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Global Insurance Legal Developments 2013

In association with

CLYDE&CO

Greg Dobie
Managing Editor, *Insurance Day*

Welcome to *Global Insurance Legal Developments 2013*, brought to you by *Insurance Day*, in association with leading international law firm, Clyde & Co

This annual guide takes a look at developments on the global horizon and highlights the legal challenges facing both established and emerging insurance markets in the coming months.

2012 will long be remembered as the year that saw superstorm Sandy devastate parts of New York and a number of other locations on the eastern coast of the US, continuing the recent spate of large natural catastrophe events that have impacted the sector around the world in recent years.

At the same time, the effects of the economic downturn continue to be felt by insurance and reinsurance carriers, with the low yield investment environment set to be the new normal for the foreseeable future.

While the sector largely appears to be in robust health there are signs of a material change in the prevailing claims environment. Increasingly, reinsurance notifications are either being contested or denied.

Against this backdrop careful review of contracts is advised. While it is true that the insurance and reinsurance industry is very much a global business, it is also imperative practitioners ensure they are familiar with the way rules and regulations associated with underwriting a whole manner of risks are changing across different territories; particularly given many carriers are looking to new markets in search of revenue-generating opportunities.

This guide will prove an invaluable aid in this regard, although it is, of course, no substitute for obtaining formal legal advice.

I trust you will find it most instructive. And make sure you keep up with the latest insurance law developments by visiting **www.insuranceday.com** and **www.clydeco.com** through the year. ■

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James Burns
Senior Partner Elect, Clyde & Co

Insurance and reinsurance is increasingly global, however the legal and regulatory frameworks which support, and underpin, the global insurance and reinsurance markets are all too often very localised in their approach.

In planning this guide, we have sought to give a birds-eye view of the major issues facing insurers in both the more traditional and less developed markets and to highlight the legal issues that you will need to be aware of.

Often the less mature markets will look to the more established legal systems for precedent and guidance in interpreting insurance law, and it is a valuable exercise to look at what is happening across the globe to spot trends, and to see what may be around the corner locally.

However, simply importing wordings from another jurisdiction without giving consideration as to how these may play out in the local courts (and to the regulatory and commercial backdrop) can cause issues, as the claims experience following the Arab Spring *(see page 36)* has shown.

$220bn
Insured loss from natural catastrophes in the last three years

VALUE OF INSURANCE

No global review of the insurance market can ignore the devastating natural catastrophes of the last three years that have caused much death and destruction.

Insured losses from these events total approximately $220bn, according to *Insurance Day*. It is at times of crisis that the true value of insurance is demonstrated most graphically.

Insurers have earned reputations dating back to the San Francisco earthquake in 1906, upon their ability to place the commercial considerations to one side in order to mobilise efforts and resources to respond to the worst natural disasters, providing the financial products, skills in crisis management, emergency planning, and contributing to the economic and social recovery of the regions affected.

FINANCIAL CRISIS

The impact of the global financial crisis continues to be significant. On one level the development of new regulatory frameworks is a direct response to this – and as Solvency II has been pushed back again – many insurers continue to invest time and effort into compliance with what may seem to be an ever-changing regulatory landscape.

The impact of regulatory development is not just felt in Europe – across the developing insurance markets there is steady growth in demand for greater regulation and regulatory reform, for example in India and China.

As the chapters in this guide show, often it seems there is little consistency to regulation on a global basis. It may not always be desirable to streamline processes and procedures, however the lack of regulatory harmony can cause confusion.

The implications for the claims landscape arising from the financial crisis are still being played out – so far there is a sense that what we have seen may be the tip of the iceberg – the outcomes of some of the early disputes which are yet to be resolved will potentially indicate whether the "tsunami" of claims ever arrives.

Within the eurozone, the potential consequences of the financial crisis causing a eurozone member state to leave the single currency are significant, and we have discussed these *on page 16*.

CONSTANT CHANGE

Many insurers, particularly in the US and EU, are well aware of the need to be mindful that the Iranian sanctions regime has tightened. With constant changes, it is essential to be aware of the impact of sanctions. Clyde & Co has developed a sanctions microsite (available at **www.clydeco.com**) and we are tracking the latest developments in this area, particularly with regard to the impact on the insurance industry.

As the global insurance industry grows, emerging markets mature and new products and new risks develop. The legal frameworks that support the sector need to evolve to meet the challenges this market poses

As the global insurance industry grows, emerging markets mature and new products and new risks develop. The legal frameworks that support the sector need to evolve to meet the challenges this market poses. It is helpful in speculating about what lies ahead, to take a global view of the market – but you cannot do without on the ground sector knowledge and expertise.

In developing this guide with *Insurance Day*, we have called upon the years of specialist expertise and knowledge within our network of 30 offices and we have also been pleased to receive assistance from BLD Bach Langheid Dallmayr, L.C. Rodrigo Abogados and NCTM. ■

UK

2011 global rankings (in US$)

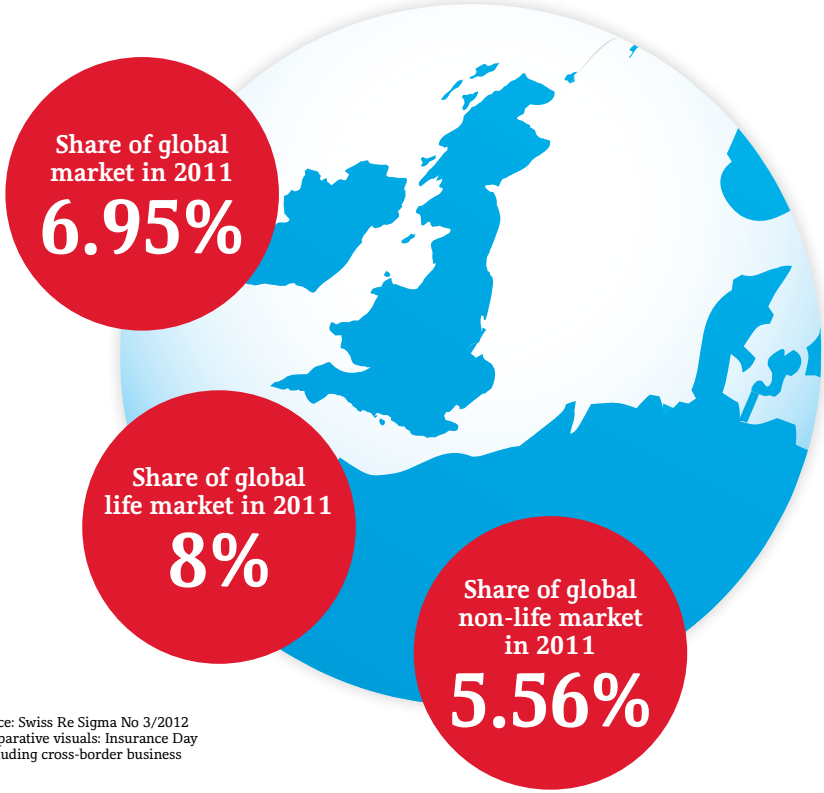
- 3 Total premium volume
- 3 Life premium volume
- 4 Non-life premium volume
- 7 Premiums per capita
- 4 Premiums as % of GDP
- 7 Ranking by GDP

Insurance density (estimated premiums per capita in US$ in 2011)*

Total business 4,535
Life business 3,347
Non-life business 1,188

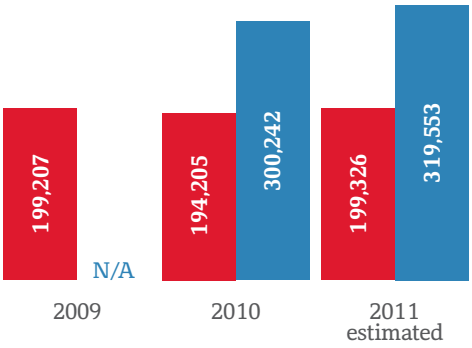
Insurance penetration (estimated premiums as a % of GDP in 2011)*

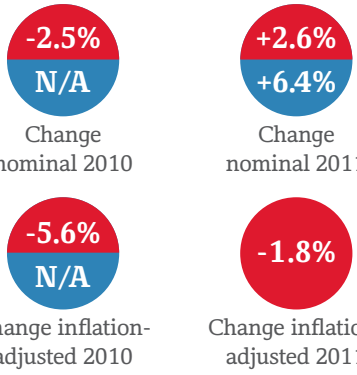
Total business 11.8%
Life business 8.7%
Non-life business 3.1%



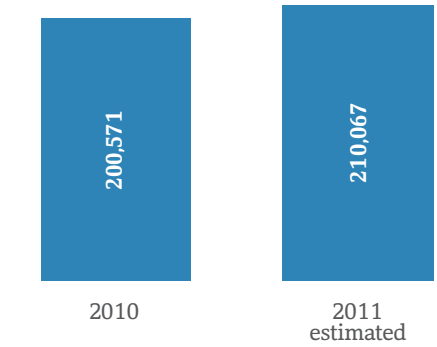
Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business

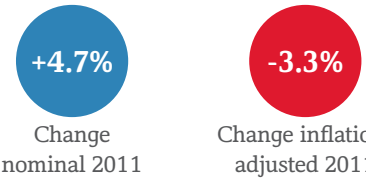
Premium volumes £m US$m



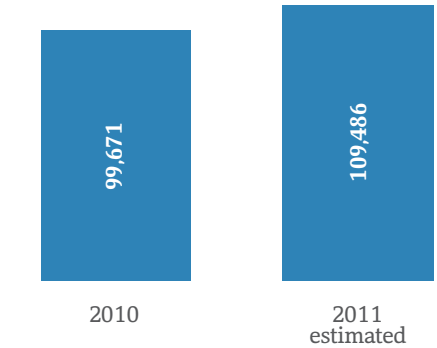


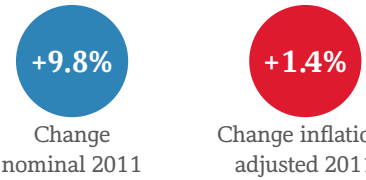
Life business premium volumes US$m





Non-life business premium volumes US$m





Road traffic incidents are reducing but indications are claims events are being fully exploited

Pincasso/shutterstock

UBS has entered into a settlement wi
LIBOR scandal

Change is afoot in the UK

The rising cost of claims remains a key issue in the UK, as legislative changes finally arrive, but the insurance sector continues to face other challenges

The UK's so-called "compensation culture" continues to generate debate, with the costs to insurers – and ultimately policyholders – rising.

The tide may start to change in 2013 with a number of Lord Justice Jackson's reforms to civil litigation funding likely to come into force in the spring.

This regulatory change, although not retrospective in effect, will go some way to helping the industry combat rising legal costs.

The claims experience is set against a backdrop of a reduction in the number of road traffic and work-related accidents; while the number of incidents is reducing, the indications are that each claim event is being fully exploited, resulting in claims deteriorating.

ON THE RADAR

While the government is seeking to reduce claims cost via statutory change, the industry will also face a number of challenges in other areas. Claims severity is likely to be impacted, as it is anticipated the Lord Chancellor will cut the discount rate applied to future losses in personal injury awards.

The discount rate is prescribed by the Lord Chancellor to take into account accelerated receipt of payment, inflation and investment returns for future losses. The Ministry of Justice's response to its consultation, which closed in October 2012, is awaited but it is expected that

th regulators in the wake of the

Female drivers will be impacted by the ECJ's *Test Achats* ruling

the current rate of 2.5% will be reduced. The consequence of a reduction in the discount rate is increased awards in severe injury claims. This will also affect reserves, reinsurance recoveries and possibly premiums in the injury market.

More broadly, legislative change is also afoot this year in the form of the new Consumer Insurance (Disclosure and Representations) Act 2012, which is expected to come into force in the spring. This is the first Act resulting from the Law Commissions' review of Insurance Contract Law. This, and other legislative changes resulting from the ECJ's *Test Achats* ruling and the Insurance Mediation Directive, is discussed on the following page.

In the financial lines market we will continue to see the fallout from increased scrutiny of the LIBOR rate being played out. So far, Barclays and UBS have entered into settlements with regulators, and we anticipate others will follow suit in the coming months. For further information on LIBOR-related developments, *see page 11*.

Last, but by no means least, the continuing tightening of Iranian sanctions will remain a key issue for insurers, both in Europe and the US. We explore the impact of these developments in the North American section of this guide on *page 26*. ■

James Burns, senior partner elect, Clyde & Co
James Dadge, partner, Clyde & Co

UK and European legislative developments

The impact of the Consumer Insurance (Disclosure and Representations) Act and ECJ *Test Achats* will be felt during 2013, while new regulations reverse the 2009 decision in *West Tankers*

On the domestic front, the Consumer Insurance (Disclosure and Representations) Act 2012 received royal assent on March 8, 2012.

It is the first Act to come out of the Law Commission's review of Insurance Contract Law. The Act covers consumer insurance contracts and, once it comes into force, (currently anticipated to be in spring 2013), it will not be possible for insurers to contract out of its provisions.

In essence, the Act provides that consumer insurance contracts will no longer be contracts of utmost good faith and there will be no requirement for the consumer to volunteer information to the insurer.

The consumer must take reasonable care when answering the insurer's questions, or when choosing to volunteer information, and an insurer will be entitled to different remedies depending on whether a non-disclosure/misrepresentation is made carelessly; or deliberately or recklessly.

In June 2012, the Law Commissions published a further paper on proposed reform of the law relating to a business insured's duty of disclosure, as well as the law on insurance warranties.

They plan to complete their project (and produce a draft bill) by the end of 2013. Actual reform may therefore be several years off and it is possible that the provisions which are finally adopted by parliament will differ to some degree from the Commissions' current proposals.

EUROPEAN DEVELOPMENTS

Following the ECJ *Test Achats* decision in March 2011, which requires insurance premiums and benefits to be gender-neutral, the UK government has introduced legislation which took effect from December 21, 2012 that will implement the judgment in the UK.

On July 3 2012 the European Commission published a provisional version of the text of the revision of the Insurance Mediation Directive (IMD2).

This will change the directive so that it will eventually make it compulsory for all intermediaries to disclose what remuneration they are receiving. It is not anticipated that the new directive will come into force before 2015, at the earliest.

Meanwhile, work also continues on the project started in 1998 to restate the common principles of European insurance contract law. These principles were first published and presented to the European Commission in December 2007, and reproduced in substantially the same form in August 2009. The Commission is currently working on further proposals.

Regulation (EC) 44/2001 has been recast into a new regulation (1215/2012 which came into force earlier in January 2013). The recast regulation confirms that proceedings relating to arbitration fall outside of its scope. This has the effect of reversing the ECJ's *West Tankers* decision in 2009 which had found that an English court may not grant an anti-suit injunction to restrain the breach of an arbitration agreement. However, although the recast regulation is now in force, the vast bulk of it will not apply until 10 January 2015. ■

After the LIBOR scandal

While LIBOR settlements, and the amounts involved, continue to make headlines, it remains unclear what impact LIBOR claims will have on insurers

LIBOR is an important benchmark rate for institutions around the world, but it has come under scrutiny since it was announced in June last year that Barclays Bank had been fined a record £290m ($467m) for manipulating the rate. This followed an investigation by authorities in the UK and the US.

