

XV AIDA WORLD CONGRESS 2018

AIDA WORKING PARTY – STATE SUPERVISION OF
INSURANCE

Saturday, 13 October 2018



"Regulatory challenges for cross border (re-) insurance business"

- Speaker: **Yves Hayaux-du-Tilly**, Mexico
"New criteria and regulatory risks to foreign reinsurers taking reinsurance risk from Mexican cedents"
- Speaker: **Ray Giblett**, Sydney
"The non-admitted (re-)insurance business from the Australian perspective"
- Speaker: **Giuliana Liasch**, São Paulo
"Regulatory challenges for insurance business in Brazil"
- Speaker: **Shivaun Moreno and Daniel Curi**, Hannover
"Regulatory rules in Brazil for Reinsurance"
- Speaker: **Daniel Alejandro Russo**, Buenos Aires
"Argentina reinsurance market: access issues"
- Speaker: **Yannis Samothrakis**, Paris
"Conducting (re-)insurance business cross border within the European Economic Area (EEA)"
- Speaker: **Gunne W. Bähr**, Cologne
"Compliance risks arising from cross border (re-)insurance business in Europe and ROW "

New criteria and regulatory risks to foreign reinsurers taking reinsurance risk from Mexican cedents

Yves Hayaux du Tilly

State Supervision Working Party Meeting

AIDA World Congress, Rio de Janeiro, 13 October 2018

- Mexican cedents may only cede risk to (and take risk from) foreign reinsurance companies registered with the National Registry of Foreign Reinsurance Companies ("**Reinsurance Registry**").
- The Reinsurance Registry only admits foreign reinsurance companies duly incorporated and licensed as reinsurance companies with minimum financial ratings from international rating agencies as set forth by the National Insurance and Bonding Commission ("**CNSF**").
- This regulatory framework of "mixed supervision" is broadly used in LatAm.

- For the first time, the CNSF cancelled the registration of a foreign reinsurer for “non-economic reasons”.
- The cancellation is the consequence of a reinsurance agreement that was entered into by the foreign reinsurance company with a Mexican cedent that in the opinion of the CNSF was entered in breach of Mexican laws.
- After following regulatory proceedings against the Mexican cedant for entering into the reinsurance agreement in which the Mexican cedant admitted liability, the CNSF initiated proceedings against the foreign reinsurer, eventually cancelling its registration with the RGRE.

- Obligations of foreign reinsurance companies was deemed to be limited to maintaining its registration with the Reinsurance Registry, as well as supervision from CNSF.
- What would be the “other” obligations of foreign reinsurance companies when entering into reinsurance agreements with Mexican cedants?
- Are foreign reinsurance companies required to undertake their own independent examination on compliance with Mexican law?
- What are the risks for relying on the assurances of Mexican cedants or not undertaking your own examination?

- Foreign reinsurance companies are now being deemed to be (jointly) liable for breaches of Mexican cedants to their obligations under Mexican law.
- Foreign reinsurance companies are expected to confirm independently that the reinsurance agreements they enter into with Mexican cedants comply with local regulations applicable to Mexican cedants.
- This criteria departs from the principle that Mexican cedants are those that are regulated in Mexico, expanding the scope of regulation to include foreign reinsurance companies by making them liable for breaches of Mexican cedants to their obligations under Mexican laws and applicable regulation.

