirements set out in the reinsurance regulations, including filing requirements for the reinsurance programme, and the wording of the reinsurance treaty contract and excess of loss cover note, as well as every new reinsurance arrangement entered into.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

As mentioned above, Indian insurers are mandated to retain risk proportionate to their financial strength and business volumes. The IRDAI has not issued any specific guidance on the appropriate minimum amount to be retained by insurers. Further, Indian insurers are also required to mandatorily cede the prescribed percentage (currently 5 per cent) of the sum assured on each policy for different classes of insurance written in India to GIC Re. So far as the 'order of preference for cession' (see question 15) is concerned, no specific amount or percentage has been prescribed for placement of reinsurance risks by an Indian insurer with the relevant entities set out therein.

Per the reinsurance regulations, surplus over and above the domestic reinsurance arrangements shall be placed outside India with only those reinsurers (cross border reinsurers (CBR)) that satisfy the prescribed criteria and have made the relevant filing with the IRDAI. Specifically, the General Reinsurance Regulations stipulate the maximum limit on reinsurance cession that can be made by an Indian insurer to a particular CBR under any insurance segment and is as follows:

- if the Standard and Poor's (S&P) rating of the CBR is BBB and BBB+, then up to 10 per cent cession is allowed;
- if the S&P rating of the CRB is greater than BBB+ and up to and including A+, then up to 15 per cent cession is allowed; and
- if the S&P rating of the CRB is greater than A+, then up to 20 per cent cession is allowed.

Any cession to a CBR that does not satisfy the eligibility criteria or where the cession is above the prescribed limit requires the prior approval of the IRDAI for placement.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

The Indian insurance regulatory framework does not specify any collateral requirements for reinsurance companies in a reinsurance transaction.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

The Indian insurance regulatory framework does not presently expressly regulate requirements for cedents to obtain credit for reinsurance on their financial statements.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The insolvency and bankruptcy law in India has recently been overhauled by way of the Insolvency and Bankruptcy Code 2016 (Insolvency and Bankruptcy Code). The Insolvency and Bankruptcy Code provides the insolvency and liquidation process for corporate persons. However, it is relevant to note that insurers have been excluded from the scope of 'corporate debtor' as defined under the Insolvency and Bankruptcy Code.

The Insurance Act specifically provides that the winding up of an insurance company shall be in accordance with the procedure laid out in the Companies Act 2013 (Companies Act). In addition, the Insurance Act specifies certain other conditions under which the court may order the winding up of an insurance company.

The process of the winding up involves compliance with various procedural requirements set out in the Companies Act. The process includes:

- the appointment of a liquidator;
- realisation of the assets of the company;
- repayment of all the outstanding creditors and any other statutory dues owed by the company; and
- dissolution of the company.

In relation to repayment of the creditors and outstanding dues of the company, the Companies Act provides that certain dues are required to be paid in priority, including dues to workmen and employees of the company, and the statutory dues owned to governmental authorities.

Further, the Insurance Act provides that the voluntary winding up of an insurance company is subject to certain restrictions. An insurance company cannot be wound up voluntarily except for the purpose of effecting an amalgamation or a reconstruction of the company, or on the ground that by reason of its liabilities it cannot continue its business.

An insurance company may also be partially wound up, whereby a class of their business is wound up but another class continues to operate either by itself or through another insurance company on transfer. In such a scenario, a scheme may be prepared and submitted in court that should provide for the following: the allocation and distribution of the assets and liabilities of the company between any classes of business affected (including the allocation of any surplus assets that may arise on the proposed winding up) for any future rights of every class of policyholder in respect of their policies; and the manner of winding up any of the affairs of the company that are proposed to be wound up. The scheme may also include provisions for altering the memorandum of association of the company with respect to its objects and such further provisions as may be expedient for giving effect to the scheme.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The Indian insurance regulatory framework does not specifically regulate the priority of claims against an insurance or reinsurance company in an insolvency proceeding.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The IRDAI regulations govern all insurance intermediaries, that is:

- insurance agents;
- corporate agents;
- insurance brokers;
- insurance marketing firms (IMFs);
- TPAs;
- surveyors and loss assessors; and
- web aggregators.

Insurance intermediaries need to obtain licences and registrations pursuant to the provisions of the specific regulations that are applicable to them in view of the nature of the business proposed to be undertaken

by them. The IRDAI has issued regulations setting out the licensing or registration requirements (including eligibility criteria, capital and net worth requirements, qualification requirements of the principal officer, directors or partners of the concerned entity) and procedures for all the above-mentioned intermediaries. Licence or registration is typically granted for a period of three years, which may be renewed thereafter. Insurance intermediaries (except corporate agents whose principal business is other than insurance distribution) are not permitted to have more than 49 per cent (under automatic route (ie, without requiring any prior government approval) as foreign direct investment and such entities must be 'Indian owned and controlled'.

Insurance agents
An individual may be appointed as an insurance agent by an insurer on complying with the conditions provided under the regulations notified by the IRDAI in this regard. An insurance agent is required to have passed the relevant examination and is also required to possess the requisite knowledge for soliciting insurance business and providing necessary services to policyholders. An insurance agent is permitted to solicit insurance business for only:
- one life insurer;
- one general insurer;
- one health insurer; and
- one each of the mono-line insurers.

Corporate agents
Entities eligible to operate as corporate agents include:
- firms;
- banks;
- non-banking financial companies;
- cooperative societies;
- non-governmental organisations; and
- companies.

An entity registered as a corporate agent may either exclusively carry on the business of insurance distribution or engage in any business other than insurance distribution as its main business. Where a corporate agent has a main business other than insurance distribution, then that agent is not permitted to make the sale of its products contingent on the sale of an insurance product, or vice versa. A corporate agent may have arrangements with a maximum of three insurers in each category of life, general or health insurance.

Insurance brokers
Insurance brokers are required to exclusively carry on the distribution of insurance products. Any company, limited liability partnership or cooperative society may apply to the IRDAI for the grant of an insurance broker licence. Applicants may register as direct brokers, reinsurance brokers or composite brokers (involved in both direct and reinsurance broking). The minimum capital for direct brokers is 5 million rupees, 20 million rupees for reinsurance brokers and 25 million rupees for composite brokers. All insurance brokers are required to be members of the Insurance Brokers Association of India. The IRDAI has recently released an exposure draft of the regulations that proposes to replace the existing regulations governing insurance brokers. However, this draft is yet to be finalised.

IMFs
Entities such as companies, limited liability partnerships or cooperative societies that are registered as IMFs are permitted to distribute insurance products along with mutual funds, pension products and certain other financial products, provided that permissions from the respective regulator are in place to distribute these financial products. IMFs are permitted to distribute the insurance products of only two life insurers, two general insurers and two health insurers at any one time, and a change in the insurer whose products are to be distributed may only take place on the prior approval of the IRDAI. IMFs are required to have a minimum capital of 1 million rupees, and are also permitted to undertake survey functions through licenced surveyors on its rolls, policy servicing activities and other activities that are permissible to be outsourced by insurers under the applicable regulatory framework.

Web aggregators
The IRDAI has recently released regulations that supersede the previous regulations governing web aggregators. An entity such as a company or a limited liability partnership that is registered as a web aggregator is permitted to display on its website information on insurance products of those insurers with whom the web aggregator has entered into an agreement with. The web aggregator is also permitted to display product comparisons on its website, carry out activities for lead generation and share leads with insurers. A web aggregator is required to have a minimum capital of 2.5 million rupees.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

There is no equivalent in India of the UK Third Parties (Rights against Insurers) Act 2010. As a general rule, Indian law recognises the principle of privity of contract, and thus a third party would be unable to bring a direct action against an insurer.

It is common practice, however, for third parties to name the defendant's insurer in motor accident-related proceedings. The Motor Vehicles Act 1988 (MVA) provides that the rights of an insured under a policy are transferred to a third party claiming against the insured in the event of the insured's insolvency. The MVA empowers the Motor Claims Tribunal to seek the insurers' involvement in a third-party action against the insured if the Tribunal believes the claim is collusive or if the insured fails to contest the claim. However, the new Motor Vehicles Act 2017 seeks to limit the insurer's liability with respect to a third-party insurance as follows:
- 1 million rupees in case of death; and
- 500,000 rupees in case of grievous hurt.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Insurance contracts require that the claims or circumstances of the claims are intimated to the insurer within the time period specified in the policy. This requirement may be expressed as a condition or a condition precedent to the insurer's liability under the policy, and the consequences of non-compliance will to some extent depend on whether the notification clause is expressed as a condition or a condition precedent. If a notice clause is a condition, then the insurer will have to show that it suffered prejudice on account of a delayed notice; if such clause is a condition precedent, then, in theory, no prejudice is required to be shown for placing reliance on the clause.

In practice, however, irrespective of whether the notice clause is expressed as a condition or a condition precedent, courts previously have stated that the condition relating to notice should not prevent settlement of genuine claims where there is a delay in intimation or in submission of documents owing to unavoidable circumstances. This is the position that the IRDAI also recommends in its circulars where insurers have been directed not to reject claims unless and until the reasons of delay are specifically ascertained and recorded, and the insurers are satisfied that the delayed claims would have been rejected even if they had been reported in time. Courts and consumer fora have also followed the view that clauses limiting the period for notification of claims are not to be construed strictly, and have often overturned the rejection of claims where the delay was reasonably justifiable.

However, in recent times, the courts and consumer forums have strictly applied this condition. For instance, in 2015 the National Consumer Disputes Redressal Commission held that any delay in the notification of loss to the insurer is fatal to the claim when there was no plausible explanation for the delay (*Saurashtra Chemicals Ltd v National Insurance Co Ltd I* (2015) CPJ351 (NC)). The principle was followed in *Reliance General Insurance Co Ltd v Jai Prakash* (Revision Petition No. 2479 of 2015, decided on 11 January 2016) and *Cosmic Trends Pvt Ltd and Ors Oriental Insurance Company Limited* (Revision Petition No. 447 of 2016, decided on 19 May 2016), whereby the National Consumer Dispute Redressal Commission held that the requirement of immediate intimation of the loss to the insurer is not a mere formality. The

purpose of the intimation is to enable the insurer to verify the alleged loss a time when the evidence is still available and the insurer is entitled to repudiate a claim because of late notification.

Recently, on 15 February 2017, in *Gopinath v UII*, MANU/CF/0092/2017, the court held that the repudiation of claim because of a delay of three months in informing the insurer was justified. But on the same day in J*agjit Singh v Cholamandalam*, MANU/CF/0099/2017, the court considered it sufficient that the 'complainant has been able to provide adequate explanation for the delay in giving intimation' and 'the Insurance Company has not been able to state or prove anywhere, as to what prejudice had been caused to them if intimation reached their office after nine to 10 days of the occurrence'.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Insurance companies in India must have an internal grievance redressal mechanism that addresses complaints raised against them by insured parties. If a policyholder feels that an insurance company has not adequately addressed his or her grievance, he or she may approach the Grievance Cell of the IRDAI or the Insurance Ombudsman (depending on the nature of grievance), or initiate formal legal proceedings against the insurance company before the consumer protection fora. The consumer fora, and the Indian courts in general, often award reasonable sums against insurance companies as compensation for the consequential loss, harassment and legal costs of policyholders in cases where it is deemed that the claim was wrongly denied, especially where the conduct of an insurance company is inferred to be arbitrary or harmful. In *Pinki Devi v NIA*, MANU/CF/0257/2015, the consumer commission imposed punitive damages of 1 million rupees on an insurance company for pursuing a meritless litigation. The damages were recovered from the salaries of the delinquent officials of the insurance company.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

A liability insurer's 'duty to defend' a claim is determined by the terms of the insurance policy. The insurer usually has either a 'right to defend' or a 'duty to defend'. The 'duty to defend' is when a claim made against the insured is to be defended by the insurer, even if it is subsequently found to be not covered. Until such time as a claim is admitted or repudiated, an insurer has to manage the claim defence. On the other hand, if the wording is 'right to defend' then the insurer can opt to defend or associate with the defence.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

Once an insured has established that the claim (usually defined to mean a written demand or civil suit, etc) falls within the insuring clause and the insurer is satisfied that none of the exclusions apply and none of the conditions have been breached, the insurer's obligation to pay would trigger as soon as the insured incurs and satisfies a liability.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

As per the provisions of the Insurance Act, a life insurance policy cannot, on any grounds whatsoever, be called into question by the insurer three years after the date of issuance or commencement of risk, or the date of revival of the policy or the date of the rider to the policy, whichever is later.

28 Punitive damages

Are punitive damages insurable?

There are no judicial precedents in India to suggest that punitive damages are insurable. In the authors' experience, insurance policies typically exclude punitive damages from the scope of insurance cover.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

There is no legislative or regulatory obligation that requires excess insurers to defend and pay a claim if the primary insurer is insolvent or its coverage is unavailable without full exhaustion of the primary limits.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Self-insured retention or deductible are not governed by any statute or regulation as such. The respective obligations of the insurer and the insured with regard to deductible or self-insured retention are usually governed by the wording of the policy or the insurance contract.

The obligation to make payment, if any, to the insolvent insured will be in accordance with the general insolvency or bankruptcy laws. In our view, the insolvency of the insured will not affect the liability of the insurer to pay the insured. If the insurer is to recover the retention amount or deductibles from the insolvent insured then, for the purposes of such recovery, the insurer will be treated as an unsecured creditor whose claim will be settled in accordance with the insolvency laws.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

The terms of the insurance policy entered into between the insurer and the insured usually determine the order of priority for payment when there are multiple claims under the same policy. For example, there are order of payments clauses in some directors' and officers' policies, which specify that the losses would be satisfied in the order in which such loss is presented to the insurer.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

The allocation of payments between the various insurers depends on the allotment of risk set out in the policy. Most policies contain an 'other insurance' clause that sets out that the policy in question would sit in excess of any other existing and valid insurance that has been taken out by the insured in respect of the same insurable interest.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Claims for restitution and disgorgement are usually not covered under insurance policies in India.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

What constitutes an occurrence may differ in scope from one policy to another, but it is usually defined as an accident, including continuous or repeated exposure to substantially the same general harmful conditions.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Under Indian law, an insurance contract is one of the utmost good faith, and insurers are entitled to a fair presentation of any risk prior to inception. If there has been a misrepresentation or non-disclosure of a material fact, an insurer may avoid the policy ab initio. Unless the

misrepresentation or non-disclosure was fraudulent, the premium must be tendered back to the policyholder. However, under the terms of the Insurance Act, in India a life insurance policy cannot be called into question on any grounds whatsoever (including fraud) after the passing of three years from the date issuance or commencement of the risk. Further, an insurer may expressly or impliedly waive his right to rescind. For example, the acceptance of premiums with knowledge of circumstances entitling the insurer to avoid the policy stops him from averring that for that reason it is not a valid policy (*Madhu Ghosh v KK Company* (1999) 2 CALLT 204 (HC)). Sometimes, policies contain wording that takes away the insurer's right to avoid a policy in case of an innocent non-disclosure and only gives the right to exclude the particular claim from the policy cover.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

There have been very few reinsurance disputes in India, and there is therefore very limited Indian case law or judicial guidance with regard to reinsurance disputes. While it is true that as a general trend, parties did prefer business solutions for their disputes, this is now changing and reinsurance disputes are being increasingly referred to arbitration and are pending litigation in various courts in India. Since, in most of the cases, the disputes have not been finally adjudicated on, the case law and precedent on the subject remains limited. However, the general principles of insurance and contract law apply.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Apart from the questions of, inter alia, coverage, and the applicability of exclusions and non-disclosure that arise in any other insurance dispute, an issue that often arises is whether, in an insurer–reinsurer dispute, an insurer is entitled to approach the consumer fora for adjudication of such dispute as the consumer fora will take a lot less time to adjudicate the dispute. A person availing of a service for commercial purposes is excluded from the purview of a 'consumer' under Indian laws; therefore, the question that arises is whether the insurer opts for reinsurance support for the purposes of indemnifying his or her losses, or to provide support for it to insure larger amounts by charging an extra premium (thus making it a commercial purpose). The matter has been decided by the National Consumer Disputes Redressal Forum in its judgment in *Harsolia Motors v National Insurance Co Ltd I* (2005) CPJ 27 (NC), wherein the Commission has clarified the definition of commercial purpose by holding that:

> *[I]t is apparent that even taking wide meaning of the words 'for any commercial purpose' it would mean that goods purchased or services hired should be used in any activity directly intended to generate profit. Profit is the main aim of commercial purpose. But, in a case where goods purchased or services hired in an activity which is not directly intended to generate profit, it would not be commercial purpose.*

The matter has been appealed against and is now pending adjudication in the Supreme Court of India. It is pertinent to mention that the judgment in Harsolia Motors was with respect to a dispute between a commercial entity and an insurer. However, disputes between insurer and reinsurer have also been admitted in the past by National Consumer Disputes Redressal Commission, but clarity will be obtained only when the case of Harsolia Motors is finally adjudicated by the Supreme Court of India.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Section 31(3) of the Arbitration Act states that an arbitral award shall contain the reasons for the same unless the parties have expressly agreed otherwise or in cases where a consent award (as per section 30 of the Arbitration Act) has been passed. It is rare to find agreements where the parties have dispensed with the obligation of an arbitral tribunal to provide reasons in its award.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

It was a settled position of law in India that arbitration is a creature of an agreement between the parties; as such, an arbitral tribunal does not have any jurisdiction to either implead or pass an award against a person who is not a party to the said arbitration agreement, as enunciated in the case of *Sukanya Holdings Pvt Ltd v Jayesh H Pandya and Ors*, 2003 (5) SCC 531. However, this was changed by way of a three-judge bench judgment of the Supreme Court in the case *Chloro Controls (I) Pvt Ltd v Severn Trent Water Purification Inc & Ors* 2013 (1) SCC 641, whereby it had been held that a reference is permissible if the agreements are 'intrinsically interlinked' and the ancillary agreements serve no purpose except in connection with the principal agreement which contains the arbitration clause. In other words, a composite transaction can be referred to arbitration even if some of the parties named as respondents are not parties to the arbitration clause. It was further held that:

> *Maybe all the parties to the lis are not signatory to all the agreements in question, but still they would be covered under the expression 'claiming through or under' the parties to the agreement. The interests of these companies are not adverse to the interest of the principal company and/or the joint venture company. On the contrary, they derive their basic interest and enforceability from the Mother Agreement and performance of all the other agreements by respective parties had to fall in line with the contents of the Principal Agreement. In view of the settled position of law that we have indicated above, we will have no hesitation in holding that these companies claim their interest and invoke the terms of the agreement or defend the action in the capacity of a 'party claiming through or under' the parties to the agreement.*

The judgment in *Chloro Controls* was, however, limited to Foreign Arbitrations alone and did not extend to domestic arbitrations.

Notably, in recent times arbitration law in India has been amended. Section 8 of the Arbitration Act, which deals with reference of parties to domestic arbitration, has been specifically amended to include the words 'through or under him'. Although the provision has not been examined by the courts in India, the legislative intent seems to be in favour of letting the non-parties to the arbitration agreement be joined as parties in arbitration agreements with the inclusion of the words 'claiming through or under him'. Subject to the view that the courts take of the amended provision, this may ultimately result in reinsurance arbitrators joining non-signatories to arbitration provided the non-signatories are claiming through or under the parties to the arbitration.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Section 34 of the Arbitration Act gives a party to arbitration proceedings a right to approach a court for the setting aside of the award. However, setting aside is only permitted if the person so challenging the award has proved that one of the grounds laid down in section 34 has been satisfied. The court has limited scope while entertaining a petition under section 34 and, unlike an appellate court, it cannot examine the merits of the award (in other words, the court is not free to interfere with the award merely because it feels, following a review of all the materials, that it would have arrived at a different conclusion); its scope of interference is limited to the grounds laid out in section 34, which include incapacity of a party to enter into arbitration, improper notice of arbitration, ultra vires jurisdiction, invalid composition of the arbitral tribunal, a conflict with the public policy of India

Update and trends

There has been tremendous growth and development in the Indian insurance sector in recent years. By dispensing with the requirement of seeking an approval from the Indian government for increasing the foreign investment cap from 26 per cent to 49 per cent in insurance entities, there has been an increase in the quantum of economic investments by existing Indian players along with foreign players exploring the options of setting up insurance joint ventures in India. It is relevant to note that the IRDAI has registered six foreign reinsurer branches and has also permitted Lloyd's India to set up a marketplace in India. Further, with the order of preference for cession being brought into effect, Indian insurers are in the process of revising their reinsurance programmes and filing the same with the IRDAI within the prescribed timelines.

There have been a series of regulatory developments, which are as follows:

- insurers are now permitted to issue products under the 'use and file' process, which has triggered an increase in product development in India;
- the IRDAI has issued regulations that stipulate the limits on the commission or remuneration payable to insurance agents and intermediaries for soliciting and procuring insurance business and has also introduced the payment of 'rewards' to such persons. Consequently, insurers and insurance agents or intermediaries are in the process of revising their existing arrangements in view of the flexibility in the amount of commission or remuneration (including rewards) payable;
- the IRDAI has recognised issuance of e-insurance policies. It has also recently issued E-Commerce Guidelines, which provide the norms for establishing an online portal for the sale and servicing of insurance policies;
- the IRDAI has released a stewardship code, which prescribes the principles to be followed by insurers in relation to their investee companies. The IRDAI has also notified regulations governing outsourcing of functions by an insurer to third-party service providers; and
- the IRDAI has also issued guidelines on information and cyber security for insurers that pertain to protection of security and integrity of insurer's data.

It is pertinent to note that these significant yet frequent changes in the regulatory framework have led to a state of flux in the insurance industry. The Indian insurance sector is currently tackling the implementation of these regulatory developments, which are expected to continue for a few more years. Consequently, players in the Indian insurance sector will be required to incorporate systems, processes and resources to keep up with such regulatory developments.

and patent illegality appearing on the face of the award. Also, by way of the amendment to the Arbitration Act, the scope of 'public policy' has been narrowed down to include only those instances where (i) the making of the award is fraudulent or corrupt or (ii) the award is in contravention of the fundamental policy of Indian law and (iii) the award is in conflict with the most basic notions of morality or justice.

In cases where the parties are still unsatisfied, the affected party can file an appeal under section 37 of the Arbitration Act, where the lower court has set aside or refused to set aside an arbitral award under section 34.

The courts place substantial value on a proper arbitral award because the parties themselves have decided on the forum and the members of the tribunal. Therefore, courts will normally refrain from interfering or setting aside an arbitral award unless one of the grounds under section 34 of the Arbitration Act has been satisfied.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The terms of the reinsurance contract usually govern the rights, obligations and processes of the insurer and the reinsurer in respect of the monitoring of claims and settlements. Claims control and claims cooperation clauses are included in reinsurance contracts, and the contracts will also occasionally contain 'follow-the-settlement' clauses that require the reinsurer to follow any settlement reached by the insurer with the insured. The effect of follow-the-fortunes wording is usually that reinsurers must pay for honest settlements that fall within the four corners of the reinsurance if such settlements have been reached by the cedant in a proper and business-like manner. 'Settlement' includes judgments, awards and reasonable settlements of liability and quantum. Good faith payments by a cedant that are made without admission of liability or on a without prejudice basis, or under a full reservation of rights will not fall within follow-the-fortunes wording and will relieve the reinsurer of his or her liability to indemnify. The intention of the follow-the-fortunes wording is therefore that the cedant, not the reinsurer, undertakes claims adjustment and settlement. If reinsurer wishes to involve themselves in the process then they should insert a proper claims control clause or stronger claims cooperation clause, and in either event remove the follow-the-fortunes wording.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Under Indian law, an insurance contract is a contract of the utmost good faith, and insurers are entitled to a fair presentation of the risk prior to inception. If there has been a misrepresentation or non-disclosure of a material fact, then an insurer may avoid the policy ab initio. Unless the misrepresentation or non-disclosure was fraudulent, the premium must be tendered back to the policyholder. The duty to disclose material facts is not confined to those facts that are in the knowledge of the insured, but also extends to those facts that the insured should have known as a prudent person. Indian courts have interpreted the expression 'utmost good faith' in insurance law to constitute an obligation to deal 'fairly' and 'honestly' which is almost identical to the definition of 'good faith' under the Indian General Clauses Act No. 10 of 1897.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There are no separate laws for facultative reinsurance and treaty reinsurance. The General Reinsurance Regulations and the Life Reinsurance Regulations regulate both these types of reinsurance in India. In addition, as mentioned above, R28(9) of the Branch Office Regulations prescribes the order of preference for cessions by Indian insurers for their facultative and treaty surpluses and does not make a distinction between the two categories.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

A third party cannot bring a direct action against the reinsurer for coverage because there is no privity of contract between the original policyholder and the reinsurer.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

There are no legislative or statutory obligations on the reinsurer to pay a policyholder's claim when the insurer is insolvent.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The type of notice that a cedant must provide and within what time period would be governed by the reinsurance policy wording. For example, notice may be required immediately, or when the insured expects the claim to exceed 50 per cent of the deductible, etc. This requirement may be expressed as a condition or a condition precedent to the insurer's liability under the policy, and the consequences of non-compliance will to some extent depend on whether the notification clause is expressed as a condition or a condition precedent. If the notice clause is a condition, the insurer will have to show that it suffered prejudice on account of the delayed notice. However, if the clause is a condition precedent, then in theory no prejudice is required to be shown for placing reliance on the clause. We also note that IRDAI's notification dated 18 August 2015 specifies that:

> *In respect of classes with 'No Limit' on cessions marked by an asterisk above [Motor, Workmen's compensation, General Aviation hull/Liability and Other Miscellaneous], the 'Indian Reinsurer' may require the ceding insurer to give immediate notice with underwriting information of any cession to it exceeding an amount per risk specified by it. Cessions in excess of such limits will be binding subject to the notice and information been given.*

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

There is no statutory guidance in relation to the mode of settlement of such claims, and this usually depends on the treaty or contractual arrangements between the insurers and the reinsurers, and on the conditions specified in the treaty. Regarding facultative reinsurance, the reinsurer has the discretion to accept or reject claims. However, in treaty reinsurances, the liability of reinsurers to settle claims arises from the conditions mentioned in the treaty.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

The existing legislation does not provide for a general right of review of the cedent's claims handling, or settlement and allocation decisions; however, there is nothing to stop the reinsurer and the insurance company from contractually agreeing to set up a review and audit mechanism.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Commutation payment terms are set out in reinsurance contracts, and there is no regulatory or legislative direction in this regard.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

There are no regulations dealing with obligations on reinsurers to reimburse a cedent for ECOs. The same will be governed by the terms of the reinsurance treaties entered into by the reinsurer and cedent. In practice, several reinsurance treaties specifically relieve reinsurers from the obligation to reimburse cedents for ECOs.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Since 1 January 2013, the Financial Services Authority (OJK) has been assigned as the supervisor and regulator for all banks and non-bank financial institutions, including insurance and reinsurance companies in Indonesia from the previous agency, the Capital Markets and Financial Institutions Supervisory Board (Bapepam-LK) of the MOF. Such authority was given under Law No. 21 of 2011 regarding Financial Services Authority. Insurance and reinsurance sector under the organisation structure of the OJK was under the Head Executive Supervisor of Non-Bank Financial Institutions. The OJK is also responsible for issuing insurance business licences for insurance companies, reinsurance companies and other insurance business companies.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Under Law No. 40 of 2014 regarding Insurance (Insurance Law), to obtain a business licence for conducting insurance and reinsurance businesses in Indonesia, the entity must be established either as a limited liability company (PT), cooperative or mutual fund. Especially for mutual funds, the OJK's current position is that it will not issue new licences for mutual fund insurance companies. There is only one licensed life insurer in the form of a mutual fund that was established in 1912. Almost all insurance companies and reinsurance companies in Indonesia are established as PTs.

The owner of insurance or reinsurance companies shall be either: (i) wholly owned by Indonesian citizens or Indonesian legal entities that are directly or indirectly wholly owned by Indonesian citizens (local insurance or reinsurance companies); or (ii) jointly owned by foreign citizens or foreign legal entities and Indonesian citizens or Indonesian legal entities that are directly or indirectly wholly owned by Indonesian citizens (joint venture insurance or reinsurance companies).

Insurance business under Insurance Law covers the following types:

- general insurance (conventional or shariah);
- life insurance (conventional or shariah);
- reinsurance (conventional or shariah);
- insurance brokers;
- reinsurance brokers;
- agents (individuals or companies); and
- insurance loss adjustors.

Once a PT is established, it can apply for insurance business licence from the OJK. Insurance Law does not stipulate a composite licence. Further, PT cannot engage in more than one type of insurance business except for PT, which engages in general insurance business and can also provide reinsurance service.

OJK Regulation No. 67/POJK.05/2016 regarding Business Licensing and Institution of Insurance, Shariah Insurance, Reinsurance and Shariah Reinsurance Companies (POJK 67/2016) regulates procedures and application requirements as follows:

- a copy of the company's articles of association that has been approved by the Minister of Law and Human Rights;
- the organisational structure of the company, complete with job description and work procedure;
- a copy of evidence of paid-up capital in the form of a cash deposit, or a minimum paid-up capital in the form of time deposit or clearing account in a licensed Indonesian bank and legalised by the receiving bank and still valid when applying the insurance business licence;
- the initial report of guarantee fund and evidence of guarantee fund placement (ie, minimum 20 per cent of minimum paid-up capital required);
- the list of share ownership;
- the list of shareholders aside from the controlling shareholder;
- the list of controller including the description on its form of control;
- evidence of hiring experts;
- the business plan for the first three years;
- a copy of the company's risk management guidelines;
- insurance product specification and description;
- a copy of agreement with other parties and the function outsourcing policy guidelines for operation;
- administration and infrastructure data management system;
- confirmation from supervisory authority in the country of origin of the foreign entity (if there is a direct foreign investment);
- evidence of licence application fee payment; and
- other supporting documents as evidence of the growth of a healthy business.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

POJK 67/2016 stipulates that an insurance or reinsurance company in Indonesia must be a member of an association in accordance with its type of business, for example, the association for life insurance business is Indonesian Life Insurance Association, the association for general insurance business is Indonesian General Insurance Association, the association for insurance and reinsurance broker business is the Indonesian Insurance and Reinsurance Broker Companies Association, the association for actuary business is the Indonesian Actuary Consultant Association, etc.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

OJK Regulation No. 73/POJK.05/2016 regarding Good Corporate Governance for Insurance Companies (POJK 73/2016) sets forth good corporate governance guidelines for insurance and reinsurance companies in Indonesia. POJK 73/2016 requires an insurance company and a reinsurance company to have a minimum of three directors and three commissioners. At least half of the members of the board of directors must have knowledge and experience in the field of risk management in accordance with the type of insurance business. Further, at least

half of the members of the board of commissioners shall constitute independent commissioners.

Prior to holding the positions, directors and commissioners shall pass the fit and proper test held by the OJK. The fit and proper test procedures are regulated under OJK Regulation No. 27/POJK.03/2016 regarding the Fit and Proper Test for Primary Parties of Financial Services Institutions (POJK 27/2016) and OJK Circular Letter No. 31/SEOJK.05/2016 regarding the Fit and Proper Test for Primary Parties of Non-Bank Financial Services Institutions (SEOJK 31/2016). SEOJK 31/2016 provides that parties that pass the fit and proper test are known as 'primary parties'. Primary parties consist of the controlling shareholder, members of the board of directors, members of the board of commissioners, members of the shariah supervisory board, internal auditor and actuary.

Under POJK 73/2016, an insurance company and a reinsurance company are prohibited from appointing directors and commissioners who are found guilty or negligent, in which case:

- the insurance company and the reinsurance company are subject to restrictions on business activities sanctioned within three years prior to his or her appointment;
- a business licence of a company in the field of financial services is revoked owing to his or her conduct violation within three years prior to his or her appointment; and
- a company in the field of financial services or non-financial services is declared bankrupt by court decision that has permanent legal force within five years prior to his or her appointment.

Aside from the aforementioned, Law No. 40 of 2007 regarding Limited Liability Companies stipulates the general requirements for appointing directors or commissioners.

Pursuant to POJK 67/2016, an insurance company or a reinsurance company must also appoint at least one certified expert in accordance with the type of insurance business, one certified actuary as an appointed actuary of the company and an internal auditor who directly reports to the president director or other equal position. An internal auditor and actuary shall pass the fit and proper test held by the OJK. Further, the insurance company or the reinsurance company shall report to the OJK on the appointment or dismissal of the expert, actuary and internal auditor.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Under POJK 67/2016, minimum paid-up capital requirements apply for insurance and reinsurance companies prior to conducting its business activities (ie, at the time of establishment) as follows:

- for insurance companies, the minimum paid-up capital is 150 billion rupiah;
- for reinsurance companies, the minimum paid-up capital is 300 billion rupiah;
- for shariah insurance companies, the minimum paid-up capital is 100 billion rupiah; and
- for shariah reinsurance companies, the minimum paid-up capital is 175 billion rupiah.

These new capital requirements do not apply to the existing insurance and reinsurance companies unless such companies conduct corporate actions that cause the change of their share composition.

POJK 67/2016 also requires insurance or reinsurance companies to have a guarantee fund of at least 20 per cent from the minimum paid-up capital required above that can only be placed in the form of a time deposit with an automatic renewal in a licensed Indonesian bank that is not affiliated with the insurance or reinsurance companies. The obligation to have the guarantee fund will discontinue once the mandatory guarantee programme is established. This matter will be regulated under a separate regulation that will be issued within three years after the enactment of the Insurance Law. However, at the time of writing, such mandatory regulation on the guarantee programme is not yet being issued or established.

Aside from the aforementioned, OJK Regulation No. 71/POJK.05/2016 regarding Financial Soundness for Insurance Companies and Reinsurance Companies (POJK 71/2016) requires insurance companies and reinsurance companies to meet minimum solvency margins. Under POJK 71/2016, the minimum solvency margin ratio is 100 per cent of risk-based minimum capital (RMC). The said companies shall annually establish their solvency target at a minimum of 120 per cent of RMC. If the companies do not meet 120 per cent solvency target, they must submit a financial restructuring plan to the OJK and are prohibited from distributing dividends or providing any kind of compensation to their shareholders. The OJK can instruct the said companies to transfer their insurance portfolios to another company if they cannot meet 100 per cent solvency margin ratio. The OJK can also revoke the companies' business licence if the solvency margin ratio is less than 40 per cent and based on the OJK view that such a condition is considered harmful to policyholders or insureds.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Pursuant to POJK 71/2016, technical reserve are one of the instruments used to measure financial soundness. The companies (through their actuaries) shall establish technical reserves in accordance with types of insurance products. Technical reserves cover the following:

- premium reserves for non-renewable or renewable insurance products with a maturity period of more than one year;
- premium reserves that are not yet acknowledged as income for insurance products with a maturity period of one year or more in which the terms and conditions of the policies can be renewed in each policy anniversary;
- reserves for insurance products that are combined with investments (PAYDI); and
- claim reserves.

If the OJK identifies companies with incorrect technical reserves or parts of technical reserves, the OJK may request the companies to:

- revaluate the technical reserves or the part of the technical reserves that are considered improper; or
- review the technical reserves or the part of the technical reserves by an independent party at the companies' cost.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

OJK Regulation No. 23/POJK.05/2015 regarding Insurance Products and Marketing of Insurance Products (POJK 23/2015) stipulates the types of insurance products as follows:

- standard insurance products: general insurance products or life insurance products that are the same as standard general insurance products or standard life insurance products issued by the relevant associations;
- PAYDI: insurance products that at least cover death risk and provide benefits based on investment results from funds collected particularly for insurance products;
- joint insurance products: insurance products whose risks are designed to be marketed and covered or managed by two or more insurance companies; and
- micro insurance products: insurance products that are designed to provide coverage for financial risks faced by low-income citizens or individuals.

POJK 23/2015 also divides applications for insurance products into two categories: (i) insurance products that shall be reported to the OJK for approval (related to PAYDI, joint insurance products and micro insurance products); and (ii) insurance products that shall be reported to the OJK for registration (related to standard insurance products) prior to insurance products that are offered for sale to customers.

The applications for approval or registration of insurance products must be accompanied by the following documents:

- the application form;
- the premium revenue projection and costs assigned for three years' marketing of insurance products (for approval only);
- the details of insurance products;

- a specimen of the insurance policy;
- the statement letter from the shariah supervisory board (only for shariah insurance products); and
- the copy of the cooperation agreement (only for joint insurance products).

Insurance companies can only market insurance products through marketing channels as follows:
(i) direct marketing;
(ii) an insurance agent;
(iii) bancassurance; or
(iv) a business entity other than a bank.

Further, insurance companies that market insurance products through marketing channels as referred to in points (ii) to (iv) shall have a written agreement with the party that conducts the marketing. For marketing through point (iii) or point (iv), the insurance companies shall obtain prior approval from the OJK.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Examinations are carried out by the OJK as the supervisory authority for the insurance sector in Indonesia. The OJK can conduct periodical examinations or whenever they view an examination is needed. Procedures of examinations are stipulated in OJK Regulation No. 11/POJK.05/2014 regarding Direct Examination of Non-Bank Financial Institutions as amended by OJK Regulation No. 63 /POJK.05/2016 (together, POJK 11/2014). Under POJK 11/2014, the frequency of periodical direct examination will be determined by the OJK in accordance with a risk-based supervision plan. The OJK can also conduct examinations at any time to insurance and reinsurance companies as well as their shareholders, subsidiaries or parties that conduct transactions with them if there are indications that pose risks to insurance and reinsurance companies or violate prevailing laws and regulations.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

POJK 71/2016 stipulates limitation of investment by insurance and reinsurance companies of the following financial instruments:
- time deposits at banks, including deposits on call and time deposits with a period of less than or equal to one month and for each bank up to 20 per cent of the total investment;
- time deposits, for each rural bank and rural Sharia bank up to 1 per cent of the total investment and up to 5 per cent of the total investment in aggregate;
- certificate of deposit for each bank up to 50 per cent of the total investment in the form of time deposits of banks as referred to in letter a above;
- shares listed on the stock exchange, for each issuer up to 10 per cent of the total investment and up to 40 per cent of the total investment in aggregate;
- corporate bonds listed on the stock exchange, for each issuer up to 20 per cent of the total investment and up to 50 per cent of the total investment in aggregate;
- medium term note and commercial papers issued by multinational institutions in which Indonesia becomes one of its members or shareholders, for each issuer up to 20 per cent of the total investment and up to 40 per cent of the total investment in aggregate;
- commercial papers issued by a country other than Indonesia, for each issuer up to 10 per cent of the total investment;
- mutual funds, for each investment manager up to 20 per cent of the total investment and up to 50 per cent of the total investment in aggregate;
- asset-backed securities, for each investment manager up to 20 per cent of the total investment and up to 50 per cent of the total investment in aggregate;
- real estate investment fund in the form of collective investment contract, for each investment manager up to 10 per cent of the total investment and up to 20 per cent of the total investment in aggregate;
- securities transactions through repurchase agreement, for each counterparty up to 2 per cent of the total investment and up to 10 per cent of the total investment in aggregate;
- direct investment in a limited liability company whose shares are not listed on the stock exchange, up to 10 per cent of the total investment in aggregate;
- land, building with strata title, or land with buildings for investment, up to 20 per cent of the total investment in aggregate;
- land for investment, up to one-third of the total investment in aggregate as mentioned in above point;
- financing through mechanisms of cooperation with other parties in the form of credit cooperation (executing), for each party up to 10 per cent of the total investment and up to 20 per cent of the total investment in aggregate;
- pure gold, up to 10 per cent of the total investment in aggregate;
- loans secured by security rights, up to 10 per cent of the total investment in aggregate; and
- policy loan, with the amount of policy loan up to 80 per cent of the relevant policy cash value.

Investment in affiliates of the insurance or reinsurance company is only permitted for maximum of up to 25 per cent of the total investment. If the insurance or reinsurance company wishes to invest more than 25 per cent, it must obtain OJK approval.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Any change of share ownership in an insurance company or a reinsurance company (by way of acquisition, merger or consolidation), whether there is a change of control or not, requires the OJK's prior approval.

If, as the result of the change of share ownership, there is a change of control, based on POJK 67/2016, the OJK will conduct a fit and proper test for the candidate controller. The party that can be categorised as controller, in accordance with POJK 67/2016, is as follows:
- shareholder; or
- non-shareholder.

The controller, as a shareholder of the insurance company or the reinsurance company or 'controlling shareholder', is a party that directly owned 25 per cent or more of the total issued shares and has voting rights or has directly owned less than 25 per cent of total issued shares and has voting rights but the party can be proven to have conducted control of the company, either directly or indirectly. The controller, as a non-shareholder of the insurance company or the reinsurance company, is a party that indirectly has the power to decide or influence actions of the board of directors or the board of commissioners.

In addition, the controller (shareholder) must comply with integrity requirement criteria and financial feasibility pursuant to the OJK's fit and proper test regulations. Further, a controller (non-shareholder) must comply with integrity requirement criteria and financial reputation pursuant to the OJK's fit and proper test regulations. Aside from the fit and proper test for the candidate controller, if the change of control results in appointing new candidate members of the board of directors and the board of commissioners, each member of the board of directors and the board of commissioners shall pass the fit and proper test held by the OJK.

POJK 67/2016 also requires any change of controller of the insurance company or the reinsurance company must be reported to the OJK along with the registry of shareholders, the details of each share ownership amount and the entire structure of the business group related to the insurance or reinsurance company and the legal entity that owns the insurance or reinsurance company up to the last owner, accompanied by supporting documents.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements or restrictions concerning financing.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

The same rules on change of ownership in an insurance or a reinsurance company (ie, obtain the OJK's prior approval) will apply if an investor acquires a minority interest in the company.

Further, according to Law No. 8 of 1995 regarding Capital Markets (Capital Markets Law), if the insurance or the reinsurance company is a public company, a shareholder that owns 5 per cent or more of the shares of the public company shall report on the status of their shareholding to the OJK and the Indonesian Stock Exchange within 10 days of the transaction.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

Insurance Law permits direct investment by foreign citizens or foreign legal entities in an insurance company or a reinsurance company through a joint venture with Indonesian citizens or Indonesian legal entities that are directly or indirectly wholly owned by Indonesian citizens. Foreign citizens may become owners of the insurance company or the reinsurance company only through transactions on the Indonesian Stock Exchange. However, a foreign legal entity may become an owner of the insurance company or the reinsurance company if the foreign legal entity: (i) has a similar insurance business; or (ii) is a holding company in which one of its subsidiaries is engaged in similar insurance business.

POJK 67/2016 further stipulates that foreign shareholders (in the form of legal entities) in the insurance company or the reinsurance company shall meet the following requirements: (i) have a minimum rating of A, or equal, from an internationally recognised rating agency (if the foreign shareholder is a holding company, its subsidiary must meet the aforesaid rating requirement); and (ii) submit a cooperation agreement between foreign shareholders and Indonesian shareholders to the OJK.

According to Government Regulation No. 73 of 1992 regarding Insurance Business Conduct as amended several times, most recently with Government Regulation No. 81 of 2008 (together, GR 73/1992) and Presidential Regulation No. 44 of 2016 regarding List of Business Field Closed and Opened with Requirements in Investment, insurance and reinsurance companies in Indonesia can be opened with a maximum of 80 per cent of foreign direct investment at the time of establishment.

The 80 per cent limit may be exceeded following new capital injection by foreign shareholders provided that the total paid-up capital of the Indonesian shareholders is maintained. The new capital injection is subject to the OJK's prior approval. The foreign ownership limitation will be further regulated in a new Government Regulation (see 'Update and trends').

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The OJK issued a set of regulations to supervise financial conglomerate in Indonesia. The regulations are:

- OJK Regulation No. 17/POJK.03/2014 regarding Implementation of Integrated Risk Management for Financial Conglomerates (POJK 17/2014);
- OJK Regulation No. 18/POJK.03/2014 regarding Implementation of Integrated Governance for Financial Conglomerates (POJK 18/2014);
- OJK Regulation No. 26/POJK.03/2015 regarding Integrated Minimum Capital Requirements for Financial Conglomerates (POJK 26/2015);
- OJK Circular Letter No. 14/SEOJK.03/2015 regarding Implementation of Integrated Risk Management for Financial Conglomerates; and
- OJK Circular Letter No. 15/SEOJK.03/2015 regarding Implementation of Integrated Governance for Financial Conglomerates.

Under POJK 17/2014 and POJK 18/2014, a financial conglomerate must identify the main entity and subsidiary companies (eg, if the financial conglomerate structure consists of the controlling shareholder and subsidiaries of the controlling shareholder, the controlling shareholder of the financial conglomerate must appoint a main entity). The main entity must be a financial services institution (FSI) with the largest total assets or the best risk management implementation quality.

Under POJK 17/2014, risks to be covered under integrated risk management consist of credit risks, market risks, liquidity risks, operational risks, legal risks, reputational risks, strategic risks, compliance risks, inter-group transaction risks and insurance risks (applicable only for insurance companies). The integrated risk management process must at least cover:

- supervision by management of the principal unit;
- adequate integrated restrictions, procedures and risk policies;
- adequate identification processes, monitoring mechanisms, measurements and IT systems to manage integrated risks; and
- a complete risk management internal control system.

Further, POJK 17/2014 requires the main entity to report to the OJK on the following matters:

- the financial conglomerate's structure regarding: (i) the appointment of the main entity and all FSIs members of the financial conglomerate; (ii) any new financial conglomerate and the appointment of the main entity; (iii) change of the main entity; (iv) change of the financial conglomerate members; and (v) dissolution of the financial conglomerate. Reports must be submitted no later than 20 working days since the event occurs. The first report on the appointment of the main entity and the list of the financial conglomerate members was due on 31 March 2015; and
- the periodical integrated risk profile report. This report is prepared every semester for the period ending in June and December and shall be submitted by the 15th day of the second month after a period ends. The first report was due by December 2015 for non-bank FSIs (ie, insurance and reinsurance companies).

Under POJK 18/2014, the main entity is obliged to implement integrated governance. Integrated governance must include:

- requirements for the board of directors and the board of commissioners of the main entity;
- the board of directors and the board of commissioners' specific duties and responsibilities;
- preparation and implementation of integrated guidance on governance;
- establishment of integrated compliance work unit and its specific duties and responsibilities;
- establishment of integrated internal audit work unit and its specific duties and responsibilities; and
- implementation of integrated risk management policies.

Further, POJK 18/2014 requires the main entity to report to the OJK on the following matters:

- the financial conglomerate's structure regarding: (i) the appointment of the main entity and all FSIs members of the financial conglomerate; (ii) any new financial conglomerate and the appointment of the main entity; (iii) change of the main entity; (iv) change of the financial conglomerate members; and (v) dissolution of the financial conglomerate. Reports to be submitted no later than 20 working days since the event occurs. The first report on the appointment of the main entity and the list of the financial conglomerate members was due on 31 March 2015; and

- the periodical integrated governance implementation report. This report is prepared every semester for the period ending in June and in December and shall be submitted by 15th day of the second month after a period ends. The first report was due by December 2015 for non-bank FSIs (ie, insurance and reinsurance companies).

POJK 26/2015 sets out the capital requirement for the financial conglomerate. The financial conglomerate shall provide an integrated minimum capital of at least 100 per cent of the aggregate regulatory capital requirement of the financial conglomerate. The OJK has the authority to determine the integrated minimum capital greater than the minimum capital as mentioned above, if the OJK determines that the financial conglomerate is facing risks that require greater capital adequacy. The main entity is obliged to submit an adequacy report of integrated capital every semester for the period ending in June and in December and shall be submitted by 15th day of the second month after a period ends. The first report was due by February 2016.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Pursuant to OJK Regulation No. 69/POJK.05/2016 regarding Business Conduct for Insurance, Shariah Insurance, Reinsurance and Shariah Reinsurance Companies (POJK 69/2016), an insurance company shall have reinsurance support in form of a reinsurance agreement. Such reinsurance agreement shall be made in writing and does not contain an agreement that promises profit for the reinsurance company. The reinsurance agreement shall contain a statement that in the event the insurance company is liquidated, rights and obligations of the insurance company that arise from a reinsurance transaction will remain binding until one of or both of the companies are liquidated.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Under OJK Regulation No. 14/POJK.05/2015 regarding Own Retention and Domestic Reinsurance Support (POJK 14/2015), insurance companies must obtain reinsurance support by first prioritising local reinsurer. For the type of coverage of simple risk, insurance companies must obtain 100 per cent reinsurance support from a local reinsurer. However, exemptions are available only for the following products:

- global insurance products whose coverage is worldwide;
- insurance products designed specifically for multinational companies; and
- new insurance products whose product development is supported by foreign reinsurers for a maximum of four years since the insurance product is reported to the OJK.

Insurance companies must obtain automatic reinsurance support for each of the marketed insurance products. If general insurance companies established reserves for catastrophic risks, then general insurance companies are exempted to obtain automatic reinsurance support for catastrophic risks. The insurance companies must obtain facultative reinsurance support in the event that automatic reinsurance support is insufficient for risks received by insurance companies and in the event that:

- no reinsurer that can provide automatic reinsurance support because of a special risk characteristic;
- insurance companies start to market new insurance lines of business;
- insurance companies market insurance products in order to fulfill requests of certain policyholders; and
- managed risks do not exceed capacity of own retention.

The insurance companies are required to report the reinsurance/retrocession programme to the OJK every year by 15 January. The insurance companies are also required to report the implementation of reinsurance placement to the OJK every year by 30 April.

The requirements regarding the amount of ceded reinsurance and own retention are further set forth in OJK Circular Letter No. 31/SEOJK.05/2015 regarding Own Retention Limit, Reinsurance Support and Reinsurance Programme Report (SEOJK 31/2015). Insurance companies must determine their own retention for each line of business. The OJK sets a maximum limit for own retention at 10 per cent of its own capital for every risk.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no collateral requirements for reinsurers.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Pursuant to POJK 71/2016, separation of asset and liability shall be disclosed in the financial statements of insurance companies. Insurance companies must hold a permitted asset in insurance fund with at least the same amount as the insurance fund liability. Insurance fund liability consists of a technical reserve, co-insurance debt, reinsurance debt and other liabilities towards policyholders or insureds. Reinsurance is categorised as a permitted asset non-investment in the financial statement of insurance companies. However, there are no specific regulatory requirements regarding credit for reinsurance.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Insolvent or financially troubled insurance and reinsurance companies are governed by the Insurance Law and OJK Regulation No. 28/POJK.05/2015 regarding Dissolution, Liquidation and Bankruptcy of Insurance, Shariah Insurance, Reinsurance and Shariah Reinsurance Companies (POJK 28/2015).

If an insurance company and a reinsurance company is financially troubled, the OJK may appoint a statutory manager to take over the authority and function of the board of directors and the board of commissioners. Duties and responsibilities of the statutory manager are as follows:

- to rescue the assets of the company;
- to control and manage the business activity of the company in accordance with laws and regulations;
- to prepare a work plan that contains the recovery measures;
- to submit a proposal to the OJK to revoke the business licence of the company in the event that the company is considered non-rescuable;
- to comply with every written instruction from the OJK concerning the control and management of the business activies of the company;
- to prevent and reduce consumers' loss; and
- to report its activities to the OJK.

Under the Insurance Law, a bankruptcy petition (or suspension of debt payment submission) for insurance and reinsurance companies can only be filed by the OJK. POJK 28/2015 stipulates that creditors may file a bankruptcy petition request against insurance and reinsurance companies to the OJK so that the OJK can file a bankruptcy petition against the said companies to a commercial court. The OJK will assess the request and will determine to approve or reject such request. For customers' interests, the OJK may file a bankruptcy petition without the creditors' request.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Under the Insurance Law, in the event that an insurance company or reinsurance company is declared bankrupt or liquidated, rights of policyholders, insureds or participants will be prioritised over distribution of assets of the company.

On the other hand, according to Law No. 13 of 2003 regarding Manpower (Manpower Law) and Constitutional Court Decision No. 67/PUU-XI/2013, dated 11 September 2014, salaries of employees of an insurance company will be prioritised against payment to secured creditors. Another regulation that should be taken into account is Law No. 16 of 2000 regarding General Provision and Taxation Procedure as amended by Law No. 16 of 2009, which stipulates that the curator shall be prohibited from dividing the assets of the taxpayer in bankruptcy to the other creditors prior to settling their tax debt.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Intermediaries under the Insurance Law consists of insurance brokers, reinsurance brokers, insurance loss adjuster companies, agents, underwriters and third-party administrators.

OJK Regulation No. 68/POJK.05/2016 regarding Business Licensing and Institution of Insurance Broker, Reinsurance Broker and Insurance Loss Adjuster Companies (POJK 68/2016) governs the licensing requirement for brokers and insurance loss adjuster companies. Brokers and insurance loss adjuster companies must obtain a business licence from the OJK prior to conducting their business by submitting business licence applications.

Under POJK 67/2016, the OJK delegates registration of insurance agents to insurance associations. Agents shall be registered in the OJK and shall obtain an agency certificate from the Profession Certification Institution in the field of insurance (particularly for agents). To date, the said Institution has not yet been established. The agency certificate is currently issued by insurance associations. Insurance companies that employ insurance agents must also register with the OJK.

POJK 67/2016 stipulates that insurance experts (underwriters) shall comply with the following requirements:

- expert certification of the highest level;
- field of risk management for at least three years; and
- have not been discharged.

The report of appointment of insurance experts shall be submitted by insurance and reinsurance companies to the OJK.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

In theory, third parties generally cannot bring direct actions against insurers unless the insurance policy (eg, banker's clause) or laws and regulations permit third parties to perform such action.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

No such regulation permitting an insurer to deny coverage based on a late notice of claim exists. In practice, the time limit for the insured to file a claim is set out in the insurance policy. The insured's claim may be rejected if the insured submits the claim after the time specified in the insurance policy.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

The insurer is subject to extra-contractual exposure based on the following provisions:

- POJK 23/2015 prohibits an insurer from including any provision in insurance policy that restricts the insured's rights to pursue legal action and that states that the insured must accept the denial of the claim payment. If an insurer conducts a wrongful denial of a claim, the insured may file a claim in tort to the extent the denial of the claim is considered as an unlawful act.
- the Insurance Law and POJK 69/2016 expressly stipulate that insurers are prohibited from taking action that may delay the payment of claim. In case of violation of this provision, the OJK may give administer sanctions such as a warning letter, limiting business activities and revocation of the business licence.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

There is no duty for a liability insurer to defend a claim. The decision to defend a claim is the prerogative right of the insurer as normally granted under the insurance policy. The insurance policy may contain exemptions or limitations that affect approval and claim payments. These conditions incur rights of the insurer to defend a claim.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The obligation of the insurer to conduct a claim payment is determined in the insurance policy. The insurer must indemnify the insured against all losses and damages arising from all accepted risks. For indemnity policies, the insurer shall be obliged to conduct a claim payment to the insured if the risks are covered in the insurance policy.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

POJK 23/2015 stipulates mandatory provisions that must be contained in an insurance policy. One of the required provisions is the period in which the insurer can no longer contest the validity of the insurance contract for a long-term insurance product. A life insurance policy must contain an incontestable clause that states that the insurer will not make cancellation of the insurance policy based on material misrepresentation or material non-disclosure if the policy has reached a certain period of time. However, POJK 23/2015 does not regulate further on the specific period of the incontestable period. In practice, the incontestable period is set for two or three years, depending on the discretion of the insurers.

28 Punitive damages

Are punitive damages insurable?

Indonesian law does not recognise insurance for punitive damages.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

The Insurance Law and its implementing regulations are silent on insurance schemes involving two insurers to provide a primary and excess policy for the insured. In practice, these schemes are applied or undertaken so long as they have prior agreement from the parties involved.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

The obligation of the insurer is subject to the provisions of the insurance policy. The insurance policy will govern the scope of each party's obligations, including in the event that the insured is unable to pay the deductible.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There are no specific regulations that govern priority for payment when there are multiple claims from the same policy. Multiple claims occurring from multiple events will be paid in order of event.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Based on article 253 of the Indonesian Commercial Code (ICOM), the amount that the insured should be covered is no higher than the total value of the coverage. Aside from this, article 252 of ICOM provides the restriction to hold a second coverage for the time period already insured for the full price. Otherwise, the second coverage is treated as a 'cancellation of coverage'.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

There are no regulations that stipulate that disgorgement or restitution claims are insurable losses. However, article 249 of ICOM stipulates that the insurer is not obliged to assume liability for damages or losses occurred because of self-decay or defect, unless it is stated clearly that such situations or claims are insurable. In this regard, disgorgement or restitution claims are insurable, provided that they are stated clearly in the insurance policy.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

No specific regulations regulate definition of occurrence. It is the discretion of the judge to determine definition of occurrence based on facts and evidences presented in the court preceedings.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Article 251 of ICOM stipulates that every incorrect or false notice, or every concealment of facts known by the insured, even though made in good faith, the nature of which is such that the agreement concerned would not have been made, or would not have been made under the same conditions if the insurer learnt the factual situation of all these matters, shall render the insurance concerned void. In other words, misstatements in the application (as part of the insurance policy) can be the basis for rescission.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Formal reinsurance disputes are rare in Indonesia. In general, the disputes are settled without formal proceedings. According to Regulation No. 1/POJK.07/2014 regarding Alternative Dispute Resolution in the Financial Services Sector (POJK 1/2014), the disputing parties shall first settle such dispute amicably. In the event the dispute is not resolved through amicable settlement, the parties may solve the disputes by alternative dispute resolution or litigation.

Aside from the above, POJK 1/2014 provides that all FSIs are obliged to become members of alternative dispute resolution bodies in their own sectors is stipulated by the OJK. Further, the OJK has issued a list of alternative dispute resolution bodies in the financial sector under OJK Directive No. KEP-6/D.07/2016 dated on December 2016. The Indonesian Insurance Mediation and Arbitration Body (BMAI) appointed as the alternative dispute resolution body for the insurance and reinsurance sector. Further, BMAI provides three stages of dispute resolution for insurance claims (ie, mediation, adjudication and arbitration). However, unlike insurance disputes, BMAI does not have a specific dispute resolution procedure for reinsurance disputes.

Update and trends

Under the Insurance Law, numerous regulations are expected to be issued as the implementing regulations of the Insurance Law, among others, the Government Regulation on the foreign investment ceiling in insurance companies. The Insurance Law calls for limits on foreign ownership within the insurance industry, but has left the task of setting the limit to the Indonesian Government to issue the Government Regulation through a consultation process with members of the house of representatives. As a result, the issuing of the Government Regulation is postponed and has exceeded the time period mandated in the Insurance Law (ie, April 2017).

Another emerging issue relates to the qualification of a public company as a shareholder of an insurance company. Pursuant to the Insurance Law and OJK 67/2016, insurance companies can only be owned by Indonesian legal entities that are directly or indirectly wholly owned by Indonesian citizens (Indonesian shareholders). In line with the said rules it creates legal uncertainty for public companies to be a qualified Indonesian shareholder in the insurance company.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Reinsurance disputes can arise with the following issues:

- breach of reinsurance agreement;
- delay of claim settlement;
- there is an outstanding debt (ie, premium payments) between the insurer and the reinsurer;
- different interpretation on claimable risk between the insurer and the reinsurer; and
- dispute on the amount of approved claim.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Law No. 30 of 1999 regarding Arbitration and Alternative Dispute Resolution (Law 30/1999) regulates arbitration proceedings including reinsurance arbitration. Under Law 30/1999, the arbitral award shall cover among other things: (i) considerations and conclusions of the arbiter or the tribunal according to the whole dispute; and (ii) opinion of each arbiter shall be stated in the arbitral award if there are dissenting opinions in the tribunal.

Further, based on BMAI Decree No. 001/SK-BMAI/09/2014 dated 1 September 2014, the arbitrator must provide reasoning for decisions and considerations before making the arbitral award. The reasoning shall also be subject to applicable law and also take into account the provisions of the treaty as well as the relevant practices and customs in the business activities or transactions concerned with the matter of dispute.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Law 30/1999 stipulates that non-parties to the arbitration agreement may participate and join the proceedings for the resolutions of dispute by the arbitration, if any element of related interest is found and their participation is agreed by the parties in a dispute and by the arbitrator or the tribunal examing the dispute. Non-parties to the arbitration agreement that have rights to submit a claim on an insurance agreement (treaty) that guarantees or extends to guarantee coverage on non-parties can submit a lawsuit through the BMAI.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Under Law 30/1999, the arbitral award shall be final and binding and also has a permanent legal enforcement on the parties, and thus the

parties cannot appeal the arbitral award to the courts. In the event that the party does not voluntarily enforce the arbitral award, the disputing party may request the chairperson of the district court to order the disputed party to enforce the arbitral award. In case of foreign arbitral award, the said award shall be submitted to the Central Jakarta District Court for enforcement in Indonesia.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There are no regulations stipulating obligations of the reinsurer to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision. Under the reinsurance agreement, the reinsurer may agree in advance to accept partial or whole the cedent's coverage portfolio.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Article 1338 of the Indonesian Civil Code (ICC) stipulates that an agreement shall be based on good faith of the parties to the agreement. This principle of good faith applies to all commercial agreements in Indonesia. Indonesian insurance doctrine also recognises an implicit duty of utmost good faith to be implemented in insurance and reinsurance contracts. The utmost good faith duty in insurance and reinsurance contracts is sterner than other commercial agreements. Article 251 of ICOM stipulates that insurance contracts that execute without full disclose of facts known by the insured will result in the insurance contract being declared void.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Facultative reinsurance and treaty reinsurance are subject to the same regulations as mentioned in question 16, regarding ceded reinsurance and retention of risk.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

In principle, a policyholder does not have the right to make any actions against a reinsurer for the risk covered by the reinsurance agreement, owing to the fact that the policyholder has no contractual relationship or legal standing with the reinsurer in the reinsurance agreement. Therefore, normally, entities that are not parties to the reinsurance agreement may not enforce any right under the agreement. However, if both parties in reinsurance agreed beforehand, a 'cut-through' clause is able to change such relationship. A cut-through clause allows a party that that does not have privity with the reinsurer (ie, policyholder) to have rights against the reinsurer under the reinsurance agreement. These cut-through rights generally are limited and are triggered only by specific events enumerated in the cut-through clause (ie, when the ceding company becomes insolvent or liquidated by an insurance regulator). A cut-through clause may take the form of a specific clause or an endorsement attached to the reinsurance agreement.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Pursuant to POJK 69/2016, the insurance agreement must provide a statement that when the insurer or the reinsurer are in the process of liquidation, all rights and obligations incurred in reassurance transactions shall remain binding until either the reinsurer or the insurer, or both, have been liquidated.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Basically, there is no regulation that stipulates that a type of notice and information must be provided by the insurer to the reinsurer with respect to the underlying claim. Therefore, it falls on the agreement between the parties in the reinsurance agreement to stipulate them.

