IBA Insurance Committee Substantive Project 2013

The Legal Nature of Insurance Contracts

Edited by Peter Etzbach

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About the International Bar Association Insurance Committee

Insurance is present in every facet of commercial, industrial and private life. Lawyers practicing in many different fields encounter insurance and its problems and can greatly benefit from the knowledge which membership of this committee provides.

The Insurance Committee aims to provide its nearly 600 members, and the IBA Legal Practice Division as a whole, with information about developments in insurance and reinsurance law, regulation and markets throughout the world as well as with specialist knowledge to assist in the efficient solution of practical insurance problems. New insurance products are also brought to the attention of members.

In addition to this publication, the Committee produces a newsletter for its members which provides updates and commentary on developments and issues in the field.

The Committee also presents sessions at the IBA Annual Conference every year. In 2013, the Conference will be held in Boston. Please see http://www.ibanet.org for more information on this and other upcoming events.

If you would like to join the Insurance Committee, or if you would like further information on the Committee's activities, please visit the insurance pages in the committee section of http://www.ibanet.org.

We also invite you to contact the IBA membership department on

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Note from the IBA Insurance Committee

In the past we have received excellent responses to our substantive projects. In 2011 we received contributions from our members in 27 jurisdictions to our survey regarding privilege in insurance disputes. In 2012 we received contributions from our members in 23 jurisdictions to our survey regarding direct third-party access to liability insurance.

Building on this past success, this year we have conducted a survey regarding the legal nature of insurance contracts. Members from 29 different jurisdictions have provided detailed information and insights into this often complex issue. This survey not only reflects issues of insurance law, but also of insurance regulation. It casts a light on the work of our newly formed Insurance Regulation Subcommittee.

Insurance and reinsurance are global enterprises which engage different legal and regulatory regimes. This, at times, results in cross border disputes, often involving both common law and civil law jurisdictions. We hope that this comparative analysis will be valuable to lawyers and other (re)insurance professionals alike.

We would like to thank those who generously contributed their time and expertise to successfully complete this project.

A pdf copy of this report will be made available on the IBA's website.

Best regards,

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Editorial

The legal nature of insurance contracts

At first sight, the topic “the legal nature of insurance contracts” might appear to be of a mere dogmatic nature. Indeed, when exploring the issue in more detail, the legal concepts underlying insurance contracts have a considerable dogmatic foundation. However, a number of practical questions arise in connection with the issue whether a contract can be qualified as an insurance contract or not: Is the product offered an insurance or not and does the contract need to be concluded by an insurance company, or can it be entered into by an unregulated institution? In this regard, it is essential to differentiate insurance products from other contracts of a similar economic nature, and such distinction may not always be clear. What are the legal consequences if a product does qualify as an insurance contract, but is entered into by a non-insurance company? What are the requirements with regard to the form and the content of an insurance contract? What if the product is distributed in several countries? Issues of supervision also play an important role.

Many insurance professionals and advisors have been confronted with these very practical questions at work and have realized that the answers are often not as clear as they should be. In addition, the global activities of the insurance industry add tremendous complexity not allowing easy solutions to these questions. On this ground the desire arouse within the Insurance Committee of the IBA to take a systematic approach to the topic and to examine the situation in different jurisdictions.

The results of the survey contained in this report provide for detailed answers to the most interesting and relevant practical questions arising in connection with the legal nature of insurance contracts, but the survey also explores the dogmatic foundation. The responses were submitted by IBA Insurance Committee members from 29 different jurisdictions, both common and civil law, allowing for a review around the globe.

The law of most jurisdictions provides for a definition of an insurance contract, which is either of a statutory nature or based on case law. As expected, there are differences when looking at the elements and criteria that need to be met in order to qualify as an insurance contract. But still, when having a closer look at the different definitions and legal concepts, the legal rationale of an insurance contract appears to be mostly similar, *i.e.* a performance of some sort on the side of the insurer in case of the occurrence of an uncertain event on the side of the insured against a consideration. Apparently, this reflects a similar economic and social understanding of the purpose of insurance across all jurisdictions.

Despite this fairly homogenous dogmatic approach towards insurance contracts, the survey reveals substantial differences between the various jurisdictions when it comes to practical implications. In particular the distinctive line between an insurance contract (or product) and economically similar contracts such as warranties, guarantees and derivatives is not clearly drawn in many jurisdictions. Moreover, in a cross-border context the prongs of the delimitation tests vary from country to country making it difficult to design a contract for use in multiple jurisdictions.

Finally, if a risk taking party – erroneously – enters into a contract of insurance without having obtained a license, the consequences in the individual jurisdictions are worth mentioning. While such a case would consistently be regarded as a punishable violation of regulatory requirements, the legal consequences for the contractual relationship differ. Many countries regard such a contract as null and void and reward damages to the policyholder. This could make it necessary for the policyholder to demonstrate and prove damages, which might not always be easy, *e.g.* in case of fixed benefit insurances. Other countries leave the contract in place so that the policyholder may insist on performance, but may alternatively chose to chancel or terminate the contract and claim damages.

The purpose of the surveys contained in this report is to provide practitioners information on the different legal concepts of insurance contracts and matters connected thereto in order to better understand the legal rationale behind insurance contracts within the various jurisdictions. It is our hope that this report will be helpful in practice and can serve a guide of first reference, for example in the field of cross-boarder insurance business, or to explore new arguments for better assessments in the home jurisdiction.

I would like to thank my colleagues at Oppenhoff & Partner, Hanno Goltz and Kirsten Scharenberg, who devoted a significant amount of their time to this project over several months and helped greatly realizing it.

Peter Etzbach

OPPENHOFF & PARTNER

September 2013

DISCLAIMER

This report is not intended to provide legal advice but to provide general information on legal matters. Transmission is not intended to create and receipt does not establish an attorney-client relationship. This report is not intended to replace legal advice and no responsibility for claims, losses or damages arising out of any use of this work or any statement in it can be accepted by the contributors or editors. Readers should seek specific legal advice before taking any action with respect to the matters mentioned in this report.

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Argentina

MANZANO, LÓPEZ SAAVEDRA & RAMÍREZ CALVO

MARTIN MANZANO AND IGNACIO SHAW

Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

Pursuant to Section 1 of the Insurance Act (Law 17,418):

> "an insurance contract exists when the insurer assumes the obligation, through the payment of a premium or quotation, to compensate a loss or to make a payment if the foreseen event were to occur"..

This definition is complemented through Sections 2 and 3 of the Insurance Act, which refer to the concepts of 'insurable interest' and 'risk'.

The principal elements in an insurance contract are (i) an insurable interest, (ii) a risk and (iii) the transfer of the risk against the payment of a premium or quotation.

Section 60 of the Insurance Act, although referring to property insurance provides a broad definition of "insurable interest":

> "…any risk may be the object of these insurance contracts if there is a legal economic interest that a loss may not occur".

