Insurance & Reinsurance Law & Regulation

Jurisdictional comparisons **First edition 2014**

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THE EUROPEAN LAWYER REFERENCE

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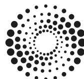

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Foreword

Clive O'Connell, Goldberg Segalla Global LLP

Insurance is about the spreading of risk. Ever since Lombard merchants introduced marine insurance in 1200 or Icelandic farmers formed themselves into a mutual later that century, the risk of one has been spread across many.

Of course, sharing risk among people exposed to the same peril does not always work. Accumulation of risk in one geographic area or some other similarly exposed grouping simply magnifies the problem. It was for this reason that reinsurance was born in the fourteenth century in order to allow greater diversification of security and of risk. Risks crossed frontiers, often on a reciprocal basis. A calamity in one place was resolved from the purses and pockets of strangers from far away.

As much early insurance and reinsurance was based upon international trade, the growth of insurance and reinsurance has always been international and the geographic sharing of risk has allowed economies to flourish or, at least, has prevented them from an even earlier demise.

Insurance and reinsurance are not the sole preserves of capitalism. Socialist countries, for example, have used the world's reinsurance markets to protect their macroeconomic interests. Even North Korea used to reinsure itself around the world until sanctions denied it protection. Countries in the former Soviet bloc used reinsurance not merely to protect themselves, but as a way to earn "hard" currency. Often they did so only to find that claims had to be paid in hard currency as well.

The global economy is growing and is becoming ever more interconnected. With the growth in economies, the need for insurance grows as well. Whereas, in the early 1980s, the USA accounted for around 40 per cent of the world's insurance premiums, that figure has fallen to under 25 per cent today while, at the same time, US premiums themselves have continued to grow.

Insurers have also tended to become larger. As global enterprises have consolidated and grown, their need for ever larger insurers has increased. These larger insurers, in turn, need larger reinsurers to protect their capital.

New markets are developing around the world. As they do so, established insurers are often seeing their opportunities for growth there rather than in established and over-competitive locations.

As economies expand, insurance is required in new areas, both geographically and conceptually. New forms of risk are emerging and insurers are struggling to apply old forms of cover to them, often restricted in what they can do by regulatory regimes.

Insurance does not merely follow but can be used as a tool to assist development. Microinsurance schemes are being established, often

in conjunction with microfinance, to help create a middle class and a sustainable economy in poorer countries, and to allow them to develop beyond subsistence. Takaful is being developed to give access to risk sharing to millions of devout Muslims, who make up a significant proportion of the world's population, often in areas undergoing some of the fastest economic growth, and who would otherwise have no recourse to cover.

The insurance and reinsurance industry, however much it may be growing, is still dwarfed by the capital markets. Following the global economic downturn and the combined effects of a number of natural disasters, a need emerged for non-correlated security to protect insurers. At the same time, capital, lacking opportunity elsewhere, was available. As economies have recovered, the capital has remained, and now it is clear that insurance-linked securities are not a temporary trend but a significant change in the way that insurers protect themselves and that capital markets interact with them.

As capital markets become familiar with and develop an appetite for risk transfer, the issue arises as to what extent they will still require the intervention of insurers or whether they might be better suited to providing new solutions to those requiring protection directly. The ability of capital markets to innovate within the confines of their regulatory framework could present the greatest challenge yet to insurers.

Regulators are bound by the limits of their jurisdiction. Those that they regulate and those they protect operate on a broader, often global, scale. Cooperation between regulators is required for fear of loopholes emerging between them which could be exploited by those without good faith.

The international nature of recent developments, adding to an already global industry, presents challenges not only to regulators, but also to legal systems. Principles of insurance law, developed from cases surrounding eighteenth- and nineteenth-century ocean voyages, where cargos were carried on sailing ships, are now being asked to respond to quasi-financial instruments protecting satellite launches.

Often the transaction will be reflected in a number of documents involving parties in a variety of jurisdictions and subject to different forms of regulation.

Existing laws and regulations are being tested. It is too early to say whether they will pass these tests, but all concerned must be aware of the issues that they face.

To aid this process, we have brought together leading insurance lawyers from around the world to ponder and opine upon some of the challenges the insurers and their lawyers and regulators will face in the coming years. The questions considered in this book will be asked for many years to come.