In summary, LIBOR, or the London Inter-Bank Offered Rate, is a rate that measures how expensive it is for banks to borrow from one another. Different banks submit rates every day to Thomson Reuters, which calculates the rate, and the average of those submissions is set as LIBOR for that day. This process is repeated for a number of different currencies and maturities. The British Bankers' Association currently oversees the LIBOR rate-setting process.

LIBOR is the reference rate for an estimated US $800trn in financial contracts, including derivative contracts, mortgages and loans, and is considered an important measure of economic health.

Despite the fact that the first public allegations of manipulation of the LIBOR rate were made against various banks in 2008 by an article in the *Wall Street Journal*, queries were raised as early as 2007.

Following the initial allegations, regulators in various jurisdictions, including the UK, US, European Union, Japan and Canada commenced investigations to uncover the extent of the alleged manipulation.

SETTLEMENTS AND LAWSUITS

To date, Barclays and UBS are the only banks to have entered into a settlement with regulators, although it is expected that more banks will be entering into settlements in the coming weeks and months.

Numerous lawsuits have been filed in the US by shareholders and investors, alleging that the banks manipulated LIBOR in order to increase profits and to ensure that banks were not seen as a credit risk during the financial crisis.

Gordon Bell/shutterstock

Barclays entered into a settlement with regulators

A lawsuit brought by a group of homeowners also alleges that banks made "hundreds, if not billions, of dollars in wrongful profits" as a result of LIBOR manipulation, which had made mortgage repayments more expensive.

A nursing home company has also commenced an action in the UK, after it purchased a derivative contract from Barclays which was tied to LIBOR.

Martin Wheatley of the UK Financial Services Authority was commissioned by the Chancellor to produce an independent report that set out a number of proposals for the reform of LIBOR, which the UK government has said it will accept and legislate for in full.

Questions remain as to the extent of any liability the banks may have to those who purchased products linked to LIBOR, such claims seemingly having high evidential and legal burdens. As a result, it remains unclear what impact LIBOR claims may have on insurers. ■

James Cooper, partner, Clyde & Co

Macondo sets a worrying example

Along with eye-watering fines, the insurers of oil companies are being hit by attempts to redraw fines as civil damages

Attention in the energy market has recently been focused on *Macondo/Deepwater Horizon* and the $4.5bn criminal fine recently accepted by BP.

BP also stands to be fined up to $4,000 per barrel of oil or a total of $20bn under the US Clean Water Act. However, in the last 12 months Nigeria, Brazil, Ecuador and China have each sought to impose enormous liabilities on oil companies for pollution incidents that massively exceed, on a per barrel basis, the fines that have been or may be imposed upon BP by the US authorities for the Macondo/Deepwater Horizon spill.

A very significant "new" peril is emerging for oil companies and their insurers. Until recently, the received wisdom was that an oil company's liability for fines for environmental damage was manageable.

This is because in most jurisdictions the maximum amount that the authorities can fine a polluter is, in relative terms, fairly modest.

While the US is the exception, the US Department of Justice tends to be fairly insistent that the wrongdoer "feels the punishment" and does not pass the financial burden of a fine to its insurers. However, other jurisdictions are not so concerned to preserve the integrity of the fine as an instrument of punishment.

FINES OR DAMAGES?

Many liability insurance policies specifically exclude any liability in respect of fines. However, what is emerging in the environmental context is a lack of any clear distinction between

Associated Press

The US authorities' response to Macondo appears to have tr

riggered copy-cat behaviour around the world

fines (intended to punish and deter) on the one hand and civil law damages (intended to be compensatory) on the other.

For example, the $20bn civil damages claim brought in Brazil against Chevron for the Frade spill is explained in the court pleadings as being primarily informed by its environmental impact. As the environmental impact appears to be negligible this looks more like a fine than a damages claim. However, Chevron has already been fined about $17m by the Brazilian authorities. In short, an express exclusion for fines in a policy may not exclude liabilities imposed on insurers that are in substance fines but have been dressed up as damages.

Finally, it should not be assumed that these liabilities have no effect outside the jurisdiction which imposes them. Despite the general principle that one state will not tend to facilitate the enforcement of another state's fines or penalties, the Ecuadorian government has recently made significant progress in enforcing its $19bn "damages" claim against Chevron in the US, Brazil and Canada. Further, as Transocean is discovering in Brazil, an entity may have to pay up if it wants to continue doing business.

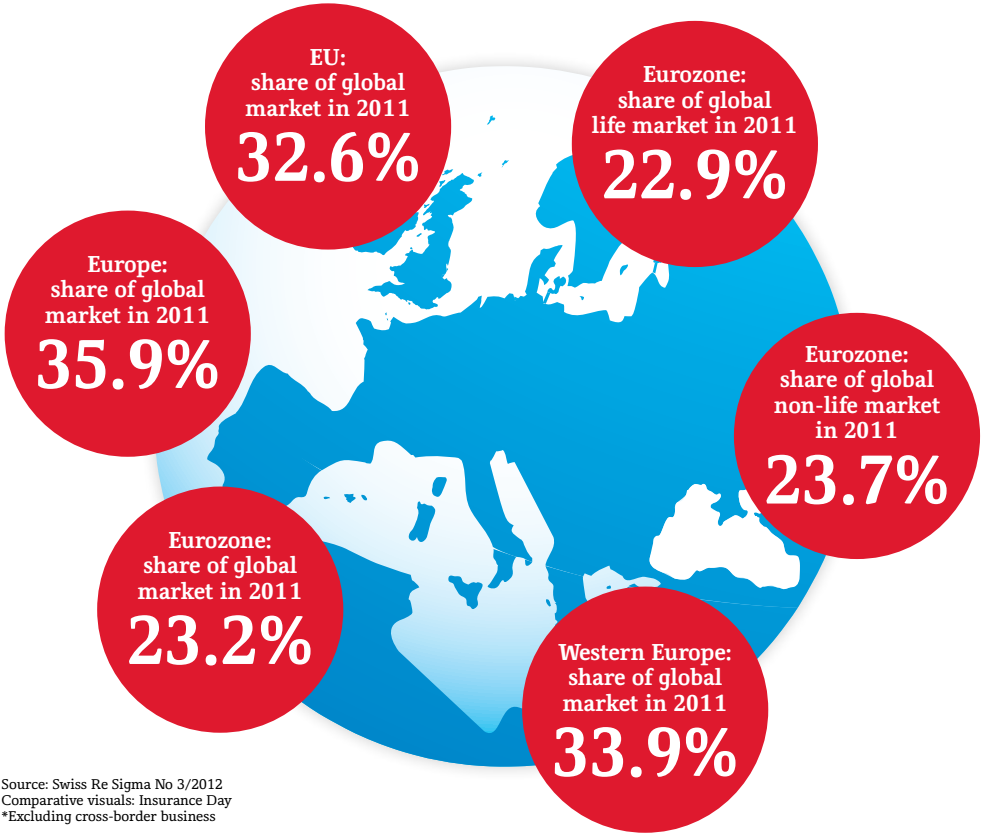
The US authorities' response to Macondo appears to have triggered copy-cat behaviour around the world. As a consequence liability in respect of environmental damage is emerging as one of the biggest, if not the biggest, single exposure for participants in energy exploration and production and their risk carriers. ■

Leigh Williams, partner, Clyde & Co

Eurozone

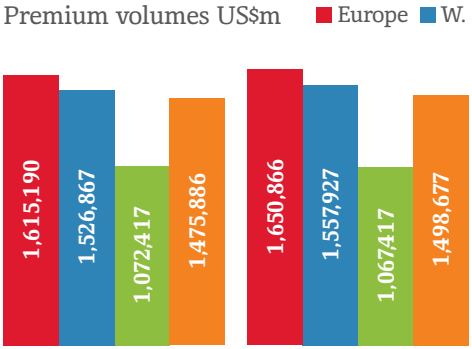
2011 Eurozone breakdown – Top 10 insurance markets $USm (estimated)

1. France $273,112
2. Germany $245,162
3. Italy $160,154
4. Netherlands $110,931
5. Spain $79,987
6. Ireland $52,250
7. Belgium $41,087
8. Finland $25,404
9. Luxembourg $23,489
10. Austria $23,051



Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business

Premium volumes US$m



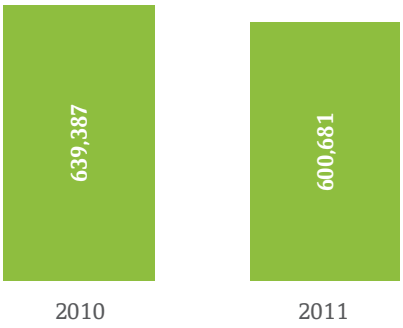
-5.2%
Change inflation-adjusted 2011

-5.8%
Change inflation-adjusted 2011

-7.5%
Change inflation-adjusted 2011

-5.9%
Change inflation-adjusted 2011

Eurozone life business premium volumes US$m

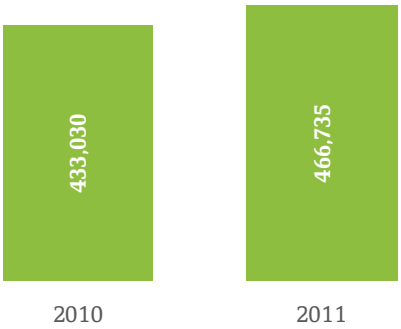


+5.2%
Change inflation-adjusted 2010

-12.7%
Change inflation-adjusted 2011

Premiums* (in % of GDP) 4.19%
Premiums* per capita (in US$) 1,657.1

Eurozone non-life business premium volumes US$m



+0.5%
Change inflation-adjusted 2010

+0.3%
Change inflation-adjusted 2011

Premiums* (% of GDP) 3.39%
Premiums* per capita (in US$) 1,340.3

New currency legislation

The debt crisis in Europe trundles on and while it does, the risk of a member state exiting the eurozone continues to be a real threat

While the investment risks associated with a Eurozone exit are familiar to most financial institutions, these are not the only risks which could impact on an insurer.

It is likely that any "new currency legislation" in an exiting member state would provide for certain contracts to automatically redenominate from euros into the new currency.

Given the rapid currency devaluation expected if a weaker country exits the eurozone this may be undesirable. The factors which are likely to be relevant to whether a contract would automatically redenominate are:

- governing law;
- location of parties;
- place of payment;
- whether there is a definition of euro.

CONTRACTUAL CONSIDERATIONS

Insurers are party to a large number of contracts in the ordinary course of business – insurance contracts, reinsurance contracts, services agreements, broker terms of business - many of which interlink and have cross-border elements.

It is possible to attempt to mitigate the probability of a contract redenominating into a new currency in the event of a eurozone exit

These contracts require particular consideration in respect of the issue of redenomination of contracts due to this inter-connectivity.

It is possible to attempt to mitigate the probability of a contract redenominating into a new currency in the event of a eurozone exit by including contractual clauses which address the possibility of a eurozone exit, which may be subject to local enforcement.

A contract continuity clause is essential to seek to prevent the contract from automatically terminating in the event of a eurozone exit. A euro definition (defining euro by reference to the single currency and not the currency of a particular country) will also be advisable in many instances.

Redenomination clauses may also be appropriate depending on the contract in question and will need to be contract-specific. Insurers will need to think carefully about what such clauses are intended to achieve if one is to be included. Factors to consider include:

- whether the contract should remain in Euros or redenominate to a new currency or to another stronger currency;
- does the insurer want to maintain the economic value of reinsurance;
- do contracts need to be back to back;
- what exchange rates will be used;
- when will redenomination be deemed to take place;
- impact on contractual payments already made;
- who is the counterparty (clauses suitable for consumer contracts will be more limited). ■

Ivor Edwards, partner, Clyde & Co

Reinsurance portfolio transfers in France - ripe for change

In contrast to the position on transfer of portfolios by insurance companies, French law does not provide for a mechanism that makes reinsurance portfolio transfers effective without obtaining each of the cedants' consent

Article L. 324-1-2 of the Insurance Code provides that reinsurers may be authorised by the French regulator, the ACP, to transfer all or part of their portfolio of contracts to reinsurance or insurance companies established in the European Union.

Their request is published in the Official Journal, giving cedants and creditors two months to present objections to the regulator.

Hurdles to the effective transfer of reinsurance portfolios have been criticised

However, authorisation granted by the regulator has no effect on each individual reinsurance agreement. The transferee must therefore seek individual consents from each of the cedants, which can be a rather complex process especially when the ceded portfolios are in run-off.

These hurdles to the effective transfer of reinsurance portfolios have been roundly criticised by the reinsurance industry. The current position constitutes a significant obstacle to the optimal management of portfolios, especially when in run-off. It is also rather paradoxical that professional cedants are afforded more protection than policyholders; the transfers of insurance portfolios are fully effective if approved by the regulator, the policyholder being simply given the option to terminate the contract.

Another oddity is that although the same mechanism applies to mergers, as the transfer of the reinsurance portfolios will still be subject to the Article L. 324-1-2 Insurance Code process, the merger can go ahead regardless of the agreement of the absorbed entity's cedants who cannot block the process.

SENSIBLE AND URGENT MEASURES

In view of the shortcomings of the current system, what can reinsurers do? One option is to adopt a fairly common process consisting of a two-step approach, starting by putting in place a 100% quota share retrocession agreement whereby the transferee reinsures the risks of the transferor.

The transferee then requests each individual cedant's agreement to the transfer. Every time an individual cedant agrees to such transfer, the corresponding assets and liabilities are transferred from the transferor to the transferee. This is of course not ideal, as the retroceded risks remain on the transferors' balance sheet pending the cedants' consent.

At a time when insurers and reinsurers are encouraged to manage their risk as efficiently as possible, in particular by the Solvency II Own Risk and Solvency Assessment (ORSA), the current situation is difficult to comprehend. Some reinsurers in France, as in the rest of Europe, will have portfolios of risks in run-off that do not match their risk profile. They, and likely their regulator, will want to be disposed of such risks. Putting in place a legal framework that allows them to do so would appear to be a sensible and urgent measure supporting good risk management. ■

Yannis Samothrakis, partner, Clyde & Co

Spotlight on Germany – defence costs in D&O contracts

A recent decision of the Frankfurt/Main court of appeal has caused an outcry among German D&O insurers

The clause under consideration provided that defence costs formed part of the insured sum. Although these clauses are standard in German domestic, and many foreign, insurance contracts, the court held that the clause was void on the basis that:

- The policyholder would not be able to determine the context in which costs deducted from the insured sum will arise. For example, whether costs arising from a dispute between insurer and policyholder, or between claimant and insured, will be deducted from the insured sum. This lack of transparency infringed the rules applying to standard form contracts
- The policyholder may not be able to estimate the amount of the costs to be deducted from the insured sum, meaning he would be taking an unknown risk in suing for cover
- The inclusion of costs which are instigated by the insurer as part of the insured sum contradicts the guiding principle of the relevant provision in the Act on Insurance Contracts (now § 101 II VVG 2008, previously § 150 II VVG 1908) and adversely affects the policyholder, rendering the clause void according to § 307 II 1 BGB (the rules applying to standard form contracts).