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47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

POJK 14/2015 does not specifically mention the allocation of underlying claim payments or settlement. With respect to this matter, POJK 14/2015 does not revoke Bapepam-LK Regulation No. PER-11/BL/2012 regarding Reinsurance Support; the Self-Retention Limit and Form and Composition of Reinsurance Program Reports (BLKR 11/2012) that stipulate the relevant provisions.

Pursuant to BLKR 11/2012, treaty reinsurance comprises proportional treaty reinsurance along with self-retention (quota share) or proportional treaty reinsurance directly after self-retention (surplus) and treaty reinsurance for excess loss. In the event that quota share and surplus treaty reinsurance both apply, the quota share treaty must be prioritised over the surplus treaty for the allocation of claim payments or settlements that are made by Indonesian companies or domestically.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

There are no regulations that provide specific rights of review provided to reinsurers.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

There are no regulations that govern such obligation. It depends on the terms agreed by the parties in the reinsurance agreement.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Indonesian law does not stipulate such obligation. Unless agreed by the parties, the reinsurer is not obliged to reimburse a cedent for ECOs pursuant to the ICC.

Ireland

Sharon Daly, Darren Maher and April McClements

Matheson

Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Ireland has a well-established efficient prudential regulatory infrastructure that complies with best international standards and focuses on risk-based regulation and the application of the proportionality principle.

The Central Bank of Ireland (Central Bank) is responsible for the prudential supervision and regulation of (re)insurance undertakings authorised in Ireland to ensure compliance with regulatory requirements. The Central Bank is a well-regarded regulatory authority and enjoys a reputation for being a robust yet business-friendly regulator.

The Central Bank plays a pivotal role in the supervision and regulation of (re)insurance undertakings in Ireland to ensure compliance with regulatory requirements without placing burdensome administrative requirements on (re)insurance operators.

The Central Bank's administrative sanctions regime provides it with a credible tool of enforcement and acts as an effective deterrent against breaches of financial services law.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Formation of (re)insurance companies

The incorporation procedure in Ireland is straightforward. A company wishing to apply for a licence to carry on (re)insurance business in Ireland may adopt the form of a designated activity company (DAC), a public limited company, an unlimited company, a company limited by guarantee or a *societas europea*.

The DAC is by far the most common form adopted by (re)insurance companies in Ireland and is very similar to the traditional private company limited by shares that existed prior to the introduction of the Companies Act 2014. The DAC's constitution includes a memorandum and articles of association. The main objects clause of the memorandum of association of a DAC sets out the activities that the (re)insurance company has the corporate capacity to undertake.

Generally speaking, a DAC may take up to five business days to be incorporated by making an application to the Irish Companies Registration Office.

Licensing of (re)insurance companies

In order to establish a (re)insurance undertaking in Ireland, an application is required to be made to the Central Bank pursuant to the European Union (Insurance and Reinsurance) Regulations 2015 (the 2015 Regulations), which implemented the Solvency II Directive in Ireland.

The Central Bank has an established process for dealing with applications for authorisation of (re)insurance undertakings. The Central Bank has published both a checklist for completing and submitting applications for authorisation under the 2015 Regulations (the checklist) as well as a guidance paper to assist applicants. The application comprises of the completed checklist and a detailed business plan, together with supporting documents (collectively, the Business Plan).

The principal areas considered by the Central Bank in evaluating applications include the following:

- legal structure;
- ownership structure;
- overview of the group to which the applicant belongs (if relevant);
- scheme of operations;
- system of governance including the fitness and probity of key personnel;
- risk management system;
- own risk and solvency assessment (ORSA);
- financial information and projections;
- capital requirements and solvency projections; and
- consumer issues (eg, minimum competency requirements and consumer protection code).

A high-level overview of the application for authorisation process is as follows:

- arrange a preliminary meeting with the Central Bank to outline the proposals. At this meeting, the Central Bank will provide feedback in relation to the proposal and identify any areas of concern, which should be addressed before the application is submitted;
- prepare and submit the completed checklist and Business Plan;
- dialogue with the Central Bank. The application process is an iterative one involving contact and consultation with the Central Bank after an application is formally submitted. During the review process, it will typically request additional information and documentation and is likely to have comments on certain features of the proposal. The Central Bank may seek additional meetings with the applicant as part of this process in order to discuss aspects of the proposal in further detail;
- the authorisation committee of the Central Bank considers the application;
- once the Central Bank is satisfied with the application, it will issue an 'authorisation in principle', which means that the Central Bank is minded to grant its approval once certain conditions are satisfied; and
- once all conditions are satisfied, the Central Bank will issue the final authorisation and the (re)insurer can commence writing business in Ireland.

From submission of the formal application to the Central Bank to receipt of the final authorisation, it takes in the region of four to six months. The Central Bank does not currently charge a fee for licence applications.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

As mentioned above, (re)insurance undertakings must obtain prior regulatory approval from the Central Bank in order to conduct insurance business in Ireland. The authorisation is granted to either: a life; or non-life (re)insurance undertaking in respect of one or more specified classes of insurance, which relate to different types of risk.

No further authorisation is required to be granted by the Central Bank provided that the undertaking is operating within the scope of the

licence granted and there are no material changes to the Business Plan submitted to the Central Bank.

Any (re)insurance undertaking authorised to carry out its activities may establish branches in other EU member states or operate in these countries on a freedom of services basis, provided that the relevant notifications are made in accordance with the 2015 Regulations.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

Part 3 of the Central Bank Reform Act 2010 (2010 Act) established a statutory system for the regulation by the Central Bank of persons performing controlled functions (CFs) or pre-approval controlled functions (PCFs) for regulated financial service providers.

A regulated financial service provider (including a (re)insurance undertaking) may not permit a person to perform certain prescribed roles unless the regulated financial service provider is satisfied on reasonable grounds that the person complies with the Central Bank's Minimum Competency Code and the person has agreed to abide by the standards of fitness and probity. The requirement ensures that such senior personnel are competent and capable, honest, ethical and of integrity and also financially sound.

Officers, directors and persons who exercise senior management positions will generally constitute PCFs and persons intending to occupy PCF roles must be pre-approved by the Central Bank in advance of a person being appointed to such roles under its fitness and probity regime.

There are 46 PCF roles prescribed by the 2010 Act including the following:

- executive and non-executive directors;
- chief executive;
- head of underwriting;
- head of claims;
- head of actuarial function;
- head of investment;
- head of compliance;
- head of internal audit; and
- head of risk.

The requirements as to the key CFs are set out in the Central Bank's fitness and probity regime and the various guidelines and policy documents published by the Central Bank. In general, the person must be able to demonstrate that he or she:

- has professional or other qualifications and capability appropriate to the relevant function;
- has obtained the competence and skills appropriate to the relevant function, whether through training or experience gained in an employment context; and
- has shown the competence and proficiency to undertake the relevant function.

Specified individuals in such functions are also required to undertake a programme of continuing professional development.

More than one of the key functions can be combined and undertaken by one individual if the entity is satisfied that the nature, scale and complexity of the (re)insurance undertaking allows it. The individual appointed to more than one PCF role must display the competency for each separate role and demonstrate that holding multiple roles will not give rise to conflicts of interest. The Central Bank must approve that person for each PCF role. As a general rule, persons carrying out internal audit functions must not assume responsibility for any other function.

It should also be noted that the Central Bank requires that the number of financial directorships (ie, directorships of insurance undertakings and credit institutions) held by a director of a non high-impact designated insurance undertaking will not exceed five (limited to three for high-impact designated firms) and this would include financial directorships of institutions authorised outside of Ireland. This restriction does not apply to other directorships held within the same group. If an individual holds more than five financial directorships, this creates a rebuttable presumption that the director has insufficient time available to fulfil his or her role and functions. Submissions can be made to the Central Bank in this regard for a derogation.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

(Re)insurance companies regulated by the Central Bank are required to meet the capital and solvency requirements set out under Solvency II and the 2015 Regulations. Irish-authorised insurance undertakings are also required to establish and maintain a further solvency margin as a buffer to ensure their assets are sufficient to cover their liabilities. The Solvency II capital requirements are calculated based on the specific risks borne by the relevant insurer and are prospective in nature (ie, each insurer must make the relevant calculations at least once a year to cover both existing business and the new business expected to be written over the following 12 months).

Solvency II imposes a solvency capital requirement (SCR) and a lower, minimum capital requirement (MCR). An insurance undertaking may calculate the SCR based on the formula set out in the 2015 Regulations or by using its own internal model approved by the Central Bank. The SCR should amount to a high level of eligible own funds, thereby enabling the undertaking to withstand significant losses and ensuring a prudent level of protection for policyholders and beneficiaries. The MCR should be calculated in a clear and simple manner, corresponding to an amount of eligible, basic own funds, below which policyholders and beneficiaries would be exposed to an unacceptable level of risk if the undertaking were allowed to continue its operations.

An insurance undertaking must have procedures in place to identify and inform the Central Bank immediately of any deteriorating financial conditions. As such, the SCR and MCR provide for clear channels by which the Central Bank can monitor the financial state of insurance undertakings. In the event of a breach of the capital requirements, the Central Bank will employ an escalating ladder of supervisory intervention, allowing for the implementation of a recovery plan by an insurance undertaking, as approved by the Central Bank. Where there is a breach of the SCR or MCR, compliance must be re-established within six months or three months respectively, otherwise the Central Bank may restrict the free disposal of the assets of the undertaking and ultimately withdraw its authorisation.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Irish-authorised (re)insurance undertakings are required to establish and maintain technical provisions in respect of all insurance and reinsurance obligations towards policyholders and beneficiaries of insurance or reinsurance contracts. The 2015 Regulations, Solvency II and the Commission Delegated Regulation (EU) 2015/35 (the Delegated Regulations) contain the 'technical provisions' relating to the calculation of reserves to be maintained by (re)insurance undertakings. The value of technical provisions is to be calculated as a combination of the best estimate and a risk margin.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The Consumer Protection Code 2012 (CPC) applies to all Irish-authorised insurers carrying on insurance business in Ireland with Irish consumers. Under the CPC, a 'consumer' means either:

- a person or group of persons, but not an incorporated body with an annual turnover in excess of €3 million in the previous financial year (for the avoidance of doubt, a group of persons includes partnerships and other unincorporated bodies such as clubs, charities and trusts, not consisting entirely of bodies corporate); or
- incorporated bodies having an annual turnover of €3 million or less in the previous financial year (provided that such body shall not be a member of a group of companies having a combined turnover greater than the said €3 million); and includes where appropriate, a potential consumer.

The CPC contains specific provisions relating to the sale of insurance products in Ireland. These include provisions relating to information

and documentation required to be provided to consumers both pre- and post-sale relating to the relevant products.

An insurance undertaking must also comply with the other legislation, which regulate the sale and marketing of certain products (including insurance products) to consumers (as defined above) in Ireland, including but not limited to the following:

- Consumer Protection Act 2007;
- Sale of Goods and Supply of Services Act 1980;
- European Communities (Unfair Terms in Consumer Contracts) Regulations 1995; and
- European Communities (Distance Marketing of Consumer Financial Services) Regulations 2004 (as amended).

It should be noted that the Central Bank does not require the submission of product documents by insurance undertakings operating in the Irish market.

Insurance undertakings that offer certain products are subject to additional regulation by other authorities. By way of example, health insurers operating in the Irish market are subject to prudential supervision by the Central Bank but are also required to be registered with the Health Insurance Authority, which also supervises health insurers particularly with regard to the products offered to Irish customers.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The Central Bank's supervisory role involves overseeing a (re)insurance undertaking's regulatory capital, corporate governance, risk management and internal control systems without placing burdensome administrative requirements on (re)insurance operators.

The Central Bank introduced its Probability Risk and Impact System (PRISM) framework in late 2011, which is a systemic risk-based framework against which the Central Bank assesses supervisory requirements. All regulated firms are categorised as either high-impact (including ultra-high), medium-high, medium-low or low. The category assigned determines the level of supervision and the regulatory fees payable to the Central Bank are aligned with the entity's PRISM rating. The ratings are set according to the systemic risk posed by regulated entities, that is, entities that are categorised as being high-impact under PRISM are subject to a higher level of supervision by the Central Bank as such firms are important for ensuring financial and economic stability. PRISM recognises that the Central Bank does not have infinite resources and selectively deploys supervisors according to a regulated firm's potential impact and probability for failure.

In addition, the Central Bank implements its supervisory function by requiring that (re)insurance undertakings submit annual and quarterly returns on solvency margins and technical reserves. The qualitative reporting under the 2015 Regulations includes the Regular Supervisory Report (RSR), the Solvency and Financial Condition Report (the SFCR), as well as the ORSA. The quantitative reporting includes the technical provisions, own funds and other data on the regulated entity. All quantitative reporting templates (QRTs), the ORSA and the RSR will be reported privately to the Central Bank. A limited number of QRTs and additional qualitative information are required to be made publically available in the SFCR on an annual basis.

In addition to PRISM, the Central Bank's administrative sanctions procedure acts as an effective deterrent against breaches of financial services law including the 2015 Regulations.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

For regulatory capital purposes, (re)insurance undertakings are required to invest assets in accordance with the prudent person principle. This principle sets out the requirements applying from 1 January 2016 to investments and the associated risk management of primary (re)insurers subject to Solvency II.

Regulation 141 of the 2015 Regulations (or article 132 of the Solvency II Directive) and the Delegated Regulations includes provisions on how (re)insurance undertakings should invest their assets and cover extensively some of the main aspects of the prudent person principle, such as asset-liability management, investment in derivatives, liquidity risk management and concentration risk management. The guidelines on the prudent person principle form part of the European Insurance and Occupational Pensions Authority (EIOPA) guidelines on the System of Governance. In addition, a supervisory review process on the review of this principle has been developed for the Central Bank supervisors.

Neither the legislation nor the EIOPA guidance provides a definition of the concept of a 'prudent person'. In general, the prudent person principle compels an undertaking to show that their investment strategy matches the interests of policyholders. With respect to the whole portfolio of assets, undertakings shall only invest in assets and instruments whose risks the undertaking concerned can properly identify, measure, monitor, manage, control and report, and appropriately take into account in the assessment of its overall solvency needs.

It further provides that all assets, in particular covering the MCR and SCR shall be invested in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio as a whole. In addition, the localisation of those assets shall be such as to ensure their availability. Assets held to cover the technical provisions shall also be invested in a manner appropriate to the nature and duration of the insurance liabilities. Those assets shall be invested in the best interest of all policyholders and beneficiaries; taking into account any disclosed policy objective.

The 2015 Regulations requires (re)insurance undertakings to hold eligible 'own funds' equal to the SCR to cover unexpected losses arising both from their underwriting business and the assets in which they invest and the investment strategy of (re)insurance undertakings is to be determined on a risk based calculation of the insurer's SCR.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

In accordance with the 2015 Regulations, a proposed acquirer shall not, directly or indirectly, acquire or dispose of a qualifying holding in an insurance undertaking without having previously notified the Central Bank in writing of the intended size of the qualifying holding (defined below).

A 'qualifying holding' means either a direct or indirect holding in a (re)insurance undertaking that represents 10 per cent or more of the capital of, or the voting rights in, the undertaking, or that makes it possible to exercise a significant influence over the management of the undertaking.

The notification is typically made by the parties jointly completing an acquiring transaction notification form (notification form) and submitting it to the Central Bank. Detailed information in respect of each of the notifying parties must be included in the notification form, particularly in respect of the target entity and the proposed acquirer or disposer. In certain circumstances, the proposed acquirer is encouraged to make contact with the competent authority of the regulated target entity in advance of making the formal notification. However, the making of such preliminary contact is more common in circumstances where the proposed transaction presents particular complexities for the entities involved.

Notification and assessment process

Following submission of the notification form to the Central Bank, it will acknowledge receipt of same within two working days and will carry out its assessment of the proposed transaction within 60 working days of this acknowledgement. It will also confirm the date on which the assessment period of the proposed transaction will end. During the assessment period, but no later than the 50th working day of that period, the Central Bank may request further information or clarification necessary to complete its assessment of the proposed transaction. If such a request is made by the Central Bank, the 60-day assessment period is taken to be interrupted for the shorter of: (i) the period between the date of the request and the date of the receipt of a response from the proposed acquirer; and (ii) 20 working days. In certain circumstances, the Central Bank may extend the interruption period to

30 working days. The Central Bank is entitled to make further requests for information. Such further requests will not, however, interrupt the assessment period.

In carrying out its assessment of the proposed transaction, the Central Bank may consult, where applicable, with other supervisory authorities in the member states of the notifying parties where relevant.

If the Central Bank does not give written notice within the assessment period that it opposes the proposed transaction, it is deemed to be approved. It is open to the Central Bank, however, to impose either a condition or a requirement or both in relation to the proposed transaction. The Central Bank may also fix a maximum period within which the proposed transaction must be completed. In rare circumstances where the Central Bank opposes the proposed transaction, it must inform the proposed acquirer or disposer of this in writing within two working days but in any case, before the end of the assessment period and provide reasons for such opposition. The Central Bank's opposition to the proposed transaction is only permitted where there are reasonable grounds for doing so or where incomplete information is provided in the notification form or in a response to a request for further information. Any decision by the Central Bank to oppose the proposed transaction can be appealed.

In general, the proposed individuals who will direct the business of the target entity as a result of the proposed transaction must be of good standing and the Central Bank will assess the suitability of all persons proposed to be appointed to a PCF who must comply with its fitness and probity regime. The approval process requires the submission of an individual questionnaire to the Central Bank for each proposed individual.

In addition, any person seeking to acquire or dispose of a shareholding or other interest that would either give them a qualifying level of control in a (re)insurance undertaking or increase that person's control above certain levels must first obtain the approval of the Central Bank.

As part of its assessment, the Central Bank will appraise the suitability of the proposed acquirer and the financial soundness of the proposed transaction against certain criteria, including but not limited to the following:

- the reputation of the proposed acquirer or disposer;
- the reputation and experience of the individuals who will direct the business of the target entity as a result of the proposed transaction;
- the financial soundness of the proposed acquirer or disposer, particularly in relation to the type of business carried on by the target entity; and
- whether the target entity will be able to comply and continue to comply with the prudential requirements of existing legislation.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements or restrictions under Irish law regarding financing of the acquisition of a (re)insurance company.

However, as noted in question 10, a notification form must be submitted to the Central Bank prior to the proposed acquisition of a qualifying holding (as defined in question 10) in an insurance company. The notification form requests details of the proposed acquisition and the proposed acquirer, the rationale for the proposed acquisition and details regarding the impact of the proposed acquisition on the target entity. In this regard, it is necessary to provide a detailed business plan for the target entity, setting out the proposed direction of the busines, including financial projections over three years, and must demonstrate that the proposed acquirer has sufficient resources to effectively support the target entity within the requirements of the supervisory regime together with full details on the cost of the proposed acquisition and confirmation as to how the acquisition will be financed.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

Where the proposed acquisition represents voting rights or share ownership of less than 10 per cent (ie, not a qualifying holding as defined in question 10), there are no specific restrictions on investors acquiring a minority interest.

However, where the interest is 10 per cent or more (ie, a qualifying holding), the regime described in question 10 will apply.

As noted above, the Central Bank must be also notified of any increase in a holding above 10 per cent in (re)insurance undertakings, which would result in the size of the holding reaching or exceeding 20, 33 or 50 per cent.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no specific regulatory requirements or restrictions in Irish law governing the investment of foreign citizens, companies or governments in (re)insurance undertakings.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

In all group undertakings, the risk management, internal control systems and reporting procedures must be implemented consistently. These group internal control mechanisms must include, at minimum, adequate mechanisms to identify and measure all material risks incurred to appropriately relate eligible own funds to risks and sound reporting and accounting procedures to monitor and manage the intra-group transactions and risk concentration. These procedures must be satisfactory to the Central Bank.

As provided for in the 2015 Regulations, participating (re)insurance undertakings and the relevant insurance holding company or mixed financial holding company should undertake the ORSA that is required as part of an insurance undertakings risk management system. The calculation of solvency at group level can be conducted using either the accounting consolidation-based method or the deduction and aggregation method. Holding companies are not themselves subject to any specific additional capital requirements under Irish legislation. However, they must comply with the processes and procedures prescribed under the 2015 Regulations for (re)insurance companies in relation to their capital requirements.

The group supervisor will usually be the supervisory body in the EEA member state where the group has its headquarters. Where the Central Bank is the group supervisor it will review the systems and reporting procedures, and review the ORSA conducted at group level to supervisory review. Further, the Central Bank may permit the participating insurance undertaking or reinsurance undertaking, insurance holding company or mixed financial holding company to undertake any assessment required in relation to risk and solvency at a group level at the same time enabling the group to produce a single document covering all relevant assessments.

However, where EU (re)insurers are part of a wider group with a parent insurer or reinsurer or holding company that is headquartered outside of the EEA, supervision may apply in one of two ways:

- by supervising the EU insurers or reinsurers in the group taking account of whether the worldwide group complies with Solvency II standards; or
- by supervising an EU sub-group only.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

The Central Bank has issued guidelines on 'reinsurance cover for primary insurers and the security of their reinsurers' (the Guidelines). The Guidelines provide that every insurer should have a reinsurance strategy, approved by the company's board of directors, that it is compliant with all legal and regulatory requirements, is appropriate to the company's overall risk profile and sets a limit on the net risk to be retained.

This reinsurance strategy should be part of the company's overall underwriting strategy and be reviewed annually or where a change in the company's circumstances or status dictates a review. The reinsurance strategy should identify the procedures for the following:

- the reinsurance to be purchased;
- how reinsurers will be selected, including how to assess the security;
- what collateral, if any, is required at any given time; and
- how the reinsurance programme will be monitored (ie, the reporting and internal control systems).

The Guidelines also provide that Irish-authorised cedents must ensure that reinsurance agreements entered into include the following mandatory terms:

- an insolvency clause requiring the reinsurer to perform its contractual obligations without reduction if the ceding insurer becomes insolvent;
- a provision stating that the reinsurance agreement constitutes the entire contract between the parties;
- a provision requiring reinsurance recoveries to be paid to a cedent without delay and in a manner consistent with the orderly payment of claims by the ceding insurer; and
- a provision providing for reports, at least quarterly, regarding premiums and paid and incurred losses.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

The Central Bank requires insurance companies to hold at least 10 per cent of their own risk; 100 per cent reinsurance is not typically permitted in Ireland.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no specific collateral requirements for reinsurers in a reinsurance transaction under Irish law. However, the Guidelines (see question 15) provide that an insurer's reinsurance strategy should include an evaluation of the reinsurer's security and collateral. Moreover, the precise nature of the collateral is an issue for the parties to the contract to agree.

It is also worth noting that the 2015 Regulations do not permit the Central Bank to impose, on reinsurers from other member states or an 'equivalent jurisdiction', collateral requirements that require the pledging of assets to cover unearned premiums and outstanding claims provisions.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Under the 2015 Regulations, a life or a non-life insurance undertaking can take credit in respect of a contract of reinsurance against its technical reserve requirements only to the amount that can reasonably be expected to be recovered under the contract of reinsurance. No account is taken of any debts arising out of reinsurance operations that are owed by intermediaries if these debts have been outstanding for longer than three months.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Generally

Section 2(1) of the Insurance (No. 2) Act 1983, enables the Central Bank to petition the court to appoint an administrator over an insurance undertaking, in circumstances when an insurer has failed to maintain its regulatory solvency margin or cannot meet claims. The administrator will assume management of a company to attempt to place the insurer on a sound commercial and financial footing. Administration is not available as a remedy for individual creditors, but is available to the Central Bank notwithstanding the availability of another remedy or cause of action being available. The following procedures are available under Irish company law for insolvent or financially troubled (re)insurance companies:

Liquidation

Under section 569 of the Companies Act 2014, a creditor, or the company itself, can petition the court for a winding-up order and the appointment of a liquidator. In the case of an insolvent company the usual grounds the petitioner relies on are that:

- the company is unable to pay its debts; and
- it is just and equitable to have the company wound up.

Part 18 of the 2015 Regulations governs the reorganisation and winding-up of insurance undertakings and Chapter 3 sets out the procedures for the commencement of the winding-up proceedings, the treatment of insurance claims, the right to lodge claims and the withdrawal of authorisation.

Receivership

Receivership is not strictly speaking an insolvency process but facilitates the enforcement of security. A receiver may be appointed by the court or on the basis of a statutory power, usually on the occurrence of a trigger event in a charge (a form of security over assets). A receiver's function is to realise the charged assets and to repay the secured debt.

Examinership

Examinership is a legal mechanism to rescue an ailing but potentially viable company by giving the company 'breathing space' from its creditors. While a company is in examinership it is afforded certain protections (which can last for a period of up to 100 days):

- the company cannot be wound up;
- a receiver cannot be appointed;
- creditors cannot enforce their claims; and
- proceedings cannot be issued or continued against the company except with the leave of the court.

Scheme of arrangement

A scheme of arrangement (that is, schemes that attempt to find a compromise between a company and its creditors and avoid the need for liquidation) is governed by section 450 of the Companies Act 2014 and can be used to rescue companies in financial difficulty. The scheme must have been approved by meetings of creditors or members who have convened the meeting.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Under regulation 277(1) of the 2015 Regulations, insurance claims, shall with respect to assets representing the technical provisions of an insurance undertaking, take absolute precedence over any other claims on the insurance undertaking including claims accorded preference under section 621 of the Companies Act 2014.

However, where a life insurance undertaking is authorised to write non-life insurance for accident or sickness, the insurance claims in relation to the life business of the undertaking shall, with respect to the assets, representing the life technical provisions of the undertaking, take absolute precedence over any claims in relation to the non-life insurance business of the undertaking. Furthermore, insurance claims in relation to the insurance business of the undertaking falling within the categories of accident or sickness shall, with respect to the assets representing the non-life technical provisions of the undertaking take absolute precedence over any claims in relation to the life business of the undertaking.

Despite this, however, expenses arising out of winding-up proceedings shall take precedence over insurance claims to the extent that the assets of the undertaking other than the assets representing the technical provisions, are insufficient to meet such expenses; and, in a situation, where a life insurance undertaking writes non-life insurance for accident or sickness, such expenses shall be divided proportionally between the assets representing life non-life technical provisions.

The priority of claims against the remaining funds in a (re)insurance company that has entered into insolvency proceedings is the same as against any company (section 621 of the Companies Act 2014). Claims will be paid out in order of priority to secured creditors, preferential creditors and unsecured creditors.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Part 2, section 5 of the European Communities (Insurance Mediation) Regulations 2005 (IMD Regulations) provides that a person cannot purport to undertake (re)insurance mediation unless they have registered with the Central Bank as a (re)insurance intermediary or are exempt from such registration. In addition to authorising insurance companies to carry out the business of insurance, it also maintains a register of authorised (re)insurance intermediaries in Ireland.

The IMD Regulations defines 'insurance mediation' broadly as 'any activity involved in proposing or undertaking preparatory work for entering into insurance contracts, or of assisting in the administration and performance of insurance contracts that have been entered into (including dealings with claims under insurance contracts)'. Activities specifically excluded from the definition include an activity that is undertaken by an insurer or an employee of such an undertaking in the employee's capacity, involves the provision of information on an incidental basis in conjunction with some other professional activity, so long as the purpose of the activity is not to assist a person to enter into or perform an insurance contract, or involves the management of claims of an insurance undertaking on a professional basis; or involves loss adjusting or expert appraisal of claims for reinsurance undertakings.

In Ireland, as the IMD Regulations captures most activities that insurance agents engage in other than limited back office claims management. However, the definition of insurance mediation in the IMD Regulations refers to activities that include 'dealing with claims' and not the management of such claims. Therefore, it is the generally accepted understanding that insurance undertakings who engage solely in the administration of insurance claims, without assisting the insured with regard to claims are not governed by the IMD Regulations.

The Irish Investment Intermediaries Act 1995 (IIA), has not been disapplied and continues to govern the regulations of intermediaries despite the IMD Regulations. As such, two pieces of Irish legislation govern intermediaries operating in Ireland. In practice, however, the Central Bank treats the provisions of the IIA as having been formally disapplied, although this is not strictly accurate. As such, technically the IIA is still inforce and insurance intermediaries should continue to comply with the IIA as well as the provisions of the IMD Regulations.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

A contract is not generally enforceable in favour of or against a person who is not a party to the contract under Irish law because of the common law doctrine of privity of contract. There is no Irish legislation providing for the rights of third parties, similar to the UK Contracts (Rights of Third Parties) Act 1999.

Section 76(1) of the Road Traffic Act 1961 and section 62 of the Civil Liability Act 1961 provide limited exceptions to this rule. For example, a claimant in a road traffic accident is entitled to claim against the insurance company of the owner or driver of the other vehicle involved in the accident. In circumstances where an insured under a liability insurance policy becomes bankrupt or dies (individual), is wound up (company) or dissolved (partnership or other incorporated association), a third party may have a direct action against the insurer under section 62 of the Civil Liability Act 1961.

The scope and operation of section 62 of the Civil Liability Act is quite limited following clarification by the High Court in recent years. The Irish courts have confirmed that liability in the underlying claim against the insured must be established before the insurer can be joined to proceedings or sued. The Irish courts will recognise a valid repudiation by an insurer, a claimant cannot remedy a breach by an insured of the insurance policy (*McCarron v Modern Timber Homes Limited (in liquidation)*, *Shaun McColgan, Daniel McColgan v Quinn Insurance Limited* (unreported) High Court [3 December 2012]) and *Yun Bing Hu v Duleek Formwork Limited (in liquidation)* and *Aviva Direct Ireland Limited* [2013] IEHC 50).

In certain circumstances, a beneficiary of a trust can directly enforce the rights of the trust against an insurer. However, the burden of proving that the trust exists rests on the beneficiary, and the beneficiary must also be able to show that he or she is entitled to the benefit of the particular insurance policy by proving 'more than a reasonable expectation' that he or she is to benefit (*In re Irish Board Mills Ltd (in Receivership)* [1980] ILRM 216).

The Consumer Insurance Contracts Bill 2017 (see 'Update and trends') passed the second stage in the Dáil (the lower house of Parliament) on 9 February 2017 and will now proceed to the committee stage (there is no clear timeline for its implementation). The Bill was published following a report by the Law Reform Commission in 2015 that recommended reforms to consumer insurance law. Section 18(1) and section 18(2) of the Bill provides that where a policy provides insurance against a liability which may be incurred to a third party, and where the person has died, cannot be found, or is insolvent, or where for any other reason it appears to a court to be just and equitable to so order, the third party should benefit from the rights of the insured person under that contract of insurance and should be entitled to enforce those rights directly against the insurer, notwithstanding anything to the contrary in any enactment or rule of law, including the doctrine of privity of contract.

Section 18(4) of the Bill provides that third parties should be entitled to issue proceedings directly against an insurer before the establishment of liability of the particular insured person, but that the liability of the insured must be established throughout the course of those proceedings before the rights of the third party can be enforced.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Generally, any consequences of late notice will be set out in the insurance policy.

In circumstances where late notice requirements are a condition precedent to liability, an insurer is entitled to deny coverage for a breach without having to demonstrate that it has suffered loss or prejudice as a result of that breach. Absent such a condition precedent, damages are the only remedy available to insurers for late notice of a claim by an insured.

The Irish courts are reluctant to allow insurers to deny coverage for technical breaches of notice conditions, particularly for mere failure to notify a circumstance. While an objective test is applied, in practice the court will consider whether an insured had actual knowledge of the particular circumstance that it is alleged should have been notified to insurers. The knowledge of the insured in that respect is subjective.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Under Irish law, an insurer is not subject to extra-contractual exposure in the event of wrongful denial of a claim. However, the insured may have a remedy in damages for breach of contract.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Irish law does not impose a duty to defend on the insurer, this is a matter of contract. The policy may impose such a duty or may simply provide that the insurer has a right to associate in the defence of the claim. In the event that an insurer takes on the defence of the claim, it must defend the claim subject to the contract of insurance.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The insured's right to an indemnity is dependent on:

- the occurrence of an event that has rendered the insured liable to a third party;
- the event and the consequent liability being within the scope of the cover provided by the policy; and
- it being established that such liability has caused loss to the insured.

Subject to the express provisions of the policy, the insurer's payment obligation is triggered when the insured's liability to a third party has been determined by agreement, award or court judgment (and not when the incident or occurrence giving rise to the liability takes place).

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Under Irish law there is no general incontestability period beyond which a life insurer cannot contest coverage based on misrepresentation in the application for coverage.

28 Punitive damages

Are punitive damages insurable?

The Irish courts occasionally award punitive or exemplary damages on public policy grounds. The Irish Supreme Court has recently confirmed that exemplary damages can be awarded where the damage caused was deliberate and malicious, and calculated to unlawfully cause harm or gain an advantage. The award of damages must be proportionate to the injuries suffered and the wrong done.

Exemplary or punitive damages are insurable in Ireland. The Law Reform Commission considered this issue in a report published in 2000 entitled *Aggravated, Exemplary and Restitutionary Damages*. In this report, the Law Reform Commission stated that public policy considerations in favour of prohibiting insurance for exemplary damages were not strong enough to require legislation in this area. However, such damages are likely to be excluded from cover in circumstances where they are awarded to remedy an intentional act.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Excess insurance is not usually triggered until primary limits have been exhausted. Whether excess coverage is required to 'drop down' in circumstances where the primary insurer is insolvent will ultimately depend on the wording of the policy. As yet, there are no reported decisions of the Irish courts on the interpretation of excess policy wording. However, an Irish court would not be expected to order a 'drop down' in the absence of an express provision in the policy.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Subject to policy terms and conditions, where an insured is insolvent and unable to pay a self-insured retention or a deductible, there is no obligation on the insurer to pay the retention or deductible. However, the insurer will generally be obliged to pay the claim net of the retention or deductible unless payment of the retention or deductible is expressed to be a condition precedent to cover in the policy.

As noted in question 22, a third party may have a direct action against the insurer under section 62 of the Civil Liability Act 1961, in circumstances where an insured under a liability insurance policy becomes insolvent. However, in *Hu v Duleek Formwork Ltd (in liquidation)* and *Aviva Direct Ireland Ltd* [2013] IEHC 50, High Court, 5 February 2013, the payment by the insured of an excess was a condition precedent to the policy and had not been paid. The court held that the third party was not entitled to remedy the breach by discharging the excess.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

Subject to the terms and conditions of the policy, where there are multiple claims under one policy, claims are usually paid in chronological order once they have been fully proved.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

In circumstances where more than one policy responds to the same loss, it is necessary to consider how the various responsive policies interact and which policy responds first.

There is a distinction between double insurance, and instances where there are layered policies to provide coverage for different levels of cover. In circumstances where there are layered policies, the excess policy is not triggered until the primary policy has been exhausted. In instances of double insurance (ie, where two or more policies cover the same risk on behalf of the same insured), the principle of contribution applies.

Section 80(1) of the Marine Insurance Act 1906 provides that, in cases of double insurance, each insurer is bound to contribute rateably to the loss in proportion to the amount for which the insurer is liable under contract. In this respect, it is also necessary to consider whether a policy contains rateable contribution clauses, non-contribution clauses or an excess clause.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Disgorgement is not a concept of Irish law, but appears to encompass the concept of unjust enrichment. The doctrine of restitution also encompasses the concept of unjust enrichment, and is an equitable remedy recognised in Irish law. Restitutionary damages are recognised as a remedy for breach of contract, however, to date there have been very few awards of restitutionary damages by the Irish courts and the courts have not considered whether such damages are insurable. In circumstances where punitive or exemplary damages are insurable under Irish law, it would appear that restitutionary damages are insurable, although they are likely to be excluded from cover in circumstances where they are awarded to remedy an intentional act.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

There are no Irish-reported decisions on aggregation. There are a number of UK decisions, however, the courts' analysis is fact-specific, therefore the judgments are of limited value. Each case depends on the particular wording of the relevant clause as highlighted by the House of Lords in *Lloyds TSB General Insurance Holdings Ltd v Lloyds Bank Group Insurance Co Ltd* [2003] Lloyd's Rep IR 623.

In liability policies, the relevant occurrence is the event that triggers the bodily injury or property damage suffered by the third party. In the English High Court decision in *Countrywide Assured Group Plc v Marshall* [2003] Lloyd's Rep IR 195, Morison J noted the difference between 'event' and 'cause'. In particular he noted the words 'event', 'occurrence' or 'claim' describe what has happened, whereas the word 'cause' describes why something has happened.

While decisions of the courts in England and Wales are not binding on Irish courts, they are generally of persuasive authority in the absence of an Irish authority.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

A 'basis of contract' clause is a declaration by the prospective insured warranting that all statements made in the proposal form are true and accurate and form the basis of the contract. The effect of such clause is

to elevate those statements to the status of contractual warranties. As a result, misstatements in the proposal form may entitle the insurer to repudiate the contract without any reference to materiality. However, basis of the contract clauses are considered to be very draconian by the Irish courts and there is a judicial reluctance to enforce such clauses. The Consumer Insurance Contracts Bill 2017 proposes to abolish basis of the contract clauses in consumer insurance policies.

Parties to contracts of insurance are subject to the duty of utmost good faith. As a result, the insured has a duty to disclose all material facts in the proposal form. The remedy for breach of the duty is avoidance.

A material fact is one that would influence the judgment of a prudent underwriter in deciding: whether to underwrite the contract; and if so the terms (such as the premium) on which it might do so.

The duty goes beyond a duty to answer questions on a proposal form correctly; however, the Irish courts have confirmed that the questions posed on the proposal form will inform the duty. There is no requirement to show inducement under Irish law.

Misrepresentation is closely related to non-disclosure and attracts the same remedy. To rely on misrepresentation, the insurer must establish that there has been a representation of fact made by the insured that is untrue. Misrepresentations can be fraudulent, negligent or innocent. The common law position is that a misrepresentation is fraudulent if made with knowledge of its falsity or without belief that it was true or with reckless disregard as to whether it was true or false.

The Consumer Insurance Contracts Bill 2017 (see 'Update and trends') will introduce proportionate remedies for misrepresentation but retains the remedy of avoidance for fraudulent misrepresentation. Section 16 of the Bill replaces warranties with suspensive conditions and abolishes basis of contract clauses. The effect of the suspensive condition is that the insurer's liability is suspended for the duration of the breach but if the breach has been remedied by the time a loss has occurred, the insurer shall (in the absence of any other defence), be obliged to pay the claim. This provision applies to any term however described that has the effect of reducing the risk underwritten by the insurer related to particular type of loss, loss at a particular time, or loss in a particular location.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

The vast majority of reinsurance agreements in Ireland include an arbitration condition, requiring all disputes under the agreement to be referred to arbitration in the first instance. As such, there are very few judicial decisions on reinsurance law in this jurisdiction as arbitration is the primary means for formal resolution of insurance disputes.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

See question 36.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Since 8 June 2010, the Arbitration Act 2010 has applied the United Nations Commission on International Trade Law (UNCITRAL) Model Law to all Irish arbitrations. The Arbitration Act provides that an award made by an arbitrator must be in writing and shall state the reasons on which it is based, unless the parties agree otherwise.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

A third party cannot be joined to arbitral proceedings without its consent and therefore, absent the agreement of the third party, an arbitrator does not have the power to join a third party to an arbitration. Section 16 of the Arbitration Act allows an arbitrator to consolidate multiple arbitral proceedings, including where these proceedings involve a different party or parties, in circumstances where all parties are in agreement with consolidation.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Under section 23(1) of the Arbitration Act, an award made by an arbitral tribunal under an arbitration agreement is enforceable by action or, by leave of the High Court, in the same manner as a judgment or order of that court with the same effect.

The Arbitration Act 2010 incorporates the UNCITRAL Model Law, aligning Irish law with international standards. Under Model Law, an award made by an arbitrator can be challenged; however, the grounds which allow for such a challenge are very limited. Article 34 of the Model Law requires that the party making an application to challenge a decision of an arbitrator furnishes proof that:

- a party to the arbitration was under an incapacity or that the agreement is invalid under the law that governs it;
- the party making the application was not given proper notice of the appointment of an arbitrator or the arbitral proceedings or was otherwise unable to present his or her case;
- the award deals with matters outside the terms or beyond the scope of the submission to arbitration, provided that, in circumstances where matters submitted to arbitration can be distinguished from those not submitted, only the part of the award relating to matter not submitted may be set aside; or
- composition of the arbitral tribunal was not in accordance with the agreement of the parties, unless such agreement was not in accordance with the law.

It is also open to parties to challenge an award where the court finds that the subject matter of the dispute is not capable of settlement by arbitration or that the award is in conflict with the public policy of the state. As such, following the enactment of the Arbitration Act and the application of Model Law, the Irish courts afford substantial deference to arbitral awards.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The onus to establish that the loss was covered and that there is actual liability for the reinsured to pay is on the reinsured unless the contract proves otherwise.

The scope of the obligations and defences available to the reinsured are generally provided for within the contract itself; this is normally prescribed to be either a 'follow-the-settlements clause' or 'follow-the-fortunes clause'.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Parties subject to contracts of reinsurance are subject to the duty of utmost good faith. It is significantly different to other commercial agreements as it imposes a positive obligation on the insured to make a disclosure. Both parties have an overriding obligation to disclose all material facts and it is possible to breach the duty by omission or silence.

Update and trends

In the aftermath of the decision of the United Kingdom to leave the European Union (Brexit), many financial services companies are now looking to establish a subsidiary in a country with access to the single market in order to mitigate the potential loss of passporting rights post-Brexit. Ireland's well-established prudential regulation, common law jurisdiction, well-educated English speaking and flexible workforce, together with its close proximity to the UK has cemented its status as a thriving hub for the insurance industry. Authorisation-related activity since the Brexit vote has continued to increase, including queries regarding insurance authorisations.

Following the Brexit vote, (re)insurance companies are considering their options and are developing plans to ensure they are fully prepared in the event of a hard Brexit. Since 2008, several overseas (re)insurance groups have chosen Ireland as the headquarters for European business, including Beazley Group plc, XL Capital Limited, Willis Group Holdings Limited and Zurich. Others have restructured to underwrite their 'Europe ex-UK' business from Ireland.

Compared to 2016 levels, we anticipate increased levels of insurance industry mergers and acquisitions (M&A) activity in 2017. While the lack of clarity about specific proposals under Brexit and the proposed changes to the US financial services industry regulations and tax code may be a short-term inhibitor of insurance M&A, once clear, some of the changes may drive increased deal-making as the year progresses.

The EU (Anti-Money Laundering: Beneficial Ownership of Corporate Entities) Regulations 2016 (the 2016 Regulations), which came about as a result of the Fourth Anti-Money Laundering EU Directive (4AMLD), requires corporate and other legal entities incorporated in Ireland to hold adequate, accurate and current information on their beneficial ownership, including details of the beneficial interests held, and to keep and maintain a beneficial ownership register since 15 November 2016. Such entities will in due course be required to file this information with a central beneficial ownership register (BOR) once established. The deadline for transposing 4AMLD into Irish law is 26 June 2017 and the BOR is expected to be in place and ready to be populated from that date. It is likely that this beneficial ownership information will become publicly accessible when related measures come into force later this year.

The Insurance Distribution (Recast) Directive ((EU) 2016/97) (IDD) is required to be transposed into Irish law by 23 February 2018, at which point the provisions of the European Communities (Insurance Mediation) Regulations 2005 will be repealed. The IDD creates a minimum legislative framework for the distribution of insurance and reinsurance products within the EU and aims to facilitate market integration and enhance consumer protection. We have no further update as regards the timeline and we are still working on the basis that the above mentioned implementation date will be met.

In a welcome move, the European Commission agreed to extend the date of application of the EU Regulation on Packaged Retail and Insurance-Based Investment Products (PRIIPs) ((EU) No. 1286/2014) (the PRIIPs Regulation), which is to be supplemented by Regulatory Technical Standards specifying the presentation, content and underlying methodology of the key information documents (KID). The European Commission expects the revised PRIIPs framework to be in place during the first half of 2017 and to apply to manufacturers and distributors of PRIIPs products as of 1 January 2018. The PRIIPs Regulation is a key piece of legislation, which aims to enable retail investors to understand and compare the key features and the potential risks and rewards of investment products, funds and investment-linked insurance policies. Alternative investment funds marketing to retail investors have until 31 December 2017 to comply with the PRIIPs Regulation. UCITS are currently exempted from preparing a KID under the PRIIPs Regulation until 31 December 2019.

Ireland's national implementing legislation, comprising of the Data Protection Acts 1988 and 2003, implements the EU Data Protection Directive 95/46/EC (the Directive) in a reasonably linear way. The existing data protection framework under the Directive will be replaced by the General Data Protection Regulation (GDPR), which will come into force on 25 May 2018. As a regulation, it will not generally require transposition into Irish law. The GDPR emphasises transparency, security and accountability by data controllers and processors, while at the same time standardising and strengthening the right of European citizens to data privacy. Over the course of 2017, the Irish Data Protection Commissioner (DPC) will be proactively undertaking a wide range of initiatives to build awareness of the GDPR. There is no indication (and we do not anticipate) at this time that the Irish legislature will gold-plate the new general data protection regulation. It is worth noting that the DPC has published a code of practice for the insurance sector, which sets out how the DPC expects insurance businesses to implement and apply data protection requirements.

Following implementation of the Insurance Act 2015 in the UK in August 2016, insurance law in Ireland is now significantly different from the UK law for the first time since 1906. We anticipate that the implementation of the Act will have an impact on the Irish insurance industry as the Irish market is closely connected to the UK (in particular the London market) and many Irish risks are written subject to English law. The significance of this impact remains to be seen.

The Consumer Insurance Contracts Bill 2017 passed the second stage in the Dáil (the lower house of Parliament) on 9 February 2017 and will now proceed to the committee stage although there is no clear timeline for its implementation. Minister for State for Financial Services Eoghan Murphy told members of the lower house that the government is 'supportive in principle' of the bill, but 'likely to submit substantive amendments' at committee stage. Murphy also said that the government wanted to examine developments in EU law since the 2015 report, including the IDD, which was agreed in 2016. The Law Reform Commission published a Report on Insurance Contracts in July 2015, together with a draft Consumer Insurance Contracts Bill 2015. The Consumer Insurance Contracts Bill 2017 is substantially similar to the Law Reform Commission's draft Bill. The Consumer Insurance Contracts Bill 2017 proposes reform of the duty of disclosure, the introduction of proportionate remedies, the abolition of basis of contract clauses, the abolition of warranties and replacement with suspensive conditions, amendment of third-party rights and granting damages for late payment of claims. It applies only to consumer insurance policies; however, the definition of consumer is widely drafted.

The Financial Services and Pensions Ombudsman Bill 2017 was published on 10 May 2017 and will change the limitation period applicable to complaints to the Financial Services Ombudsman (FSO) in respect of long-term financial services (including insurance products such as life insurance policies) to three years after the date on which the policyholder becomes aware of a claim or reasonably should have been aware. Significantly, it is proposed that the amendment will have retrospective effect.

The High Court has confirmed that after-the-event insurance is valid and does not fall foul of the rules on maintenance and champerty, which remain in force in Ireland. Following the 2015 decision of the Court of Appeal in *Greenclean Waste Management Ltd v Leahy*, the way is clear for ATE insurance to be used as a legitimate form of third-party funding in this jurisdiction, provided the policy in question is sufficiently certain. ATE insurance is the only valid third-party funding in this jurisdiction, pending the outcome of an appeal to the Supreme Court in another decision of the High Court, *Persona Digital Telephony Ltd & Another v Minister for Public Enterprise*, which confirmed that professional third-party funding arrangements are unlawful. The Supreme Court's judgment is currently awaited.

Finally, in recent times, there has been a significant increase in the number of insurance law decisions emanating from appeals of findings by the FSO. For example, in the recent decision of *Richardson v Financial Services Ombudsman & another*, the High Court upheld a finding of the FSO that an insurer was entitled to avoid a life assurance policy on the grounds of non-disclosure. This was a significant judgment as the Irish courts have traditionally been reluctant to permit insurers to avoid policies. The decision of the High Court turned on the strength of the proposal form and serves as a useful reminder to insurers of the importance of a well-drafted proposal form.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Under Irish law, both facultative reinsurance and treaty reinsurance are treated the same. Treaty reinsurance is generally more common than facultative reinsurance in the Irish market, although this depends on what the parties are trying to achieve. Reinsurance contracts are discussed generally in question 15 above.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

In accordance with the common law doctrine of privity of contract, a contract cannot be enforceable in favour of or against a person who is not party to the contract.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The Guidelines (see question 15) provide that Irish authorised cedents must ensure that reinsurance agreements entered into include a mandatory insolvency clause requiring the reinsurer to perform its contractual obligations without reduction if the ceding insurer becomes insolvent.

However, the reinsurer, for reasons of privity (see question 44) is not required to settle policyholder claims.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

There are no prescribed provisions under Irish law that specifically govern notice and information between insurer and reinsurer. Usually these issues are dealt with in the reinsurance agreement together with the remedies for failure to comply.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

As there is no statutory law that regulates the allocation of underlying claims, the allocation of such claim payments or settlements depends on the respective reinsurance agreements. The reinsurance agreements may provide that the allocation of claims has to occur in proportion to the reinsured amounts or, alternatively, it may establish a ranking between the respective reinsurance policies where the reinsured must exhaust the first-ranked policy before turning to subsequent reinsurance policies.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Irish law does not provide any specific type of review rights in favour of the reinsurer. In practice, such a right of the reinsurer will be dealt with by the terms of the reinsurance agreement, and will most commonly include the submission of information or documents proving the occurrence of the loss or the fact that allocation was made in accordance with the reinsurance contract.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Irish law is silent as to whether a reinsurer is obliged to follow the cedent's settlement of reinsurance claims by way of commutation. In practice, the obligation of the reinsurer to reimburse the cedent for its commutations with the underlying insured will depend on the terms of the reinsurance contract, particularly with reference to the provisions as to 'follow-the-settlements' and as to the claims settlement authority vested in the cedent.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Irish law does not provide any specific rule regarding ECOs. Instead, the reinsurer's liability towards the cedent is determined by the reinsurance agreement usually within loss settlements reinsurance clauses.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Decree Law No. 95 of 6 July 2012, as amended and converted into Law No. 135 of 7 August 2012, dissolved the Italian Private Insurance Supervisory Agency (ISVAP) and replaced it with the Insurance Supervisory Agency (IVASS), a department of the Bank of Italy.

From 1 January 2013, IVASS took over all functions carried out by ISVAP, including the power of authorisation, direction, inspection, enforcement of precautionary measures and sanctions, as well as the adoption of any regulation necessary for the sound and prudent management of undertakings or for disclosure and fairness of behaviour by supervised entities, including the control of intermediaries, the financial promoters and agents listed in the Register of Insurance and Reinsurance Intermediaries (RUI). In contrast, the Register of Insurance and Reinsurance Loss Adjusters and the Italian Information Centre, responsible for providing information to parties entitled to compensation following an accident that has occurred in an EU member state (other than the country of residence of the party) and caused by motor vehicles registered and insured in one of the states of the European Economic Area, have been taken away from the insurance regulator's competences and passed to the Public Insurance Services Agency.

The General Manager of the Bank of Italy is also the president of the new Italian supervisory agency, and he or she promotes and coordinates the activities of the Council, which is responsible for the overall administration of the agency.

Other governing organs of IVASS are the Council and the integrated directorate made up of some members of the board of directors of the Bank of Italy and the IVASS advisers. The directorate has competence in integrating and directing the public body activities and strategic decisions.

The new Italian regulator adopted an internal organisational regulation providing for a full integration into the Bank of Italy structure, although it does preserve some logistical autonomy.

Following its logistical and administrative reforms, the Italian regulator has been active in reshaping a rigid and overcrowded insurance market, enhancing the transparency and clarity of information but preserving the negotiating simplicity for insureds, and securing, at the same time, effective sanctions against insurance companies that are not compliant with the new market rules.

First, IVASS regulated the insurance services offered via the internet laying down rules setting out the minimum requirements any insurance or reinsurance company's website shall have in order to legitimately promote insurance business or services offered electronically through insurance portals. Then IVASS reformed the administrative fines and the application of disciplinary sanctions in respect of insurance and reinsurance intermediaries, and the norms ruling the operativity of the guarantee committee that shall oversee sanctions proceedings. Subsequently, IVASS introduced an obligation for (re)insurers and intermediaries to adopt a certified email address simplifying the formal communications and services of judiciary writs on these subjects and shortly after IVASS dealt with the long-term property insurance reintroduced by Law No. 99/2009. Because of a multitude of protests made by insureds complaining about companies' refusal to grant an early termination of multi-year insurance contracts, IVASS directed all insurance to 'specifically and with adequate graphic evidence' indicate in the insurance wording whether the insured benefited from a discount because of the long duration of the contract and the fact that, because of the discount applied, the policyholder cannot exercise the right of early withdrawal from the contract for the first five years of the contract.

Subsequent IVASS interventions regarded the receivership of (re)insurance companies, the due diligence and anti-money laundering registrations on the part of (re)insurance companies and intermediaries. In addition, IVASS published Regulations Nos. 6 and 7 on the occupational requirements of insurance and reinsurance intermediaries, respectively, especially regarding the professional requirements that the intermediaries must possess. During the first quarter of the 2015 IVASS-issued Regulation No. 8 concerning measures to simplify the contractual relations between insurers, intermediaries and customers enhancing the use of an advanced electronic signature in all contracts. Furthermore, this Regulation introduced an obligation for intermediaries to facilitate electronic payment and specifies the requirement for the intermediary to 'make available' to their customers an electronic documentation and information package if the client requires such in electronic format instead of a paper copy of the policy.

The Italian insurance regulator has been particularly active regarding complaints handling. The first set of new rules amended ISVAP/IVASS Regulation No. 24 (dated 19 May 2008) and included a number of significant changes, particularly for insurers receiving more than 20 complaints per year, which shall now catalogue the complaints and report them to IVASS on a regular basis.

A more radical and important reform of the complaints handling took place with Regulation No. 46 of 3 May 2016, which, amending ISVAP Regulation No. 24, adjourned the procedure for the submission of complaints to IVASS and provided the complaints management guidelines for both insurance companies and intermediaries. According to the new regulation, the relevant insurance companies must handle complaints related to their insurance agents who shall be involved in the management of the complaints and must provide the insurance company with all necessary information.

A dedicated complaints management policy is available to insurance brokers, EU intermediaries, banks, financial intermediaries, Italian investment firms and Poste Italiane; they shall directly manage the complaints received and shall implement an internal structure in charge of complaints handling. The complaints handling or specific phases of the procedure can be outsourced and Regulation No. 46 lays down specific rules for the transparent and efficient handling of the complaints.

Complaints received in accordance with the terms and procedures applicable to Italian insurance companies and intermediaries must be dealt with and an answer must be sent to the complainant within 45 days. When the grievance is rejected, partially or in full, the response shall contain a clear description of the insurance or the intermediary's positions, in simple and plain language.

Complaints shall be recorded in a dedicated archive and all pre-contractual documentation shall include information on the complaints submission procedure with details of the insurance or the intermediary's internal structure in charge of handling the complaints.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

According to Italian insurance law, only public companies, cooperatives and mutual insurance companies or equivalent foreign companies can apply to IVASS for an authorisation.

Lloyd's syndicates are the sole exception, and they have been specially authorised by way of the Industry Ministry Decree of 2 July 1986 because of their particular historical status and in accordance with the Treaty on the Functioning of the European Union (formerly the EC Treaty).

Insurance and reinsurance companies must be incorporated in Italy, in a member state of the European Union or elsewhere in the world. Different requirements and conditions apply for the formation and licensing of a company depending on where it is incorporated.

In Italy, it is forbidden to set up a company whose sole object is the exclusive pursuit of insurance business abroad.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

New insurance and reinsurance companies that want to undertake or start a new business in Italy can do so only once they have been authorised or licensed by IVASS through an order (if the undertaker has its head office within the territory of Italy) or by an acknowledgement of the formal communication made by the company, which has to be backed up by a confirmation of the supervisory authority of the state where the undertaker has its head office.

Both the order and the acknowledgement of the formal communication must be published in the Official Journal, and the newly authorised or licensed insurance and reinsurance company may start underwriting insurance or reinsurance only after such publication.

An insurance and reinsurance company that applies to IVASS for an authorisation shall submit a number of documents. The most important are as follows:

- a certified copy of the memorandum and articles of association, showing the insurance classes that the insurer will underwrite and if it also intends to offer reinsurance. A side letter undertaking the obligation to become a member of the Italian Bureau and of the Motor Guarantee Fund shall have to be produced if the compulsory motor or vessel liability insurance is listed within the declared classes of business;
- evidence that the memorandum and articles of association have been deposited with the registrar of companies and that the incorporation has taken place in accordance with the Civil Code provisions or the applicable local laws;
- a scheme of operations and a technical report drawn up according to the IVASS regulations, including the names of the persons charged with administration, management and internal control and corporate governance functions, and the names of the natural or legal persons who directly or indirectly have controlling interests or qualifying holdings in the company with an indication of the amount of each holding;
- proof that the company has a share capital or guarantee fund fully paid up in cash sufficient to meet the liabilities of the intended business plan, and proof that the company possesses the minimum organisation fund required by ISVAP Order No. 97/1995, Order No. 98/1995, or both, fully paid up in cash; and
- for foreign companies, proof of the appointment of a general representative, who must be domiciled for the appointment at the address of the branch. If a company is appointed as general representative then the registered office must be within the territory of Italy.

If the application is incomplete or IVASS's requests for further information are not met, the authorisation is usually not granted. It is also refused if no proof is given that the share capital or guarantee fund has been fully paid up or that the organisation fund is actually and immediately available to the company. Equally, the authorisation or licence is denied if any persons charged with the administration, management and internal control functions do not meet the prescribed requirements, or if the scheme of operations does not satisfy the financial needs and the technical rules for the correct management of an insurance business.

A major role in the authorisation process is played by the laws, regulations and administrative provisions of any EU or non-EU state to which the company or one or more of its shareholders is subject, and any difficulties in meeting such requirements may delay the application or even entail a final refusal.

An IVASS order refusing an authorisation is notified to the company by means of a registered letter with advice of receipt within six months from the date of the complete application with all documents required of law or with the additional documents and information requested by the authority. If the six months elapse with no response received by the applicant company, then the authorisation shall be considered refused.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The directors, officers, statutory auditors and general directors must all meet the prescribed requirements of probity, independence and trustworthiness according to the relevant Civil Code provisions, article 4 of Ministerial Decree No. 186/1997 and Ministerial Decree No. 162/2000, thereby being able to ensure sound and prudent management. The sensitive question of the 'interlocking directorates' has been addressed and dealt with by article 36 of Decree Law No. 201 of 6 December 2011, introducing a prohibition for an individual to be a member of two or more boards of insurance companies, financial institutions or banks if these are in competition among themselves.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

In Italy, an insurance company's minimum share capital or guarantee fund fully paid up in cash must not be less than:

- for companies intending to pursue life insurance: €5 million;
- for companies intending to pursue non-life insurance:
  - €5 million for insurance classes 10, 11, 12, 13, 14 and 15;
  - €2.5 million for insurance classes 1, 2, 3, 4, 5, 6, 7, 8, 16 and 18; and
  - €1.5 million for insurance classes 9 and 17;
- for companies intending to pursue life insurance, personal accident and sickness insurance simultaneously:
  - €5 million for life insurance; and
  - €2.5 million for the pursuit of personal accident and sickness insurance; and
- for cooperative companies the minimum share capital is reduced to half the listed amounts.

EU Directives 2002/12/EC and 2002/13/EC on solvency margin requirements for life and non-life insurance undertakings were implemented in Italy in 2003; ISVAP Regulations Nos. 2322/2004 and 2415/2006 were subsequently issued on the same subject for domestic insurers and branch offices of non-EU insurers.

The aim of the new ISVAP Regulation No. 36 dated 31 January 2011, which almost entirely repeats the provisions of the two previous regulations, is to improve policyholder protection and strengthen the measures for preventing insolvency.

The implementation date of EU Solvency II has been postponed several times in the past, until 27 May 2016 when the European Commission adopted a Regulation on the risk-free rate under the Solvency II Directive. This Regulation lays down guidelines for insurance companies to follow when calculating technical reserves and financial data with reference to dates between 31 March and 29 June 2016.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Italian law provides for statutory and free reserves not corresponding to particular underwriting liabilities or to adjustments of asset items.

At present, the reserves are considered and regulated by the Private Insurance Code.

Foreign insurance companies operating in Italy under the freedom-of-establishment system shall comply with the provisions on technical reserves that apply to companies with a registered office in Italy.

The adequacy level of the reserves is a source of major concern for the Italian regulator, which has effected a certain number of investigations and controls to guarantee the adequate reservation level of insurers and reinsurers subject to the controls.

On 6 June 2016 IVASS enacted Regulation No. 24 providing for investment limits and coverage of technical reserves. This new set of rules amends ISVAP Regulation No. 27 of 14 October 2008 in order to provide guidelines on how technical reserves of insurance and reinsurance companies should be invested and listed in a register to be kept by the companies. In this respect, insurance companies must have determined their investment policies by 30 September 2016 and must fully comply with the new Regulation No. 24 provisions from 1 October 2016.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The proposing company attaches specimens of their wording to the business plan and technical operation scheme that have been drafted in accordance with the local laws. Unless there are clear and large-scale violations of the Italian public order, IVASS does not exercise any other form of supervision over the wording of insurance provisions.

On the contrary, IVASS, along with the Italian Competition Authority, will assess and potentially investigate whether two or more insurers for one or more class of business are creating cartels in breach of the freedom of competition and to the detriment of consumers. In these cases, 'supervision' of the insurance companies will turn into a full investigation with administrative sanctions and orders to do or not to do something.

For some other products such as pension funds and some life policies, the united index-linked products can be subject to the control of multiple agencies. This is typical with pension products, which are subject to the supervision and control not only of IVASS but also of the Supervisory Commission for Pension Funds (COVIP).

The COVIP was set up by Legislative Decree No. 124 of 21 April 1993, but actually started to operate with its current configuration, functions and scope after Legislative Decree No. 252 of 5 December 2005, in tandem with the introduction in Italy of social security. This act attributes some specific functions to the COVIP, such as:

- authorising and supervising pension funds;
- approval of their memorandum, articles of association and regulations for complementary or voluntary social security;
- supervising and inspecting the technical management, financial institution, assets and bookkeeping of the pension funds; and
- reviewing the adequacy of their organisational structure, including the duty to ensure respect for the principles of transparency in the relationships between the pension products, funds and clientele.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

According to article 39 of Decree Law No. 1 of 24 January 2012, as amended and updated on 19 April 2012, IVASS shall annually verify that all intermediaries, financial promoters and agents listed in the RUI are carrying proper errors and omissions insurance. Moreover, in accordance with the same law provision, IVASS can perform random examinations of the single intermediary, the financial promoter and the agent listed in the RUI to determine their fulfilment of the requirements of probity, independence and trustworthiness, their professional qualifications and their continuous professional education.