Gibraltar

ISOLAS
Peter Albert Isola & Christian James Caetano

1. WHAT RISKS MUST BE INSURED?

1.1 What are the compulsory classes of insurance?

Gibraltar is a self-governing British Overseas Territory and enjoys special status within the EU. Under Article 299(4) of the EC Treaty, it is within the EU by virtue of being a European territory, the external relations for which the UK is responsible; however, Article 28 of the UK Accession Treaty 1972 specifically excludes Gibraltar from the Common Customs Tariff, the Common Agricultural Policy and the harmonisation of turnover taxes, in particular value added tax. Subject to these exceptions, Gibraltar is subject to all EU legislation, having successfully transposed all pending EU Directives. This means that all EU Insurance and Reinsurance Directives currently in force have effect in Gibraltar, including those relating to compulsory insurance.

Third party motor liability insurance cover is compulsory in Gibraltar pursuant to the Insurance (Motor Vehicles) (Third Party Risk) Act 1986 (the Third Party Act). Under the Third Party Act, it is unlawful for a person to use, or to cause or permit any other person to use, a motor vehicle on a road unless there is in force, in relation to the use of the vehicle by that person or that other person, as the case may be, such a policy of insurance in respect of third party risks as complies with the requirements of the Third Party Act. In the case of a vehicle which is registered in Gibraltar, the policy of insurance must be a policy issued by an 'approved motor vehicle insurer' as defined in the Third Party Act. An approved motor vehicle insurer means an insurer that is authorised to carry on motor vehicle insurance business under the Financial Services (Insurance Companies) Act (the 'ICA') and is a member of the Motor Insurers' Bureau of the United Kingdom. In the case of a vehicle which is normally based in a territory (other than Gibraltar) of a member state or of a relevant foreign state, then that policy must comply with the relevant laws of that state.

Professional indemnity insurance is another compulsory class of insurance for professional service providers such as solicitors, accountants, investment advisors and insurance intermediaries. These policies would typically cover incidents of professional negligence, breaches of duties of care, loss of customer monies and breaches of confidentiality or liability resulting from the loss of customer documents. In the case of solicitors admitted to practise in Gibraltar, every solicitor is required under the Solicitors' (Practising Certificates) Rules 2005 to take out and maintain professional indemnity insurance in the minimum sum set by the Chief

Justice of Gibraltar from time to time by notice in the Gibraltar Gazette. As of 1 May 2014, this amount shall be deemed to be £1,000,000 for each claim and in the aggregate. Larger law firms may, however, maintain a level of cover far in excess of this to reflect the risk associated with higher value and complex instructions.

The Financial Services (Investment and Fiduciary Services) Act 1989 (the 1989 Act) makes provision for the licensing of, *inter alia*, insurance and reinsurance intermediaries by Gibraltar's statutory financial services regulator, the Gibraltar Financial Services Commission (FSC). Under the 1989 Act, any intermediary conducting (re)insurance mediation business in or from within Gibraltar shall, on a permanent basis, hold professional indemnity insurance (or some other comparable guarantee against liability arising from professional negligence) valid throughout the European Economic Area for at least 1,000,000 (or sterling equivalent) applying to each claim and in aggregate 1,500,000 (or sterling equivalent) per year for all claims (unless such insurance or comparable guarantee is already provided by an insurance undertaking, for example, on whose behalf the intermediary is acting). Fiduciary services firms, also licensed under the 1989 Act, require professional indemnity insurance as part of their authorisation by the FSC. This is a statutory requirement provided by the Financial Services (Conduct of Fiduciary Services Business) Regulations 2006 (subsidiary legislation made under the 1989 Act). A licensee under the 1989 Act in possession of a Company Manager or Professional Trustee Licence shall, so far as such insurance is reasonably available, have a minimum cover of £500,000 or £1,000,000, respectively, or their equivalent in another currency.

Under Gibraltar law, the Provision of Services Regulations 2010 (the Services Regulations) gives effect to Directive 2006/123/EC on services in the internal market (the Services Directive). Article 23 of the Services Directive provides that member states *'may require providers whose services present a direct and particular risk to the health or safety of the recipient or a third person, or to the financial security of the recipient, subscribe to professional liability insurance appropriate to the nature and extent of the risk, or provide a guarantee or similar arrangement which is equivalent or essentially comparable as regards its purpose'*. Despite the wording of the Services Directive being optional, Gibraltar transposed this particular requirement affirmatively, thereby placing an obligation on applicable service providers to obtain professional liability insurance appropriate to the nature and extent of the risks of their business (with financial services and other certain activities being excluded). The type of 'services' caught by the Services Regulation apply to any self-employed economic activity normally provided for remuneration as referred to in Article 57 of the Treaty on the functioning of the European Union, which are set out in the Treaty as activities of an industrial, commercial and professional character.

