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Implementation of the EU Reinsurance Directive (2005/68/EC) in Liechtenstein

Liechtenstein has implemented the EU Reinsurance Directive (2005/68/EC) on 1 January 2010 by amending its Insurance Supervision Act and Ordinance. Consequently, statutory rules on capital and solvency as well as non-financial requirements such as risk management, internal control systems and a responsible actuary have been introduced. Whilst the passporting regime now applies with respect to the EEA, third country reinsurers are no longer able to carry on reinsurance business in Liechtenstein on a cross-border basis without equivalent home state supervision.

Situation prior to the implementation

Already prior to the implementation of the EU Reinsurance Directive in 2010, reinsurance undertakings domiciled in Liechtenstein were subject to supervision and required an authorisation from the Liechtenstein Financial Market Authority (FMA) in accordance with the provisions of the Insurance Supervision Act of December 6, 1995 (ISA) and the Insurance Supervision Ordinance of December 17, 1996 (ISO).

These statutory rules, however, did not specify the capital and solvency requirements for reinsurers. Furthermore, there were no statutory provisions regarding risk management, internal control systems and actuaries for reinsurers.

As to reinsurance undertakings domiciled outside of Liechtenstein (whether or not within the EEA) and carrying on exclusively reinsurance business in Liechtenstein, they were exempt from supervision

by FMA. This applied even if the foreign reinsurer operated through a branch office in Liechtenstein.

Finally, Liechtenstein reinsurers did not benefit from the freedom of services and establishment within the EEA – unlike the direct insurers, based on the Direct Insurance Directives –, and there were no provisions governing Insurance Special Purpose Vehicles (ISPV).

Implications of the EU Reinsurance Directive in Liechtenstein

As a member state of the EEA, Liechtenstein has now enacted into national law the required regulatory and administrative provisions for the implementation of the EU Reinsurance Directive by amending the ISA and ISO. The main implications of these amendments, which came into force on 1 January 2010 – i.e. two years after the intended date – are as follows:

Definition of reinsurance

A definition of the term “reinsurance” has now been included in the ISA. It encompasses the independent commercial activity of accepting risks ceded by a direct insurance company or by another reinsurer, the insurance of risks in the pension sector and the insurance of risks ceded by a member of Lloyd’s.

Passporting rights

Reinsurance undertakings authorised in Liechtenstein are now allowed to carry on reinsurance business throughout the EEA under the freedom of services and establishment, by using the passport regime, and vice-versa.

Treatment of third country reinsurers

With regard to the treatment of non-EEA reinsurers wishing to underwrite exclusively reinsurance risks, Liechtenstein chose to let them continue to benefit from the exemption from its supervision, provided that they are subject to an “equivalent supervision” in their home state. The equivalence of a third country regime is assessed against the key principles of supervision contained in the EU Reinsurance Directive and the objectives each of these principles seeks to achieve. As this exemption applies to cross-border reinsurance only, non-EEA reinsurers are no longer permitted to carry on reinsurance business via a Liechtenstein branch office without a license from FMA.

Rules on capital and solvency

Prior to the implementation of the EU Reinsurance Directive, the Liechtenstein statutory capital requirements for reinsurers only consisted of a minimum share capital of at least CHF 0.5 million. There were no further specific statutory provisions on minimum capitalisation (such as a guarantee or organisational fund), solvency or technical provisions applicable to reinsurers. Such rules have now been included in the ISA and ISO:

- The aforementioned minimum share capital amount stipulated in the ISA has been replaced by a more general requirement for Liechtenstein-domiciled (re)insurance companies to guarantee the on-going fulfilment of their liabilities. As before, the actually required share capital for each individual (re)insurer needs to be established on a case by case basis in collaboration with FMA.

- Reinsurers also need a solvency margin, which is calculated on the basis of the higher of the annual premium income (premium index) and the average loss ratio (loss index). Reinsurers carrying on both life and non-life reinsurance need a solvency margin covering the total amount of the solvency margin required for life and non-life reinsurance.
- In addition to this, a guarantee fund is required. One-third of the solvency margin constitutes the guarantee fund, but it may not be less than EUR 3.2 million (EUR 1.1 for captive reinsurers, subject to FMA’s approval). With respect to the organisational fund which is also needed, it is required to be set up in an amount covering 20% to 50% of the minimum capital.
- Finally, a reinsurance undertaking must accumulate technical provisions that guarantee the fulfilment of all liabilities resulting from all its activities. Detailed rules for the creation and valuation of technical provisions and equalisation reserves are now included in the ISO.

Risk management, internal control systems, actuaries and the enhancement of the financial situation

With the implementation of the EU Reinsurance Directive, provisions regarding risk management, internal control systems, the responsible actuary and enhancement of the financial situation of reinsurance undertakings were adopted in the ISA and ISO. These risk management and organisational requirements are new for Liechtenstein insurers and apply to all lines of business (i.e. both direct insurers and reinsurers).

ISPV rules

Liechtenstein has chosen to allow the establishment of ISPVs (“Zweckgesellschaften”) in its jurisdiction. Accordingly, rules for ISPVs were implemented in the ISA, and the provisions applicable to insurance companies regarding licensing requirements, amendment of licence, risk management, supervision, etc. were declared applicable to these vehicles. An ISPV must furthermore guarantee to meet the liabilities under all reinsurance contracts at all times. Therefore, the current value of the capital assets must at all times exceed the exposures under the reinsurance contracts.

Advantages of Liechtenstein as a (re)insurance location

Now that the passporting regime also applies with respect to reinsurance business in Liechtenstein, local parameters such as the attractive tax regime and the very business-oriented regulatory authority FMA – whose approach to fulfilling its task as insurance regulator is an advantage of the Liechtenstein (re)insurance domicile as compared to many other jurisdictions – will contribute to make Liechtenstein an attractive (re)insurance domicile.

Contacts

The content of this newsletter is for information purposes only and does not constitute a legal advice or opinion. Should you require specific advice in this matter, please get in touch with your usual contact at ALTENBURGER or with one of the below authors of this newsletter:

Zurich



Melissa Gautschi
Partner, Zurich
gautschi@altenburger.ch
Seestrasse 39
CH-8700 Küsnacht-Zürich



Dominique Müller
Associate, Zurich
mueller@altenburger.ch
Seestrasse 39
CH-8700 Küsnacht-Zürich