2. Does an insurance contract require an element of uncertainty? Please describe.

As mentioned above, the Insurance Act includes the concept of insured risk (under Section 1 of the Insurance Act, the occurrence of the "foreseen event") as an essential element in the definition of the insurance contract. According to Section 3 of the Insurance Act, the non-existence of the risk makes the insurance contract null and void. If the loss has already occurred or the possibility of its occurrence has disappeared, there cannot be a valid insurance contract due to the lack of risk.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Pursuant to Section 1 of the Insurance Act, the assumption of the risk by the insurer is an essential element to the insurance contract under Argentine Law.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

The insured party must have an 'insurable interest'. As mentioned above, this is also a principal element of the definition of insurance contracts established in Section 2 of the Insurance Act, under which the object of the insurance contract is defined as

> "any class of risk if an insurable interest exists, unless there were an express prohibition of the law".

As mentioned above, Section 60 of the Insurance Act, although referring to property insurance, provides a broad definition of "insurable interest":

> "…any risk may be the object of these insurance contracts if there is a legal economic interest that a loss may not occur".

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Except in life insurance policies, the insurance contract may be entered into on account of a third party, with or without naming expressly the insured third party. In case of doubt, the insurance contract will be deemed to have been entered into on behalf of the policyholder (Section 21, Insurance Act).

The policyholder may act as beneficiary to the contract if the policy remains in his possession, although the insurer may demand evidence of the consent of the third party as a condition to the payment of the compensation to the policyholder (Section 23, Insurance Act)

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The Insurance Companies Act (Law 20,091) demands that the exclusive corporate purpose of an insurance company is the insurance activity (Section 7). Even though it is not expressly required by the Insurance Companies Act, the mitigation of risk through large number of contracts becomes a natural element of habitual insurance practice, as insurance companies are not allowed to pursue any other business simultaneously. For instance, Section 26 of the Insurance Companies Act requires that the premiums are sufficient to cover the insurer's obligations.

Also, the number of insurance policies in force is a principal factor in the financial and technical planning

of the companies, which are closely controlled by the regulator in these aspects.

However, the insurance of a large number of similar risks is not a legal condition for the validity of an individual insurance contract.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Under Argentine Law the insurance contract definition does not differ between life insurance and none life insurance. Although there are of course specific regulations for each kind of insurance, the general definition provided by Section 1 of the Insurance Act is applicable to all types of insurance.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Even though the risks involved in gambling and insurance are of a different nature according to the majority of Argentinean authors, our laws do not provide an express solution to this matter.

The Insurance Act (which is part of the Argentinean Commercial Code) and other complementary national laws and regulations govern the insurance business.

If an insurance contract were to be disguised under the form of another contract, the National Superintendency of Insurance (the "NSI") may declare it null and void and apply penalties for unauthorized insurance (Section 61 of the Insurance Companies Act) to the insurer in breach.

Also, the NSI may apply the Insurance Companies Act to parties who perform similar operations which may be identified as insurance contracts (Section 3, Insurance Companies Act).

ii) Warranty, guaranty or any other surety contracts

Under Argentinean Law, insurers are allowed to issue performance bonds ("seguro de caución").

The specification of the contract as an insurance operation, governed by the Insurance law, derives from the qualification of the insurer. The operations of an authorized insurer fall under the Insurance Act and the complementary laws and regulations that govern the insurance business.

Any contract granted by a party who is not an authorized insurer will be governed mainly by the Civil and Commercial Codes.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Insurance contracts over purely financial risk are forbidden under Section 24, last paragraph, of the Insurance Companies Act.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

As mentioned above, the Insurance Act provides a broad definition of insurance contract. There are no provisions in the Insurance Act or in the Insurance Companies Act which exempt operations similar to insurance contracts or any particular kind of insurance from the application of these statutes.

The Insurance Companies Act establishes that the NSI may apply this statute to parties who perform similar operations which may be identified as insurance contracts (Section 3, Insurance Companies Act).

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

There are no exceptions of this kind under Argentinean Law. As mentioned above, in the case of performance bonds ("*seguros de caución*"), -which is the type of insurance with most similarities to an operation which may be performed by a non-insurer-, the specification as an insurance operation -governed by the Insurance Act-, derives from the qualification of the insurer.

The characteristics and legal treatment of these operations shall be different depending on the application of either the Insurance Act or the Civil/Commercial Codes (as is the case with sureties granted by non-insurers).

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Once the NSI authorizes an entity as an insurer, with approved insurance plans and policies, it can enter into valid insurance contracts, otherwise the contract shall be deemed irregular and the insurer may be subject to sanctions.

12. What are the legal consequences for the risk-taker acting without license?

Pursuant to Section 61 of the Insurance Companies Act, the announcement or offer of insurance by a risk-taker not authorized by the NSI to operate as an

insurer, may be sanctioned with a fine of up to ARS 50,000.

If the risk-taker in breach of this provision were a limited liability company, a cooperative association or mutual, its directors, administrators, trustees or members of the board of vigilance shall be severally liable for the payment of the fines and consequences of the nullity of the contracts entered into.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, there is. Licensed insurance companies are required to operate exclusively as insurers, as its sole corporate purpose (Section 7, Insurance Companies Act). Therefore, insurers may not enter into non-insurance business.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

The terms and conditions of insurance contracts need to be approved by the NSI. Pursuant to Sections 23 and 24 of the Insurance Companies Act, the text of the insurance policy and the proposal form, as well as the technical calculation of premiums and reserves must be submitted to the approval of the NSI prior to entering into effect.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Under Argentine law, insurance coverage involving persons, assets or any insurable interests of Argentine jurisdiction may only be provided by an insurance company licensed in Argentina to carry out insurance business.

Section 2 of law 12,988 (*t.o.* 1953) provides that insurance coverage for persons, assets or any other insurable interest of Argentine jurisdiction must be purchased from Argentine-licensed insurance companies. Infringements to this provision may result in a fine against the insured and the intermediary of up to 25 times the amount of the premium.

The insurance contract issued by a non-licensed party would be null and void, pursuant to Section 61 of the Insurance Companies Act.

The policyholder who entered the contract in good faith may terminate the contract and claim damages. The directors, officers, and/or trustees of the non-licensed party are severally liable before the policyholder.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

The main statutes applicable to insurance contracts in Argentina are (i) the Insurance Act (Law 17,418) that deals mainly with the insurance contract and contains a few guidelines on reinsurance, (ii) the Insurance Companies Act (Law 20,091, as implemented by the General Insurance Regulation –NSI Resolution 21,523-), that provides the regulatory framework of the insurance activity and (iii) NSI Resolution 35,615, which establishes the legal framework for the reinsurance activity in Argentina.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

The terms and conditions of the insurance contract must be inserted in the wording of the insurance policy. Any amendment to the policy must also be issued in writing and executed by the parties.

This is a consequence of the general principle established in Section 11 of the Insurance Act, according to which the insurance contract can only be evidenced in writing, and other means of evidence may be admitted if there is any form of written proof which may indicate the existence of the contract ("*principio de prueba por escrito*"). Any ambiguous or obscure terms shall be construed against the insurer.