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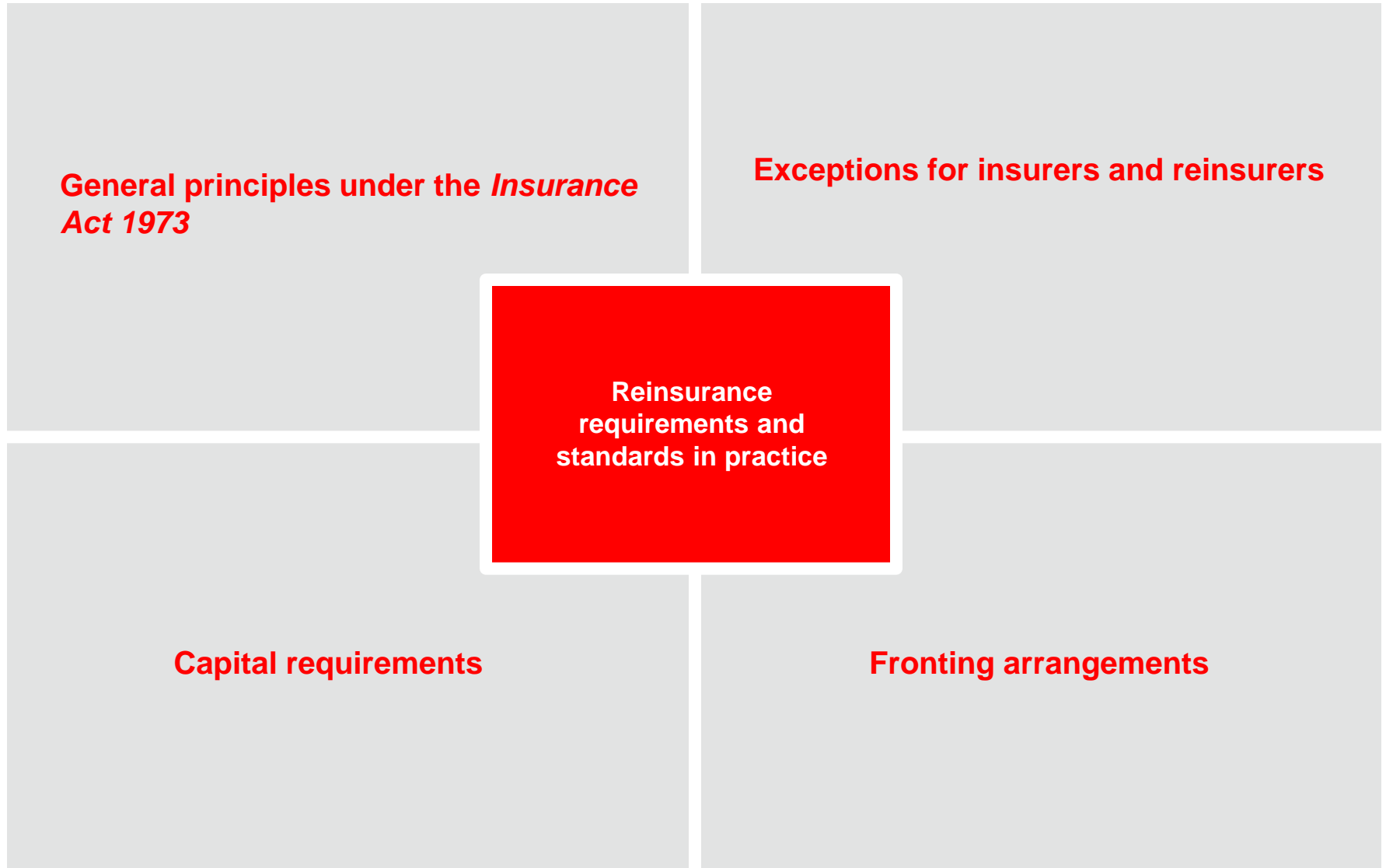
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The non-admitted (re)insurance business from the Australian perspective

Presented by Ray Giblett, Partner, Norton Rose Fulbright



Topics



What is insurance business?



insurance business means the business of undertaking liability, by way of insurance (including reinsurance), in respect of any loss or damage, including liability to pay damages or compensation, contingent upon the happening of a specified event, and includes any business incidental to insurance business as so defined...



Non-admitted foreign (re)insurers in Australia

General rule: All (re)insurers (local or foreign) must be authorised by the *Australian Prudential Regulation Authority* to carry on (re)insurance business in Australia – sections 9 and 10 of the *Insurance Act 1973*

Insurance Act 1973 – section 9: Persons other than bodies corporate and Lloyd's underwriters carrying on insurance business

- (1) A person commits an offence if:
- (a) the person carries on insurance business in Australia; and
 - (b) the person is not a body corporate or a Lloyd's underwriter; and
 - (c) there is no determination in force under subsection 7(1) that this subsection does not apply to the person (the effect of which is to allow the person to carry on insurance business without being authorised under the Act to do so).

Insurance Act 1973 – section 10: Bodies corporate and Lloyd's underwriters carrying on insurance business

- (1) A body corporate (other than a Lloyd's underwriter) commits an offence if:
- (a) the body corporate carries on insurance business in Australia; and
 - (b) the body corporate is not a general insurer; and
 - (c) there is no determination in force under subsection 7(1) that this subsection does not apply to the body corporate (the effect of which is to exempt the body corporate from being authorised under the Act to carry on insurance business).



Non-admitted foreign reinsurers in Australia

Exceptions for reinsurers – exceptions to ‘carrying on’ insurance business under the Insurance Act 1973

Insurance Act 1973 – section 3 was amended on 1 July 2008 to include incidental business with reinsurance exemptions inserted on 27 July 2010

(5) Without limiting the scope of what is incidental to insurance business for the purposes of the definition of insurance business in subsection (1), a business of a person is taken, for the purposes of that definition, to be a business incidental to insurance business to the extent that it involves one or more of the following kinds of acts:

- (a) inducing others to enter into contracts of insurance with the person as the insurer;
- (b) publishing or distributing a statement relating to the person's willingness to enter into a contract of insurance as an insurer;
- (c) procuring the publication or distribution of such a statement.