In respect of insurance companies subject to IVASS control, there is no compulsory periodic examination of insurance and reinsurance companies; however, IVASS tends to prudentially execute verifications, especially in respect of the technical reserves and with respect to the Solvency II requirements.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Technically, each insurer is free to determine the amount of investment, with the only limitation being in respect of the margin of solvency as dictated by article 44 of the Private Insurance Code. In reality, ISVAP intervened on a precautionary basis and issued Regulation No. 19 of 19 March 2008, which provides different standards for life and non-life insurance companies. After 1 January 2016, the date in which Solvency II came into effect, IVASS concentrated its regulatory activity on insurers' profitability and capitalisation. To this extent, the Regulator first issued Regulations Nos. 25, 26 27 and 28 of 26 July 2016 and Regulation No. 29 of 6 September 2016 followed on 10 August 2016 by a letter to the market better illustrating how to determine the capital requirement using the standard formula as well as the look-through approach dictated by Regulation No. 28/2016.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

All mergers that involve insurance companies operating in Italy are subject to IVASS's prior agreement, but if the merger could end up in a position of market dominance, the Italian Antitrust Authority may also have to give its preliminary authorisation of the operation.

The relevant arrangements and the new memorandum and articles of incorporation are subject to IVASS control.

In the event of a merger resulting in the setting up of a new company with its head office in Italy, the new company must be authorised before it can legitimately underwrite insurance, whereas if one of the parties in the merger has its head office in another EU member state, IVASS agreement to the operation can only be given after the relevant home supervisory authority has expressed its positive opinion.

In the process of reviewing the merger's relevant arrangements, new memorandum and articles of incorporation, IVASS carries out a limited background investigation on the officers and directors of the acquirer or of the new company to ensure that they all respect the Civil Code provisions or meet the applicable legal requirements.

Moreover, following the enforcement of its Regulation No. 10 of 22 December 2015 concerning the processing of equity investments by or into (re)insurance companies, currently IVASS exercises supervisory powers on the (re)insurance companies holding. In particular, IVASS can deny the permit or condition to certain circumstances the acquisition if the transaction appears to be contrary to the sound and prudent management of the Italian (re)insurance company or group, or derives a danger to the stability of the same or group.

Subject to prior authorisation are always: acquisition of control or even significant influence in any (re)insurance company or in a financial or credit institution with registered office in a non-EU country. On the contrary, acquisition of control or dominance in a (re)insurance company or in a financial or credit institution with a registered office in Italy must be pre-authorised only in specific circumstances clearly listed in Regulation No. 10.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The sole requirement is that the incorporating company or the new company resulting from the merger has the necessary solvency margin, taking into account the merger and the consolidated liabilities.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

No specific regulatory requirements and restrictions exist on investors acquiring a minority interest in an insurance or reinsurance company;

they shall comply with the existing anti-money laundering legislation, and provide evidence of their probity and that they are not in breach of any antitrust legislation.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no restrictions regarding investments in, or the acquisition of, an insurance or reinsurance company, subject to the fact that the funding of the operation does not breach any anti-money laundering provision or public policy.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

IVASS has supervisory power over foreign companies controlled or participated in by companies or holdings and subject to their direct control. Furthermore, IVASS has a residual controlling power over Italian companies that are part of a foreign conglomerate that is subject to an EU regulatory body.

In this scheme, the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company are subject to the normal company law provisions dictated by the Civil Code as integrated in Legislative Decree No. 58 of 24 February 1998 and the implementing regulations issued by the National Commission for Enterprises and the Stock Exchange (Consob, which was established under Law No. 216 of 7 June 1974 and which is an independent administrative authority with legal personality and full autonomy. Consob's activity is directed at investor protection, efficiency, transparency in financial conglomerates and the development of the Italian securities market) on intermediaries, markets and issuers.

Following Regulation No. 10 of 22 December 2015 concerning the processing of equity investments by and within (re)insurance companies and the Legislative Decree No. 74 of 12 May 2015, implementing the Directive 2009/138/EC on the taking-up and pursuit of insurance and reinsurance business, IVASS controls that the single company as well as the group to which the former belongs are operating in accordance with the European Insurance and Occupational Pensions Authority (EIOPA) guidelines on the solvency capital requirements and in respect of Solvency II financial requirements. For such purposes, IVASS pursues the health and prudent management of (re)insurance companies, together with Consob, each to the extent of its respective scope of authority, transparency and fairness towards customers.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

At present, the regulatory requirements with respect to agreements for reinsurance ceded and assumed by insurance and reinsurance companies domiciled in Italy are found in EU Directive 2005/68/EC of 16 November 2005 on reinsurance, which modified EU Directives 73/239/EEC and 92/49/EEC as well as Directives 98/78/EC and 2002/83/EC, although the relevant provision at law has not yet been formally enforced in Italy.

On 10 March 2010, ISVAP published Regulation No. 33 on Reinsurance, which aims to implement the provisions of the Insurance Code as modified by the adoption of the EU Reinsurance Directive (2005/68/EC). The regulatory framework is complex, with its 143 articles detailing and providing in particular for:

- the exclusive conduct of reinsurance activities by companies with a registered office in Italy or Italian branches of companies with registered offices abroad (or both);
- the procedures for authorising such activities; and
- licensing for companies that have a registered office in Italy and authorisation to conduct reinsurance activities and to carry on such activities in other EU member states under the applicable regulations on freedom of establishment and freedom to provide services.

This regulation has been obligatory for all reinsurers operating in Italian territory since 1 September 2010.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There are no requirements and restrictions governing the amount of ceded reinsurance; this depends on the reinsured company's capacity, its margin of solvency and other contingent business decisions.

Typically, Italian fronting companies retain at least a minimum percentage of risk between 1 and 5 per cent of the overall risk, but it is not uncommon to have policies reinsured 100 per cent.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

In Italy, only licensed or accredited reinsurers can provide reinsurance. Therefore, there is no need for collateral to allow a deduction from the liabilities stated on the reinsured company's statutory financial statement. However, collateral might become necessary with a retrocessionaire (reinsurer of a reinsurer) of the reinsurer that is neither licensed nor accredited. In this case, the retrocessionaire must provide some form of collateral to allow a deduction from the liabilities carried on the reinsured company's statutory financial statement.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Regulatory requirements for cedents to obtain credit for reinsurance on their financial statements has been given by IVASS on the basis of the EIOPA guidelines on the system of prospective evaluation of risks for the Solvency II test.

According to these directions, Italian companies shall determine a variation of the solvency margin in light of risks ceded, and they could get facilitations on their financial statements, depending on how they have structured their reinsurance programmes and the rating of their reinsurers, which will 'lighten' the companies' counts for the definition of the solvency margin.

Of particular interest in this respect is the IVASS letter dated 24 March 2015 to the market. In this communication IVASS drew the attention of Italian insurance companies to the EU Delegated Regulation No. 2015/35 of 10 October 2014, supplementing Directive 2009/38/EC implementing the provisions of Solvency II, which, since 1 January 2016, have direct application at the national level.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Chapter IV (articles 245 to 265) of the Private Insurance Code provides for the administrative compulsory winding-up of insolvent or financially troubled insurance and reinsurance companies.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

There is no priority for claims in an insolvency proceeding against an insurance or reinsurance company, and the claimants participate in the company bankruptcy on an equal footing. The sole exception to this rule is contained in article 1930 of the Civil Code, according to which, in the case of insolvency of the reinsured, the reinsurer shall pay the full indemnity but net of the due premiums and pre-deductions of other receivables.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The RUI was set up by the Private Insurance Code, implementing Directive 2002/92/EC on Insurance Mediation, and is governed by ISVAP Regulation No. 5 of 16 October 2006. According to such regulations for the protection of consumers, any insurance and reinsurance intermediation activity has been reserved solely to the persons listed in the RUI.

Based on the Private Insurance Code, the Register is divided into five sections, as follows, and no intermediary may be recorded in more than one section:

- section A for insurance agents;
- section B for brokers;
- section C for direct canvassers of insurance undertakings;
- section D for banks, financial intermediaries as per article 107 of the Consolidated Banking Law, stockbroking houses and the banking division of the Italian Post Office; and
- section E for collaborators with the intermediaries registered under sections A, B and D conducting business outside the premises of such intermediaries.

Just before its dissolution, the ISVAP sent the RUI a list of intermediaries either residing or having a head office situated in EU member states. This special section contains information on natural persons and companies duly licensed as insurance and reinsurance intermediaries in other EU or EEA states who have also been licensed to pursue insurance mediation in Italy, either on freedom of establishment or freedom of services.

Today, article 182 of the Insurance Code assigns to IVASS the duty to ensure that insurance intermediaries comply with the principles of clarity, recognition, transparency and fairness of advertising and information on the conformity of the insurance contract in advertising and in the pre-contract negotiations (informative note) and in the execution of the insurance contract (policy conditions). In this respect, the former Italian regulator issued Regulation No. 35 of 26 May 2010 providing specifically for the level of information to be provided to the prospective insured, and produced a simplified, standardised information note in order to facilitate an understanding of the products on offer and their comparability.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

In general, no third party has any privity to the insurance contract in cases of liability insurance; thus, third parties have no right of action.

Only in exceptional and very limited cases, when the policyholder or insured entity remains inactive with the risk of having the right to indemnity time-barred, may a third party subrogate itself, according to article 2900 of the Civil Code, into the policyholder or insured rights and claim the insurance coverage.

Further exceptions to the mentioned rule are the special provisions of Law No. 990/69 on Compulsory Motor Accident Insurance, article 149 of the Private Insurance Code (see Constitutional Court judgment No. 180/2009) and very recently Law No. 24, article 12 of 8 March 2017 regulating Medical Malpractice.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Article 1913 of the Civil Code provides that notice must be given within three days of the loss or within three days from the day on which the insured entity received notice of the loss.

A lack of notice or late notice does not permit the insurer to deny liability unless prejudice has been suffered, and in this case the denial shall be proportional so as to reflect the prejudice suffered. The onus of proving the prejudice rests with the insurer.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

No specific sanction is provided for wrongful denial of a claim, but because litigation usually follows, the court might then be entitled to award not only the judiciary interests from the date of the judgment, but from the date in which the indemnity was due to the date of the judgment or to the date of final settlement. In some cases of property insurance, the courts considered it legitimate to award the interests provided for by Legislative Decree No. 231 of 9 October 2002, which, at present, stands at the European Central Bank annual interest rate plus 8 per cent (since 1 July 2016, the interest rate has been 8 per cent).

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Article 1917 of the Civil Code on liability insurance contracts provides that a claim made by a third party by way of registered letter or service of a writ of summons that is notified to the liability insurer triggers the latter's duty to defend the claim.

The duty remains until the liability insurer has exhausted the policy limits, in which case the liability insurer shall be obliged to defend until the end of the proceeding degree. The duty to defend also triggers a sub-limit for defence costs, equal at least to one-quarter of the policy limit. If the judgment or arbitration award exceeds the policy limit, the defence costs are apportioned between the insurer and the insured according to their respective interests.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

For all non-liability insurance, the insured event or the loss occurrence triggers the insurer's payment obligations if the insured knew of the event or occurrence, or the insured should have known of the event or occurrence.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

No, an insured entity can always deny liability on misrepresentation in the application or proposal form if it has discovered the non-disclosure after the occurrence of loss.

On the contrary, if the insurer discovers the misrepresentation before any loss occurs, then it has three months to rescind the contract; if the contract is not challenged in time for a declaration of nullity, then any insurer has no right based on the misrepresentation or non-disclosure in the application or proposal form.

28 Punitive damages

Are punitive damages insurable?

The Supreme Court of Cassation, in its leading precedent No. 1183 of 19 January 2007, recently restated in judgment No. 1781 of 8 February 2012, declared punitive damages alien to the Italian system and therefore contrary to public policy. However, in its very recent ruling, No. 9978 of 16 May 2016, the Court of Cassation dealing with the issue of the enforceability in the Italian legal system of foreign decisions ordering the payment of punitive damages, recognised the judgment and, implicitly, the punitive damages moving away from the traditional approach of its consolidated case law.

Therefore, no insurance can insure punitive or exemplary damages awarded in Italy; even though, it is possible to insure in Italy against punitive damages awarded legitimately in other jurisdictions.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

In Italy, the excess insurer usually includes a 'drop-down clause' providing for this specific case. It is notable that, should this provision not be included, the primary limits will be assimilated into an excess and the excess insurer obligation will guarantee only the proportion of the claim exceeding the primary layer limit.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

When the insured has a self-insured retention or deductible and is insolvent and unable to pay it, the insurer's obligation is to indemnify the loss in accordance with the policy terms and conditions for the amount in excess of the self-insured retention or deductible, unless a drop-down clause providing for this specific case has been expressly negotiated.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

The existence of multiple claims under the same policy can have different effects depending on whether the claimant is the same person or there is a more than one claimant.

In the first case, the guarantee will indemnify the oldest claim first, up to the most recent claim, until the policy limit is exhausted.

Whenever there is more than one claimant, all of them are covered by the indemnity policy, which is divided in proportion to the level of each respective claim.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

In a situation technically defined as indirect co-insurance, each and every insurer will concur on the indemnity in proportion of its policy limit (that is, its share of interest in the risk). In this situation there is no joint and several liability; therefore, the insured should recover the respective indemnity from each of the insurers, but it might also be able to get all the indemnity from one insurer who then will have the right of recourse against the other insurers for their quota shares. If one of the insurers should become insolvent, its quota share shall be divided among all the remaining insurers in proportion to their policy limits.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Disgorgement or restitution claims are unknown in Italy and, because more often than not such claims are the consequence of a wrongful or wilful conduct, they would be excluded in accordance to article 1901 of the Italian Civil Code, which excludes insurance operativity for any loss or damage caused wilfully by the insured.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

A single event resulting in multiple injuries or claims constitutes a plurality of occurrences under an insurance policy, unless the insurance contains a 'claim series clause'. Such clause is usually contained in a product liability insurance policy, and is a provision that takes all product losses related to a given product and contractually classifies them as a single loss.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Wilful or gross negligent misrepresentation of a risk can ground the unilateral rescission of the insurance contract in accordance with article 1892 of the Italian Civil Code; the same law provision indicates that wilful or grossly negligent misstatements can ground the claim dismissal if the loss took place before the misstatement is communicated to the insurer and the latter had the opportunity to decide to attack the contract as null and void.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

In Italy, it was traditional to resolve eventual disputes arising from reinsurance agreement interpretation, execution or breach by negotiation or with the services of a mediator. However, this traditional approach has been abandoned in recent years as arbitration, and especially litigation in court, are occurring more and more frequently.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

The most commonly disputed issues are the execution of the reinsurance agreement and the method of calculating damages. Good faith issues in 'follow the fortune' contracts as well as misrepresentation of the reinsurance risk have been litigated recently along with statute of limitation and scope of the reinsurance contract disputes.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Yes. According to article 823(5) of the Civil Procedure Code, the reason for the decision, even if summarily exposed, is a necessary element of the arbitration award, the omission of which renders the award voidable.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Because arbitration is a private form of justice, arbitrators do not have any powers over non-parties to the arbitration agreement. It should be noted that they have the power, granted to them by article 816-ter of the Civil Procedure Code, to lodge a request with the chair of the competent court to obtain a subpoena to oblige reluctant witnesses to appear in front of the arbitrators and render evidence.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Yes, the losing party can appeal a negative arbitration award according to articles 828 and 829 of the Civil Procedure Code. The appeal is divided into two phases; the first, seeking to vacate the arbitration award, is necessary; second, on the merit of the controversy, is not, and it takes place only if the arbitration award has been voided.

Judicial confirmation of the arbitration award is necessary only if the arbitration was informal; in fact, the award in this case has an efficacy equivalent to a contract, and the party that does not comply with the arbitration award can be sued for breach of contract and damages.

However, no judicial confirmation of the arbitration award is necessary if the arbitration was formal; according to article 824-bis of the Civil Procedure Code, the award has the same efficacy as a court judgment.

Update and trends

In 2017, the profitability of Italian non-life insurers should remain stable and continue the positive underwriting performance in non-motor lines characterised by a firmer rates increase. Motor rates will continue to be soft but should still positively offset the higher claim costs, also maintaining this line of insurance on the profitable side.

In contrast, during the past 12 months (and the trend should continue throughout 2017), the Italian life insurance market suffered a contraction with the sales of unit-linked products falling slowly, but steadily, reflecting the volatility of the equity markets and their underperformance.

Italian insurers seem to have performed well in meeting Solvency II financial requirements. Nonetheless, the negative trend on life insurance and Italian insurers' high exposure to government bonds could affect their credit profiles and change the overall situation. In fact, the unit-linked business generates lower capital exposure to adverse movements in interest rates, equity and credit markets, and Italian insurers may face the risk of further increases in capital being requested to meet the required standards should the European regulators remove the zero-risk weighting for sovereign debt under Solvency II's standard formula.

Brand-new Law No. 24 of 8 March 2017, which lays down provisions on the safety of healthcare as well as on the professional liability of practitioners in health professions, should radically change the medical malpractice landscape over the next two to three years. The new Act works on two levels: (i) bettering the risk management of hospitals; and (ii) reducing the pressure of the liability on the physicians and the other practitioners in health professions by reducing the impact of the 'defensive medicine'. The law imposed the compulsory insurance for both doctors and the other practitioners in the health professions as well as for every hospital. This will open new and potentially profitable markets for insurers who will be able to take advantage of the changes introduced by the law.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Under general provisions at law, a reinsurer's obligations are determined by the scope and extension of the reinsurance agreement. Therefore, in the absence of an express contractual provision to that effect, a reinsurer has no obligation to follow its cedent's underwriting fortunes and claims payments or settlements.

In practice this is not the case, and it is customary for a reinsurer to follow its cedent's underwriting fortunes despite an express contractual provision to that effect in the reinsurance agreement.

The reinsurer has the right to avoid its obligations under a follow-the-fortunes clause in very limited cases, notably:

- when the indemnified or settled claim falls outside the scope and limits of the underlying insurance policy;
- when the cedent company did not oppose legitimate and valid defences to the insured, wilfully assuming liability for a claim that was excluded by the underlying policy; and
- in the event of breach of the claim control clause, or in very limited cases of breaching the claim control or cooperation clause.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

A duty of utmost good faith is implied in reinsurance agreements as in insurance agreements, and it is stricter than the one provided for contracts in general. In particular, non-disclosure during the negotiation phase has substantial consequences for the validity of the insurance and reinsurance, and the duty of utmost good faith continues to have effect during the execution of the contract, requiring the parties to meet timely terms and comply with warranties and conditions.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

No, both are subject to the same set of laws, namely, the Civil Code and the Private Insurance Code.

From the regulatory perspective, the reinsurance companies undertaking facultative and treaty reinsurance are subject to title VI (articles 62 to 67) of the Private Insurance Code and ISVAP Regulation No. 33 of 10 March 2010, which integrated the provisions of the Private Insurance Code as modified by the adoption of the EU Reinsurance Directive (2005/68/EC).

The framework set forth in article 143 of Regulation No. 33 details and provides for all aspects of the reinsurance practice, from the conduct of reinsurance activities by companies with a registered office in Italy or abroad, to the procedures for authorising such activities and the financial securities that have to be demonstrated and maintained during the conduct of reinsurance activities in Italy or other EU member states, under both the freedom of establishment or the freedom to provide services.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

No policyholder or non-signatory to a reinsurance agreement has any privity to the reinsurance contract, and hence has no consequential right of action.

The sole exception to this general rule at law is the existence of a 'cut-through clause' in the reinsurance agreement providing a party not in privity with the reinsurer to have rights against the reinsurer under the reinsurance agreement.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

A reinsurer has no duty to pay a policyholder's claim directly unless this is expressly requested by the liquidator or the trustee of the insolvent company, or a 'cut-through' or 'pass-through' clause exists in the reinsurance agreement. Under Italian law, the contractual obligation arising from reinsurance remains between the reinsurer and the cedent company, even if the latter becomes insolvent and subject to a compulsory winding-up procedure.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The type of notice and information a cedent has to provide with respect to an underlying claim depends on whether the reinsurance is a treaty or a facultative reinsurance.

In treaty reinsurance, information is typically limited to the date of loss and the consequent liabilities and attached administrative and adjustment costs all summarised in the bordereaux.

In facultative reinsurance, information depends on whether there is either a claim control clause or a cooperation clause, or neither, and the duty to notify and provide information or data depends on the clause extension.

Within this perspective, the language of a reinsurance contract not only determines the extent of the cedent's obligations but also affects the availability of remedies to the reinsurer.

In general, delaying relevant information might affect the right to recover under the reinsurance agreement, but the delay should constitute a relevant breach of the contract.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

According to article 1910 of the Civil Code, where there is an underlying loss or claim that triggers multiple policies, with the sole condition that each of the triggered policies is insuring the very same interest, each insurance contributes to the indemnification in proportion to the respective policy limit. In this case, the cedent company cannot allocate the claim or the majority of the loss to just one policy, sparing all the others; all triggered insurances have to contribute in proportion. In this situation, each triggered policy will then activate the facultative applicable reinsurance.

In contrast, in treaty reinsurance it is common to have a 'batch clause' providing that only one excess (or retention) and only one limit applies per loss event, regardless of the number of claims resulting from that underlying loss or claim.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Italian law does not provide for a general right of review with respect to a cedent's claims handling and settlement and allocation decisions; this is why, more often than not, Italian reinsurance agreements have an express contractual provision providing for a right of review and audit.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Commutations are freely determined; therefore, the liabilities related to these are voluntary obligations that fall outside the scope of reinsurance. Thus, the obligation of a reinsurer to reimburse a cedent for commutation payments is limited to the reinsurer's willingness to support the cedent, and there are no strict obligations by law.

However, when the commutation is made between the reinsurer and the cedent, often as a negotiated way to prevent a dispute, the commutation's terms and conditions are obligatory for the reinsurer and their breaches are a source of damages.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

In Italy, ECOs in general refer to damages awarded by a court against an insurer or reinsurer that are outside the provisions of the insurance policy and that are because of the insurer's bad faith, fraud or gross negligence in the handling of a claim. Typical examples of ECOs are punitive damages and losses in excess of policy limits, which are considered against public policy by the Italian courts. In reality, the Italian courts very recently started to award such damages for frivolous litigation or resistance to legitimate claims in accordance with article 96 of the Civil Procedure Code. In these cases, the reinsurer has a full obligation of indemnifying the cedent for such ECOs.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Financial Services Agency (FSA) is the government agency that is responsible for regulating insurance and reinsurance companies under the legal and regulatory framework of the Insurance Business Law (IBL), Law No. 105 of 1995, as amended. The FSA has broad authority to set rules, and to supervise and penalise insurance and reinsurance companies as well as their major shareholders or insurance brokers and agents.

The FSA is charged with the supervision of broker-dealers and asset managers as well as banks primarily under the Financial Instruments and Exchange Law (Law No. 25 of 1948, as amended) and the Banking Law (Law No. 59 of 1981, as amended).

Certain administrative functions, such as the insurance broker registration, are delegated to regional financial bureaux subordinated to the FSA.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Foreign companies that are considering establishing a vehicle in Japan to acquire an insurance business licence from the FSA may choose either a subsidiary or a Japanese branch. The subsidiary must take the form of a stock company under the Company Law (Law No. 86 of 2005, as amended). The IBL requires a minimum capital of ¥1 billion.

During the licensing procedure, the FSA examines the company's documents, including:

- the general policy conditions;
- the business method statement;
- the premium and reserve calculation method statement;
- the business projections (generally for 10 years); and
- the CVs of directors.

A licence is not issued unless the FSA is convinced of the credibility of the applicant in terms of sufficient financial assets, human resources and business projections. Formation of a Japanese branch is simpler, but the same licensing requirements apply. In lieu of the minimum capital requirement, the IBL requires the Japanese branch to make a deposit of at least ¥200 million prior to commencing insurance business in Japan.

The preceding rules generally apply to reinsurance companies as well.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

The IBL sets forth three types of insurance business licence, namely life insurance, general insurance and small-amount short-term insurance. The latter is intended for small mutual association-type businesses, which presumably is not an option for foreign entrants into the Japanese mainstream insurance market.

There is no additional licence specifically for the reinsurance business. Foreign reinsurance companies that intend to carry out reinsurance in Japan must acquire a general insurance business licence, regardless of whether the Japanese vehicle assumes the portfolio of general insurance or life insurance from the ceding companies. The licence is not required if foreign reinsurance companies assume reinsurance offshore without reinsurance activities in Japan.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

There are no specific examinations or other qualification requirements. It is expected that the management as a whole has sufficient capability to run insurance or reinsurance companies, with each director or officer having the background relevant to the duties assigned; for example, the compliance officer should have experience as such.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

In addition to the minimum capital requirement noted above, insurance and reinsurance companies are required to meet the solvency margin ratio of 200 per cent. If the ratio drops below 200 per cent, the FSA may issue an order to direct appropriate measures to improve the solvency. Because of practical considerations, such as avoidance of risk to the company's reputation, insurance and reinsurance companies generally maintain much higher solvency margin ratios.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance companies must set forth their method of reserve calculation in respect of each line of their insurance business in the premium and reserve calculation method statement, which is subject to review and approval by the FSA during the licensing procedures. Insurance companies must set aside reserves in accordance with the approved premium and reserve calculation method statement and the regulations set by the FSA from time to time.

Under the IBL, the chief actuary hired by the insurance or reinsurance company is responsible for checking the adequacy of the reserves and recommending that the management takes appropriate actions (eg, capital increase) if any deficiency or other problem is found or expected based on the business projections. The FSA and the chief actuary have meetings to discuss the adequacy of the reserves and other financial matters after the end of each fiscal year and from time to time as necessary.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance products must generally be reviewed and approved by the FSA before they are offered for sale to customers. Certain insurance products for corporate customers are exempted from the approval

requirements. The FSA examines the products from the standpoint of protection of customers as well as public policy. The FSA is the sole agency in charge of insurance product approval.

Certain securities regulations in respect of public distribution (for instance, the suitability test) are built into the IBL and apply to the offer for sale of investment-type insurance products like variable annuities. Compliance with these regulations is supervised by the FSA like any other regulations under the IBL.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Based on the supervisory authorities, the FSA conducts on-site examinations of financial service providers, including licensed insurers and reinsurers doing business in Japan. Typically, each insurer and reinsurer is visited by the FSA examination team once every three to five years. Depending on the nature, scale and complexity of the insurers and reinsurers, the on-site examination period varies, but typically it takes two to three months, followed by off-site monitoring and progress reporting obligations. The scope of examination extends to all functions of insurers and reinsurers, including their market conduct, claims, asset liability management or enterprise risk management (ERM) (or both), and governance and internal control generally, as well as their financial status. From time to time, the FSA also requires reporting on specific matters by individual companies or across the industry.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The permissible types of investment assets are broad; moreover, on 18 April 2012, the FSA lifted the limitations on certain specified asset types, such as a 30 per cent cap on domestic stocks, a 30 per cent cap on any foreign-denominated assets, and a 20 per cent cap on real property where 'xx per cent' means the percentage of the sum invested into that asset category against the total general account assets of the insurer or reinsurer. As such, there is no specific set of regulations or guidelines binding insurers and reinsurers as to investment types in terms of amounts. There are credit limit restrictions that are intended to achieve control over exposure to concentration risks in terms of limitations on capital infusion or other investment into one person or a group of persons.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Prior to the change of control, the acquirer of the majority stock shares in the insurance or reinsurance company must obtain FSA approval to become either an insurance major shareholder or an insurance holding company depending on the asset size of the acquirer: that is, if the value of the acquired stock shares in the insurance company, together with any other Japanese subsidiaries, exceeds 50 per cent of the total assets of the acquirer, the acquirer is deemed to be an 'insurance holding company' for the purpose of the IBL. Otherwise, the acquirer constitutes an 'insurance major shareholder' for the purpose of the IBL. The FSA will examine the background of the directors and controlling persons of the acquirer during the approval procedures.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific restrictions, but the FSA will review the financing of the acquisition while assessing the application for approval (see question 10).

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

Acquisition of a minority interest less than the 'major shareholder threshold' (see question 13) lies outside the scope of the regulatory requirements. However, acquisition of more than 5 per cent of the voting share, and any fluctuation of 1 per cent or greater of the voting share ownership thereafter, must be notified to the FSA within five days, in principle.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

Foreign investment in insurance businesses is not considered to have national security implications. There are no requirements or restrictions from the standpoint of foreign investment control.

All the same, if the foreign investor is to constitute an 'insurance major shareholder', as noted above, it must obtain the FSA's approval before making its investment into the insurance or reinsurance company in Japan. The FSA will conduct a background check on the acquirer, such as an examination of the purpose of the investment and the acquisition finance during the application processing to see whether the investment could hamper the sound management of the insurance or reinsurance company. Ownership of a 20 per cent (or 15 per cent in certain circumstances) voting share in an insurance or reinsurance company is the threshold to qualify as an 'insurance major shareholder'.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The insurance holding company approval (see question 10) is rendered on the assumption that the holding company is capable of establishing, implementing and maintaining governance and control across its group companies. In addition, a group-wide ERM is a key framework that must be implemented by the holding company in an appropriate manner, and the FSA expects that each holding company will establish its ERM framework depending on the nature, scale and complexity of its group-wide businesses. In light of the group-based ERM, each holding company is expected to establish a group-wide policy regarding enterprise risk and solvency assessment and management, while the group insurers and reinsurers are expected to implement solo risk and solvency assessment and management policies, and to make reports to the holding company in an appropriate fashion in accordance with the group-wide policy.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Other than financial reinsurance, parties may execute reinsurance contracts, either treaty or facultative, without obtaining FSA approval. In the case of financial reinsurance, it is the obligation of the ceding company, not the assuming company, to make prior notification to the FSA, which will examine the purpose of the transaction and its effect on the finances of the ceding company.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There are no anti-fronting or other regulations that specifically restrict the amount or ratio of ceded business against the retention. Within the broad powers assigned to the FSA, it may direct the ceding companies to reconsider their risk-taking and reinsurance practice if it believes that the reinsurance is excessive or otherwise not appropriate from the risk management standpoint.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no collateral requirements. Ceding companies may take credit as to the portfolio ceded to qualified reinsurance companies, such as insurance or reinsurance companies with the general insurance business licence in Japan. Collateral is irrelevant to the qualification (see question 18).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

If the business is ceded to insurers or reinsurers licensed in Japan, the ceding companies may generally obtain reinsurance credit. As to businesses ceded to offshore reinsurers without a licence in Japan, there are no concrete requirements for taking on reinsurance credits, such as a collateral requirement or the reinsurer's credit ratings.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Insolvent or financially troubled companies are governed primarily by the IBL and the Reorganisation Law for Financial Institutions (RLFI), Law No. 95 of 1996, as amended (Reorganisation Law). The IBL sets forth the administrative procedures governing insolvent or financially troubled insurance and reinsurance companies. The procedures under the IBL are supervised by the FSA. The Reorganisation Law governs the legal procedures to revitalise insolvent insurance and reinsurance companies under the supervision of the court. After the enactment of the Reorganisation Law, the administrative procedures under the IBL are virtually superseded by the court-sponsored procedures set out in the Reorganisation Law. Reorganisation allows for a number of different methods of business combination, such as stock purchases, asset purchases and mergers involving the insolvent companies.

Laws subordinate to the IBL set forth the policyholder protection funding structure for the purpose of protecting the interests of the holders of insurance policies issued by insolvent insurance companies.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

In the event of the insolvency of life insurers, the holders of life policies and the beneficiaries have a statutory lien over the total assets, and not over specific assets ring-fenced as security for them. In cases of insolvency of property and casualty insurers, no such priority is granted to the policyholders or beneficiaries.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The IBL sets forth two types of intermediaries in insurance distribution or execution of reinsurance contracts, namely insurance agents and insurance brokers. Insurance agents distribute insurance products on behalf of the insurance companies under their direction. They are required to be registered as such at the competent regional financial bureaux. The registration procedures for insurance agents are much simpler than those for insurance brokers, which are described below. Practically speaking, the administration of the insurance agent registration is delegated to the insurance industry associations.

Intermediary activities of banks are regulated under special provisions of the IBL, but they are subject to the same registration requirements.

Insurance brokers intermediate in their capacity as an independent broker. They are also required to be registered at the competent regional financial bureaux. The brokers must have passed the examination sponsored by the brokers' association, which is conducted only once a year, prior to their filing of the application for registration with the regional financial bureaux. The brokers were required to make a guarantee deposit of at least ¥40 million prior to commencement of the broking business. This minimum deposit sum was reduced to ¥20 million during 2014. Reinsurance broking from offshore without conducting broking activities in Japan does not require the insurance broker to register.

Registration under the IBL is required when the person engages in insurance soliciting, but the term 'insurance soliciting' is unclearly defined for practical purposes. (For instance, it is unclear how far telephone receptionists at a call centre contracted by an insurance company can go without needing to register to act as its insurance agent when they talk to customers about the products of that insurance company.)

Finally, claims adjusters may provide services to insurance companies without any licence or registration under the IBL.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Third parties generally may not bring direct coverage actions against insurance companies unless it is specifically provided that they may (eg, victims of motor vehicle accidents against motor vehicle liability insurers). Victims are generally protected against insolvency of the insured to the extent that section 22 of the Insurance Act (Law No. 56 of 2008) provides the victims with statutory lien over the insured's claims for indemnification against their liability insurers.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

An insurer may deny coverage if it has successfully demonstrated extraordinary bad faith on the part of the policyholder in respect of the late notice in breach of the agreed policy wording. Otherwise, the insurer may reduce its claim payment obligation only to the extent of the actual damage suffered due to the late notice, and only after successfully demonstrating because of the actual damage.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

The insurer will owe a tort liability in respect of wrongful denial of a claim. The insurer may also incur an administrative penalty from the FSA, such as a temporary business suspension order. Punitive damages are not available in Japan.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Liability insurers do not have a duty to defend a claim. Liability insurers indemnify policyholders from expenses incurred by them to defend a claim in accordance with the terms of liability insurance policies.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The triggers can be occurrence of losses, discovered losses, claims made, risk attaching or otherwise as agreed in the indemnity policy.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

A life insurer may not allege misrepresentation in the application after the expiry of five years from the execution date of the policy. Moreover, a life insurer may not allege misrepresentation if it fails to contest within one month from the time when it is known to the life insurer.

28 Punitive damages

Are punitive damages insurable?

It is generally thought that punitive damages are not insurable. Punitive damages are generally not awarded or enforceable by courts in Japan.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

The law does not impose such an obligation on the part of the excess insurers. In practice, it is not unusual for the parties to specifically set forth in the excess of loss cover contract wording as to whether the excess insurers owe such an obligation.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

If an insurer agrees with the insured that it shall absorb the first layer of loss and the insurer shall pay the excess, the subsequent insolvency of the insured where it may not bear a retention or deductible would not affect the insurer's obligation to cover the excess as agreed with the insured.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There are no statutorily or judicially determined rules.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Section 20 of the Insurance Act provides that if a risk is covered by policies issued by multiple insurers, the insured person may recover from any such policies up to their respective full insured sum, up to the full amount of the loss. Once the payment is made by one insurer, the allocation will be made among the multiple insurers on a pro rata basis.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Restitution as compensation for damage in tort or breach of contract generally is covered by liability insurance, while disgorgement is excluded.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The courts would follow the definition of 'occurrence' as specified in the relevant policies. For instance, if a policy sets out that an 'occurrence' includes an occurrence in respect of bodily injury, an accident, or a continuous, intermittent or repeated exposure to substantially the same general harmful conditions that causes or allegedly causes the bodily injury, then the multiple injuries or claims allegedly caused by such 'an accident or a continuous, intermittent, or repeated exposure to substantially the same general harmful conditions' would be deemed to constitute a single 'occurrence' for the purposes of the policy. The question for the court would then come down to fact-finding on such 'accident' or 'exposure', rather than counting the injuries or claims.

Update and trends

Amending legislation (Law No. 65 of 2015) of the Act on the Protection of Personal Information is anticipated to take effect in the second quarter of 2017. The amended law is intended to strengthen the protection of personal information in certain areas, such as cross-border data transfer. The Personal Information Protection Commission, which is the newly established governmental agency with the centralised supervisory functions to ensure data protection compliance in all businesses, including (re)insurance undertakings, has already published supervisory guidelines. Among other things, the amended law specifies that the data protection provisions shall apply in an extraterritorial fashion. Offshore entities, which do not own permanent establishment in Japan, shall nonetheless comply with the data protection provisions of the Act to the extent that they use Japan-sourced personal information having been acquired in connection with the provision of services to individuals who are the subject of the personal information. The amended law will also impose stricter requirements for cross-border data transfer. In principle, unless the offshore data recipients are subject to equivalent data protection enforcement, the data holders who are to transfer the personal information must acquire the prior consent of the individuals who are the subject of the relevant personal information.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

If the misstatements are made with knowledge or with gross negligence on the side of customers without any inducement or other intervention by the intermediating sales agents and without the insurer's knowledge of the misstatements, the policy may be cancelled by the insurer. As to the incontestability period, see question 27.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Given the nature of the reinsurance market (where risks are transferred to each other in what is a small community), formal reinsurance disputes are rare. Quite often, insurers opt to reach business solutions without formal proceedings.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Typically, disputes relate to the scope of coverage, which sometimes is written in vague terminology or industry jargon, the meanings of which are not necessarily clear.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

If the arbitration clause in a reinsurance contract sets forth that the arbitration panel shall issue a written and reasoned award, the panel will include the reasoning for the decision in the arbitration award. Otherwise, it is up to the arbitrators whether to include the reasoning of the decision in the arbitration awards.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitrators do not have any powers over non-parties to the arbitration agreement in respect of the arbitration proceedings.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Japanese courts will generally honour arbitration clauses in reinsurance contracts (like any other commercial agreements) and arbitration awards issued by the agreed panel. Foreign awards may be brought to the Japanese courts for enforcement in Japan.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Without express contractual provision, the reinsurer is not obliged to 'follow the fortunes' of the ceding company unless the circumstances demonstrate that such a practice is established (and, therefore, the parties are deemed to have agreed to cede and assume the risks based on that practice in addition to the express terms and conditions in the reinsurance contract). Even if such an obligation exists on the part of the reinsurer, it may try to refuse payment based on gross negligence in claims settlements on the part of the ceding company if there is material deviation from the generally accepted prudent and professional manner.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The ceding company is expected to take reasonable care in claims settlements, and the level of such reasonable care will be determined based on the industry standard, not the notional ordinary commercial standard. The ceding company is also expected to act in good faith in entering into reinsurance contracts. However, it is not considered to be a duty of utmost good faith.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There is no different set of statutes for facultative reinsurance and treaty reinsurance, but the court will consider the difference of the two types in deciding reinsurance disputes.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

A policyholder or non-signatory may not bring a direct action against the reinsurer.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The reinsurer must discharge its own liability against the insolvent ceding company under the terms and conditions of the reinsurance contracts, regardless of whether the liability of the ceding company against its policyholders is reduced in the reorganisation proceedings. Practically speaking, the reinsurers will have the opportunity to negotiate commutation of the assumed portfolio with the reorganisation trustee of the insolvent ceding company in charge of collection from the reinsurers.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The ceding company must provide notice and information as set forth in the reinsurance contract that will vary depending on the type of the reinsurance; for example, treaty versus facultative or the reinsured risks.

It is not unusual that the reinsurance contracts require timely delivery of all material claim-related information, including the information about the contested claims, together with reasonable supporting documents, and also set forth the consequence of failure by the ceding company to make timely delivery of the required notice and information.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

There are no statutorily or judicially determined rules other than section 20 of the Insurance Act (see question 32). Reinsurance contracts can set forth the manner of claim allocation among multiple

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reinsurance contracts differently from section 20. If such an agreement is made, the agreed manner of allocation will govern the relevant reinsured and the reinsurers.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

There are no specific rights of review afforded to reinsurers by statutes. There are no judicially established rules.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

There are no specific statutorily or judicially established rules. Practically speaking, the reinsureds will advise the reinsurers of the terms of commutation prior to its execution and obtain their consent.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

ECOs of a ceding company are typically specifically excluded from the reinsurance liability.

Korea

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

In Korea, the Financial Services Commission (FSC) is vested with authority to actively supervise the business activities of insurance and reinsurance companies through licensing, approval or regulation of certain activities. The FSC is a national administrative agency falling under the jurisdiction of the Office of the Prime Minister of Korea, established pursuant to the Act on the Establishment, etc of the Financial Services Commission (FSC Act) to principally carry out financial supervisory and regulatory duties. With respect to insurance and reinsurance businesses, the FSC is responsible for the licensing of insurance and reinsurance businesses; the establishment and amendment of the Insurance Business Act (IBA), its enforcement decrees, its enforcement regulations and subordinate insurance supervisory regulations; and overall supervision and regulation of insurance and reinsurance businesses. For that purpose, the FSC may issue necessary orders affecting every level of an insurance company's operations, require an insurance company to submit documents and have the Financial Supervisory Service (FSS) review them, and also investigate individuals suspected of violating the IBA and related laws and regulations.

The FSS is a special purpose, zero-capital corporation established pursuant to the FSC Act, and is responsible for the examination and supervision of insurance companies under the guidance and supervision of the FSC. In particular, the FSS examines the affairs and status of assets of insurance companies and, depending on the results of the examination, it may sanction insurance companies. The FSS also supports the FSC and its subordinate agencies in the performance of their duties.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

To engage in the insurance or reinsurance business, an insurance business licence must be obtained before commencement of business. Persons qualified to obtain an insurance business licence are joint stock companies, mutual companies and foreign insurance companies. The establishment of insurance companies in the form of a joint stock company is based on the Commercial Code, while the establishment of insurance companies in the form of a mutual company is based on the IBA.

A person (company) who intends to engage in the insurance or reinsurance business has to obtain a licence from the FSC for each category of insurance business. The types of insurance businesses are broadly categorised into life insurance business, casualty insurance business and 'third category' (miscellaneous other) insurance business, and a person (company) who has received a licence for any such insurance business category is deemed to have received a reinsurance licence for the same insurance business category.

To apply for a licence, the applicant has to file an application with the FSC, together with a copy of its articles of incorporation, business plan (including pro forma financial statements for the first three years), basic business documents (including standardised contracts, a manual on business operations and a manual on calculation of insurance premiums and reserves) and other documents prescribed by Enforcement Decree. The FSC has to review and decide whether to grant a preliminary licence within two months after receiving such application and documents. If the person (company) of receiving preliminary licence satisfies the conditions prescribed by the preliminary licence and thereafter applies for a principal licence, the FSC is required to grant such principal licence.

The insurance business licensing requirements for a domestic insurance company are as follows:

- the company must maintain the minimum amount of paid-in capital or funds (ie, at least 30 billion won or two-thirds of such amount if the company solicits insurance contracts using means of communication, such as telephone, mail, computer network or etc);
- the company must maintain specialised personnel and material facilities necessary to engage in the insurance business;
- the company's business plan must be reasonable and sound; and
- the company's large shareholder must be qualified as an 'officer' of the company under the Act on Corporate Governance of Financial Companies (ACGFC), and must also have adequate capital contribution capability and sound financial condition, and must not have previously engaged in conduct that harmed the sound economic order.

The insurance business licensing requirements for a foreign insurance company are as follows:

- the company must maintain the minimum amount of working capital (ie, at least 3 billion won);
- the company must maintain specialised personnel and material facilities necessary to engage in the insurance business;
- the company's business plan must be reasonable and sound;
- the company must be engaged in the same insurance business, pursuant to foreign laws and regulations, in which it intends to engage in Korea; and
- the company's status of assets, financial soundness and operational health must be adequate for it to engage in the insurance business in Korea, and recognised internationally.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

No licence, authorisation or qualification, other than an insurance business licence (see question 2), is required for insurance and reinsurance companies to conduct business in Korea. If a reinsurance company obtains a licence for a certain insurance business category, it is deemed to have received a reinsurance licence for the same insurance business category.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The ACGFC governs qualifications with regard to the 'officer', defined as a director, statutory auditor, executive officer (limited to the cases

where an executive officer appointed under the Commercial Act exists), or operating officer of insurance companies and must be persons who do not fall under any of the following:

- a person who is a minor, a person under adult guardianship, or a person under limited guardianship;
- a person was declared bankrupt and has not yet been reinstated;
- a person was sentenced to imprisonment without labour or a heavier punishment, and five years have not yet elapsed since he or she completed, was deemed to have completed, or was exempted from the sentence;
- a person was sentenced to the suspension of imprisonment without labour or a heavier punishment, and is still in the suspension period;
- a person was sentenced to a criminal fine or a heavier punishment under the ACGFC or any other finance-related statute, and five years have not yet elapsed since he or she completed, was deemed to have completed, or was exempted from the sentence;
- a person is, or was, an officer or an employee of a financial company (limited to persons specified by Enforcement Decree of the ACGFC as directly liable for the cause of such measures or those reasonably responsible for such measures), and five years have not yet elapsed since any of the following measures were taken against the company:
  - revocation of permission, authorisation, or registration for business under a finance-related statute;
  - a measure of timely correction under the Act on the Structural Improvement of the Financial Industry (ASIFI); and
  - an administrative disposition under the ASIFI;
- a person was subject to sanction under the ACGFC or any finance-related statute for his or her conduct as an officer or employee (or a notice equivalent to the sanction in the case of a retired or resigned person), and the period specified by the Enforcement Decree of the ACGFC within the maximum of five years for each category of sanctions has not yet passed since he or she was subject to sanction; or
- a person is designated by the Enforcement Decree of the ACGFC because public interest and sound management of the relevant financial company or credit order are likely to be undermined.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

In principle, insurance or reinsurance companies may engage in the insurance or reinsurance business after contributing a minimum of 30 billion won in paid-in capital or funds. However, if an insurance or reinsurance company intends to engage in only parts of the insurance business categories prescribed in the IBA, then the minimum amount of paid-in capital to be contributed varies according to business category: 30 billion won in the case of reinsurance business, 20 billion won in the case of life insurance, pension insurance and motor vehicle insurance business, and 10 billion won in the case of fire insurance, liability insurance and accident insurance business. If an insurance or reinsurance company engages in two or more insurance business categories, then the minimum paid-in capital amounts for all of them is combined, but if the combined total amount is more than 30 billion won, the minimum paid-in capital amount is capped at 30 billion won. If an insurance or reinsurance company solicits customers through telecommunication, such as by telephone, email or computers, as prescribed by the Enforcement Decree, then it may engage in the insurance or reinsurance business after contributing the equivalent of two-thirds of the minimum amount of paid-in capital or funds (ie, 30 billion won).

If a foreign insurance or reinsurance company intends to engage in insurance or reinsurance business in Korea, the minimum amount of working capital required is 3 billion won.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance and reinsurance companies are required to comply with the following standards on financial soundness prescribed by the Enforcement Decree of the IBA in order to ensure its ability to pay out insurance proceeds and the soundness of its operation:

- a payment reserve ratio (payment reserve amount divided by payment reserve standard amount) of 100 per cent or higher;
- accumulation of loss reserves of a certain ratio or higher; and
- compliance with standards on insurance companies' risk, liquidity and reinsurance management established and notified by the FSC.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance companies are required to prepare basic documents on insurance products that they intend to handle, and when an insurance or reinsurance company intends to prepare or change such basic documents, it may be required to file a report with the FSS depending on the type of insurance product provided.

Products where the basic documents must be reported (reporting products) are insurance products that fall under one of the following categories:

- if a new insurance product is introduced or subscription to an insurance product is mandated pursuant to an enactment or amendment of law;
- if an insurance company solicits customers through a financial institution as an insurance retailer; or
- if an insurance product is prescribed by the Enforcement Decree as required for the protection of insurance policyholders.

For reporting products, the insurance company has to file a report with the FSS by no later than 30 days before the scheduled date for implementation of the basic documents. The FSS then has to review the soundness of the reporting product, then either provide notice that the report has been accepted or recommend a modification of the reporting product within 20 days of the report being received.

In principle, the basic documents of products that do not fall under any of the categories as described above do not have to be reported to the FSC in advance. However, the FSC may require insurance companies to submit materials related to the basic documents of such products in cases where the FSC deems such submissions necessary with respect to protection of insurance policyholders and other relevant factors equivalent to such.

The standards for the review of insurance products are prescribed by the Guidelines on Review of Insurance Products, which are a type of enforcement rule of the FSS.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Insurance companies are required to close their accounting books on 31 December of each year and submit their financial statements, including supplementary details, and business reports to the FSC within three months from the account book closing, and submit a report stating the monthly business details to the FSC by the last day of the following month.

In addition, insurance companies are required to report the following matters from time to time. If an insurance company comes to hold a subsidiary, it must submit the articles of incorporation of the subsidiary and other documents prescribed by an Enforcement Decree to the FSC within 15 days of the date on which it came to hold the subsidiary, and submit the balance sheets of its subsidiaries and other documents prescribed by Enforcement Decree to the FSC within three months of the end of the business year of such subsidiary. If an insurance company amends its articles of incorporation, it must inform such amendment to the FSC within seven days of the amendment.

Moreover, insurance companies must report any of the following to the FSC within five days of its occurrence:

- a change in its company or trade name;
- the suspension or resumption of business of its head office;
- a change of its largest shareholder;
- a change in the number of shares held by its large shareholders by an amount of 1 per cent or more of the total number of issued voting shares of the company;

- an increase in capital or funds;
- a resolution to change its organisation;
- any punishment or sanction under the IBA;
- any tax delinquency or punishment for violating tax laws;
- any overseas investments under the Foreign Exchange Transactions Act or the establishment of places of business and other offices in foreign countries; or
- any litigation against the insurance company by a shareholder or a former shareholder

Also, according to the ACGFC, the insurance companies must report an appointment or dismissal of an officer to the FSC without delay.

Finally, the FSC may order insurance companies to submit a list of their shareholders or a report of their business (and related materials) in connection with the inspection obligation of the FSC under the IBA to protect public interest and the policyholders. In conjunction with such inspection, the FSS may, as necessary, require an insurance company to file a report on its business or assets, submit relevant material, procure the personal appearance of relevant employees and provide a testimony. The inspector must carry his or her credentials and display these to relevant persons. Once the inspection is complete, the FSS must take necessary measures pursuant to the result of the inspection and report its findings to the FSC. The FSS may also require an external auditor of an insurance company to submit any information the external auditor may have come to learn as a result of an external audit or other information regarding management practices of the insurance company.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Insurance companies must ensure stability, liquidity, profitability and the public interest in managing its assets, and must manage their assets in accordance with the duty of care.

Insurance companies may not manage their assets in the following manner:

- possession of real estate (excluding any real estate acquired by exercising a security right such as a mortgage) other than for business purposes;
- possession of real estate through special accounts;
- provision of loans for speculation in goods and securities;
- provision of loans, directly or indirectly, for purchasing their own shares;
- provision of loans, directly or indirectly, for political funds;
- provision of loans to their executives or employees; and
- foreign exchange transactions or derivatives trading that do not satisfy conditions set by the FSC.

In addition, there is a limitation on the ratio of the total assets that insurance companies may commit to specific investments (such as granting credit to the same entity, owning bonds and stocks of the same entity). The limitation ranges from 3 to 30 per cent of the total assets in the case of general accounts, and 5 to 20 per cent in the case of special accounts for retirement insurance contracts. However, insurance companies are exempt from the foregoing limitation by approval from the FSC if there has been a change in asset status owing to any change in the price of their assets, the exercise of security rights or other involuntary reasons, if such exemption is necessary to comply with the financial soundness standards under the IBA, or if such exemption is necessary to protect the interests of policyholders.

Also, insurance companies may not own more than 15 per cent of voting shares of any other company. Moreover, insurance companies may not swap their voting shares for those of another financial institution or another company to avoid the above-described asset management limitations or restriction on acquisition of own shares, and insurance companies may not exercise the voting rights attached to the shares so acquired.

Insurance companies are also prohibited from directly or indirectly extending credit to their large shareholders for investment in another company, and from gratuitously transferring their asset or otherwise purchasing, selling, exchanging or entering into reinsurance contracts under terms that are clearly unfavourable to them compared with prevailing industry standards. Finally, if an insurance company intends to extend credit to its large shareholder or acquire bonds or shares issued by its large shareholder in an amount greater than 0.1 per cent of its shareholders' equity or 1 billion won (whichever is less), such transaction must be subject to a unanimous resolution of the board of directors.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

The 'large shareholder' refers to a legal person falling under any of the following:

- a person and any related parties of such person who collectively hold the largest number of the issued and outstanding shares with voting rights of the insurance or reinsurance company, regardless of in whose name the shares are held, as long as they are held beneficially for such person;
- a person who holds 10 per cent or more of the total issued and outstanding shares with voting rights of the insurance or reinsurance company; or
- a shareholder who actually exercises influence over major business matters of the insurance or reinsurance company through the appointment of officers or otherwise.

A legal person who plans to become the large shareholder of an insurance or reinsurance company through the acquisition of shares must not posess any aspect that disqualifies the legal person as an officer under the ACGFC (see question 3). Such legal person must have sufficient investment capabilities and sound financial standing with no history of disturbing sound economic order, and also must obtain prior approval from the FSC under the ACGFC.

A legal person wishing to become a large shareholder, and its representative, its largest shareholder, and a shareholder who actually exercises influence over major business matters of such legal person are subjected to evaluation for the approval. For a legal person wishing to become the largest shareholder, related parties are also subjected to the approval. Each party is subjected to different set of requirements, and such requirements differ based on nature of the legal person (ie, whether the legal person is a natural person or a company, and whether a company is financial institution, PEF, or others, etc), or nationality of such legal person, etc.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The Enforcement Decree of the ACGFC prescribes the requirements for approval to change the large shareholder of an insurance or reinsurance company:

- if the large shareholder is a domestic financial institution, it has to satisfy the financial soundness standard prescribed by the FSC, and if such institution is an affiliate of the enterprise group subjected to limitations on debt guarantees or mutual contribution under the Monopoly Regulation and Fair Trade Act, the ratio of debt financed by affiliates of the enterprise group (debt financed by affiliates of the enterprise group divided by total amount of debt) must be under 300 per cent (or lower if the FSC sets forth otherwise);
- if the large shareholder is a domestic corporation other than a financial institution, it has to satisfy the standards prescribed by the FSC with a debt-to-equity ratio of less than 300 per cent (or lower if the FSC sets forth otherwise) as of the most recent fiscal year end and capital financed as debt should not be more than two-thirds of total capital for acquisition of the stocks at stake;
- if the large shareholder is a financial institution, it has to satisfy the 300 per cent debt-ratio standard and also a financial-soundness standard prescribed by the FSC; and
- if the large shareholder is a foreign corporation, it has to obtain a credit rating of investment grade or higher from an internationally recognised credit rating institution or satisfy the financial soundness standards prescribed by the supervisory authority of the foreign corporation's country.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no specific restrictions on acquiring a minority interest in an insurance or reinsurance company.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

The Regulations on Foreign Investment and Introduction of Technology (Ministry of Trade, Industry and Energy (MOTIE) Notification) contain a list of the business categories from which foreign investment is excluded or restricted, but such list does not include the insurance and reinsurance business. The Foreign Investment Promotion Act (FIPA), a law of general application on foreign investment in Korea, applies when a foreigner intends to acquire and own shares or equity interest in a domestic company, and under the FIPA, a foreigner who intends to invest in a domestic company, including an insurance or reinsurance company, has to file a report with the MOTIE.

Meanwhile, for a foreign company to acquire shares of a domestic insurance company and become its large shareholder, it must obtain prior approval of the FSC and satisfy the following conditions:

- it must be engaged in the insurance business at the date of the application for approval;
- it must receive an investment-grade rating from an internationally recognised credit rating agency or be recognised as financially sound by the regulatory agency of its home country;
- it must not have been subject to a warning, or more severe administrative sanction, from the regulatory agency or subject to a fine or more severe criminal sanction in its home country in connection with its financial business during the preceding three years;
- it must not have been subject to a criminal sanction equivalent to, or more severe than, a fine for violating the finance, antitrust or tax-related laws during the preceding five years;
- it must not have undermined soundness of financial order (eg, by defaulting on obligations) during the preceding five years;
- it must not be the large shareholder of, or be specially related to, a financial institution that has been designated as insolvent or whose licence, permit or registration was revoked pursuant to relevant laws (unless it is subject to specific exemptions as prescribed by the FSC, such as being found not to be responsible for such insolvency by the court or taking economic responsibility for such insolvency); and
- it must not have undermined the soundness of the financial transaction order as determined by the FSC.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The Monopoly Regulation and Fair Trade Act regulates large enterprise groups designated by the Korea Fair Trade Commission. Companies belonging to such large enterprise groups are subject to the following restrictions on guaranteeing loans to other companies:

- prohibited from mutual investment;
- must pass a resolution of the board of directors and publicly disclose any large transactions with each other;
- must publicly disclose material information on private companies within the enterprise group; and
- must publicly disclose general matters regarding the enterprise group.

As such, an insurance company belonging to a large enterprise group would also be required to comply with the foregoing. In addition, a financial company or an insurance company belonging to an enterprise group is, in principle, prohibited from exercising the voting rights attached to the shares it owns in other companies within the same enterprise group; this is because the basic purpose of shareholding in another company by a financial company or an insurance company is to maximise performance of the entrusted investment assets, and the possibility of such companies becoming a de facto holding company controlling the operation of its affiliates must be prevented.

An insurance company that has a holding company as the large shareholder may also be subject to the Financial Holding Companies Act (FHCA), which regulates the establishment, shareholding, business, inclusion of subsidiaries and operation of a financial holding company that controls financial companies or companies otherwise closely related to financial business. The FHCA provides whether or not a company that satisfies the conditions can become a financial holding company. A financial holding company is a company whose primary business is to control companies carrying on financial business or other companies closely related to the operation of financial business through the ownership of their stocks according to the standards prescribed by the Enforcement Decree. Such company must receive authorisation from the FSC and must meet the following criteria:

- it shall control at least one financial institution
- its total assets shall be not less than 500 billion won; and
- it shall obtain authorisation from the FSC under the FHCA.

A financial holding company that controls one or more financial institutions, including an insurance company, is defined as an 'insurance holding company (non-banking holding company)'. The FHCA provides specific regulations regarding insurance holding companies. Insurance holding companies must satisfy additional conditions to those required of financial holding companies in securing authorisation of the establishment of an insurance holding company and inclusion of subsidiaries, as well as regarding the control of subsidiaries, subsidiaries of subsidiaries and other companies.

Any company that meets the requirements for financial holding companies must obtain authorisation from the FSC in accordance with the following standards:

- the business plan as a corporation shall be appropriate and sound;
- the business plan of a corporation that is to be subsidiary (either directly or indirectly) shall be appropriate and sound;
- large shareholders and related persons shall have adequate investment capacity, financial soundness and social credibility;
- the financial standing and business management of a company that is to be a financial holding company and its subsidiary shall be sound; and
- where it becomes a complete holding company through an all-inclusive stock swap pursuant to article 360-2 of the Commercial Act or an all-inclusive stock transfer pursuant to article 360-15 of the said Act, the swap ratio of stocks shall be appropriate.

In addition, if a financial holding company intends to acquire shares of an insurance company, it must satisfy the requirements prescribed by ACGFC and obtain a prior approval of FSC (see question 10).

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

If a reinsurance company obtains a licence for a certain insurance business category, it is deemed to have received a reinsurance licence for the same insurance business category (see question 3). An insurance company is prohibited from entering into a reinsurance agreement with its large shareholder or subsidiary if it is doing so on terms that are clearly disadvantageous to it in comparison with ordinary trading terms.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

The IBA and related regulations do not contain any express restrictions on the amount of ceded reinsurance and retention of risk by insurers. A reinsurance company must accumulate liability reserves for the portions reinsured, and the insurance company covered by reinsurance

must indicate such liability reserves as separate assets if a reinsurance contract satisfies all of the following:
- insurance risks are transferred; and
- the relevant reinsurance contract is likely to cause damage to the company accepting the reinsurance.

Also, the insurance company must reduce its reinsured assets by method prescribed by the FSC if the reinsurance company falls under any of the following methods:
- it fails to satisfy the criteria for financial soundness prescribed by domestic or foreign supervisory agencies; or
- its credit appraisal rating conducted by an internationally recognised credit rating agency (including the credit appraisal rating conducted by a domestic credit appraisal rating agency corresponding thereto) within the past three years is below investment grade, provided that any foreign insurer in which a foreign government rated by an internationally recognised credit rating agency within the past three years as investment grade has invested at least half of the capital shall be excluded herefrom.

The Regulation on the Supervision of Insurance Business by the FSC and its subordinate regulation by the FSS provide standards for evaluation of risk transferred by reinsurance.

Under the Model Standards on the Management of Reinsurance by Insurance Companies, which are supervisory regulations of the FSS, insurance companies are required to deliberate and decide on the establishment or change of their operational strategy for reinsurance through their board of directors or risk the management committee, and to also review their appropriateness from time to time and take appropriate measures. The above operational strategy for reinsurance includes plans for risk retention and ceding of insurance and retrocession of reinsurance, and when an insurance company establishes a plan for risk retention and ceding of insurance, it is required to evaluate the assumed risk and establish a plan for risk retention and ceding of insurance, and when a reinsurance company establishes a plan for retrocession of reinsurance, it is required to confirm whether the estimated maximum loss amount of major risks from the retrocession of reinsurance exceeds its reserves.

Although the regulatory authorities do examine whether the above plan for ceding of insurance and plan for retrocession of reinsurance were properly established, they tend to defer to the insurance and reinsurance companies regarding the appropriateness of such plans, and after such plans have been established, the regulatory authorities are usually concerned only with whether the plans are being implemented as established.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no collateral requirements prescribed by law for reinsurers in a reinsurance transaction.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

A reinsurance company must accumulate liability reserves for the portions reinsured, and the insurance company covered by reinsurance must indicate such liability reserves as separate assets if a reinsurance contract satisfies all of the following:
- insurance risks are transferred; and
- the relevant reinsurance contract is likely to cause damage to the company accepting the reinsurance (see question 16).

With regards to the financial statement of a reinsurance company, a reinsurance contract that does not transfer reinsurance risk must be accounted for as a deposit.