Under insurance law, there are few specific rules concerning the incorporation of terms, which mainly refer to the notice to the insured of relevant terms (e.g. exclusion clauses must be fully listed in Annex 1 of the insurance policy, so the insured can easily identify all the exclusion clauses applicable, Section 25.1.1.1. of the General Insurance Regulation).

The general content of an insurance policy requires the approval of the NSI prior to entering into effect.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Section 11 of the Insurance Act provides that the insurance policy must be clearly written and be easily readable. Based on this Section, courts and authors generally consider that ambiguous or obscure clauses must be construed against the insurer.

Also, pursuant to Section 158 of the Insurance Act, there are certain rules of the Insurance Act which cannot be modified by the parties.

These rules involve: non disclosure (Section 5), willful non disclosure (Section 8), losses occurred during the term of three months in which the insurer may challenge the contract due to non disclosure (Section 9), adjustment of the premium due to risk decrease (Section 34) and the duty to notify the insurer any aggravation of the risk (Section 38).

Other rules enumerated in Section 158 can only be modified in favor of the insured. These modifications cannot be included within the general conditions of the contract.

Currently there is a trend in Argentine courts to apply the rules of consumer law to the insurance contract, in favor of the insured, in matters such as statute of limitation (one year under the Insurance Act, extended to three years under the Consumer Defense Act, Law 24,240) and general interpretation of contracts.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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CLAYTON UTZ

DAVID GERBER AND CRAIG HINE[1]

Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

In Australia, there is no clear definition of what is an insurance contract under statutory or case law. There is case law which outlines the characteristics of an insurance contract. There is also legislation dealing with the concept of what are contracts of insurance for specific purposes.

Australian courts have cited with approval the test for determining whether something is an insurance contract set out in the judgment of Channell J in the English case of *Prudential Insurance Co v Inland Revenue Commissioners*[2]. The common law test has been further refined in a number of cases. The main requirements are that:

- There must be a binding contract whereby for some consideration the insured secures some benefit, usually the payment of a sum of money or equivalent, upon the happening of some event;
- The event should involve some amount of uncertainty, either as to whether it will ever happen or, if the event must happen at some time, as to when it will happen;
- The insured must have an interest in the subject-matter of the insurance so that the uncertain event must be an event that is prima facie adverse to the interest of the insured;[3]
- The happening of the uncertain event must be outside of the control or responsibility of the insurer.[4]

There is no statutory definition of an "insurance contract". However, some legislation expands on the concept of what is a contract of insurance for specific purposes. For example, the *Insurance Contracts Act 1984* (Cth) (ICA) and *Corporations Act 2001* (Cth) (Corporations Act) operate so that a reference to a contract of insurance in that legislation includes (i) a contract that would ordinarily be regarded as a contract of insurance even if some of its provisions are not by way of insurance; and (ii) a contract that includes provisions of insurance in so far as those provisions are concerned, even if the contract would not ordinarily be regarded as a contract of insurance.[5] The *Life Insurance Act 1995* (Cth) defines what is a "life policy" for the purposes of the legislation (discussed further under Question 7 below).

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. An insurance contract must include an obligation on the part of the insurer which is dependent upon the occurrence of some uncertain future event.[6] This may be uncertainty as to whether the specified event will occur at all, or merely when the event may occur.[7] The happening of the uncertain event must be beyond the control or responsibility of the insurer.[8]

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

There is no express requirement for an insurance contract to provide for the transfer of risk from insured to insurer for the contract to be recognized as an insurance contract.

In *Fuji Finance Inc v Aetna Life Insurance Co Ltd*, the English Court of Appeal affirmed that risk to an insurer

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[1] The authors acknowledge, with thanks, the contributions to this article of Peter Mann (Partner, Clayton Utz) and Reuben Ray (Lawyer, Clayton Utz).

[2] [1904] 2 KB 658 at 662-663. This case has been widely accepted in Australia. See for instance *Australian Insurance Association Ltd v Esso Australia* (1993) 116 ALR 523 and the cases cited in that judgment.

[3] Note that, for the purposes of certain general insurance contracts, ss 16 and 17 of the ICA modify the requirement for insurable interest.

[4] *Re Barratt; Ex parte Young v NM Superannuation Pty Limited* (1992) 34 FCR 508 at 523 per von Doussa J.

[5] Insurance Contracts Act 1984 (Cth) (ICA), s 10 and Corporations Act 2001 (Cth) (Corporations Act), s 764A(2).

[6] *Australian Insurance Association Ltd v Esso Australia* (1993) 116 ALR 523. See also the answer to Question 1.

[7] *JJ Lloyd Instruments Ltd v Northern Star Insurance Co Ltd (The Miss Jay Jay)* [1985] 1 Lloyd's Rep 491.

[8] *Re Barratt; Ex parte Young v NM Superannuation Pty Limited* (1992) 34 FCR 508 at 523 per von Doussa J.

is not required under the law of England.[9] *Fuji Finance* has yet to be considered by an Australian court in an insurance context, and so it is unclear whether that principle will be adopted in Australia. However, we expect that an Australian court may adopt a similar approach having regard to the existing authorities at common law as to definition of an insurance contract.

The *Life Insurance Act 1995* (Cth) regulates certain investment linked contracts which may not involve risk transfer or be contracts of insurance, but are nevertheless regulated under legislation because they fall within the definition of a 'life policy'.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

In most cases, there must be an insured interest for an agreement to be an insurance contract.

The general common law position is that an insured party must have an interest in the subject-matter of an insurance contract. This common law position applies except where it is altered by statute in relation to particular types of insurance contracts.

For those contracts of general (i.e. non-life) insurance which are subject to the ICA, the common law position is altered. Section 16 of the ICA states that a contract of general insurance is not void by reason only that the insured did not have, at the time when the contract was entered into, an interest in the subject-matter of the contract.[10] Section 17 of the ICA provides that a legal or equitable interest is not required at the time of loss. Instead, it is sufficient that the insured suffers a pecuniary or economic loss because of the damage to or destruction of the property that is the subject-matter of the contract. [11] Finally, Section 18 of the ICA deals with circumstances in which an insurable interest is not required in respect of certain life insurance contracts.

Not all contracts of insurance are subject to the ICA. Section 9 of the ICA specifies a number of types of contracts which are excluded from the operation of the ICA including, for example: marine insurance, health insurance, workers' compensation insurance and reinsurance contracts.

For marine insurance contracts, there is a statutory requirement that an insured party must have an insurable interest at the time of the loss in order for the contract to be valid.[12] An insurable interest in this context is defined to mean a legal or equitable interest.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

In Australia, the requirement for an insured interest is impacted by Sections 16 and 17 of the ICA (discussed in Question four above). These Sections apply by reference to the contracting insured (e.g. the policyholder).

A third party who is not a party to the contract of insurance, but is a person specified or referred to in the contract as a person to whom the benefit of cover extends, is a third party beneficiary with rights which are enforceable pursuant to the Section 48 of the ICA. However, the third party beneficiary is not an "insured" for the purposes of Sections 16 and 17 of the ICA.