(5A) Subsection (5) does not apply if the contracts of insurance referred to in that subsection are contracts of reinsurance. (emphasis added)

(6) Without limiting the circumstances in which a person is taken, for the purposes of this Act, to carry on insurance business in Australia, a person is taken to carry on insurance business in Australia if:

- (a) the person carries on a business outside Australia that, under this Act, would constitute insurance as if it were carried on in Australia; and
- (b) another person in Australia acts:
 - (i) directly or indirectly on behalf of the first-mentioned person; or
 - (ii) as a broker of insurance provided by the first-mentioned person, or directly or indirectly on behalf of such a broker; in relation to the business carried on outside Australia.

(6A) Subsection (6) does not apply if the business referred to in paragraph (a) of that subsection is solely a business of reinsurance. (emphasis added)



Non-admitted foreign (re)insurers in Australia

Exceptions for (re)insurers – certain insurance contracts that are not insurance business

• *Insurance Act 1973* section 3A and *Insurance Regulations 2002* Part 2 – certain insurance contracts are not insurance business



Atypical risks



Risks that cannot be reasonably placed in Australia



Reinsurance contracts required under laws of foreign country



High value insured
 - \$200 million revenue
 - value of gross assets is at least \$200 million
 - number of employees is at least 500

• Lloyd's underwriters – exempt from 'carrying on' provisions of *Insurance Act 1973* section 9

• Can establish local operations in Australia by way of subsidiary or branch – subject to the same requirements as local insurers

Capital requirements

Capital requirements for reinsurers

General rule: all reinsurers (including foreign branches) are required to maintain assets in Australia at least equal to its total sum liabilities in Australia.



Two sources: **legislation** and **prudential standards**

1. *Insurance Act 1973* – Section 28: General insurer must hold sufficient assets (note: for the purposes of this section of the Act, no distinction is made between general insurers and reinsurers).

A general insurer commits an offence if:

- (a) it does not hold assets in Australia (excluding goodwill and any assets or other amount excluded by the prudential standards for the purposes of this section) of a value that is equal to or greater than the total amount of its liabilities in Australia other than pre-authorisation liabilities; and
- (b) APRA has not authorised the insurer to hold assets of a lesser value; and
- (c) there is no determination in force under subsection 7(1) determining that this subsection does not apply to the insurer.

2. Prudential Standards (APRA) – more stringent requirements

•GPS 110 requires regulated insurers to hold sufficient capital to meet the Prudential Capital Requirement above the standard set in the *Insurance Act 1973*.

•GPS 112 requires insurers to hold at least 80% of the prescribed capital amount as 'Tier 1 Capital', which must satisfy the following essential characteristics:

- provide a permanent and unrestricted commitment of funds;
- are freely available to absorb losses;
- do not impose any unavoidable servicing charge against earnings; and
- rank behind the claims of policyholders and other more senior creditors in the event of winding up of the issuer; and
- provide for fully discretionary capital distributions.

•GPS 120 sets requirements for insurers holding assets in Australia for the purpose of satisfying the requirement that an insurer maintain assets of an equal or greater value than the insurer's liabilities in Australia.

Other barriers for foreign reinsurers / fronting

Risk from prudential supervision standpoint GPS 114 (Capital Adequacy – Asset Risk Charge)

- Asset Risk Charge in relation to default stresses applicable to reinsurance recoverables
- Increased risk charge where reinsurance arrangement is with a non-APRA regulated insurer

Increased risk charge can be mitigated by:



Letter of Credit



Collateral



Guarantee

Counterparty grade	Default factor (%) if APRA authorised reinsurer	Default factor (%) if non APRA authorised insurer
1 (government)	0	2
1 (other)	2	2
2	2	4
3	4	6
4	6	8
5	8	12
6	12	20
7	20	20

Any questions?