Meanwhile, if the reinsurer either fails to satisfy standards for financial soundness as determined by domestic supervisory agencies or receives a non-investment grade rating from an internationally recognised credit rating agency within the preceding three years, the total amount of the reinsured assets must be reduced (see question 16). However, the amount of such reduction may be reduced by the liability reserves (including both payment reserves and unearned premium reserves) of the relevant reinsurance contract.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Insolvent insurance and reinsurance companies are subject to regulation by the IBA and the Act on the Structural Improvement of the Financial Industry. The IBA provides that insolvency is grounds for dissolution of an insurance company, and an insurance company's insolvency proceedings are regulated by the Act on the Structural Improvement of the Financial Industry. Procedures other than those prescribed by the above statutes are contained in the Act on Debtor Rehabilitation and Bankruptcy, a law that applies to ordinary companies.

According to the Act on the Structural Improvement of the Financial Industry, if the FSC determines that the financial condition (such as the capitalisation ratio) of an insurance or reinsurance company falls below the standards for timely corrective measures, or that the financial condition of an insurance or reinsurance company will clearly fall below the standards for timely corrective measures owing to the occurrence of a financial accident or unrecoverable claim of a considerable amount, the FSC may take corrective measures, including:
- issue a caution or warning;
- a reprimand or order a salary reduction;
- order a capital increase or decrease;
- order a disposal of assets or the reduction of the organisation;
- order a prohibition on the acquisition of assets or restriction of the receipt of the insurance premium;
- order the suspension of an officer's duties and the appointment of a substitute manager to perform such officer's duties;
- order a stock cancellation or merger;
- order the suspension of business;
- order the merger with, or sale to, a third party; or
- order the assignment of contracts.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Insolvency proceedings in Korea place priority on the public interest claims (ie, estate claims), which consist of administrative expenses in connection with the insolvency proceedings. These priority claims include court expenses for the communal benefit of all related parties, expenses for the administration and disposition of insolvency assets, and claims arising out of the trustee's actions following the commencement of insolvency proceedings. Other claims are rehabilitation (ie, bankruptcy) claims, which are repaid in accordance with the relevant insolvency proceedings. Claims for insurance benefits by a policyholder are, in principle, rehabilitation claims that do not have priority.

However, policyholders and beneficiaries have priority in acquiring the amount accumulated for the insured among the assets of the insurance company unless otherwise specifically provided by law. That is, if an insurance company becomes insolvent, unless there are legal provisions to the contrary, policyholders and beneficiaries receive their portion of the residual assets of the insurance company before other creditors. The specific legal provisions include, inter alia, wages and retirement allowances of employees under the relevant labour laws and secured claims. Meanwhile, if the amount accumulated for the insured has been deposited by the insurance company pursuant to an FSC order, the relevant policyholder or beneficiary has priority in recovering such amount even if there are legal provisions to the contrary. However, if an insurance company actually becomes bankrupt, the supervisory authorities protect policyholders by transferring the insurance contracts of the bankrupt insurance company to other insurance companies pursuant to the IBA. Even if another insurance company does not assume the insurance contracts, the Korean Deposit Insurance Company provides compensation of up to 50 million won to policyholders pursuant to the Depositor Protection Act.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

A person who intends to become an insurance or reinsurance broker must register with the FSC. The requirements for registration as an insurance or reinsurance broker are prescribed in the Enforcement Decree of the IBA, and such requirements provide for education (ie, undertaking training sessions mandated by the FSC), work experience in the type of insurance business that the registration is for. If it a company intends to engage in insurance brokerage, one-third of its workers must satisfy requirements above.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

In principle, when an accident covered by insurance occurs, the insurer has to pay insurance proceeds to the insured or the beneficiary according to insurance contract.

However, in the case of liability insurance, the injured third party may directly request an insurer to compensate for losses caused by an accident attributable to the insured, within the limit of the insured amount, povided that an insurer may assert against the third party with a defence that the insured has in connection with the accident. If the insurer receives such request, the insurer must notify the insured thereof without delay. The insured is obliged to cooperate in presenting necessary documents and evidence, making testimony, or calling a witness on the insurer's request.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The insurance policyholder, the insured and the insurance beneficiary are each required to notify the insurer without delay when it obtains knowledge of the occurrence of an accident cover by the insured, and if any loss occurs or increases because of a delay in the provision of such notice, the insurer is not liable for the increased amount of loss from such delay. In principle, it is not possible to refuse payment of insurance proceeds on the grounds that the notice of occurrence of an insurance accident was delayed, but if the right to claim payment of insurance proceeds is not exercised within three years of the date the insurance accident occurred, such right becomes extinguished because of the expiration of the statute of limitations on such claims. Therefore, if the notice of occurrence of an insurance accident and the claim for payment of insurance proceeds are not made within three years from the date when the insurance accident occurred, the insurer may refuse to pay insurance proceeds on the grounds that the right to claim payment of insurance proceeds has expired.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

An insurer may bear contractual and tort liability for wrongfully refusing to pay insurance proceeds, and may also receive a caution, warning, corrective order or other sanctions from the FSC.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The liability insurer does not bear the duty to defend a claim. However, the litigation costs and other costs spent by the insured to defend a third-party claim are usually expressly covered by a policy, and the insured may request the insurer to pay such costs in advance. Further, if a third party claims payment of insurance proceeds directly from the insurer, the insurer is required to notify the insured without delay; furthermore, the insurer may raise defences against the third party that the insured has against the third party.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

Subject to the express terms of the insurance contract, the insurer's payment obligations are triggered as soon as the insurance accident occurs and the insured notifies the insurer thereof. The insurer must pay the insured proceeds to the insured or beneficiary within the agreed period if there is one, or within 10 days after determination of the insured proceeds payable without delay, upon receipt of notification from the insured. However, if the insurance accident occurred owing to bad faith or the gross negligence of a policyholder, the insured or beneficiary, the insurer is not liable to pay the insurance proceeds. Also, if the insurance accident is caused by war or other public disturbances, the insurer is not liable to pay the insurance proceeds, unless otherwise agreed by the parties.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

If the policyholder or the insured, intentionally or through gross negligence, fails to disclose or inadequately discloses material information at the time of entering into an insurance contract, the insurer may terminate the insurance contract within one month of becoming aware of such fact or three years after the date when the insurance contract was executed, whichever is earliest. However, the insurer may not terminate the insurance contract if the insurer knew or failed to know through gross negligence of the material information that the insured failed to disclose at the time of entering into the insurance contract. After such period, the insurer may not terminate the insurance contract based on misrepresentation in the application. Any information requested by the insurer in writing is presumed to be material information. Even if an insurance accident has occurred, and the insurer has terminated the insurance contract for breach of such disclosure requirement above, the insurer is not liable for payment of insurance proceeds, and the insurer may claim the return of any insurance proceeds that has already been paid. Yet, the insurer may also be required to pay the insurance proceeds if it is proven that the insured's non-disclosure did not contribute to the occurrence of the insurance accident.

28 Punitive damages

Are punitive damages insurable?

In Korea, punitive damages are generally not recognised, and at this time, punitive damages have been adopted in a limited way and only for certain areas. Thus far, there is no statutory law, case precedent or authoritative interpretation on the issue of whether punitive damages are insurable, and if punitive damages are more widely adopted in Korea, the issue is likely to be further discussed and implemented.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

'Drop down and defend' excess insurance arrangements are not expressly regulated by law. Therefore, unless such obligation of the excess insurer is not prescribed by the insurance contract, the insurer bears no such obligation.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

If the insurer and the insured agreed to have the insurer cover only the amount in excess of the self-insured retention or deductible then, even if the insured becomes insolvent and unable to pay the self-insured retention or deductible, the insurer's payment obligation remains limited only to the amount in excess of the self-insured retention or deductible as originally agreed.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is no order of priority for payment in such cases prescribed by law, being governed by the provisions of the policy. In practice, if there are multiple claims under the same policy, the insurer pays the claim based on the chronological order as such claims are fully proven according to the policy.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

It depends on the nature of the insurance policy. If multiple insurance contracts have been executed for the same insurance contract purposes and same covered insurance accidents, the insurers are jointly liable each up to the amount of their insurance coverage amount. The ratio of liability among insurers is decided by the ratio of each insurer's insurance coverage amount. However, if it is personal insurance, then the insurance proceeds are a fixed amount in the policy. The insured may request each of the insurers' full amount of insurance proceeds according to the policy.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

The Commercial Code explicitly provides for liability insurance, which is an insurance to 'indemnify for losses incurred by the insured against a third party by perils insured against during the period of coverage'. Accordingly, any indirect loss of the insured because of its liability for compensation of damages to a third party is also a risk that may be covered by an insurance company. Meanwhile, it is not entirely clear whether it is possible to insure against liability for disgorgement of unjust enrichment owing to an accident during the term of insurance as the Commercial Code does not explicitly provide for such liability.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

There is no legal term that directly corresponds to such a concept. Even if multiple losses occur as a result of a single event, the insurer must pay all claims arising out of all actual losses suffered by the insured that are causally related to the event (as determined in the insurance policy) within the scope of the insured amount.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The Commercial Code provides that if the policyholder, or the insured, fails to disclose or insufficiently discloses material facts owing to bad faith or gross negligence at the time of the insurance contract, the insurer may terminate the contract within one month after it becomes aware of such non-disclosure or insufficient disclosure and within three years after the contract was entered into. However, if the insurer was aware of this fact or was unaware owing to its gross negligence, the insurance contract may not be terminated. In addition, the insurer may void the insurance contract pursuant to the Civil Code if the insurer was mistaken as to a matter of fact or was defrauded owing to misrepresentation of the policyholder or the insured in the insurance application.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

In Korea, the reinsurance industry is rather small and transaction counterparties are limited. As a result, when a dispute occurs, it could cause difficulties from a business standpoint. Therefore, when reinsurance disputes occur, the parties often resolve their disputes through negotiation and without resorting to formal proceedings. Owing to this peculiarity of the reinsurance industry, case precedents and examples of disputes that have become public are relatively few.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Since there are relatively few express statutory provisions on reinsurance, for specific cases it is necessary to review the terms and conditions agreed between the parties and customary practice, and as a result, the most common issues that arise involve interpretation of the language contained in the reinsurance contract. In addition, there could be a gap between the time when the underlying insurance contract was executed and the time when the reinsurance contract was executed, and issues involving the scope of coverage of insurance accidents that arise in between such times are also common. Other common issues involve changes to the insurance premium amount and rate under the relevant contract or for the relevant industry after the occurrence of a large insurance accident and the recovery of insurance proceeds.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Under the Arbitration Act, arbitration decisions are required to include the reasoning for the decision. However, if the parties agree not to include the reasoning for the decision, or if the decision is based on the parties' settlement, then it is permissible not to state the reasoning for the decision.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitrators have no authority over persons who are not parties to the arbitration agreement. However, arbitration panels may request a court to conduct an examination to gather evidence.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Since arbitration awards have the same legal effect between the parties as a final, non-appealable judgment of a court, in principle, arbitration awards cannot be challenged. However, an arbitration party can file a suit with a court to have an arbitration award vacated. A court may vacate an arbitration award in either of the following cases:

- first, the party seeking to have an arbitration award vacated proves the existence of any of the following circumstances:
  - a party to the arbitration agreement was not competent to be so at the time of entering into the arbitration agreement;
  - if the arbitration agreement is invalid under the governing law designated by the parties, or under Korean law if there is no designated governing law;
  - if the party seeking to have an arbitration award vacated did not receive proper notice of the selection of arbitrators or regarding the arbitration proceedings, or otherwise was unable to defend the case on its merits;
  - the arbitration award addresses a dispute that is not covered by the arbitration agreement or a matter outside the scope of the arbitration agreement; or
  - the composition of the arbitration panel or the arbitration procedures did not comport with the agreement of the parties or, if there was no agreement, it did not comport with the Arbitration Act; or
- second, a court, by its own authority, may determine that the dispute covered by an arbitration award is not permitted to be resolved through arbitration under Korean law, or that the recognition or

enforcement of the arbitration award is contrary to the public policy or social order of Korea.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

If there is no express contractual provision, then the reinsurer does not bear the obligation to follow its cedent's underwriting fortunes and claims payments or settlements. However, reinsurance contracts typically provide that the reinsurer bears the same coverage obligation as the coverage obligation assumed by the cedent under the ceded insurance contract. In such cases, the reinsurer is required to pay reinsurance proceeds to the cedent for the insurance proceeds paid by the cedent under the cedent insurance contract, according to the same method of payment, unless there are grounds expressly relieving the reinsurer from liability under the reinsurance contract.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The duty of utmost good faith applies generally to all contracts, including insurance and reinsurance contracts. Reinsurance contracts typically contain a provision requiring the parties to act in good faith, as a general condition. The duty of good faith in reinsurance contracts requires the cedent to notify the reinsurer of material facts relating to the reinsurance contract in good faith, and upon breach of such duty, the reinsurance contract may be invalidated.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There is no different set of laws for facultative reinsurance and treaty reinsurance. The FSS and other supervisory authorities view facultative reinsurance and treaty reinsurance as different in terms of transaction form or method of ceding insurance. Therefore, cedents and reinsurers may decide on the method of ceding insurance according to individual negotiations, without any restrictions imposed by any particular law or regulation.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

The provisions on liability insurance under the Commercial Act are to be applied mutatis mutandis to reinsurance contracts to the extent not contrary to their nature. Meanwhile, the provisions shall not be applied mutatis mutandis to the right of a third party to claim insurance proceeds directly to the reinsurer (see question 22), since it is unreasonable to view the ceding insurer under the reinsurance contract in the same way as the injured party under liability insurance, which assumes a function for the protection of the injured party and given that reinsurance is insurance between companies used to reasonably spread risk between insurers. Thus, the right to claim insurance directly from the reinsurer should be denied, removing an express provision in the reinsurance contract allowing the insured under the ceded insurance to bring a direct action against the reinsurer for coverage. In practice, by removing such express provision, the insured under the ceded insurance may not bring a direct action against the reinsurer for coverage.

Update and trends

The FSC has announced that it will permit the issuing of a hybrid bond (perpetual bond) by insurance companies for the purpose of satisfying the financial soundness requirement. The FSC plans to set out the relevant rules in the insurance business regulations. Insurance companies are undergoing anticipatory recapitalisation to prepare for the implementation of IFRS 17 principles, such as the reporting of insurance liabilities on market value. A hybrid bond, which is often mentioned as one of the recapitalisation methods, has the advantage of having a lower priority of subordinate debts in which interest payments on it can be stopped; however, insurance companies have been passive about issuing it because of the concerns that the FSC may not approve.

The FSC also plans to revamp the qualitative criteria for evaluating an insurance company's financial status in order to reflect the new risks and to eliminate the redundant evaluation. The FSC will add criteria on the adequacy of the following:

- product development and sales;
- contract acquisition and management;
- review for insurance proceeds payment; and
- overall management of assets and liability.

Additionally, the FSC will require insurance companies to reflect the credit risks and market risks arising out of managing pensions for which principle is protected in calculating the risk-based capital (RBC) ratio. In the past, such credit risks and market risks were reflected in the insurance company's management index, but not in the RBC ratio.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Under the Commercial Code, in principle, a reinsurance contract is a wholly separate contract from the ceded insurance contract, and the reinsurance contract has no effect on the validity of the ceded insurance contract. Therefore, even if the ceding insurer becomes bankrupt or insolvent, a policyholder may not raise a claim under the ceded insurance contract against the reinsurer.

In other words, if the ceding insurer becomes bankrupt, then the reinsurance proceeds become a part of the ceding insurer's bankruptcy estate, and the beneficiary under the ceded insurance contract is only an unsecured creditor in the ceding insurer's bankruptcy proceedings. However, if the reinsurance contract contains a separate provision (ie, cut-through endorsement (mortgagee assumption)), the right of an insurance policyholder to claim directly against the reinsurer is recognised as an exception. Although the insertion of such clause is not legally mandatory, the regulatory authorities are tending to recommend insertion of such clause in reinsurance contracts for the protection of policyholders.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The insurance policyholder, the insured and the insurance beneficiary are each required to notify the insurer without delay when they obtain knowledge of the occurrence of an insurance accident. Further, if losses increase owing to a delay in the provision of such notice, the insurer is not liable for the increased amount of loss from such delay. If the policyholder or the insured, intentionally or through gross negligence, fails to disclose or inadequately discloses material information at the time of entering into an insurance contract, the insurer may terminate the insurance contract within one month of becoming aware of such fact or three years after the date the insurance contract was executed, whichever is earlier. Such general insurance law provisions also apply to reinsurance contracts, and there are no other laws that prescribe any notice requirement applicable particularly to reinsurance contracts. In addition, as a matter of practice, reinsurance contracts often contain

a provision whereby the reinsurer is not obliged to pay insurance proceeds with respect to losses attributable to matters not notified by the ceding insurer. The requirement to provide notice and information in other cases may vary depending on the reinsurance contract terms.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

Since the IBA does not provide different set of rules for reinsurance, general principles apply to the reinsurance absent special terms agreed between reinsurers and ceding insurers. Liability between reinsurers is allocated in the same way: if multiple insurance contracts have been executed for the same insurance contract purposes and same covered losses, and if the aggregate total amount of insurance exceeds the insurable value, then the insurers are jointly liable each up to the amount of its insurance coverage amount.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

There is no law that grants such right to reinsurers and such issues are usually governed by the policy.

49 Reimbursement of commutation payments

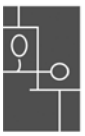
What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Such obligation of the reinsurer is not prescribed by law. Since reinsurance contracts often contain a provision whereby the reinsurer is not obliged to pay insurance proceeds with respect to losses attributable to matters not notified by the ceding insurer, the effect of a breach of duty to report claims would depend on the reinsurance contract terms.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Exercise of rights and the performance of obligations must be in accordance with the principles of good faith, and the rights shall not be abused. These general principles of the Civil Code are applicable to insurance contracts and reinsurance contracts. However, as these principles are contained in general provisions, there are no specific standards for conduct complying with principles of good faith in specific circumstances; as such, determination of whether such principle has been violated must be made on a case-by-case basis in consideration of legal stability and specific rationality. The Act on Regulation of Standardised Contracts provides more distinction regarding the principle of good faith, and voids provisions of standardised contracts that are unduly unfair to the consumer and thereby undermines the principles of good faith.



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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Insurance Commission (CAA) is the official and exclusive regulatory authority in charge of the supervision of the insurance sector in Luxembourg.

The CAA supervises Luxembourg-incorporated insurance, reinsurance undertakings and professionals of the insurance sector, as well as activities carried out in Luxembourg by foreign entities under the principle of freedom to provide services or to operate through branches located in Luxembourg. This supervision is performed on an ongoing basis, as the regulatory authority must ensure that the insurance and reinsurance undertakings subject to the Luxembourg legislation continue to comply with the conditions under which they are authorised to carry out their activities.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Luxembourg insurance and reinsurance undertakings are authorised by the Minister for the Treasury and Budget (Minister), after due submission of an application filed with the CAA, which is in charge of reviewing it.

The law of 7 December 2015 on the insurance sector, as amended (2015 Law), the implementing Grand Ducal Regulation of 14 December 1994 specifying the conditions for authorisation and practice of direct insurance undertakings, as amended (1994 Regulation), the implementing Grand Ducal Regulation of 5 December 2007 establishing the terms and conditions of the supplementary supervision of insurance and reinsurance undertakings that are part of an insurance or reinsurance group (Group Regulation) and the CAA regulation No. 15/03 of 7 December 2015 relating to insurance and reinsurance companies, as amended (CAA Regulation) set out the rules governing the formation and authorisation of insurance undertakings. The 2015 Law, the Group Regulation, the Grand Ducal Regulation of 5 December 2007 specifying the conditions for the authorisation and practice of reinsurance undertakings, as amended (2007 Regulation) and the CAA Regulation set out the rules governing the formation and authorisation of reinsurance undertakings.

In order to be authorised by the Minister, an insurance or a reinsurance undertaking must adopt one of the following legal forms:

- public limited liability company;
- partnership limited by shares;
- mutual insurance association;
- cooperative company;
- cooperative company organised as a public limited liability company;
- European company; or
- European cooperative society.

It is also necessary for all insurance and reinsurance undertakings authorised by the Minister to have their central administration established in Luxembourg.

Furthermore, the corporate object of an insurance undertaking must be limited to insurance activities and activities deriving directly therefrom, while the corporate object of a reinsurance undertaking must be limited to reinsurance activities and activities deriving therefrom (with the exception of any direct insurance activities). Hence, the possibility for insurance and reinsurance undertakings to carry out any other commercial activity is excluded. The 2015 Law further provides that insurance undertakings must choose to exercise either life insurance or non-life insurance activities, as these activities are, as a matter of principle, incompatible (see question 3 for more details).

Moreover, the direct and indirect shareholding structure of insurance and reinsurance undertakings must be transparent. The identity of all shareholders holding directly or indirectly a qualifying holding therein (ie, representing at least 10 per cent of the share capital or the voting rights of the entity) and the amount of such holdings must be disclosed to the CAA. The 2015 Law also states that these shareholders must also provide evidence that they are able to ensure sound and prudent management of the undertaking.

In addition, an authorisation as an insurance or reinsurance undertaking will only be granted by the Minister if the applicant provides a business plan and holds the minimum guarantee fund mentioned in the 2015 Law.

Applicants wishing to be authorised as an insurance undertaking must ensure that they have an effective actuarial function exercised by persons who have knowledge of actuarial and financial mathematics, commensurate with the nature, scale and complexity of the risks inherent in their business. They must also demonstrate that once authorised, the undertaking will be effectively managed by at least one person who fulfils a series of legal conditions (such as their good repute, professional experience and knowledge and an effective physical presence in Luxembourg) and holds a regulatory authorisation.

Finally, the Minister will consent to grant an authorisation as a reinsurance undertaking if the applicant demonstrates that it will be managed effectively by a natural person holding a regulatory authorisation or an authorised management company of reinsurance undertakings (whose representative holds the authorisation required by the law) linked to the entity by a services agreement. Hence, the daily management of reinsurance undertakings must be carried out by their own personnel, or by a management company of reinsurance undertakings with which they have entered into a services agreement.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

As mentioned above, Luxembourg insurance and reinsurance undertakings must obtain an authorisation delivered by the Minister.

This authorisation granted to insurance undertakings is limited to one or several specific classes of insurance, which relate to different sorts of risks and belong to either the life insurance or the non-life insurance sector. As a matter of principle, an insurance undertaking cannot be authorised for both life insurance and non-life insurance sectors. However, the 2015 Law has introduced specific and restrictive exceptions to that principle, as it is now possible, under certain

circumstances, to combine life and non-life activities (for the classes of direct insurance regarding accident and sickness).

Although the 2015 Law provides as a general principle that a licence is granted for an entire class of insurance, undertakings only apply in practice for an authorisation relating to several risks only (not for the whole sector).

Any insurance or reinsurance undertaking authorised to carry out its activities by the Minister may establish branches in other EU member states or operate in these countries in accordance with the principle of freedom to provide services.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The person or each of the persons in charge of the day-to-day management of an insurance or reinsurance undertaking (authorised managers) must be first authorised by the Minister, after due submission of an application filed with the CAA, which is in charge of reviewing it.

In principle, the manager must be a natural person. The 2015 Law, however, allows that reinsurance undertakings be managed either by a natural person or by an authorised management company of reinsurance undertakings. In the latter case, the management company must be represented by a delegated manager of reinsurance undertakings, who is him or herself duly authorised as a manager of reinsurance undertakings.

The legal requirements to be authorised as a manager of an insurance undertaking or a reinsurance undertaking are identical.

The authorised managers must first demonstrate their good repute (which relates to both their morality and professional standing). They must also have the necessary professional experience. Finally, the authorised managers must effectively manage the insurance or reinsurance undertaking and must be physically present in Luxembourg in order to allow such effective and permanent management.

These requirements will be assessed on the basis of documents submitted by the applicant, such as a curriculum vitae detailing his or her education and professional career, a copy of his or her diplomas, an excerpt of his or her criminal record or, if not available in a specific country, an affidavit sworn before a notary demonstrating the applicant's good repute and certifying that he or she has not been involved in insolvency or similar proceedings.

The management companies of reinsurance undertakings are also regulated and must be incorporated under one of the forms available for Luxembourg commercial companies, or as an economic interest grouping or a European economic interest grouping. In addition, these management companies must, inter alia, comply with minimum capital requirements (share capital of €50,000 on the incorporation of the company and €125,000 five years thereafter), have their central administration, their accounting and their documents in Luxembourg, and conclude a civil liability insurance policy. Moreover, the members of the administration, management and supervisory bodies and the shareholders of a management company of a reinsurance undertaking must demonstrate their good repute.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

From a corporate law point of view, Luxembourg insurance and reinsurance undertakings are not subject to any minimum share capital requirements, aside from those imposed by the law of 10 August 1915 on commercial companies, as amended, depending on the corporate form of the relevant entity.

Nevertheless, insurance and reinsurance undertakings must comply with certain obligations regarding own funds. Own funds are composed of basic own funds, which appear in the undertaking's balance sheet, and ancillary own funds, which are not recorded in this balance sheet. Own funds are divided into three tiers pursuant to quality criteria.

Eligible basic own funds must cover the minimum capital requirement imposed on insurance and reinsurance undertakings whose threshold and calculation methods are defined by the CAA Regulation.

In addition, insurance and reinsurance undertakings must ensure that they hold eligible own funds which cover the solvency capital requirement. The solvency capital requirement must reflect a level of eligible own funds, which enables insurance and reinsurance undertakings to absorb significant losses and that gives reasonable assurance to policyholders and beneficiaries that payments will be made as they fall due. The solvency capital requirement shall be calculated on the presumption that the undertaking will pursue its business as a going concern. It shall be calibrated to ensure that each insurer will be able to meet its obligations over the next 12 months with a probability of 99.5 per cent (confidence level). The 2015 Law provides for two alternative calculation methods: either a standard formula determined by the CAA Regulation or a formula based on integral or partial internal models set up by the insurance or reinsurance undertaking and approved by the CAA.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

The 2015 Law determines the scope of the technical provisions and the categories of assets covering technical provisions. The value of the technical provisions corresponds to the current amount that insurance and reinsurance undertakings should pay if they were transferring forthwith their insurance and reinsurance obligations to another insurance or reinsurance undertaking.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The CAA shall not require the prior approval or systematic notification of general and special policy conditions, of scales of premiums, of the technical bases used in particular for calculating scales of premiums and technical provisions, or of forms and other printed documents that an undertaking intends to use in its dealings with policyholders.

Nevertheless, the general and special conditions of mandatory non-life insurance policies (eg, third-party motor liability insurance policies) offered by insurance undertakings authorised in Luxembourg must be communicated to the CAA before their use.

In addition, for life insurance and for the sole purpose of verifying compliance with national provisions concerning actuarial principles, the CAA may require systematic notification of the technical bases used for calculating scales of premiums and technical provisions. That requirement shall not constitute a prior condition for the authorisation of a life insurance undertaking.

Furthermore, the CAA requires the communication of a technical note for life and non-life insurance products which the insurance or reinsurance company intends to use in its dealings with policyholders.

Moreover, on application of Regulation (EU) No. 1286/2014 of the European Parliament and the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs Regulation), a key information document (KID) will have to be issued from 1 January 2018 by life insurance undertakings for each packaged retail insurance-based investment product destined for retail investors. This requirement is, however, limited to life insurance contracts where the benefits under the contract are not payable only on death or in respect of incapacity owing to injury, sickness or infirmity.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

In the performance of its ongoing prudential supervision, the CAA examines the annual reports and accounts of undertakings and also carries out on-the-spot checks on a regular basis. International groups are under the supervision of a European college of supervisors.

Insurance undertakings must provide the CAA with some documents on an annual basis, inter alia:

- an annual report;

- an annual statement of the assets used to cover technical provisions;
- annual financial statements, the management report and the minutes of the ordinary general meeting of shareholders approving the annual accounts and deciding on the allocation of the results;
- a statement of depositary agreements;
- a statement of various statistics;
- the data sheet;
- an actuary's report;
- a special report of the auditor of the undertaking; and
- the governance and risk management report.

Reinsurance undertakings are required to provide the CAA on an annual basis with their annual reports, which including, inter alia, the following:

- the balance sheet of the undertaking;
- a profit and loss account and a statistical annex on the gross amount of claims paid;
- an annex about the overhead costs;
- a table outlining the geographical origin of the premiums;
- a table determining the cap of the provision for fluctuations in the occurrence of insured events;
- a statement on the investment policy; and
- a governance report.

In addition, insurance undertakings must keep a permanent inventory of the assets covering technical provisions and transmit it on a quarterly basis to the CAA.

The CAA is empowered to, among others, perform verifications on the Luxembourg territory with respect to the information which has been disclosed to it in relation to Luxembourg insurance and reinsurance undertakings. To that end, the CAA is also allowed to carry out remote supervision or on-site inspections at the premises of insurance and reinsurance undertakings and can be provided with copies of the books, accounts, registers and other deeds and documents. Such controls relate mainly to the management and internal structure of the relevant undertakings and their compliance with the legal, regulatory and prudential requirements. For instance, they can purport to verify the existence of appropriate and effective internal control procedures and compliance with the anti-money laundering obligations that apply to insurance and reinsurance undertakings. Insurance or reinsurance undertakings are also subject to the supplementary supervision of the CAA when they are members of an insurance or reinsurance group or, under certain circumstances, part of a financial conglomerate. In some specific instances, insurance and reinsurance undertakings must, upon request from the CAA, provide the CAA with all relevant information to enable it to exercise its supplementary supervision. Insurance and reinsurance undertakings must calculate the solvency capital requirement at least once a year and report the result of that calculation to the CAA.

In the event of any major development affecting significantly the relevance of the information disclosed to the CAA regarding their solvency and financial condition, insurance and reinsurance undertakings shall voluntarily disclose appropriate information on the nature and effects of that major development to the CAA.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

As a matter of principle, insurance and reinsurance undertakings must invest all their assets in accordance with the 'prudent person' principle in compliance with the rules set out by the CAA. As a consequence, they must invest into assets and instruments that represent risks that can be easily identified.

The 1994 Regulation defines some requirements that must be complied with in relation to the assets covering the technical provisions of insurance undertakings. In particular, such assets must take account of the type of operations performed by the relevant insurance undertaking in order to ensure the security, profitability and liquidity of the investments made by that entity. To that end, insurance undertakings must ensure that the investments they make are sufficiently dispersed and diversified, and that they comply with the specific rules provided for in the 1994 Regulation (eg, in relation to investments in shares, bonds and real estate properties). This Regulation provides for some requirements in relation to the valuation of the invested assets.

Moreover, the Circular Letter 15/3 of 24 March 2015 of the CAA relating to investment rules for life insurance products linked to investment funds (Circular Letter) contains specific rules on the investments that can be made by insurance undertakings further to the subscription by policyholders to contracts linked to investment funds or to mixed contracts. In such instance, the assets invested by the insurance undertaking further to the execution of the insurance contract can only consist of shares in external funds, shares of funds with no guarantee of future performance or liquid assets, or a combination thereof.

When the life insurance contract concerns investments into external funds, an insurance undertaking should only acquire shares in undertakings for collective investment in transferable securities, alternative investment funds or funds of alternative investment funds and real estate funds, within the more specific limits indicated in the Circular Letter.

If the life insurance contract involves investments by the insurance undertaking in internal funds with no guaranteed return or a dedicated fund, some specific rules concerning the assets in which these funds can invest must be complied with, depending on the category to which the policyholder belongs (which is determined on the basis of the amount of wealth in transferable securities and of the amounts invested in the insurance contract or contracts concluded with the insurance undertaking). Furthermore, investments into dedicated funds are only allowed for insurance contracts with a minimum premium of €125,000.

Reinsurance undertakings are subject to a series of investment rules regarding assets covering technical provisions that are contained in the 2007 Regulation. More specifically, these assets must be invested in a manner that takes account of the operations undertaken by the relevant reinsurance undertaking in order to ensure the sufficiency, liquidity, security, quality, profitability and matching of its investments. Furthermore, assets must be diversified and adequately spread to allow the reinsurance undertaking to meet changing economic circumstances and to avoid excessive reliance on any particular asset, issuer or group of undertakings and accumulations of risk in the portfolio as a whole. Moreover, investments in assets that are not admitted to trading on a regulated financial market must be kept to prudent levels, and investments in derivative instruments are only possible insofar as they contribute to a reduction of investment risks or facilitate efficient portfolio management by the reinsurance undertaking. The 2015 Law forbids the CAA from retaining or introducing a system with gross reserving for the establishment of technical provisions, which requires to pledge assets to cover unearned premiums and outstanding claims provisions where the reinsurer is an insurance or reinsurance undertaking authorised in accordance with Directive 2009/138/EC (Solvency II).

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Contemplated acquisitions and disposals by any person of shares of an insurance or reinsurance undertaking that constitute a qualifying participation (ie, representing at least 10 per cent of the share capital or the voting rights of the entity), or that result in crossing (upwards or downwards) the ownership thresholds of 20, 33.33 or 50 per cent or the insurance or reinsurance undertaking becoming the subsidiary of the acquirer, must be notified by such person or persons to the CAA in advance and in writing. The notification must include all the relevant details regarding the information on the proposed acquisition or disposal of shares.

The CAA must render a decision within a maximum of 60 to 90 business days from the date of its acknowledgement of receipt of the notification, depending on whether the proposed acquirer is a resident of the EU or the European Economic Area (EEA) or not, whether or not it is subject to EU prudential supervision and whether or not the CAA issues a supplementary request for information. If, during this assessment period, the CAA does not object in writing to the envisaged acquisition, the transaction is presumed to be authorised.

Moreover, the insurance or reinsurance undertaking must inform the CAA of such disposals and acquisitions as soon as it has knowledge thereof.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements or restrictions in the 2015 Law concerning the financing of the acquisition of insurance or reinsurance undertakings.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

The 2015 Law provides for specific requirements and restrictions on investors acquiring, directly or indirectly, alone or in concert, a qualifying holding (ie, representing at least 10 per cent of the share capital or the voting rights of the entity) in insurance or reinsurance undertakings, or having any other possibility to exercise a significant influence on the management of these entities. Similarly, the 2015 Law contains specific requirements to be complied with when the holding of shareholders of insurance or reinsurance undertakings exceeds or becomes lower than a series of defined ownership thresholds (see question 10).

In the case of a contemplated acquisition of a qualifying holding or a holding exceeding the specific thresholds indicated in the 2015 Law, the CAA will assess the potential influence of the proposed acquirer over the insurance or reinsurance undertaking in order to ensure the sound and prudent management of the entity. In particular, the CAA will assess the following criteria:

- the morality and professional standing of the proposed acquirer;
- the morality, professional standing and professional experience of any person who will direct the business of the insurance or reinsurance undertaking as a result of the proposed acquisition;
- the financial soundness of the proposed acquirer;
- the possibility for the undertaking to continue to comply with the applicable legal and regulatory requirements after the proposed acquisition; and
- the existence of reasonable grounds to suspect that the acquisition is connected to, or increases the risk of, money laundering or terrorist financing.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

The 2015 Law does not contain any specific requirements or restrictions for investments by foreign citizens, companies or governments in insurance or reinsurance undertakings, except the requirements for the acquisition of a qualifying participation or the crossing of the ownership thresholds (see question 10).

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The 2015 Law, the 2007 Regulation and the Grand Ducal Regulation of 17 November 2006 relating to financial conglomerates for which the CAA assumes the role of coordinator include:

- general provisions on financial supervision on a standalone basis of Luxembourg insurance and reinsurance undertakings;
- specific provisions on the supplementary supervision of insurance or reinsurance undertakings belonging to an insurance or reinsurance group; and
- specific rules on the supplementary supervision of insurance undertakings belonging to a financial conglomerate.

Each of the three supervisory regimes is independent from the two others.

Any insurance or reinsurance undertaking subject to the supplementary supervision of insurance and reinsurance groups must implement internal control procedures that are adequate and useful for its reporting obligations to the CAA. In that context, insurance and reinsurance undertakings must implement risk management procedures and suitable internal control mechanisms to identify, measure, monitor and verify appropriately intra-group transactions and risk concentration between them and affiliated companies, holding companies of these affiliates or companies linked to these holding companies, or natural persons having holding in the latter companies or in the insurance or reinsurance undertaking.

The supplementary supervision of insurance undertakings in financial conglomerates in respect of which the CAA assumes the function of coordinator is independent from the supplementary supervision of insurance undertakings belonging to an insurance group or the supervision of these entities on an individual basis. The appointment of the CAA as the competent authority responsible for exercising supplementary supervision (ie, the coordinator) is based on the following criteria:

- the financial conglomerate is headed by a Luxembourg-regulated entity;
- the parent of two regulated entities based in the European Union is a Luxembourg-based mixed financial holding company; and
- the financial conglomerate is headed by more than one mixed financial holding company with a head office in different EU member states and there is a regulated entity in each of these states, if the largest balance sheet total is based in Luxembourg if these entities are in the same financial sector, or if one of those entities belonging to the most important financial sector of the group is based in Luxembourg.

All the entities of the financial sector belonging to the financial conglomerate, whether regulated or not and whether established in an EU member state or a third country, are included in the scope of the supplementary supervision performed by the CAA. The supplementary supervision exercised by the CAA concerns the financial situation of the financial conglomerate and more particularly, the adequacy of stockholders' equity, the risk concentration and the intra-group transactions, as well as the internal control systems and procedures of risk management set up at the level of the financial conglomerate. The CAA, when it assumes the function of controller of the group, identifies, after consulting the other supervisory authorities concerned as well as the group, the type of risk that insurance and reinsurance undertakings of a given group shall report in any circumstances. The very significant intragroup transactions must be reported as quickly as possible.

Moreover, mixed financial holding companies, third-country regulated entities and unregulated entities belonging to financial conglomerates whose coordinator is the CAA are not subject to any supervision on an individual basis by the CAA.

Where an insurance or reinsurance company governed by Luxembourg law and belonging to a financial conglomerate has its parent undertaking located outside an EU member state (and therefore is subject to supervision of a third-country competent authority), the CAA must verify than an equivalent supervision as the one performed by the CAA by application of the 2015 Law has been implemented. Where such equivalent supervision does not exist, the CAA shall apply the provisions concerning the supplementary supervision to the regulated entity.

The rules concerning the supplementary supervision in financial conglomerates in respect of which the CAA assumes the function of coordinator are as follows:

- insurance and reinsurance undertakings must ensure that own funds, which must at all times be at least equivalent to the applicable capital adequacy requirements, are available at the level of financial conglomerate;
- the entities at the head of the financial conglomerates must, at least once a year, notify the CAA of the results of the calculation of the own funds and the capital adequacy requirements for the financial conglomerate and all supporting data, any significant concentration of risks within the relevant financial conglomerate

and any significant intra-group transactions involving regulated entities in the relevant financial conglomerate;
- the entities at the head of financial conglomerates must also regularly notify the CAA of the details of their legal structure, governance system and organisational structure including information on all the regulated entities, non-regulated subsidiaries and branches of significant importance; and
- the entities at the head of financial conglomerates must publish annually, at the level of the financial conglomerate, a description of their legal structure, either in its entirety, or by reference to equivalent information.

Moreover, Luxembourg insurance undertakings belonging to a financial conglomerate whose coordinator is the CAA have to implement risk management and internal control procedures at the level of the financial conglomerate.

The risk-management procedures must comprise:
- the sound and prudent governance and management of the business in light of the risks incurred, including approvals and periodic reviews by appropriate governing bodies at the level of the financial conglomerate, of strategies and policies for all risks incurred;
- adequate policies as regards capital requirements;
- appropriate procedures to guarantee the suitability of the risk supervision methods and the existence of steps for the coherence of the systems in the financial conglomerates to ensure that the risks are measured, monitored and controlled at the level of the financial conglomerate; and
- schemes allowing the creation and, as the case may be, the development of appropriate and regularly updated safeguard and crisis resolution plans and mechanisms (which are regularly updated).

The internal control procedures include appropriate systems that identify, measure and manage the important risks incurred and procedures that guarantee the capital requirements in relation to the risks incurred, and accounting and reporting procedures allowing the identification, measure, follow-up and control of intra-group transactions and risk concentrations.

The entities belonging to a financial conglomerate whose coordinator is the CAA, the mixed insurance holding companies and the Luxembourg entities in the insurance sector that belong to a financial conglomerate subject to a coordinator other than the CAA, must implement internal-control procedures allowing the provision of information necessary for the supplementary supervision, for example:
- in case of changes regarding their managers;
- to verify information relating to an entity belonging to a financial conglomerate and having its head office in another EU member state with the competent authorities of the other EU member state;
- to describe their legal structure, their governance system, their organisational structure; and
- for Luxembourg insurance undertakings belonging to a financial conglomerate whose coordinator is not the CAA, to implement adequate risk management and internal control procedures, as well as sound administrative and accounting procedures, that are suitable to the financial conglomerate.

Luxembourg insurance undertakings belonging to a financial conglomerate whose coordinator is not the CAA must allow information (ie, the results of the calculations of stockholders' equity, the capital adequacy requirements, any significant concentration of risks and any significant intra-group transaction involving regulated entities in the relevant conglomerate) to be at the disposal of the entity at the head of the financial conglomerate, or, where necessary, of another entity regulated by the financial conglomerate required by the coordinator to notify it of the results of the calculations, to allow the coordinator to estimate if, at the level of the financial conglomerate, stockholders' equity is equivalent at all times to at least the capital adequacy requirements.

The CAA, in its capacity as coordinator, exercises prudential supervision regarding compliance with the above requirements and it can regularly impose stress tests on the financial conglomerates for which it assumes the function of coordinator. The financial conglomerate must report, on a regular basis and at least annually, to the CAA, all significant intra-group transactions.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

There are no regulatory requirements in respect of reinsurance agreements. Reinsurance agreements are expressly excluded from the scope of the law of 27 July 1997 on the insurance contract, as amended (1997 Law), and are consequently only subject to the general Luxembourg contract law principles (consent, causation, absence of fraud, performance in good faith, etc).

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There are no specific requirements or restrictions on the amount of ceded reinsurance and retention of risk by insurers.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Reinsurance undertakings must establish technical provisions with respect to all of their reinsurance obligations vis-à-vis beneficiaries of insurance or reinsurance contracts.

Those technical provisions must be established with a credit institution which has its registered office or a branch in an EU member state, or with a credit institution which has its registered office outside the EEA but has a branch or an agency in one of the EU member states.

There is no such requirement concerning the localisation of technical provisions for the amounts recoverable from reinsurance contracts against undertakings authorised in accordance with Solvency II, or having their head office in a third country whose solvency regime is deemed to be equivalent.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

There are no regulatory requirements for cedents to obtain credit for reinsurance on their financial statements under Luxembourg law.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Book III of the Luxembourg Commercial Code, which relates to bankruptcy proceedings, the provisions of the law of 4 April 1886 concerning composition to prevent bankruptcy as well as the Grand Ducal Regulation of 24 May 1935 completing the legislation in respect of suspended payments, and composition to prevent bankruptcy through the institution of controlled management, are not applicable to insurance undertakings. Conversely, reinsurance undertakings remain subject to the general bankruptcy rules contained in the Luxembourg Commercial Code.

The 2015 Law provides the following specific rules:
- the suspension of payment of an insurance undertaking may be requested in court by the CAA or by the company itself (with prior notification to the CAA) when the credit of the insurance undertakings is impaired or when it finds itself in a non-liquid situation. The judgment granting the suspension of payment will appoint one or more supervisory auditors in charge of controlling the management of the insurance undertaking;
- the judicial dissolution and winding-up of an insurance undertaking may only be requested in court by the CAA or the public prosecutor when a suspension of payment measure previously ordered does not permit the rectification of the situation or when the financial situation of the undertaking is impaired in such a way that the undertaking is no longer able to meet its commitments. The court deciding on the judicial winding-up will appoint a judge-commissioner as well as one or more liquidators. The court may decide to apply certain provisions governing bankruptcy.

Moreover, the insurance undertaking put into judicial winding-up automatically loses its licence;
- the CAA has the power to take all the necessary measures to safeguard the interests of policyholders under insurance contracts, or the obligations arising out of reinsurance contracts; and
- the licence granted to a reinsurance undertaking that is unable to take the measures provided for in the restoration plan or in the short-term financing scheme in due time may be withdrawn by the Minister. In such event, the CAA will appoint one or more liquidators in charge of liquidating the reinsurance contracts and the assets representing the technical provisions.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The 2015 Law defines the priority of claims against an insurance undertaking in insolvency proceedings.

The 2015 Law provides that the assets covering the technical provisions constitute a separate estate over which the insurance creditors (ie, the policyholders, the insured or the beneficiaries of an insurance policy entered into with the insurance undertaking) benefit from a legal privilege. Such legal privilege will rank before any other legal privileges to the extent that the assets covering the technical provisions have been recorded in a separate inventory, which is communicated to the CAA on a quarterly basis, or that a registration of mortgage has been taken over the immoveable assets covering the technical provisions. The Luxembourg Court of Appeal recently held that the concept of 'separate estate' (which was already mentioned in the law of 6 December 1991 on the insurance sector, as amended, which was replaced by the 2015 Law) does not prevent the insurance creditors from having an entitlement over all the assets of the insurance undertaking and does not limit their rights to the underlying assets of their insurance contract.

If the separate estate is insufficient to satisfy all existing claims, the insurance creditors retain a legal privilege over the estate of the insurance undertaking, up to the amount of their unsatisfied claim. In this case, the claim covered by the legal privilege will rank before any claims, but after a series of specific claims, to which Luxembourg law attributes a legal privilege. Such specific claims will then rank first and are as follows:
- claims for legal costs;
- claims for salaries, remunerations and indemnities that result from an employment contract for the last six months of work, and claims for indemnities owed further to the termination of the employment contract or apprenticeship contract, up to an amount not higher than six times the reference social minimum salary;
- claims mentioned in the preceding item, to the extent that they are higher than six times the social minimum salary;
- claims arising from an accident and for the benefit of third parties in that accident, or their right holders, which are owed by the insurer pursuant to the insurance contract; and
- other specific claims secured by a legal privilege in favour of the State Treasury, the municipalities, the social security bodies and the professional chambers.

In the event of an insurance or a reinsurance undertaking being wound up, commitments arising out of contracts underwritten through a branch or under the free provision of services shall be performed in the same way as those arising out of contracts directly concluded in Luxembourg by that insurance or reinsurance undertaking.

Finally, the policyholder of an insurance contract related to a dedicated fund, benefits only from a legal privilege over the separate estate created by the insurer, and in theory has no preferential entitlement over the dedicated fund.

The distribution of assets of an insurance undertaking among its creditors will be carried out in compliance with the general rules on insolvency. Privileged claims, notably claims of the State Treasury and employees and legal privilege, are paid in preference over the claims of general creditors. Among the other creditors, there is as a matter of principle no preference concerning their entitlement to the distribution of the bankrupt assets. Nevertheless, any financial collateral arrangement or netting agreement duly formed pursuant to the law of 5 August 2005 on financial collateral arrangements, as amended, are immunised against, inter alia, the Luxembourg law provisions on bankruptcy, and are enforceable against the bankruptcy trustee and third parties.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Luxembourg intermediaries must be authorised by the Minister in accordance with the 2015 Law, after due submission of an application to the CAA, which is in charge of reviewing the file. Once authorised, Luxembourg intermediaries are registered in the special register of intermediaries held with the CAA, which can be consulted electronically.

The authorisation may only be granted to a natural person acting as an agent, insurance and reinsurance broker, manager of a brokerage company or sub-broker, and to legal persons acting as an insurance agency or insurance or reinsurance brokerage company. These activities are also subject to an authorisation delivered by the Minister pursuant to the 2015 Law. The granting of such authorisation is subject to separate provisions in the 2015 Law.

Moreover, in order to obtain the authorisation, the direct and indirect shareholding structure of intermediaries must be transparent. The identity of all shareholders holding directly or indirectly a qualifying holding therein and the amount of such holdings must be disclosed to the CAA. The 2015 Law also states that these shareholders must also provide evidence that they are able to ensure sound and prudent management of the intermediary.

Insurance or reinsurance brokerage companies must be managed by a manager authorised by the Minister, have a paid-up capital of at least €50,000 at incorporation (€125,000 after five years) and have their central administration in Luxembourg. Insurance and reinsurance brokers must fulfil conditions of sound professional reputation and relevant expert knowledge, have a net worth of at least €25,000 (€50,000 after five years), be covered by a professional civil liability insurance, effectively exercise their activity and have their principal establishment in Luxembourg.

The exercise of the activity as an insurance broker, manager of a brokerage company and sub-broker is not compatible with the activity of an agent. It is, however, possible to combine the functions of an insurance broker with those of a reinsurance broker, respectively an insurance brokerage company and a reinsurance brokerage company, provided the CAA has been previously informed thereof.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

As a matter of principle, and unless otherwise provided by the parties, a contract can only be binding on and be of benefit to the parties thereto. Nevertheless, the 1997 Law expressly provides that in the context of liability insurance, the injured third party has a direct action against the insurer, and the creditors of the insured will have no right on the indemnity paid by the insurer to the third party.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Pursuant to the 1997 Law, the insured must inform the insurer as soon as possible, and in any case within the period specified in the insurance contract. Moreover, the insured must provide the insurer with all the relevant information and respond to any questions raised by the insurer, in order to determine the circumstances and extent of the claim. However, the insurance undertaking cannot make use of the fact that the deadline for notifying the claim has not been met, if such notification is made within a reasonable time.

If the insured fails to comply with these obligations, and the insurance undertaking suffers a loss as a result of this breach, the insurer has the right to reduce the indemnity up to the amount of the loss suffered by it. The insurance undertaking may, however, deny coverage without demonstrating loss where the insured fraudulently failed to comply with these obligations.

It is important to note that the parties to an insurance contract regarding the cover of large risks (as defined in the 2015 Law, except baggage and moving insurance) may expressly deviate from the above-mentioned provisions.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Under Luxembourg law, it is not possible for an insured person to initiate proceedings in respect of both contractual and extra-contractual liabilities of the insurer. Therefore, the insurer could only see its extra-contractual liability questioned if no contractual remedies are available for the insured person.

Even though the rule prohibiting the combination of contractual and extra-contractual liabilities is not considered as a public policy rule in Luxembourg, the case law regarding this matter is well established.

In addition, an insurer can be held liable in tort for wrongful denial of a claim if this contractual breach has caused damage to the third party.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

In the case of indemnity insurance, the insurer is obliged to defend a claim as soon as the insurer's coverage becomes due, to the extent that the insured calls for such coverage.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The insurer's payment obligation is triggered when the insured event is realised and provided that it occurred during the coverage period foreseen in the insurance contract. The 1997 Law provides that the insurer will not cover losses or damages caused intentionally or fraudulently.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

The 1997 Law provides that as soon as the life insurance contract is effective, the life insurer cannot contest the coverage on the basis of a non-intentional misrepresentation of the insured in the application.

The insurance contract can, however, include a specific provision concerning the postponement of the incontestability period for a period not exceeding one year.

28 Punitive damages

Are punitive damages insurable?

Punitive damages are not valid under Luxembourg law. As a consequence, they cannot be enforced by the Luxembourg courts and cannot be insured in an insurance contract governed by Luxembourg law.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

This issue is not regulated by the 1997 Law. Unless otherwise agreed between the parties to the relevant insurance contract, the excess insurer will only indemnify the insured losses exceeding the insured amount of the primary insurance contract.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Luxembourg law does not operate any distinction between self-insured retentions and deductible.

In practice, the insurer will only be required to pay the amount determined in accordance with the insurance contract after due deduction of any sum that is borne by the insurer as deductible.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is no specific provision in that respect in the 1997 Law. However, the law of 16 April 2003 regarding mandatory third-party motor liability insurance, as amended, provides that in the event that there are several injured third parties and the total due indemnification exceeds the insured amount, the rights of the injured third parties against the insurer are reduced proportionally.

However, if the insurer ignores the existence of other claims and pays in good faith to an injured third party an amount exceeding his or her pro rata share, the other injured third parties will only be entitled to the balance of the insured amount.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

If a particular interest is insured against the same risk with several insurers, the insured may, in the event of a loss, seek indemnification from each insurer within the limits of the obligations of each of them, and up to the amount of the indemnity to which he or she is entitled.

Except in the case of fraud, none of the issuers may deny coverage by referring to the existence of other contracts covering the same risk.

The 1997 Law determines the method of apportionment among the insurers in relation to insurance of compensatory character. Nevertheless, it is possible for the insurers to contractually provide for a different method of apportionment.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Luxembourg liability law does not recognise the concepts of 'disgorgement' or 'restitution' claims. In addition, damages that are awarded by the courts by application of Luxembourg law can only be of a compensatory nature. Punitive damages are therefore excluded (see question 28). In addition, the 1997 Law provides that no insurer can be forced to indemnify any damages resulting from the insured's gross negligence or wilful misconduct. Moreover, criminal fines and settlements cannot be covered by an insurance contract.

Aside from these rules, the risks covered in the insurance contract are, as a matter of principle, left to the contractual freedom of the parties. Accordingly, insurance contracts would generally exclude any fault committed in order to realise a gain to the extent that it is not already caught under one of the exclusions set out in the preceding paragraph. It is usually considered that indemnifying the insured in such instance would be tantamount to 'unjust enrichment'.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

This situation is commonly referred to as a 'serial accident'.

The courts held that when a damage has been caused by several events, the guardian of a thing having caused this damage has to be considered as having caused the entire damage. The solution adopted in France could therefore be applied in Luxembourg since Luxembourg civil law derives from the French and Belgian legal systems. Under French law, a set of harmful facts having the same technical cause must be regarded as a single event, regardless of the time and place of each claim. Insurance undertakings can include a provision for the globalisation of claims in their insurance policies in order to be able to apply deductibles and covering ceilings uniformly to the entire serial accident.

Update and trends

On 9 November 2016, the European Commission extended the application date of the PRIIPs Regulation by one year. This extension gives issuers and distributors of PRIIPs products until 1 January 2018 to issue a KID for each packaged retail insurance-based investment product destined for retail investors.

In addition, the Regulation 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data (GDPR) will apply from 25 May 2018. The GDPR will repeal the current Directive 95/46/EC and will impose some onerous obligations to companies which undertake to process personal data. In particular, under the GDPR, each controller of personal data shall have to demonstrate, at any time, compliance with the data protection principles set in the GDPR (principle of accountability). Therefore, companies that will have to perform data protection impact assessments to evaluate the risk of their processing (and take into account data protection risks throughout any processing of personal data), to keep extensive internal records of their data protection activities, to designate a data protection officer and to notify any data breach to their national data protection authority. Moreover, the GDPR will require companies to put mechanisms into place to ensure that, by default, only personal data that are necessary for each specific purpose are processed. Any failure to comply with the requirements imposed by the GDPR will be sanctioned by a fine amounting to a maximum of 4 per cent of the total worldwide annual turnover of the company.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

In the event that the insurer discovers the existence of unintentional misstatements regarding the description of the factual elements for the determination of the risks, which were made on the formation of the contract by the insured, the insurance contract shall be terminated only if the insured rejects the insurer's proposal to modify the terms of the insurance policy; the insured has not expressed its approval to modify the policy within a set period of one month; or the insurer proves that it would never have insured this risk if it had been aware of all relevant elements.

In cases where the insured makes wilful misstatements that mislead the insurer on the risk assessment elements on the formation of the insurance contract, the insurance policy is not terminated but will be declared null and void by the competent court.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

To the best of our knowledge, there are no published judicial precedents in Luxembourg. This confirms that litigation between insurers and reinsurers is rare. Disputes are usually settled out of court or through arbitration proceedings. Conciliation mechanisms might also be provided for in the reinsurance contract.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

We are not in an adequate position to identify a trend in this type of dispute (see question 36).

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

There are no specific rules governing reinsurance arbitration awards in Luxembourg. According to the general principles set forth in the Luxembourg New Code of Civil Procedure (NCPC), the arbitration award must include the reasoning for the decision. However, the parties may agree to exempt the tribunal from the obligation to specify it in the decision.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitration awards are only binding on the parties to the arbitration agreement. Therefore, arbitrators cannot assume jurisdiction over persons who are not themselves parties to such agreements.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Even though some articles of the NCPC refer to an appeal against an arbitral award, these references are inaccurate, since the possibility of appeal was abrogated by a regulation of 8 December 1981 amending and supplementing certain provisions of the single heading entitled 'Arbitration' of Book III of the second part of the Code of Civil Procedure (being replaced by the NCPC).

A distinction must be drawn between Luxembourg and foreign arbitration awards.

The only possibility to challenge a Luxembourg arbitration award is through proceedings for annulment by way of opposition to the enforcement order delivered by the president of the district court. Proceedings to have the arbitration award declared null and void must be filed with the district court, and be based on one of the terms of article 1244 of the NCPC. This article lays down an exhaustive list of 12 causes for annulment:

- the arbitral award is contrary to the public interest;
- the dispute cannot be settled by way of arbitration;
- there was no valid arbitration agreement between the parties;
- the tribunal has exceeded its power or jurisdiction;
- the tribunal has omitted to decide on one or more issues that are indivisibly linked to the settled issues;
- the tribunal was not properly constituted;
- the rights of the defence have been violated;
- the tribunal has not included the reasoning for the decision, unless the parties have agreed to exempt the tribunal from this obligation;
- the arbitral award contains conflicting provisions;
- the arbitral award was obtained by fraud;
- the award was based on evidence that has been declared false by virtue of an irrevocable court decision or on the basis of evidence that has been recognised to be false; or
- it is discovered that one party has concealed evidence that would have been a decisive factor for the award.

As a matter of principle, an arbitration award cannot be modified. However, if an arbitral tribunal has omitted to decide on one or several aspects of a dispute that can be dissociated from those on which the arbitration awards was rendered, it can complete its decision if the parties make such a request, even if the deadline to render a decision has expired. If a party disputes the assertion that the items can be dissociated, the district court will issue a decision on the independent character of these items. Should the dissociation be accepted by the district court, the matter will be referred again to the arbitral tribunal, which will then complete its decision.

In the case of a foreign arbitration award, the enforcement order is delivered by the president of the district court on an ex parte basis and it is possible to challenge the enforcement order before the court of appeal. The effect of these proceedings is not to annul the foreign arbitration award, but to prevent its enforcement in Luxembourg. Articles 1251 and 1244 of the NCPC set forth the grounds for annulment or non-recognition of the enforcement order (eg, the arbitral sentence can still be challenged before an arbitral tribunal and the tribunal has not ordered the provisional enforcement). It must be noted that Luxembourg has signed the New York Convention of 10 June 1958 on the recognition and enforcement of foreign arbitral awards, and has ratified it by a law of 20 May 1983. The recognition and enforcement

of an arbitral award rendered in a jurisdiction that is a party to the New York Convention could be refused on the grounds of article V of this convention.

From the above, it can be inferred that Luxembourg gives full deference to arbitral awards.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Luxembourg law does not provide for such an obligation. However, the parties to the reinsurance contract may agree that the reinsurer will have to follow the cedent's fortunes, provided that it is not contrary to the activity programme submitted by the reinsurer to the CAA. The scope of the obligation can be freely determined by the parties.

Defences available to the reinsurer are those generally available to all contractors: the parties must always act in good faith and must not abuse the rights granted by the contract or wilfully harm their contractor's interests.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

According to the general principle laid down in article 1134, paragraph 3 of the Luxembourg Civil Code, the parties to a contract must perform their contractual obligations in good faith. This principle also applies to reinsurance contracts. However, there are no specifications in relation to the duty to act in good faith in reinsurance agreements.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

No, Luxembourg law does not make a distinction between facultative reinsurance and treaty reinsurance.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

There is no such direct action. Luxembourg law does not give the right to the policyholder or the non-signatory to a reinsurance agreement to sue the reinsurer directly for coverage. This rule derives from article 1165 of the Luxembourg Civil Code, which provides that a contract can only be binding on and be of benefit to the parties. By exception, the parties may agree to grant certain rights to third parties.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

There is no obligation under Luxembourg law for the reinsurer to pay a policyholder's claim in the event of insolvency of the insurer.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The type of notice and information is usually defined in the reinsurance contract, since this issue is not governed by Luxembourg law. Pursuant to the general principles applicable to the contracts, the parties must always act in good faith and have a duty to bring to the attention of their contractor all information that might be relevant for the performance of the contract. If the contractor fails to comply with this obligation, he or she might face a liability claim for breach of contract.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

This matter is not specifically governed by Luxembourg law.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Luxembourg law does not provide any specific rule regarding the review. This is usually governed by the terms of the reinsurance contracts.

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49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

The obligation of the reinsurer to reimburse the cedent is defined in the contract, as there are no mandatory rules under Luxembourg law.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

The obligation of the reinsurer to reimburse a cedent for ECOs is not governed by any specific laws or regulations. Hence, this issue is left to the contractual freedom of the parties or the general principles of tort law.

Nigeria

Funke Agbor and Jamiu Akolade

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The regulatory agencies responsible for regulating insurance and reinsurance companies in Nigeria are the National Insurance Commission (NAICOM or the Commission) and the Chartered Insurance Institute of Nigeria (CIIN). The Corporate Affairs Commission is charged with the regulation of companies generally.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

One requirement for the formation and licensing of new insurance and reinsurance companies in Nigeria is that companies must be incorporated as a limited liability company under the Companies and Allied Matters Act, or must be a body duly established by law to transact the business of insurance or reinsurance. At least one of the promoters of the company must have insurance qualifications. The company must be registered with NAICOM after incorporation.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Apart from those listed in question 2, no other licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business in Nigeria.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The Insurance Act 2003 (Insurance Act) provides that a person shall not be appointed as a director, chief executive, manager or secretary of an insurance or reinsurance company if he or she:

- is of unsound mind;
- has previously been convicted of any offence involving dishonesty;
- is not a fit person for the position;
- is guilty of misconduct in relation to his or her duties;
- is a person with professional qualifications who has been disqualified or suspended from practising his or her profession;
- is a person whose appointment with an insurance company or financial institution has been terminated; or
- has been convicted for criminal misappropriation.

Furthermore, the minimum educational qualification requirements for officers and directors of insurance and reinsurance companies is a higher national diploma from any polytechnic, or a bachelor's degree or its equivalent from any university. In addition, such a person must also obtain a professional qualification from the Chartered Insurance Institute of Nigeria or the Chartered Insurance Institute of the UK.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Under the provisions of section 9(4) of the Insurance Act, NAICOM has stipulated that the minimum paid-up share capital requirements for all insurance and reinsurance companies are as follows:

- for life insurance companies: 2 billion naira;
- for general insurance companies: 3 billion naira; and
- for reinsurance businesses: 10 billion naira.