It appears that, despite the limited application of Section 16 and 17 to the policyholder, a third party beneficiary may still assert their rights under Section 48. Therefore, if the third party beneficiary has insured interest, they have the right to claim directly against the insurer.

The position may be different under contracts which are not subject to the ICA. For example, a marine insurance contract is void if the insured does not have an insured interest - irrespective of the position of a third party beneficiary.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

There is no requirement that an insurer must cover a large number of similar risks in order for a contract to be considered insurance. However, the fact that one party to a contract is engaged in assuming a large number of similar risks may be a factor that is relevant to determining whether the contract in question is insurance. It may also be relevant to the question as to whether a person is carrying on insurance business and therefore subject to licensing or other prudential requirements.

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[9] Fuji Finance Inc v Aetna Life Insurance Co Ltd [1997] Ch 173; affirming Flood v Irish Provident Assurance Co Ltd [1912] 2 Ch 597 and Joseph v Law Integrity Insurance Co Ltd [1912] 2 Ch 581.

[10] ICA s 16.

[11] ICA s 17.

[12] *Marine Insurance Act 1909 Pt. II*, Div. 2.

The insurance of large numbers of similar risks is certainly a supervisory and actuarial issue. The Australian Prudential Regulation Authority (APRA) issues prudential standards relevant to its regulation of licensed insurers. These include capital adequacy and other requirements which are relevant to an insurer's risk profile.[13]

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

The *Life Insurance Act 1995* (Cth) defines what is a "life policy" for the purposes of the legislation.[14] That definition is directed primarily to the subject matter of a contract of insurance. However, the Act does not define what is a 'contract of insurance'.

Therefore, for the purposes of considering the characterization of a contract as life insurance, it is necessary first to conduct the analysis as to whether the contract is question is an insurance contract. The approach would be the same as that outlined for non-life insurance.

It is worth noting that there are certain types of contracts that are "life policies" under the Life Insurance Act (and subject to regulation as life insurance), even if they are not 'contracts of insurance'. A contract - whether or not it is a contract of insurance - that constitutes an investment account contract or an investment-linked contract[15] is a 'life policy' for the purposes of the legislation.[16]

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Gambling and other similar contracts of chance are not insurance contracts.

The main distinction between an insurance contract and gambling or other contracts of chance is that the insured under an insurance contract must have some form of interest in the subject matter of the contract or, in the case of some contracts, suffer a pecuniary or economic loss upon the happening of an insured event.[17] There is legislation dealing with gambling and it is generally clear what is the distinction between insurance and gambling. This is so notwithstanding that an insured interest is not required for some general insurance contracts.

ii) Warranty, guaranty or any other surety contracts

Contracts of warranty, guaranty and other surety contracts are generally not regarded as types of insurance contracts. However, the distinction between these types of contracts and insurance contracts can sometimes be difficult to identify.

Depending on what the warranty covers, a warranty that is provided by a manufacturer or seller of a product will typically not be an insurance contract because the manufacturer or seller has some control over the event giving rise to a benefit under the warranty.[18] This can be contrasted with an insurance contract under which the insurer has no control over whether an insured event will occur.

However, in circumstances where the promise is to provide a benefit upon the occurrence of an uncertain event which is independent of the quality or other characteristics of the relevant product, what might be marketed as a warranty could in fact constitute an insurance contract.

When considering whether a product is a 'warranty' or 'insurance', it is necessary to consider a number of factors. The factors which indicate that a contract is a warranty and not an insurance contract, include: under a warranty, information necessary to enable an informed identification and evaluation of the risk lies primarily with the warrantor; the warrantor is expected to inform itself of the risk it is assuming and not rely on disclosure; the warranty is usually offered only to customers of a particular product and is not available to consumers at large; the warrantor's payment from the customer is not solely connected to the event indemnified against and is usually linked to the provision of some other product or service; a warrantor's rights are usually limited to action against the customer and they do not have rights of subrogation; and a warrantor's essential obligation is usually to repair or replace a product in its own discretion rather than cover all forms of loss.

The characteristics that typically distinguish guarantees and other surety contracts from insurance

[13] APRA Prudential Standards *GPS 116: Insurance Concentration Risk Charge and LPS 115: Insurance Risk Charge.*

[14] *Life Insurance Act 1995* (Cth), s9.

[15] Section 14 of the *Life Insurance Act 1995* (Cth) describes what is an 'investment account contract' or an 'investment-linked contract'.

[16] *Life Insurance Act 1995* (Cth), s9.

[17] See our answer to Question 4.

[18] *Re Barratt; Ex parte Young v NM Superannuation Pty Limited* (1992) 34 FCR 508 at 523 per von Doussa J.

contracts are similar to those that distinguish warranties from insurance contracts. In particular, under a contract of guaranty, the information necessary to enable an informed identification and evaluation of the risk lies primarily with the guarantor. A guarantor also does not have rights of subrogation but rather has rights that are usually limited to action against the principal debtor, or against a co-surety for equitable contribution. [19] Furthermore, a guarantor's payment obligation is quantified by reference to the debt outstanding and it is not necessary that the counterparty suffer any actual loss as a result of the default of the principal debtor.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts such as hedging contracts, swaps and derivatives are generally not regarded as types of insurance contracts. However, again, it can be difficult to distinguish these contracts from insurance - particularly in circumstances in which the hedging contract, swap or derivative has the same economic effect as an insurance contract.

The main distinguishing features of such contracts will differ depending on the nature of the financial contract being considered. Generally speaking, the contracts can be distinguished on the basis that neither of the parties to the contract has an interest in the subject matter that equates with the type of interest present under insurance contract. Such contracts will also typically involve an upfront payment (which is at risk) rather than a payment by way of indemnity when the uncertain event occurs. Furthermore, the return on the contract is usually not in the nature of a premium. Finally, the mere taking of credit risk does not, of itself, constitute insurance.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

There are no express exceptions or exemptions in the legislation applying to insurance contracts, to deal with contracts which in principle meet the characteristics of an insurance contract but should not be treated as such.

While some contracts share characteristics with insurance contracts (see for instance the answers to Question 8 above), they are distinguishable on the basis of principles of interpretation as to what should properly be considered insurance.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

This does not create an exception. However, a close legal or economic nexus to a non-insurance transaction may be a relevant factor in the broader analysis as to whether a contract is insurance.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Yes, subject to certain exemptions for foreign insurers and reinsurers. Unless an exemption applies, a party may only enter into a contract of insurance as the insurer if they are authorized, registered or licensed (as the case may be) to do so. The nature of the authorization, registration or license that is required differs depending on the nature of the insurance business being carried on by the insurer.