Insurers offering D&O cover in Germany are well advised to adapt their wordings

§ 101 II VVG 2008 provides that if a sum insured has been determined, the insurer must also reimburse the costs of a legal dispute conducted at its instigation (including the costs of the claimants´ lawyers and the court) and the costs of defence counsel to the extent they exceed the sum insured plus the insurer's expenses for indemnifying the policyholder. This rule also applies to interest payments which are payable to a third party by the policyholder as a result of a delay occasioned by the insurer.

ADAPTING WORDINGS

Although court decisions in Germany are not binding on other courts and the court of appeal is "only" the court of second instance, below the Federal Court (BGH), this decision will impact other courts. Additionally, defence costs in Germany can reach a substantial percentage of the insured sum. Therefore insurers offering D&O cover in Germany are well advised to adapt their wordings.

In particular, insurers should note that § 101 Abs. 2 VVG is a modifiable provision. However, this is only the case if the insurer clearly states that it is departing from the legal rule. The clause should indicate in which disputes (for example, against specified insureds) the deduction from the insured sum applies, and ideally fix the amount of the deduction. ■

Reinhard Dallmayr, partner, BLD Bach Langheid Dallmayr

A new regulator in Italy

Supervisory change aims to help insurers and public authorities in the fight against insurance fraud

At the beginning of 2013, the regulation of the insurance and reinsurance industry passed to a new regulatory authority.

The changes are made under the Decree Law no. 95/12, as amended and converted into Law no. 135 of August 7, 2012 and took effect on January 1.

Under the new regime, ISVAP, the Italian Private Insurance Regulatory Authority, is replaced by a new regulatory authority named IVASS - Istituto di Vigilanza sulle Assicurazioni (Insurance Supervision Institute).

IVASS is under the control of the Bank of Italy and will undertake all of the supervisory and control functions previously exercised by ISVAP.

The main change under the new regulations is that there will no longer be an independent authority with exclusive jurisdiction over the insurance industry – previously, ISVAP had exclusive jurisdiction over insurance, reinsurance and intermediary companies, while the Bank of Italy had exclusive jurisdiction over banks, financial companies and financial intermediaries. Under the new regime, IVASS will oversee the insurance and reinsurance market in connection with the other bodies of the Central Bank.

One of the principles behind the decree is transparency, intended to be supported by this connection between the Bank of Italy and IVASS.

The intention is that this will assist IVASS in one of its new additional functions; an express responsibility to help insurers and public authorities to fight insurance fraud. According to the Italian government, fraud is one of the main reasons why motor TPL insurance has become so expensive.

To assist IVASS in discharging its responsibilities, a new and more comprehensive information database has been developed. This database pulls together information previously contained in a patchwork of different systems, as well as holding additional information which insurers will be obliged to contribute. In addition to IVASS, judicial authorities, security forces, public bodies and insurers will also be permitted to access the new database.

COMPULSORY PII

Meanwhile, on the claims side, professional indemnity insurers will be gearing themselves up for the introduction of compulsory professional indemnity insurance in Italy.

In accordance with the recent legislation designed to reform Italy's "regulated professional bodies" (Italian Decree Law no. 138 of August 13, 2011, converted, with amendments, by Italian Law no. 148 of September 14, 2011), anyone providing professional services will be obliged to hold insurance covering third-party liability that may arise from the carrying out of such services.

The obligation derives from Presidential Decree no. 137 of August 7, 2012 and takes effect 12 months after the coming into force of the decree, meaning professionals falling within the scope of the decree must obtain the mandatory cover by August 14, 2013.

The provisions apply to Italy's "regulated professional bodies" (i.e. lawyers, public notaries, accountants, architects, etc.).

The professional must disclose to the client, at the time of the engagement, certain details relating to the insurance policy, including its limit. The general conditions of insurance policies may be negotiated, in agreement with its members, by the National Board of Professional Associations/Orders. ■

Anthony Perotto, partner, NCTM

Financial crisis claims in Spain

A rise in criminal and other claims against directors has brought a number of policy issues under the spotlight

The financial crisis in Spain has triggered an increase in several types of claims falling within the scope of directors and officers coverage.

In particular, in the last few months there has been an appreciable increase in claims reported to carriers as a consequence of criminal complaints lodged against the directors and officers of Spanish financial institutions.

By way of example, in June 2012 the Anti-Corruption Prosecutor filed a complaint against five former officers (senior management) of Caixa Galicia and Caixanova (unlisted savings associations or "Cajas de Ahorros"), now merged as Nova Caixa Galicia Bank, founded on the criminal offence of misappropriation and false administration arising from the generous terms set by the officers for their retirement benefits.

There has been an appreciable increase in claims reported to carriers as a consequence of criminal complaints

Another financial scandal, well known as the "preference shares case", has made many bank customers aware of the possibility of redress against financial institutions.

Several criminal complaints have been lodged by bank customers against bank officers (branch managers) accusing them of fraud, alleging that they were told that preference shares were a safe financial product which could be sold at any time, when in fact they are a high-risk complex financial instrument that most Spanish banks sold to increase solvency ratios under strict regulatory requirements and are not protected by the Spanish Deposits Guarantee Fund.

In the context of these types of claims, tensions have arisen between insurers and insureds on the interpretation and application of certain key aspects of D&O policies, such as the advancement of defence costs, cover for civil bonds for the potential civil liability, and the expenses of criminal bonds (bail), among others.

Defence costs are usually advanced for covered risks in the course of litigation and usually fall to be repaid to the insurer if the insured is convicted for an intentional crime. Coverage for these claims can prove to be a source of tension between insureds, brokers and insurers, not to mention reinsurers.

NOTIFICATION ISSUES

A further key issue is assessing whether the risk was declared to insurers correctly, potentially leading to harsh consequences for insureds under article 10 of the Insurance Contract Act 1980. This is particularly relevant considering the substantial differences between the accounts published by certain savings associations and the restatement of those accounts by their new management.

As a general rule, losses resulting from acts perpetrated in bad faith by the insured are excluded from coverage (Section 19, Insurance Contract Act 1980).

The increasing number of criminal cases brought against directors and officers must be taken into account when assessing the severity of D&O litigation in Spain. Criminal proceedings can be attractive to claimants, exerting an undoubted pressure on defendants and enabling wider investigation at a lesser cost. ■

Jorge Angell, partner, L.C. Rodrigo Abogados

Harmonising regulation in the EU

Maximum harmonisation of regulation across the EU is on the agenda, but currently insurers have the worst of both worlds

As the European Union shifts to maximum harmonisation in the arena of financial services, it would be expected that each member state would have a more or less identical regulatory regime for insurers.

While this is the dream of the bureaucrats in the EU's institutions, the reality for the insurers trying to operate on a pan-European basis is rather different, with different member states applying their own gloss to the rules hammered out (often following a significant amount of negotiation) at EU level.

The increase in cross-border transactions within the EU, as insurers restructure their operations ahead of Solvency II, reveals the widely different approaches the competent authorities in different member states can have to the same set of rules.

This creates difficulties not only in establishing the respective competencies of the authorities involved; but also in reconciling their different expectations and requirements.

Many of these issues are inherent in the nature of the EU legislation. Minimum harmonising rules, such as the Solvency I capital regime, result in inevitable variations in the degree of "gold-plating"' by different member states.

Solvency II is set to address this with a maximum harmonising regime, but the delay means insurers currently have the worst of both worlds: the effort and expense of preparing for implementation without the compensating advantage of a level playing field.

It is expected that some member states will introduce de facto Solvency II regimes ahead of the implementation date to allow firms to make use of their internal models, which is likely to exacerbate the situation. Even when Solvency II is implemented it is unlikely that each member state's approach to operating the rules will be the same.

It is expected that some member states will introduce de facto Solvency II regimes ahead of implementation

INSURANCE MEDIATION DIRECTIVE

Similar issues arise with the Insurance Mediation Directive (IMD 2), another minimum harmonising directive. Unlike the position in other member states, the UK rules extended its application to insurers. While IMD 2 will eliminate this discrepancy, as it too is a minimum harmonising directive, there is plenty of scope for fresh discrepancies between member states.

It may be that the utopia of consistent regulatory requirements across all member states is unachievable. Differences in the operation of local markets, regulatory cultures and national interests and even linguistic issues arising from translation of the rules will always lead to different interpretations.

Changing to maximum harmonisation offers the best chance of ensuring that everyone is playing by the same rules. The Solvency II experience, however, suggests that this will not happen in a short timeframe. ■

Geraldine Quirk, partner, Clyde & Co

North America

Market ranking by premium volume

1 US

9 Canada

Insurance penetration premium ranking

13 US

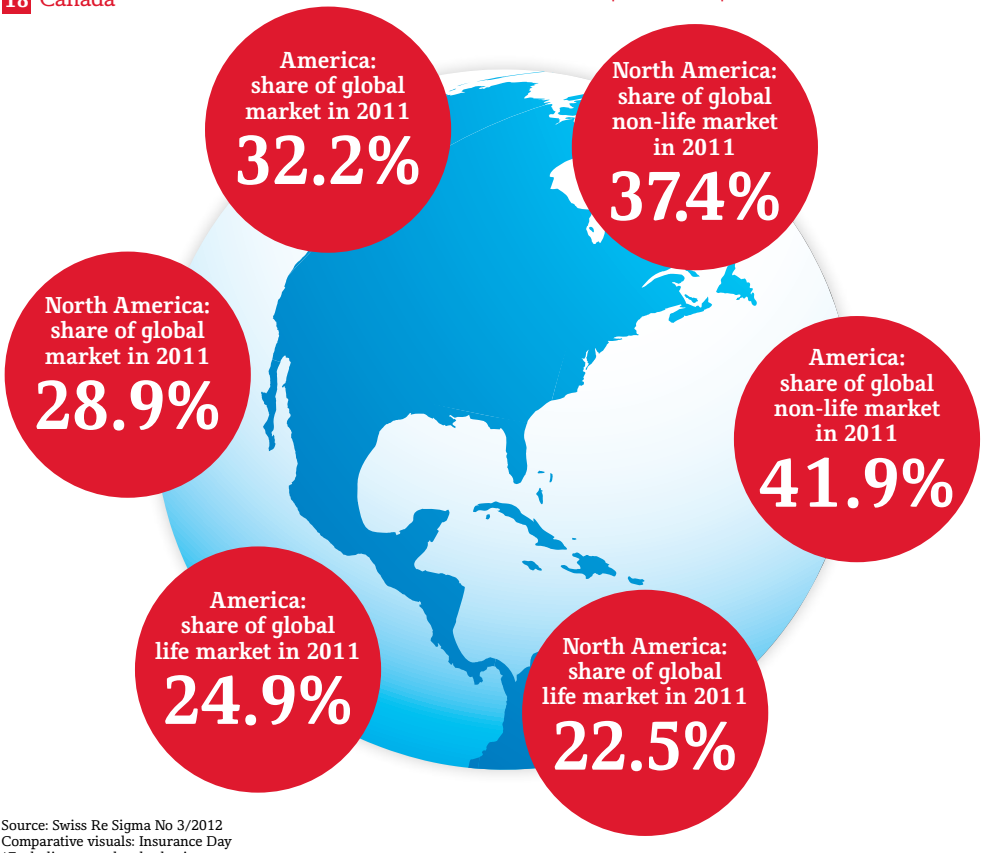
18 Canada

Estimated and provisional penetration premiums* as a % of GDP in 2011

US
Total 8.1% | Life 3.6% | Non-life 4.5%

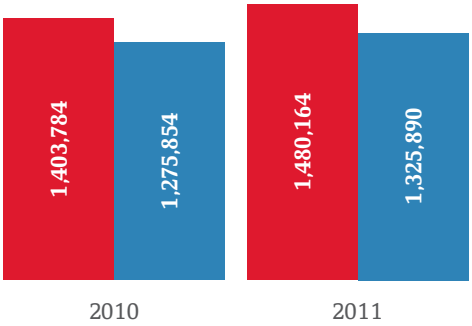
Canada
Total 7% | Life 3% | Non-life 4%

North America
Total 7.9% | Life 3.5% | Non-life 4.4%



Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business

Premium volumes US$m America North America



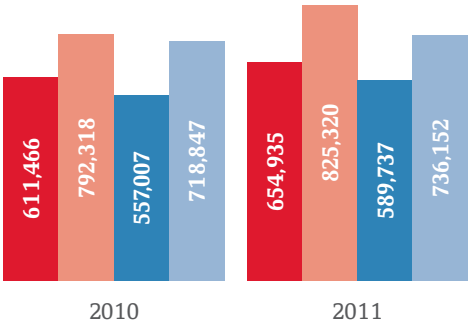
+0.3%
Change inflation-adjusted 2010

+1.3%
Change inflation-adjusted 2011

-0.4%
Change inflation-adjusted 2010

+0.4%
Change inflation-adjusted 2011

Life and non-life premium volumes US$m America life America non-life North America life North America non-life



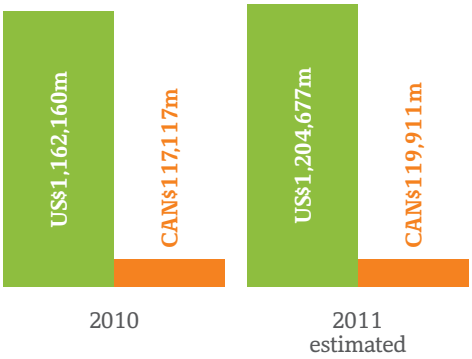
+2.9%
Change inflation-adjusted 2011

0%
Change inflation-adjusted 2011

+2.3%
Change inflation-adjusted 2011

-1.1%
Change inflation-adjusted 2011

North America premium volume breakdown in local currency US Canada



-0.6%
Change inflation-adjusted 2010

+0.5%
Change inflation-adjusted 2011

+1.3%
Change inflation-adjusted 2010

-0.5%
Change inflation-adjusted 2011

US issues come to the fore

Legal repercussions from superstorm Sandy, environmental liability, sanctions and the impact of the recent presidential election will be occupying the minds of insurers through 2013

spirit of america/shutterstock

It is now a case of "all systems go" in 2013 in relation to "Obamacare"

2012 will long be remembered as the year that saw superstorm Sandy devastate parts of New York and New Jersey.

With claims continuing to roll in, Sandy has overshadowed many of the preceding series of natural catastrophes that have dominated the headlines in recent years.

The legal repercussions of this disaster are considered on *page 25*. We also consider the environmental risks associated with natural disasters such as Sandy, as well as incidents arising in the energy sector.

A political storm also swept across the US, with the 2012 presidential elections taking centre stage. It is now a case of "all systems go" in 2013 in relation to "Obamacare".

Following President Obama's re-election and the decision by the US Supreme Court upholding the Patient Protection and Affordable Care Act (PPACA), the cogs are in motion for the implementation of PPACA.

The legislation will publish regulations which, among other things, will govern the coverage that health insurers must provide. Health insurers will be watching these developments closely.

Aside from finding itself at the centre of the political universe during the US elections, Ohio has also been under the spotlight in the financial lines sphere following a ruling by the Court of Appeal of the Sixth Circuit that essentially redefines the parameters of traditional computer crime coverage. Analysis of the Ohio decision is set out on *page 28*.