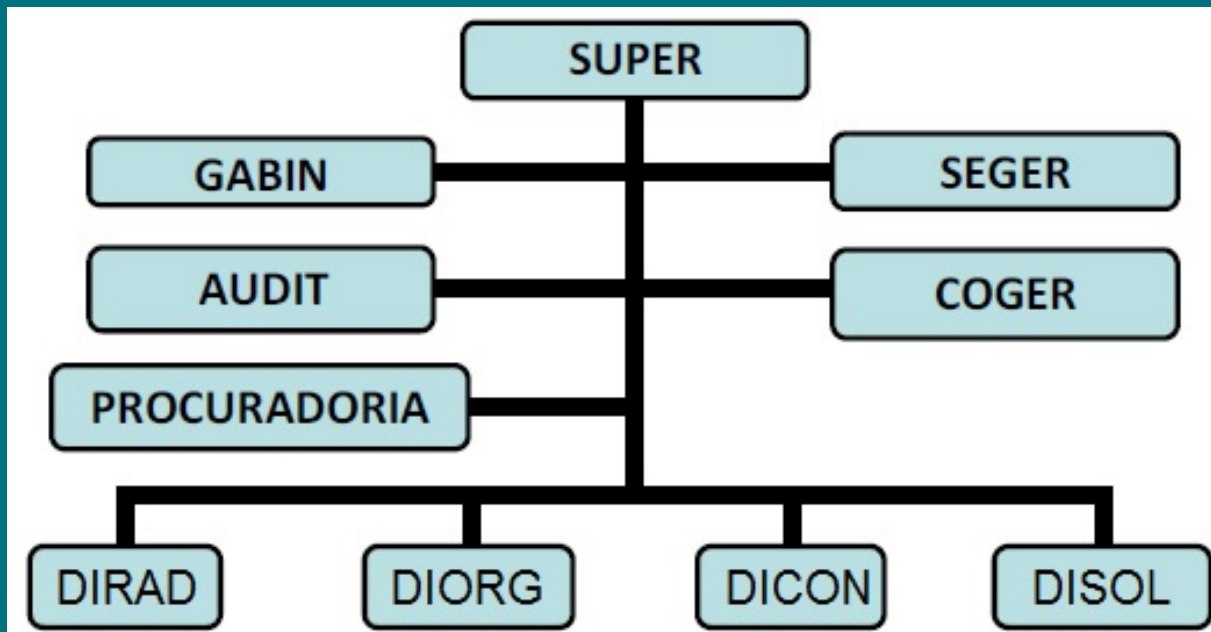
Regulatory challenges for insurance business in Brazil



SUSEP

**Our local regulator with 3 representative offices:
São Paulo; Brasília and Rio Grande do Sul.**

Organization:





- SUSEP's attributions
- SUSEP's restrictions



Examples:

- ▷ Cancel specific product
- ▷ Remove technical clause
- ▷ Reject special changes



Thank you



somewhat
different

Regulatory Rules in Brazil for Reinsurance

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History

- ▶ Instituto de Resseguros do Brasil (IRB) was the local monopolist for about 60 years
- ▶ Lei Complementar Nº 126 of 15 January 2007 terminates the monopoly and establishes the framework for the reinsurance industry
- ▶ Resolução CNSP (National Council of Private Insurance) 168/2007 defines the different classes of reinsurers and stipulates a set of obligatory clauses for reinsurance agreements

Regulatory Rules

Right of First Refusal

Resolução CNSP 168/2007:

- ▶ 3 classes of reinsurers
 - local, seated in Brazil
 - admitted, non-resident but with representative office in Brazil
 - eventual, registered with SUSEP (Superintendence of Private Insurance) and without local presence

- ▶ “Dº de Recusa”: ceding companies have to make a preferential offer to local reinsurers of min. 40% of total of ceded premium per risk (fac and obl) (Art. 15)

Regulatory Rules

Intra Group Cessions

- ▶ Before: prohibition of transfer of risk from local companies (primary and reinsurers) to foreign companies belonging to the same financial group
- ▶ Resolução CSNP 232/2011:
transfer of risk allowed up to a limit of 20% of the premium corresponding to each coverage

Regulatory Rules

Opening of the Market

► Resolução CNSP 353/2017

(which altered partially Res. CNSP168/2007):

- Kept the preferential offer for local reinsurers of 40%
- Each and every treaty or facultative
- Demands equal treatment on the offer
- Revoked the risk transfer limitation between affiliated companies or same financial conglomerate



Obligatory Clauses for Reinsurance

Resolução CNSP 168/2007

▶ Art. 34 Cut through:

- in principle reinsurers do not respond to the insured directly
- exception: insolvency of the company
 - obligatory business: the contract must contain a CTC
 - facultative business: cut through applies automatically

▶ Art. 35 Intermediary:

- to define whether or not Intermediary is authorized to receive payments
- if so, reinsurer has to bear the intermediary's solvency risk i.e. clause has to establish that payments by the reinsurer to the intermediary only have a redemptive effect when actually received by the cedant
- not to include clauses limiting the direct relationship between cedants and reinsurers