Compulsory insurance classes can also be found in more obscure sectors, such as that of merchant shipping and maritime pollution. In Gibraltar, it is a requirement to have insurance against liability for pollution in prescribed

circumstances under the Merchant Shipping (Oil Pollution) Regulations 1999. These Regulations generally stipulate that ships may not enter or leave the port of Gibraltar, or arrive at or leave any terminal in the territorial sea of Gibraltar, unless they possess a certificate showing that there is in force in respect of the ship a contract of insurance or other security satisfying the requirements of Article VII of the Liability Convention (cover for owner's liability). Furthermore, the Gibraltar Merchant Shipping (Insurance for Maritime Claims) Regulations 2012 requires owners of ships entering the port of Gibraltar, or operating in British Gibraltar Territorial Waters, to have insurance covering that ship.

1.2 Who must they be insured with?

1.2.1 Locally admitted insurers

Although there is no definition of 'non-admitted insurers' in Gibraltar law, the ICA states that, subject to certain exceptions, no person shall conduct insurance business in Gibraltar except under a licence issued under the ICA. In terms of the exceptions, these include insurers licensed elsewhere in the EEA and underwriting members of Lloyds. Under the ICA, Gibraltar-based insurers must be licensed under the ICA by the FSC in a class (or part of a class or group of classes) of insurance business.

1.2.2 Foreign insurers

EEA insurers may also carry on business in Gibraltar under the principle of freedom of services or by way of establishment, provided that they satisfy EU 'passporting' requirements. Therefore, subject to compliance with the respective provisions of the ICA, both 'local' and 'foreign' insurers may insure compulsory classes of business in Gibraltar. The same applies to non-compulsory classes of risk.

2. WHO CAN INSURE NON-COMPULSORY CLASSES OF RISK?

2.1 Locally admitted insurers

The ICA divides insurance business into general business and long-term business. In terms of general business, the ICA implements the classification of business as found in the First Non-life Directive. However, there are some peculiarities with the ICA, such as the definition of risks to be included in certain classes and also the inclusion of reinsurance within classes. As part of an insurance company's application to the FSC, it will set out the classes of business which it proposes to carry out business under. However, it should also be noted that, once authorised, an insurer may apply to the FSC for an extension to its licence classes, as well as surrender its authorisation in respect of classes that it may no longer require.

In order to insure non-compulsory classes or risk in Gibraltar, the insurance undertaking must either be licensed by the FSC under the ICA or meet the requirements to carry on direct business in Gibraltar via the single European passport. In effect, therefore, any insurer, as long as suitably authorised by the FSC, may cover non-compulsory classes of risks in or

from within Gibraltar. In order to be licensed by the FSC and considered a local or 'Gibraltar Insurer' (as defined in the ICA), the insurer must be incorporated in Gibraltar and have its 'head office' in Gibraltar. However, there is no statutory definition of head office under the ICA, meaning that a practical and common sense approach is required in order to determine this. Accordingly, the FSC considers each insurance company's licence application cautiously to ensure that management and control will be exercised from within Gibraltar. Although each insurance company will be structured differently, common themes considered by the FSC include the role of the board of directors, physical office arrangements and relationships with third party service providers.

2.2 Foreign insurers

In accordance with EU Insurance Directives, the ICA makes provision for the recognition in Gibraltar of EEA insurers, which may passport insurance services into Gibraltar by virtue of their European 'passport' on either a freedom of services or branch establishment. For the purposes of Gibraltar law, an EEA insurer means an insurance or reinsurance company which is incorporated in or formed under the law of an EEA state; which has its head office in that state; and which, in the case of an insurance company, is authorised in accordance with Article 6 of the First General Insurance Directive (as extended, where applicable, by the EEA Agreement) or Article 4 of the Long-Term Insurance Directive (as so extended); or which, in the case of a reinsurance company (an 'EEA reinsurer'), is authorised in accordance with Article 3 of the Reinsurance Directive (as extended, where applicable, by the EEA Agreement).

An EEA insurer may not carry on direct insurance business of a class or part of a class through a branch in Gibraltar unless authorised in accordance with Article 6 of the First General Insurance Directive or Article 4 of the Long-Term Insurance Directive to carry on insurance business of that class or part of a class. In addition, the supervisory authority in the insurer's home state must send to the FSC the particulars and notification documents required under the EU passporting framework, confirming, *inter alia*, that the insurer has the required minimum margin of solvency. EEA insurers wishing to cover relevant motor vehicle risks in Gibraltar must also ensure that they are a member of the Motor Insurers' Bureau (being a company limited by guarantee in the UK), and that either it has appointed a claims representative or the insurance is provided by it participating in a Community co-insurance operation (as in Council Directive 78/473/EEC) other than as the leading insurer.

2.3 Excess and surplus lines markets

N/A.