SANCTIONS REGIME

A newly-effective expansion of US sanctions laws now means that US insurers and other companies are, for the first time, responsible for the conduct of foreign subsidiaries that they own or control.

So, if those subsidiaries conduct business with Iran, the US owner is in violation. US insurers are now obliged to monitor and govern the conduct of their subsidiaries in a way that they had not been previously required.

Given that penalties for violation of these laws can be severe, even where the violation is inadvertent, it is expected that company management will insist upon regular and independent audits of their foreign subsidiaries' activities as a means of not only complying with the law but also protecting management from the severe penalties that result from non-compliance. ■

Mike Knoerzer, partner, Clyde & Co

Sandy and the concept of "damage"

The series of recent natural catastrophes has raised a number of old and new issues with which the market is grappling

To say 2011 was a bad year for natural catastrophes is a serious understatement. 2012 was paling by comparison until superstorm Sandy hit late in the season.

The catastrophes highlighted the importance of the concept of "damage" and new situations challenged how that concept is applied.

For example, in New Zealand, in the aftermath of the Christchurch earthquakes, whole areas had to be abandoned due to the higher potential for liquefaction. Residents had clearly lost their properties but those properties were at that time undamaged. How does one apply traditional principles of damage to this situation?

THE BUSINESS INTERRUPTION FACTOR

A number of issues have also arisen in relation to the application of business interruption (BI) insurance and again damage was at the forefront of these.

BI to supply chains in Japan and recently in the US arose often out of widespread loss of power. Where damage to a supplier is necessary under a policy can it be said that there is actual damage in that situation?

Again in relation to BI the issue of wide area damage arises. In many BI policies the BI must arise from the damage to the insured's property.

If the surrounding area has been evacuated or utterly destroyed then under many BI policies the business interruption is not a result of the damage to the property; even if the property was undamaged there would be no-one in the area to use the business and generate income.

Equally if one is putting, for example, a hotel back in the position it would have been if it had not been damaged in a populated area, is this done on the basis the hotel would be the only viable business in town?

Lastly, the long supply chains of modern business have shown that immediate supplier BI cover may not be sufficient. Where the peril is very slow moving, as in the Thai floods (covered in further detail on *page 40*), questions may be raised as to why insureds did not remove themselves and their equipment from the path of the flooding if possible.

Anton Oparin/shutterstock

In relation to BI the issue of wide area damage arises. In many BI policies the BI must arise from the damage to the insured's property

IN FOCUS: Sanctions

EU and US insurers will be well aware that the Iranian sanctions regime tightened in 2012 and in 2013 the sanctions theme looks set to continue, with a number of new regulations in January and US sanctions remaining top of the the agenda.

The current regimes impact a large proportion of the global marine insurance market. Stringent sanctions in the EU, expanded in July 2012, prohibit the provision of insurance for the purchase or transportation of Iranian origin crude oil to anywhere in the world, as well as a broader ban on insuring Iranian entities (additional regulations in December 2012 impose similar prohibitions in relations to natural gas).

While most marine policies will include a sanctions clause, this must be supplemented by appropriate due diligence on insurers' part during the life of the policy in question to ensure sanctions compliance.

Although EU sanctions do not prohibit trade with Iran altogether, logistical challenges exist in practice. For example, while the selling of books to Iran is permitted, the prohibitions will affect the insurance of cargo into Iran at the point where the risk passes to the recipient Iranian entity which will then be regarded as the insured and as falling within the prohibitions.

The non-Iranian seller may also have practical problems in obtaining payment from its Iranian buyer in light of financial restrictions on dealing with Iranian banks, (extended in the EU in December 2012).

ITRA IMPACT

The US has ramped up its regime over the last year. The most recent development is IFCPA, which becomes effective July 1, 2013, and applies a range of further sanctions to Iranian industries, and includes specific prohibitions on the insurance industry. IFCPA comes months after the introduction of ITRA in August 2012 which includes sweeping sanctions largely focused on the energy market and which affect both US and non-US insurers trading with Iran.

In particular, Section 218 imposes prohibitions on non-US subsidiaries of US companies (including insurers) with sanctions for non-compliance being meted out to the US parent.

IFCPA goes further imposing sanctions on "any person" ie whether or not they are US-owned or controlled, knowingly providing insurance within the areas listed. ■

Mike Roderick, partner, Clyde & Co
Nigel Brook, partner, Clyde & Co

In addition to these concerns are more familiar problems. Where the losses are widespread or occur over a very long period of time there may be issues defining the four corners of an "event" for the purposes of aggregation. The application of hours clauses can also be questioned in these circumstances.

Well-worn issues of exclusions will also inevitably arise; natural catastrophes often involve both wind and flood and exclusions may apply to those.

Where a catastrophe is extreme there may also be little left of the damaged property to be clear what the proximate cause of the damage was.

These are all issues with which the insurance and reinsurance market will have to grapple in the coming months. ■

David Abbott, partner, Clyde & Co

Environmental liability

Insurers can expect an increase in claims relating to oil exploration and extraction, hydraulic fracturing and climate change in future years

The search for new oil deposits is expanding to unexplored regions that present greater challenges. Drilling in deep ocean floors may enhance the risk of incidents comparable to *Deepwater Horizon* as the bounds of engineering are tested.

Exploration and extraction within the Arctic Circle may present the risk of similar incidents in addition to shipping accidents. The fragility of the environment and the inaccessibility of the region would multiply the adverse impacts of any major incident.

Hydraulic fracturing has already triggered myriad environmental claims. Various claims arise from damage allegedly caused by the fracking process.

Others relate to the increased volume of transportation equipment and materials attendant to the process. These claims will continue to mount in areas where fracking is in progress.

With the promise hydraulic fracturing has demonstrated, by yielding massive quantities of natural gas, fracking will expand internationally with a corresponding increase in claims.

The nascent exploration and extraction of oil from oil sands may present the risk of similar claims. Deforestation incident to accessing the oil sands may present the risk of varied environmental impacts to surface water and animal life.

ADVANCING CLIMATE CHANGE

Carbon emissions from the extraction process may advance climate change. Additional risks will arise from the construction and operation of pipelines to transport oil from the oil sands regions to downstream refineries and storage facilities.

Of course climate change presents a wide range of environmental risks. While carbon emission nuisance and property damage claims have been restricted in the US based on preemption principles, such claims will not face comparable hurdles in other jurisdictions.

Hydraulic fracturing has already triggered myriad environmental claims

Of perhaps greater concern, claims indirectly related to global warming are likely to multiply. Storms are increasing in number and severity and will trigger pollutant releases ranging from raw sewage to refinery by-products to industrial wastes.

These storms will also bring more rain and storm surge that will leave mould damage in their wake.

Some of the most significant environmental calamities in history have occurred in recent years, whether associated with “superstorms” like Hurricane Katrina, transportation of oil in sensitive ecological regions like *Exxon Valdez*, or oil drilling like *Deepwater Horizon*. Unfortunately, similar incidents are likely to occur in the years ahead. ■

Kevin Haas, partner, Clyde & Co

Computer crime coverage for third-party loss?

Fidelity insurers were among the first to respond to the need for products protecting against risks arising from computer use in developing computer crime coverage

Unlike specialised cyber liability policies, however, fidelity coverage contains a key feature. Coverage is available only for losses *resulting directly from* the covered peril – here, computer fraud.

By contrast, cyber liability policies offer coverage for third-party liability. In *Retail Ventures, Inc. v. National Union Fire Ins. Co. of Pittsburgh, PA*, 2012 WL 3608432 (6th Cir. 2012), the distinction was blurred between computer crime and cyber liability policies by holding that computer crime coverage afforded coverage for an insured's third-party liability.

The insured in *Retail Ventures* fell victim to a computer hacking scheme whereby hackers downloaded credit card and account information on the insured's customers, and used it to conduct fraudulent transactions.

Thereafter, the insured incurred expenses arising from resulting customer claims and lawsuits, investigations by state attorney generals and the Federal Trade Commission, customer communications, and public relations.

The insured in *Retail Ventures* fell victim to a computer hacking scheme whereby hackers downloaded credit card and account information on the insured's customers

The insured sought coverage for its losses under a blanket crime policy issued by National Union. The policy contained computer and funds transfer coverage, under which National Union agreed to pay for "loss which the insured shall sustain *resulting directly from*... the theft of any insured property by computer fraud."

The definition of computer fraud included "the wrongful conversion of assets under the direct or indirect control of a computer system by means of ... the fraudulent accessing of such computer system."

CAUSE OF THE LOSSES

National Union did not dispute the computer fraud but declined coverage on the basis that the insured's losses did not result directly from computer fraud.

Rather, they took the position that the direct cause of the losses was the insured's legal liability to third-parties who asserted claims after the data breach occurred.

The Sixth Circuit predicted the Ohio Supreme Court would apply the broader *proximate cause* standard and, on that basis, concluded the insured's loss resulted directly from the theft of insured property by computer fraud.

Retail Ventures potentially opens a Pandora's Box of computer crime coverage for third-party liability. Some commentators suggest insurers now should look to their fidelity bonds for broader cyber coverage. ■

William Lutz, partner, Clyde & Co

Issues to watch for in Canada

The impact of *Progressive Homes Ltd v. Lombard General Insurance Co,* signs of increasing severity of losses in financial services and D&O sectors in Canada and increasingly inventive use of the *Companies' Creditors Arrangements Act* will be occupying the minds of risk practitioners during 2013

The impact of the Supreme Court of Canada judgment in *Progressive Homes Ltd v. Lombard General Insurance Co* (2010 SCC 33) is being felt as contractors are now challenging their carriers for coverage, based upon the Court's interpretation of the terms "occurrence" and "property damage" in the context of a Commercial General Liability (CGL) policy.

In this case, the Supreme Court rejected the insurer's argument that damage to the project itself could not constitute covered "property damage" and held that faulty workmanship could constitute an "occurrence" depending on the facts of the case. The overall impact of this case remains to be seen as various coverage disputes work their way through the court system.

Signs of increasing severity of losses in financial services and D&O sectors in Canada were observed in 2012. Most noteworthy, December 2012 saw the settlement for C$117m ($118m) (court approval pending) of the C$6.5bn Ontario class action claim by Sino-Forest's shareholders against the company's auditors.

It is the largest settlement to date in the rash of Canadian Chinese reverse-merger securities litigation and by far the largest settlement in Canadian history by an auditor of a claim in respect of a Canadian-listed company. Litigation in Sino-Forest continues against the co-defendants, including the directors and officers and securities underwriters.

2012 has also continued the trend toward the inventive use of the *Companies' Creditors Arrangements Act* (CCAA) as a vehicle for the settlement of complex financial litigation in Canada in a quick and cost-effective manner.

In 2008, the Supreme Court of Canada gave the green light to use the CCAA for broad litigation bars in the Canadian asset-backed commercial paper matter. Since then, it has been used by converting receiverships into CCAA proceedings as a vehicle to resolve class action litigation, including the use of deemed releases, broad bar orders and dismissal of putative class proceedings and largely circumventing lawyers for the putative class.

LEGISLATIVE DEVELOPMENTS

On the legislative front, the bill which will amend the Federal Government's privacy law is anxiously awaited but no date is set for its coming into force. This legislation will require compulsory reporting in the event of data breach. Only one province in Canada, Alberta, requires compulsory reporting under its privacy legislation. The Federal bill has been criticised as somewhat out-of-date given the enforcement powers that some international data protection agencies have or will shortly have, calling for stronger enforcement tools for Canada.

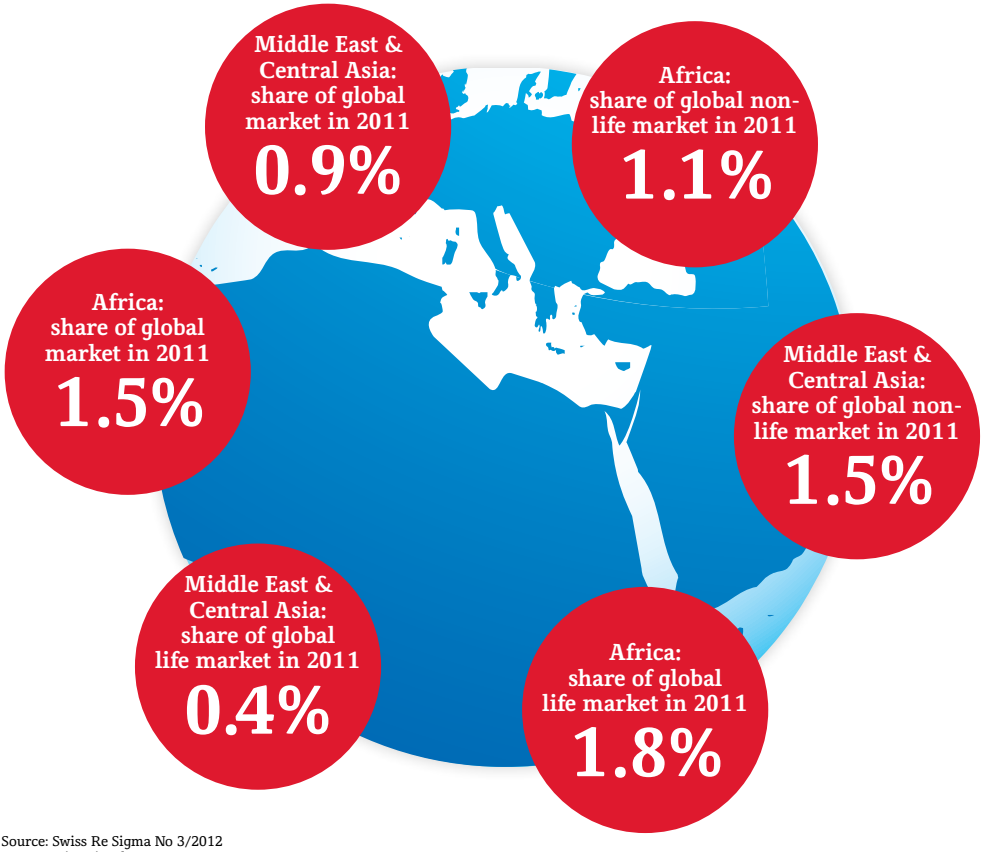
At this time, secondary market liability legislation, which amended existing securities legislation and imposed civil liability on directors and officers and others for misrepresentations and the failure to make timely disclosure, remains of great interest. Numerous preliminary motions have been pled under these new provisions, but insurers, and directors and officers anxiously await a judgment on the merits, which has the potential to influence the markets for years to come. ■

Carolena Gordon, partner, Clyde & Co

Middle East & North Africa

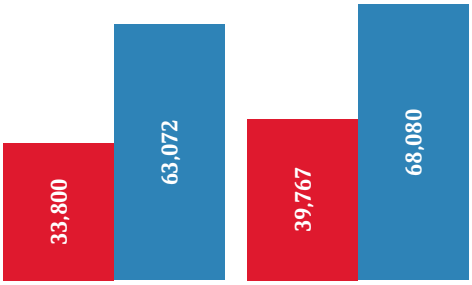
2011 Middle East & North Africa non-life market breakdown – Global rankings by premium