The *Insurance Act 1973* (Cth) (Insurance Act) prohibits any body corporate from carrying on general (i.e. non-life) insurance business in Australia without express authorization from APRA.[20] Foreign insurers who wish to insure risks in the Australian market also need to be authorized to do so by APRA unless certain exemptions apply.[21] These exemptions include where the insurance is for certain high valued insureds, for atypical risks (e.g. nuclear or biological risk, risk of damage or loss arising from the operation of space objects, war, … etc.) or other risks that cannot reasonably be placed in Australia. There is also some level of exemption for certain foreign reinsurers who provide reinsurance through intermediaries in Australia.

The *Life Insurance Act 1995* (Cth) (Life Insurance Act) and the *Private Health Insurance Act 2007* (Cth) (PHIA) similarly require any entity carrying on life insurance business or health insurance business in Australia to be registered under the Life Insurance Act or PHIA respectively.

The provision of life insurance and some types (mostly personal lines) of general insurance in Australia will also usually require the insurer to hold an Australian financial services license (AFSL) under the Corporations Act. This is because such insurance constitutes a "financial product", the issuing of such a "financial product" constitutes carrying on a "financial services business" and a person must be authorized to carry on a "financial services business" in Australia.

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[19] *Seaton v Heath* [1899] 1 QB 782 at 793 per Romer LJ, applied in Australia in, for instance, *Hallmark General Insurance Co Ltd v Commissioner of Stamp Duties* (19 October 1988) Tasmanian Supreme Court, Neasey J; and *McLeod v Turner & Ors* (1982) 2 ANZ Insurance Cases 60-491

[20] *Insurance Act 1973* (Cth) Part III.

[21] *Insurance Amendment Regulations 2008 (No. 1)* (Cth) r.4A & r.4C.

12. What are the legal consequences for the risk-taker acting without license?

A person who carries on insurance business in Australia in contravention of the Insurance Act, Life Insurance or PHIA, or carries on a financial services business in Australia in contravention of the Corporations Act, commits an offence and would be liable to pay a monetary fine. The extent of the fine differs depending on what type of insurance business is being carried on by the insurer and therefore the legislation which is being contravened.

A person operating without the required authorization, registration or license can expect to face, on the basis of the current law, the following penalties up to the following amounts:

- AUD 110,000 for carrying on life insurance business without a license;
- AUD 33,000 for carrying on general insurance business without a license;
- AUD 4,400 for each day on which the person carries on health insurance business in Australia without being registered to do so;
- AUD 110,000 for carrying on a financial services business without an AFSL or imprisonment for up to 2 years or both.

There may be other provisions which are incidentally breached by a person who carries on the relevant type of business without the required registration, authorization or license. Further penalties would likely apply in respect of these further contraventions.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Under the Life Insurance Act, a company that carries on life insurance business is prohibited from carrying on other types of insurance business.[22] A life company must also maintain a separate statutory fund for certain types of business and keep the assets of each statutory fund distinct and separate from assets of other statutory funds and from all other money, assets or investments of the company.[23]

The Insurance Act does not contain similar provisions dealing with the position of general (non-life) insurers. The extent to which licensed general insurance companies are able to engage in non-insurance business is controlled by APRA. APRA may impose certain restrictions on an insurer's authorization. In practice, insurers that carry on non-insurance business typically do so through a separate entity which is part of a larger group of companies.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

There is no formal requirement for the terms and conditions of insurance contracts to be submitted to or approved by APRA before entering into effect.

Insurers issuing contracts of insurance that constitute financial products under Chapter 7 of the Corporations Act are required to provide a Product Disclosure Statement (PDS) which contains a summary of the product as well as certain mandatory disclosures. While there is no obligation to submit to a regulator for prior approval the PDS connected with an insurance contract, the insurer must give the Australian Securities & Investments Commission (ASIC) an 'in-use notice' with a link to the PDS.[24] It is possible that ASIC will review that PDS for compliance with the PDS requirements at any time.[25]

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

The Life Insurance Act states expressly that a life company's failure to comply with the Act does not invalidate any policy issued by the company.[26] Therefore a life policy is legally valid even if issued by a party that is not a registered life insurer.

The Insurance Act does not contain similar provisions in respect of general (i.e. non-life) insurance. However, the same outcome is likely. Australian courts have traditionally been reluctant to declare contracts legally invalid on the basis of a regulatory breach by one party which did not affect performance

[22] Life Insurance Act, s234.

[23] Life Insurance Act, s34.

[24] ASIC *Regulatory Guide 168: Disclosure - Product Disclosure Statements (and other disclosure obligations)* 6 September 2010, RG 168.133 to RG 168.136.

[25] ASIC *Regulatory Guide 168: Disclosure - Product Disclosure Statements (and other disclosure obligations)* 6 September 2010, RG 168.5.

[26] *Life Insurance Act 1995* (Cth) s 230.

or the benefit received by the other party.[27] Therefore a contract of general insurance is likely to be legally valid even if issued by a party that is not a registered general insurer.

There are no statutory provisions that give a person the right to terminate, avoid or contest the contract. The relevant legislation does not give the policyholder an express right to claim damages.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes. There are a number of statutes applicable to insurance contracts in Australia, including the following:

- *Insurance Contracts Act 1984* (Cth) which regulates the rights and obligations of parties to life insurance contracts and certain general insurance contracts;
- *Insurance Act 1973* (Cth) which regulates entities providing general (non-life) insurance;
- *Marine Insurance Act 1909* (Cth) which regulates the provision of marine insurance;
- *Life Insurance Act 1995* (Cth) which regulates the provision of life insurance;
- *Health Insurance Act 1973* (Cth) and *Private Health Insurance Act 2007* (Cth) which regulates the provision of health insurance;
- *Corporations Act 2001* (Cth) which additionally regulates the provision of certain insurance contracts; and
- *Australian Securities and Investment Commission Act 2001* (Cth) (ASIC Act) which regulates the conduct of certain insurers where insurance products are regulated under the Corporations Act.

Insurance contracts will also be subject to the regulations validly made under these acts.

Despite the Commonwealth government having responsibility for insurance under the Constitution, certain State and Territory laws also address insurance. These laws include laws with respect to workers' compensation arrangements, which are operated by the respective State and Territory governments. There is also legislation dealing with compulsory third party liability insurance in respect of registered motor vehicles.

[27] *Yango Pastoral Co Pty Ltd v First Chicago Australia Ltd* (1978) 139 CLR 410; *Fitzgerald v F J Leonhardt Pty Ltd* (1997) 189 CLR 215.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

The regulations under the ICA[28] prescribe the content of certain insurance contracts. The prescribed contracts must cover certain events, must provide cover for certain minimum amounts and may be subject to certain exclusions. The prescribed contracts providing this standard cover are contracts for the following personal lines of insurance: motor vehicle insurance, home buildings insurance, home contents insurance, sickness and accident insurance, consumer credit insurance and travel insurance.

The Insurance Contracts Act Regulations do not affect an insurer's ability to provide more or less than the standard cover prescribed. However, the insurer is obliged to bring to the attention of an insured those terms of the insurance contract that derogate from the standard terms of a prescribed contract before the contract is entered into.[29]

Where a contract is not prescribed, insurers must nonetheless clearly inform insureds of unusual policy terms before the insured enters into the contract.[30] Insurers are prohibited from attempting to exclude the operation of the ICA either directly, or by contracting around it.[31] Otherwise, insurers are free to offer their own preferred contractual terms. However the ICA will govern, and may significantly impact upon, how the contract operates.