Obligatory Clauses for Reinsurance

Resolução CNSP 168/2007

- ▶ Art. 33 Insolvency: the responsibilities of the reinsurer subsist in case of insolvency of the cedant
- ▶ Art. 38: Law and Jurisdiction Brazil; free election of procedural rules for arbitration
- ▶ Art. 40: exact date and time of commencement and end of contract period; termination criteria and their consequences; exclusions

Duties for Reinsurers

Resolução CNSP 168/2007

- ▶ Art. 37: Contract formalization up to 270 days from the beginning of the term
 - SUSEP Circular 524/2016: clarifying criteria
 - clear identification of the reinsurer: date and full name
 - physical or electronic form
 - acceptance by broker and cover note do not substitute express acceptance of the cedant nor the reinsurance contract

- ▶ Art. 41: duty to communicate lawsuits / arbitrations related to rejected claims to SUSEP (Superintendence of Private Insurance)

Perguntas? Duvidas?

Obrigados pela sua atenção!



Argentina reinsurance market: access issues.

Agenda

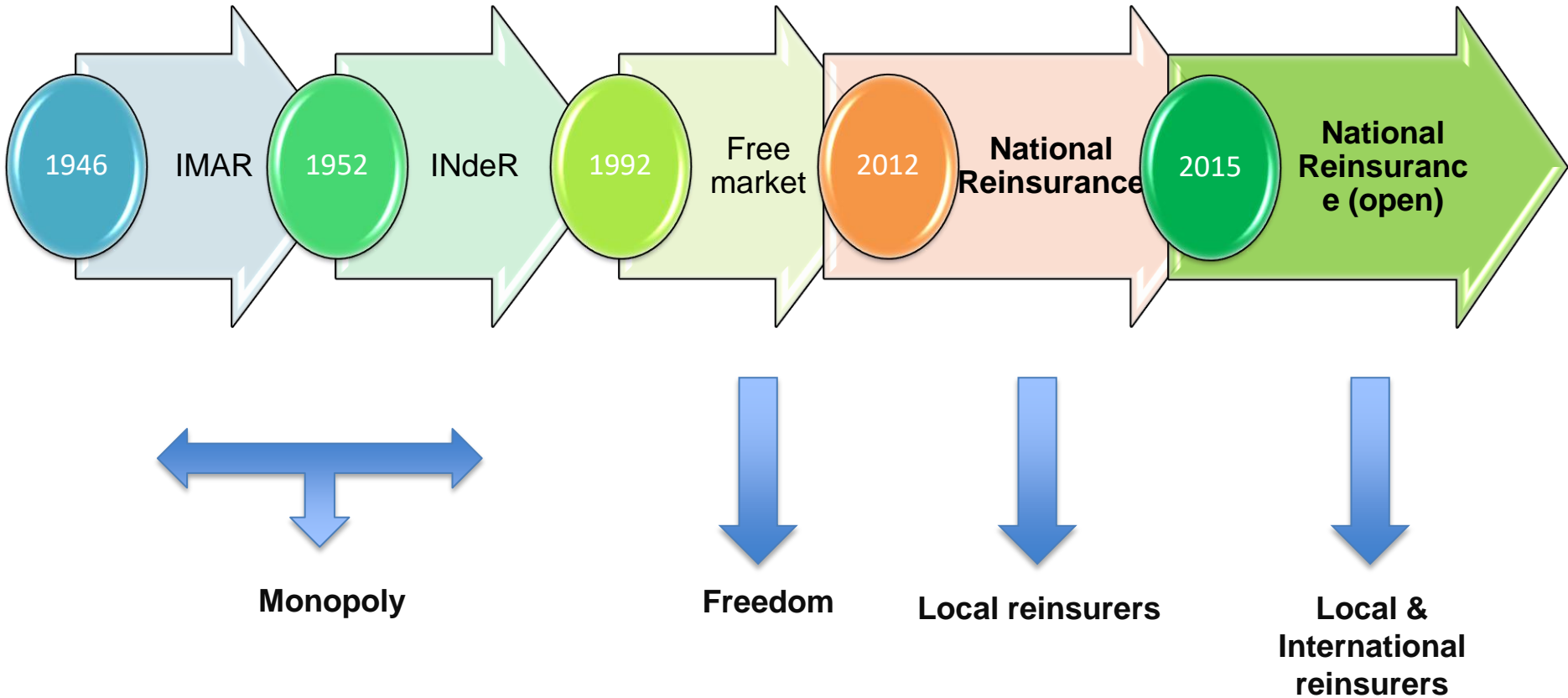


Historical
issues

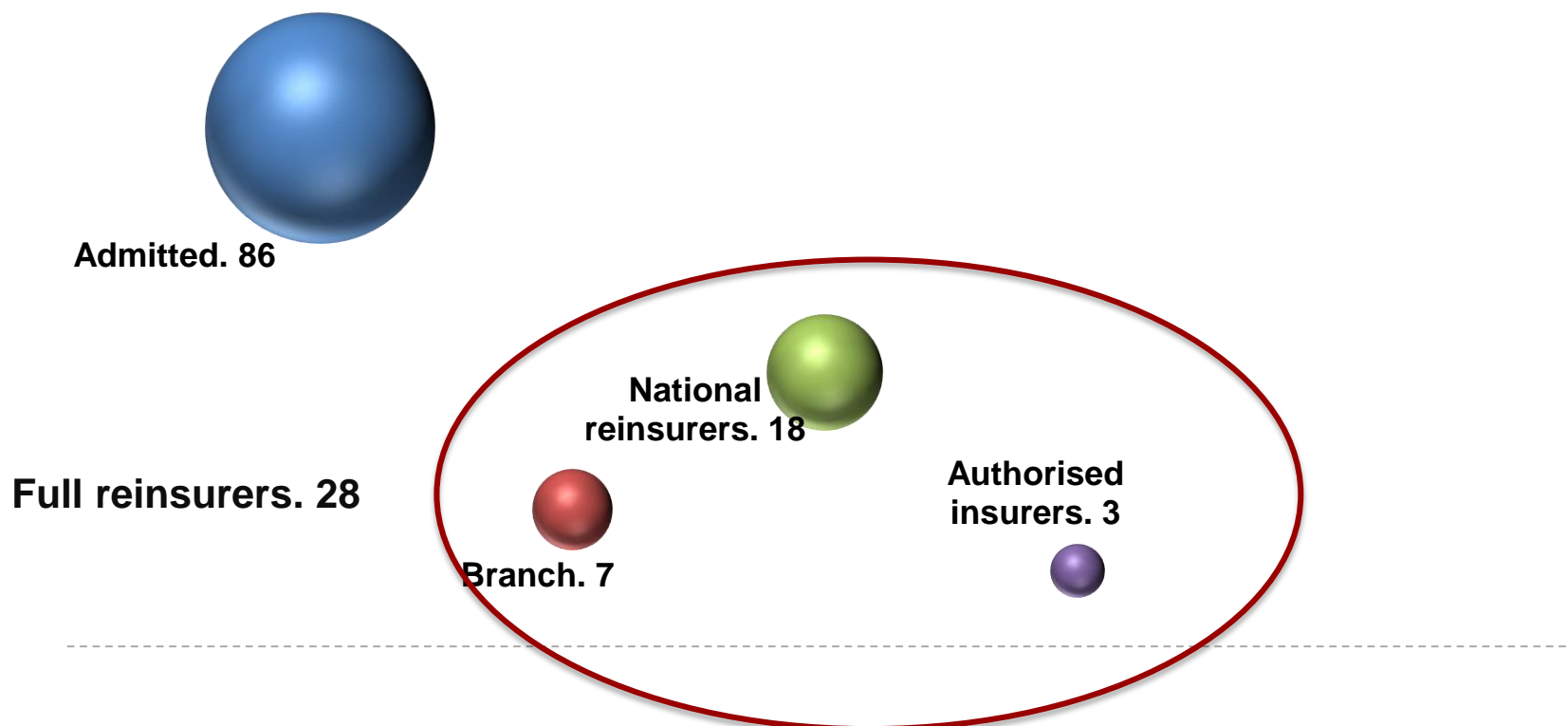
Current
Situation

The future

Reinsurance in Argentina. Evolution.



Argentina Reinsurance market.



Full reinsurers

- ✓ Local company
 - ✓ Branch
 - ✓ Insurance companies with authorization to act as a reinsurer.
-
- ✓ Activity as exclusive corporate purpose;
 - ✓ Minimum capital;
 - ✓ Register at the Public Registry;
 - ✓ File a feasibility report and business plan

Admitted reinsurers

- ✓ Act from their home offices and must be registered at the National Insurance Bureau.

- ✓ A net worth of USD 100 million

- ✓ Insurers could cede the 50% (2017) of the risk up to 75% in July 2019.

- ✓ Catastrophe plans can be fully ceded.

Reinsurance legal framework



Mandatory clauses

- 1) Law & Jurisdiction: Argentina (arbitration admitted)
- 2) Reinsurer will pay directly to the liquidator (IB) in case of liquidation of the cedant.