- 32 Iran
- 35 Israel
- 36 United Arab Emirates (UAE)
- 41 Saudi Arabia
- 50 Morocco
- 58 Algeria
- 62 Egypt



Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business

Premium volumes US$m ■ Middle East and Central Asia ■ Africa



+6.5%
Change inflation-adjusted 2010

+9.4%
Change inflation-adjusted 2011

-6.8%
Change inflation-adjusted 2010

+1.8%
Change inflation-adjusted 2011

Life and non-life premium volumes US$m ■ ME & CA life ■ ME & CA non-life ■ Africa life ■ Africa non-life

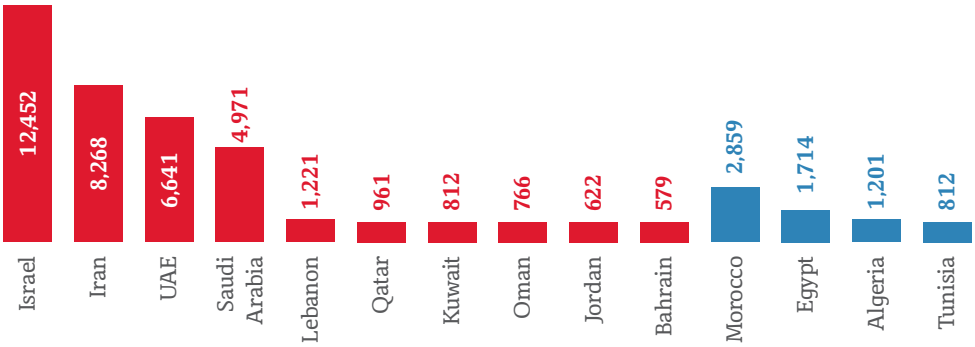
+9.4%
Change inflation-adjusted 2011

+8.9%
Change inflation-adjusted 2011

+1.3%
Change inflation-adjusted 2011

+3.3%
Change inflation-adjusted 2011

2011 Middle East & North Africa premium volumes by country US$m (estimated/provisional)



Recent developments across the GCC

Insurers operating in the region need to be increasingly alert in order to keep pace with local regulatory developments, often underpinned by hard-to-access legislation

The insurance market across the Gulf Co-operation Council (GCC) countries continues to mature, with varying levels of progress.

The realisation has dawned on regional regulators that improved and modernised regulation is required in an overly-crowded market operating at unsustainable premium rates. However, implementation remains patchy.

At the one extreme, the financial centres in Dubai (DIFC) and Qatar (QFC) embody world-class regulatory systems, which are sometimes seen as too developed for the markets in which they operate. At the other, government ministries continue to handle insurance as one of their many portfolios, with an outdated approach to regulation and little effective enforcement.

Newer, homegrown regulators such as the Saudi Arabian Monetary Authority (SAMA) in Saudi Arabia, or the insurance authority in the UAE, have tended to forge ahead with their own brand of market regulation (SAMA), or fallen back for lack of implementation and enforcement (UAE).

HEALTH INSURANCE

Health insurance remains a hot topic in the region. The challenge of introducing social health insurance schemes continues, with Qatar leading the charge in implementing a compulsory social health insurance system, with a target date of 2014. Bahrain and Kuwait have declared an intention to follow, while the long-awaited Dubai scheme has yet to emerge, although there has been a recent announcement that a UAE federal health insurance law and regulator will be established. How this new law and regulator will interface with existing regulators remains to be seen.

Of those territories that have introduced compulsory health insurance, Abu Dhabi continues to build on a strong start and is actively collating health statistics as the system matures. The challenge for the insurance market in each of these territories is what role the private insurance market will be allowed to play. Abu Dhabi has a free market but is dominated by the state-owned Daman. Qatar appears to be establishing a state-owned insurer to provide the compulsory cover, which is likely to leave private insurers on the fringes.

DISTRIBUTION CHANNELS

Distribution channels in the GCC insurance market remain relatively constrained by local regulations. Bahrain is the only territory in the region that permits appointed representatives (such as car showrooms and travel agents) to act as intermediaries for consumer insurance products.

Bancassurance continues to grow in the region. In Oman a definitive decision on the topic was issued by the Capital Markets Authority. However, in the UAE, draft legislation that was issued has not yet been promulgated, although a circular providing guidance on bancassurance in practice appears to set the standards which insurers and banks must adopt. In the absence of binding legislation, most insurers and banks are taking a prudent approach in establishing distribution networks and alliances. The guidance is not comprehensive, and it is hoped that when legislation is finally issued it will clarify a number of issues.

More recently in 2012 the UAE Insurance Authority issued a consultation document outlining a new draft regime for the regulation of insurance intermediaries. It was hoped that this would signal the commencement of a regulatory overhaul of the roles

played by insurance intermediaries. Unfortunately the draft fails to recognise the multiple roles that agents play in a modern insurance landscape, and does not enact the necessary checks and balances that are required in a modern, risk-based regulatory system.

AROUND THE REGION

In the UAE, a three-year reprieve has recently been announced by the insurance authority to extend an earlier July 2012 deadline to 2015 for insurance companies carrying on composite business to adjust their status and undertake separate life and non-life business.

It has been reported in the press that the decision to extend the deadline was influenced by the ongoing impact of the global downturn and in order to foster a competitive environment in the UAE. The news has been well received by the regional market and especially UAE composites who have been allowed to postpone the costs and additional capital requirements that will inevitably be associated with the segregation of their life and non-life business.

At present there is no clear indication as to how UAE insurers will be able to spin off their life and non-life business into separate operating entities, and as publicly-listed companies, this is likely to require the involvement of the stock market regulators.

This initiative coincides with ongoing efforts in the UAE market to revamp solvency and prudential rules. However, following an extensive consultation process at which the insurance market expressed reservations on the effectiveness of the draft proposals, these too are on hold. There remains much to do on the solvency and prudential front, with current regulations (dating back to the early 1980s) heavily slanted towards general business, and virtually no regulations that take into account the existence of life insurance.

Qatar is leading the charge in implementing a compulsory social health insurance system

Recently the regulator in Oman has introduced a requirement for foreign insurers established as branches in Oman to hold local capital. This is a departure from the traditional approach which entitles foreign insurers to rely on parent ratings and capital to satisfy local requirements.

The DIFC continues to grow in stature as a regional reinsurance hub. Recent entrants include Swiss Re, Standard Life and Royal & Sun Alliance, who join the ranks of Zurich, AIG and Munich Re in the centre. The DFSA continues to adopt a healthy approach to enforcing its rulebook, and reforming its rules. A recent AML consultation is likely to see a new AML regime come into place in the near future.

In Qatar, recent developments indicate that the long-awaited single regulator for the financial

services market (including banks and insurance companies) may be emerging. The challenge for the new body will be to align the detailed and world-class regulatory framework which governs the QFC with an outdated and limited regulatory system that has governed financial services conducted in the State of Qatar. The Qatar insurance law dates back to the early 1960s.

REGULATORY PROGRESS IN SAUDI ARABIA

The region is currently characterised by varying rates of progress in regulatory development. The Saudi insurance market, which is regulated by SAMA, continues its rapid progress issuing a range of new government laws common to a host of market sectors that are contributing to the insurance industry's growth.

SAMA is well-known in the region for its efforts to establish a comprehensive regulatory framework for financial services in the kingdom.

SAMA and the Capital Markets Authority have recently signed a memorandum of co-operation which is anticipated to streamline regulatory processes in Saudi by providing for coordination from both organisations in issuing new regulations or providing market guidance.

Another important Saudi development is the mortgage and finance laws issued by SAMA in November 2012. These now allow mortgages to be taken over properties in Saudi Arabia where previously they were not permitted. This will undoubtedly result in increased insurance sales in the areas of credit, life and property insurance. On the regulatory front, having issued comprehensive regulations governing insurers and brokers, SAMA's focus has been on conduct of business issues and the regulation of service providers.

Recent outsourcing regulations will require Saudi market players to reassess their outsourcing activities and align their operations with the comprehensive new requirements.

RENEWED INTEREST IN KUWAIT

At the other end of the spectrum and lagging somewhat behind its neighbours, the Insurance Department of the Ministry of Commerce and Industry (MOCI) is responsible for the regulation and supervision of the insurance industry in Kuwait, still operating under laws dating back to the 1960s. After an extended period of inactivity, the Kuwaiti government has recently shown signs of renewed interest in its domestic insurance market.

The MOCI is working on restructuring the insurance directorate by establishing an independent Supervisory and Control Commission to oversee the insurance sector and work on developing the industry. With a rumoured new insurance law in the wings and the establishment of a state health insurer under way, work is clearly still being undertaken to find the right solutions to ensure growth and prosperity in the Kuwaiti industry.

The result of this multi-track process has been to produce a number of difficulties for the insurance market. Whilst some territories (especially the financial centres at DIFC and QFC) have transparent practices and easily accessible legislation, others remain opaque and often unclear. The region is no closer to regulatory homogeny that would allow passporting across the GCC. Consequently, insurers operating in the region need to be increasingly alert in order to keep pace with local regulatory developments, often underpinned by hard-to-access legislation.

Going forward, while the region has good growth prospects, it is abundantly clear that unless outdated laws are replaced with carefully considered, responsive legislation, growth and innovation in the region's insurance market will be hampered long-term. ■

Wayne Jones, partner, Clyde & Co

Focus on Dubai – extended reach of the DIFC court

The jurisdiction of the Dubai International Financial Centre (DIFC) court was recently extended by Dubai Law No. 16 of 2011, which allows parties with no specific connection with the DIFC to elect to have their commercial disputes resolved by the court. Prior to this extension, the court would only be granted jurisdiction if one of the parties was located in the DIFC; the contract was entered into in the DIFC; or the property at dispute was located in the DIFC.

There are clear attractions for the regional insurance market to use the DIFC court, which guarantees interpretation of international practices and laws from leading, developed Western financial centres and one can expect to see terms of business agreements between insurers and brokers and other service providers increasingly including court jurisdiction clauses. The court also oversees a world-class international arbitration centre.

Other key advantages of the DIFC court include: excellent legal infrastructure with a track record for judicial quality; common law rules and procedures; an advantageous regional location; English language proceedings; the ability to recover costs from a losing party; and, importantly, an assurance that DIFC judgments will be enforceable in the UAE and further afield.

The court provides a stable forum for dispute resolution between insurers, intermediaries and other service providers and has particular application to international business and contractual relationships where English is used as the commercial language and disputes are best determined by the application of common law principles and procedures.

Invariably limitations exist. It is unlikely that local regulators will permit DIFC jurisdiction and

Mark Preston/shutterstock

law clauses to govern direct insurance policies in their territories. So, it is unlikely that DIFC arbitration and jurisdiction clauses will be capable of being included in domestic insurance policies. Rather, the DIFC court ought to be an attractive venue for disputes between market participants such as brokers, service providers and reinsurers. However, it remains to be seen whether the courts of other GCC territories, and even other Emirates such as Abu Dhabi, will respect the parties' choice of jurisdiction.

Mutual arrangements have been established with the Dubai courts, which should permit DIFC court judgments and arbitration awards to be "rubber stamped" by the Dubai courts, and therefore capable of enforcement in the UAE and abroad.

How the court is used by the regional insurance industry going forward will be interesting. Undoubtedly, careful consideration will be required when including DIFC jurisdiction clauses in commercial contracts. ■

After the unrest

Claims arising from the Arab Spring have put previously overlooked definitions and exclusions under the spotlight

In December 2010, civil unrest began to spread across much of the Arab world, leading to regime change in Tunisia, Egypt, Libya and Yemen, widespread conflict in Syria, violent clashes in Bahrain and demonstrations in a number of other countries, some of which may yet suffer the high profile fate of their neighbours.

It is no surprise that the widespread civil unrest, demonstrations, rebellion and revolution which define the events of what has become known as the Arab Spring had significant consequences for insurers operating in those countries.

In particular, a number of large claims arose for property damage in Egypt, where in the weeks culminating up to the overthrow of President Hosni Mubarak, the uprising went from being largely peaceful to violent clashes between security forces and protesters. In late January 2011, vandalism and looting in Cairo and Alexandria were widespread.

These claims have raised a number of interesting issues for domestic insurers and the international insurance and reinsurance market. In particular, the categorisation of the events (i.e. whether at any given date of a loss, the cause is a riot, civil commotion, uprising, insurrection, rebellion or revolution) and what is and is not covered under a particular policy wording came into sudden focus.

Mohamed Elsayyed/shutterstock

The Arab Spring had significant consequences for insurers operating in the countries affected

FOCUS ON WORDINGS

Many claims were made under property (all risks) and, less commonly, political violence policies. In a few cases, the insured may have had the benefit of both. This led to potential double insurance issues, or the insured facing the prospect that neither policy responded for certain excluded losses.

The property, political violence and reinsurance wordings that came under the microscope were, in most cases, simply imported from the London market with little thought given to how those concepts would be interpreted in local courts, or how such distinctions should be conveyed in the Arabic language.

The terms commonly found in these policies (as exclusions or named perils respectively) such as “civil commotion”, “uprising” or “insurrection” have well-established meanings, developed over time under English case law.

In contrast, in the civil law jurisdictions of countries affected by the Arab Spring, no such

IN FOCUS: Political risk, civil unrest and terrorism

In tandem with a period of significant civil unrest and political uprising globally (most notably in North Africa and the Middle East), the ongoing recession in many of the more developed economies threatens to bring civil disturbances closer to home. Whilst those uprisings were largely driven by a demand for political regime change, many are beginning to speculate that an economic bloodbath in economies such as Spain and Greece, countries continuing to struggle with a wave of bankruptcies and sovereign debt, will be accompanied by civil unrest and riots with economic and political motivation at their core.

COVERAGE JIGSAW

Against this backdrop, a key issue for the insurance industry is how "all risks" property and business interruption covers, which conventionally exclude losses arising from civil commotion, war and terrorism, dovetail with standalone political violence and terrorism products. Putting to one side the expectation gap among risk managers, many of whom wrongly assume that property damage arising out of a civil disturbance will always be covered by the all risks policy, it can be difficult to ascertain which policy should respond to the loss in question and the way these policies are typically structured leaves open the real possibility of a gap in cover.

For example, all risks cover typically excludes losses both directly and indirectly caused by civil unrest. Standalone political violence cover will respond only to cover losses as a direct result of an insured cause of loss. There is therefore the possibility that a loss may be the indirect result of an excluded risk in the property insurance, but that risk is not a sufficient direct cause of the loss to be covered by the political violence policy. Hence the insured could fall between two stools, depending on the root cause of the loss.

Determining the true cause of the losses sustained and which losses are insured and under which cover can be extremely difficult in circumstances (Syria being a current example) where the market cannot gain access to undertake the necessary investigations, potentially exacerbating the problem identified above. ■

Andrew Grant, partner, Clyde & Co

body of binding precedent exists. Interpretation of standard London market wordings (once translated into Arabic) falls to Arabic-speaking judges adopting their own approach to these important definitions.