At common law, the parties to a contract of insurance must act towards each with the utmost good faith. The ICA codifies this principle, but also modifies its application.[32] Parties cannot rely on a provision of a contract of insurance where to do so would be to fail to act with the utmost good faith.[33] In determining whether an insurer's reliance on a provision of a contract of insurance would constitute a failure to act with the utmost good faith, the court will have regard to any notification of the provision that was given to the insured, including (but not limited to), whether notification of unusual terms has been made.[34]

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing

[28] *Insurance Contracts Regulations 1985* (Cth).

[29] ICA s35.

[30] ICA s37.

[31] ICA s5.

[32] ICA, ss 13 and 14.

[33] ICA s14(1).

[34] ICA s14(3), read with the disclosure requirements in s37.

information or other requirements? If yes, please briefly describe.

Yes, there are a number of consumer protection measures in laws regulating insurance contracts. These include disclosure requirements as well as the availability of various remedies that are favorable to consumers and other consumer protection measures.

For example, the ICA requires an insurer to bring to the attention of consumers any terms which derogate from standard cover in connection with certain personal lines of insurance or generally any other unusual terms. The ICA provides further protection to consumers, including provisions which have the effect of:

- permitting an insured to make a recovery in some cases notwithstanding that the insurer has avoided the contract on the basis of an allegation of a fraudulent failure to comply with the duty of disclosure or fraudulent misrepresentation;[35]
- preventing an insurer from unilaterally varying a contract of insurance by making any provision purporting to allow it to do so ineffective;[36]
- preventing the insurer from refusing to indemnify an insured for a loss in some cases by reason of an act or omission of the insured occurring after the contract was entered into;[37]
- preventing the insurer from avoiding an insurance contract entirely in the event of a fraudulent claim by a person that is not the policyholder under the insurance;[38]
- automatically extending certain insurance cover if an insurer fails to notify the expiration of cover;[39] and
- preventing the insurer from cancelling an insurance contract other than in accordance with the ICA.[40]

These protections cannot be excluded, restricted or modified to the prejudice of a person other than the insurer by a provision of a contract of insurance.[41]

These legislative provisions are supplemented by further consumer protection measures in the Corporations Act and the ASIC Act. Those measures include additional disclosure obligations in connection with the sale of insurance products to consumers and provide remedies associated with an insurer's conduct.

Consumers generally have the benefit of access to the Financial Ombudsman Service (FOS), an independent dispute resolution service for financial services providers (which includes certain insurers as members as a condition of the insurer's AFSL). FOS provides rulings on disputes brought by consumers which are binding on the financial services provider, and can also sanction its members for breaches of the codes of conduct it issues.

Many general insurers subscribe to an industry code of conduct - *the General Insurance Code of Practice* - which contains provisions for the benefit of consumers.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Insurance has been the subject of several law reform efforts in Australia over the past decade. One proposed reform is to several provisions of the ICA. The legislation is due to be amended in accordance with the *Insurance Contracts Amendment Bill 2013* (Cth). Upon this Bill passing through Parliament, the various amendments to the ICA will impact upon the rights and obligations of parties to an insurance contract including, for example, the rights of third party beneficiaries of cover. There are also proposals to amend the ICA to include provisions dealing with unfair contract terms.

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[35] ICA s31.
[36] ICA s53.
[37] ICA s54.
[38] ICA s56.
[39] ICA s58.
[40] ICA s63.
[41] ICA s52.

Belgium

LYDIAN

HUGO KEULERS AND ANNE CATTEAU

Definition of an Insurance Contract

1. <u>Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.</u>

Insurance contracts are defined by Article 1.A. of the 25 June 1992 Statute on non-marine insurance contracts ('the 1992 Statute') as

> "any contract according to which, in return for the payment of a fixed or variable premium, a party, the insurer, commits itself towards another party, the policyholder, to provide the benefit stipulated in the contract in case an uncertain event emerges that, depending on the circumstances, either the insured or the beneficiary does not wish to emerge".

The 1992 Statute therefore requires the presence of four essential elements for an insurance contract:

- An insurer;
- An insured party;
- The existence of a risk;
- The insurable interest.

2. <u>Does an insurance contract require an element of uncertainty? Please describe.</u>

Yes, the risk is defined by the 1992 Statute as

> "the emergence of an uncertain event".

In order to be insured, the risk must be:

i) Uncertain: the uncertainty may concern either the realization of the event or the moment of such realization;

ii) Possible: the insurance contract is null and void if the risk does not exist or has already realized itself at the conclusion of the insurance contract;

iii) Independent from the will of the insured.

3. <u>Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?</u>

Insurance contracts require the transfer of risk from the insured to the insurer, but this constitutes one of the essential elements. Other contracts, as for instance warranty contracts, also organize risk transfer.

4. <u>Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?</u>

The existence of a personal and legitimate insured interest is one of the necessary requirements for an insurance contract to be valid. The existence of the insured interest distinguishes the insurance contract from the gambling contract.

There is an insurable interest where the realization of an uncertain event leads to a loss suffered by a person or entity.

With regard to non-life insurance (property insurance, liability insurance and costs insurance), the insurable interest is the economic or personal interest which the insured has in avoiding the realization of the risk and its consequences.

With regard to life or personal insurance, any moral interest in the subject matter of the risk may be sufficient (e.g. the personal relationship between the insured and the beneficiary).

5. <u>Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?</u>

The policyholder is the person who signs the insurance contract and who pays the insurance premiums. There must always be a policyholder for assuming these obligations.

Insurance contracts may also be taken out for the account of any person whom it may concern ("insurance for account", Article 38 of the 1992 Statute). In this case the insured is the person who proves an insurable interest on the occurrence of the insured event. Any defense inherent to the insurance contract which the insurer may raise against the policyholder may also be raised against the insured, whoever he may be.

The insured that it may concern, does not necessarily need to be the policyholder.

6. <u>Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?</u>

In its definition of "insurance contract" the 1992 Statute does require the presence of an "insurer". The 1992 Statute however, does not give any definition of "an insurer".

For some legal authors this definition has been given by an important judgment of the Belgian High Court (*"Cour de Cassation*") of 1992, stating that the insurer

is "the one who professionally concludes insurance contracts, what means the mitigation of a large number of risks". For those authors, the technique of insurance therefore necessarily implies (1) the aggregation of risks, (2) the use of statistics, (3) a risks selection, and (4) the use of reinsurance.

For other legal authors, one may not rely on such judgment from the Belgian High Court because it was rendered on the basis of the old Insurance Statute of 1874 and not on the basis of the 1992 Statute.

Since the 1992 judgment of the High Court, there has been little case law on this issue, and the existing case law is rather divided.