3. WHICH REINSURERS CAN BE USED?

3.1 Must they be locally admitted?

Under the ICA, 'insurance business' shall mean and include reinsurance unless otherwise expressly provided. 'Reinsurance' for the purposes of the ICA shall mean the activity of accepting general reinsurance, long-term reinsurance and all kinds of reinsurance risks ceded by an insurance company or by another reinsurance company. In the case of the association of Lloyd's underwriters, 'reinsurance' also means the activity consisting in accepting risks, ceded by any member of Lloyd's, by an insurance or reinsurance company other than the association of Lloyd's underwriters.

The FSC may authorise a reinsurer to carry on in or from within Gibraltar non-life reinsurance and related operations, life reinsurance and related operations or all kinds of reinsurance and related operations as may be specified in the authorisation, and such authorisation shall permit the reinsurer to carry on its authorised reinsurance business throughout the entire EEA. Conversely, an EEA reinsurer may passport reinsurance services into Gibraltar. However, it shall not carry on direct reinsurance business of any description through a branch (or otherwise) in Gibraltar unless authorised in accordance with Article 3 of the Reinsurance Directive to carry on reinsurance business of that description.

3.2 If not, are security requirements imposed?

The ICA also makes provision for non-EEA insurers to be authorised by the FSC to carry out insurance business in Gibraltar. A 'non-EEA insurer' means an insurance or reinsurance company the head office of which is not in the EEA but which is licensed in Gibraltar. The main requirements for authorisation are that the applicant is a body corporate entitled under the law of the place where its head office is situated to carry on long-term or, as the case may be, general business there. In addition, the applicant must hold in Gibraltar assets of such value as may be prescribed, and have made a deposit of such amount and with such person as may be prescribed. The wording in this regard is very flexible, allowing each non-EEA applicant to be considered on a case-by-case basis. Non-EEA insurers are also required to have a 'general representative', which shall be a person resident in Gibraltar designated as the applicant's representative. This representative must be authorised to act generally, and to accept service of any document, on behalf of the applicant (but may not be the applicant's auditor).

4. THE TAXATION OF INSURANCE

4.1 What taxes are levied on insurance premium?

N/A.

4.2 What exceptions are there?

There is no insurance premium tax (IPT) payable in Gibraltar. However, a Gibraltar insurer writing business in Italy, for example, would be liable to pay IPT in Italy, as well as be required to appoint a fiscal representative in said country in accordance with Italian regulations. In addition, most types

of investment income are not taxable, such as bank interest. Insurance companies are, however, subject to a flat corporation tax rate of 10 per cent on income accrued and derived from Gibraltar.

5. INSURANCE REINSURANCE AND CAPITAL MARKETS

5.1 How is finite reinsurance treated?

The ICA expressly provides for the making of regulations in respect of the pursuit of finite reinsurance activities and for the objectives, requirements, conditions and procedures in respect of these activities. However, no such regulations have been enacted, and there are no specific provisions under Gibraltar law restricting the use of financial reinsurance (also referred to as finite reinsurance) by insurance companies. The FSC is, however, wary that financial reinsurance may be used to reduce liabilities and in effect disguise the true financial position of its insurers. As a result, the FSC will require detailed reasons and analysis behind any financial reinsurance agreement which an insurer proposes to put in place. Furthermore, statutory filings and annual returns should be sufficiently detailed to enable the effect of any financial reinsurance arrangements to be transparent and easily identifiable. Where necessary, the FSC is able to consult its external actuarial advisors.

5.1.1 What constitutes risk transfer?

Under Gibraltar law, reinsurance is similar to direct insurance and requires a risk transfer in order to be considered as such. Given the variety of financial reinsurance products, it is impossible to dissect each type, but it is generally accepted that this must involve a transfer of risk from insured to insurer to be treated as reinsurance. In terms of the risk itself being transferred, this ordinarily includes timing risk, market risk and underwriting risk.

5.2 Derivatives, ILWs and wagering agreements

5.2.1 What constitutes insurable interest?

The requirement for an insurable interest is laid down in Gibraltar statute by virtue of the Insurance (Marine) Act (which is not restricted exclusively to marine insurance), as well as the Life Assurance Act 1774. In order for an insurance policy to be effective as such, a policyholder must have a sufficient interest in the subject matter being insured. A policyholder must therefore be in a position of benefit regarding the preservation of the insured subject matter, or a position of disadvantage in the event that the subject matter was to be lost.