Inevitably, the handling of claims was also subjected to a degree of political pressure driven by the desire of local regulators to influence the swift payment of claims in order to allow rebuilding to begin as soon as possible. In such cases the interests of local insurers were not always well-aligned with their international reinsurers.

The claims arising from the Arab Spring have focused the attention of domestic insurers (and the international reinsurers that support them) on the scope of previously-overlooked definitions and exclusions, as well as increasing the awareness among insureds as to what cover they are actually buying and whether they need more specialist cover for losses suffered during the tide of social and democratic reform that is engulfing the region. ■

Mark Beswetherick, partner, Clyde & Co

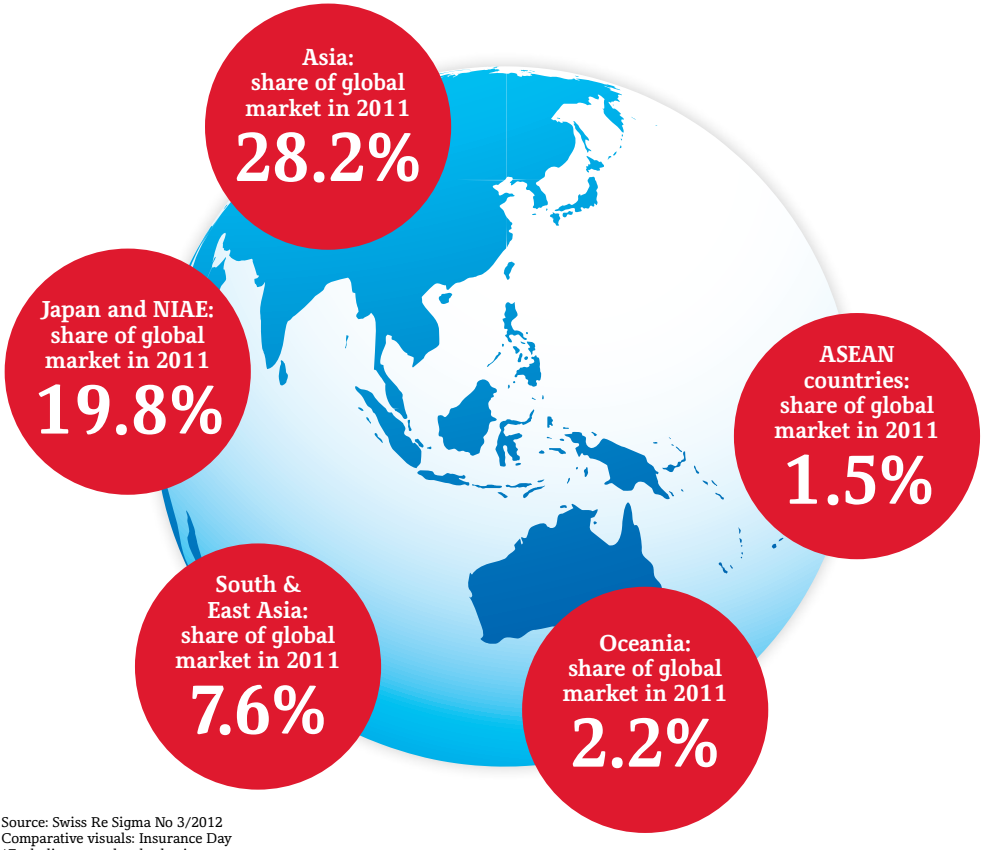
Asia-Pacific

Premiums as % of GDP*

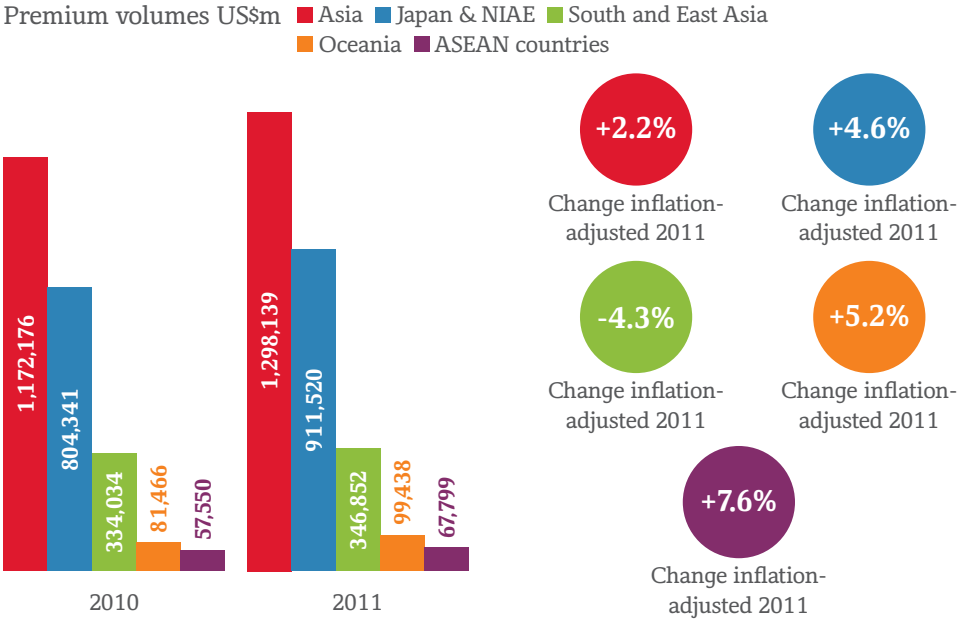
Asia 5.85%
Japan and newly-industrialised Asian economies (NIAE) 11.3%
South and East Asia 7.55%
Oceania 5.94%
ASEAN countries 3.06%

Premiums per capita in US$*

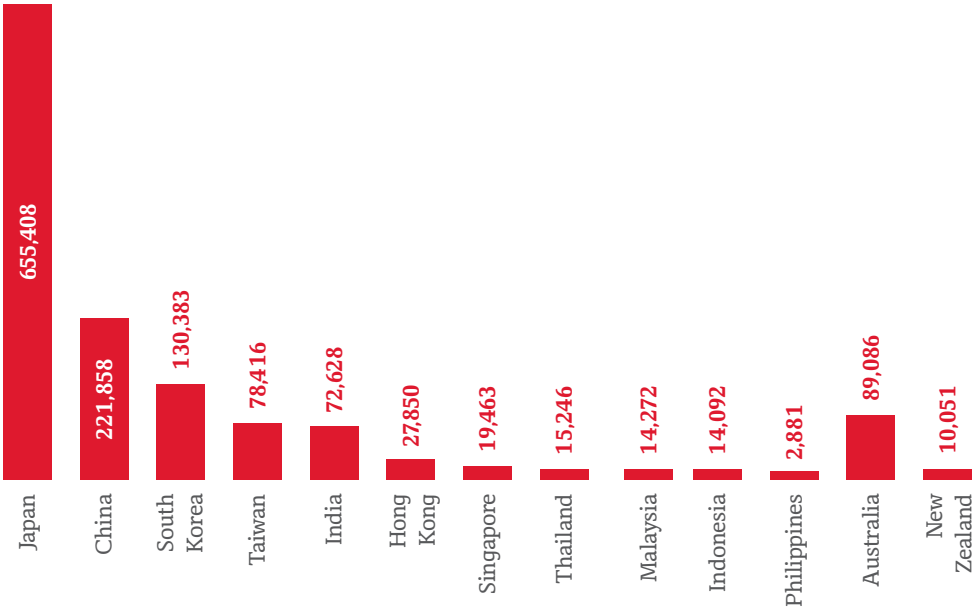
Asia 313.9
Japan and newly-industrialised Asian economies (NIAE) 4,297.8
South and East Asia 96.6
Oceania 2,759.2
ASEAN countries 122



Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business



2011 Asia-Pacific premium volumes by country US$m (estimated and provisional)



Thai floods: loss prevention one year on

A key focus for insurers and reinsurers is the question of whether insureds have complied with reasonable precautions obligations

It is over a year since the floodwaters of the Chao Phraya river drained from seven industrial estates in the Ayutthaya and Pathumthani provinces of central Thailand.

While the ensuing 12 months of recovery efforts have served to highlight a number of insurance and reinsurance coverage issues, one specific concern has been the obligation on insureds in certain circumstances to take reasonable precautions for loss prevention purposes.

As is well known, the Thai flooding was triggered by persistent rainfall during the period between July and October 2011, the meteorology of which involved combinations of monsoon precipitation, cyclonic activity, four tropical storms and Pacific La Nina conditions.

The pressure exerted on Thailand's flood infrastructure was immense: records from the Royal Irrigation Department of Thailand confirm that in June and July 2011 authorities released into the Ping River (a tributary of the Chao Phraya) a daily average of 4.5 million cubic metres of water from the Bhumibol Dam in north-western Thailand.

Given the continuing rainfall however, this daily average figure steadily increased through August (22 million cubic metres) and September (26 million cubic metres) to over 77 million cubic metres per day during the period October 1 to October 14 2011.

Scale in this context can be appreciated from the fact that a single cubic metre of water contains over 220 gallons. Releases on a roughly similar scale also occurred from the Sirikit Dam in north-eastern Thailand, over the same period.

Against this background the Chao Phraya river began to flood in Central Thailand in mid-September. Roughly adjacent as it was to the seven above-mentioned industrial estates, each estate – starting with Saha Rattana Nakorn on approximately October 4, and ending with Bangkadi on approximately October 19 – consecutively flooded during the said period.

The inundation lasted over 40 days, with over 1,300 factories affected, many of which manufactured precision electronic parts/equipment for global supply.

REASONABLE PRECAUTIONS OBLIGATIONS

While much has been written since about issues of aggregation, hours clause terms, underinsurance, concurrent causes and Orient Hotel-type wide area damage considerations (for BI purposes), the relevant insureds' reasonable precautions obligations have also increasingly come to the fore for insurance and reinsurance purposes.

Such clauses were commonly found in Japanese law material damage policies as issued to Japanese insureds with manufacturing facilities in Thailand. Those clauses classically (and very simply) required that the insured should take all reasonable precautions to prevent damage to the property insured.

As a matter of English law the requirement to take reasonable precautions for loss prevention purposes can only be breached where the insured has been reckless as regards the risk appreciated: simple negligence is not enough. In the context of Japanese law policies, by contrast, reasonable

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The stringency of loss prevention steps taken to minimise loss in the wake of the floods appears to have been variable

precaution obligations centre on Article 13 of the Japanese Insurance Act, which provides, inter alia, that an insured must attempt to prevent the occurrence, and/or expansion, of damage from an insured event upon appreciating the occurrence thereof.

This is largely reflected in the reasonable precautions contractual provisions referenced above.

Whether an insured's (in)actions meet or breach the applicable reasonable precautions requirement accordingly depends on various factors as a matter of Japanese law, including the level of peril appreciated, the relative ease of loss prevention and comparisons with loss prevention methods used by other entities faced with the same circumstances.

AVAILABLE INFORMATION

With the maturing of the Thai floods loss adjusting process, more information has progressively become available regarding the hydrology of the floods, the warnings issued, the circumstances of each estate's inundation and the steps taken by various entities to proactively minimise their losses in advance.

Certain manufacturers stripped their factories of components/stock and moved them to higher ground pre-flooding, given that the prospect of flooding was both evident and foreseeable: indeed it was the subject of repeated warnings to manufacturing concerns by both industrial estate owners and municipal authorities.

Notwithstanding this, the stringency of loss prevention steps taken to minimise loss (through removal of machinery, equipment and stock) appears to have been variable. This has inevitably given rise to coverage issues from both an insurance and reinsurance perspective, such that compliance with reasonable precaution obligations – where stipulated - has gradually emerged as a significant coverage factor in the Thai floods material damage context. ■

Nigel Brook, partner, Clyde & Co
Garrett Moore, partner, Clyde & Co

Asia Pacific market overview – Hong Kong

Regulation remains on the agenda in Hong Kong with the launch by the government of a consultation regarding the establishment of a new independent insurance regulator

The proposed regime is intended to align Hong Kong with international practice and prudential standards.

Legislation is intended to be introduced into the Legislative Council in 2013, with the new Independent Insurance Authority (IIA) taking over the insurance regulator role in 2015.

The proposed changes will significantly alter the regulatory environment, particularly for insurance intermediaries who are currently self-regulated.

Proposed changes will significantly alter the regulatory environment, particularly for brokers who are currently self-regulated

Important changes for insurance intermediaries will include the imposition of a standard of reasonable care and diligence (including "know your client" obligations) and making necessary disclosure of information, which is likely targeted towards disclosure of commissions by insurance brokers.

Proven misconduct or being not "fit and proper" could result in penalties of up to HK$10m ($1.3m). Insurers will also need to appoint responsible officers, who will be deemed to include the insurer's chief executive.

Meanwhile, insurers had until the end of January 2013 to notify the current Hong Kong insurance regulator, the Commissioner of Insurance of any current material outsourcing arrangements. Following the publication by the Commissioner of a guidance note on outsourcing, insurers must inform the regulator before entering into any material outsourcing arrangement.

DATA BURDEN

Insurers will bear a heavy burden over the next year or so in ensuring they comply with various obligations designed to protect personal data. Following an increase in consumer complaints, and a general heightened emphasis on the protection of personal information, the Hong Kong Privacy Commissioner has now issued a guidance note on the correct handling of consumer data by insurance companies.

Allied with this are important changes to the personal data/privacy legislation, which now impose serious fines and sanctions for misusing personal information, and criminal offences for the sale of such data.

The insurance industry will be affected shortly by two additional elements: (a) restrictions on the use of personal data for direct marketing – the insurance industry is waiting for regulatory guidelines to assist it to determine how severe the changes to their practices may need to be; and (b) the data user return scheme – which will require insurers (among banks and others) to file quarterly returns regarding their data privacy systems, controls, and compliance.

The proposed regime is intended to align Hong Kong with international practice and prudential standards

PRODUCT DEVELOPMENT

On the product development side, the Hong Kong market is placing a great deal of emphasis (as is the Asian region as a whole) on cyber cover, designed to meet the insurance needs of the technological age.

Products cover third party claims for breaches of privacy, disclosure of personal data; and first party claims which arise from hacked security and computer systems, loss of data, damage to computer infrastructure, among others. This form of cover is in its nascent stage, but the market is recognising its potential for growth as a new form of insurance in the region.

The regularity of US securities class actions against Chinese companies which have listed on NYSE or NASDAQ continues to create real exposures for the insurance market, and also presents claims handling issues which are complex and commercially sensitive.

The latest trend is that the raft of such claims appears now to be leading to many US-listed Chinese businesses seeking to delist, or privatise – which is only giving rise to further securities class actions in the US in the M&A context, commonly alleging breach of fiduciary duty by the company controllers for approving transactions potentially or arguably at undervalue.

It appears that some of these Chinese companies will be the target of class actions at both ends of the listing process. ■

Simon McConnell, partner, Clyde & Co
Mun Yeow, partner, Clyde & Co

Spotlight on Singapore

Data protection laws, claims against directors and officers and revised corporate governance guidelines will be among the main issues on insurers' radars over the next 12 months

The Personal Data Protection (PDP) Bill was approved in October 2012. This provides one source of data protection laws in Singapore whereas previously the law was scattered over 150 different provisions in different acts.