Some recent lower cases decided that the simple transfer of a risk necessarily implied the insurance technique. For example a lower court decided therefore that a leasing agreement, where the lessor proposes a cover for material damage to the vehicle, constitutes an insurance agreement. On the contrary, some recent case law qualifies such risk transfer as a "warranty agreement" (*"pacte de garantie"*).

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No, there is no difference.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Both insurance contracts and gambling contracts are "aleatory contracts". In insurance contracts the existence of an insured interest is required; this is not the case in gambling contracts. The insurance contract has an economic justification; this is also not the case in gambling contracts.

ii) Warranty, guaranty or any other surety contracts

Both insurance contracts and warranty or guaranty contracts organize the transfer of risks. For many legal authors, the difference between insurance contracts and warranty contracts relies in the fact that only (authorized) insurers may offer insurance contract. In other words, when the contract should qualify as an insurance contract, but is issued by a non-insurer, it constitutes a warranty contract.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Hedging contracts, swaps or derivatives are issued by banks. They are used to cover a certain risk, but such cover is not based on any statistics calculation or mitigation by simultaneous contracts.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

According to Article 48 of the 1992 Statute, the insured interest must be lawful. Contracts meeting the characteristics of an insurance contract, but covering unlawful insured interests are therefore null and void.

When the insured interest is unlawful the insurance contract is null and void, Belgian case law is relatively soft on that aspect. The Belgian High Court refined this principle recently by stating that the insurance contract covering an unlawful insured interest will be null and void only in the event that insurance contract has created or helped to maintain an illegal situation. For instance, the insurance contract covering a building that had been built without a planning permission is not illegal because the insurance contract has not created any illegal situation. The goal of this insurance is to indemnify the insured, allowing him to re-build a building, this time with a planning permission.

As mentioned above, some recent case-law admitted that a leasing contract can perfectly meet all the characteristics of an insurance contract and can therefore be qualified as such.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

As mentioned above, while some case law found that a leasing contract was in fact an insurance contract, other case law found that even if the leasing contract meets the characteristics of an insurance contract, it cannot be qualified as such because of the lack of an "insurer". Both contracts do have a close legal and economic nexus.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Relying on the 1992 decision from the Belgian High Court, only an authorized insurer may offer insurance contracts. Some legal authors and some lower judges do not agree with such an interpretation.

According to Article 3, §1 of the Act of 9 July 1975 regarding supervision of insurance undertakings, insurance contracts concluded with non-authorized insurers are null and void.

12. What are the legal consequences for the risk-taker acting without license?

The insurance contract will be null and void (Article 3, §3 of the 1975 Act). However, if the policyholder acted in good faith, the insurer will be obliged to meet its obligations under the insurance contract.

Directors from insurance companies, persons in charge of the management and representatives of insurance companies who tried to or actually underwrite insurance contracts although the insurance company is acting without any license can face a possible jail sentence of one month to five years and/or a fine of EUR 6,000 to EUR 60,000 (Article 83 of the 1975 Act).

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, according to Article 9 of the 1975 Act, licensed insurance companies must limit their corporate purpose to the activity of insurance operations and to the "operations which are associated with insurance operations".

There are currently discussions about the meaning of "operations which are associated with insurance operations", and we already faced an unresolved divergence of opinions on that point between the National Bank of Belgium (the control authority for banks and insurers) and the Authority of Supervision of Financial Markets (the control authority for financial intermediaries).

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

No, the terms and conditions of insurance do not need to be submitted to nor to be approved by the regulator prior to their launching on the market, unless in case of mandatory insurance contracts (such as third party motor insurance policies).

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

According to Article 3, §3 of the 1975 Act and as stated above, the contract will be null and void unless the policyholder acted in good faith (i.e. ignored the insurer did not have any license): in this case he will be entitled to claim indemnification after occurrence of a loss. He will of course be entitled to terminate the insurance contract when he realizes the insurer was not authorized. The policyholder will be entitled to claim damages only if he can prove he suffered any damage from the fact the insurer was not licensed, which in fact will be rather difficult because if the policyholder is of good faith he is already protected by Article 3, §3 of 1975 Act.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

The general applicable law is the 25 June 1992 Statute on non-marine insurance contracts, which is applicable to all insurance contracts, except to reinsurance, transport insurance and marine insurance.

Belgian law provides for some specific regulation for some insurance products, such as the Royal Decree of 14 November 2003 on life insurance, the Act of 9 November 1989 on mandatory third-party motor insurance, or the Royal Decree of 24 December 1992 on fire insurance.

Not all insurance products are regulated under Belgian law. Apart of the abovementioned exception, the 1992 Statute is however applicable to all insurance products. Please note that many provisions of the 1992 Statute are mandatory.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

According to Article 10 of the 1992 Statute, the insurance contract and the amendments thereto must be evidenced by writing between the parties.

The insurance contract must contain at least:

- The date on which the contract was concluded and the date on which the contract enters into force;
- The duration of the contract;
- The identity of the policyholder and, when the occasion arises, the identity of the insured and the beneficiary;
- The name and address of the insurer or of the co-insurers;
- The name and address of the insurance intermediary, if any;
- The risks covered;
- The premium or the method to calculate the premium.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Belgian law is very protective of consumers. Besides the 1992 Statute on non-marine insurance contracts, which contains many provisions written in favor of the insured party, the 1975 Act regarding supervision of insurance undertakings and the 1991 Royal Decree executing the supervision Act both contain many information obligation from the insurer towards the customer. The 1995 Act on insurance intermediation also impose some information requirements on insurance intermediaries towards their clients.

Also, when the policyholder is a customer (i.e. acting within the sphere of his private life), the 2010 Act on consumer protection and market practices will also be applicable. Such Act provides specific information obligations regarding distant selling, voice telephony, etc.

Specific for life insurance, the 2003 Royal Decree provides also for specific information obligations for the insurers.

Belgian insurance companies and intermediaries are also submitted to soft law instruments, such as code of conducts regarding advertisement, etc.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Although Belgian legislation seems to be clear on many of these issues, we see in practice that legal authors, judges and even the regulatory authorities develop their own interpretation of some concepts. The matter is therefore still evolving, notably on the issue of warranty agreements versus insurance contract.

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Preliminary comments

Canada is a federation with two distinct jurisdictions of political authority: the country-wide federal government and the ten provincial governments and three territories. The division of powers between the federal and provincial governments was initially outlined in the *British North America Act, 1867* (now known as the *Constitution Act, 1867*). There is no express provision in the Constitution Act, 1867 for jurisdiction over insurance. The matter was somewhat settled through the courts over the years which have interpreted the provinces' constitutional power to regulate "property and civil rights" to include the marketplace regulation of insurance. Accordingly, except for marine insurance[2], the regulation of contracts of insurance is largely a provincial matter.