Facultative & treaty reinsurance contracts are commonly used in Argentina



**“Those that fail to learn from
history are doomed to repeat it.”**

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Conducting cross-border insurance
& reinsurance business within the
EEA

AIDA Working Party on State Supervision – 13 October 2018

EU Passport: introduction

- **Source:** several decades of insurance directives ⇒ Solvency II:

Article 15: Scope of authorisation

“1. An authorisation pursuant to Article 14 shall be valid for the entire Community. It shall permit insurance and reinsurance undertakings to pursue business there, that authorisation covering also the right of establishment and the freedom to provide services.”

- **(Not so) basic notions:**
 - **Home Member State** (Article 13 (8)): insurance company's head office
 - **Host Member State** (Article 14 (9)): where the risk insured is situated
 - Freedom of establishment / freedom of services:
 - Principle of single passport
 - Notification

EU Passport: Home / Host Member State

- **Home Member State:** prudential supervision
- **Host Member State:**
 - Conduct of business
 - General Good
 - Potentially applicable law (subject to Rome I Regulation)
 - Potentially jurisdiction (subject to Brussels I Regulation)

EU Passport : Location of Risk

- **Location of risks criteria:**

- a) Building / contents: Member State where the property is situated
- b) Vehicle: the Member State of registration
- c) Travel (<4 months): the Member State where the policyholder took out the policy
- d) All other cases, the Member State in which either of the following is situated:
 - i. the habitual residence of the policyholder; or
 - ii. if the policy holder is a legal person, that policyholder's establishment to which the contract relates;

EU Passport: Applicable Law (1/2)

Applicable law: Rome I Regulation – Article 7

- For large risks: parties are free to choose applicable law, in the absence of choice then law of the country where the insurer is established unless the contract is manifestly more closely connected with another country.
- For mass risks:
 - Member State where the risk is situated upon conclusion of the contract;
 - habitual residence of policyholder;
 - for insurance contracts covering risks limited to events occurring in one Member State other than the Member State where the risk is situated, the law of that Member State;
 - Professional risks with two or more risks in different Member States, the law of any of the Member States concerned or the law of the country of habitual residence of the policy holder.

EU Passport: Applicable Law (2/2)

Some further considerations:

- Compulsory insurance (Article 7 (4)):
 - The insurance contract must comply with the specific provisions laid down by the Member State that imposes the obligation.
 - Where the law of the Member State in which the risk is situated and the law of the Member State imposing the obligation to take out insurance contradict each other, the latter shall prevail.
- Overriding mandatory provisions (Article 9)

Provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract 2. Nothing in this Regulation shall restrict the application of the overriding mandatory provisions of the law of the forum.

Some complex situations

- Some grey areas in the split between home / host Member States competences
- Contracts covering several risks in different countries
- Group or collective insurance contracts on a cross-border basis
- What consists in conducting insurance business is apprehended differently depending on the country
- Distribution
- Brexit

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Compliance risks arising from cross border (re-)insurance business in Europe and ROW

Saturday, 13. October 2018

Dr Gunne W. Bähr
AIDA Working Party – State Supervision

Background

- No harmonised international insurance regulatory laws
- Insurance supervisory law in EU/EEA (regulation 2009/138/EG) states that the taking up of business of direct insurance or reinsurance is subject to prior authorisation
- E.g. in Germany an offence is punished by imprisonment up to 5 years or a fine (section 331 para 1 insurance supervisory law)
- Similar rules can be found in many jurisdiction all over the world, with slightly different consequences in case of conducting insurance business as a non-admitted insurance company
- Thus, especially insurance companies that operate all over the world face high compliance risks and have to deal with many different legal requirements

Examples of possible sanctions in the event of conducting non-admitted insurance business

Country	Criminal sanctions
Switzerland	Custodial sentence up to three years in the event of willful act. In the event of negligence fine up to CHF 250'000.
Japan	Imprisonment up to two years or JPY 3 million of criminal fine (although enforcement outside of Japan might not be likely)
Brasil	Individuals and legal entities operating in the insurance sector without the required license are subject to a fine equal to the value of the insured amount
Ireland	If convicted of a summary offence (i.e. a more minor offence), the undertaking and / or relevant person is liable to a fine not exceeding EUR 5,000 or to imprisonment of a term not exceeding 12 months, or to both. On conviction on indictment (i.e. a more serious offence, which operating without a license most likely constitutes) the undertaking and / or relevant person is liable to a fine not exceeding EUR 500,000 or to imprisonment for a term not exceeding three years, or to both.