5.3 Side cars and CAT bonds

5.3.1 To what extent are these governed by the law relating to insurance contracts?

The Insurance Companies (Special Purpose Vehicles) Regulations (the SPV Regulations) allow the FSC to licence special purpose vehicles (SPVs) to carry on in or from within Gibraltar reinsurance business which consists of assuming risks of such particular kind from insurers or reinsurers as may be

specified in the licence. Under the SPV Regulations, an SPV may assume risks from insurance or reinsurance undertakings by fully funding its exposure to such risks through the proceeds of a debt issuance or some other financing mechanism where the repayment rights of the providers of such debt or other financing mechanism are subordinated to the reinsurance obligations of such a vehicle.

5.4 Other ILS and ART products

Gibraltar recently announced plans to establish itself as an insurance-linked securities (ILS) jurisdiction within the EU through the use of dedicated insurance SPVs. There is a strong appetite for a well-regulated, EU-compliant jurisdiction within a market traditionally dominated by the Caribbean domiciles. Gibraltar already has legislation in place in the form of the SPV Regulations which will form the backbone of its ILS framework. In addition, the introduction of the Solvency II Directive is expected to allow insurance undertakings to mitigate their capital requirements through the use of ILS SPVs as a form of alternative risk transfer. This much delayed Directive is expected to come fully into force no earlier by 1 January 2016, and the FSC meets with insurers and reinsurers at least once every six months to monitor the steps being put in place for compliance with the new regime.

Gibraltar's protected cell companies (PCCs) legislation is a further attraction, potentially enabling ILS SPVs and other reinsurance transactions to be incorporated within PCC structures. Solvency II's capital requirements are well documented, so this form of ART may prove to be a unique method of capital relief available to Gibraltar insurers and their promoters. Although still in its infancy, the Gibraltar ILS model will provide a unique offering, combining streamlined regulatory approval from the FSC with stringent regulation derived from EU law.

6. COMMISSIONS

6.1 What commissions and brokerages are permissible? What disclosure of commissions is required?

It is common for Gibraltar insurance companies, particularly those passporting into EU member states, to use third party service providers. These arrangements typically include business producer, claims handling and other brokerage agreements which must be notified to the FSC. The FSC will then ask to review the service agreement, and will pay special attention to agreements with connected parties. Although the FSC does not effectively give official approval to an insurer's third party arrangements, it may object on a number of grounds. In practice, if the FSC objects to an agreement, an insurer would be best advised to amend the contract accordingly or find a suitable alternative. Otherwise there is a risk that the FSC could question the soundness of the insurer's management.

As mentioned above, the FSC's role in supervising arrangements where there is common ownership between the controllers of an insurer and connected parties is vital. Particular consideration is given to the level of remuneration set out in agreements with connected parties in order to

determine that these are reasonable and in line with market practice. The payment of secret commissions, and other methods whereby controllers of insurers may seek to divert or dissipate income away from the company are at the forefront of the FSC's concerns. There is, however, no maximum or minimum level of commission prescribed by Gibraltar law which insurers may pay to its service providers. This means that, as long as the insurer can demonstrate that it would be receiving fair, valuable and proportionate consideration in exchange for those payments, these arrangements are possible.

7. HOW ARE AGENTS (BROKERS AND UNDERWRITING AGENTS AND THIRD PARTY CLAIMS ADMINISTRATORS) REGULATED?

The FSC is an independent regulator established by statute under the Financial Services Commission Act 2007. It is governed by a commission of members, and has a number of statutory objectives which underpin its supervision of financial services, such as the promotion of market confidence, the protection of consumers and the reduction of financial crime. The FSC undertakes the supervision and regulation of all financial services business in Gibraltar, including that of insurance brokers and intermediaries.

The FSC's duties and powers are enshrined within a number of pieces of legislation, which are collectively referred to as the Supervisory Acts. The Supervisory Act for insurance intermediaries, for example, is the 1989 Act, which contains the bulk of licensing requirements for brokers and intermediaries. Generally, the FSC employs a risk-based methodology in its supervision of licensees, combining a mixture of written analysis with a more 'hands-on' on-site inspection programme. This entails members of each supervisory division routinely conducting office visits for discussions and assessments of licensees. In addition, the FSC is required to maintain standards and supervisory practices which match the standards governing the provision of financial services within the UK, whilst also complying with requirements under EU law. In this respect, the FSC also works closely with the Gibraltar government to ensure that all applicable financial services legislation is transposed in a timely fashion.

Intermediaries are split up by the FSC into two categories, being general and life business intermediaries, both of which can operate either independently or as agents. In addition to the 1989 Act, intermediaries are subject to a number of regulations made thereunder. These include the Financial Services (Conduct of Business: Investment Firms & Insurance Intermediaries) Regulations 2006 (the Intermediary Regulations). The Intermediary Regulations stipulate *inter alia* that insurance mediation business must be conducted with integrity, due skill, care and diligence. Intermediaries must also avoid conflicts of interest and treat customers fairly by complying with extensive rules relating to independence, commissions and complaint handling, amongst others. Other notable regulations of applicability to intermediaries are the Financial Services (Advertisement)

Regulations 1991, regulating the content and dissemination of promotional material, as well as the Financial Services (Unsolicited Calls) Regulations 1991, prohibiting cold-calling practices.