Furthermore, under section 10(1) of the Insurance Act, an insurer intending to commence insurance business in Nigeria after the commencement of the Insurance Act is required to deposit the equivalent of 50 per cent of the paid-up share capital with the Central Bank of Nigeria. Section 10(2) of the Insurance Act provides that 80 per cent of this deposit shall be returned, with interest, to the company on registration with NAICOM. Under section 10(3) of the Insurance Act, in the case of existing companies (set up before the commencement of the Insurance Act), an equivalent of 10 per cent of the minimum paid-up share capital shall be deposited with the Central Bank.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

The reserves required to be maintained by insurance and reinsurance companies are as follows:

Insurance companies

Insurance companies are required to establish and maintain contingency reserves to cover fluctuations in securities and variations in statistical estimates. An amount of not less than 3 per cent of the total premium or 20 per cent of the net profits (whichever is greater) shall be credited into the contingency reserves by insurance companies. This amount shall accumulate until it reaches the amount of the minimum paid-up capital or 50 per cent of the net premiums (whichever is greater).

Life insurance companies are in addition required to maintain the following reserves:

- a general reserve fund, which shall be credited with an amount equal to the net liabilities on policies in force at the time of the actuarial valuation, and an additional 25 per cent of net premium for every year between valuation dates; and
- a contingency reserve fund, which shall be credited with an amount equal to 1 per cent of the gross premiums or 10 per cent of the profits (whichever is greater) and accumulated until it reaches the amount of the minimum paid-up capital.

Reinsurance companies

Reinsurance companies are required to establish a general reserve fund, which shall be credited with the following:

- an amount not less than 50 per cent of the insurer's gross profit for the year where the fund is less than the authorised capital of the insurer; and

- an amount not less than 25 per cent of the reinsurer's gross profit for the year where the fund is equal to or exceeds the authorised capital of the reinsurer.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Insurance products are regulated exclusively by the Commission. Section 16 of the Insurance Act prohibits the introduction of a new product in any class of insurance business without the prior approval of the Commission.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

As part of its supervisory and regulatory functions, the Commission, through its Inspectorate Department, carries out the following supervisory inspections and examinations:

- not less than once every two years, it authorises an inspection, examination or investigation of every insurance institution for the purpose of satisfying the Commission as to whether the provisions of the Insurance Act or any regulations made thereunder are being complied with; and
- without prejudice to the above, at any time it may authorise one or more inspectors or other officers to inspect, examine or investigate any aspect of an insurance institution's business.

Additionally, the Commissioner for Insurance, who is appointed pursuant to the National Insurance Commission Act, may at any time (with the approval of the governing board established under the National Insurance Commission Act) order a special inspection or investigation of the books of any institutions where he or she suspects that:

- it is in the public interest so to do;
- the insurance institution has been carrying on its business in a manner detrimental to the interests of its policyholders;
- the insurance institution does not have sufficient assets to cover its liabilities to the insuring public and it is necessary for it to have such;
- the insurance institution has been contravening the provisions of the Insurance Act; or
- an application is made therefor by a director, shareholder or partner of the insurance institution, or a policyholder of the insurance institution.

Once every three years, an insurer transacting life insurance business shall, in respect of its life insurance business, allow an investigation to be made into its financial position by an actuary appointed or secured by the insurer.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The Insurance Act compels insurers to invest and hold invested in Nigeria assets equivalent to not less than the amount of the policyholders' funds in such accounts of the insurer. In addition, the Insurance Act provides that policyholders' funds shall not be invested in property and securities apart from:

- shares of limited liability companies;
- shares in other securities of a cooperative society registered under a law relating to cooperative societies;
- loans to building societies approved by the Commission;
- loans on real property, machinery and plant in Nigeria;
- loans on life policies within their surrender values;
- cash deposits in or bills of exchange accepted by licensed banks; and
- such investments as may be prescribed by the Commission.

The Insurance Act provides that no insurer shall, in respect of its general insurance business, invest more than 35 per cent of its assets in real property; or, in respect of its life insurance business, invest more than 35 per cent of its assets in real property. 'Assets' for this purpose means assets equivalent to not less than the amount the amount of policyholders' funds in such accounts of the insurer.

Contravention of the above-stated prohibition on investments is an offence, and an insurer is liable on conviction to a fine of 50,000 naira.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

A company that wishes to acquire an insurance or reinsurance company must comply with the requirements for formation and licensing of an insurance and reinsurance company outlined in question 2. Furthermore, officers, directors and controlling persons of the acquirer will be subject to background checks, as section 14 of the Insurance Act stipulates that a change of the chief executive of an insurer must be approved by the Commission. An insurer must serve the Commission with a written notice for such an appointment must be approved by it. The Commission carries out background checks on directors and controlling persons of insurers. The Insurance Act bars individuals from taking up directorship positions for various reasons, including disqualification from professional practice, or conviction of an offence involving dishonesty or fraud.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The requirements regarding financing of the acquisition of an insurance company are regulated by the Insurance Act. The Act requires that a notice of intention to make an application be sent to the Commission at least three months before an application to acquire an insurance company is made. Applicants are also required to apply to the Federal High Court to sanction a proposed acquisition of an insurance or reinsurance company.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no provisions in the National Insurance Commission Act or in the Insurance Act stipulating any requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

The Insurance Act is silent on restrictions concerning investment in an insurance company by a foreign citizen or company. However, section 20 of the Companies and Allied Matters Act allows foreign citizens to incorporate companies, which involves the acquisition of shares. Thus, foreign citizens (including companies) can invest in insurance companies through the acquisition of shares without any restriction. However, it is important to note that if the investment entails a total acquisition of an insurance company, the requirements stated in question 10 (relating to change of control) would apply.

There are no specific rules or provisions under either the Insurance Act or the National Insurance Commission Act (NICA) regarding allowing a foreign government to invest in either an insurance or reinsurance company. Section 30(1)(a) and (b) of the Insurance Act, however, stipulates that no insurer shall amalgamate with, transfer to or acquire from any other insurer any insurance business or part thereof without the approval of NAICOM. It would appear that the type of investment permissible in an insurance or reinsurance company under the Act is one between Nigerian-registered insurance and reinsurance

companies, and not an acquisition or investment by a foreign government. NAICOM is empowered by section 7(e) of the NICA to regulate transactions between insurers and reinsurers in Nigeria and those outside Nigeria. However, the Securities and Exchange Commission (SEC), which was established under the Investment and Securities Act (ISA) 2004, generally oversees dealings in shares of companies. In this connection, section 99(2) of the ISA stipulates that notwithstanding anything to the contrary contained in any other enactment, any merger, acquisition or business combination between or among companies shall be subject to the prior review and approval of the SEC. Investments contemplated under the ISA also preclude investment by a foreign government.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Neither the Insurance Act nor the National Insurance Commission Act make provision for groups of companies containing an insurer or reinsurer (combining foreign and domestic insurance, reinsurance and other non-insurance companies in a holding company system).

Therefore, the supervisory framework for any group of companies would be regulated under the Companies and Allied Matters Act, which requires companies with subsidiaries, in addition to preparing individual accounts, to also prepare group financial statements (being accounts or statements that deal with the state of the affairs and the profit or loss of the company and its subsidiaries). There is no holding company or group capital requirements for insurers and reinsurers.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Generally in Nigeria, parties are free to enter into contracts on terms acceptable to them without any form of regulation by statutes or government agencies. This also applies to reinsurance agreements.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

There are no provisions in either the National Insurance Commission Act or the Insurance Act regulating the amount or proportion of ceded reinsurance or retention of risk.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Nigerian law does not require a reinsurer, whether foreign or local, to furnish any collateral in respect of or as a condition for concluding reinsurance contracts.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

There are no regulatory requirements in Nigeria for cedents to obtain credit for reinsurance of their financial statements.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The National Insurance Commission Act, Insurance Act, Companies and Allied Matters Act and Marine Insurance Act are the main statutes governing the affairs of insolvent and financially troubled insurance and reinsurance companies. These statutes also contain provisions allowing resort to the relevant provisions of the Companies and Allied Matters Act 1990.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The Insurance Act provides a priority list for settling debts (insurance or otherwise) that is separate and distinct from the priority list under the Companies and Allied Matters Act. The priority under the Insurance Act is as follows:

- liquidation fees;
- secured creditors;
- policyholders;
- other creditors;
- staff; and
- shareholders and directors.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The Insurance Act provides that intermediaries such as insurance agents, brokers, reinsurance brokers and loss adjusters must possess certificates of proficiency issued by the CIIN, be duly appointed by an insurer and be licensed by NAICOM to carry on business as insurance agents, brokers and loss adjusters. Furthermore, directors of firms or companies carrying on business as loss adjusters must possess professional qualifications in insurance, have experience in insurance business of not less than seven years or be certified by the Institute of Loss Adjusters of Nigeria. The registration of insurance agents, brokers and loss adjusters is subject to annual renewal. A breach of these provisions by any person not so licensed and registered under the Act attracts penal sanctions.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Under Nigerian law, a third party generally cannot maintain an action against the insurer to the exclusion of the insured. This is because an insurer can only be vicariously liable for damages that may be awarded against the insured on the basis of the relationship existing between the insured and the insurer. Although section 11 of the Insurance (Special Provisions) Decree No. 40 of 1988 applies, it merely confers the right on a third party to join the insurer as a party in respect of the claim.

The position differs for motor vehicle cases, as section 10 of the Motor Vehicles Third Party Insurance Act 1950 confers a right on a third party to sue an insurer directly.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Generally, Nigerian law does not allow an insurer to deny coverage on the ground of late notice of claim. However, section 69(2)(a) of the Insurance Act permits an insurer to avoid or deny payment to a person entitled to the benefit of any judgment if, before or within seven days of the commencement of the proceedings, notice of the proceedings leading to the judgment was not given to the insurer.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

There is no extra-contractual exposure for wrongful denial of a claim by an insurer under the Insurance Act. An insurer is only mandated (under section 70(1)(c)), where he or she does not accept a claim made by an insured or other person entitled thereto, to deliver a statement in writing stating the reason for disclaiming such liability to the person

making the claim not later than 90 days from the date on which the person delivered his or her claim to the insurer. Failure to comply with this provision attracts criminal prosecution and, on conviction, a fine of 500,000 naira.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The circumstances that can trigger an insurer's duty to defend a claim are those determined by the terms and conditions of the policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

This also depends on the terms and conditions of the policy, although generally the insurer's indemnity obligations are triggered when the insured event has occurred and the insured makes a claim for loss. This is the basis of a contract of insurance.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

There is no incontestability period beyond which a life insurer cannot contest coverage based on misrepresentations in the application. The principle of utmost good faith applies at all times to the contract. A misrepresentation discovered at any time, and particularly where it is fraudulent, is a ground for repudiating the coverage.

28 Punitive damages

Are punitive damages insurable?

The Insurance Act makes no provisions regarding punitive damages, but under the common law rule of indemnity, the assured is prohibited from taking out insurance over a risk of loss he or she has created. Consequently, insurance companies in Nigeria do not insure punitive damages.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

The Insurance Act makes no provisions regarding the liability of an excess insurer. However, under common law, an excess insurer has no obligation to pay a claim where the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits. The obligation of the excess insurer is only for the excess insured and not the primary obligation; as such, except if otherwise provided in the policy, there is no obligation on an excess insurer to assume liability where the coverage is otherwise unavailable without full exhaustion of primary limits.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

There is no obligation on the insurer if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it. Under Nigerian law, an insurer is only liable to the extent of the cover provided under the policy. The liability of the insurer in any case is the amount of a claim less the deductible or retention. The inability of the insured to pay on grounds of insolvency does not impose any further obligation on the insurer under the agreed terms of the policy. The deductible or retention in a policy is an obligation the insured voluntarily assumes in consideration for a reduced premium.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

The Insurance Act does not provide for priority of payment, so this is governed by the contract. However, where this is not covered by the contract, the practice among Nigerian insurance companies is to pay according to time of notification.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

The Insurance Act does not provide for allocation of payments among multiple policies triggered by the same claim, so this depends largely on the underlying contract.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Disgorgement or restitution claims are not insurable risks based on the principles under Nigerian law, especially where the disgorgement or restitution orders are the result of wilful misconduct on the part of the insured.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The courts would usually consider a single event resulting in multiple injuries or claims as one occurrence, and the amount of cover will be limited to the limits stated in the terms of the insurance policy.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

In a contract of insurance, a breach of the terms (whether called a warranty or a condition) shall not give rise to any right of, or afford a defence to, the insured unless the term is material and relevant to the risk or loss insured against.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Formal reinsurance disputes are not common in Nigeria, and insurers try to reach business solutions for their disputes without formal proceedings. However, in the event that business solutions cannot be agreed, parties may resort to arbitration (and arbitration is a common feature in most insurance agreements) and may, as a rare last resort, proceed to litigation in court. We are not aware of any precedent for substantive issues arising in the litigation or arbitration of insurance disputes. Substantive issues are dealt with under the common law of contract.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

The common issues that arise in reinsurance disputes are whether the claim is covered under the policy, whether the claim is made within the policy period and the amount to be paid.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

There are no special rules for reinsurance arbitration. Arbitration in Nigeria is generally governed by the Arbitration and Conciliation Act

2004. Section 26 of the Act provides that an arbitration award must state the reasons on which it is based unless the parties agree otherwise or it is an award made on agreed terms pursuant to a settlement. The award must also be in writing, be signed by the arbitrators, and carry the date on which it was made and the place of the arbitration.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

The powers of reinsurance arbitrators do not differ from those of other arbitrators under the Arbitration Act. Their powers over non-parties to the arbitration agreement are limited to administering oaths or taking affirmations of witnesses and, subject to the agreement of the parties, appointing experts to report to it on specific issues. They cannot compel witnesses to attend the proceedings but, if this is required, a court may make the appropriate order.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Yes; parties may seek to vacate reinsurance arbitration awards through the judicial system, but not for reasons of the adequacy or correctness of the award. The judiciary gives a lot of deference to arbitral awards, and an award can only be set aside or vacated for specific reasons. For instance, sections 29 and 30 of the Arbitration and Conciliation Act provide that decisions may be set aside by the court in the following circumstances:

- where a decision was made on matters that are beyond the scope of the submission to arbitration;
- where an arbitrator has misconducted him or herself; and
- where the arbitral proceedings or award has been improperly procured.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

This depends on the contract, and cannot be implied if it is not expressly provided for. Although a follow-the-fortune clause, where such obligation exists, limits the reinsurer's defence, the following defences are available to the reinsurer: bad faith or gross negligence on the part of the reinsured; or the settlement was not within the scope of the reinsurance coverage.

This does not make a reinsurer liable for risks beyond what was agreed on in the reinsurance certificate. In that regard, the reinsurer retains the right to question whether the reinsured's liability stems from an un-reinsured loss. A loss would be un-reinsured if it was not contemplated by the original insurance policy or if it was expressly excluded by terms of the certificate of reinsurance.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Utmost good faith between the reinsurer and cedent is a critical component of the custom and practice of the Nigerian reinsurance industry. In respect of the duty of disclosing all material facts, reinsurance contracts do not differ from those of insurance contracts, and is the duty of the assured to place the underwriter in the same situation as him or herself, and to give to him or her the same means and opportunity of judging of the value of the risk (ie, each party to the reinsurance transaction must hold the interests of the other party equally as dear as its own interests). The relationship between a reinsurer and a reinsured is one of utmost good faith, requiring the reinsured to disclose to the reinsurer all facts that materially affect the risk of which it is aware and of which the reinsurer itself has no reason to be aware.

A cedent's failure to fulfil its duty of disclosure will mean that the reinsurance contract will be voided. Generally, a reinsurer can rescind a reinsurance contract based on a cedent's misrepresentation if the misrepresentation or non-disclosure was made with an actual intent to deceive or the misrepresented matter was material. Based on this general rule of law, a reinsurer could rescind a reinsurance policy even if the cedent innocently misrepresented a material fact.

Other commercial agreements require good faith, but it must be noted that the rule governing the general law of contract is that each party to the contract is entitled to make the best bargain that he or she can, and as long as he or she does not make a false or fraudulent statement, he or she does not need to draw the attention of the other party to anything that might influence his or her judgement (the rule is caveat emptor). The reason for the caveat emptor rule is that the other party is expected to carry out his or her due diligence before entering into any contract and, if not satisfied with the outcome of the due diligence, can abandon the transaction.

Update and trends

The Commission recently revealed that it would release referral agency guidelines under which it would partner with professionals such as stockbrokers, lawyers and accountants as referral agents in the insurance distribution channels it has proposed to set up. In return, the stockbrokers will earn a percentage commission on any business they are able to generate for the insurance company. The Commission said this is part of its ongoing effort to deepen insurance penetration in the country.

The Commission is also in the process of commencing a verification of the capital resources of all insurance companies to ensure the protection of policyholders and beneficiaries of insurance contracts against unexpected losses by an insurance company. The verification of capital will entail a verification of the assets and liability of all insurance companies and wiil ensure that professionals who took part in financial reporting discharged their duties credibly.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

The Insurance Act regulates the operation of all types of reinsurance in Nigeria. However; facultative reinsurance is more common in Nigeria among local insurers than the alternative method of treaty reinsurance. The same set of laws applies to both methods of insurance.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Generally, there is no privity of contract between the policyholder and the reinsurer. As such, the policyholder cannot usually bring a direct action against the reinsurer for coverage; however, some reinsurance agreements contain cut-through clauses under which the policyholder is given a right to direct action against the reinsurer in the event of the insurer's insolvency, and in principle it is perfectly possible for reinsurers to agree to accept direct liability to the policyholder.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Ordinary principles of insolvency law shall apply in this situation, particularly the scheme under the Companies and Allied Matters Act 1990; under this scheme, the reinsurer will be liable to the insolvent insurance company. The liquidator of the insolvent insurance company can recover the amount of the claim as a debt from the reinsurer, while the policyholder will be a creditor of the insolvent company for the amount of the claim. The policyholder will rank in priority after the liquidation

fees and secured creditors in a winding-up proceeding under section 32(4)(c) of the Insurance Act.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The Insurance Act makes no provision for the type of notice and information a cedent must provide in respect of an underlying claim. Therefore, no particular format is provided under Nigerian law. In practice, such notices are usually in accordance with the policy agreement between the cedent and the reinsurer. Typically, however, a notification letter suffices together with apportionment of the risks and a survey report.

The remedies available are mostly common law-based remedies, and are as follows:

- rescission: the agreement between the cedent and reinsured is cancelled, both sides are excused from further performance and any money advanced is returned;
- payment of monetary damages; and
- any other remedy provided in the policy agreement.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

This largely depends on the provisions of the various reinsurance agreements between the parties to the policy. However, it appears that an approach that makes the policy agreement in force at the time of notification enforceable has been adopted by most insurers when the claims are being paid.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

Decisions arising from claims handling, settlement and allocation are not generally covered by any of the laws governing insurance. However, an aggrieved party may decide to request arbitration if the policy makes provision for arbitration, or approach the courts for a variation or total cancellation of a decision, if the decision is in itself not in accordance with sound insurance principles and if it is unreasonable.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Reimbursement obligations are dependent on the terms of the policy agreement between the cedent and reinsurer. Cedents are generally required to report incurred but not reported claims as part of their yearly reports. Unless otherwise agreed, the reinsurer will not generally indemnify its cedent on incurred but not reported claims.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Given that ECOs are not provided for under policies, a claim for such obligations will be subject to proof gathered through evidence and the common law principles of awards for damages that are direct losses arising from a breach of contract. In the event of bad faith, fraudulent practice and negligence, a successful plea of the elements of such bad faith and negligence would trigger an award in general and exemplary damages that are usually discretionary according to the circumstances of each case. Note that in cases where a breach of contract occurs and the party in the right is able to establish a wilful act or misconduct, the court, in addition to damages directly arising from the wilful act or misconduct, may award aggravated, general or punitive damages.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Norwegian financial supervisory authority, Finanstilsynet, oversees companies' conduct of business in the financial market, including companies that provide insurance and reinsurance services. Finanstilsynet supervises their financial strength and whether their level of risk is acceptable. Finanstilsynet aims to ensure financially sound and risk-aware insurers and pension funds with good management and control.

Finanstilsynet's supervision and the regulations are instrumental in ensuring that users receive correct and adequate information that enables them to understand the risk accompanying their choices (consumer protection). The regulations and Finanstilsynet's supervision are also important in safeguarding customers' short and long-term rights under insurance and pension contracts, and in instilling public confidence in the market.

For companies established within the EEA or EU carrying out business in Norway, the supervisory responsibility remains in general with the home member state. Companies domiciled outside the EEA or EU are subject to the full supervision of Finanstilsynet.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

To carry out insurance activity in Norway, a company is required to have a licence pursuant to the Act on financial institutions and financial groups of 10 April 2015 (Financial Institutions Act of 2015). Finanstilsynet grants authorisations to conduct insurance activities in Norway, unless for cases of importance or fundamental nature in which the Norwegian Ministry of Finance should grant the authorisation. A licence is granted for one or more classes of insurance (life insurance, non-life insurance and reinsurance).

Companies subject to authorisation are required to have their head offices in Norway. The authorities can deny an application if not convinced that any owner that holds a qualified share in the company is suitable. The application shall be denied unless more than three-quarters of the company's share capital in a share issue is without preference for subscription by the shareholders or others.

The applications shall be refused if:

- the insurance company does not have its headquarters and registered office in this country unless the insurance company seeks permission pursuant to Chapter 5 of the Financial Institutions Act of 2015;
- the terms regarding ownership requirements, minimum requirements of initial capital and the requirements to the management of the insurance company (compare sections 3-3 to 3-5 of the Financial Institutions Act of 2015) are not met;
- it is not satisfied that the insurance company will be able to meet requirements for proper business (arising from sections 8-16 to 8-20, 13-4 to 13-7, 13-13, Chapter 14 and section 16-1 of the Financial Institutions Act of 2015); and
- there are reasons to assume that the insurance company will not meet the requirements of the law or regulations issued pursuant to the law, or that the business would be contrary to public policy.

An application for a licence should, inter alia, include a business plan for the company's first three years of business and the articles of association.

The business plan should include:

- a report on issues such as ownership and management after the establishment of the insurance company;
- controlling mechanisms;
- how the insurance company intends to provide capital to fulfil the capital requirements for businesses described in the business plan;
- a capital and solvency ratio for each of the first three years;
- a budget with an income statement;
- balance sheets and financial analyses for each of the first three years of operation;
- the insurance company's group affiliation; and
- anti-money laundering measures.

Further, the insurance company shall include information about the classes of insurance that it will offer and explain principles the company will apply for premium calculation.

The application should also include, inter alia:

- information on qualifications;
- work experience;
- tasks or employment in other financial institutions;
- a certificate of good conduct from the police for each director;
- deputy and observer on the board;
- the CEO and other persons to be included in the actual business management or parts of the company; and
- other individuals with key corporate functions.

In general, the authorities would normally require further information with respect to the capital requirements, actuarial function and organisation of the firm and its activities.

Companies established within the EEA or EU that have a licence from their home authority have a right to carry out the licensed business in Norway through a branch or by way of cross-border services on the basis of the European passport (single licence principle). EEA or EU companies are required to notify their home state regulator in accordance with the notification procedure.

Companies established outside the EEA or EU must obtain a licence if they intend to conduct insurance activities in Norway. One specific requirement is that Finanstilsynet has entered into an agreement on supervisory activities and supervisory cooperation with the home state regulator of the foreign company.

The application shall be decided upon within six months.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Pursuant to the Personal Data Act, insurance companies are required to obtain an authorisation from the Norwegian Data Protection Authority

because they are handling personal information in connection with, inter alia, customer management, invoicing and implementation of agreements. If the undertaking chooses to outsource processing personal data wholly or partly to other enterprises, data processors, the relations between a data controller and a data processor must be regulated by a data processor agreement.

Besides that, no further authorisations are required as long as the business is carried out within the scope of the licence granted, and without any alterations or amendments that Finanstilsynet would need to approve.

A licence is subject to the terms therein, and may be granted to one or more branches of insurance, or part of such branch. Licences for companies that carry out direct insurance shall be granted for specified classes of insurance. A licence can also be granted for a specific geographical area or a specific group of insured, or in any other way.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The application will not be granted if the board members, CEO or other persons that de facto manage the business do not have the necessary experience, cannot certify that that they have not been convicted for a criminal offence, or otherwise have shown that they are not suitable.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

The start-up capital of Norwegian insurance companies needs to stand in 'reasonable proportion' to the insurance activity that a company shall carry out under the licence granted. The current minimum equity capital requirement is €3.7 million for a life insurance company or €2.5 million for other insurance companies; however, it is €3.7 million if the entity provides third-party insurance related to motor vehicles, aircraft or ships or other liability insurances, or credit and guarantee insurance, and €3.6 million for a reinsurance company. Nonetheless, the requirement is €1.2 million for a reinsurance entity, which, pursuant to its articles of association, only may assume reinsurances limited to a determined group of policy holders.

Insurance companies shall maintain free and unrestricted capital in the amount of the solvency margin, which is calculated on the basis of the overall volume of the business. The solvency margin is calculated as a percentage of either the gross premium income or the gross claims payments.

The Solvency II regime entered into force in Norway on 1 January 2016.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Companies are required to build several technical reserves to ensure their ability to meet their obligations arising out of insurance policies.

Such reserves include, inter alia, reserves for unearned premiums refund of premiums, claims outstanding and anticipated losses. The technical reserves are established by methods set out in a special regulation.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

There are no general regulatory requirements with respect to insurance products offered for sale. A company may not, however, offer insurance against criminal penalty if such insurance is deemed contrary to the legal order. Insurance contracts are, however, regulated by the general Insurance Contract Act, which contains several provisions that cannot be deviated from in contracts.

There are certain specific requirements regarding insurance in relation to, for example, damages caused by motor vehicles under the Act on Damages Caused by the use of Motor Vehicles of 1961, and regarding insurance in relation to industrial injury under the Act relating to Industrial Injury Insurance of 1989. Another example is the Norwegian natural hazards insurance, which is a statutory insurance scheme. A person who takes out fire insurance on property and households consequently also has insurance against natural hazards.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The supervisory regime shall ensure that companies are solid, risk-aware and that they have good governance. Supervision consists of on-site and off-site supervision. Finanstilsynet has developed an audit methodology using three risk modules concerning market and credit risk, insurance risk in general insurance and insurance risk in life insurance. Each module consists of a guide for evaluating the risk level and a guide for evaluating the system for management and control of the relevant risks. The factors to assess (best practice) in the guidelines for the management and control are based on the modules for banks, relevant recommendations of the IAIS and experiences gained from its supervision. Sub modules are applied for evaluating institutions' systems for management and control in connection with on-site inspections.

The methodology (stress tests) applied in assessing the level of risk is largely based on that present in Solvency II.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

As a starting point, an insurance company may only carry on insurance activities and activities naturally associated with insurance activities (section 13-1 of the Financial Institutions Act of 2015).

Insurance companies shall provide for prudent asset management. In order to ensure the fulfilment of its insurance liabilities, an insurance company shall ensure that assets covering the technical provisions are at all times appropriately and satisfactorily invested viewed in relation to the nature of the insurance liabilities, and in terms of safety, risk diversification, liquidity and return. Further rules on asset management are set out in separate regulations for respectively non-life insurance companies and life insurance and pension companies, including the amounts of investments.

Finanstilsynet supervises companies' systems for management and controls of asset management and enterprise risk. The level of risk at any given time should be appropriate to the company's risk-bearing capacity. Should Finanstilsynet find that an insurance company has invested its capital contrary to law or regulations, or in an otherwise unsatisfactory or evidently detrimental manner, it may order the company to change the investment within a stipulated period.

Pursuant to section 13-9 of the Financial Institutions Act of 2015, an insurance company may not own, or by voting represent, 15 per cent or more of the shares or units in a company carrying on activities that, pursuant to section 6-1 of the Insurance Act, may not be carried out by insurance companies. There are certain exceptions.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Owners of qualified holdings shall be fit and proper to own such holdings and to exercise such influence in the undertaking as is conferred by the holdings. 'Qualified holding' means a holding that, calculated pursuant to the rules of section 6-1 of the Financial Institutions Act of 2015, represents 10 per cent or more of the capital or votes of the institution, or which otherwise enables the exercise of significant influence on the management of the institution and its activity.

An acquisition whereby the acquirer will become the owner of a qualified holding, or the owner of 20, 30 or 50 per cent of the capital or voting rights, may not be carried out without prior notification to Finanstilsynet in accordance with the procedure set out in the sections

6-1 et seq of the Financial Institutions Act of 2015. There are certain specific rules as to the calculation of the holdings.

The notification shall state the size of the holding it is to acquire and the size of the overall holding in the financial institution after the acquisition. The notification shall disclose information on factors that will be of significance for the calculation of the owner's overall holding. Further, the notification shall also contain information that will be of significance for assessing whether authorisation shall be granted.

The question of whether authorisation in respect of the acquisitions of qualified holdings shall be granted shall be decided within a period of 60 working days from the date Finanstilsynet confirms receipt of the notification (the assessment period). If the Ministry or Finanstilsynet has made a request in writing for further information before 50 working days have elapsed, the request shall suspend the assessment period from the time the request is made until the requested information is received, but not for more than 20 working days, or for more than 30 days if the acquirer is not subject to supervision or is domiciled outside the EEA. Other requests for further information shall have no effect on the length of the assessment period.

In the decision of whether authorisation shall be granted, the Ministry or Finanstilsynet shall, with due regard for the need to assure proper and adequate management of the financial institution and its activities, and in consideration of the level of influence the acquirer as owner will be able to exercise in the institution after the acquisition, undertake an assessment of the acquirer's fitness and propriety as owner of his or her overall holding after the acquisition, and of whether the acquisition of the holding is financially adequate in relation to the institution's current and future activities. There are certain specific issues that will be taken into consideration, including, in particular, the acquirer's general reputation, professional competence, experience and previous conduct in business relationships.

If certain thresholds are met, the acquisition also needs to be notified to the competition authority.

Certain officers, directors and other persons of the acquirer are subject to background investigations. The identity of the owners of the insurance company shall be known and the Ministry shall be convinced that the owners of qualifying holdings are fit to hold such holdings and may exercise such influence in the insurance company as the ownership stake gives reason to. The insurance company cannot have directors, manager, other persons in the actual management thereof or other persons with key positions who:

- it is assumed do not have the necessary qualifications and professional experience to exercise the position or task;
- are convicted of a criminal offence, and the offence gives reason to assume that the person will not be able to safeguard the position or task in a proper manner; or
- in such position, or in the conduct of other duties, has demonstrated such behaviour that it is reasonable to assume that the person will not be able to safeguard the position or task in a proper manner.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements concerning the financing of the acquisition of an insurance or reinsurance company; however, there are certain restrictions on credit assistance in relation to the acquisition of shares in an insurance or reinsurance company organised as public or private limited liability companies in the applicable company laws.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no specific requirements concerning the acquisition of a minority interest in insurance or reinsurance companies, provided that the investment does not constitute a qualified holding; see question 10.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no specific or different requirements regarding investment in an insurance or reinsurance company by foreign citizens, companies or governments; however, the requirements for the acquisition of a qualifying holding apply.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Finanstilsynet supervises financial groups consisting of both insurance and non-insurance companies. As a starting point, all units in a financial group are mainly regulated equally, for example with respect to equity requirements; the same equity is required for a holding company as well as the companies in the group and on a consolidated basis. Finanstilsynet does not supervise insurance companies domiciled in another EEA or EU member state.

Group supervision principles are imposed as a consequence of the implementation of the EU Solvency II regime.

As a starting point, capital requirements shall be applied on a consolidated basis in respect of a holding company or other parent company in a financial group; however, there are certain options for exemptions.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

The content of reinsurance agreements is generally not subject to regulatory supervision.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

An insurance company shall at all times have reinsurance that is adequate in relation to the company's risk exposure and its financial position. This applies to risk exposure in general, and covers both financial and insurance risks.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Subject to the reinsurance agreement, there are no additional regulatory collateral requirements that have to be observed by reinsurance companies conducting reinsurance transactions.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Reinsurance agreements would be taken into account when considering the solvency requirements of an insurance company.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The Financial Institutions Act of 2015, Chapter 21, provides a specific procedure in connection with insolvency of financial entities, including insurance companies, in Norway. Regular debt negotiation or

winding-up proceedings may not be initiated against insurance and reinsurance companies.

The board and managing director of an insurance company have a notification duty if there are reasons to believe that the insurance company cannot meet its liabilities as they fall due, the insurance company cannot fulfil the minimum capital requirements or there are circumstances that may result in serious loss of confidence or losses that will substantially weaken or threaten the solvency. In such circumstances Finanstilsynet shall, in cooperation with the insurance company, clarify what measures that are necessary to apply, and impose measures if needed. If Finanstilsynet assumes that the insurance company does not have a secure financial basis for continued satisfactory operation, a notification shall be made to the Ministry. The notification shall include an assessment of whether the company should be placed under public administration. The Ministry may resolve that an insurance company shall be placed under public administration.

Once a public administration order has been made, certain effects come into play, including, inter alia, an administration board becoming appointed, and the company's former governing bodies becoming inoperative and having an obligation to provide information on the institution's position and activities to the administration board.

If, within a year after the order, it is not probable that the insurance company can resume operations in the near future, be merged with others or have its activities taken over by others, the administration board shall wind up the insurance company's activities and undertake settlement with the creditors. The authorities may stipulate a different period. In the case of winding up and settlement of the estate, the rules of Chapter VIII et seq of the Debt Settlement Proceedings and Bankruptcy Act apply correspondingly insofar as appropriate. Finanstilsynet makes such decisions as are required pursuant to that Act.

When the bankruptcy order is issued, all accessible assets will be confiscated and converted into monetary amounts. The means will be distributed among the creditors in accordance with the provisions of the Creditors Recovery Act and the Debt Reorganisation and Bankruptcy Act insofar as they apply.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Certain claims are considered preferential (in addition to the claims that enjoy statutory lien, and secured creditors), and thus will rank before other claims. The most important ones, in ranked priority, are claims originating from the bankruptcy proceedings, certain wage-related claims as well as unsettled income tax and VAT. Unsecured creditors will receive dividends on a strictly mathematical parity basis.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The Insurance Mediation Directive (2002/92/EC) is implemented into Norwegian law. Insurance mediation activities in Norway are mainly regulated by the Act on Insurance Mediation of 2004.

In order to carry out an insurance mediation activity in Norway, a company is required to obtain an authorisation from Finanstilsynet. Applications for authorisation shall contain information of significance to the assessment of whether authorisation should be granted, including, inter alia, the following:

- a description of which categories of insurance or risk the insurance brokerage firm will mediate in Norway;
- compliance with organisational requirements;
- compliance with rules on insurance coverage;
- compliance with qualification requirements; and
- the honourable conduct of the management and for insurance brokers.

The activities may start once the conditions for authorisation are met and the insurance brokerage firm has received confirmation from Finanstilsynet.

The CEO or other persons that de facto manage the business shall at all times possess the knowledge and competence necessary in relation to the insurance brokerage firm's activities and, in cases where the management provide intermediation services, they must comply with the qualification requirements applicable to insurance brokers and insurance agents.

Insurance brokers who are registered in another EEA state may commence activities in Norway through a branch or as a cross-border service one month after Finanstilsynet has received notification of the planned activities from the supervisory authority in the undertaking's home country. Insurance brokers who are registered in another EEA state and pursue activities in Norway must comply with certain additional requirements, such as complying with good brokering practice, information requirements, and informing the Norwegian Natural Perils Pool and Finanstilsynet of their activities.

Insurance agencies registered in another EEA state can commence their activities in Norway once they have notified the competent authority in their home country.

The coming implementation of EEA-rules corresponding to the Insurance Distribution Directive (2016/97/EU) of 20 January 2016 on insurance distribution (recast) will involve amendments of the current Act on Insurance Mediation.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

A third party that has a claim against an insured covered by liability insurance may, according to the Insurance Contract Act, bring a direct action against the insurer. Both the insured and the insurer are under an obligation upon request to inform the third party whether such liability cover exists.

If a third party brings a direct action against the insurer, the insurer is required to inform the insured without due delay and keep the insured informed about the handling of the claim. Any admission from the insurer towards the third party is not binding for the insured. If court proceedings are initiated by the third party against the insurer, the insurer may demand that the third party includes the insured in the same court proceedings.

The insurer may, in a direct action, invoke the same defence as the insured itself has against the third party. The insurer may also invoke any defence it has towards the insured under the insurance contract, as long as it is based on circumstances prior to the occurrence of the insured event. The latter defence is, however, not available if the insured's liability cover is required by law, and the insurer knew or ought to have known that this was the case.

These provisions may be deviated from in insurance contracts linked to businesses of a certain size and business carried out abroad, and under certain other situations. However, the third party's claim has some mandatory protection if the insured becomes insolvent.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

The insured is normally required to notify the insurer without undue delay, or within one year at the latest. If the insured fails to notify the insurer, the insurer can deny cover without demonstrating prejudice. This is, however, different with a third-party claim under a liability cover (see question 22).

If the claim has been notified to the insurer before it is time barred under the General Limitation Act, it cannot be time barred before a six-month period has lapsed from the date the insurer:

- states that the claim is (now) time barred under the Limitation Act;
- states that the insurer will invoke this Act; and
- informs the insured (or third party) in accordance with set formal requirements of the possibility to file a complaint against the insurer's decision.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

There are no specific provisions for insurance companies subjecting the insurer to extra-contractual exposure for wrongful denial of claims. However, the company is exposed to an obligation to pay late payment interest, which includes a penalty element, if the claim is not settled within two months of the claim being notified to the insurer. In addition, the insurer will be exposed to carrying both its own and the insured's (third party's) costs in unsuccessful court proceedings.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The insurance contract will regularly regulate the insured's rights and obligations to defend the claim.

The general regulation seems to be that the insured is required to defend the claim but may, according to the insurance contract, recover its defence cost within the insured sum.

The insurer may have a contractual right to approve any legal advice retained by the insured in advance, and it is normally stated that the insured may not give any admissions or enter into any settlement agreements with the claimants without prior written consent from the insurer.

In cases where a third party brings a direct action against the insurer under the Insurance Contract Act, which regularly is the situation in liability cases, the insurer will be the defendant and as such have a direct self-interest to defend against the claim.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The insurer's payment obligation should normally be settled within two months of the date the insurer is notified of the claim. If not paid within two months, late payment interest applies. However, this is conditioned on the fact that the insured (or third party) has provided sufficient documentation for the claim.

This main rule is subject to the terms of the insurance contract, which may include an obligation for the insurer to pay the agreed indemnity on demand subject to (potential) reimbursement.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Regarding life insurance, the insurer can only contest coverage based on misrepresentation in the application if the insurable event has occurred within two years or the insurer has notified the insured within two years that such misrepresentation will be invoked.

This incontestability period does not apply if fraud is involved or, in the case of disability insurance, if the insured has acted with gross negligence.

28 Punitive damages

Are punitive damages insurable?

The company may not offer insurance against a criminal penalty if deemed contrary to public policy.

As punitive damages cannot be awarded in Norway, it has not been clarified whether such damages would be covered by this prohibition.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

If not regulated in the contract, the excess insurer has no obligation to 'drop down and defend' and pay a claim without full exhaustion of primary limits.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

As a main rule, the insurer does not have an obligation towards a third party to pay the self-insured retention, even if the third party brings a direct action against the insurer under a liability cover.

However, this may be different under special mandatory schemes, such as, for example, the scheme for damages caused by vehicles or other mandatory schemes where the cover is regulated by law or regulations.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

In the case of multiple claims that are all substantiated and covered by the same policy and the insured sum is exceeded, the insurer is required to distribute the insured sum pro rata among the claimants.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

If the same loss is covered by more than one policy, the insured may choose which policy (or policies) to use, up and until the insured has recovered its loss.

If more than one insurer is involved, the respective insurers are liable in proportion to the cover they have granted to the insured.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Restitution claims will generally not be considered a loss, and the coverage of such claims is regularly excluded from the agreed liability cover.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The court will in general decide this based on an interpretation of the insurance contract, in particular if the insurance contract includes an aggregation clause or series of loss clause.

In the case of mandatory liability insurance, or specific insurance contracts regulated by law, the legal question of whether a single event resulting in multiple injuries or claims constitutes one or more occurrences under an insurance policy will depend on the court's interpretation not only of the insurance contract, but also of the said law or regulation and case law.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The main rule according to the Insurance Agreement Act in cases of misstatement in the application is not rescission but a right for the insurer to terminate the insurance contract with a 14-day notice period. However, if the insured has acted fraudulently, the insurer may rescind immediately, and not only the said insurance contract but all insurance contracts with the insured.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

There are no public statistics about whether such disputes are solved without formal proceedings. These contracts are mainly of an international character, which regularly contains an arbitration clause, and

if Norwegian law is agreed, the proceedings are then regulated by the arbitration agreement and the Norwegian Arbitration Act.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

As there are no public statistics available, it is difficult to give an overview of the most common issues that arise in reinsurance disputes. It seems, however, that common issues include the scope of the cover agreed in the reinsurance agreement, and whether the reinsurer should accept settlements entered into by the insurer as being binding for the reinsurer.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

According to section 36 of the Norwegian Arbitration Act, the award shall include the panel's reason for the decision and whether it is unanimous. If the decision is not unanimous, the award shall include information about the judge that does not agree, and which points the judge disagreed on.

An award that only affirms a settlement between the parties to the arbitration does not include a reason.

The above can be deviated from in accordance with an agreement between the parties to the arbitration proceedings.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

The arbitrators do not have any power over non-parties to the arbitration agreement, and non-parties to the arbitration proceedings are not bound by the award. The arbitrators cannot summon witnesses to appear before the panel, but may request the ordinary courts to obtain witness statements from witnesses and secure other evidence.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

The arbitration award may not generally be appealed through the judicial system, but either party may, within three months of receipt of the award, initiate court proceedings to set aside the award.

Only certain grounds can be invoked in order to set aside the award:

- one of the parties to the arbitration agreement lacked legal capacity;
- the arbitration agreement is void according to the law agreed on, or lacking such agreement, according to Norwegian law;
- insufficient notice to a party of either the appointment of an arbitrator or of the arbitration proceedings, or if a party was not given sufficient opportunity to present his or her case;
- the arbitration award went beyond the subject matter of the arbitration agreement;
- the panel is not composed correctly;
- the proceedings did not follow the rules to such extent that it affected the arbitration award; or
- the award or its enforcement violates public policy.

If only parts of the award are affected, only the affected part of the award is set aside.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There is no general legal obligation for the reinsurer to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of a contractual provision to that effect.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

In contract law, a general obligation of loyalty and good faith applies, which may influence the interpretation of the reinsurance agreement. This duty of care implied is similar in principle to that implied in other commercial agreements.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There are no separate regulations established that distinguish between facultative and treaty insurance. The different nature of the two types of reinsurance agreements may, however, have an impact on the interpretation of the agreed cover of risk, and how the good faith principle applies in concrete disputes.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

As a starting point, only parties to a reinsurance contract may bring a direct action against a reinsurer for coverage. Thus, the insured cannot bring a direct action against the reinsurer under Norwegian law. The insured may, however, in non-life insurance contracts, be protected by a guarantee scheme in the event that the insurer becomes insolvent.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

There is no general legal obligation on the reinsurer to pay a policyholder directly if such obligation is not included in the reinsurance agreement. However, an insurer will not go through regular winding-up proceedings, but will be placed under public administration (see question 19). In addition, special guarantee funds may have been established for special risk.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

If a circumstance or insurable event occurs, the insurer will typically notify the reinsurer in accordance with the reinsurance agreement. Such notification should describe the claim, and the circumstances upon which the claim is based. The insurer should also continuously update the reinsurer and liaise in potential settlements situations.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

The allocation of underlying claim payments or settlements depends at the outset upon the wording of the reinsurance agreements. In the event of unclear regulation in the reinsurance contract, the allocation principle explained in question 32 may be relevant.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

These issues are not particularly regulated in the regulations, but rather in the reinsurance agreement, which should give the reinsurer a contractual right to review the cedent's claims handling. This is also supported by the good faith principle. As a last resort in the case of disputes and court proceedings, a reinsurer may require evidence that the insurer has complied with the reinsurance agreement when handling the claim.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

This depends upon the interpretation of the reinsurance agreement.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

There are no general ECOs for the cedent towards the insured (see question 24), and this issue does not generally arise. If the cedent has such obligations towards the insured, whether the reinsurer will be obliged to reimburse the insurer, in full or in part, depends on what is agreed in the reinsurance contract.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Since April 2014, insurance is regulated by the Central Bank of Russia and the Ministry of Finance. The Central Bank of Russia, in its capacity as 'mega-regulator', undertakes regulation and control in all spheres of the financial market. It is the authority that issues and revokes insurance licences, checks compliance with insurance legislation, including requirements for capital and reserves, and handles the registry of insurance professionals. The Ministry of Finance elaborates state policy and prepares draft bills in the sphere of insurance.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Insurance and reinsurance companies should be formed as commercial entities (limited liability companies or joint-stock companies). The law provides some specific requirements regarding the names of insurance and reinsurance companies, which should clearly specify the type of insurance business they carry out.

Insurers, reinsurers and brokers must have a licence (see question 3) issued by the Central Bank.

Insurers, reinsurers and brokers can make pooling arrangements and participate in unions and associations. Entities such as unions, associations and pools do not require separate licences.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

A licence is required to conduct insurance and reinsurance. To qualify for a licence, insurers or reinsurers should provide the Central Bank with a set of documents that includes registration and corporate documents, relevant rules of insurance, calculation of tariffs, proof of their financial stability, and evidence of the qualifications of their general director and chief accountant.

Normally licences are issued for an undefined period. Where the Central Bank discovers that the insurer or reinsurer has infringed an insurance regulation, it will issue a decree ordering the offender to rectify the violation. If the decree is not complied with, the Central Bank is entitled to suspend the insurer's licence, in which case the insurer is prevented from entering any further insurance contracts.

In the event of serious or repeated violations of insurance regulations, licences may be withdrawn, which results in the termination of the insurance business for the relevant insurer or reinsurer.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

Qualification requirements for the officers of insurers or reinsurers form part of the licensing requirements. Chief executive officers of insurance and reinsurance companies should have a higher economic or financial education, and have at least two years' professional experience in the insurance business or other financial business.

Chief accountants should also have higher education in economics or finance and must have worked as accountants with Russian insurance or reinsurance companies for at least two years in the five years preceding their appointment.

General directors and chief accountants of Russian insurance and reinsurance companies, including subsidiaries of foreign insurers or reinsurers, should have a clean criminal record. Persons who were previously held liable for violations that resulted in withdrawal or suspension of a licence, or held liable under certain types of administrative charges, cannot qualify.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Insurance companies dealing with medical insurance only have to show a minimum capital of 60 million roubles. For other insurance companies, the base capital is 120 million roubles. A capital of 240 million roubles is required to carry out certain types of life insurance, property and financial risk insurance, and the threshold for reinsurance companies is 480 million roubles.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

There are a number of decrees issued by the Ministry of Finance and the Central Bank that govern matters relating to reserves, such as the types of reserves that an insurance company must maintain; the method of calculation of reserves; types of and requirements for assets that can cover (secure) reserves; and the structure of such assets. The requirements for reserves vary depending on the type of insurance (life or non-life, obligatory drivers' liability insurance, etc).

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

An insurance company may either provide life insurance or non-life insurance. For each product, the insurer must elaborate and approve the rules of insurance. The rules of insurance must comply with the Civil Code of the Russian Federation and other acts relating to specific types of insurance. These rules are then filed with the Central Bank. The Central Bank is allowed to review the rules and point out any inconsistencies with the law it may find, ordering the insurer to

amend the rules accordingly. Nevertheless, the Central Bank carries no such obligation. When entering into an insurance contract, parties may deviate from the approved rules by including relevant provisions to the contract or policy.

Rules of insurance must be placed on the website of the insurance company.

For some types of obligatory insurance, the authorities in the relevant field may participate in the elaboration of governing legislation or check compliance with the obligatory insurance regulations. However, they do not interfere in the contractual relations between the insured and the insurer.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The Central Bank is the authority that effects control over the insurance and reinsurance companies. This includes analysis of reports that insurance and reinsurance companies file to the Central Bank. Reports are filed on a yearly basis and must contain information on the major financial parameters of the insurer or reinsurer's businesses. The Central Bank is also allowed to undertake inspections of insurers' activities. There is currently no legal provision regarding the frequency of such inspections, and they are carried out at the discretion of the Central Bank.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

There is a specific regulation issued by the Central Bank on this issue. The Regulation provides, inter alia, a list of assets in which the insurers and reinsurers are entitled to invest. The list includes securities issued or warranted by the Russian Federation, mortgage securities, shares of private companies, loans to assureds under life insurance contracts, money deposits, real estate, and gold and other precious metals. Shares and securities must be either issued on the Russian market or subject to a number of requirements, including stock exchange listings and appropriate ratings. Insurers and reinsurers may not invest into assets under pledge or mortgage.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Under Russian law, 'change of control' of a legal entity shall be understood as a transfer of shares in the charter (share) capital to a third person. Rules of transfer of shares in the charter capital are subject to the corporate form of a legal entity and to its charter, but do not depend on the type of the legal entity's activity (insurance, reinsurance or other). Accordingly, the law does not provide specific requirements for the change of control of insurers and reinsurers; general rules of transfer of shares shall be applied.

There are no requirements in respect of officers and directors of the acquirer. Nevertheless, the law establishes requirements for the managers (including chief accountants) of the insurance (or reinsurance) company itself (see question 4); these are licensing conditions that concern the education and professional experience of managing staff. Thus, if a change of control of an insurer or reinsurer entails a change in its managers, new staff must meet licensing requirements.

Additional restrictions may apply if the acquirer is a foreign entity (see question 13).

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements regarding financing of the acquisition of insurance or reinsurance companies except for restrictions relating to the investments by foreign persons and entities (see question 13). In other aspects, general provisions of civil, banking and corporate law shall be applied.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

No specific requirements in this regard are set out. The general provisions of corporate law are applied.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

In order to conduct insurance business in Russia, the insurer needs a licence, which is issued to Russian legal entities only. Therefore, representative offices of foreign insurance companies cannot act as insurers in Russia, and separate legal entities need to be formed under Russian law.

Such entities, if the share of the foreign insurer is more than 49 per cent, are restricted from providing certain types of life insurance, and insurance of state-owned organisations. If such share is more than 51 per cent, the insurer is not authorised to offer obligatory motor insurance. To form a subsidiary of a foreign insurer to allocate or transfer shares in a Russian insurance company to a foreign shareholder, a special permit from the Central Bank is required. This can be refused if the overall share of foreign investment on the Russian insurance market exceeds 50 per cent.

In order to establish a subsidiary insurance company in Russia, the foreign insurer must show that it has carried out insurance business in its main place of business for at least five years.

Some of the above restrictions do not apply to insurers that are more than 49 per cent owned by foreign shareholders if such insurers were established or reorganised by 22 August 2012 and were, by that date, entitled to carry out insurance business in Russia.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

The Law on the Organisation of Insurance Business in the Russian Federation (Law) does provide requirements for an insurance group holding (head) company and participants, but with no specification of whether these relate to Russian entities only, or also to foreign ones. At the same time, the meaning of the Law and of insurance regulation in general can lead to the conclusion that the requirements pertain to Russian companies. In particular, insurers shall comply with:

- financial requirements;
- requirements related to the order of the formation of reserves;
- requirements related to the order and conditions of investments;
- requirements related to the regulatory ratio of the capital and liabilities; and
- other requirements provided by the Law and regulatory acts of the supervisory authorities.

Each member of the insurance group shall submit reporting forms to the supervisory authorities in the order provided by the Law and regulatory acts of the supervisory authorities.

The head company of the insurance group shall also comply with the above requirements on a consolidated basis, including reporting to the supervisory authorities on a consolidated basis in the established order provided by the Law.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Reinsurance agreements are considered as bilateral (or multilateral) transactions; that is, actions directed at the establishment, change or termination of civil laws and duties. Accordingly, the general provisions on obligations and on contracts shall apply. Important amendments to the Law on the Organisation of Insurance Business in the Russian Federation with regard to reinsurance were adopted in July 2013 and became effective as from January 2014. Until then, participants in the reinsurance business applied customs commonly used in foreign markets to the limited Russian regulation. The amended Law provides the possibility for reinsurers to issue not only reinsurance contracts, but also other documents used in accordance with the customs of the reinsurance business. The definitions of different types of reinsurance are also provided by the amended Law.

In other respects, the Law did not change the general approach to reinsurance. Unless otherwise provided by the reinsurance agreement (or a document issued pursuant to reinsurance business customs), rules regulating insurance of business risks are applied to the reinsurance agreement. Only risks of the reinsured itself may be reinsured, and only for its benefit. The reinsurance agreement shall be void with regard to a person who is not the reinsured, and shall be considered concluded for the benefit of the insured.

Reinsurers are not liable under insurance contracts.

Some of the restrictions applicable in insurance (eg, regarding the obligation to indicate the insured amount in the insurance contract, the activities of non-Russian insurers) do not apply in reinsurance.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Russian law does not provide specific amounts. In the light of the amended article 13(1) of the Law on the Organisation of Insurance Business in the Russian Federation, the size of retention shall be established by the accounting policy of the reinsured (ie, of an underlying insurer). Risks exceeding the retention shall be reinsured.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Collateral requirements concern business solvency of reinsurers: they must have economically justified tariffs, sufficient reserves and capital adequacy.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

No specific requirements are set out.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

There are two main statutes that govern these issues: the Law on the Organisation of Insurance Business in the Russian Federation and the Law on Insolvency (Bankruptcy).

The Law on the Organisation of Insurance Business in the Russian Federation provides both financial requirements and the consequences of insolvency of an insurer or reinsurer. The Law on Insolvency (Bankruptcy) provides the grounds for matters such as insolvency, steps required to prevent a bankruptcy and applicable procedures.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

Generally, creditors' claims fall under three groups of priority. In cases of insolvency proceedings in relation to an insurer, the claims of the insureds may fall into the first or the third group of priority. Thus, the first group will include claims for personal injury and moral damages, and assureds' claims arising out of endowment policies. The second priority group includes employees' claims for earned wages and similar claims. All other creditors fall into the third group of priority. While, generally, all creditors of the third group are in equal position, where the debtor is an insurance company the situation is different, and the creditors are divided into five subgroups. The first subgroup includes claims arising out of obligatory insurance contracts. The second subgroup is allocated to claims under life insurance contract. Claims arising out of insurance contracts whereby liability for personal injury is insured form the third subgroup. The fourth subgroup comprises claims under civil liability insurance (except liability for personal injury) and property insurance contracts. All other creditors are part of the fifth subgroup.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

In Russian insurance practice, there are intermediaries of two types: insurance agents and brokers. The activity of insurance agents is not licensed. The activity of insurance brokers shall be licensed, and the Law provides a number of requirements to insurance brokers that relate, inter alia, to the qualifications of the manager and chief accountant. There are also certain requirements related to activity, non-compliance with which could negatively influence the licence. Regulation of activity of insurance agents is less restrictive. Both agents and brokers who carry out their activity in Russia should be permanently established or permanently reside in Russia.

Foreign brokers are not allowed to act in Russia, with the exception of reinsurance and other cases set out by the law.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Third parties may have a direct claim against insurers where the insurance is obligatory or where such possibility is expressly provided by law. For other cases of liability insurance, the wording of the relevant rules is somewhat ambiguous, and different approaches are taken in court practice and legal science on this matter. The governing approach, however, is that direct action is not allowed.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Insurers sometimes try to refuse payment, citing late notice. Court practice, however, stands on the principle that the insurer must show that late notice resulted in prejudice for the insurer. There are a number of court and arbitration cases where the insurer's argument on late notice was not accepted as prejudice was not shown.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Where the insurer commits a grave violation of the insurance contract (including a wrongful denial of a claim), the insured, as well as any other interested party, may file a complaint to the Central Bank. In the past such complaints did not have any serious effect. However, recent practice has shown a number of cases where insurers were forced by the insurance authority to pay insurance compensation to avoid the suspension of their licence.

The insured may also be entitled to statutory interest if the insurer delays the insurance payment, unless a different interest rate is provided in the insurance contract. Where consumer protection law is applied to the insurance contract, the court may apply a higher interest rate, a fine for wrongful denial of claim as well as compensation for moral damages.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Only a relevant provision of the insurance contract triggers a liability insurer's duty. Under general rules of the Civil Code, the liability insurer has no obligation to defend the claim. There is a general concept that the insured should act in such a manner as if the insurance contract did not exist (including, inter alia, mitigating damages and defending the claim).

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

This is a difficult question under Russian law. Generally, an insurer's payment obligation becomes due when the insured event occurs. In the case of liability insurance, the insurer's payment obligation is triggered where the insured's liability to the injured party is established in a manner prescribed by law or the insurance contract. Unless otherwise provided by the insurance contract, this would happen when the insured's liability is confirmed by a judgment or award of a competent court or arbitration or by an amicable settlement agreement, provided it was entered into with the insurer's consent.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Disclosure rules for life insurance are the same as for other types of insurance. They do not provide for an incontestability period.

28 Punitive damages

Are punitive damages insurable?

Russian law does not prohibit punitive damages. Therefore, although there is a general prohibition for insurance of illegal interests, this would not include insurance of punitive damages. The problem lies elsewhere: as punitive damages may be recovered under a contract, they would be insurable under the contract liability policy. Insurance of the insured's contractual liability is allowed only for cases expressly provided in the legislation. For example, it is possible to insure contractual liability arising out of construction contract, but this is not possible for a contract of forwarding.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Such type of obligation is not specifically provided for the law. However, the parties may agree its terms at their discretion, and the duties of the excess insurer would be governed by the respective insurance contract.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Under Russian law, there is no difference between a deductible and a self-insured retention. In fact, a deductible is defined as a 'part of the risk retained by the insured'. The insured's inability to pay the deductible does not create any additional obligation on the insurer. Some types of obligatory insurance, however, do not allow a deductible in the insurance policy.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

This depends on why there are multiple claims under the same policy. If there were several insured events, then each event would be investigated separately, and the insurer would make a decision to pay or to refuse payment on the basis of such particular investigations. The priority would then depend on the speed of such investigations or, if the insurer refused payment, on the dates when the insureds would obtain court judgments to recover the insurance monies.

If, however, multiple claims arise from the same incident but are due to several co-insureds according to their respective interests, then, provided that there are no grounds for refusal of any of their claims (including possible individual grounds relating to only one or several co-insureds), the priority of their claims would be equal.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Most likely, liability triggered by the same insured event would be covered by one policy that is valid for the time period when the event occurred, even though the exact scope of liability may be established subsequently. If the claims are different in nature (eg, property and liability insurance), they will be treated separately. In the case of double insurance, insurers will be liable pro rata to their respective insured limits, as compared with the amount of their loss.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

The law only prohibits insurance of illegal interests, and there are no signs that disgorgement or restitution may be found as such by the courts. In practice, however, cover for disgorgement should be specifically sought and negotiated. Restitution cover is offered on a larger scale, for example, as a part of a mortgagor's insurance package.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

This largely depends on the wording of the insurance contract. In the absence of relative wording, the court would analyse aspects such as whether the claims are filed by one or different claimants, whether those claims have a similar or different legal nature, and what is the proximate cause of each claim.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Under the Civil Code, the insured must disclose all material information about the risk. Information is considered material if it is included in the insurer's questionnaire or similar document. Therefore (apart from for non-marine insurance – see below), the duty of the insured is not to make misrepresentations or omissions when answering the insurers' questions. The test for disclosure is subjective (ie, only such information should be disclosed that was known to the insured). If the disclosure obligation is not met, the insurer is entitled to file a claim for the rescission of the insurance contract in court.

The situation is different for marine insurance, where it is the duty of the insurer to define what information is material, and where the test is objective (information must be disclosed if it is known or ought to be known by the insured). While in non-marine insurance the insurer, in cases of misstatement, must file a separate court claim to invalidate the insurance contract, in marine insurance the insurer may, in cases where the disclosure obligations were breached, unilaterally refuse payment.

Update and trends

The review in 2014 of the leading legislation in the insurance field, the Law on the Organisation of Insurance Business, introduced some new rules, such as electronic policies and the launch of a unified motor insurance database. 2014 also saw a major reform of the obligatory motor insurance law, with a serious increase in the level of insurers' liability.

The government continues to discuss suggestions to introduce a number of new types of obligatory insurance. For some of the existing types of obligatory insurance, new laws or bills increase the minimum insured amount and introduce other additional regulations.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

In Russia, parties to a reinsurance agreement generally tend to come to a compromise. However, if disputes cannot be solved by means of negotiation, they are, as a rule, considered by the courts.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

One controversial issue relates to payments after expiry of the reinsurance agreement but under claims that occurred within its validity. This issue is connected with the interpretation of an insured accident under reinsurance agreements. In several cases, the commercial courts interpreted an insured accident under reinsurance agreements as payment of insurance compensation to original assureds and, based on that, refused claims of re-assureds (insurers in underlying contracts), arguing that compensation on underlying insurance was made when the reinsurance agreements had terminated. This approach of the court infringes the interests of both the primary assureds and the insurers. In fact, under Russian law, reinsurance is qualified as the insurance of the risk of an obligation to pay insurance compensation.

Other important issues in reinsurance disputes are discrepancies between insurance and reinsurance cover (gap in cover), that is, cases when reinsurance agreements are not made in accordance with the underlying contracts (regarding validity of compensation under underlying contracts, etc). Difficulties can also arise in connection with a 'follow the leader' clause (if any in the reinsurance contract), and this is caused by lack of regulation of this concept in the law and insufficient contractual definition.

Recently there was a dispute where a court – upon application of the reinsurer – determined that a contract of reinsurance was unconcluded. The judgment was argued by reference to a reinsurance slip that was issued and signed by the reinsurance broker, but that was not signed or stamped by the reinsurer. The higher courts upheld this judgment. Although this case has not become a common issue of disputes yet, it exposes a risk to the general practice of concluding reinsurance contracts, and we remind parties to reinsurance contracts of the specificities of Russian regulation in this area.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

As a rule, reinsurance disputes are referred to state commercial courts rather than to arbitrations. Both court judgments and arbitral awards must include the motivation for the decision.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitrators of reinsurance disputes have general powers of arbitrators provided by the Law on Arbitration Courts and the Law on International Commercial Arbitration. Claims brought by or against non-parties to the arbitration agreement shall be terminated on grounds of lack of competence unless the claimant and the defendant agree the competence of the respective arbitration.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Arbitration awards can be contested or enforced through competent commercial courts as part of the state judicial system. The law provides the scope of powers of commercial courts while considering such cases. Generally they are limited to formal (procedural) evaluation of an award; accordingly, courts shall not reconsider a dispute on its merits. Courts may enforce arbitration awards or refuse enforcement in the few cases expressly provided by the law, but they cannot amend arbitration awards.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The obligations of a reinsurer to 'follow the fortunes' of an original insurer and the scope of the original insurance are contractual conditions and therefore shall be regulated as the parties agree. Despite this, reinsurers are entitled to raise objections to decisions of cedents irrespective of whether the obligation to follow is expressly provided in the reinsurance agreement. Reinsurers' objections may vary, depending on reinsurance agreements and specific cases (eg, late notice, incomplete file, wrongful compensation of underlying claim).