Main Compliance Risks

(based on the example of German/EU/EEA law) I

- Insurance companies from ROW face the risk to commit a crime if they conduct insurance business in Germany without prior authorisation ([exemption for reinsurance companies situated in a country whose solvency regime has been declared as equivalent by the European commission \(Section 169 para 1 VAG\)](#))
- Despite the **single-licence-principles** established in the EU/EEA, EU/EEA insurance companies also face the risk of punishment according to section 331 para 1 Nr. 2 VAG if they conduct insurance business in the EU/EEA area outside their home member state without prior notification

Main Compliance Risks

(based on the example of German/EU/EEA law) II

- In addition, most jurisdictions impose taxes on the insurance premiums (insurance premium tax = IPT) that are usually collected by the insurance companies, although the policy holder is the tax debtor
- IPT usually must be paid where the risk is located
- If insurance companies are running insurance business and covering risks in other jurisdictions than their home jurisdiction, they possibly don't pay IPT to the right creditor and might even be committing the crime of tax evasion
 - moreover, the non-compliance with tax law and general requirements of supervisory law might have a negative impact on the fit and properness of the managers that run the insurer or have a "key function"
- In a worst-case scenario insurance companies lose their licence
- Similar rules might also apply in other jurisdictions (in Switzerland for example FINMA might impose a prohibition to work in the profession for up to five years)

P: Requirement of an authorisation

- According to German law, an authorisation is required, if an insurance company is conducting insurance business in Germany
- No exact definition when that is the case, but generally acknowledged if:
 - Policyholder has its habitual residence in Germany
 - The insurance contract entitles the insured persons to make claims against the insurance company
 - Or if they have to pay premiums to get entitlements from the insurance contract
- In many jurisdictions, the question where insurance business is conducted depends on where the risk is considered to be located → often where the policyholder or insured person has its habitual residence
- Nonetheless, there are different approaches to answer the question of where insurance business is being conducted, leading to the risk of conducting insurance business "by mistake"

Example 1: Group Insurance Contracts

- A group insurance contains t&c by which the master policyholder (e.g. employer) enters into an insurance contract to the benefit of a certain group (e.g. its employees); these group members are the insured persons
- In case insured persons and master policyholder are located in different countries, two main questions or potential compliance risks arise:
 1. Where is the insured risk located, where is insurance business being conducted? Seat of master policyholder or habitual residence of insured person? Thus, licence or notification required?
 2. Where must IPT be paid?
 - paying IPT to the wrong tax office can mean committing the crime of tax evasion

Example 2: International Insurance Programs

- International corporates need a global standardized insurance coverage for all their subsidiaries
- But in case that an insurance company is covering risks that are located elsewhere, they run the risk to conduct insurance business without a licence
- Potential solution: **Financial Interest Coverage (FInC)**
- This program does not cover the liability or material damage interest of the subsidiaries, but the financial interest of the parent company that is affected if a loss occurs to the subsidiary
- Is this an option to avoid non-admitted issues? Or may this concept be qualified as an improper **circumvention** of insurance regulation

Tax Compliance and Insurance Business – Kvaerner - Ruling of the ECJ

- Problem of IPT-related compliance risks became present with ECJ ruling on Kvaerner (ECJ ruling from 14th June 2001 C 191/99 Kvaerner ./.
Staatssecretarissen van Financiën)
- Before that ruling, the unofficial opinion in Germany was that IPT must be paid to the tax offices of the country where the policyholder is located
- Background of Kvaerner-Ruling:
 - Parent Company in UK is concluding a contract with an UK-insurer covering the risks of its subsidiaries in and outside of UK, premiums are paid by all subsidiaries.
 - One of the subsidiary is located in the Netherlands. Thus, the Dutch tax authorities raised taxes for the Dutch subsidiary.

The judgement

- The court ruled that member states are permitted to:

" 1. Levy insurance tax on a legal person established in another Member State in respect of premiums which that legal person has paid to an insurer, also established in other Member State, to cover the business risks of its subsidiary or sub-subsidiary established in the Member State making the levy. It makes no difference if the legal person which paid the premiums and the legal person whose business risks are covered are two companies in the same group linked by a relationship other than that of parent and subsidiary company

2. In interpreting 'policy-holder' or 'Member State in which the risk is situated' for the purposes of Article 2(d), final indent, of Directive 88/357, the way in which the premium relating to the risk insured is invoiced or paid within a group of companies is immaterial."

Consequences of that judgement

- IPT is to be levied where the insured interest is located
- The ECJ did not decide, where that place might be in case of master policies
- Also in cases of group insurance contracts it can remain unclear, where the insured risk is located and thus, where IPT is to be levied
- If an insurance company realizes that taxes have been paid to the wrong authority it should:
 - **Not** just remain silent and do nothing
 - Instead, a self-accusation could be the right option, but must be carried out with great care → only if it is done the right way a voluntary self-denunciation can avoid penalty
 - Correction of tax returns could be an additional measure
- All measures should only be taken after due consideration and depend on the individual case and the jurisdictions involved



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