One of the main features of the FSC's regulation of licensees, extending to all areas of financial services, is the criteria of sound and prudent management, which must be complied with on an ongoing basis. In summary, this requires licensees to demonstrate that their business is carried on with due skill, care and integrity, and with the necessary professional expertise. An important element of this principle is therefore the regulation of firms' directors and senior management personnel. The 1989 Act, for example, requires all persons associated with a prospective or actual licensee to be fit and proper persons. Although this concept lacks a statutory definition, the FSC will at all times consider a person's professional background in order to establish whether there are any potential issues regarding integrity or competency which could affect the running of the licensee.

8. IS TAKAFUL POSSIBLE?

N/A.

9. WHAT SCOPE IS THERE FOR MICROINSURANCE?

N/A.

10. EXIT SOLUTIONS – WHAT SOLUTIONS ARE AVAILABLE AND HOW DO THEY OPERATE? HOW ARE FOREIGN SOLUTIONS RECOGNISED?

10.1 Portfolio transfer

On 17 July 2014, HM Government of Gibraltar received written confirmation from HM Treasury, UK Government, that transfers under Part VII of the UK Financial Services and Markets Act 2000 (also referred to as Part VII transfers) can take place between UK and Gibraltar insurers, subject to approval of the relevant regulators and upon Court approval (where applicable). This development therefore opens up a whole new area of business for the Gibraltar insurance market. Part VII transfers will enable UK insurers to transfer their insurance and reinsurance portfolios and related assets and liabilities into Gibraltar, through an established legislative framework. It is anticipated that Gibraltar, with all of its advantages, will prove an attractive proposition for run-off business, particularly as UK insurers take strategic decisions to comply with the impending capital requirements of the Solvency II Directive, which Gibraltar is of course on course to implement.

10.2 Statutory portfolio transfer

The ICA contains the procedure under which a Gibraltar insurer (the transferor) is able to undertake a transfer of insurance business to another body (the transferee) (together, an insurance business transfer). The insurance business transfer process is an EU-wide concept introduced by

the Consolidated Life Directive (2002/83/EC), the Third Non-life Directive (92/49/EEC) and the Reinsurance Directive (2005/68/EC) (together the Insurance Directives). The Insurance Directives require EU member states to provide a method for transferring insurance portfolios from one member state to another. An insurance business transfer is therefore possible between a Gibraltar-based insurer and insurance companies domiciled and licensed within the EEA, as long as those jurisdictions have equivalent provisions enacted within their own laws.

Under Gibraltar's insurance business transfer process, the insurer prepares a scheme under which the whole or part of its insurance business is to be transferred to another insurance company. This scheme is subject to approval of either the Supreme Court of Gibraltar (the Court) or the FSC, depending on whether the insurer was authorised to write long-term business or general insurance business, respectively (the scheme). The class(es) of insurance which the insurer is authorised to write by the FSC would therefore determine if the insurance business transfer would require a court application or FSC approval. Where the insurer is structured as a PCC, additional consents may be required from the FSC and affected parties, such as creditors of the PCC or cellular creditors of the PCC's cellular assets. A scheme involving a PCC will also require submission of a separate application to the Court under the provisions of the Protected Cell Companies Act.

One of the main components of an insurance business Transfer is the portfolio transfer agreement (PTA), which sets out the main terms of the scheme. This would include details of the respective assets and liabilities to be transferred and the proposed effective date of the scheme. Where there is a Gibraltar transferor involved, the PTA should be governed by Gibraltar law to ensure that both the Court and the FSC are able to consider the same without the need to obtain legal advice from other jurisdictions.

Long-term insurance business transfer

As a matter of practice, the FSC welcome insurers and/or their professional advisors to meet with them in order to discuss any potential change of circumstances and points of principle. This is true even for transfers of the whole or part of a long-term business (long-term business transfer). Although a long-term business transfer requires the approval of the Court, the FSC must be involved from an early stage as it also has an important role to play. The Court will follow closely the recommendations and views of the FSC and material objections from the regulator would be highly adverse to the applicant's prospects of success in obtaining the Court's sanction.