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The implementation of a good faith principle in Russian insurance and reinsurance law is specific and differs from the concept of good faith in certain other jurisdictions. There is no act that would expressly declare the principle of good faith both in insurance and reinsurance. However, the law sets out an obligation on parties to display good faith at all stages of an insurance or reinsurance contract. The obligation to comply with the good faith principle is mutual; the insured or reinsured and the insurer or reinsurer should satisfy certain requirements.

In particular, the following rules may be considered as the principle of good faith in reinsurance: the duty of disclosure, and obligations to notify changes affecting the risk, to pay premium, to procure confidentiality of information and to pay compensation.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

No. Both types are regulated by the Law on the Organisation of Insurance Business in the Russian Federation.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

No. This is provided for by article 967(3) of the Civil Code: 'In case of reinsurance, the person liable to the insured for payment of insurance compensation or the insured sum under the basic contract of insurance remains the insurer under this contract.'

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

There is no such obligation.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

The types of information to be provided to a reinsurer and the rights of a reinsurer in the event of failure to disclose such information shall be defined in the reinsurance agreement. Generally, this shall include giving notice to the reinsurer on the occurrence of an incident having features of an insured event, and informing of developments relating to the incident or the claim handling. Where the insurer fails to provide such notice in a timely or sufficient manner, the reinsurer may be entitled to raise objections to the decisions of the cedent or exercise other remedies as provided by the reinsurance contract.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

Reinsurance agreements must provide (inter alia) a clear specification of the reinsured risk and the share of the reinsurer in the respective risk. Otherwise, the reinsurance contract shall not be considered concluded.

Payments or settlements of a claim made by the reinsured shall be allocated depending on the share of every reinsurer in the insured risk according to reinsurance contracts. The underlying insurance policy or policies should not necessarily provide a specification of reinsurance allocations, as insurance and reinsurance are considered separate contracts and, as a rule, reinsurance does not affect the underlying insurance contract.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

The law provides no specific types of review; since all the mentioned issues are contractual, they are considered depending on the terms of agreements and particular circumstances.

References to a claims control clause or a simultaneous payment clause frequently appear in reinsurance contracts. These clauses, on full control over claims handling or the payment of a claim by the reinsurer at the same time as a claim is paid on the original insurance, are not directly regulated by Russian law. However, the fact that they are widely used in reinsurance practice makes these clauses 'a custom of reinsurance business' in the sense of the Civil Code and so the source of Russian reinsurance law. The scope of review shall be the same as in original law and practice.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Commutation payments are not common in Russian practice. The law does not oblige reinsurers to reimburse claims that are not yet due under the reinsurance agreement. Nevertheless, reinsureds do not create risk by agreeing a final settlement with reinsurers before closing claim files under underlying contracts. This is connected not only with commercial, but also with taxation, issues. All the same, it appears in practice that reinsureds obtain advance payments of unconditional expenses and the right to claim other sums when they become due.

Compensation for late reported claims (see question 23) is agreed by the parties on a case-by-case basis.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Russian law does not oblige reinsurers to pay claims resulting from occurrences outside the terms and conditions of the contract. Reimbursement for extra-contractual losses can be agreed by the parties on a case-by-case basis.

**This chapter is accurate as of June 2016.*

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Swiss Financial Market Supervisory Authority (FINMA) supervises insurance and reinsurance undertakings, insurance intermediaries and groups as well as other financial institutions (eg, banks, stock exchanges, securities dealers and collective investment schemes).

Insurance and reinsurance operations are regulated on the federal level. The Swiss Federal Financial Market Supervision Act 2007 as amended (FINMASA) sets out supervision principles and instruments of FINMA in respect of all financial markets. The Swiss Federal Insurance Supervision Act 2004 as amended (ISA) and the Swiss Federal Insurance Supervision Ordinance 2005 as amended (ISO) contain the rules and regulations for insurance and reinsurance undertakings.

Social insurance schemes (such as for mandatory disability, unemployment or health and accident insurance) are subject to the supervision of the Swiss Federal Office of Social Insurance or the Swiss Federal Office of Public Health, respectively. Occupational pension funds are mainly subject to supervision by the cantons, although there is also a federal supervisory body.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Any company with its domicile in Switzerland must obtain a licence from FINMA before engaging in insurance or reinsurance activities. It must submit to FINMA an application that consists of a formalised business plan and ancillary documentation on:

- financial aspects (minimum share capital, solvency, organisational fund, opening balance sheet, pro forma financial statements, reinsurance or retrocession plan, etc);
- management aspects (information on the board of directors and executive management);
- organisational aspects (by-laws, organisational regulations, risk management and other policies, outsourcings, subsidiaries); and
- business rationale, material shareholders, insurance classes and products.

Applications may be filed with FINMA in draft form. FINMA customarily decides on an application within three months of receipt of the complete application documents, although the process may be substantially longer depending on the complexity and quality of the initial draft application.

Before or during the licence application process, the company is formed and entered into the commercial register. For regulatory purposes, the company must have the legal form of a corporation or cooperative. The predominant legal form is the corporation. The founders may determine the specific location within Switzerland based on the local business and tax environment. A company is regularly established with the corporate law minimum share capital of 100,000 Swiss francs and funded up to the relevant regulatory minimum share capital (see question 5) by means of a capital increase immediately before the licence grant.

Insurers whose domicile is abroad must obtain a licence from FINMA in respect of insurance activities conducted in or from Switzerland (subject to differing provisions in international treaties, and currently only the case with Liechtenstein). An insurance activity is deemed to be conducted in Switzerland if one of the policyholders or insured persons or the insured risk is located in Switzerland. A FINMA licence is not required for mere reinsurance activities conducted in Switzerland by companies domiciled abroad, or for insurance of marine, air transportation, international transports and war risks as well as risks located abroad.

In order to obtain the licence, foreign insurers must set up a branch in Switzerland, designate a branch head, demonstrate that they are duly licensed and adequately capitalised in their home jurisdiction, have an adequate organisational fund in Switzerland and deposit with the Swiss National Bank collateral generally of 10 per cent of the required solvency margin. Since Switzerland is not part of the EU or EEA, companies with their domicile in any EU or EEA member state may not conduct business cross-border or through a branch office on the basis of the EU passport principle and home state regulator regime.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Once FINMA has licensed a company to conduct insurance or reinsurance business (see question 2), no further licences, authorisations or qualifications are required as long as the business is carried out in line with the business plan. Amendments to the business plan are subject to FINMA approval.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The persons entrusted with the ultimate direction, supervision, control and management must enjoy a good reputation and ensure sound business practices. The board of directors must be composed of at least three members who, as a whole, have the necessary insurance expertise, and are able and have enough disposable time to effectively supervise and ultimately direct the company. Board members may not simultaneously be part of the executive management (insurance companies must implement this rule by 1 July 2018). At least one-third of the members of the board of directors must be independent. Board members are deemed independent if they:

- are not and have not in the previous two years been employed in some other function within the insurance company or by the insurance company's audit firm as lead auditor of the regulatory audit responsible for the insurance company;
- have no commercial links with the insurance company that, in view of their nature and scope, would lead to conflicts of interest; and
- are not a shareholder of the insurance company and do not represent any shareholder.

FINMA may approve exceptions from foregoing criteria, provided there is good reason to do so (eg, for reinsurance captives or subsidiaries of insurance groups and conglomerates supervised by FINMA).

Insurance companies within supervisory categories 2 and 3 (very important, complex, high-risk or large and complex, significant-risk) must establish an audit and a risk committee. The chair of the board of directors may not be a member of the audit committee or the chair of the risk committee. The foregoing rules must be implemented by 31 December 2019.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

The minimum share capital is set by FINMA generally within a range of 5 million to 12 million Swiss francs for life insurers, 3 million to 8 million Swiss francs for non-life insurers and 3 million to 10 million Swiss francs for third-party reinsurers.

In addition to the minimum share capital requirement, insurers and reinsurers must have sufficient free and unencumbered capital resources in relation to their activities (solvency margin).

Two methods are used to evaluate solvency whereby Solvency I is only applicable if required by an international treaty (currently only the case for non-life insurers based on the treaty between Switzerland and the EU):

- the Solvency I test: based on the statutory balance sheet, the necessary capital resources are determined by the volume of premiums or claims (required solvency margin) and the eligible capital resources (available solvency margin); and
- the Swiss Solvency Test: based on an economic balance sheet and a market-consistent valuation of assets and liabilities, the required capital resources are determined in relation to the insurance, market and credit risks (as well as operational risks) to which an insurer or reinsurer is exposed (target capital) and the eligible capital (risk-bearing capital).

Insurers and reinsurers must also have an organisational fund reserved for financing the setting up and any material expansion of business operations. The organisational fund is 20 per cent of the minimum share capital, unless FINMA determines otherwise.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurers and reinsurers must establish adequate technical reserves to cover their entire insurance activities. Technical reserves are established based on actuarial methods, and the accountable actuary is responsible for ensuring their adequacy. In general, insurance technical reserves consist of reserves to cover expected liabilities under written insurance contracts; and claims equalisation reserves to account for uncertainties inherent in actuarial projection methods, random fluctuations in insurance losses and claims expenses, and changes in the general environment that may cause the actual claims to materially deviate from the actuarial estimate.

From an equity perspective, Swiss regulation provides that insurers and reinsurers must allocate at least 20 per cent of their annual net profits (10 per cent for life insurers) to the general reserve until this reserve amounts to 50 per cent of the total paid-in nominal share capital. The lower corporate law thresholds do not apply. This requirement limits the ability of insurers and reinsurers to distribute dividends.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

Swiss insurance and reinsurance regulation sets rules at the company level and does not provide for a systematic and preventive control of insurance products (contract terms and rates), except for products offered in Switzerland in connection with occupational pension plans, supplementary insurance to social health insurance and insurance of damages caused by natural hazards.

The contractual relationships between insurers and policyholders in Switzerland are governed by the Swiss Federal Insurance Contract Act 1908 as amended (ICA) and, supplementary to it, by the Swiss Code of Obligations 1911 as amended (SCO) and the Swiss Civil Code 1907 as amended. The freedom of contract is the governing principle, which is limited by a moderate number of mandatory provisions of the ICA, namely provisions that may not be modified by insurers at all or not to the disadvantage of policyholders or insured persons.

FINMA is under a duty to intervene against improper market conduct such as the use of contract terms that violate mandatory provisions of the ICA or other applicable laws, or that provide for an allocation of rights and obligations that is significantly contrary to the nature of the contract, provided that such improper market conduct occurs repeatedly or may affect a large number of persons, or if a substantial unequal treatment of policyholders is not justifiable by legal or insurance technical reasons.

The creation and use by the insurance industry of common claims expenditure statistics and common insurance contract terms (eg, the standard policy terms of the Swiss Insurance Association) are subject to the rules and restrictions of Swiss competition law. The Swiss Federal Competition Commission has indicated that its practice is closely aligned with the block exemption regulations of the European Union.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Insurance companies must currently comply with quarterly financial reporting obligations to FINMA (this has been as short as one month during the financial crisis) as well as a number of yearly reporting obligations. The yearly reporting obligations include but may not be limited to the annual report, annual financial statements, annual supervisory report and annual reports on Solvency I (if at all applicable; see question 5), on the Swiss Solvency Test, on tied assets, on the activities of the insurance company relating to financial derivatives and on own risk and solvency. FINMA has discretion to decide on shorter reporting cycles for the annual reports or to add additional reporting obligations. Furthermore, insurance companies must prepare an annual report on their overall financial situation and solvency that must be made publicly available.

Insurance companies must have an insurance regulatory auditor that conducts an annual insurance regulatory audit and submits a report to FINMA on such audit. The insurance regulatory auditor also has additional ad hoc reporting obligations to FINMA for certain critical findings. FINMA rarely conducts on-site examinations itself, but usually determines that such examinations are to be conducted by the insurance regulatory auditor.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Swiss law does not contain any overall rules for allowed or disallowed kinds and amounts of investments that insurance and reinsurance companies may make (contrary to the Swiss regulatory regime for pension funds), beyond the general solvency supervision requirement that asset management by insurance and reinsurance companies must be in line with generally recognised best market practices.

However, detailed provisions and rules exist on the type and amounts of assets that the insurance company may assign to its tied assets, as well as on how such tied assets must be managed (not applicable to reinsurance companies as they do not have tied assets). In general, tied assets must be chosen primarily on the basis of security, the financial situation of the insurance company and the predicted development of the insurance portfolio, whereby a fair market return and appropriate diversification must be sought, while ensuring the foreseeable liquidity requirements at all times (in particular, also in various adverse scenarios for which the insurance company must conduct appropriate stress tests).

In general, the asset categories that may be assigned to an insurance company's tied assets are:

- cash and other money market investments;
- bonds;
- structured products;
- securitised debt and other promissory debt;
- shares (if they are traded in a regulated market and can be sold at short notice);
- real estate in Switzerland owned by the insurance company and participations in real estate companies if the participation amounts to at least 50 per cent;
- debt that is secured by real estate property in Switzerland;
- hedge funds and private equity;
- financial derivatives that serve hedging purposes and are not leveraged;
- participations in collective investment schemes; and
- funds.

Additional specific requirements and restrictions apply to all listed categories pursuant to Swiss law and FINMA practice. In particular, the allocation of financial derivatives by insurance companies to its tied assets is especially limited.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Swiss law provides that whoever intends to acquire a direct or indirect participation in an insurer or a reinsurer with its domicile in Switzerland must notify FINMA thereof if the thresholds of 10, 20, 33 or 50 per cent of the capital or voting rights will be reached or exceeded by such an acquisition. FINMA may prohibit acquisitions or impose conditions if the nature and scope of the participation could endanger the insurance undertaking or the interests of the insured persons. Therefore, acquirers of a material participation must substantiate that they have sufficient resources to finance the transaction and are able to ensure sound and proper management of the insurer or reinsurer. The members of the board of directors and executive management must pass a fit-and-proper test (see also question 4).

Notification to FINMA is made after signing. Approval or a statement of non-objection by FINMA is customarily a condition precedent to the closing of the sales transaction. FINMA decides within four to eight weeks following receipt of the complete notification documents (however, no statutory time limit applies).

Similar notification duties apply to any person that intends to reduce its participation in an insurer or reinsurer with its domicile in Switzerland if such a participation falls below any of the thresholds set out above, and any insurer or reinsurer with its domicile in Switzerland that intends to acquire or sell a participation in any other undertaking and thereby passes any of the thresholds set out above.

In addition, the insurer or reinsurer must report to FINMA any material change in their shareholder base as a business plan change.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements regarding financing of the acquisition of an insurer or reinsurer.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no specific requirements regarding investors acquiring a minority interest in an insurance or reinsurance company, if such minority does not exceed 10 per cent of share capital or share votes (in which case, the answer to question 10 applies).

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no specific insurance regulatory restrictions for foreign, natural or legal persons to acquire an equity participation in an insurer or reinsurer located in Switzerland.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Swiss law contains consolidated frameworks for supervision of both insurance (or reinsurance) groups and conglomerates. Two or more companies constitute an insurance group if:

- at least one is an insurance company;
- they are, as a whole, primarily engaged in the field of insurance; and
- they form an economic unit or are otherwise connected with each other (ie, through influence or control).

Two or more companies constitute an insurance conglomerate if:

- at least one is an insurance company;
- at least one is a bank or securities dealer of considerable economic importance;
- they are primarily engaged in the field of insurance; and
- they form an economic unit or are otherwise connected with each other (ie, through influence or control).

FINMA may impose consolidated supervision (but has no obligation to do so) on an insurance group or conglomerate if a Swiss company is part of such an insurance group or conglomerate, and if it is factually managed from Switzerland or if it is managed from abroad but is not subject to comparable group supervision abroad. If FINMA, as well as a foreign regulator, both claim total or partial supervisory jurisdiction, FINMA will attempt to find an agreement with the foreign regulator and will consult with the involved Swiss company before taking its decision. In practice, FINMA is most interested in supervision of large groups that have a complex structure.

The consolidated supervision by FINMA is supplementary to the individual company supervision. All companies that form part of the supervised group must comply with information requests by FINMA. Supervised insurance groups must provide FINMA with information on their organisation, reporting and management structures at a group level, and FINMA determines one group company to be its counterpart for all regulatory requirements and requests. FINMA must be informed in advance of all important group internal events ('important internal events' are all those events that involve loans, guarantees, changes to capital, reinsurance transactions, cost-sharing agreements or other risk transfer instruments that significantly impact the financial situation of the group or group companies) and a consolidated report of all important internal events must be prepared every year. FINMA must also be informed in advance of any intended acquisition or sale of a significant participation by any group company. Furthermore, the supervised group must provide FINMA with a report on group-wide risk concentrations and management as well as the results of the group-wide own risk and solvency assessment and on the group-wide Swiss Solvency Test. All these obligations also apply to insurance conglomerates. Insurance groups and insurance conglomerates are required to meet their required solvency margin on the basis of a group-wide Swiss Solvency Test, which must be based on consolidated group figures. With approval by FINMA, a granular group-wide Swiss Solvency Test may be used as an alternative.

As part of the business plan that must be filed with FINMA for an insurance licence, an applicant must inform FINMA of the organisation and the regional scope of business of both the applicant itself and the reinsurance group or conglomerate to which the applicant belongs.

The insurance licence can be conditional on the existence of an appropriate group supervision by a foreign supervisory authority.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

The principle of freedom of contract prevails in reinsurance. In general, the terms of reinsurance contracts are valid as long as they are not unlawful or against public policy in the sense of the SCO. Most importantly, the rules and restrictions of the ICA do not apply to reinsurance contracts.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Swiss insurance regulation does not per se limit the amount of insurance risks that insurers may cede to reinsurers.

However, insurers must, as a rule, continue to account for the full technical reserves for the ceded risks and maintain a pool of tied assets as a function of the gross amount of such full technical reserves (gross accounting principle). At the request of insurers, FINMA may allow:

- that claims of non-life insurers against reinsurers under reinsurance contracts are fully or partially admitted as tied assets. The financial strength or rating of the relevant reinsurer is the key factor for FINMA to determine the admissibility of reinsurance claims. Limitations apply in respect of counterparty risks; and
- that life insurers are partially exempt from the gross accounting principle and entitled to reduce their technical reserves after ceding risks to reinsurers.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no specific regulatory collateral requirements for reinsurers in reinsurance transactions. If, however, a reinsurance claim is secured by collateral or another security, cedents may, subject to FINMA's approval, be in a position to either procure reinsurance coverage from unrated reinsurers or allocate a larger portion of the reinsurance claim to their tied assets (see question 16).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

Swiss law does not limit the creditability of reinsurance for insurance companies on their financial statements overall. However, certain limitations apply for the recognition and process of crediting reinsurance to tied assets (see question 16). Separately, any reinsurance or retrocession of risks is fully credited to the target capital under the Swiss Solvency Test within the scope of the actual quantifiable risk transfer. The risk of default of the reinsurance provider is reflected in the calculation of the target capital.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

In the event of an insolvency of an insurer or a reinsurer with its domicile in Switzerland, the provisions of the Swiss Debt Enforcement and Bankruptcy Act 1889 as amended are applicable to the extent that the ISA does not provide otherwise. The ISA was amended on 1 September 2011, and FINMA issued the Insurance Bankruptcy Ordinance 2012 as amended (IBO), with the following main features:

- FINMA will revoke the licence and initiate bankruptcy proceedings in the case of a substantiated concern of over-indebtedness or serious liquidity problems of an insurer or reinsurer, and where there are no prospects of reorganisation or a failure of the same;
- FINMA will nominate and supervise one or several bankruptcy liquidators;
- FINMA convenes creditors' meetings and appoints creditors' committees on the liquidator's request; and
- insurance claims set out in the books of the insurer or reinsurer are deemed to have been submitted in the bankruptcy proceedings.

In the event of non-compliance by an insurer or reinsurer with the law or an order of FINMA, or any other endangerment to the interests of insured persons, FINMA may adopt protective measures as necessary (and proportionate) to safeguard the interests of the insured persons, such as the following:

- prohibit the unrestricted disposition of the insurer's or reinsurer's assets;
- order the deposit or blocking of assets;
- assign authority from directors and officers to a third person;
- assign insurance or reinsurance portfolios to a third party (with the consent of such third party);
- order the liquidation of tied assets;
- request the dismissal of the accountable actuary or any person entrusted with the ultimate direction, supervision, control or management, and prohibit them from engaging in any insurance activity for up to five years;
- assign assets to the tied assets; and
- order the extension of payment terms and adjournment of due dates in the event of financial distress.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The insolvency of an insurance or reinsurance company licensed by FINMA is subject to a separate and specific insolvency procedure managed directly by FINMA pursuant to the IBO, with additional specific rules for foreign insurance companies in Switzerland. FINMA has substantial discretion to deviate from the applicable general Swiss law rules in the insolvency proceedings of an insurance company. In short, general Swiss law on insolvency foresees that the claims of secured creditors are satisfied out of the net proceeds from the realisation of the collateral, whereas for unsecured creditors, Swiss law distinguishes three classes of creditors that are satisfied in order of priority, with the class next in priority only receiving the remaining surplus after satisfaction of all claims of the prior class.

Additionally, certain specific rules apply regarding priority of claims. In the insolvency of an insurance company, the costs of the insolvency proceeding itself are satisfied first, followed by the claims of policyholders that result from the books of the insurance company to the extent they are covered by the proceeds of the liquidation of tied assets (not applicable to insolvency of a reinsurance company because it does not have tied assets). Any surplus falls into the general bankruptcy estate, and any shortfall is allocated to one of the three general creditor classes. This mechanism does not automatically apply to life insurance policies that are secured by tied assets, for which FINMA may decide on a separate procedure.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

Insurance intermediaries are persons offering or concluding insurance contracts on behalf of insurance undertakings or other persons.

A registration duty applies to insurance brokers, defined as insurance intermediaries that are independent from any insurance undertaking in the legal sense (eg, that do not have an exclusive distribution agreement) and in the economic sense (eg, that do not achieve the majority of commissions from one or two insurance undertakings in any calendar year). Insurance agents (tied insurance intermediaries) are entitled but not obliged to register themselves. The register is public and accessible online. A registration requires sufficient professional qualifications of the insurance intermediary or, if the insurance intermediary is a legal entity, its personnel, and professional indemnity insurance that covers damages of up to at least 2 million Swiss francs per year or equivalent financial security.

For natural persons, registration also requires the provision of an extract from the criminal register that must not contain entries involving activities incompatible with the business of an insurance intermediary, and an extract from the debt enforcement register that must not contain references to outstanding certificates of unpaid debts whose underlying claim is incompatible with the business of an insurance intermediary.

Insurance intermediaries are required to inform prospects of their identity, their ties to insurers and the processing of personal data. They may not engage in any intermediary activities in Switzerland for the benefit of insurance undertakings that are subject to a licensing requirement (see question 2) but have not been granted a licence from FINMA.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

The obligations of insurers under insurance policies are generally only towards policyholders and insured persons. Direct actions of injured parties require a basis in the insurance policy or statutory law, such as:

- motor liability insurance (article 65 of the Swiss Federal Road Traffic Act 1958 as amended (Road Traffic Act));
- liability insurance for fuel and gas pipes (article 37 of the Swiss Federal Pipeline Act 1963); and
- nuclear energy liability insurance (article 19 of the Swiss Federal Nuclear Energy Liability Act 2003).

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

On occurrence of the insured event, rightful claimants (eg, policyholders or insured persons) must notify insurers of the insured event as soon as they become aware of the event and their insurance claim. Notification must be made in writing if the insurance policy so provides.

If the rightful claimant has omitted the immediate notice:

- with the intention of preventing the insurer from establishing the circumstances of the insured event in a timely manner, the insurer is not bound by the insurance policy and may deny coverage;
- with (gross or light) negligence, the insurer may reduce its coverage by the amount the damage would have been reduced in the case of a timely notice; and
- without any attributable fault, the notice can be made to the insurer immediately on removal of the hindering circumstances without loss of coverage.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Punitive damages are not available under Swiss law. Except in very exceptional circumstances, an insurer wrongfully denying cover does not run a risk of being held liable based on statutory law. If a court finds that the cover was wrongfully denied, the insurer has to settle the claim, including any damages caused by the delayed settlement as well as the rightful claimant's legal expenses.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Insurance policies customarily stipulate that:

- the insurer must indemnify the insured person from justified third-party claims as well as costs and expenses to defend unjustified third-party claims, to the extent covered by the insurance policy;
- the insurer may handle the claims (which exceed the deductible amount) and, in particular, represent the insured person in the negotiations with the injured person; and
- the insured person must assign the necessary authority to the legal representative determined by the insurer if legal proceedings are instigated, and refrain from acknowledging a claim without the prior consent of the insurer or from raising actions that contravene the provisions of the policy.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

The insurer must settle a claim if it has finally established the occurrence of an insured event and the amount of the respective damage. Indemnification payments will not become due and payable as long as the policyholder has not provided all information reasonably requested by the insurer regarding the event and necessary to assess the claim. If the insurer has been provided with all relevant information, the indemnification payments will become due and payable four weeks thereafter (even if the insurer has not made its final assessment by that date). If the policyholder provides all relevant information to a single part of an insurance claim, such a part will become due within the same time period. In the event of an acknowledgement of the claim by the insurer, the insurance claim becomes immediately due and payable.

A contractual clause that provides that an insurance claim becomes due only after being acknowledged by the insurer or upheld by a court decision is null and void.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

There is no incontestability period under the ICA. The insurer may in general contest coverage based on misrepresentation in the application at any time (subject to the rules set out below).

If the policyholder omits to notify or incorrectly notifies the insurer of a significant risk factor that he or she knew or should have known about which he or she was questioned in writing, then the insurer is entitled to terminate the insurance policy. The termination right expires four weeks after the insurer has obtained knowledge of the breach of the notification duty. If the insurer terminates the contract, its obligation to indemnify the policyholder for damages ceases (and the insurer may rightfully contest coverage and claim back payments made) if and to the extent that the omitted or incorrect notification of the significant risk factor has influenced the occurrence or extent of the damage.

If a life insurance policy that may be surrendered terminates, the insurer must provide to the insured person the benefits due in the event of surrender.

28 Punitive damages

Are punitive damages insurable?

Punitive damages are not available under Swiss law. Further, Swiss courts may be precluded from awarding punitive damages even if the applicable foreign substantive law provides for those damages owing to Swiss public policy or if in connection with product liability according to article 135 of the Swiss Federal International Private Law Act 1987 as amended (IPLA).

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Swiss statutory law does not provide for any 'drop down' of insurance coverage of an excess insurer if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits. Unless otherwise agreed in the policy, the excess insurer is liable towards the policyholder only for its own share and entitled to provide for its own defence, regardless of the primary insurer's insolvency.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Swiss law does not regulate retainer amounts or deductibles. Deductibles are commonly agreed in Switzerland. Insurance policies customarily contain the right of insurers to pay out the full indemnification amount directly to injured persons, and to request policyholders

to reimburse without objection any deductible not applied. Insurers ultimately bear the risks that policyholders become insolvent and thus are unable to repay the deductible. Self-insured retentions are not customary in Switzerland.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is no general Swiss law rule as to the priority for payment for multiple claims under the same insurance policy. Pursuant to the Road Traffic Act, if the policyholder caused damage to several persons, which in total exceeds the insured sum set out in the insurance policy, the claim of each injured person against the insurer is reduced proportionally, and the insurer or the initial claimant may cause the competent court to request other injured persons to raise their claims in the same court proceedings.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Both cumulation (ie, the insured receives multiple payments based on multiple policies) and coordination (ie, the insured receives only one payment based on multiple policies) exist in Swiss law depending on the type of insurance policies triggered by a claim and the interaction with coverage of the same claim by other liable persons.

For indemnity insurance, if a policyholder has obtained cover for the same risk from more than one insurer, and if the total cover exceeds the insurance value (double insurance), then the policyholder must notify this to each insurer in writing (and the insurer may deny coverage if he or she does not do so with the intention of obtaining an unlawful monetary advantage), and each insurer is liable only proportionally (individual cover divided by total cover) while being entitled to the entire agreed premium. Only if an insurer becomes insolvent are the other insurers liable for the insolvent insurer's share proportionally to their insured sums, each to the extent of the insured sum. Furthermore, an indemnity insurer may also deny coverage in the case of double insurance in bad faith by the insured with the intent of obtaining an unlawful monetary advantage.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Swiss law is silent on whether claims comparable to disgorgement or restitution under Swiss law (ie, claims that involve a repayment of profits gained in bad faith on the part of the insured party) are insurable. While loss of profit can be insured, the law is silent on whether this is also the case if such profits were made in bad faith. In general, gross negligence can be (and regularly is) insured, while intent can be insurable (but is only insured in very rare circumstances), but there is a risk under Swiss law that an insurance of intent or of claims caused in bad faith may be considered to be contrary to general principles of law or public policy, similar to the insurance of monetary fines, which is not permissible.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

Whether a single event resulting in multiple injuries or claims constitutes one or more occurrences under a policy is determined by courts based on an interpretation of the applicable insurance policy. Insurance policies under Swiss law regularly include wording to the effect that a single event resulting in multiple claims constitutes only one occurrence under the policy.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

An insurer may withdraw from a contract if the insured has made misstatements at the conclusion of the insurance contract. This is the case if the insured has miscommunicated or withheld a significant risk. The insurer has a right of rescission even when the insured is not at fault for the misstatement. The insurer must give notice of rescission within four weeks after he or she has received knowledge of the misstatement. In principle, this is possible without adhering to a specific form.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

It is common practice to agree on arbitration clauses in reinsurance contracts. Arbitral tribunals continue to be the most suitable means for differences that cannot be resolved amicably because of the important role that custom (long-standing market practice) plays in the reinsurance industry, the parties' common interest in confidentiality and the worldwide enforceability of arbitration awards pursuant to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 as amended.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Common issues that arise in reinsurance disputes are:

- misrepresentation;
- insured event definition and permissibility of aggregation;
- limitations of the follow-the-fortunes and follow-the-settlement principles (see also question 41); and
- contract interpretation issues.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

The arbitral award must be made by the arbitral tribunal in accordance with the rules of procedure and in the form agreed on by the parties. The award must be in writing, reasoned, dated and signed (at least by the chair of the arbitral tribunal) (article 189 of the IPLA). The reasoning requirement may be waived by the parties (eg, for reasons of cost efficiency). However, the award typically includes the reasoning owing to the fact that the arbitrators' written considerations on the merits are an important element for the parties to appeal against an award (see question 40).

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Arbitrators do not have any direct jurisdiction over non-parties; however, they can request the support of courts in taking evidence. Courts, in turn, can make use of their powers and assist the arbitral tribunal, for example, by compelling non-parties to provide testimony or to produce documents (article 184 of the IPLA).

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

In international arbitration, arbitral awards may only be brought before the Swiss Federal Supreme Court for the following exhaustive grounds (article 190, paragraph 2 in conjunction with article 191 of the IPLA):

- the arbitral tribunal has been incorrectly constituted (or the sole arbitrator improperly appointed);
- the arbitral tribunal has wrongly assumed or denied jurisdiction;
- the arbitral tribunal has decided beyond the claims submitted to it or failed to decide one of the claims;
- the principle of equal treatment of the parties or their right to be heard in an adversary procedure (due process) has been breached; or
- the award is incompatible with public policy.

Update and trends

Partial revision of ISO – conclusion of revision work by FINMA
The partial revision of the ISO, which includes revised Circulars on corporate governance, the Swiss Solvency Test and the actuary responsible and a new Circular on business plans.

Revision of outsourcing regime for banks and insurers
FINMA is in the process of revising its Circular 2008/7 'Outsourcing – banks' and will (among a revision of the requirements with respect to the outsourcing of essential functions) extend its scope to insurers. The consultation draft for the revised circular 'Outsourcing – banks and insurers' was published in December 2016. The consultation ended on 31 January 2017 and the circular is expected to enter into force on 1 July 2017; however, the consultation report is pending and therefore the detailed wording of the circular is still subject to change. At present, the specific requirements in relation to outsourcing arrangements of insurers are not governed on a Circular level, but by FINMA's explanatory notes to the business plan. An insurer's business plan must, in accordance with the ISA, provide information on contracts or other arrangements by which essential functions are outsourced. This general rule (see also question 2) will not be affected by the revised Circular.

In view of the limited number of the grounds on which an award may be sought to be set aside, this remedy is not a further appeal. In particular, findings of fact are never reviewed.

The parties may exclude all setting-aside proceedings (or limit such proceedings to one or several grounds set out in article 190, paragraph 2 of the IPLA) by an express statement in the arbitration agreement or by a subsequent agreement in writing, provided that none of the parties has its domicile, habitual residence or place of business in Switzerland (article 192, paragraph 1 of the IPLA).

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

The ICA is not applicable to reinsurance contracts. The general provisions of contract law set out in the SCO apply. Further, Swiss legal practice and doctrine provide that in absence of a contractual provision, a competent court will interpret reinsurance contracts based on generally recognised reinsurance custom and standards. In particular, the paramount principles of reinsurance (such as follow the fortunes, follow the settlement and the reinsurer's right to inspect the cedent's file) are considered to be implied in reinsurance contracts and applicable also in the absence of a specific clause relating thereto. As to the content of the reinsurance principles, no relevant specific Swiss customary practice exists, and a competent Swiss court also takes foreign legal doctrine and case law into account.

In general, the reinsurer is obliged to share the fate of the underlying risks accepted by the cedent (follow the fortunes) and to accept as binding the decisions and measures taken by the cedent under its right to manage the reinsured business (follow the settlement); however, only to the extent that the claim falls within the scope of the reinsurance agreement and the cedent has managed the business in an orderly and prudent manner.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The principle of utmost good faith is regarded as reinsurance custom in Switzerland. Utmost good faith is an accentuated version of the general principle of good faith (that is, that rights are exercised and obligations fulfilled in good faith (article 2, paragraph 1 of the Swiss Civil Code)). It is justified by the special relationship of trust between the parties to a reinsurance agreement and critical to determine the care and loyalty due in connection with, for example, the risk selection and claims management by the cedent.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

The same set of Swiss statutory law applies to facultative and treaty reinsurance. Differences between facultative and treaty reinsurance are, however, taken into account according to reinsurance custom (eg, the principle of utmost good faith seems to have more relevance in treaty reinsurance than in facultative reinsurance).

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

There is no contractual or statutory basis for a direct claim of the policyholder against the reinsurer. The reinsurance agreement may allow policyholders to do so; this is usually referred to as a 'cut-through' clause.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Policyholders have no direct claim against the reinsurer (see question 44) even if the direct insurer is insolvent or not able to provide coverage for other reasons.

The insurer's claim against the reinsurer to compensate for covered losses may form part of the tied assets of the insurer (see question 16). In the event that the insurer falls into bankruptcy, the tied assets are liquidated, and the proceeds are used to cover the rights and claims of the policyholders.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Swiss law is silent on this matter. The nature and scope of the cedent's obligation to notify the reinsurer of a loss event mainly depends on the terms of the reinsurance contract. In the absence of contractual provisions to the contrary, the notification must be provided in due course, while any delay does not necessarily lead to a loss of the cedent's right to be compensated for covered losses.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

The allocation of claims and settlement payments of the reinsured depends on the terms of the reinsurance agreement.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

The equivalent to the cedent's right to manage the insurance business is the reinsurer's right to audit the cedent's files in connection with any relevant claim. The reinsurer's inspection right is a generally recognised reinsurance custom and applicable also in the absence of a

specific clause relating thereto. The cedent is also obliged to give the reinsurer access to information on the management of the reinsured business based on Swiss contract law (article 394 et seq of the SCO).

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

Swiss law is silent as to whether a reinsurer is obliged to follow the cedent's settlement of reinsurance claims by way of commutation. The follow-the-settlement principle (see question 41) applies. The cedent is generally well advised to obtain the reinsurer's consent before entering into commutation agreements.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Swiss law is silent as to whether a reinsurer must reimburse a cedent for ECOs; this depends on the terms of the reinsurance agreement.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The Undersecretariat of the Treasury (UT) is the main regulatory body in Turkey with respect to state supervision on insurance and reinsurance activities. The UT supervises the insurance and reinsurance companies through two agencies, the Insurance Supervisory Board (ISB) and the General Directorate of Insurance (GD). Insurance Law No. 5684 (Insurance Law) and the Law Concerning the Organisation and Duties of the Undersecretariat of the Treasury No. 4059 set out the organisation and duties of the ISB and the GD.

The ISB, according to article 28 of the Insurance Law, is the main regulatory agency responsible for regulating insurance and reinsurance companies in Turkey. The ISB is responsible for the supervision of all insurance operations in accordance with their special laws, insurance and reinsurance intermediaries, loss-adjusting activities, actuaries and other persons operating in the insurance sector.

The GD's duties are to carry out tasks stipulated under insurance-related legislation, namely:

- to draft, implement and monitor the implementation (by those concerned) of said legislation;
- to conduct the harmonisation process of Turkey's insurance-related legislation with that of the European Union;
- to take measures to protect insureds and the development of the country's insurance sector; and
- to perform other similar duties as assigned by the UT.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Pursuant to article 3 of the Insurance Law, legal entities intending to be involved in insurance and reinsurance activities shall be incorporated under the legal structure of a joint stock company or cooperative. The companies engaged in the intended activities are not permitted to be involved in other fields of activity. Accordingly, the requirements of the founders (either real persons or legal entities) of insurance and reinsurance companies are in general terms defined as follows:

- they shall not have been bankrupted;
- they must hold financial assets and have a good reputation; and
- they shall not have a criminal record with respect to financial crimes.

With regard to the share certificates of insurance and reinsurance companies, it is obligatory that the certificates are issued as a cash offer for their equity.

The requirements for foreign entities aiming to enlarge their engagement of insurance and reinsurance business in Turkey are stipulated in the Decree on Insurance Sector's International Activities (Decree) published in the Official Gazette No. 26602 on 3 August 2007. Accordingly, a foreign entity is permitted to carry out its business in Turkey by forming a branch office. The foreign company must not have been banned from carrying out business in the countries where the activities are performed, and the capital to be assigned in Turkey shall not be less than the capital determined for insurance and reinsurance companies directly established in Turkey. Further, the activities of foreign insurance experts are based on the principle of reciprocity. However, experts appointed by foreign reinsurance companies are exempted from this principle while carrying out their duties in Turkey.

Insurance agents aiming to conduct their activities in Turkey are subject to the same provisions stipulated for Turkish insurance agents. In addition to that, a foreign insurance agent carrying out the activities in person must be resident in Turkey, whereas a branch office shall be established for the insurance agent aiming to perform the activities under the structure of legal entity. Insurance agents are entitled to operate solely for and on behalf of Turkish insurance companies.

The Regulation on the Establishment and Rules of Procedures for Insurance and Reinsurance Companies published in the Official Gazette No. 26623 on 24 August 2007 (Regulation) contains the provisions for licence applications to be made by foreign insurance and reinsurance companies seeking to open branch offices in Turkey.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Pursuant to article 5 of the Insurance Law, insurance and reinsurance companies shall obtain a licence from the UT in order to conduct their business. Insurance and reinsurance companies are permitted to conduct their business only in one of the fields among the life insurance and non-life insurance groups. The companies shall be bound to increase the paid capital in the amount designated by the UT depending on the field so chosen provided that the same is not less than 5 million liras.

Companies that do not apply to obtain the licence within one year of finalisation of company formation transactions may not use 'insurance company' or 'reinsurance company' in their company titles.

The reasons for rejecting an application for a licence are stipulated in article 6 of the Insurance Law, and the reasons for annulling the licence are stipulated in article 7.

The Regulation sets out the conditions to be met for obtaining and renewing licences, the documents to be procured and the conditions of assessment, while considering the applications and also the announcement of annulment of licences.

The provisions stipulated in the Turkish Commercial Code (TCC) in respect of the formation of joint stock companies and cooperatives shall be complied with during the establishment of insurance and reinsurance companies.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The requirements are stipulated both in the Insurance Law and the Regulation. According to article 8 of the Regulation, officers and managers working in the accounting departments of companies shall have knowledge of insurance accountancy systems and Turkish financial reporting standards. Managers are required to have a minimum of three years' professional experience. Most positions require at least a university degree.

The requirements for the directors and deputy directors of branch offices of foreign insurance and reinsurance companies are the same as those stipulated for Turkish entities. In this respect, it is mandatory for holders of both positions to have a university degree in at least one of the following subjects – insurance, economics, management, law, public finance, mathematics, statistics, actuary or engineering – and to have 10 years' professional experience (directors) and seven years' experience (deputy directors).

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Under a circular published by the UT, the capital requirement for non-life insurance firms is 6.6 million liras, whereas the capital requirement for life insurance groups is 6 million liras. Non-life reinsurance firms must have 4 million liras in capital and firms operating in the life insurance area must have 3 million liras in capital. These are subject to annual review.

As long as the insurance and reinsurance companies carry out their fields of activities, the capital shall be maintained. The Insurance Auditing Board (Board) has the authority to inspect and audit insurance and reinsurance companies pursuant to article 28 of the Insurance Law. Accordingly, the Board shall impose precautionary measures on insurance and reinsurance companies pursuant to article 20 of the Insurance Law in the event of failure to maintain the required capital.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurance and reinsurance companies are obliged to maintain reserves. The broad principles to be complied with are described in article 16 of the Insurance Law, and the particularities are set out in a regulation published in the Official Gazette on 7 August 2007. The reserves required to be maintained by insurance and reinsurance companies consist of the following:

- unearned premium reserves;
- ongoing risks reserves;
- provisions for outstanding claims;
- mathematical reserves;
- equalisation provisions; and
- provisions for discount and bonus.

Meanwhile, insurance and reinsurance companies are obliged to maintain an actuarial department consisting of a sufficient number of actuaries, assistants and staff to ensure that the reserves and pricing are calculated in the correct way.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The relevant ministries publish the general provisions for each insurance product. As long as the product may be offered for sale under the licence that the insurance or reinsurance company has already obtained, no prior approval shall be required. However, if the product falls within the ambit of another licence, the relevant licence must be obtained prior being offered for sale. On the other hand, article 13 of the Insurance Law states that insurance companies may not refuse to provide compulsory insurances such as compulsory automobile liability insurance and compulsory earthquake insurance.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

While the operations, assets, affiliates, receivables, equities and liabilities, and all other elements that affect the financial and administrative structure of insurance and reinsurance companies, are supervised by the Insurance Supervisory Board as per article 28 of the Insurance Law, the frequency and the periodical intervals are not stipulated by the law. On the other hand, as for the market research of insurance and reinsurance companies, the companies should prepare a three-year business plan about their market share objectives, estimations and strategies, which should be reviewed periodically. However, the law and the regulations do not make any reference to how to conduct the research for preparing such a business plan.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Pursuant to the Insurance Law, insurance and reinsurance companies cannot engage in businesses other than insurance activities and those directly related to insurance activities. In this connection, insurance or reinsurance companies cannot make investments unless the business in which such companies would invest is directly related to insurance activities.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Under article 4 of the Insurance Law, the directors, general managers (and their auxiliaries) and the controllers operate under the conditions as stated in question 4. Directors of the acquirer shall have no criminal record, although no special provisions are stipulated for officers. The conditions applied to the directors and controllers shall also apply to any person of equal or greater authority than a director, according to the same provision.

The voluntary liquidation of insurance or reinsurance companies, or the merger or transfer of the same with the assets and liabilities or the partial or whole transfer of their portfolio, is subject to the consent of the Ministry of Finance. The merger or transfer of the company or the portfolio shall be announced at least twice in a newspaper that is among the top 10 in terms of national circulation.

A share acquisition exceeding 10 per cent of the company's capital or a share transfer causing the decrease of the transferee's shares to less than 10 per cent requires permission to be obtained from the UT. The UT shall conclude the application within three months. Any other transaction shall be notified to the UT within one month.

These procedures should always comply with the general provisions stated in the TCC.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements regarding the financing of the acquisition of an insurer or reinsurer in Turkey.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

There are no restrictions or regulatory requirements imposed specifically on the minority interests in the company; however, it is important to refer to the share transfer requirement as set out in article 9 of the Insurance Law where the shares, directly or indirectly, reach or exceed 10, 20, 33 or 50 per cent of the capital of an insurance company or reinsurance company, as well as share transfers that will cause the shares of a shareholder to achieve or to fall below such ratios. These are subject to authorisation by the UT, otherwise the share transfer shall not be registered at the share book of the company. It is essential that shareholders who directly or indirectly hold 10 per cent or more of the capital or voting rights and beneficial interest, or an interest that is lower than the said ratios but that gives the privilege of nominating members to the executive boards of the management in a manner to influence management and supervision, meet the same criteria that are required in the

founders of the insurance company or reinsurance company. Insurance and reinsurance companies shall notify shareholders who fail to meet such criteria to the UT. Shareholders who lose these qualifications shall not benefit from the shareholder rights (except dividends). In that case, shareholder rights are exercised by the trustee.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

Pursuant to article 3 of Foreign Direct Investment Law No. 4875, unless otherwise stipulated by special provisions or international agreements, foreign investment in Turkey is permissible. Therefore, there are no specific requirements or restrictions concerning foreign investors, as they are subject to the same requirements and restrictions defined for Turkish insurance and reinsurance companies. However, as mentioned previously, existing foreign insurance and reinsurance companies are permitted to conduct their business in Turkey by opening branch offices, but this rule does not prevent the incorporation of a new insurance company within Turkey through foreign capital, and accordingly most of the insurance companies in the Turkish market have foreign capital shares.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

According to the relevant regulation, groups of companies containing an insurer or reinsurer in the holding company should report (along with their independent audit report) the following:

- a direct or indirect relationship between the companies (including but not limited to the corporate and management structures);
- the relationship between the corporate capital and the performance capacity;
- the reinsurance policy and its correlation with the risks;
- group guarantees and securities and potential legal liabilities;
- internal group transactions and relevant risks; and
- the reporting chain and risk management process.

It is important to note that the group of companies should have a solid and reliable reporting system addressed directly or indirectly (through special audit companies) to the UT; otherwise, the UT shall abolish the authority of these companies to enter into insurance contracts.

Under article 3 of the Insurance Law, in addition to the capital requirements stated above, a holding company's financial condition shall be sufficient to perform insurance activities.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

There are currently two reinsurance companies, Milli Reasurans TAS and Arti Reasurans AS, and the latter has not yet commenced carrying out business. This situation inevitably leads insurance companies to place their risks mainly in foreign reinsurance companies. Therefore, the Turkish insurance sector conducts business in line with the practice of the international reinsurance market. Reinsurance agreements are conducted in the following forms:

- proportional reinsurance treaties;
- quota share reinsurance treaties;
- surplus reinsurance treaties;
- non-proportional reinsurance treaties; and
- excess of loss treaty and stop loss treaties.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Under Turkish law, there are no requirements and restrictions on insurance companies when placing their risks in reinsurance companies.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Insurance companies are required to maintain collateral as determined in article 17 of the Insurance Law in exchange for the undertakings stipulated in the insurance agreement they entered into in Turkey. The provisions with respect to the collateral are stated in article 4 of the Regulation on the Financial Structure of Insurance, Reinsurance and Pension Companies. As a general principle, insurance companies are obliged to procure collateral in proportion to the undertakings they assume.

The collateral for insurance companies involved in the life insurance field consists of the remaining amount after deducting the mathematical reserve corresponding to uncollected premiums from the total of the mathematical and pending reserves, whereas in the non-life insurance field, the collateral consists of one-third of the required capital stock. Pursuant to article 17 of the Insurance Law, the UT may decide to reserve special collateral not exceeding 10 per cent of these amounts.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

According to the Regulation on the Measurement and Assessment of Capital Requirements of Insurance and Reinsurance Companies and Pensions Companies, insurance and reinsurance companies are subject to specific rules for the preservation of the equity capital; therefore, any loan or credit to be added to the equity capital is subject to the UT's approval, and should meet further requirements as mentioned in article 5 of the above Regulation. Apart from the foregoing requirement regarding the equity capital, there is no further regulatory requirement for cedents to obtain credit for reinsurance.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

General provisions of the TCC shall be applied to insolvent or financially troubled insurance and reinsurance companies. However, pursuant to article 9 of the Regulation on the Financial Structure of Insurance, Reinsurance and Pension Companies, in the event of insolvency, the transfer of the portfolio may be realised with the consent of the UT without waiting for the finalisation of the insolvency procedure.

The situations that constitute 'financial troubles' are defined in article 11 of the Regulation on the Financial Structure of Insurance, Reinsurance and Pension Companies. The principal situations named therein are as follows:

- in the event of not being able to cover own capital, failing to present a payment schedule acceptable to the UT or failing to comply with such payment schedule;
- own capital not covering the guarantee funds;
- failing to provide the guarantee so requested;
- failing to perform the commitments described in the agreements or failing to pay insurance compensation within the legal time frame without any justified reason, or making a practice of delays in payment; and
- failing to hold the necessary reinsurance guarantee in order to insure its undertakings, especially for highly risky insurance groups.

In such events, the UT shall warn the companies and, if the state of financial trouble continues, necessary precautions such as cessation of allocations of profit, an amendment to the pricing policy or an invitation to the company's general assembly to hold an extraordinary meeting as defined in articles 12 and 13 of the same Regulation shall be applicable.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

According to article 10, sub-paragraph 4 of the Insurance Law, the insured shall participate in the bankrupt's estate at the third rank.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

As per article 3 of the Decree, a foreign insurance agent carrying out activities in person in Turkey must be resident in Turkey, and a local branch office must be established for the insurance agent aiming to perform the activities under the structure of a legal entity. In addition to these requirements, pursuant to article 23 of the Insurance Law, insurance agents should be entered in the registry kept by the Union of Chambers and Commodity Exchanges of Turkey. The insurance agent must also obtain a certificate of compliance from the UT.

The qualifications required for an insurance broker are defined in the Regulation on Insurance and Reinsurance Brokers. Pursuant to article 6 of the Regulation, insurance brokers shall obtain the relevant licences from the UT for conducting their business.

Activities of foreign insurance experts that involve activities of claims adjusters are based on the principle of reciprocity pursuant to article 2 of the Decree. The qualifications required for insurance experts are defined in article 5 of the Regulation on Insurance Experts. Persons willing to conduct this business must attend special courses, and after passing the corresponding examination must obtain a licence from the relevant chambers as authorised by the Union of Chambers and Commodity Exchanges. It should be noted that different kinds of licence exist for each field of insurance. Article 21 of the Regulation on Insurance Experts confers responsibilities such as impartiality, privacy and secrecy on practitioners.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Pursuant to article 1478 of the TCC, a third party suffering loss may be entitled to bring action directly against an insurer for coverage provided that the claim amount does not exceed the insurance amount. There are also special provisions entitling the suffering third party to bring direct action. For example, pursuant to article 97 of Highway Traffic Law No. 2918, it is legitimate to bring direct action against the insurer for coverage of the insurance amount specified in the compulsory automobile liability insurance.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

In liability insurance, as a general term, the insurer shall be obliged to notify the insurer within 10 days on occurrence of the incident covered by the insurance policy pursuant to article 1475 of the TCC.

As a general principle, pursuant to article 1446 of the TCC, the insured shall be responsible for notifying the insurer of the occurrence of an insured risk without any delay. However, a delay in notification does not relieve the insurer of its liability. According to sub-paragraph 2 of article 1446, unless the insurer previously acknowledged the risk in any other manner, it shall be entitled to make a deduction of the compensation to be paid in the event that the delay in notification caused the compensation amount to increase. The assessment of deduction shall be based on the degree of negligence of the insured.

Pursuant to article 1420 of the TCC, all claims arising from an insurance policy are time-barred within two years from the date the claim become due, and all claims arising from insurance indemnity and insurance costs are time-barred six years after the occurrence of the risk, save that the regulation of article 1482 of the TCC indicates a time bar of 10 years for claims related to liability insurance.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

In the event of occurrence of the insured risk, the insurer is liable to indemnify the insured pursuant to article 1409 of the TCC. Exemptions for each type of insurance are defined in the general provisions. However, the insurer is under responsibility to enlighten the insured about the provisions of the insurance according to article 1423 of the TCC. As such, the burden of proof rests on the insurer in the event of an allegedly legitimate denial of a claim. In addition, if the conduct of the insurer in denying the claim is interpreted as a malicious act, any damages or losses thereby shall be claimable based on the general principle of honesty defined in article 2 of the Civil Law.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Under the general principles of Turkish insurance law, there is no explicit provision with respect to the insurer's responsibility to defend a claim. However, in terms of liability insurance policies, the insurer may be obliged to cover the expenses that the insured might incur with respect to the demands presented to him or her pursuant to article 1474 of the TCC.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

In liability insurance agreements, unless otherwise specifically agreed, the insurer shall be obliged to indemnify the suffering party for the insured's liabilities arising out of an incident that occurred during the insurance period even if the damage occurs at a later stage according to article 1473 of the TCC.

The obligation of the insurer to pay indemnity is principally described in article 1427 of the TCC. Accordingly, in the event that the insurance policy does not contain a clause to put the insurer under the obligation of payment in kind, the insured must be satisfied with cash payment. The indemnity obligation will become due within 45 days after the occurrence of the risk and presentation of the supporting documents of the insurer, but in any event on service of notification with regards to the occurrence of risk. This period is prescribed as 15 days for life insurance. Any agreement aiming to discharge the insurer from paying interest will be regarded as null and void.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Pursuant to article 1435 of the TCC, the insured is liable to inform the insurer about the important issues pertaining to the subject matter of insurance. Failing that, the insurer may be entitled either to renege on the insurance contract or to claim premium difference.

With respect to life insurance, in the event that five years have elapsed since the beginning of the insurance coverage (including renewals), the insurer will not be entitled to renege on the insurance contract but can only claim the difference in premium if the insured fails to provide accurate information. Reneging may be possible if the lack of information is a wilful breach on the part of the insured.

28 Punitive damages

Are punitive damages insurable?

Under Turkish law, there is no provision preventing the parties from entering into a mutual agreement for ensuring the coverage of punitive damages; therefore, the freedom of contract is respected in this regard. Pursuant to article 4.3 of the General Conditions on Professional Liability Insurance, all types of administrative and judicial fines and punitive damages, as well as any expenses arising therefrom, shall be interpreted as cases excluded from coverage unless there is an agreement to the contrary.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Under Turkish insurance law, there is no specific provision for the obligation of an excess insurer to 'drop down and defend' and pay a claim. However, unless the relevant policies contain provisions to the contrary, an excess insurer's liability shall continue.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

There is no specific provision in this regard under Turkish insurance law. Therefore, such obligations are subject to the policy conditions.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

Under Turkish insurance law, there is no general provision in this regard. However, special provision may be found in article 96 of the Highway Traffic Law, where it is stated that in the event the total indemnity to which the interested parties are entitled is in excess of the insurance amount, a deduction shall be made on each insurer's indemnity amount on a pro rata basis by taking into account the size of the indemnity each party is entitled to from the insurer under normal circumstances. In this respect, Turkish law tends to distribute the payment rather than put them in a priority order. Another special provision along the same lines can be found in compulsory liability insurance for passengers' transportation by sea.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

In liability insurance agreements, unless there is a specific agreement to the contrary, the insurer shall be obliged to indemnify the suffering party for the insured's liabilities arising out of an incident occurring during the insurance period according to article 1473 of the TCC. In the view of the foregoing, subject to any expert findings, the payments may be allocated. Allocation will be based on the size of the individual policies (see question 31).

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

There is no doubt that, pursuant to the TCC, the interest that is taken under insurance cover should be measurable by money. On the other hand, the TCC does not prevent the parties to an insurance contract from determining indemnification as restitution in kind, given that article 1427 of the TCC states that insurance indemnity will be paid in cash unless the parties agree otherwise. The parties to an insurance contract may also agree on including loss of profit within the scope of the insurance cover.

However, regarding disgorgement, under article 1404 of the TCC, losses arising out of any act in breach of the mandatory rules, moral values, public order or personality rights cannot be covered by insurance, as disgorgement claims against insureds or policyholders are not among insurable claims.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

In these kinds of incidents, the Turkish courts generally hand over the case files to experts in order for their determination as to whether, or which, risks that were covered by the insurance policy have occurred, and each incident is examined on its own circumstances.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

Pursuant to article 1435 of the TCC, statements that are disclosed or stated insufficiently or untruly to the insurer, or that are not disclosed at all, shall be deemed important if they can lead to the non-conclusion of the insurance contract or conclusion of the same with different terms. In cases where such circumstances of importance are not disclosed at all or are disclosed incorrectly to the insurer, the insurer may then exercise the right of rescission within 15 days from the date the insurer became aware of the breach of duty of disclosure, or request additional premium. In cases where the request for additional premium is not accepted within 10 days, the insurer shall be deemed to have rescinded from the contract.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Reinsurance practice is very limited in Turkey. Indeed, there has historically only been one reinsurance company, Milli Reasurans TAS. Although a second firm, Arti Reasurans AS, has been established, it has not yet commenced business. The reinsurance agreements to which Turkish insurance companies are party are mostly subject to jurisdiction outside Turkey. Therefore, reinsurance disputes are not common. Although not common, there is an arbitration procedure foreseen under article 30 et seq of the Insurance Law.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

See question 36.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Reinsurance arbitration awards do not exist in the domestic jurisdiction (see question 36).

As far as insurance disputes are concerned, article 30 of the Insurance Law, which sets out the rules to be complied with in insurance arbitration, refers also to the provisions of Law of Civil Procedure No. 6100 for situations for which there are no specific stipulations. Pursuant to article 297 of the Law of Civil Procedure, an arbitrator is under an obligation to include in the award the consideration of the evidence, the findings and factual grounds on which the award is based. In addition, article 141 of the Turkish Constitution states that any judicial decision will include its reasoning. Therefore, the reasoning will be included in arbitral awards.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Reinsurance arbitration awards do not exist in the domestic jurisdiction (see question 36).

As far as insurance disputes are concerned, the powers of reinsurance arbitrators are not specifically described in the Insurance Law or in the Regulation on Reinsurance Arbitration. However, article 23 of the Insurance Law clearly refers to the provisions of the Law of Civil Procedure, of which article 31 puts judges under an obligation to clarify the merits of the case by permitting them to invite the parties for the purpose of providing information and evidence pertaining to the claim. As regards non-parties, this power is still valid and effective provided that a party to the case requests the judge to invite a third party to the claim in order to produce information or documentation or a witness statement. The reason for this limitation is based on the principle that disputes that are not related to public policy must be brought by one of the parties to the dispute.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Reinsurance arbitration does not exist in the domestic jurisdiction (see question 36).

As far as insurance disputes are concerned, parties to reinsurance arbitration can seek to vacate or enforce the award through the judicial system. Awards involving a monetary value of up to 5 million liras are final, whereas any award exceeding this value can be challengeable before the Insurance Arbitration Commission. The decision of the Insurance Arbitration Commission is final and binding on the parties provided that the claim amount is less than 40,000 liras. Once the right of appeal to the Commission is exhausted, decisions can be appealed by pursuing the general rules prescribed in the Law of Civil Procedure, pursuant to the clear reference in article 30 of the Insurance Law. The following are grounds for appeal:

- a misinterpretation of the contract or the law;
- an irregularity on the cause of action;
- the disregarding of any evidence of substantial effect; or
- the presence of procedural errors or deficiencies.

Irrespective of the value of the dispute, any award can be appealable where:

- the award is rendered after the lapse of the arbitration period;
- the award relates to matters on which arbitrators are not competent to decide;
- the award includes rulings on matters that were not requested by the parties; or
- the award does not relate to the allegations of the parties.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There is no practice in this regard. See question 36.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Article 32 of the Insurance Law puts insurers, reinsurers, brokers and experts under obligation to act in good faith while conducting their activities. In this respect, it is explicit that the duty of utmost good faith is implied in reinsurance agreements.

The duty of good faith in other commercial agreements relies on the general principles of law, where good faith is defined as a fundamental principle in article 3 of the Civil Law. The particularities of the same duty in reinsurance agreements is described in a more specific manner where the insurers, reinsurers, brokers and experts are under the obligation to avoid any act that might infringe the rights and interests of the insured. Any misconduct in this respect is defined as a ground for the cancellation of the insurer's insurance licence pursuant to article 7 of the Insurance Law. Therefore, the duty of good faith in insurance activities is interpreted in a very strict manner in comparison with other commercial agreements.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

No, there are no different sets of laws for facultative reinsurance and treaty reinsurance.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Under article 1403 of the TCC, as a general principle, a policyholder or non-signatory to a reinsurance agreement cannot bring direct action against a reinsurer for coverage. However, as this principle is not mandatory under article 1452 of the TCC, the parties may agree otherwise, thereby enabling a policyholder or non-signatory to a reinsurance agreement to bring direct action.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

The reinsurer shall pay the policyholders' claim to the bankrupt's estate. This payment shall reflect the reinsurer's obligation under the reinsurance policy.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Unless the reinsurance contract provides a specific wording about the form of notice and the information to be contained therein, the interpretation of the conditions to be met shall be in line with the general provisions. In this respect, article 18 of the TCC states that any notice for the purpose of putting the other party in default, terminating the contract or reneging on a contract shall be made in the following manner:

- through a notary public;
- by registered mail;
- by telegraph; or
- by registered secure email.

In the event of failure of timely or sufficient notice, unless the reinsurance contract provides specific remedies, article 1446 of the TCC may be taken into account in interpreting the remedies available to a reinsurer. In this respect, if the reinsurer previously did not acknowledge the risk in any other manner, it shall be entitled to reduce the compensation to be paid in the event that the time delay caused the compensation amount to increase.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

As there is only one reinsurance company (Milli Reasurans TAS) currently operating in Turkey, as far as Turkish law is concerned there is no practice in this matter.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

In general terms, review is available in that, pursuant to article 30 of the Insurance Law, a party to a dispute may avail itself of the right to apply to an insurance arbitration even if the reinsurance contract does not contain an arbitration clause, whereas under the general rules of civil proceeding, an arbitration clause must be included in an agreement in order for parties to be able to have recourse to it.