A number of developments include the establishment of a Personal Data Protection Commission (DPC), and the broadening of the definition of personal data to include electronic, as well as non-electronic, data.

Importantly, the PDP Bill intends to impose a number of fines and enforcement mechanisms against individuals, companies and their directors and officers. It is intended that the DPC will be able to issue directions to ensure compliance with undertakings made by private organisations, settlements with wronged consumers and it will be able to prosecute offending private organisations, depending on whether the breach arises under any other applicable legislation. Currently there are no express notification requirements but it is likely to be a feature of directions issued by the DPC. The PDP Bill will come into force during 2013.

As a result of the impending data protection legislation and as hacking and cyber crime increases there is an emphasis on new cyber products in the Singapore insurance market. Cyber products are being launched to cover first party losses such as restoration of corrupted or stolen data and third party losses such as claims relating to privacy breaches.

D&O ACTIONS EXPECTED TO RISE

There has been an increase in the number of claims against directors and officers due to the ongoing tweaking of company regulation and a trend towards bringing civil proceedings in this area. We expect an increase in actions brought by regulators following the recent and high profile decision of *Madhavan Peter v Public Prosecutor* [2012] SGHC 153. New personal directors and officers products are being developed and sold in the Singapore market to avoid any doubt about cover for future claims when the company ceases to maintain insurance.

The regulator, The Monetary Authority of Singapore (MAS) proposes to extend the application of the Insurance (Corporate Governance) Regulations and the MAS guidelines on corporate governance for banks, financial holding companies and direct insurers. Currently, only "significant insurers" are included in the corporate governance regulations which apply to direct life insurers, incorporated in Singapore with assets of at least S$5bn ($4.1bn). The proposed amendments will place emphasis on corporate governance and will have an impact on who can and cannot hold directorships in the regulated insurance companies.

In respect of corporate developments there continues to be investment by insurance companies in Singapore, some moving from the Hong Kong market into the Singapore market as capacity increases.

The marine insurance market has seen a steady increase in premiums as more shipowners move their operations to Singapore. A number of P&I clubs have intentions to set up new branch offices in Singapore in early 2013 to meet the increase in demand for further capacity in the market. ■

Melissa Russell, senior associate, Clyde & Co

Australia overview

The Australian insurance and reinsurance industry, along with many Australian communities and businesses, is still recovering from recent natural disasters

Natural disasters included the Queensland floods, cyclones Larry and Yasi, the Victorian and Tasmanian bushfires and, for many Australian insurers, the effects of the New Zealand earthquakes. These events have brought about some significant changes intended to better prepare both insurers and insureds in the event of future disasters. For example, a standard definition of flood for all insurance policies is now Australian law.

In far north Queensland, insurers have been forced to lift premium prices to provide sufficient capital funds to cover the risk of future catastrophes.

For products such as residential strata (building) insurance, the combination of increased premiums and falling property prices is said to be contributing to the unaffordability of strata unit properties in far north Queensland.

In New Zealand, the situation remains complicated following the earthquakes which struck Christchurch in 2011. This has also had a significant impact on Australian insurers and reinsurers.

New Zealand's earthquake commission has been handling claims but it is still expected to be a long time before the claims process will be resolved. Insurers have been faced with issues such as inadequate or poor policy wording, miscalculation of risks including business interruption loss issues, inappropriately priced deductibles and an overall lack of understanding of the rebuilding or repair process.

SECURITIES CLASS ACTIONS

The threat of securities class actions continues to be a risk for insurers in Australia. 2012 saw the largest Australian class action settlement ever reached in the Centro matter for A$200m ($210m).

The litigation funder behind the class action confirmed it would be receiving A$42m from the settlement. The Australian government confirmed its support for the litigation funding of class actions, by enacting legislation in July 2012 which confirms that litigation funders are not required to hold Australian Financial Services licences as managed investment schemes.

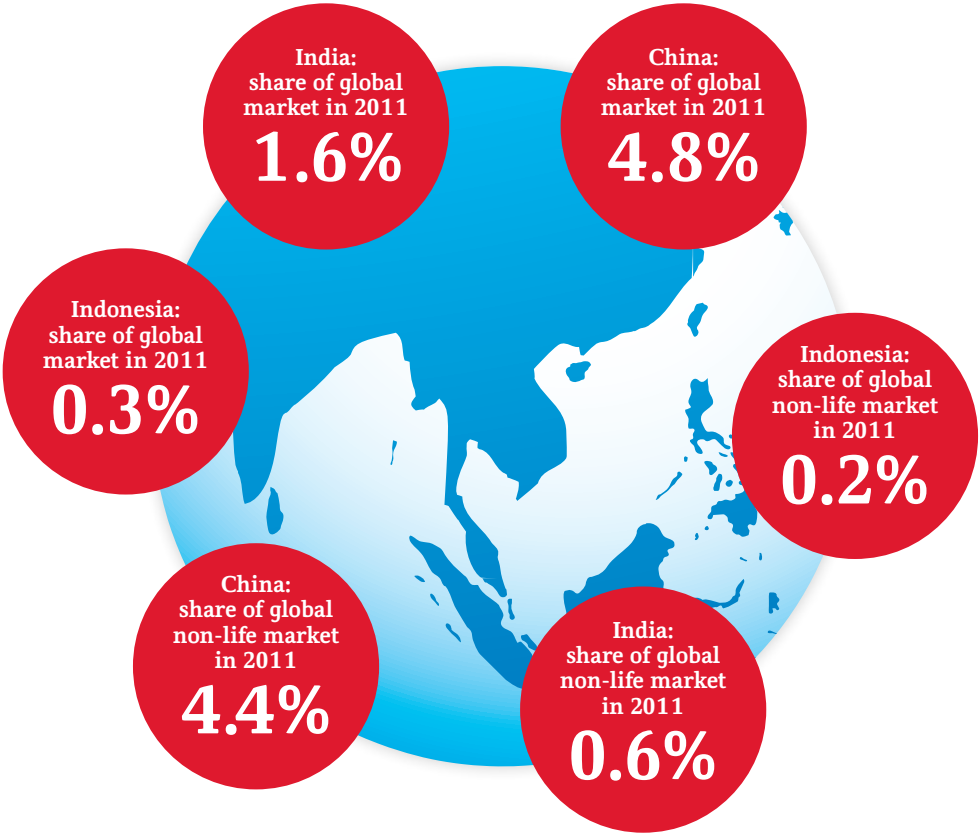
Australia is yet to have any final judgment in this area meaning that complex and important questions of causation and damages in relation to securities class actions remain uncertain, presenting an obvious risk to insurers.

For D&O insurers, the decision by the New Zealand Court of Appeal in December 2012 to overturn the High Court's *Bridgecorp* decision will be welcomed. The Court of Appeal disagreed with the lower court that Section 9 of the Law Reform Act 1936 (NZ) operated to prevent directors from being paid defence costs under D&O policies to ensure funds were preserved to pay any settlement to the plaintiff in the proceedings. This was a concern for Australian insurers because of similar legislation which exists in Australia and pending the appeal, some insurers had been proactive about developing companion policies to provide certainty on D&O costs and expenses.

Another significant court decision is the recent Federal Court landmark decision against Standard and Poor's and ABN Amro concluding that S&P's AAA rating of financial products constituted misleading and deceptive conduct and was negligent to investors. The funder of the litigation has said that it is looking to commence similar proceedings in Europe and the US. ■

John Edmond, Partner, Clyde & Co

Emerging markets



Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business
Inflation-adjusted premium growth/decline is in local currency

Premium volumes US$m India Indonesia China

-2.4%
Change nominal 2011

-5.5%
Change inflation-adjusted 2011

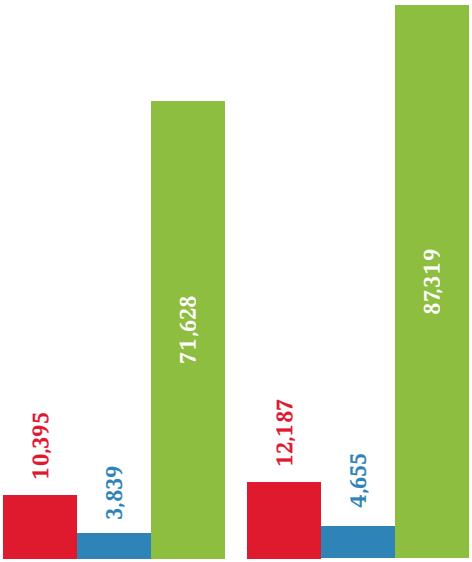
+21.6%
Change nominal 2011

+11.7%
Change inflation-adjusted 2011

+3.4%
Change nominal 2011

-6.4%
Change inflation-adjusted 2011

Non-life premium volumes US$m India Indonesia China



+17.2%
Change nominal 2011

+13.5%
Change inflation-adjusted 2011

+21.2%
Change nominal 2011

+11.3%
Change inflation-adjusted 2011

+21.9%
Change nominal 2011

+10.4%
Change inflation-adjusted 2011

Emerging insurance market overview – China

Following the appointment of a new chairman, the Chinese supervisor has committed to further regulatory reform of what is already the world's sixth largest insurance market

As one of the fastest-growing economies, China saw its premium income reach CNY1.434trn ($229bn) by the end of 2011. In addition, total assets in the insurance sector amounted to approximately CNY6trn by the end of 2011.

According to the China Insurance Regulatory Commission (CIRC), which is authorised by the State Council of China to regulate the insurance market, there were 10 insurance groups, 130 insurance companies and 11 insurance asset management companies in the market as of December 31, 2011. Of those, 54 were foreign-invested insurance companies (defined as an insurance company with foreign shareholding of 25% or more), which however only had a collective market share of 3.1%. The top five foreign-invested insurers in the P&C sector are Chartis, Liberty Mutual, Tokio Marine, Mitsui Sumitomo Insurance and Samsung Insurance. On the life side, the top five foreign-invested life insurers are AIA, Generali, Aviva-Cofco, Citic-Prudential and MetLife.

This change in policy is expected to become a significant engine for the growth of foreign-invested P/C insurers in China

Market concentration is high. In 2011, the market share was 74.4% and 72.7% for the top five P&C insurers and life insurers respectively.

The dominant position of motor insurance in China's P&C sector remains unchanged, which accounted for 73.3% of the P&C market in 2011.

From May 1 2012, foreign-invested insurers have been permitted to write compulsory motor third-party liability insurance (CMTPL). At the time of writing, Chartis, Liberty Mutual, Allianz, Samsung Insurance, Hyundai Insurance and Cathay Insurance appear to have been approved by the CIRC to write CMTPL. This change in policy is expected to become a significant engine for the growth of foreign-invested P&C insurers in China.

STEPS TAKEN BY THE CIRC

On the other hand, following the appointment of its new chairman in October 2011, the CIRC has committed to further regulatory reforms in the insurance sector. This was reflected by a series of guidelines and circulars issued by the CIRC in 2012.

In March 2012, the CIRC announced it was suspending the granting of new licences for insurance intermediaries with a few exceptions. This has been commented on as transforming the Chinese insurance intermediary market by increasing the market entry thresholds. At the same time, the CIRC has made it clear that the establishment of insurance intermediary groups and insurance agencies and brokers with strong financial capacity is still encouraged.

The CIRC also intends to establish a less stringent regulatory environment in relation to the

Foreign-invested insurers have been permitted to write compulsory motor third party liability business

utilisation of insurance funds. During the six months from May to October 2012, the CIRC issued nine new rules and circulars on the utilisation of insurance funds.

Those rules cover various aspects of insurance funds utilisation such as asset allocation, entrusted investment, investment in bonds, overseas investment and derivative products etc.

In addition, the CIRC has also indicated that it has been working on the second generation of the solvency framework with a view to bringing its solvency regulation on a par with its international counterparts. It is the CIRC's intention to implement the regulations on the new solvency framework in 2016.

It is also worth noting that the CIRC has recently approved China National Petroleum Corporation (CNPC) to establish an onshore captive insurance company in China. This will be the first captive insurer in China. Since the PRC Insurance Law has no specific provisions on captive insurance companies, it remains to be seen how the regulation and supervision of the operation of this type of insurance company will work in practice. ■

Carrie Yang, partner, Clyde & Co

Emerging insurance market overview – India

It remains to be seen whether the ruling coalition, which does not have a majority in the Upper House, is able to garner enough support to push through the ambitious reforms contained in the Amendment Bill

The global insurance market has been tracking the Indian insurance sector with interest and anticipation since it was opened up to foreign direct investment in 2000. Not only is the India story enthralling, but low penetration and a large population presents a huge potential opportunity. However, India appears to be trying hard to attract FDI (foreign direct investment), while remaining sceptical of it. This is reflected clearly in the policy flip-flop of various governments. Successive governments have acknowledged the need for further reforms but have lacked the political will to implement them.

Parliament is due in February to consider a bill (the Amendment Bill) that proposes to usher in significant changes to the current insurance laws and framework, and is intended to foster much needed further growth in the insurance industry.

The Amendment Bill proposes to allow foreign investors to hold up to 49% of the capital in an Indian insurance company, an increase from the current levels of 26%. It also paves the way for nationalised general insurance companies to raise funds from the capital markets.

The Amendment Bill provides for appeals against decisions by the industry's regulator, the Insurance Regulatory Development and Authority (IRDA). One of the most significant provisions is the inclusion of Lloyd's within the definition of a foreign company; thereby opening the doors for Lloyd's to enter India.

The mandatory requirement for Indian promoters of an insurance company to reduce their stake to 26% within a period of 10 years is also proposed to be dropped. More broadly, the Amendment Bill proposes to permit a policyholder to completely assign all rights under the policy to a third party subject to conditions and prescribes stricter penalties for insurers that fail to meet social sector obligations (insurance products for poor rural communities).

RIGOROUS ENFORCEMENT

On the regulatory front IRDA, which is now over a decade old, has recently tried to expand its canvas by bringing several unregulated players within its supervision and ambit.

IRDA is also enforcing insurance regulation in a more rigorous manner than ever before. Bancassurance and health insurance are the areas where more flexible guidelines are expected while IRDA is expected to be more stringent on issues surrounding product pricing and design. Restrictions on non-admitted insurance, statutory and regulatory ceilings in commissions, brokerages etc., regulation of reinsurance are particular areas that stakeholders must watch out for.

It remains to be seen whether the ruling coalition, which does not have a majority in the Upper House, is able to garner enough support to push through the ambitious reforms contained in the Amendment Bill.

While, the going has been good since the sector opened up, there is an urgent need to further capitalise Indian insurers. Indian joint venture partners do not seem to have an appetite for further capital infusion. Accordingly, were the Amendment Bill not passed by the Indian parliament it will be equivalent to an own goal – completely self-defeating. ■

Sakate Khaitan, partner, Clasis Law

Emerging insurance market overview – Indonesia

Indonesia's demographics, economic growth and impressive increase in new premiums written look likely in 2013 to sustain the attention of major global players

The Indonesian insurance sector continues to go from strength to strength. Despite the promise of reforming Myanmar, and Thailand's announced desire to promote that country as ASEAN's insurance center, Indonesia is the South-east Asian market of the moment.