One of the key aspects of a long-term business transfer is the preparation of a report on the terms of the scheme, to be prepared by an independent actuary. This is a requirement under the ICA and forms a key part of the Court's considerations when approving a scheme. In addition, it is highly advisable for transferors/transferees to commission their own actuarial reports from their appointed actuaries giving their own opinions on the impact of the scheme on policyholders. The focus of both the FSC and

the Court will be to avoid unfair prejudice to policyholders affected by the scheme and the parties' proposals should bear this in mind insofar as possible.

Due to Gibraltar's unique companies' legislation, long-term business transfers are made by the presentation of a petition to the Court. This is in contrast to the UK's Part VII procedure, for example, which follows the provisions of the Civil Procedure Rules. Once a petition has been lodged, the Court must then be satisfied that a report has been prepared by an independent actuary, that the petition has been publicised, and that both policyholders and the FSC have been notified and consulted. The final hearing will be before a Supreme Court judge in Court and evidence is given by affidavit. Any person who alleges that they would be adversely affected by the scheme may appear in person or by counsel to argue his case. In addition, the FSC is usually represented by counsel. The Court's concern at the final hearing shall be whether policyholders or other affected persons are adversely affected by the scheme. If these concerns can be suitably allayed by the applicant, the Court should approve the scheme.

General insurance business transfer

A transfer of general insurance business carried out under the ICA (general business transfer) is subject to the FSC's final approval. An application is made to the FSC accompanied by draft documents such as a PTA, policyholder statements, notices and witness statements. The FSC would then require the parties to satisfy it that the ICA's requirements, such as publication and circulation of documents to policyholders, had been complied with. The ICA does not set a timetable for long-term business transfers or general business transfers. However, long-term business transfers are subject to both FSC consultation and Court approval, meaning that they typically take considerably longer to conclude.

10.3 Novation

Gibraltar's legal system is based on the common law and statute law of England. Therefore, the common law and the rules of equity in force in England from time to time also apply to Gibraltar, including contract law principles such as novation. A novation of liabilities under Gibraltar law involves the transfer of liabilities to policyholders from one insurer to another. Novation of insurance policies involves the 'transfer' of rights and obligations under a policy to a third party, but not quite by way of a direct transfer. Effectively, an existing policy contract is terminated and replaced with a new policy contract. A third party then takes on the rights and obligations which the original insurer had to the policyholder under the original contract.

Novation, however, requires all parties to consent in order for it to be valid and effective in law, making novation generally inappropriate for insurers with large numbers of policyholders. Policyholders could resist entering into a new agreement with a new insurer which they perceived to be less financially stable or reputable than their existing provider.

10.4 Commutation

A commutation involves the contractual discharge of liabilities by an insurer in respect of its policyholders. As with novation, commutations are carried out by non-statutory means and require the agreement of the respective policyholder. As a result, commutation is most suitable where the insurance company has only a small policyholder base, such as with a captive.

10.5 Policy buy-back

N/A.

10.6 Solvent scheme

Schemes of arrangement

An alternative to the appointment of a provisional liquidator, liquidator and/or formal liquidation of an insurance company is to use a scheme of arrangement. Gibraltar's companies' legislation makes provision for schemes of arrangement which allow creditors to submit an estimate of claims, with a view to the making of distributions once agreed. The Gibraltar Companies Act provides that a compromise or arrangement may be proposed between a company (which includes an insurance company) and its creditors or members (or any class of them). Therefore, any creditor or member may apply to the Court for an order summoning a meeting of creditors or members. The company itself may also apply for such a meeting to be summoned, as may any liquidator or administrator duly appointed to the company.

Subject to a majority in number representing 75 per cent in value of the company's creditors or members (as applicable) agreeing a compromise or arrangement at such a Court-summoned meeting, the Court may sanction the scheme proposed. A compromise or agreement sanctioned by the court is binding on all creditors or the class of creditors, or on the members or class of members, together with the company or, in the case of a company in the course of being wound up, the liquidator and contributories of the company.

A scheme of arrangement may be used for a number of purposes, its principle benefit being to enable a partial run-off of an insurer's business on a flexible basis. However, there are significant costs and difficulties involved with such a scheme, particularly when attempting to agree and apply a suitable valuation methodology with creditors and policyholders. Furthermore, in circumstances where a book of business is unlikely to be profitable or there is a very small pool of assets available to creditors, the costs associated with such a scheme could have the effect of increasing the potential creditor deficit, rather than reducing it. In cases where policies written outside of an insurer's formal systems exist, or are suspected to exist, a scheme of arrangement would similarly not be suitable.