The interpretation of the dispute, either before the Insurance Arbitration Commission or the courts, shall be guided by the reinsurance contract, legislation, precedents and market practice.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

There are no clear provisions with regard to the strict obligation of the reinsurer to reimburse its cedent for commutation payments. Therefore, such obligation may be freely defined in the reinsurance contract to ensure a binding effect on the reinsurer.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Turkish insurance legislation does not stipulate a specific rule regarding the reimbursement of the cedent for ECOs; accordingly, the reimbursement liability will depend on the terms and conditions of the agreement between the reinsurer and the cedent.

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

The United Arab Emirates (UAE) contains two distinct jurisdictions: onshore UAE and free zones. Onshore UAE comprises seven separate and independent Emirates (Abu Dhabi, Dubai, Sharjah, Ras Al Khaimah, Fujairah, Ajman and Umm Al Qwain). Federal Law No. 6 of 2007 (the Insurance Law) regulates onshore insurance and reinsurance companies through the UAE Insurance Authority (the Insurance Authority). This body is predominantly concerned with:

- insurance and reinsurance companies located or operating in the UAE;
- customers located or operating in the UAE; and
- licensed insurance intermediaries.

There are also dedicated regulators for the health insurance sector in Dubai (the Dubai Health Authority (DHA)) and Abu Dhabi (the Health Authority of Abu Dhabi (HAAD)).

The UAE contains various free zones, which are governed by their own respective laws and authorities. Of these, only the financial free zones are allowed to establish insurance-related entities. The Dubai International Financial Centre (DIFC) and the Abu Dhabi Global Markets (ADGM) regulate insurance and reinsurance within those free zones and have their own independent courts. The ADGM's regulations and structural framework were formalised in 2016 and are very similar to that of DIFC, both deriving from the English law and the United Kingdom's Financial Conduct Authority. This chapter will focus on the DIFC.

The DIFC Authority and the Dubai Financial Services Authority (DFSA) regulate companies and intermediaries licensed in the DIFC. Detailed rules concerning the conduct of insurance business within the DIFC are contained in the DFSA's Rulebooks. The Rulebooks apply to all contracts of insurance, 'which are effected or carried out in or from within the physical parameters of the DIFC'. Insurers licensed by the DIFC primarily deal with reinsurance.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Onshore

The Insurance Law permits two types of corporate organisations to undertake insurance activities from or within onshore UAE, namely:

- a locally incorporated public joint-stock company, listed on the UAE stock exchange, in which UAE or Gulf Co-operation Council (GCC) nationals own at least 75 per cent of the shares; and
- a branch of a foreign insurance company. New licences are only granted if the UAE market requires additional capacity or a foreign insurer provides products that existing local insurers do not.

To operate in Dubai, an onshore insurer requires a licence from the Insurance Authority, which requires the submission of an application and business plan to the Insurance Authority. Following the Insurance Authority's pre-approval, the applicant may apply for a commercial licence from the Department of Economic Development. A certificate of registration is also required from the Dubai Chamber of Commerce and Industry. The applicant should also register with the Ministry of Labour and the Ministry of Interior's Immigration Department, to allow the insurer to sponsor individuals for employment and residency purposes. Separate approvals are required for the health insurance sector in Dubai and Abu Dhabi, which requires additional licensing with the DHA and HAAD respectively.

DIFC

The DFSA Rulebook permits two types of corporate organisations to provide insurance services within or from the DIFC, namely:

- a company limited by shares; and
- a recognised foreign company (or branch of a foreign company).

The authorisation procedure in the DIFC requires the submission of a business plan to the DFSA, following which the DFSA and DIFC Authority conduct meetings with the applicant to agree the proposed business model. Depending on the category of risk being undertaken by the entity, the applicant can apply for the different categories of licence. Category 5 is for a company with the least exposure to risk and Category 1 is for a company with the maximum exposure to risk, such as those 'accepting deposits' or 'providing credit'.

Following compliance with DFSA requirements, the applicant may seek DFSA approval as an authorised company. Once approval is granted, a request is submitted to the DIFC Authority to incorporate the proposed entity.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Onshore insurance companies must maintain a minimum paid-up share capital of 100 million UAE dirhams for insurers and 250 million UAE dirhams for reinsurers. Depending on the class of insurance written, an insurance company is also required to make a deposit with a UAE bank as a form of guarantee of its obligations. The deposit is currently 2 million UAE dirhams per branch for an insurer writing property or liability insurance, and 4 million UAE dirhams per branch for an insurer writing life insurance and fund formation not exceeding 6 million UAE dirhams in total. Until recently, there was some confusion as to whether these capital requirements applied to foreign branches as well. A recent draft regulation from the Insurance Authority clarifies that for foreign branches, proof from the regulator of the capital available with the parent company for the UAE exposures is sufficient and local capitalisation is not necessary.

In order to issue debt or equity security, there must be a requisite 75 per cent UAE mandatory shareholding. The Insurance Authority must be notified of the issuance of debt or security prior to the issuance. Furthermore, the Insurance Authority must also be informed of any change in shareholding after the debt or equity security issuance.

In addition, insurance and reinsurance companies must observe the levels of customer service and conduct of business requirements set out under the Insurance Law, Federal Law No. 5 of 1985 (Civil Code), the Insurance Authority Board of Directors Resolution No. 2

of 2009 (Executive Regulations) and the Insurance Authority Board of Directors Resolution No. 3 of 2010 Concerning Instructions on the Rules of Ethics and the Professional Practice (Code of Conduct).

DIFC licensed entities must comply with the DFSA's Rulebook's requirements. The prudential requirements of the DFSA Rulebook stipulates that the share capital of an insurance company must be at least US$10 million. Any proposed issue of securities triggers an obligation to notify the DFSA where there is or may, be a change of control, as defined in the DFSA Rulebook.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

The Insurance Law does not specify qualification requirements but there is an expectation that the person being proposed for the role must be suitably qualified and experienced. Approval of the Insurance Authority needs to be sought before recruitment of senior officers of insurance companies and the Insurance Authority has discretionary powers to accept or reject the recruitment of a person depending on whether the candidate is suitable for the role.

Similarly, the DIFC does not specify minimum qualification criteria but has discretionary powers to determine whether a person is suitable for a role or not, which is based on wide parameters such as experience in the region.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

See question 3.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Insurers seeking to operate in the UAE must comply with a number of important prudential and corporate governance regulations and requirements. In terms of prudential regulations, these include paid-up capital and capital reserve requirements. With regard to corporate governance, insurers must meet record-keeping and reporting standards, ensure that the board of directors and senior executives meet the necessary qualifying standards and comply with regulations regarding anti-money laundering and the employment of UAE nationals as part of the UAE government's Emiratisation policy.

Article 45 of the Insurance Law stipulates the reserve funds that need to be maintained by insurers. The value of the reserve funds depends on whether insurance policies issued are individual term, individual decreasing term, or whole life and endowment.

The Insurance Authority published the Financial Regulations for Insurance Companies and Takaful Insurance Companies in December 2014 (the Financial Regulations) and introduced a number of controls around the solvency requirements. In addition to the minimum capital requirements (MCR), the following also need to be measured to fulfil the solvency requirements:

- The minimum guarantee fund (MGF): to be calculated on the following basis:
  - not less than one-third of the solvency capital requirement (SCR); and
  - the higher of a minimum amount to be specified by the Insurance Authority for each type of business and a specified percentage of the net earned premium for each type of business; and
- The SCR – the amount calculated by reference to the risks to which the insurer is exposed using the solvency template published by the Insurance Authority.

Insurers are required to maintain funds that are the higher of the MCR, the MGF and the SCR.

In the DIFC, the Prudential Regulations lay down the capital requirements, and require every insurer to have capital resources that are, in the opinion of its directors (formed on the basis of reasonable assumptions), adequate for the conduct of its business, taking into consideration the size of the insurer and the mix and complexity of its business.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

The Insurance Law requires that onshore policies must comprise a certificate, a schedule, accompanying policy terms and conditions and endorsements. Furthermore, article 28 of the Insurance Law, read with article 7 of the Insurance Authority's Code of Conduct, sets out various regulatory requirements that the policy documents should comply with. For example, the policy documents should include all the terms and conditions regulating the contractual relationship and any condition that limits must be highlighted with a different colour or font.

The Insurance Law also requires that insurance policies issued in the UAE are written in Arabic. They may then be translated into any other language, but in the event of a difference in interpretation between versions, the Arabic text prevails. Failure to issue an insurance policy in Arabic will not generally affect its validity, but the insurer may be at risk of a penalty and in the event of a dispute, the interpretation of the individual terms by a court may be subject to uncertainty.

It is important to note that the Civil Code is strict when dealing with terms that are regarded as permissible and that may be included in policies. Recently, the DHA and HAAD have issued regulations and guidance for mandatory health policy wording to be used in Dubai and Abu Dhabi. These regulations provide for mandatory minimum benefits.

There are no corresponding content requirements in the DIFC. The DIFC effectively follows English law concepts and is therefore likely to recognise the English common law approach of utmost good faith or otherwise regulate the good faith requirements in accordance with the choice of the governing law the parties have agreed.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

Every insurer and reinsurer based onshore must provide the Insurance Authority with various detailed reports on its operations. The main reports and requirements include, but are not limited to, the following:

- aquarterly report and analysis of the company's investment portfolio authenticated by its external auditor, which has to be submitted within 45 days of the quarter-end of the quarter period;
- an annual risk analysis report of the company's investment portfolio, strategy and management process. This report has to be certified by the actuary, authenticated by the external auditor and endorsed by the chairman of the board. This report is required to be submitted at the same time as the audited annual financial results.
- solvency reports quarterly certified by the actuary within a period of 45 days from the end of the quarter-end and annually certified by the actuary and the external auditor and endorsed by the chairman of the board of directors within four months from the fiscal year end; and
- financial statements quarterly in Arabic and annually in both Arabic and English.

In line with the trend of international regulators to focus on the role of key individuals within financial services organisations, the Financial Regulations impose significant requirements on the board of directors (and, in particular, the chairman of the board) and senior management, to understand the risks faced by insurance companies and to develop and implement appropriate systems and controls to manage such risks. There are also detailed requirements as to the role and obligations of the actuary, investment committee, internal audit department, external auditor and, to a lesser degree, the compliance officer.

There are extensive reporting obligations in relation to solvency requirements, including the annual submission of the company's solvency template and a quarterly report on the SCR. In addition, insurers

are required to 'immediately' report any non-compliance with the solvency requirements and to submit a realistic recovery plan.

In addition to the foregoing, the Insurance Authority has the power to request additional reports and documentation from the company.

The DFSA Rulebook

For insurance companies in the DIFC, the DFSA has investigation and enforcement powers that are provided in the laws and regulations of the DFSA. These powers are very wide in nature and the DFSA has the discretion to investigate all matters that are connected to the operations of DIFC entities, whether within the DIFC company or an onshore company.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

The Financial Regulations regulate the distribution and allocation of investments. There are limits on the proportion of assets that may be held in various classes of investment:

- 30 per cent limit on real estate investment;
- 30 per cent limit on investment in equity instruments in listed and unlisted companies within the UAE, of which no more than 10 per cent may be invested in a particular class of asset;
- 20 per cent limit on equity instruments issued by listed and unlisted companies in capital markets outside the UAE, of which no more than 10 per cent may be invested in a particular asset class;
- 30 per cent limit on loans secured by life policies (excluding unit-linked funds-related policies) issued by the insurance company;
- 30 per cent limit on secured loans, deposits with non-banks, debentures, bonds and other debt instruments rated strong or very strong by reputed and independent rating agencies;
- 1 per cent limit on financial derivatives or complex financial instruments used for hedging purposes only; and
- 10 per cent limit on 'other' invested assets (which term has not been defined).

Other important provisions include the ability for insurance companies to invest up to 100 per cent of their assets in UAE government bonds, and up to 80 per cent in non-UAE government bonds. In both cases there is a 25 per cent limit on each individual investment. If an insurance company wishes to invest its assets in cash and deposits with a bank registered with the Central Bank of the UAE, there is a minimum requirement of 5 per cent. In addition, insurance companies can hold the insurance fund for UAE policies in a foreign jurisdiction, but the total of invested assets held outside the UAE shall not exceed 50 per cent of the total invested assets, or 100 per cent of the total technical provisions for policies outside the UAE, whichever is greater. Insurance companies are allowed to outsource the investment function to a third-party service provider situated in the UAE.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

Onshore, a change in ownership of an insurer or reinsurer requires the prior approval of the Insurance Authority. DIFC authorised companies must submit an application or notification of the change to the DFSA at least 28 days in advance of, or immediately on becoming aware of, a proposed or actual 'change in control'. Officers, directors and controlling persons of the acquirer are usually required to provide undertakings and, on certain occasions, certificates of good standing may be requested from the regulating authority of the acquirer. There are no specified requirements in this regard, but the Insurance Authority may request additional information on a case-by-case basis.

DFSA rules and regulations specify that the approved person (the term used for authorised representatives of the company in case of DIFC entities) of the company must obtain prior approval of the DFSA in case of change of control of the company.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

The UAE insurance regulatory framework is silent on this.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

The UAE insurance regulatory framework is silent on this.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

Onshore UAE insurers that are not a branch of a foreign insurance company must be a public joint stock company, 75 per cent owned by UAE or GCC nationals or companies and listed on a local stock exchange. No such local ownership requirements apply to branches of foreign insurance companies, although a local Emirati sponsor must be appointed as a local service agent to act on behalf of the foreign insurance company. Companies established in the DIFC can be 100 per cent foreign-owned.

The Insurance Authority and DFSA will require persons controlling insurance and reinsurance companies to prove a high degree of experience and demonstrate a trading history in the relevant activities undertaken by that company.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

There is no such supervisory framework.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

Although the Insurance Law specifically provides that the law applies to reinsurance arrangements, there are no distinct provisions specific to reinsurance in the UAE. Neither has the Insurance Authority issued any specific regulations concerning reinsurance arrangements.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Presently, there is no requirement or restriction on ceding or retention of risk by an onshore insurer. We have seen many examples where 100 per cent of risks are ceded. However, the UAE enacted the Anti Fronting Law (Federal Law No. 17 of 2004), which was to be effective from 2007 but the implementation was delayed by UAE Cabinet Resolution No. 229/12 of 2007. There is uncertainty over its implementation but fronting as a market practice is prevalent in the UAE. We understand that onshore insurers may, in the future, receive instructions by the Insurance Authority to take on or increase risk retention.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

The UAE insurance regulatory framework does not specify any collateral requirements for reinsurance companies in a reinsurance transaction.

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

The UAE insurance regulatory framework does not expressly require cedents to obtain credit for reinsurance on their financial statements.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The Financial Regulations published in 2014 introduced new solvency requirements for insurers and reinsurers onshore. In the event of the insolvency of an insurer or reinsurer or other insurance-related entity, the Federal Law on bankruptcy applies, as provided within the Commercial Code (Federal Law No. 18 of 1993), the Commercial Companies Law (Federal Law No. 2 of 2015) and the UAE Bankruptcy Law (Federal Law No. 9 of 2016). A number of priority debts and creditors are identified within articles 713 to 716 of the Commercial Code. These would rank above any debts owed to policyholders of the distressed insurer.

In the DIFC, the DIFC Insolvency (Insurers) Regulations 2009 are dedicated to the insolvency of insurers and reinsurers and provide a ranking of debts, beginning with preferential debts, followed by insurance debts with any surplus to be paid to all other creditors. Insurance debts rank equally with each other and should be paid either in full or otherwise in equal proportions after payment of preferential debts. Policyholders are offered no regulatory protection under the DIFC insolvency regime.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The UAE Bankruptcy Law, which was enacted in 2016, consolidated and streamlined the bankruptcy procedure. Chapter 6 of the Bankruptcy Law deals with the order of debt settlement and the order of priority for debt settlement, depending on the type of bankruptcy or insolvency. That said, article 95 of the Insurance Law governs the priority of claims in an insolvency proceeding, namely:

- rights due to employees and workers for the previous four months;
- expenses and costs incurred, and loans obtained, by the liquidator;
- rights accruing to the insured persons and beneficiaries from insurance policies; and
- rights of other creditors according to the order of their preferences under existing laws.

The DIFC Insolvency (Insurers) Regulations 2009 set out the priority of payment in the liquidation of an insurer or reinsurer established in the DIFC. The order of priority is: preferential debts, insurance debt, with any surplus going to all other creditors.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The Insurance Law and the Insurance Authority regulate all persons and entities conducting insurance business in the UAE, including insurance intermediaries. The Insurance Authority is therefore responsible for registering and licensing intermediaries.

The Insurance Law defines an insurance agent as 'the person approved and authorised by the company to carry out insurance operations on its behalf or on behalf of any branch thereof'. An insurer wishing to appoint an insurance agent must ensure that the insurance agent is properly licensed and that any agreement with the agent pursuant to their appointment has been submitted to the Insurance Authority.

The Insurance Law also recognises insurance advisers (commonly known as 'insurance consultants'). The insurance consultant examines the insurance requirements of his or her clients, gives advice on insurance cover, and charges his or her clients a fee for such advice. An individual or a company wishing to become a consultant or consultancy must apply to the Insurance Authority to obtain a licence.

The Resolution of the Board of Directors of the Insurance Authority No. 15 of 2013 concerning Insurance Brokers (the Brokers Regulations) provides requirements for obtaining and maintaining a broking licence, including an obligation for a broker to maintain paid-up capital of 3 million UAE dirhams for UAE companies and 10 million UAE dirhams for branches of brokers established in a free zone or branches of a foreign company. In addition, Resolution No. 58 of the Insurance Authority (the Supplementary Regulation) provides strict solvency margins on brokers, requiring that at all times they maintain 'available capital' (that is, the difference between the value of assets over liabilities) of not less than 'the required minimum' (that is, those amounts detailed above).

The DFSA Rulebook's Prudential Investment, Insurance Intermediation and Banking Business Module (PIB), applies specifically to insurance intermediaries and insurance managers licensed to carry out insurance business. The DFSA Rulebook's General Module (GEN) defines insurance intermediaries as entities that advise on the merits of insurance policies, act as agents in the sale and purchase of insurance, and make arrangements for other persons to purchase insurance. Insurance intermediaries generally include insurance brokers and underwriting agents. Meanwhile insurance management is defined in the GEN as being practised by entities providing management services and 'exercising managerial functions, including administration and underwriting for an insurer'. Insurance intermediaries and insurance managers are classified as 'category 4' authorised firms as defined by, and most specifically regulated by the PIB, which defines category 4 firms as:

> *'[A firm whose] Licence authorises it to carry on one or more of the Financial Services of Arranging Credit or Deals in Investments, Advising on Financial Products or Credit, Arranging Custody, Insurance Broking or Insurance Management or Operating an Alternative Trading System, Providing Fund Administration or Providing Trust Services; and ... does not meet the criteria of Categories 1, 2, 3 or 5.'*

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

DIFC laws are essentially mirrored on English law and so the answers in the following sections are confined to onshore UAE laws.

Except for claims under a fire insurance cover, a third party has no rights against an insurer unless they are specifically provided for under the policy. That said:

- there is nothing to prevent a direct action by a third party;
- in circumstances where the insurer has provided third-party cover, it is not uncommon for insurers to be added as defendants in a claim by a third party against an insured; and
- courts on occasion make awards against insurers in favour of third parties. This is as a consequence of article 1026(1) of the Civil Code, which stipulates that insurers may pay either the insured or a 'beneficiary'.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

An insurer is generally unable to deny coverage owing to late notice, because even though notification requirements are a factor for a claim to be triggered, they are, however, subject to article 1028 of the Civil Code, which stipulates that notice clauses under an insurance contract are void when they:

- result in the lapse of the right of the insured owing to delay in notification, if there is a reasonable excuse for the delay; or
- are arbitrary, in that a breach would have no effect on the occurrence of the insured (eg, breach of a notification clause).

Subject to the above, in situations where the insured provides notice of the claim, but fails to provide all relevant information to ascertain the incident or the extent of the loss, an insurer can deny the claim (article 9(6) of the Insurance Authority Code of Conduct).

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

In accordance with the Civil Code and the Insurance Authority's Code of Conduct, an insurer owes a general duty of good faith when dealing with its insured and must inform its staff about this and the other obligations contained in the Code of Conduct.

In theory, it is possible for an insured to claim damages for breach of the duty of good faith (in the context of adjusting and settling claims). In practice, we are not aware of any cases in the UAE that have considered these issues.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

UAE law provides that the insurer's 'obligation' arises when a third party makes a claim on the insured (article 1035 of Civil Code). 'Obligation', however, is not defined, and so the actual 'trigger' in any case will depend on the policy wording. It should also be noted that policies in this region tend to provide that insurers have the 'right to defend' a claim rather than a 'duty to defend' (ie, the insurer can opt to step in and run a defence, but otherwise the defence obligation lies with the insured, albeit the insurer might agree to fund the defence).

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

UAE law requires indemnity on the 'manner agreed upon' on the materialisation of the risk or time set out under the policy (articles 1026(1) and 1034 of Civil Code). Therefore, it follows the policy wording.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

There is no specific period.

28 Punitive damages

Are punitive damages insurable?

In theory, there is no restraint on such damages being insured or reinsured. In practice, punitive damages are not generally awarded.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Drop down coverage is not expressly provided under UAE law. Should such a provision exist, it will be governed by the terms of the policy.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Self-insurance is not expressly provided under UAE law. Should such a provision exist, it will be governed by the terms of the policy.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is nothing specific regulating the priority of multiple claims under the same policy.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

UAE law is silent on allocation except in the case of policies covering fire loss. Pursuant to article 1043 of the Civil Code, an insurer of a fire loss is entitled to proportionate contribution from any other policy covering the same loss.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

The UAE and DIFC legislation do not provide for insuring disgorgement or restitution claims.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

Pursuant to article 1026(1) of the Civil Code, a claim is triggered under an insurance policy on the materialisation of the risk or event set out under the policy, which on one interpretation would be the occurrence of the event causing the loss. Besides that, there is no specific definition for or guidance on 'occurrence', and so we follow policy wordings to determine whether a single event, resulting in multiple injuries or claims, constitutes more than one occurrence under an insurance policy.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

An insurer may terminate a policy for breach of disclosure obligations under the contract, pursuant to article 1033 of the Civil Code, but the premium can only be retained if the insured acted in 'bad faith'.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

Reinsurers and insurers prefer business solutions to disputes. If disputes occur, then those are subject to the governing law and jurisdiction agreed in the reinsurance contract.

Article 1028 of the Civil Code provides that if the parties to an insurance contract wish to resolve disputes through arbitration, they must enter into a separate arbitration agreement independent of the insurance contract. While there is no specific reference to reinsurance contracts, it is safe to assume that the same applies to an arbitration agreement in a reinsurance contract.

The DIFC is fast emerging as the most preferred jurisdiction for local reinsurance disputes, either through litigation before the DIFC courts or for arbitration with the seat in the DIFC and under the DIFC – London Court of International Arbitration Rules.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

There are no laws specific to reinsurance in the UAE. It is generally accepted that laws governing insurance apply to reinsurance contracts. Issues that can give rise to disputes include insurance and reinsurance policies being subject to different governing laws or jurisdictions and the operation of claims control and claims cooperation clauses.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

An arbitration award under UAE law is invalid if the reasons for the decision are not provided in the Civil Procedure Law (Federal Law No. 11 of 1992).

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

UAE law is stringent on arbitration agreements and allows arbitration only between parties to the agreement. Arbitrators can, however, (though court applications) take the assistance of the court to compel non-parties in certain situations. For example, article 209 of the Civil Procedure Law allows an arbitrator to request the court to compel an abstaining witness to attend.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

UAE courts may not consider the merits of an arbitral award (article 217(1) the Civil Procedure Law), but can annul an award on limited procedural and public policy grounds.

An arbitral award needs to be ratified by a UAE court (which includes the DIFC court) before it can be executed (article 215 of the Civil Procedure Law). During ratification, courts can rectify material errors (accidental typing or arithmetical errors), but are required to seek clarifications from arbitrations on any substantive errors.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

There is no UAE law specific to reinsurance. Obligations are therefore determined on the basis of the terms of the reinsurance contract or the law applicable to the reinsurance, which need not be UAE law.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

Article 246 of the Civil Code requires that all contracts (including insurance contracts) must be performed in a manner consistent with the requirements of good faith. Further, the duty of good faith is not limited to the terms of the contract, but also extends to the obligations connected with contracts and to the nature of the transaction.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

There is no UAE law on reinsurance, so the question does not arise.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Unless provided for in the reinsurance policy or assigned by the insurer, under the Civil Code, an insured or third party generally cannot claim directly against a reinsurer. There is a possibility that a UAE court may allow a reinsurer to be joined in a claim by a policyholder against the insurer, especially in scenarios involving a cut-through clause. The position would be similar where the insurer is insolvent or cannot provide coverage.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

See question 44.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

This will depend on the requirements set out in the reinsurance agreement and the law governing the interpretation of the reinsurance agreement.

Kennedys

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47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

See question 46, except that UAE law is silent on allocation unless applicable to a fire policy, such position may similarly apply to a UAE law-governed reinsurance (see question 32).

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

There is nothing specific under UAE law. These issues would be governed by the terms of the reinsurance agreement.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

See question 48. Reinsurers may, however (in situations where the reinsurance is subject to UAE law), be liable to 'incurred but not reported' claims in the same way as an insurer.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

There is no specific requirement under UAE law for ECOs. In situations of bad faith or fraud, a reinsurer may void the reinsurance under UAE law.

United Kingdom

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

Under the Financial Services and Markets Act 2000 (as amended) (FSMA), insurance and reinsurance companies in the UK are regulated by both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA), which are responsible for prudential regulation and conduct supervision of authorised firms. The PRA and the FCA are under a statutory duty to cooperate and coordinate their activities. Insurance intermediaries, such as brokers, are regulated by the FCA only. Lloyd's of London (or the Society of Lloyd's) is regulated by the FCA and the PRA. Lloyd's managing agents are also dually regulated by the FCA and the PRA. Members' agents and Lloyd's brokers are regulated by the FCA. The Bank of England and Financial Services Act 2016 makes the PRA a part of the Bank of England.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

A firm intending to conduct insurance and reinsurance business in the UK must obtain a Part 4A FSMA permission (Part 4A permission) from the PRA (unless it is exempt or able to rely on the EU's passporting regime). The FCA must consent to the PRA's grant of permission. Insurance intermediaries must apply to the FCA for permission. In order to obtain a Part 4A permission, an applicant must be able to satisfy the 'threshold conditions' on an ongoing basis. This includes demonstrating that its head office is in the UK or it carries on business in the UK; it is adequately capitalised to conduct the insurance and reinsurance business in question; and it has appropriate management systems and controls in place, as well as suitably qualified and fit and proper persons capable of performing the relevant 'controlled functions'.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Unless an exemption applies, prior regulatory approval must be obtained to carry out 'regulated activities' in the course of business in the UK. 'Regulated activities' are defined in the Financial Services and Markets Act (Regulated Activities) Order 2001 (as amended). Insurance mediation activities are regarded as regulated activities. The relevant regulator (the PRA, the FCA, or both) must approve each regulated activity individually. The regulator has the power to impose restrictions on the scope of an insurer's or reinsurer's regulated activities.

On 6 March 2017, the FCA published CP17/7: *Insurance Distribution Directive (IDD) – Implementation Paper I*. The FCA's consultation will closed on 5 June 2017, a Policy Statement is expected in September 2017. The Insurance Distribution Directive (2016/97/EU) (IDD) came into force on 22 February 2016 and updates the Insurance Mediation Directive (2002/92/EC) (IMD), which establishes the framework for regulating EU insurance brokers, agents and intermediaries. The IDD must be implemented into national law by 23 February 2018. The IDD deals with the authorisation, passporting and general regulatory requirements for insurance and reinsurance intermediaries or distributors. It also encompasses organisational and conduct of business requirements for insurance and reinsurance undertakings. CP17/7 is the first of two consultation papers by the FCA setting out the proposals for the implementation of the IDD. It covers:

- the application of the IDD;
- professional and organisational requirements;
- complaints handling and redress;
- changes to conduct of business rules for non-investment insurance contracts; and
- the regulatory regime for ancillary insurance intermediaries.

The FCA's second consultation paper on the IDD is expected to be published later in 2017.

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

Officers, directors and persons who exercise senior management functions or 'controlled functions' under FSMA (such as, for example, the director function, chief executive function, actuary function, or systems and controls function) must be approved by the FCA or the PRA, or both, prior to performing such functions. Once approved to perform such functions, the person in question becomes subject to the senior insurance managers regime (SIMR) and accompanying Conduct Rules which impose a number of significant responsibilities, including a duty to comply with regulatory requirements, general principles and expectations on an ongoing basis. The SIMR, which came into force on 1 January 2016 for Solvency II firms, including UK branches of non-EEA firms, the Society of Lloyd's and Managing Agents, and insurance special purpose vehicles, as well as the more streamlined version of the SIMR for smaller insurers falling outside the Solvency II framework, which was introduced between 1 January 2016 and 7 March 2016, replace the Approved Persons regime. The senior insurance management functions (SIMFs) are intended to be more detailed than was the case under the Approved Pensions regime. The purpose for introducing the SIMFs was to ensure greater transparency about which individuals have responsibility for which aspects of managing the business. There is a new Group Entity Senior Manager Function (SIMF7) which is intended to capture anyone who exercises significant influence over the management or conduct of the affairs of the UK-regulated entity and is employed by, or is an officer of, a parent or holding company. Such a person, regardless of his or her physical location, will need to be approved by the relevant UK regulator prior to exercising significant influence over a UK regulated firm. New conduct rules apply to the new SIMR.

On 28 September 2016, the PRA published Policy Statement 27/16 *Strengthening accountability in banking and insurance: PRA requirements on regulatory references (part II)*, which follows Policy Statement 5/16 *Strengthening accountability in banking and insurance: Implementation of the senior managers and certification regime (SM&CR) and SIMR; PRA requirements on regulatory references* and Policy Statement 16/22

Strengthening accountability in banking and insurance: regulatory references, which set our requirements for the obtaining of regulatory references from all current and former employers in the previous six years for persons intending to exercise FCA controlled functions, other key function holders and notified non-executive directors. On 7 March 2017, the regulatory reference requirements set out in PS27/16 *Strengthening accountability in banking and insurance: PRA requirements on regulatory references (part II)* and certain SM&CR-related FCA requirements came into effect. The PRA and the FCA are expected to consult on the extension of the SM&CR to all regulated firms, including further developing the regime for insurers in 2017. The extended regime is expected to enter into force in 2018.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

UK capital requirements currently adopt, but also enhance, the requirements established by the EU Insurance Directives and are contained in the PRA Handbook. Different requirements are imposed on general and life insurers and pure reinsurers, with an overarching reserve power of the PRA to impose additional capital requirements (individual capital guidance) if deemed necessary. Pillar 1 of Solvency II, which came into force on 1 January 2016, introduced new quantitative capital requirements at both the solo entity and group level. Companies and particularly groups can develop their own internal risk-based capital models according to their economic capital needs relative to their risk profile. Pillar 1 capital requirements have two distinct levels: a minimum capital requirement (MCR) representing the minimum amount of capital that an insurer or reinsurer needs to cover its risks, and a solvency capital requirement (SCR), which is effectively the amount of capital that an insurer or reinsurer requires to operate as a going concern, assessed on a value at risk measure.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

Solvency II (adopted into the PRA Rulebook) introduced material changes to reserving and the calculation of reserves, or 'technical provisions' according to Solvency II. Articles 76 and 77 of Solvency II set out the basic requirements as to establishment and possession of technical provisions and as to their calculation. Unsurprisingly (re)insurers are required to establish technical provisions with respect to all their insurance and reinsurance obligations towards policyholders, and to calculate those provisions in a prudent, reliable and objective manner. The value of the technical provisions must correspond to the current amount the (re)insurer would have to pay if it were to transfer its insurance and reinsurance obligations immediately to another (Solvency II-regulated) (re)insurer. A major challenge introduced to the reserving process by Solvency II, however, is that the technical provisions must not only represent a best estimate, but also include a 'risk margin' each of which are to be calculated as prescribed. In addition, when calculating technical provisions, (re)insurers must segment their insurance and reinsurance obligations into homogenous risk groups and by lines of business as prescribed, hence raising specific allocation issues.

On 11 April 2017, the PRA sent a request to the UK's largest general insurers to provide information about the impact of a range of stress tests on their projected own funds, as well as providing additional information on their sectoral exposures to the UK economy by 14 July 2017. The General Insurance Stress Test 2017 (GIST 2017) exercise is split into two broad areas of interest: (i) a set of five severe but conceivable scenarios (four natural catastrophe scenarios and one economic downturn scenario consistent with the Banking Stress Test); and (ii) a capture of exposures that will allow the PRA to better understand the impact of potential losses by various sectors of the economy.

The EU Commission is expected to conduct a review of the implementation of Solvency II within EU member states in 2018. Despite the United Kingdom European Union membership referendum (Brexit) result on 23 June 2016 and the triggering of article 50 of the Treaty on European Union on 29 March 2017, the UK is currently in the process of withdrawing from the EU, it will still be a member of the EU in 2018. Discussions are currently ongoing between the British government and the EU Commission about the 'equivalence' post-Brexit status of the UK in terms of the requirements of Solvency II. Even though, at present, the UK has fully implemented the requirements of Solvency II, third country equivalence decisions are a matter for the EU Commission.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

No prior regulatory approval or registration of insurance products is required in the UK. Instead the FCA, in the exercise of its statutory objective of consumer protection and its 'outcomes focused' approach to regulatory supervision, imposes on insurers requirements as to their conduct of business and as to the suitability of insurance products sold to consumers, and regulates the selling and administration of insurance contracts, providing detailed rules including on categorisation of customers, communications with and financial promotions to customers, conflicts of interest, recordkeeping, disclosures required to be made to customers and product information. Insurers must also comply with the FCA's General Principles for Business and in this context insurers (particularly selling retail products) must be mindful of the need to 'pay due regard to the interests of customers and treat them fairly' and 'pay due regard to the information needs of clients and communicate information to them in a way which is clear, fair and not misleading'. The FCA has statutory powers of product intervention that would allow it to restrict the use of certain insurance product features, require that a product not be marketed or sold to certain categories of customer, or even ban the marketing or sale of a product.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

US-style examinations of insurers and reinsurers do not occur in the UK, and there is no public hearing process provided for in the usual conduct of regulatory affairs by the FCA or the PRA. Instead, the UK regulatory approach is to provide regulatory oversight through a combination of reporting, self-reporting and regulatory intervention if required. Regulatory oversight is usually exercised by the FCA (as to conduct) and the PRA (as to prudential matters) working together pursuant to a memorandum of understanding. Underpinning the oversight function are the duties imposed on insurers and reinsurers under the Principles for Business, which are applied by both the FCA and the PRA. Financial reporting and financial requirements were already provided for in the PRA Handbook, and have been supplemented by Solvency II requirements from 1 January 2016. Both the FCA and the PRA conduct visits and in-person interviews with insurers and reinsurers on a regular basis (the former 'arrow' visit regime under the FSA was continued initially by the PRA and the FCA, but has now been replaced with a new regime concerned with a firm systemic framework).

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

Insurers are required to hold admissible assets to cover their technical provisions, and in addition to maintain an adequate available solvency margin on top of the technical provisions. Solvency II has introduced a less prescriptive regime as to the nature and identity of admissible assets, focusing instead on broader quality criteria for the assets concerned if they are to form part of the requisite 'own funds' that are to comprise the MCR and the SCR. Capital of the highest quality will be eligible to be categorised as tier 1, and capital of lower quality will be tier 2 or tier 3. Tier 1 is itself divided into 'restricted' and 'unrestricted' tier 1 capital. The types of assets eligible to be 'own funds' within the three Tiers are classified in articles 69 to 78 of Commission Delegated Regulation (EU) 2015/35. Solvency II has removed many of the previous restrictions under GENPRU as to admissibility and percentage holding of assets, and instead has given insurers greater freedom to invest in assets that are appropriate to their business and to their individual solvency capital requirement.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

By virtue of Part XII of FSMA, a person must not acquire or increase control in a UK regulated insurance or reinsurance company without the prior approval of the PRA (it is a criminal offence to do so without such prior approval). 'Control' is defined as the acquisition of 10 per cent or more of the shares or voting power of the regulated entity or its parent entity with an overarching (and ill-defined) concept of the ability to exercise significant influence over the management of the regulated entity by virtue of a shareholding or voting power in the regulated entity or its parent. Prior regulatory approval will also be required where an existing controller proposes to increase its shareholding or entitlement to exercise voting power in the insurer or reinsurer or its parent above 20, 30 or 50 per cent. The PRA must consult with the FCA, and the FCA may request the PRA to reject the application or impose conditions on the approval of the change in control.

Applications for a change in control in respect of insurance intermediaries are made to the FCA.

Directors and officers of the proposed acquirer may need to apply to become senior managers in respect of exercising senior management functions in the regulated target entity, and will be subject to background investigations.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

There are no specific requirements or restrictions in respect of the financing of the acquisition of an insurance or reinsurance company. Where the acquirer is itself an insurance or reinsurance company, any debt or equity raised to fund the acquisition may affect the acquirer's own regulatory capital position and overall availability of resources. It will also need to be considered whether any acquisition financing or debt push down to the target or targets would either come within the financial assistance regime under Part 18, Chapter 2 of the Companies Act 2006, or would otherwise impact the regulatory capital position of the acquirer or the target or targets. There are no specific UK rules mandating or prohibiting any particular acquisition financing method.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

At less than 10 per cent of voting rights or share ownership, there should be no restrictions unless the acquirer of the minority interest is able to exercise significant influence over the management of the insurer or reinsurer, which could trigger a requirement for change of control approval. Otherwise, the regime described in question 10 will apply.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no specific restrictions or prohibitions on investment in an insurance or reinsurance company by foreign citizens, companies or governments. The same change of control rules apply as discussed in question 10.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Solvency II introduced new concepts of 'group supervision' and brought the entire group within the Solvency II framework, requiring groups subject to Solvency II to comply with Solvency II requirements under each of the three Pillars both at the level of the authorised insurance and reinsurance entities and on a group-wide basis. Groups have to establish an own risk and solvency assessment process for the group as a whole, as well as adequate and consistent risk management and governance procedures throughout the group, and satisfy regulatory supervisors as to the adequacy of these measures. Groups will also have to comply with all Pillar Three regulatory and public disclosure requirements for groups.

The group supervisor under Solvency II will usually be the supervisor in the state where the group has its headquarters, but groups may be supervised at more than one level and may have more than one group or individual supervisor, working as a college. Reporting and disclosure under Solvency II are required at the group and solo entity level, although a group may apply for approval to report as a single entity.

Primary disclosures are made through annual solvency and financial condition reports (SFCR), as well as through public disclosure of the SCR. In addition to the annual SFCR, a regular supervisory report will need to be submitted on an annual basis (but need not be publicly disclosed), and quantitative reporting templates will need to be submitted on both a quarterly and an annual basis.

Group solvency, which includes the holding company, must be calculated at least annually. The consolidated group SCR is the sum of the capital requirements of all the entities in the group. Group solvency must be calculated in accordance with the accounting consolidation method, the deduction and aggregation method or a combination of both methods. The accounting consolidation method is the default method for the calculation of group capital requirements. All group solvency calculations are to be carried out at the ultimate parent insurance entity or insurance holding company level. In the context of global groups, where sub groups exist at the EU level, supervisory authorities may decide to apply the group solvency calculation at the EU sub group level.

The implementation and effectiveness of the SCR standard formula under the Solvency II framework is being reviewed by the European Insurance and Occupational Pensions Authority with the findings to be delivered to the European Commission in 2018. The Solvency II regime as a whole will be reviewed by 2021. Following the result of the UK's Brexit referendum, the UK will no longer be a part of the EU by 2021. A Treasury Select Committee was established in September 2016 to look into EU insurance regulation. The Chairman of the Treasury Committee said: 'The Treasury Committee will now take a look at the Brexit inheritance on insurance to see what improvements can be made in the interests of the consumer.' Huw Evans, Director General of the Association of British Insurers in his evidence to the Treasury Committee on 25 January 2017 said:

> *'Equivalence is currently a political process, which can be withdrawn very quickly. It is something that, of course, has been designed and used by the European Union, not for huge member states that are departing it, but for countries like Bermuda and Switzerland that have always had a parallel relationship with it. It is not something that can, under its current form or its accepted usage, bear the weight of expectation that is being placed on it. ...That is why we are all in agreement that the way to move forward, whatever the ultimate political settlement, is to have a bespoke treaty between the UK and the European Union. The treaty should cover much of the same ground, but do so in a way that is appropriate for this huge insurance presence immediately neighbouring the EU 27, and can ensure the full range of access and regulatory co-operation that would be required to make that relationship a success. It should not use something that was never, ever designed for it.'*

Discussions are currently ongoing nationally and with the EU Commission about the 'equivalence' post-Brexit status of the UK in terms of the requirements of Solvency II. Even though, at present, the UK has fully implemented the requirements of Solvency II, third country equivalence decisions are a matter for the EU Commission.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

The various rules attached to the content of consumer insurance contracts generally do not apply to reinsurance contracts, and there is no specific UK regime prescribing the content, scope or application of reinsurance contracts governed by English law. In the UK, reinsurance is generally regulated in the same way as primary insurance, and English law on insurance contracts generally applies likewise to reinsurance agreements.

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Cedents will have to consider a number of factors when judging the size of any cession or retention, the starting point being the basic requirement that a cedent may only take credit for reinsurance if and to the extent that there has been an effective transfer of risk from the cedent to a third party. A reinsurer that is authorised as an insurance special purpose vehicle (ISPV) will have to fully fund its exposures to risks it assumes through the proceeds of a debt issuance or some other financing mechanism. Both cedent and reinsurer, if regulated in the UK, will also have to be mindful of the provisions in the PRA Rulebook as regards prudential requirements and risk assessment monitoring and control. Solvency II requires insurers to establish and maintain adequate technical provisions with respect to all of their insurance and reinsurance obligations towards policyholders (article 76). To the extent that an insurer has entered into risk mitigation techniques (such as reinsurance) then Solvency II and the PRA Rulebook provide detailed requirements as to how the amounts recoverable under reinsurance contracts and ISPVs are to be calculated (Appendix 1 of the PRA Rulebook).

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

There are no prescribed forms of collateral to be put up by reinsurers under English law or UK regulation. The ceding insurer and the reinsurer are at liberty to agree whatever form of collateral (if, indeed, any) they choose. From December 2008, the Reinsurance Directive has prohibited member states from requiring EEA reinsurers (but not non-EEA reinsurers) to pledge assets to cover their part of the cedent's technical provisions. Insofar as reinsurance arrangements are collateralised to protect against counterparty risk, they can be structured under English law to qualify as 'financial collateral arrangements' under the EU Financial Collateral Directive (2002/47/EC), which facilitates the enforcement of security over financial collateral within the EU. Under Solvency II, member states are no longer able to impose on reinsurers from an 'equivalent' jurisdiction (or another member state) collateral requirements that require the pledging of assets to cover unearned premiums and outstanding claims provisions (article 173).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

The extent to which a ceding insurance company can take credit for reinsurance, including by treating the reinsurer's share of technical provisions as an admissible asset of the ceding company or by reducing the ceding company's solvency requirements or valuing cash flows for the purposes of reserves, will depend on whether and, if so, to the extent that the contract of reinsurance effectively transfers risk from the ceding company to the reinsurer. INSPRU 1.1.19 used to set out the basic risk transfer requirement for all reinsurance contracts (including those with an ISPV) and for analogous non-reinsurance financing agreements for which a ceding company might likewise wish to take credit (such as contingent loans and securitisations) but is not included in the PRA Rulebook. The requirements of INSPRU 1.1.19 have become industry standards (also looked to by auditors and actuaries when considering the valuation of reinsurance coverage programmes) and so the current provisions of the PRA Rulebook on Technical Provisions (Chapter 7) on valuation of recoverables from reinsurance contracts and ISPVs (implementing article 81 of the Solvency II Directive) should be read with that in mind. Reference should also be made to Commission Delegated Regulation (EU) 2015/35, which sets out rules relating to technical provisions.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

Under Part XXIV of FSMA, the UK regulators (PRA and FCA) are given the right to be involved in insolvency proceedings against insurers. The insolvency proceedings available in the UK against insurers include liquidation, administration, a company voluntary arrangement and the appointment of a provisional liquidator. Insolvent insurance companies can also use a scheme of arrangement under Part XXVI of the Companies Act 2006. Relevant UK legislation includes the Insurers (Reorganisation and Winding Up) Regulations 2004 (2004 Regulations), the Insolvency Act 1986, Part XXIV of FSMA and the Insurers (Winding Up) Rules 2001. The 2004 Regulations set out a governing framework to determine issues arising in insurance insolvencies within the EU, and provide for mutual recognition of member states' insurance insolvency and winding-up measures. The 2004 Regulations also establish the priority of payment of insurance and other claims in an insurance insolvency. The Insolvency Act 1986 provides the basic law and framework for insolvency, administration and voluntary and involuntary liquidation in the UK and applies to insurers, as it applies to other corporate entities, procedures for the appointment of administrators and liquidators and for the winding up of insurers by court order. The Insurers (Winding Up) Rules 2001 provide detailed rules as to the conduct of an insurance liquidation and the procedures to be followed by the liquidator, and for the separation of life or long-term business assets in a liquidation from other assets. Lloyd's has its own procedures in the event of a syndicate or member being in financial difficulties, including a cash call on syndicate members to pay losses, the syndicate year of account being unable to close at 36 months and being left open in effective runoff until closure is possible, and the liabilities being settled in whole or in part by (and at the discretion of) the Lloyd's Central Fund.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The Insurers (Reorganisation and Winding-Up) Regulations 2004 provide, inter alia, that preferred creditors (being those with preferential debts such as monies due to Her Majesty's Revenue and Customs, social security and pension scheme contributions, and employee remuneration) will rank first in order of priority and that (subject to the claims of preferred creditors) direct insurance claims (eg, monies owed to an insurer's own policyholders) will have priority over the claims of all other unsecured creditors (with the exception of preferred creditors), including reinsurance creditors, on a winding up by the court or a creditor's voluntary winding up of the insurance company. In the case of insurers carrying on both insurance and reinsurance business, sums due to direct policyholders are given priority over sums due to cedents. Instead of making a winding-up order, a UK court may, under section 377 of FSMA, reduce the amount of one or more of the insurance company's contracts on terms and subject to conditions (if any) that the court considers fit. In the case of preferential debts and in the case of insurance debts, the debts of each class respectively rank equally among themselves and must be paid in full or, if assets are insufficient to meet them, the debts are abated in equal proportions. For a composite insurer authorised to carry on both life and non-life business, the life and non-life debts must be determined separately, and life claims

settled from only the life assets and non-life claims settled only from non-life assets.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

The IMD, adopted in the UK in 2005, and as updated by the IDD, applies to and requires authorisation of both independent intermediaries (such as insurance brokers) and also authorisation of insurers and reinsurers insofar as they conduct insurance and reinsurance mediation activities. The regulatory requirements applicable to intermediaries, mirror, to a considerable extent, many of the requirements applicable to insurers and reinsurers, including as to principles for business and conduct of business, and the approved persons regime. The IDD also enables intermediaries to operate throughout the EU using freedom of services or of establishment. Insurance intermediaries require authorisation from the FCA primarily, but if the intermediary is part of a group that includes a firm authorised by the PRA, then the FCA will also have to consult with the PRA before granting any Part 4A FSMA permission for insurance mediation. The IDD includes a number of exclusions and exemptions from the need for intermediaries to be authorised and the UK will retain the system whereby an intermediary can itself be an 'appointed representative' of another authorised person and thereby obviate the need for individual authorisation of the intermediary.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

By virtue of the Third Parties (Rights Against Insurers) Act 1930 and the Third Parties (Rights Against Insurers) Act 2010, as amended by the Insurance Act 2015, a third party with a claim against an insured can bring proceedings against the insurer in the event of the insured's insolvency. It is not possible to contract out of this. The rights transferred to the third party are the rights of the insured against the insurer under the contract of insurance in respect of the liability in question. Rights that are not referable to that liability are not transferred. The above-mentioned third-party actions do not apply to reinsurance contracts.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

In commercial policies, there is usually an express requirement to notify the insurer within a given number of days of the claim arising. The consequences of late notice will depend on whether the notice requirement is a condition precedent to the insurer's liability. If so, the insurer will be able to avoid paying the claim even if the delay in notifying the claim did not prejudice the insurer's position. In *Taylor v Builders Accident Assurance Ltd* [1997] PIQR p247, it was held that the delay in notifying the claim to the insurer deprived the insurer of its right to investigate and defend the claim, thus amounting to a repudiatory breach notwithstanding the fact that the condition breached was not expressly stated as a condition precedent. The court will look at the facts in each case and consider each policy on a case-by-case basis.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

As a general principle, English law does not provide a remedy in damages for the insured in the event of a wrongful denial of claim by the insurer. The burden of proof will be on the insured. See question 50 for a further discussion of extra-contractual liabilities.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

The notification by the insured of an event or circumstance within the terms of the policy for which the insurer may be liable triggers the insurer's duty to defend a claim.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

In order to succeed in a claim on an indemnity policy, the insured must demonstrate to the insurer that the insured is under a legal liability to one or more of those claiming against the insured and that the loss in question is covered by the policy (*Peninsular & Oriental Steam Navigation Co v Youell* [1997] 2 Lloyd's Rep 136, CA).

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

Subject to any provision to the contrary in the terms of the policy, there is no general incontestability period beyond which a life insurer cannot contest coverage based on misrepresentation in the application for coverage.

28 Punitive damages

Are punitive damages insurable?

Subject to the terms of the insurance policy, as a matter of general principle and public policy, damages awarded by a court, whether ordinary or punitive, are insurable.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Subject to a contractual provision to the contrary, an excess insurer will not be under a duty to 'drop down and defend' or pay the claim unless the primary insurer's limit of cover is fully exhausted.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

In *Teal Assurance Co Ltd v (1) WR Berkley Insurance (Europe) Ltd; (2) Aspen Insurance UK* [2013] UKSC 37, the Supreme Court held that a requirement in a policy for the insured to have 'paid' the amount of the self-insured retention or deductible prior to the insurer indemnifying the insured under the terms of the policy did not mean that the insured had to have made a monetary payment. Instead, the word 'paid' should be understood as being used as a measure of liability incurred.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

There is no particular order of priority for the payment of claims in circumstances where multiple claims are presented under the same policy. Each case will depend on the exact wording of the policy.

The court will look at the reality and facts of each case (see *Mabey and Johnson Ltd v Ecclesiastical Insurance Office plc* [2004] Lloyd's Rep IR 10 as per Morrison J).

Claims are usually paid in chronological order once they have been fully proved.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

As a starting point, the insured may not recover more than the loss sustained. The insured may choose, subject to the terms of the policy, which policy it wishes to claim under. The insurer who covers the loss may then be able to seek a contribution from the other insurer under the equitable doctrine of contribution (*Boag v Economic Insurance Company Ltd* [1954] 2 Lloyd's Rep 581). The obligation to contribute applies even

though a co-insurer's policy may be narrower or broader in its coverage provided that:

- the co-insurer's policy is in force and has not been repudiated (eg, due to a breach of the duty to disclose);
- the co-insurer's policy conveys the same risk as the policy under which the claim was paid;
- the same risk under both co-insurer's policies led to the loss;
- the insured had the same interest in the subject matter of each insurance policy; and
- the policies are effected by, on behalf of or provide benefit for, the same insured.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

There is no statutory definition of 'insurable losses'. In P*rudential Insurance Co v Commissioners of Inland Revenue* [1904] 2 HB 658, it was held that in order to be insurable, the loss must have the following characteristics: there must be an element of uncertainty about whether, when and how the loss will occur; if it were to happen, the loss must have an adverse effect on the insured; and the insured must have an insurable interest in the subject matter of the loss. Disgorgement is available only when the insured has breached an obligation of good faith or loyalty. Consequently, disgorgement is not an insurable loss. On the other hand, restitution claims are capable of being an insurable loss.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The terms 'occurrence' and 'event' are often not precisely defined in insurance contracts. In *Kelly v Norwich Union Fire Insurance Society* [1989] 2 All ER 888, the Court of Appeal held that the word 'event' referred to the peril rather than the damage in respect of various claims that had been made.

In A*XA Reinsurance UK Ltd v Field* [1996] 1 WLR 1026, the House of Lords defined an 'event' or an 'occurrence' as something that happens at a particular time, and in a particular place and way. In *Mitsubishi Electric v UK Ltd Royal London Insurance (UK) Ltd* [1994] 2 Lloyd's Rep 249, the court aggregated a number of separate losses as one loss, holding that all the losses arose from the same occurrence. In *Lloyds TSB General Insurance Holdings Ltd v Lloyds Bank Group Insurance Co Ltd* [2003] Lloyd's Rep IR 623, the House of Lords emphasised that each case must depend on the exact wording of the relevant 'occurrence' clause. Further, it stressed that in clauses of this kind it is essential to focus on the question of the causes of the various losses.

In *AIOI Nissay Dowa Insurance Company Limited v Heraldglen Limited and Advent Capital (No. 3) Ltd* [2013] EWHC 154, a case that considered the definition of 'event' or 'occurrence' in the context of the terrorist attacks of 11 September 2001 on the Twin Towers of the World Trade Center in New York, Field J held that the 'four unities' of the circumstances and purposes of the persons responsible, cause, timing and location of the 'event' or 'occurrence' represented a useful test for establishing whether there was one or more 'event' or 'occurrence'. In *AIG Europe Ltd v OC320301* [2016] EWCA Cir 367, the Court of Appeal had to determine the true construction of the phrase 'a series of related transactions' in the aggregation clause in the standard minimum terms and conditions of solicitors' compulsory liability insurance. The Court of Appeal held that the first instance judge had misdirected himself in saying that the transactions had to be 'dependent' on each other before aggregation could occur. Instead, the connection between the matters or transactions had to be an intrinsic relationship rather than an extrinsic one with a third factor.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

The Insurance Act 2015, which came into force on 12 August 2015, abolished 'basis of contract' clauses in insurance contracts. Such clauses have the effect of elevating the insured's answers to an insurer's questions to the status of contractual warranties. If the insured's answers are in fact material misstatements, the insurer may rescind the contract. A misstatement is material if it would influence the judgement of a prudent insurer in pricing the premium or deciding whether to take the risk. The Insurance Act 2015 imposes a duty of fair representation on the insured. Where the breach of this duty is deliberate or reckless, the insurer may avoid the contract, refuse all claims and need not return any of the premiums paid. Where the breach was neither deliberate nor reckless, the insurer may avoid the contract and refuse to pay all claims but must return the premiums paid.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

There are no special procedures for reinsurance disputes under English law. Most reinsurance contracts contain an arbitration or choice of forum clause. Where the English courts have exclusive jurisdiction, disputes are likely to be referred to the Commercial Court, which has experience in dealing with reinsurance disputes. If a reinsurance contract contains an arbitration clause, disputes arising from that contract may be resolved by an arbitral tribunal. Parties to a reinsurance contract may also choose to reach a settlement prior to initiating formal proceedings. Indeed, the Pre-Action Protocols under the Civil Procedure Rules require that attempts to settle out of court be made before litigation is commenced.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Jurisdiction is one of the most common issues that arises in reinsurance disputes (see *Faraday Reinsurance Co Ltd v Howden North America Inc & Another* [2012] EWCA Civ 980). In addition, 'follow-the-fortunes' and 'cut-through' clauses are also often disputed.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

It is a well-established principle of English law that arbitral awards must give reasons for their decision. Arbitrations that have their seat in England and Wales are governed by the Arbitration Act 1996. Section 52(4) of the Arbitration Act requires that an award 'shall contain the reasons for the award unless it is an agreed award or the parties have agreed to dispense with reasons'. The International Chamber of Commerce and the London Court of Arbitration are commonly used arbitral institutions with their own independent rules to govern the proceedings. Most London arbitrators will follow the procedure of the Commercial Court, particularly in relation to evidence and reasons for the decision.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Non-signatories to a contract may, in certain circumstances, claim the benefits of that contract as third-party beneficiaries under the Contracts (Rights of Third Parties) Act 1999. In such circumstances, the third party may either invoke or be bound by an arbitration clause contained in the contract. It is generally accepted that if a third party is bound by the same obligations stipulated by a party to a contract and this contract contains an arbitration clause or, in relation to it, an arbitration agreement exists, such a third party is also bound by the arbitration clause, or arbitration agreement, even if it did not sign it. Note, however, that where the Contracts (Rights of Third Parties) Act 1999 has been expressly excluded, a non-party beneficiary may not be able to claim the benefits of that contract before an arbitral tribunal formed under the arbitration clause in the contract.

Update and trends

Political events, and the uncertainties resulting from them, have been to the fore, affecting both the insurance and reinsurance markets, including:

- the UK's triggering of article 50 and the uncertainties surrounding any final Brexit outcomes for the (re)insurance market;
- the potential loss to UK insurers of the insurance 'single market' and the moves by UK insurers (including Lloyd's itself) to establish post-Brexit EU subsidiaries to retain some benefit from the single market; and
- the unexpected announcement in February 2017 by the Ministry of Justice that the Ogden discount rate (used in the calculation of awards in the UK for serious injuries that require long term care) was being reduced from a positive 2.5 per cent (where it had been since 2001) to a negative 0.75 per cent. As a result, reserves held for large outstanding claims subject to Ogden must be increased very significantly, with an estimated cost to UK insurers (particularly in motor, employers' liability and public liability classes) of £7 billion.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

Under section 58(1) of the Arbitration Act, a tribunal's award is final and binding between the parties. However, a party may apply to the English courts to remit, set aside or declare non-effective an award on a number of grounds, including where the tribunal lacked jurisdiction, where there were serious irregularities in the arbitral proceedings or, unless parties agree to the contrary, to address a question of law arising from an award made in the proceedings.

A party to arbitral proceedings may apply (on notice to the other parties and to the tribunal) to the court challenging an award in the proceedings on the ground of serious irregularity affecting the tribunal, the proceedings or the award.

The English courts have afforded procedural decisions in international arbitrations substantial deference: 'It is not a ground for intervention that the Court considers that it might have done things differently,' (*ABB AG v Hochtief Airport GmbH* [2006] EWHC 388, paragraph 67). Rather, an award will only be annulled if the arbitral process was 'so removed from what could reasonably be expected of the arbitral process that the Court should be expected to intervene' (*Latvian Shipping Co v Russian Peoples' Ins Co* [2012] EWHC 1412 (Comm)).

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

In the absence of a contractual provision to the contrary, the burden of proof to establish that the loss was covered and that there is an actual liability for the reinsurer to pay is on the reinsured.

'Follow-the-settlements' clauses, which oblige reinsurers to indemnify their reinsured against compromises of the insured's claim without requiring proof of liability, are common in reinsurance agreements, as are various types of 'follow-the-fortunes' clauses.

'Claims cooperation' clauses, which impose an obligation on the insured to cooperate with the reinsurer, are also popular. The scope of the obligation and the defences available to the reinsurer are determined by the terms of the reinsurance contract.

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The starting point in general commercial contracts rests on the principle of caveat emptor, which places the duty of establishing the facts that are the subject matter of the agreement on the buyer. Per contra, prior to the Insurance Act 2015, contracts of insurance used to be based on the principle of uberrimae fidei (utmost good faith), which placed the insured under a duty to disclose all material facts and circumstances that could influence the insurer in its decision about the acceptance or the price of the risk in question. Breach of this duty used to render the insurance contract voidable.

Section 14 of the Insurance Act 2015 modifies the concept of uberrimae fidei in contracts of insurance by introducing a statutory duty of fair presentation in section 3 of the Insurance Act 2015. Consequently, it is no longer possible to avoid the contract of insurance on the basis that the duty of uberrimae fidei has not been observed. The Insurance Act 2015 introduces proportionate remedies for non-disclosure and other breaches.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Although the two types of reinsurance operate under the same basic legal framework, historically, unlike facultative reinsurance, treaty reinsurance was generally not strictly regarded as a contract of reinsurance (see *Glasgow Assurance v Symondson* (1911) 16 Com Cas 109). In *Citadel Insurance Co v Atlantic Union Insurance Co* [1982] 2 Lloyd's Rep 543, it was held that while in facultative reinsurance the duty of disclosure exists up to the time that the reinsurer agrees to take the risk, in treaty reinsurance, although the duty exists until the conclusion of the treaty, it may not persist where the reinsurer is bound to take the risks ceded, given that there is no opportunity for the reinsurer to exercise judgement in respect of those risks. However, if treaty reinsurance or open cover enables the reinsurer to query or refuse the risks, or both, the duty of disclosure is likely to continue throughout the obligations assumed (see *The Litsion Pride* [1985] 1 Lloyd's Rep 437).

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

As a matter of general principle, the doctrine of privity of contract prevents a person who is not a party to a contract (ie, the reinsurance contract) from relying on or having rights under the contract (eg, bringing a direct action for coverage under the reinsurance agreement). A reinsurance contract is an agreement between the reinsured and the reinsurer. The primary insured is not a party to the reinsurance agreement, and therefore does not have any rights under it. However, unless expressly excluded by the terms of the reinsurance contract, the Contracts (Rights of Third Parties) Act 1999 enables a third party to bring proceedings under the contract where the contract expressly enables this to happen, or where the contract purports to confer a benefit on him or her. In practice, most reinsurance agreements expressly exclude the Contracts (Rights of Third Parties) Act 1999.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

There is no general obligation on a reinsurer to pay a policyholder's claim in the event of the insurer being insolvent and not being able to pay the claim. However, unless expressly excluded, which in reinsurance contracts it usually is, the Contracts (Rights of Third Parties) Act 1999 may enable a policyholder to rely on the reinsurance policy where the insurer is insolvent and cannot pay.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

There are no prescribed provisions under UK law or regulation as to the notice provisions to be included in a reinsurance contract. It is for the cedent and reinsurer to agree such terms as they see fit, and to possibly take account of basic provisions in the Interpretation Act 1978 as to timing and deemed service of notice. It is in the interests of the reinsurer to be careful as to the notice provisions, given its exposure on 'follow the fortunes' and other grounds, so a reinsurance treaty would usually contain detailed provisions on service (and often seek to exclude deemed service) of notice by the cedent insurer. The basic common law rule is that the description of the event or claim must be sufficient for the reinsurer to be able to understand the nature of what is being notified, so as to be at liberty to enquire further if it so elects. The consequence of failure to notify to the contractual standard as to timing and detail applicable will depend on the terms of the reinsurance contract, a key point being whether strict compliance with the notice clause has been expressed as a condition precedent (any breach of which would enable the reinsurer to avoid liability under the contract) or merely as a condition (breach of which would give the reinsurer a right to damages depending on whether the reinsurer can show loss arising from breach of the condition). Generally, it would be unusual under current UK practice for failure to provide a sufficient and punctual notification to give the reinsurer a right of repudiation of the reinsurance contract, and damages would usually (depending on the precise contractual wording) be the only realistic remedy (the loss suffered by the reinsurer owing to late or inadequate disclosure (or both) being a key and potentially difficult issue for it to prove).