Driven by economic growth rates averaging over 5% during the last five years and a middle class numbering 30 million out of 242 million, Indonesians are a significant target for foreign players and local heavyweights, such as Bank Central Asia.

In Asia, life insurance premiums are annually increasing at 11%, five times faster than in Europe and the US. Indonesia's year-on-year growth numbers range from 15.5% (all lines by value - 1H/2012), 37.1% (life total revenue - 1Q/2012), and 100% (all lines by premium – projected 2012 for one global giant). Rating agency Fitch, however, notes the Indonesian insurance industry is "tempered by limited institutional transparency, public disclosure, and risk management".

The insurance supervisory functions of BKPM-LK, the capital markets and financial services supervisory authority, are transitioning to a new financial regulator, the Otoritas Jasa Keuangan (OJK).

Observers expect the OJK's approach will be characterised by continuity, not change. The OJK is formed out of the existing insurance, capital markets and finance company divisions of BKPM-LK and the bank supervisory functions of the central bank, Bank Indonesia. Recent moves by the new regulator to impose annual fees on financial institution assets, viewed by participants as too high, have left finance professionals in Jakarta wondering if further change is in store for financial institutions. Political maneuvering will surely increase in the run-up to the 2014 national elections; a close watching brief is needed for both current insurance regulation and political attitudes to possible future regulation.

NEW LICENSES

New insurance licenses are difficult to come by. BKPM-LK, the predecessor regulator, appeared to view the Indonesian insurance sector as including too many small, often essentially dormant, players.

A 250% increase in minimum capital requirements from 2010 to 2014 partially addresses this concern by driving mergers. Similarly, restricting new licenses looks to evidence a policy that new entrants should be steered to investment in local companies, and not seek to establish new platforms. In addition, foreign equity investment remains limited to a maximum of 80% which suggests new foreign entrants will need to engage with local partners going forward.

Nevertheless, these facts emphasise the importance of careful legal due diligence when investing, and the need for sound governance, reporting and control structures going forward.

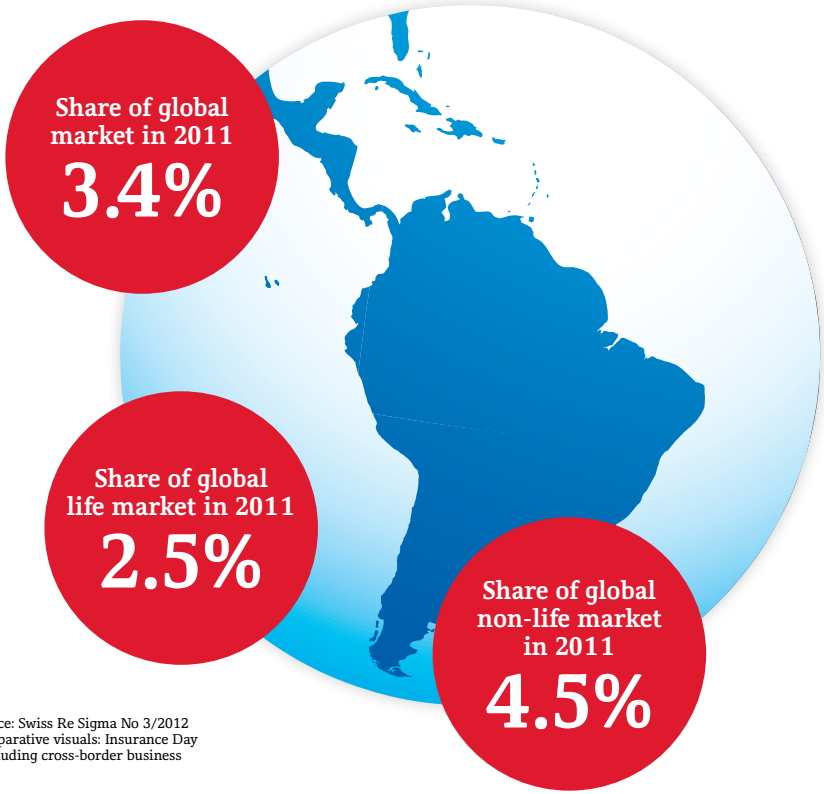
The new Social Security Agency aimed to increase its office network by more than 300% by the end of 2012, and is entering partnerships with the national Post Office system and several state banks. These promise to become formidable distribution channels and private insurers may well benefit by placing products through the new agency and such channels. ■

Michael Horn, partner, Clyde & Co

Latin America

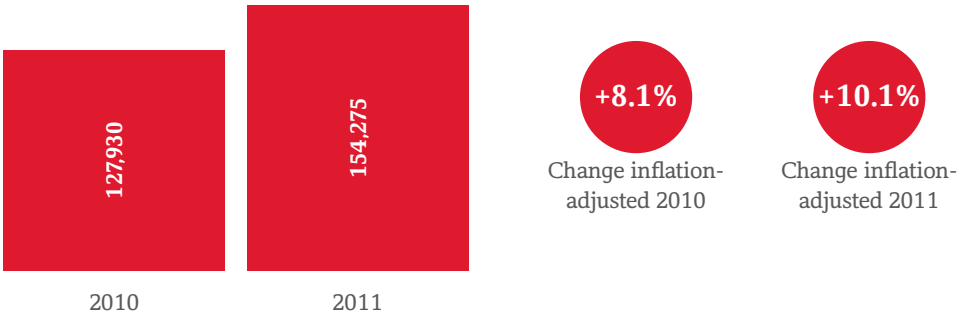
Top 10 Latin American markets in 2011
(Insurance penetration: premiums* as a % of GDP)

1. Chile (4.1%)
2. Venezuela (3.4%)
3. Panama (3.4%)
4. Brazil (3.2%)
5. Argentina (2.9%)
6. Colombia (2.3%)
7. Costa Rica (2%)
8. Ecuador (2%)
9. Mexico (1.9%)
10. Uruguay (1.8%)

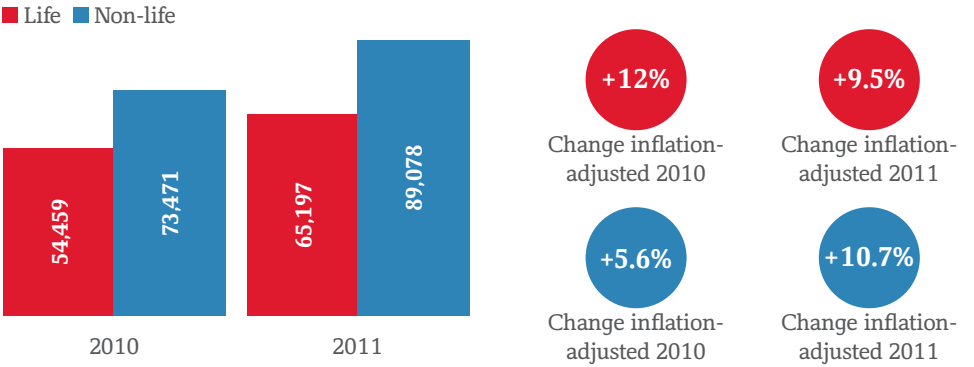


Source: Swiss Re Sigma No 3/2012
Comparative visuals: Insurance Day
*Excluding cross-border business

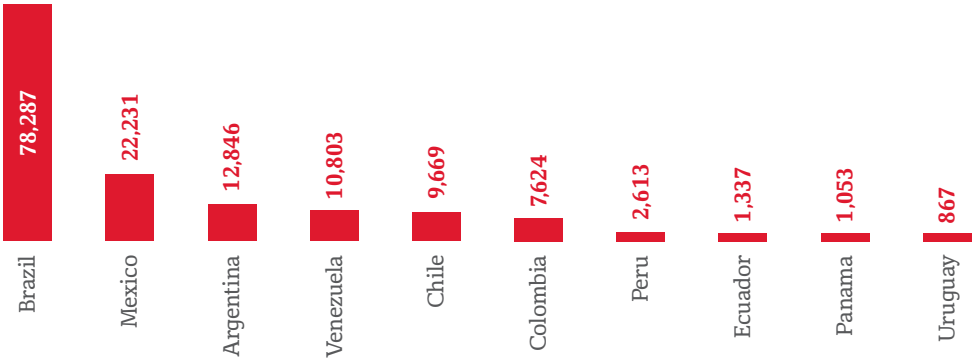
Latin America and Caribbean premium volumes US$m



Latin America and Caribbean life and non-life premium volumes US$m



2011 Latin America premium volumes by country US$m (estimated and provisional)



Sustained growth in Latin America

For the South American market, the buck, or a large proportion of it, now stops at home when it comes to its burgeoning insurance and reinsurance markets. Is this trend to continue, and if so how and to what extent?

Driven by the abundance of natural resources such as oil, gas and ore deposits, infrastructure investment and the expansion of a consumerist middle-class, most South American countries are in the midst of a sustained period of growth.

This is reflected in a burgeoning insurance and reinsurance market. This growth has many of the hallmarks of a significant tilt in the geographic centre, or centres, of gravity of that market.

Within the global insurance market it is capital that ultimately speaks loudest and the changing nature of the South American market can be seen in both the inflow and outflow of capital.

The increase in the inflow of capital is reflected in both (i) the growth in overall premiums written and (ii) the decrease in the ratio of premiums ultimately ceded to the international market. The detail of that inflow of capital is a statistical exercise best discussed elsewhere.

However, the changes in the market are already reflected in the outflow of capital by way of the management and payment of losses. Where large losses no more than a decade ago were the exclusive preserve of international reinsurers, it is now commonplace for the markets on such losses to be a mixture of international and domestic/regional players.

REGIONAL BREAKDOWN

It is too simplistic to view the region as a composite whole. For the purposes of this review we see three broad groupings as follows:

- Brazil *(see also page 56)*
- The fast-growing "Andean" countries of Chile, Colombia and Peru
- "None of the above"

With Brazil, Chile, Colombia, Venezuela and Argentina being the five largest economies of South America, but crossing each of these categories, the groupings do not correlate to scale. Rather, deeper themes have to be considered.

Brazil is an economic powerhouse but remains somewhat economically isolated from the balance of the continent, partly due to the sheer size of its domestic markets and partly due to cultural (especially language) and historical reasons.

The Brazilian insurance market is in the midst of a profound change, marked not only by an influx of foreign capital and the large international underwriters setting up operations, but a growth in the domestic players.

What seems clear however is that the Brazilian market is destined to be large enough to stand on its own.

While involvement from the international market will continue, it already increasingly means that "the buck stops here" for some of the capital at risk for claims. With the expansion of domestic and international underwriting capital inwards this trend is likely to continue.

"ANDEAN" GROUPING

The countries in the "Andean" grouping are diverse but each is marked by an increase in economic and political stability and broadly open markets.

For example Chile is 39th in the World Bank's "Ease of doing business" rankings, Peru 41st and Colombia 42nd – contrast this with Brazil's position at 126th.

While the majority of the ultimate capital for current claims within this grouping remains from the international markets, the ratio with domestic capital has slowly but consistently shifted towards domestic underwriters retaining more of the ultimate risk.

How far that trend will develop and the future direction of the wider "Andean" grouping is less clear. It seems unlikely that any of them individually has a large enough market to generate sufficient capital to support an internal market like Brazil.

In the absence of one of the grouping becoming a leader across this region, the alternatives are either for a continued lead role of the international markets (with the Spanish underwriting giants having a cultural and historic advantage) or of Brazil shaking off its historic insularity and seeking to become the leader of a truly pan-South American market.

"NONE OF THE ABOVE"

Finally, the "none of the above" grouping. It is not easy to categorise markets as diverse as those of Uruguay (successful, stable but small), with those of Argentina and Venezuela (with their sometimes challenging and uncertain legal and regulatory framework).

This grouping also takes into account the more isolated economies of Ecuador, Bolivia, Paraguay and the smaller nations and islands on and off the Eastern Caribbean coast.

What is a consistent feature, however, is that the ultimate capital for current claims remains almost exclusively from the international markets, but the response to, and management of, losses needs to have a heavy domestic flavour.

The countries in the "Andean" grouping are marked by an increase in economic and political stability and broadly open markets

In respect of the future direction of these markets perhaps the only likely outcome is that they will be carried by any wider tide within the continent but each will retain their own idiosyncrasies. Any attempt at wider characterisation is fraught with uncertainty.

The international market has to be alive to these changes, and competition, when seeking to market products and in the management of claims. For instance, current assumptions as to the mechanics of claims control and cooperation provisions may need to be reconsidered in light of the broader spectrum of interests. ■

Peter Hirst, partner, Clyde & Co
Lee Bacon, partner, Clyde & Co

Insurance and reinsurance opportunities in Brazil

The sector is expected to continue to grow, although there are a number of hurdles to foreign penetration

There has been talk for some time about opportunities for foreign insurers and reinsurers in Brazil.

Brazil is currently the world's seventh largest economy in the world and the government's growth acceleration programme is set to inject a further $878bn into the country's infrastructure in the next few years.

The recent discovery of sub-salt oil reserves off the coast of Sao Paulo and Rio de Janeiro state (and perhaps some high-profile pollution incidents) will only further increase this growth potential.

Insurance penetration rates, which were traditionally low, have now risen to around 7.5% of the country's gross domestic product according to some estimates and by 2020 the insurance industry is expected to be worth around $144bn.

Brazilian banks are increasingly keen to offer insurance products – especially life and accident policies. Brazil's largest bank, Banco de Brasil, recently announced the creation of a separate insurance and pensions unit, to be listed in 2013.

As a result of all this, the market continues to attract foreign insurers and reinsurers. What hurdles might they face?

REGULATORY CHALLENGES

The country's sometimes challenging regulatory environment has been well-reported. For example, in 2010, local insurers generally were required to offer a right of first refusal of 40% of each reinsurance cession to domestic reinsurers. The government introduced further changes in 2011, and this cession then became obligatory.

Cessions to foreign "occasional" reinsurers are also limited to 10% of the insurer's portfolio. Furthermore, only Brazilian companies can operate in the domestic market.

Nevertheless, there is nothing to prevent those companies being foreign-owned. It should be noted, though, that a foreign company wishing to hold control of a Brazilian insurer must be registered with SUSEP (the Superintendant of Private Insurance) which supervises and controls the Brazilian market, or must be a holding company whose exclusive purpose is the ownership of companies authorised to operate by SUSEP.

The reinsurance market was opened up in 2007, although foreign reinsurers need a licence to operate there. It is understood that the regulator is considering further easing (or at least clarification) of reinsurance regulation.

Policy wordings must be provided or approved by SUSEP. It is possible for SUSEP to require changes to be made to the wordings – something which no doubt comes as a surprise to London market insurers and reinsurers. However, reinsurance wordings are not subject to regulatory approval (although there are some mandatory clauses; for example a requirement that Brazilian law and jurisdiction will apply if the risk is located in Brazil – notwithstanding that the reinsurance policy may be placed in England).

There is virtually no reinsurance case law in Brazil (and no courts specialising in insurance and reinsurance), and hence there is a need for clear contractual drafting to ensure that the policy accurately and expressly reflects the intentions of the parties. ■

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