Run-off

Insurance companies may also allow their business to run off in circumstances where the portfolio is expected to be profitable. When running off a book of insurance business, the insurer may book premium in respect of which policyholders would otherwise be entitled to claim for as dividends in a liquidation. This is particularly attractive for insurers with low levels of claims, but is not without its disadvantages and risks, not least that it would not be allowed to write any new business. Allowing a portfolio to run off may give rise to further potentially material claims that would adversely affect the position of existing insurance creditors and policyholders. Furthermore, the insurer would need to bear the significant of managing the business, as well as all associated costs, which would ultimately be borne by creditors. In a run-off there would also be little prospect of any distributions being made to creditors until the last policies expire, which, in classes of insurance such as surety and guarantee business, could extend the run-off by many years.

10.7 Assignment

The assignment of insurance policies is possible under Gibraltar law under established English contract law principles. Assignment is suitable in situations where a portfolio of business is being sold and the benefits of that business's contracts are to be assigned to the purchaser. In theory, the actual benefit of a contract may be assigned to a third party without obtaining the other party's prior approval. However, the majority of agreements have non-assignment clauses which may prohibit this in practice. A commonly cited limitation of assignment is, however, that the burden of a contract may not be assigned, which creates a number of uncertainties in the assignor/assignee relationship.

Additional exit solutions

Cross-border merger

The European Cross-Border Merger Directive (Directive 2005/56/EC) applies in Gibraltar and has been transposed into Gibraltar law through the Companies (Cross-Border Mergers) Regulations 2010 (the CBMR). The CBMR apply to all companies within the meaning of the Gibraltar Companies Act, other than a company limited by guarantee or a company being wound up. Under the CBMR, a company from one EEA state may merge with a company in another EEA state as an alternative to the conventional business transfer procedure.

A cross-border merger provides for the automatic transfer of all assets and liabilities of the transferor by operation of law and the automatic dissolution of the transferor company, without that company going into liquidation. All of the relevant EEA states would, however, need legislation in place giving effect to Directive 2005/56/EC. Cross-border mergers are becoming increasingly popular, particularly as part of intragroup reorganisations where groups wish to consolidate assets, capital and resources within one entity, rather than two or more.

The CBMR provide for three general types of merger:

- merger by absorption, where one or more transferor companies transfer all their assets and liabilities to an existing transferee company;
- merger by absorption of a wholly owned subsidiary, where a wholly owned subsidiary transfers all of its assets and liabilities to its parent company (the most common form of merger); and
- merger by formation of a new company, where two or more transferor companies transfer all of their assets and liabilities to a newly formed company.

In terms of the Gibraltar requirements for a cross-border merger, these include the drafting of a draft terms of merger document and providing particulars of the merging companies to the Registrar of Companies. In addition, a director's report must be prepared explaining the background to the merger, and any anticipated impact on employees, creditors or members of the merging companies.

The CBMR, however, remain relatively untested to date by regulated entities such as Gibraltar insurers. In the absence of Gibraltar judicial authority in the area, the Gibraltar courts usually consider the equivalent UK practice. In this regard, a UK transfer of insurance business to another EEA jurisdiction (under the UK Part VII procedure) would need to be combined with the equivalent UK cross-border merger process. Similarly, there is nothing in the ICA or CMBR which suggests that the mandatory insurance business transfer provided for in the ICA, would be overridden or dispensed with by the CMBR. This would mean that both processes would need to be combined under Gibraltar law. Indeed, there has been extensive debate at the EU level about whether the objectives of Directive 2005/56/EC are undermined by this situation, and therefore this particular exit solution is yet to be taken full advantage of by Gibraltar insurance companies.

Redomiciliation

Gibraltar has 'redomiciliation' legislation, in the form of the Companies (Re-Domiciliation) Regulations 1996 (the Redomiciliation Regulations), which allows Gibraltar incorporated companies to redomicile abroad to jurisdictions with compatible redomiciliations legislation. A Gibraltar insurer is therefore able to establish a domicile in countries that are part of the EEA and have compatible redomiciliations laws. The first step in any proposed redomiciliation of an insurer would be to review the insurer's memorandum and articles of association with regard to the possibility of transferring its statutory seat from Gibraltar to the chosen jurisdiction.

One of the advantages of redomiciliation is the continuity of the insurer since there would be no transfer of business or assets involved. An insurance business transfer application would therefore not be necessary, for example, as there is no actual transfer of insurance policies/business. Similarly, when dealing with a PCC, there would be no transfer of cellular assets, and therefore no applications required under PCC legislation. Note that the redomiciliation of an insurer structured as a PCC to another domicile would

also require that domicile to have equivalent protected cell legislation in force.

An insurer carrying out a redomiciliation would, however, need to obtain legal advice confirming the requirements under the applicable law of the new domicile for the continuation of the insurer's insurance activities. This includes obtaining authorisation from the authority responsible for regulating insurance business under the applicable jurisdiction's insurance laws and regulations.

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