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

The allocation of underlying claim payments or settlements depends on the wording of the reinsurance agreement. Excess of loss reinsurance is generally provided on a 'loss occurring' basis so that the reinsured must prove that it suffered the loss during the policy period. A reinsured cannot choose the order of allocation of payments or settlements. Once a layer has been exhausted, the next excess policy becomes the underlying policy. Consequently, that layer and its reinsurer are liable once the liability of the insured has been established.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

In the absence of a 'follow-the-settlement' clause, the reinsurer must prove its loss, as a part of which it may be necessary to review the insured's documents. In *Pacific & General Insurance Co Ltd (in liquidation) v Baltica Insurance Co (UK) Ltd* [1996] LRLR8, it was held

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that although each case depends on its own specific facts, where the reinsurer makes a timely request for inspection of the reinsured's documents, the court is likely to grant the request (unlike in cases where the reinsurer makes an application for inspection of the reinsured's documents when a summary judgment against it is imminent).

In *Commercial Union Assurance Co plc v Mauder* [1996] 2 Lloyd's Rep 640, the reinsurer applied for disclosure of documents relating to the insurer's liability under the original contract of insurance. The insurer argued that such documents were privileged and, in any event, unnecessary to dispose of the dispute fairly. It was held that the test of relevance was wide and was not restricted to documents that will be admissible in evidence. Documents relating to negotiations leading to a settlement of a dispute may be relevant and disclosable.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

The reinsurer's obligations to reimburse the cedent for its commutations with the underlying insured will depend on the terms of the reinsurance contract, particularly with reference to the provisions as to 'follow the settlements' and as to the claims settlement authority vested in the cedent.

Usual 'follow-the-settlements' clauses in the London market will generally commit the reinsurer to follow a settlement, including a commutation, made by the cedent (up to the reinsurance policy limit) where the cedent has entered into a loss settlement or compromise of liability or quantum, or both. The reinsurer will tend to be bound by a commutation payment where the cedent has entered into the commutation in a 'bona fide and business-like fashion' (*Insurance Co of Africa v Scor (UK) Reinsurance* [1985] 1 Lloyd's Rep 312) and so the onus will be on the reinsurer to establish a lack of bona fides or business-like dealing on the part of the cedent given that the reinsurer may be bound even if it is proved subsequently that the policy did not in fact create a liability to the insured or that the insured's claim was otherwise ineligible (eg, owing to misrepresentation or fraud by the insured).

A well-constructed commutation agreement between a cedent and its underlying insured will include incurred but not reported claims (IBNR) within its scope, both as to valuation and so as to include IBNR within the full and final termination and settlement of liabilities under the commutation. From the reinsurer's perspective, IBNR by its very nature represents an estimate of claims that might be made in future but are not yet claims made under the insurance policy or loss settlements to which in either case the reinsurance would respond. Depending on the breadth of the 'follow the settlements', the reinsurer may accordingly be able to deny liability for IBNR.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

ECOs (sometimes referred to as 'extra-contractual damages') stem from acts or omissions of an insurer towards its insured that are found by a court to constitute an event for which the insurer is liable to its insured outside the strict boundaries of the policy, perhaps for negligence, bad faith or misconduct (often in claims handling), and which leads to a monetary award being made against the insurer, sometimes by way of punitive damages. The sum in question is 'extra-contractual' because it falls outside the contractual bounds of the coverage provided under the insurance policy. The London Market standard ECO clause is NMX 100.

The ability of the insurer to then recover from its own reinsurers for liability to ECOs will depend on the terms of the reinsurance contract. Some reinsurance treaties include coverage for the cedent's ECOs within specific monetary and coverage limits, while others may expressly exclude ECOs or be silent on coverage for ECOs.

Coverage for ECOs will usually exclude arising through fraud or bad faith, and may operate in excess of any concurrent errors and omissions coverage.

Given that in the UK (unlike in the US) courts do not award punitive damages, reinsurers' concerns as to coverage of ECOs arising from an award of punitive damages against the reinsured are less acute.

United States

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Regulation

1 Regulatory agencies

Identify the regulatory agencies responsible for regulating insurance and reinsurance companies.

In the US, insurance business (including reinsurance) is primarily regulated at the state level. Each state has an insurance department, and laws, regulations, policies and procedures that regulate virtually every aspect of the operations of insurers and reinsurers. States also regulate the actions of insurance intermediaries, including insurance producers, agents, brokers, reinsurance intermediaries and third-party administrators.

The Supreme Court held in *United States v South-Eastern Underwriters Association*, 322 US 533 (1944), that Congress had the power to regulate the industry. In response, Congress enacted the McCarran-Ferguson Act, which, broadly speaking, left regulatory control over insurance to the states, as long as their laws and regulations do not conflict with federal antitrust laws on rate fixing, rate discrimination and monopolies. Some national insurance programmes, including, but not limited to, the Terrorism Risk Insurance Act, the National Flood Insurance Program, the Federal Crop Insurance Program and the Longshore and Harbor Workers' Compensation Act, were created by federal act, and are subject to regulation by the federal government with certain regulatory responsibilities left to the states.

After the passage of the McCarran-Ferguson Act, each state continued to develop its own set of insurance laws, regulations and rules for state agencies to impose on the business of insurance in their respective states. As a result, insurance companies, reinsurance companies and insurance intermediaries are subject to the laws and regulations of each US jurisdiction in which they transact business. This can be quite onerous for companies seeking to do business nationwide.

Recent developments at the federal level have begun to affect certain aspects of insurance regulation in the US, including in connection with surplus lines insurance and credit for reinsurance, and have introduced a federal regulatory overlay on some of the largest US insurers. Specifically, the Dodd Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was enacted in 2010 and resulted in changes in the regulation of the US surplus lines market (see question 3) and credit for reinsurance requirements (see question 18). These changes:

- remove the ability of multiple states to tax a surplus lines transaction by restricting such tax to an insured's 'home state' (as defined under the federal legislation);
- establish uniform standards for surplus lines insurer eligibility;
- streamline surplus lines placements for larger commercial insureds that qualify as 'exempt commercial purchasers' under the law; and
- restrict determination of credit for reinsurance to the cedent's domiciliary jurisdiction (see questions 17 and 18).

The Dodd-Frank Act also created:

- the Federal Insurance Office (FIO), an office of the US Department of the Treasury charged with monitoring all aspects of the insurance industry (other than health, long-term care and crop insurance), including identifying gaps in insurance regulation; and
- the Financial Stability Oversight Council (FSOC), an interagency body charged with identifying systemic risks in the US financial services industry and designating systemically important financial institutions (SIFIs), including insurers and reinsurers, which are to be supervised by the Board of Governors of the US Federal Reserve System (Federal Reserve) and subject to enhanced prudential standards. To date, the FSOC has designated three US insurers as SIFIs, and two remain so designated (with the third one having successfully contested its designation in federal court). SIFI designations are subject to an annual re-evaluation process conducted by the FSOC.

The future of many aspects of the Dodd-Frank Act, however, remains uncertain under the new Trump administration and the Republican-controlled Congress. Based on early indications from the Trump administration and Republican proposals in Congress, the current insurance-based SIFIs may be de-designated under the new administration. Moreover, the designation and supervisory powers of the FSOC and Federal Reserve over non-bank financial institutions under the Dodd-Frank Act could be circumscribed and perhaps even repealed. The authority and responsibilities of FIO may also be significantly modified or potentially repealed. There has been no indication as of yet that any of the Dodd-Frank Act reforms relating to the surplus lines market or credit for reinsurance requirements will be repealed or revised.

In addition, the National Association of Insurance Commissioners (NAIC) continues its efforts to coordinate regulation of insurance in US jurisdictions. The NAIC is a private organisation, created and governed by the chief insurance regulators from all US jurisdictions, that serves as a vehicle for cooperation among state insurance regulators. One way the NAIC accomplishes its purpose is to propose model laws and regulations for consideration by state legislatures. In addition, the NAIC establishes that some model laws or regulations are accreditation standards, thereby practically compelling states to adopt laws or regulations based on such models. The purpose of the NAIC's accreditation programme is for state insurance departments to meet baseline standards of solvency regulation, particularly with respect to the regulation of multi-state insurers. NAIC accreditation allows non-domestic states to rely on the accredited domestic regulator to fulfill a baseline level of effective regulatory supervision, promoting inter-state reliance and reducing regulatory redundancies (all 50 states are currently accredited).

The NAIC also helps to improve efficiency by pooling resources through its centralised facilities. For example, insurance regulators in the US use the NAIC's financial databases, often as their primary data source. While the NAIC is a voluntary organisation and cannot mandate the states to enact any laws, it is a strong influence. In recent years, there has been increasing pressure on states to coordinate their efforts and work towards uniformity in light of proposals to replace or supplement the state-based system of insurance regulation with a federal regulatory system.

2 Formation and licensing

What are the requirements for formation and licensing of new insurance and reinsurance companies?

Insurance company licensing

To form a US insurance company, the first step is to determine the appropriate type of company. There are two main types of insurance companies in the US: mutual companies and stock companies. A stock

insurer is a profit-making company funded by an initial capital investment by the owners of the insurer. Mutual insurers are owned by their policyholders, rather than stockholders.

Companies must also select a state of domicile. The factors that a company may consider in selecting a state of domicile include the location from which it will operate the business, the speed with which it wants to become licensed and the regulatory environment in that jurisdiction.

Generally, the US insurance industry consists of two major product lines: property and casualty insurance, and life and health insurance. Property and casualty insurance products include automobile and homeowners' insurance sold to individuals (personal lines of insurance) as well as products designed to protect businesses from property damage and liability (commercial lines of insurance). The life and health insurance industry sells three major types of products: life insurance, annuities and health insurance.

Every insurance company must obtain a licence or certificate of authority in its chosen state of domicile before it may begin transacting business and seek the authority to transact business in other jurisdictions. Each state has statutory minimum capital and surplus requirements, which generally are fixed amounts based on the lines of business the company seeks to write. States also require that every insurance company maintain, in addition to minimum capital and surplus, risk-based capital that is calculated pursuant to a formula based in part on the amount and kinds of insurance it writes (see question 6).

Reinsurance company licensing

Reinsurance companies may be either licensed or accredited. The licensing requirements for reinsurance companies are largely the same as those applicable to insurance companies, as described above. However, subject to jurisdictional considerations with respect to activities in-state that might constitute the 'doing of an insurance business', a non-US reinsurer may operate in the US market on an 'unauthorised' basis, without having to subject itself to the US insurance licensing regime.

A licensed reinsurer is one that has undergone the state's formal application and approval process, and has obtained a licence or certificate of authority to transact reinsurance business within the state. In most states, an insurance company may act as a reinsurer for any line of business it is licensed to write on a direct basis. Some states allow for a reinsurance-only licence.

Accredited reinsurers, while not formally licensed by the state, satisfy certain criteria in order to provide reinsurance in a particular jurisdiction. The criteria for accreditation as a reinsurer generally require that the company:

- submit to jurisdiction in the state;
- submit to the state's authority to examine its books and records;
- be formally licensed to transact insurance in at least one other state;
- file an annual financial statement with the state insurance commissioner; and
- maintain a minimum capital and surplus reserve.

3 Other licences, authorisations and qualifications

What licences, authorisations or qualifications are required for insurance and reinsurance companies to conduct business?

Once a company is licensed in its state of domicile, it must obtain a licence or become accredited in any other US jurisdiction in which it will be authorised to conduct an insurance business. A non-US reinsurer need not comply with licensing requirements if it conducts its US reinsurance business on an 'unauthorised' basis in compliance with the applicable state laws in the US (see questions 2, 17 and 18).

Surplus lines insurance

There are certain limited exceptions in the US to insurance company licensing requirements, including, but not limited to, placements with surplus lines insurers. A surplus lines insurer is generally not licensed to transact business directly in any jurisdiction other than its domiciliary state. Before any business can be placed with a surplus lines insurer in a given state, the insurer must be deemed eligible under that state's surplus lines laws and in accordance with the Dodd-Frank Act (which establishes uniform standards for surplus lines insurer eligibility), and the insurance generally must be unavailable from licensed carriers in that state. Such 'surplus' business must be 'exported' by specially licensed surplus lines brokers who make appropriate tax and other required regulatory filings. Surplus lines insurance is subject to less stringent regulation than insurance written by licensed companies. See questions 4 to 21 for a discussion of the regulation of US-licensed insurers and reinsurers (the regulation of surplus lines insurance in the US is not discussed).

4 Officers and directors

What are the minimum qualification requirements for officers and directors of insurance and reinsurance companies?

States impose a variety of minimum standards for directors of insurance and reinsurance companies, including age and residency requirements. Some states also require that a specified number of directors be independent. All officers and directors of insurance and reinsurance companies must submit biographical affidavits to the insurance departments of the states in which the company is licensed, and are subject to background investigations. US states through the NAIC have been placing greater focus recently on enhancing reporting of corporate governance practices.

5 Capital and surplus requirements

What are the capital and surplus requirements for insurance and reinsurance companies?

Capital standards are the main tool used by regulators to monitor the solvency of insurers and reinsurers. Insurance companies and reinsurance companies are required by state laws to have certain amounts of capital and surplus to establish and continue operations and satisfy risk-based capital requirements. The specific amounts of capital and surplus (including risk-based capital) required vary depending on the lines of business for which the insurer is licensed and the volume of business. In addition, states regulate the investments of a company's assets (see question 9). Only permitted assets under the investment guidelines, known as 'admitted' assets, may be counted towards the company's capital and surplus.

6 Reserves

What are the requirements with respect to reserves maintained by insurance and reinsurance companies?

In addition to setting capital requirements, state laws require insurers to set aside certain reserve amounts for future benefit and loss payments. The reserve requirements for life insurers are based on standard actuarial procedures and assumptions promulgated by the NAIC and adopted by the various states. The requirements for property and casualty insurers are more variable given the subjective factors affecting future obligations (ie, in contrast to life insurance claims, which are typically more predictable, the range of potential outcomes with respect to property and casualty insurance contracts can vary widely depending on, inter alia, whether claims are made and the ultimate costs of settlement). Regulators require actuarial opinions in respect of the reserves maintained by insurance and reinsurance companies to assess whether they are establishing adequate reserves. The form and content of the actuarial opinion differs between property and casualty and life insurers.

States, through the NAIC, are also in the process of implementing a new method for calculating life insurance policy reserves, referred to as principle-based reserving (PBR), which, when fully implemented, will replace the current formulaic approach to determining policy reserves with an approach that more closely reflects the risks associated with increasingly complex life insurance products using justified company experience factors, such as mortality, policyholder behaviour and expenses. PBR became effective on 1 January 2017, commencing a three-year transition period during which PBR will be optional and following which PBR will become mandatory. PBR is also expected to eliminate, or at least diminish, the life insurance industry's need to use captive insurance companies to finance reserves required under current regulations for certain term life insurance policies (known as 'XXX reserves') and certain universal life insurance policies (known as 'AXXX reserves') in cases where statutory reserves are considered excessive or redundant compared to economic reserves.

7 Product regulation

What are the regulatory requirements with respect to insurance products offered for sale? Are some products regulated by multiple agencies?

In order to sell its products in a state, an insurer generally must first obtain approval from the state's insurance department for the rates and forms it proposes to use. State laws typically require that rates not be inadequate (to prevent company insolvency), excessive, discriminatory or unreasonable in respect of the benefits provided. Regulators review policy forms to confirm that they do not provide inadequate coverage, or contain provisions that could be illegal or confusing or misleading to consumers. Certain types of commercial insurance are exempt from rate and form filing requirements in some states. Variable life and annuity products are also subject to regulation under federal and state securities laws. For example, the US Department of Labor recently promulgated new fiduciary investment advice rules that are expected to lead to significant changes in the way financial services providers, including insurers, sell financial products and provide investment advice to retirement plans and IRAs. However, these fiduciary rules remain controversial and the current US administration has delayed the effective date of the rules, which will likely be significantly revised, replaced or possibly repealed. Some types of coverage, such as workers' compensation insurance and health insurance, may also be subject to regulation by state agencies apart from the insurance department (eg, workers' compensation commissions and departments of public health). Several aspects of health insurance are also regulated by, and subject to laws and regulations of, federal government agencies.

8 Regulatory examinations

What are the frequency, types and scope of financial, market conduct or other periodic examinations of insurance and reinsurance companies?

The insurance laws in most states require the insurance regulator to perform financial and market conduct examinations of licensed insurers no less than every three to five years. Financial examinations are typically conducted by the insurance regulator in the insurer's or reinsurer's domiciliary state. Examinations may either be routine, in the case of periodic examinations required by law, or targeted, as, for example, in the case of market conduct complaints received by the regulator or the emergence of solvency concerns or other regulatory issues. Financial examinations typically focus on the financial condition of the insurer, while market conduct examinations focus on areas such as sales, advertising, claims handling and the insurer's business practices more generally.

9 Investments

What are the rules on the kinds and amounts of investments that insurance and reinsurance companies may make?

In order to ensure that an insurer's investments are appropriate to support its liabilities, state insurance laws generally regulate the types and amounts of assets in which an insurer may invest. Permissible investments acquired or held pursuant to the applicable law qualify as 'admitted assets' for purposes of inclusion in the company's financial statements. State insurance regulation of insurance and reinsurance company investments, however, is not uniform, as the NAIC has two distinct model laws relating to insurer investments that alternatively restrict insurer investments by imposing either a 'defined limits' or a 'defined standards' approach. Under a defined limits approach, regulators place certain limits on amounts or relative proportions of different assets that insurers can hold to ensure adequate diversification and limit risk. Under a defined standards approach, regulators restrict investments based on a 'prudent person' approach, allowing for discretion in investment allocation if the insurer can demonstrate adherence to a sound investment plan. Furthermore, states have not generally adopted investment laws that strictly follow the NAIC models.

10 Change of control

What are the regulatory requirements on a change of control of insurance and reinsurance companies? Are officers, directors and controlling persons of the acquirer subject to background investigations?

The change of control of insurance and reinsurance companies is subject to the approval of state insurance regulatory agencies. 'Control', under most states' insurance laws, is presumed to exist on the acquisition of ownership of 10 per cent or more of the voting securities of an insurer or a person controlling the insurer (see question 12). A person or entity seeking to acquire or merge with an insurance company or a person or entity controlling the insurer is required to file with the insurance department in the state of domicile an acquisition of control statement, commonly known as a 'Form A', regarding the proposed merger or acquisition. The Form A contains information about the merger or acquisition, such as the method of acquisition, identity and background of the acquirer and its directors and officers, source and amount of consideration used to fund the proposed merger or acquisition, future plans of the acquirer with respect to the insurer, information about voting securities and other financial information and projections. The acquiring company is typically required to submit biographical affidavits of its officers, directors and individuals owning a certain percentage (typically 10 per cent) of the acquiring entity either directly or indirectly. Some states also require that fingerprint cards and third-party background investigations of these directors, officers and stockholders be submitted.

State insurance departments review the Form A to determine that, after the change of control, the domestic insurer would be able to satisfy the requirements for the issuance of a certificate of authority, the merger or acquisition would not substantially lessen competition in insurance or tend to create a monopoly in the state, and the financial condition of the acquiring party will not jeopardise the financial stability of the acquired company. In some states, a hearing before the insurance commissioner is required before an approval order is issued.

Certain states, including New York, have recently adopted more stringent review requirements for the acquisition of control of insurers, in particular when the acquiror is affiliated with a private equity firm. The NAIC recently updated its Financial Analysis Handbook (which is frequently consulted by insurance regulators) to include similar measures.

11 Financing of an acquisition

What are the requirements and restrictions regarding financing of the acquisition of an insurance or reinsurance company?

A party wishing to acquire or merge with a US insurer or reinsurer must disclose to state regulators the source and amount of the consideration to be used to fund the transaction, although such information may be kept confidential by the regulator. The Form A will not be approved if it is determined that the financial condition of the acquiring party is such that it could jeopardise the financial stability of the target company or the interests of policyholders. In most cases, the acquirer will not be permitted to use any assets of the target company to finance the acquisition, and there are limitations on the amount of debt that may be used.

12 Minority interest

What are the regulatory requirements and restrictions on investors acquiring a minority interest in an insurance or reinsurance company?

As noted above, any person seeking to acquire 'control' of an insurance or reinsurance company must receive approval from the insurance regulator of the insurer's domiciliary state prior to completing such acquisition (see question 10). 'Control', under most states' insurance laws, is presumed to exist upon the acquisition of ownership of 10 per cent or more of the voting securities of an insurer or a person controlling the insurer. However, a person acquiring a minority, but more than 10 per cent, interest in an insurer may elect to submit a 'disclaimer of control' to the domiciliary regulator to rebut the presumption of control, and thereby be excused from a Form A filing and not

be considered a controlling person for insurance regulatory purposes following the acquisition. The disclaimer of control process is generally less burdensome than the Form A process, and typically requires disclosure of all material relationships between the parties as well as the basis for disclaiming control. Approval of a 'disclaimer of control' is subject to the regulator's discretion.

13 Foreign ownership

What are the regulatory requirements and restrictions concerning the investment in an insurance or reinsurance company by foreign citizens, companies or governments?

There are no per se restrictions under state insurance laws on investments in insurance or reinsurance companies by foreign citizens or companies. In reviewing an application seeking approval of a proposed acquisition of control of an insurer, the state insurance commissioner may deny the application if he or she determines that the competence, experience or integrity of those persons who would control the target company are such that it would not be in the interests of the policyholders of the target company or the public to permit the investment. In addition, approximately 30 states have 'government ownership' statutes, which generally provide that no certificate of authority or licence to transact any kind of insurance within a state will be issued or continued if the insurer is owned or controlled by any other state or foreign government or political subdivision thereof. Outside of the insurance regulatory context, there are also non-insurance federal reporting requirements in connection with foreign investments in US business enterprises (see the US Department of Commerce reporting requirements).

In addition, acquisitions by a foreign acquirer may be subject to review and scrutiny by the Committee on Foreign Investment in the US (CFIUS) if the acquisition could potentially threaten US national security (which, for example, can include, based on a prior CFIUS review of a foreign insurance company acquisition, the provision of insurance policies to federal employees), CFIUS is an inter-agency committee of the US government that reviews the national securities' implications of foreign investments in US companies or operations. CFIUS is chaired by the Secretary of Treasury and includes representatives from 16 US departments and agencies.

14 Group supervision and capital requirements

What is the supervisory framework for groups of companies containing an insurer or reinsurer in a holding company system? What are the enterprise risk assessment and reporting requirements for an insurer or reinsurer and its holding company? What holding company or group capital requirements exist in addition to individual legal entity capital requirements for insurers and reinsurers?

Following the adoption by the NAIC of amendments to the model holding company act in December 2010, US states amended their insurance holding company laws to modify their group supervisory framework and provide regulators with new tools for evaluating enterprise risks within insurance groups. The amendments include several notable features, such as:

- expanding regulators' ability to investigate a parent or any affiliate within an insurance holding company system that could pose a reputational or financial risk to an insurer;
- requiring submission of a new annual Enterprise Risk Report (Form F) aimed at reducing potential risks faced by regulated insurance companies that may arise from issues at their non-regulated affiliates;
- enhancing regulators' rights to access information (including books and records) regarding parents and affiliates to better ascertain the financial condition of an insurer; and
- codifying regulators' ability to participate in supervisory colleges.

In addition, the NAIC adopted a model regulation regarding an insurer's own risk and solvency assessment (ORSA), which requires every US insurance and reinsurance company (or their holding company group) that exceeds certain annual written premium thresholds to complete a self-assessment of their risk management, stress tests and capital adequacy on a yearly basis, and the filing of a summary ORSA report. Many states are in the process of adopting the ORSA regulation. Further revisions to the model holding company act were adopted by the NAIC in 2014, which provide domiciliary regulators of internationally active insurance groups even greater authority over the holding company system of such groups, although only a handful of states have adopted these revisions to date.

The NAIC is also in the early stages of constructing a US group capital calculation using a risk-based capital aggregation methodology. Furthermore, as a result of the Dodd-Frank Act, insurance holding companies that own an insured bank or thrift company or have been designated as SIFIs by the FSOC are subject to the consolidated supervision of the Board of Governors of the Federal Reserve System, which, under Title I of the Dodd-Frank Act, includes establishing consolidated leverage and risk-based capital requirements and various liquidity requirements.

15 Reinsurance agreements

What are the regulatory requirements with respect to reinsurance agreements between insurance and reinsurance companies domiciled in your jurisdiction?

As discussed in question 14, states protect policyholders against insurer insolvency by requiring minimum financial reserves to pay losses. At the same time, insurance companies seek to decrease their risk and lessen the amount of reserves they must carry by reinsuring a portion of their liabilities.

Unlike primary insurance, states generally do not regulate the terms, rates or forms of reinsurance contracts. Rather, states regulate reinsurance by granting or withholding credit for reinsurance on the ceding company's statutory financial statements. Insurance companies may only 'credit' loss reserves by amounts transferred to reinsurers that meet certain conditions (see questions 17 and 18). Although states do not generally review and approve reinsurance agreements (unless the transaction is between affiliates or involves the transfer of a significant amount of business), in order to take credit for reinsurance ceded to another company, the agreement must contain certain minimum provisions (eg, insolvency provisions protecting insureds) (see question 45).

16 Ceded reinsurance and retention of risk

What requirements and restrictions govern the amount of ceded reinsurance and retention of risk by insurers?

Certain states restrict insurers from ceding 100 per cent of liabilities to a reinsurer, and require the ceding company to retain some portion of direct insurance liabilities. Fronting arrangements, whereby a licensed carrier issues a policy and cedes 100 per cent of the liabilities to an unlicensed company, have historically triggered heightened regulatory scrutiny in the US, as regulators may view the transaction as a way for the reinsurer to circumvent state licensing and solvency requirements. Although fronting arrangements are not prohibited per se, state regulators may take issue with a transaction where the ceding company retains no risk, particularly where the assuming company also services the underlying policies. Reinsuring a significant portion of an insurer's in-force business or line of business may also be subject to prior regulatory approval under 'bulk reinsurance' statutes.

17 Collateral

What are the collateral requirements for reinsurers in a reinsurance transaction?

Only when ceding to licensed or accredited reinsurers (see question 2) can the ceding company automatically (ie, without a requirement that the reinsurer post collateral) take statutory financial statement credit for liabilities ceded (see question 15). If the reinsurer is neither licensed nor accredited, the reinsurer must provide some form of collateral to allow a deduction from the liabilities carried on the reinsured company's statutory financial statements. Reinsurers that are not licensed or accredited may provide collateral directly to the ceding company, typically by establishing a trust or providing a letter of credit. Over the past few years, many states have adopted laws providing for reduced collateral requirements for 'certified reinsurers' (see question 18).

18 Credit for reinsurance

What are the regulatory requirements for cedents to obtain credit for reinsurance on their financial statements?

If the reinsurer is licensed or accredited in the US, the ceding company may take full credit for the reinsurance on its statutory financial statements. Until a few years ago, a reinsurer not licensed or accredited in the US was required to post collateral or provide letters of credit in an amount at least as great as the liabilities reinsured (often with a 2 per cent buffer) in order for the ceding company to obtain full credit for the reinsurance. Now, many states have adopted laws allowing certified reinsurers to post collateral in lesser amounts on a sliding scale (from zero to 100 per cent depending on the 'rating' assigned to the reinsurer) if they are from qualified jurisdictions and otherwise satisfy specified certification criteria.

Reduced collateral for reinsurance assumed by non-US reinsurers may also result from 'covered agreements' authorised by the Dodd-Frank Act. A covered agreement is defined in the Dodd-Frank Act as a written agreement regarding prudential measures with respect to the business of insurance or reinsurance that is entered into between the US and one or more foreign governments and relates to the recognition of prudential measures that achieves a level of protection for consumers that is substantially equivalent to the level of protection achieved under state insurance regulation. On 13 January 2017, the US and EU announced they had successfully concluded negotiations on a covered agreement and the agreed text was submitted to the appropriate committees of Congress, starting a 90-day review period required by the Dodd-Frank Act. The 90-day period has expired and it is not clear yet what position the new US administration will take on the agreement, and whether it will take the steps necessary to have the agreement enter into force from the US perspective. The agreement seeks, among other things, to impose equal treatment of US and EU-based reinsurers that meet certain financial strength and market conduct conditions. In the US, once fully implemented, the agreement requires US states to lift all reinsurance collateral requirements on qualifying EU-based reinsurers and provide them equal treatment with US reinsurers or be subject to federal pre-emption.

19 Insolvent and financially troubled companies

What laws govern insolvent or financially troubled insurance and reinsurance companies?

The laws of the state in which an insurance company is domiciled are the primary source of law applicable to insolvent or financially troubled insurance companies. If the state insurance commissioner determines, through review of a company's financial information, that the company is unable to pay its outstanding lawful obligations, or the admitted assets of the company are less than the aggregate amount of its liabilities, the commissioner may order the company to eliminate the impairment or discontinue the issuance of any new policies, or both, while the impairment exists. Depending on the severity of the impairment, the insurance commissioner may also seek an order to rehabilitate or liquidate the financially impaired insurance or reinsurance company. Typically, the insurance commissioner in the insurance company's domiciliary state serves as the receiver in any formal delinquency proceeding, subject to review by a supervising court. In addition, an insurance commissioner may revoke or suspend the licence of an insurance or reinsurance company deemed to be insolvent, regardless of whether it is domiciled in the state. States also have guarantee funds, capitalised through assessments on licensed insurers, to supplement payments to insureds in the event of the insolvency of an insurer.

20 Claim priority in insolvency

What is the priority of claims (insurance and otherwise) against an insurance or reinsurance company in an insolvency proceeding?

The priority of claims (insurance and otherwise) in an insolvency proceeding involving an insurance or reinsurance company is determined by the insurance laws in the insurance or reinsurance company's domiciliary state. The classes of claims are typically listed in the domiciliary state's insurance laws, with payment of administrative expenses of the estate paid first and payments to shareholders and other owners of the company paid last. Claims of policyholders for benefits under their insurance policies are generally ahead of claims of general creditors. As claims are paid, the highest priority of claims is paid first, and every claim in each successive class must be paid in full before members of the next lower priority class receive any payment. If there are not sufficient assets to pay a particular class in full, the creditors of that class will share in any distribution on a pro rata basis based upon the assets available and the total amount of claims in that class.

21 Intermediaries

What are the licensing requirements for intermediaries representing insurance and reinsurance companies?

All insurance intermediaries, including agents, brokers, claims adjusters, third-party administrators and reinsurance intermediaries, are subject to licensing requirements in any state in which they are transacting business. To obtain a licence, many states require agents to pass a minimum competency examination. Applicants for agents' and brokers' licences are screened for past criminal conduct. Sanctions, including licence suspensions and fines, are employed to punish fraud.

In January 2015, the National Association of Registered Agents and Brokers Reform Act (NARAB II) was enacted at the federal level to provide a mechanism through which licensing, continuing education and other non-resident insurance producer qualification requirements and conditions may be adopted and applied on a multi-state basis.

Insurance claims and coverage

22 Third-party actions

Can a third party bring a direct action against an insurer for coverage?

Only a few states allow a third party to bring a direct action against an insurer before a judgment has been entered against an insured. Louisiana, however, permits a direct action against liability insurers by injured persons (or their survivors or heirs) under a number of circumstances, including:

- when the insured is insolvent;
- of citation or other process cannot be made on the insured;
- the cause of action is for damages as a result of an offence between children and their parents or between married persons;
- the insurer is an uninsured motorist carrier; or
- the insured is deceased.

Many states, such as New York, allow a third-party claimant to bring a direct action against an insurer when a judgment against the insured is unsatisfied. New York by statute also allows direct actions in certain situations when an insurer denies coverage of a personal injury or wrongful death claim based on late notice, unless the insurer or the insured has commenced a declaratory judgment action within 60 days after the insurer's denial of coverage and named the injured person or other claimant as a party to the action. Minnesota, by statute, permits direct actions by the state of Minnesota against an insurer for coverage of environmental response costs related to mixed municipal solid waste disposal facilities that are caused by the insured and covered by the insurer's policy.

Case law in the US is split as to whether and when a settlement between the policyholder and insurer, pursuant to which the insurer has been released from liability under the policy, can bar a subsequent direct action against the insurer by a third-party claimant.

23 Late notice of claim

Can an insurer deny coverage based on late notice of claim without demonstrating prejudice?

Whether an insurer can deny coverage based on late notice without a showing of prejudice depends on the language of the policy, the jurisdiction and the type of insurance policy involved. Some states, such as New York in certain instances, require that policies issued in the state contain provisions dealing with whether and to what extent prejudice is required to defeat coverage based on late notice.

With respect to occurrence-based policies, the majority of states do not permit an insurer to deny coverage based on late notice unless the insurer has been prejudiced by the delay. New York, which used to be

known for its rule that late notice bars coverage regardless of prejudice, has now modified its common law rule as to certain types of liability policies issued or delivered in New York by amending section 3420 of the New York Insurance Law, effective 17 January 2009, to prohibit an insurer from denying coverage under certain circumstances owing to late notice absent prejudice to the insurer. The statute also shifts the burden of showing prejudice depending upon the tardiness of the notice.

Courts are much more likely to deny coverage for late notice regardless of prejudice under a 'claims-made-and-reported' policy, where notification of a claim within a certain period of time is an express part of the insuring agreement, rather than merely a contractual condition.

24 Wrongful denial of claim

Is an insurer subject to extra-contractual exposure for wrongful denial of a claim?

Most jurisdictions allow an insured to recover some form of extra-contractual damages if an insurer acts in bad faith in certain circumstances, such as when it wrongfully fails to settle a case within policy limits and that failure results in a judgment against the insured in excess of policy limits, or when it is found to have wrongfully denied a defence or indemnity, and thereby breached its duty of good faith and fair dealing. The standard of conduct as to what constitutes bad faith, however, varies from state to state, ranging from failure to act reasonably to gross disregard of an insured's interests to wilful misconduct. In some states, various unlawful claims handling practices are identified by statute, but a number of these statutes permit enforcement only by the state rather than by private action.

Certain states, such as Florida, permit a cause of action for bad faith if the insurer does not take affirmative action to settle a case within policy limits, even absent a settlement demand from the underlying claimant, when liability is clear enough and damages serious enough that an excess judgment is probable.

Depending on the jurisdiction, an insured may be able to recover punitive or consequential damages, or both, when the insurer has acted in bad faith. Some states, however, limit recovery of punitive damages to situations involving egregious conduct directed at the public at large.

25 Defence of claim

What triggers a liability insurer's duty to defend a claim?

Because the duty of an insurer to provide a defence is contractual, courts generally look to the wording of the insurance policy to determine whether and to what extent an insurer is obliged to defend a claim.

Where the policy imposes a duty to defend certain claims, a majority of jurisdictions determine the existence of a duty to defend a given claim based upon some form of the 'four corners' rule. Under this rule, an insurer's defence obligation is determined by comparing the allegations of the claimant's complaint to the policy provisions. If, accepting the complaint's allegations as true, there is even a single claim that would require the insurer to indemnify the insured in the event of a judgment, an insurer is usually obliged to defend the entire action, although in some jurisdictions the insurer may be able to allocate the defence costs to particular claims if the costs incurred are severable. There may also be a duty to defend against certain claims that, if true, would fall within an exclusion when the insured denies the allegations.

In some jurisdictions, courts will consider extrinsic evidence outside of the four corners of the complaint in determining whether the insurer has a duty to defend. In most of these cases, however, extrinsic evidence of actual facts has been used to impose the duty to defend rather than permit the insurer to defeat it.

26 Indemnity policies

For indemnity policies, what triggers the insurer's payment obligations?

Under an indemnity policy, an insurer's obligation to provide indemnification for defence costs and other loss is determined by a comparison of the scope of coverage afforded by the policy and the claim submitted for indemnity. If the claim falls within the coverage provided by the policy, the claim will be covered. A complaint may include both covered and uncovered claims, and only covered claims in a complaint are generally subject to indemnity.

27 Incontestability

Is there a period beyond which a life insurer cannot contest coverage based on misrepresentation in the application?

For life insurance, state statutes generally require a one or two-year contestability period beyond which a life insurer cannot contest coverage based on a misrepresentation in the application, although some jurisdictions permit contestation even after the general contestability period where the misstatement was made with intent to defraud. A contestability period allows an insurer a limited time in which to investigate statements made by the insured in its application to determine whether the statements were truthful. If the misrepresentation is discovered within the contestability period, the life insurer may deny coverage even if the fact misrepresented had nothing to do with the cause of the insured's death.

28 Punitive damages

Are punitive damages insurable?

Whether and to what extent punitive damages are insurable varies by jurisdiction. In some states, there is no public policy against insurance for punitive damages, and an insurance policy providing coverage for such damages will be enforced in accordance with its terms. Other states, however, have a public policy against insurability of punitive damages, at least when imposed to punish the wrongdoer. Not all 'punitive' damages, however, are imposed as punishment, and when they are imposed under a state law that views the damages as compensatory, they may be viewed as insurable, even in a jurisdiction that generally bars coverage for punitive damages. Similarly, punitive damages imposed on account of vicarious liability for the acts of another may be viewed as insurable even by a state that generally bars punitive damages coverage.

There are often significant choice-of-law questions when the public policy of the state in which a punitive damages judgment has been rendered differs from the public policy of the jurisdiction whose law governs the insurance policy. In such a situation, the decision may depend on the forum in which the public policy issue is determined. Some policies (especially certain directors' and officers' liability (D&O) policies) include a clause providing that insurability for punitive damages will be governed by the law of the jurisdiction that is the most favourable to the insured, so long as that jurisdiction has one of several specified relationships with the parties or the underlying claim against the insured. In some other policies, coverage disputes are resolved by arbitration, and the arbitrator is contractually directed to enforce coverage for punitive damages regardless of the law that might otherwise apply to the policy.

29 Excess insurer obligations

What is the obligation of an excess insurer to 'drop down and defend', and pay a claim, if the primary insurer is insolvent or its coverage is otherwise unavailable without full exhaustion of primary limits?

Whether an excess insurer is obliged to 'drop down' is generally a matter of contract. Courts usually look to the policy wording to determine whether and when an excess insurer is required to drop down.

There is a distinction between compelling an insurer to 'drop down' so that it assumes the obligations of an underlying insurer, and requiring the excess insurer to provide coverage when the insured, rather than the underlying insurer, has paid some or all of the amount of the underlying policy limit. In the latter situation – particularly if the excess policy merely requires exhaustion of the underlying insurer's limits, without expressly requiring that such exhaustion be through full payment of limits by the underlying insurer – some courts refuse to excuse the excess insurer from its obligations. Sometimes this is because the courts construe the term 'exhaustion' to include cessation of the underlying insurer's liability rather than full payment of its limits. Other times, courts rely on a public policy rationale, reasoning that the excess carrier would receive an unjustified windfall if it were permitted to avoid coverage when it has not been prejudiced. In addition, where failure of the underlying insurer to pay the full amount of its limits is because of a settlement between that insurer and the insured, some courts reason that to permit the excess insurer to avoid coverage because of the settlement would defeat the public policy in favour of settlement. Many

courts, however, will enforce the literal terms of an excess policy that require, as a condition of coverage, exhaustion of the underlying policy by full payment of limits by the underlying insurer.

30 Self-insurance default

What is an insurer's obligation if the policy provides that the insured has a self-insured retention or deductible and is insolvent and unable to pay it?

Whether an insurer remains obliged to pay under a contract of insurance when the insured is incapable of satisfying a self-insured retention (SIR) owing to its insolvency varies by jurisdiction. There are two general schools of thought. The public policy approach provides that an insurer is responsible for the amount of covered loss in excess of the SIR notwithstanding that the SIR has not been paid. The strict contract interpretation approach construes the insurance contract strictly and finds that an insurer's obligations under a policy with an SIR are not triggered until the insolvent insured has paid the SIR. Neither of these schools of thought requires an insurer to drop down and pay the SIR for the insured in the event of the insured's bankruptcy or insolvency.

Some states that follow the public policy approach have enacted legislation requiring liability policies to include a provision that the insured's bankruptcy will not relieve the insurer of its obligations under the policy. In those states, even if a policy expressly makes the payment of an SIR a condition precedent to coverage, the obligation of the insurer to pay covered amounts in excess of the SIR amount remains despite the insured's inability to satisfy the SIR. States that follow the strict contract interpretation approach rely on the law of contracts and treat payment of the SIR as a strict condition of coverage even if the insured is insolvent.

If the insured's policy contains a deductible amount that is included within the limits of a policy, rather than an SIR over which the policy limits apply, the inability of the insured to pay the deductible generally does not relieve the insurer from its obligation to pay covered claims and expenses. In general, the insurer would have the duty to pay without regard to the payment of the deductible by the insured and, in turn, would have to seek reimbursement for the amount of the deductible from the insured. In such cases, the insurer is generally considered a creditor of the insured with respect to the amount of the deductible paid on the insured's behalf.

31 Claim priority

What is the order of priority for payment when there are multiple claims under the same policy?

Certain types of policies contain provisions setting forth the priority of payments when there are multiple claims under the same policy or claims against multiple insureds. For example, D&O policies often include provisions indicating that the individual insured's claims should be paid first, before the insured organisation is paid. If not specified in the policy, jurisdictions look at different factors in determining priority of payment. Such factors include potential liability, excess exposure and ripeness for settlement.

Some courts have allowed an insurer, when faced with multiple claims against one insured, to exhaust its policy limits in settling one claim, even if that leaves another claim unsettled, where the settlement is reasonable. However, where there are multiple insureds under one policy, some jurisdictions have held insurers to be in violation of their duty of good faith if the settlement of one claim against one insured favours one insured over another. Many jurisdictions have not ruled on the specific issue of whether an insurer can enter into a settlement benefiting one insured to the detriment of others. In a number of instances, insurers facing uncertainty as to how a settlement on behalf of fewer than all insureds will be viewed have commenced interpleader actions, seeking a judicial determination of how the policy limits should be distributed.

32 Allocation of payment

How are payments allocated among multiple policies triggered by the same claim?

Case law concerning allocation of coverage for a claim that triggers multiple policies in various years is complex and conflicting. A number of different theories have evolved with respect to policies that contain standardised terms that do not deal specifically with the allocation issue. Many of these theories were developed in connection with asbestos insurance coverage cases, and then were subsequently used in pollution coverage cases, which many courts view as analogous.

While there are variations, the following theories are ones generally relied on by the courts:

- the 'exposure' theory: under this theory, the policies in effect at the time of the exposure to the hazardous substances are triggered. In personal injury product liability cases, the exposure period is the time during which the underlying claimant was exposed to the product. In pollution cases, the exposure period is the time during which hazardous substances were released or deposited at the site;
- the 'manifestation' theory: under this theory, the policies in effect at the time that the injury or damage becomes manifest provide coverage;
- the 'continuous trigger' or 'triple trigger' theory: under this theory, the injury or damage is viewed as a continuous injurious process, so that all policies from initial exposure through manifestation are triggered; and
- the 'injury in fact' theory: under this theory, a policy is triggered if injury in fact occurred during the policy period, even if the injury was, in and of itself, not compensable.

Where multiple years of coverage are involved, courts have split on:

- whether stacking of triggered policies is permitted;
- whether a triggered policy is responsible up to policy limits for all sums owed to the underlying claimant or merely a pro rata share of the liability;
- how and when excess coverage in a given year applies when fewer than all of the primary policies in triggered years have been exhausted; and
- whether and to what extent an insured must bear responsibility for uninsured periods that would otherwise be triggered had appropriate coverage been obtained.

33 Disgorgement or restitution

Are disgorgement or restitution claims insurable losses?

Courts disagree on whether and to what extent disgorgement or restitution claims are insurable. A decision of the United States Court of Appeals for the Seventh Circuit, which has been followed by a number of courts, held that a settlement of such claims was uninsurable as a matter of public policy, even though there had been no adjudication of wrongdoing. Other courts, however, have found that public policy does not bar coverage at least for defence and settlement of restitution or disgorgement claims, and that any public policy concerns are satisfactorily addressed by the standard conduct exclusion in insurance policies.

Because of the concern that uninsurability of disgorgement or restitution could deprive insureds of coverage for various US securities claims, thereby making D&O policies less marketable, many D&O policies now contain a provision whereby the insurer agrees not to contend that claims under sections 11 and 12 of the Securities Act of 1933 – and sometimes other securities laws provisions as well – are uninsurable.

34 Definition of occurrence

How do courts determine whether a single event resulting in multiple injuries or claims constitutes more than one occurrence under an insurance policy?

The manner in which the policy defines 'occurrence' can be determinative of whether a single event resulting in multiple injuries or claims will be considered one or multiple occurrences. In the absence of explicit policy language addressing the question, some courts have adopted a 'cause' test, while others have adopted an 'unfortunate event' test. Under the cause test, if there is a single cause of the injuries and claims, that cause will generally be viewed as constituting the occurrence. Under the unfortunate event test, however, which is applied in New York, each of the individual injuries or claims may be considered an unfortunate event that is itself a separate occurrence.

35 Rescission based on misstatements

Under what circumstances can misstatements in the application be the basis for rescission?

In order for an insurer to rescind a policy based on misstatements in the application, courts generally require, at a minimum, that there be a material misstatement in the application upon which the insurer relied in issuing the policy. In some states, an intent to defraud the insurer is also required. Ordinarily, a misrepresentation is considered material if the insurer would not, had it received accurate information, have provided the coverage at issue for the premium charged. It is ordinarily not required that the insurer show it would not have issued any policy at all.

Fidelity insurance applications, however, are often treated differently for rescission purposes than other types of coverage. This is because one of the purposes of fidelity insurance is to provide coverage for employee thefts or other losses caused by employee dishonesty that took place prior to the issuance of the policy but are discovered during the policy period. If the dishonest employee's knowledge were imputed to the insured, the purpose of the coverage would be defeated. Thus, a failure to disclose in the application thefts known only to the dishonest employee or employees will generally not be considered a misrepresentation in the application. If, however, the dishonest employee is the person who actually signs the application, some courts will permit rescission, although other courts will not.

Reinsurance disputes and arbitration

36 Reinsurance disputes

Are formal reinsurance disputes common, or do insurers and reinsurers tend to prefer business solutions for their disputes without formal proceedings?

While cedents and reinsurers usually attempt to resolve their disputes before commencing arbitration or litigation, the relationship between cedents and reinsurers has grown increasingly contentious since the 1980s, resulting in more formal proceedings.

Arbitration is generally the preferred mechanism to resolve such disputes, and many reinsurance contracts contain arbitration clauses. Arbitration provides the advantage of resolution by a panel of industry professionals, is often viewed as more cost-effective and efficient than litigation, and generally entails a level of confidentiality not always available through court proceedings. The Federal Arbitration Act (FAA) and case law interpreting it generally govern the procedural aspects of most reinsurance disputes arbitrated in the US to the extent not otherwise provided by the contract.

Although some reinsurance contracts contain choice-of-law provisions that govern substantive issues, arbitration clauses often relieve the arbitrators from following strict rules of law and provide that their decisions should be made with regard to the customs and practices of the reinsurance industry.

Notwithstanding the popularity of arbitration clauses for reinsurance disputes, many reinsurance disputes continue to be litigated, often in New York federal or state courts. When parties choose to resolve their dispute through litigation, courts tend to rely more heavily upon the language of the policy and less on industry custom and practice.

37 Common dispute issues

What are the most common issues that arise in reinsurance disputes?

Issues that commonly arise in reinsurance disputes include:

- liability of the reinsurer for defence costs in addition to the limit of liability stated in the reinsurance certificate;
- liability of the reinsurer for declaratory judgment action expenses incurred by the cedent in coverage litigation;
- whether and to what extent a reinsurer is bound by the methodology used by the cedent to allocate payments to particular years of coverage;
- whether arbitrators or courts should decide arbitrability, consolidation, joinder and collateral estoppel issues;
- the scope of a cedent's duty of utmost good faith with respect to disclosure of risks, handling of claims, timely notice, settlements and allocation issues;
- the right of a party to a reinsurance agreement to offset amounts owed under that agreement based on amounts allegedly owed under a different agreement with the same counterparty;
- whether reinsurance proceeds owed to an insolvent reinsured constitute a general asset of the reinsured's insolvent estate or should be used for the benefit of the underlying claimant; and
- whether and to what extent the McCarran-Ferguson Act, which generally leaves insurance regulation to the states, precludes preemption by the FAA of state insurance laws that relate to arbitration.

38 Arbitration awards

Do reinsurance arbitration awards typically include the reasoning for the decision?

Arbitrators do not typically issue reasoned awards unless the reinsurance contract at issue requires them to do so or they agree, at the parties' request, to do so. Reasons for this approach include confidentiality and finality. There is, however, an industry-wide debate as to whether arbitrators should issue reasoned awards more frequently.

39 Power of arbitrators

What powers do reinsurance arbitrators have over non-parties to the arbitration agreement?

Because arbitration is a creature of contract, non-parties to an arbitration agreement generally cannot be joined as parties to an arbitration without their consent as well as the consent of the other parties to the arbitration. If the non-party is an alter ego of one of the contracting parties, however, it may be joined on the theory that it is the same entity as the one that signed the arbitration agreement.

Section 7 of the FAA provides arbitrators with the authority to compel non-parties to appear before them at a hearing to produce documents and provide testimony, but courts have split on whether and under what circumstances this provision authorises pre-hearing discovery, as opposed to production of documents or testimony at the arbitration hearing; whether 'hearing' can be defined to include non-substantive preliminary hearings held for discovery purposes; and whether a distinction should be drawn between the authority of an arbitrator to order production of documents, as opposed to testimony, from a non-party during the discovery phase of the arbitration.

While some courts have found that section 7 of the FAA empowers arbitrators to obtain discovery from non-parties anywhere in the United States, most have held that the jurisdictional reach of an arbitrator's subpoena power pursuant to section 7 of the FAA is limited to 100 miles, just as the reach of a district court subpoena is limited to 100 miles from where the court sits.

40 Appeal of arbitration awards

Can parties to reinsurance arbitrations seek to vacate, modify or confirm arbitration awards through the judicial system? What level of deference does the judiciary give to arbitral awards?

The primary authority for confirmation of an award is provided by section 9 of the FAA, which permits the contracting parties to agree that a court can issue judgment confirming the award. The courts have also held that even if the contract does not expressly provide for confirmation by a court, section 9 of the FAA authorises a court to confirm an arbitration award as long as the contract provides for 'final and binding' arbitration.

Section 11 of the FAA permits the court to modify an award, but only if:

- there is evidence of a material miscalculation of figures or a material mistake in a description of a person, thing, or property referred to in the award;
- the arbitrators have awarded on a matter not submitted to them (unless the matter does not affect the merits); or
- there is an error in the form of the award not affecting the merits.

Under section 10(a) of the FAA, an award can be vacated only if:

- it was procured by corruption, fraud or undue means;
- there was evident partiality or corruption on the part of the arbitrators;

- the arbitrators were guilty of misconduct in refusing to postpone a hearing on sufficient cause shown, refusing to hear pertinent and material evidence, or engaging in other misbehaviour by which the rights of a party were prejudiced; or
- the arbitrators exceeded their powers or so imperfectly executed them that a mutual, final and definite award on the subject matter was not made.

Traditionally, an additional basis for vacating an award has been if the arbitrator's award was in 'manifest disregard of the law'. The continuing viability of that doctrine, however, was called into question by the US Supreme Court decision in *Hall Street v Mattel*, 552 US 576 (2008). Subsequent to *Hall*, some courts have declined to apply the doctrine or have cast serious doubt on its continuing validity, while other courts have continued to apply the doctrine, either as an independent basis for vacatur of an award or as a judicial gloss on the statutory ground concerning instances of the arbitrators exceeding their powers. In *Stolt-Nielsen SA v AnimalFeeeds International*, 559 US 662 (2010), the US Supreme Court, in the course of vacating an award under section 10(a) of the FAA because the arbitrators exceeded their powers, again refused to rule on the viability of the manifest disregard of the law doctrine, but noted that that doctrine also would have required vacatur.

Reinsurance principles and practices

41 Obligation to follow cedent

Does a reinsurer have an obligation to follow its cedent's underwriting fortunes and claims payments or settlements in the absence of an express contractual provision? Where such an obligation exists, what is the scope of the obligation, and what defences are available to a reinsurer?

Courts are split as to whether a reinsurer is bound to follow its cedent's underwriting fortunes and claims payments or settlements absent an express contractual provision requiring it to do so. Requiring a reinsurer to follow its cedent is generally known as the 'follow-the-fortunes' doctrine. Some courts use this term interchangeably with the 'follow-the-settlements' doctrine.

Early case law on the issue suggested that courts were not willing to read follow-the-fortunes language into reinsurance contracts that did not expressly contain the provision. More recent case law, however, suggests a greater tendency to apply the doctrine to all contracts of reinsurance, often by finding that the follow-the-fortunes doctrine exists as a matter of industry custom and practice regardless of whether the provision is expressly contained in the reinsurance agreement.

When the follow-the-fortunes doctrine applies, either through an express provision or otherwise, it imposes on a reinsurer an obligation to indemnify a cedent for a claim payment reasonably or arguably within the terms of the cedent's policy with its insured, even if not technically covered by that policy, provided that the payment is not fraudulent, collusive, in bad faith, or outside the terms, conditions and limits of the reinsurance contract at issue.

The United States Court of Appeals for the Second Circuit, in *Global Reinsurance Corp of Am v Century Indem Co*, 843 F3d 120 (Second Circuit 2016), certified question accepted, 28 NY3d 1129, 68 NE3d 98 (2017), recently certified to the New York Court of Appeals the question of whether, under New York law, there is 'either a rule of construction, or a strong presumption, that a per occurrence liability cap in a reinsurance contract limits the total reinsurance available under the contract to the amount of the cap regardless of whether the underlying policy is understood to cover expenses such as, for instance, defense costs.'

42 Good faith

Is a duty of utmost good faith implied in reinsurance agreements? If so, please describe that duty in comparison to the duty of good faith applicable to other commercial agreements.

The relationship between the insurer and the reinsurer has been characterised as one of utmost good faith (sometimes referred to as 'uberrima fides'). Traditionally, the duty of utmost good faith has run from the cedent to the reinsurer. Some jurisdictions, however, now treat the duty as reciprocal. Claims of breach of the duty of utmost good faith can be made with respect to any element of the relationship between the cedent and the reinsurer, including the cedent's disclosure of the risks, handling of underlying claims, allocation decisions and the timing of notices to reinsurers.

Courts are divided on the standard to be applied to this duty, with some defining it as a fiduciary duty, some as a quasi-fiduciary duty and some as no more than the duty of good faith implied in all commercial agreements. At least with respect to the duty of disclosure of relevant facts to a treaty reinsurer prior to inception of the contract, courts have generally recognised an elevated duty of good faith beyond that applicable to most commercial agreements because the reinsurer is not able to select which risks it will accept, but instead automatically assumes the risks underwritten by the reinsured that are covered by the treaty.

43 Facultative reinsurance and treaty reinsurance

Is there a different set of laws for facultative reinsurance and treaty reinsurance?

Treaty reinsurance agreements are contracts between the cedent and reinsurer whereby the reinsurer agrees to accept the reinsurance risk as to an entire class or classes of the cedent's insurance policies. Facultative reinsurance, on the other hand, is reinsurance of part or all of a specific insurance policy.

Generally, the same body of law is applicable to facultative and treaty reinsurance, although, as noted above, the duty of utmost good faith tends to be more stringently applied against a cedent in the treaty context because the reinsurer has less ability to make its own examination of the risks in the treaty context than in the facultative reinsurance context. Additionally, several courts have found that where a facultative reinsurance contract contains a 'follow-the-form' provision, a presumption of concurrency exists between the terms of that reinsurance contract and the reinsured policy, subject only to any clear limitation to the contrary in the facultative certificates themselves. In such a situation, the facultative reinsurer may be bound by the terms of the underlying policy to the extent the language of the facultative certificate is not different.

44 Third-party action

Can a policyholder or non-signatory to a reinsurance agreement bring a direct action against a reinsurer for coverage?

Because of the lack of privity of contract, policyholders and other non-parties to a reinsurance contract generally cannot assert a direct action against a reinsurer absent an express provision in the reinsurance contract allowing them to do so. Such a provision is customarily referred to as a 'cut-through' clause. Some courts, however, have carved out a very limited fact-based exception to this rule to permit a policyholder or other non-signatory to have direct access to reinsurance coverage if it can prove that a business relationship exists between it and the reinsurer such that it should be accorded the status of a third-party beneficiary of the reinsurance contract. Moreover, some courts have also held that when a reinsurer agrees to assume the policies of the reinsured and exercises actual control of claims, the reinsurer may become directly liable to the insureds for whatever the reinsured is liable to pay.

45 Insolvent insurer

What is the obligation of a reinsurer to pay a policyholder's claim where the insurer is insolvent and cannot pay?

Most states have statutes prohibiting ceding insurers from receiving statutory financial statement credit for liabilities ceded unless their reinsurance contracts contain 'insolvency clauses'. These clauses require a reinsurer to pay the liquidator of an insolvent ceding insurer amounts on reinsurance claims regardless of whether the insolvent insurer has actually paid its insured for the underlying insurance claims. Since ceding insurers almost always wish to obtain that credit, insolvency clauses are generally included in reinsurance agreements so that, as a practical matter, reinsurers must pay otherwise valid claims under their contracts even when the cedent is insolvent and has not fulfilled its own payment obligations. The statutes requiring an insolvency clause in order to receive credit for reinsurance were enacted largely as a reaction to the US Supreme Court decision in *Fidelity & Deposit Co v*

Pink, 302 US 224 (1937), which found that a reinsurer was not required to reimburse the liquidator of an insolvent ceding company for losses not actually paid by that insurer. This holding remains valid if there is no insolvency clause in the reinsurance agreement, the language of the reinsurance agreement requires actual payment by the cedent in order to trigger the reinsurer's liability and state law does not forbid the result.

46 Notice and information

What type of notice and information must a cedent typically provide its reinsurer with respect to an underlying claim? If the cedent fails to provide timely or sufficient notice, what remedies are available to a reinsurer and how does the language of a reinsurance contract affect the availability of such remedies?

Many reinsurance contracts contain provisions that specify the type of notice and information that the cedent must provide to its reinsurer, as well as when such notice must be provided. A cedent is generally expected to provide a reinsurer with sufficient information to reserve properly, adjust premiums to reflect loss experience under the reinsurance contract and decide whether to exercise the option of associating with the reinsured in handling an underlying claim, to the extent the contract allows the reinsurer to do so.

Under US case law, the timeliness of a cedent's notice to its reinsurer is judged under an objective standard and generally must be reasonable in light of the facts of the specific claim. The majority view is that late notice defeats reinsurance coverage only if the reinsurer has been prejudiced by the delay, the cedent was grossly negligent or the cedent acted in bad faith.

47 Allocation of underlying claim payments or settlements

Where an underlying loss or claim provides for payment under multiple underlying reinsured policies, how does the reinsured allocate its claims or settlement payments among those policies? Do the reinsured's allocations to the underlying policies have to be mirrored in its allocations to the applicable reinsurance agreements?

There are a variety of different methodologies that may be employed when allocating loss payments to the policies triggered by an underlying lawsuit, depending on the facts surrounding a particular claim and the language of the policies involved. Courts have generally required deference by the reinsurer to the cedent's allocation-related decisions. Thus, a reinsurer is ordinarily precluded from avoiding payment so long as the cedent's allocation decisions were reasonable and in good faith, and the allocation is within the terms and conditions of the underlying policy or policies and reinsurance contract or contracts. New York's highest court has ruled that the cedent's allocation must be one that it would have, or reasonably could have, adopted if it had no reinsurance coverage.

48 Review

What type of review does the governing law afford reinsurers with respect to a cedent's claims handling, and settlement and allocation decisions?

The follow-the-fortunes and follow-the-settlements doctrines generally prevent a reinsurer from second-guessing the claims, settlement and allocation-related decisions of its cedent, so long as the liability is reasonably within the scope of the reinsurance, and the reinsured's decisions were reasonable, made in good faith and would have, or reasonably could have, been adopted by the reinsured even if it had no reinsurance coverage.

49 Reimbursement of commutation payments

What type of obligation does a reinsurer have to reimburse a cedent for commutation payments made to the cedent's policyholders? Must a reinsurer indemnify its cedent for 'incurred but not reported' claims?

US case law does not specifically address a reinsurer's obligation to follow a cedent's commutation-related payment. However, as a commutation is a form of settlement, a reinsurer's obligation to reimburse a cedent for a commutation payment is likely to be subject to the same standard as other settlements under the 'follow-the-fortunes' and 'follow-the-settlements' doctrines, so long as there have been sufficient claims under the policy to justify the commutation payment amount. For example, if there are claims valued at US$3 million and the cedent's policy with its insured is only for US$1 million, the follow-the-fortunes and follow-the-settlements standards are likely to apply even if coverage of the claims under the cedent's policy has been hotly contested.

Whether the follow-the-fortunes and follow-the-settlements doctrines extend to incurred but not reported (IBNR) claims, as opposed to actual claims payments, has also not specifically been addressed by US courts. The New Jersey Supreme Court, however, has held, in the context of a cedent's insolvency, that IBNR claims could not share in the distribution of the assets of the estate because they were not 'absolute' as of the liquidator's claim bar date. In so holding, the Court noted that its decision was important to reinsurers, who otherwise faced the prospect of having to pay an enormous amount of money for claims that had not yet been brought. Depending upon the language of the reinsurance agreement, a court could similarly refuse to bind the reinsurer to coverage of a reinsured's commutation of a policy with the original insured to the extent such commutation was based upon the mere possibility of claims being brought in the future.

50 Extra-contractual obligations (ECOs)

What is the obligation of a reinsurer to reimburse a cedent for ECOs?

Generally, a reinsurer is required to indemnify a cedent only to the extent that the cedent's payments or losses are reasonably or arguably within the scope of the cedent's underlying insurance policy. A

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reinsurer will not be held liable for losses arising from the cedent's bad faith unless the reinsurance contract is interpreted as covering that exposure. Moreover, some states, as a matter of public policy, preclude coverage for punitive damages, regardless of the language of the contract.

Where, however, the reinsurer has actively participated in the alleged bad faith conduct through its association in the defence or settlement of the claim, some courts have found that the reinsurer has taken the role of a 'co-insurer' and is therefore also liable for losses caused by the bad faith conduct regardless of its policy limits.

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