All provinces and territories of Canada have used their "property and civil rights" power to shape insurance contract law extensively and to license any insurers undertaking insurance in the province or territory. Each province and territory has legislation dealing with most aspects of insurance contracts made within its boundaries. Apart from auto insurance, which varies widely across the various provinces and territories, the legislation regarding insurance is similar in most provinces and territories. The provincial and territorial statutes deal both with the form and the content of contracts and address several classes of insurance, each of which has different rules. The provincial and territorial statutes include rules regarding disclosure and misrepresentation in negotiations, entry into force, content of policies, notice and proof of loss, valuation of loss, third party rights and termination of contracts, amongst others.

The province of Québec distinguishes itself from the rest of Canada in that its private law is governed not by the common law, but by *the Civil Code of Québec* (the "CCQ") containing a comprehensive set of legal principles covering all aspects of civil law. Provincial statutes such as the *Act respecting Insurance* (Québec) and the *Act respecting the Distribution of Financial Products and services* (Québec) amongst others, and the regulations adopted thereunder, complete this legal framework.[3] The general principles of Quebec insurance law are contained in Chapter XV of the CCQ. For the most part, the rules governing insurance in Québec are similar to those elsewhere in Canada. Some of the articles under property insurance are devoted exclusively to fire insurance.

The incorporation and the corporate and solvency regulation of insurers in Canada is divided between the federal government and the governments of each of the 13 provinces and territories. The federal legislation relating to insurance, that is the *Insurance Companies Act* (the "ICA"), is confined to the creation and licensing of federal insurance companies and the supervision of their financial health. The federal government has the exclusive jurisdiction to regulate the entry into Canada of foreign insurers that wish to operate a Canadian insurance branch. This activity is also covered by the ICA. There is a national regulator, the *Office of the Superintendent of Financial Institutions* ("OSFI") which conducts prudential regulation. Each province and territory also has its own insurance department which regulates market conduct and the licensing and supervision of insurance intermediaries such as agents, brokers and adjusters in their province. In Québec, for example, the *Autorité des marches financiers* (the "AMF"), is the regulator of Québec incorporated insurance companies and of extra-provincial insurance companies licensed to conduct insurance business in the province of Québec.

Our responses to this questionnaire focus on both the common law provinces and the civil law province of Québec, with some responses focusing on federally regulated insurers.

Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

common law

Each of the common law provinces and territories of Canada has its own statutory definition of "contract" or "contract of insurance" as well as its own statutory definition of "insurance". With the adoption of a statutory definition in each such jurisdiction, there is no common law definition of "insurance" *per se*, although

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[1] Our thanks to Hartley Lefton, former associate, and to Martin Bergeron, student at law, for contributing to the preparation of our responses to this questionnaire.

[2] Some would argue that provinces have at least a concurrent jurisdiction with the federal government (which has power over navigation and shipping) in the field of marine insurance. In 1993, the federal government adopted the *Marine Insurance Act*, a statute whose provisions are similar to its provincial counterparts.

[3] See our response to question 16 for additional Québec statutes applicable to insurance.

relevant case law binding or persuasive in the particular jurisdiction is used to interpret the scope of that term.

The definitions of "contract" or "insurance of contract" and "insurance" are identical or nearly identical from one common law province or territory to another, except in the case of Manitoba. Ontario, for example, defines these terms as follows:

- "Contract" means a contract of insurance, and includes a policy, certificate, interim receipt, renewal receipt, or writing evidencing the contract, whether sealed or not, and a binding oral agreement;
- "Insurance" means the undertaking by one person to indemnify another person against loss or liability for loss in respect of a certain risk or peril to which the object of the insurance may be exposed, or to pay a sum of money or other thing of value upon the happening of a certain event, and includes life insurance;

In an oversimplification, *insurance* is sometimes said to require that one person undertake to indemnify another person. Although this may be true for indemnity insurance, it is not so for contingency insurance such as life insurance, this being reflected in the above-quoted definition which recognizes insurance as an undertaking "to indemnify against loss or liability for loss" *or* as an undertaking "pay a sum of money or other thing of value upon the happening of a certain event".

In Manitoba, "contract" and "contract of insurance" are each defined as "a contract the subject matter of which is insurance", and "insurance" is defined nearly identically as is quoted above in the case of Ontario, except that Manitoba expressly adds the proviso that "insurance" does not include certain agreements of the nature commonly described as investment contracts. This proviso is somewhat of a distinction without a difference since the securities statutes of the various provinces define a "security" as including an investment contract and, accordingly, regulation of such contracts is effected pursuant to securities rather than insurance laws.

It is important to note that despite the presence of a statutory definition of insurance, the jurisprudence is consistent in holding such definition to be unreasonably wide and that many transactions or relationships that otherwise satisfy or fit the definition are nonetheless not insurance. There is considerable jurisprudence, industry practice and regulatory guidance around the insurance boundary line and what constitutes a warranty or an indemnity in the commercial rather than the insurance sense.

It has sometimes been questioned whether the payment of a premium is required as a necessary element of an insurance contract due to the absence of any reference thereto in the statutory definitions. As far as life insurance is concerned, the various insurance statutes provide that the contract does not take effect unless payment of the first premium has been made to the insurer or its authorized agent. Although the focus of such provision might be said to be on the payment of the premium, it is nonetheless statutory confirmation that a premium is necessary at least in the case of life insurance. Statutory recognition is also found in the fact that a premium is required content for the life insurance policy, whether individual or group. Express statutory recognition for the requirement of a premium is also found in respect of accident and sickness insurance in corresponding provisions, although different considerations apply to unpaid premiums. Apart from life and accident and sickness insurance, various court decisions have recognized the requirement for consideration for an insurance contract, and the consideration that flows from the insured in return for the insurer's promise, is the payment of an agreed sum of money (*i.e.,* the premium) or the promise to pay an agreed sum of money.

civil law (Québec)

As mentioned earlier, most legal concepts under the civil law province of Québec is derived from the CCQ. Article 2389 CCQ provides for a broad definition of an insurance contract:

> **2389**: A contract whereby the insurer undertakes, for a premium or assessment, to make a payment to the client or a third person if an event covered by the insurance occurs.
>
> Insurance is divided into marine insurance and non-marine insurance.

The "payment" provided for in art. 2389 CCQ is not limited to a monetary payment, and could imply the obligation to defend (liability insurance), repair, rebuild or replace goods.

Life insurance is specifically defined at art. 2393 para 1 CCQ and damage insurance is specifically defined at arts. 2395-2396 CCQ. All insurance-related legislation in the province of Québec is based on the concept of "insurance" as provided for in the CCQ.

2. <u>Does an insurance contract require an element of uncertainty? Please describe.</u>

common law

Yes. Although it is not an express requirement of statute, an insurance contract does require an element of uncertainty – i.e., whether the events will happen or not (e.g., fire or auto collision) or if the event is one which is certain to happen at some time (e.g., death of an individual), there must be uncertainty as to the time when it will occur.

civil law (Québec)

Yes. Since insurance is, by nature, protection against the occurrence of a loss, this loss should not be up to the will of the insured or the insurer. Without risk, there can be no insurance contract. In damage insurance, the insurer is generally not responsible for damages

intentionally caused by the insured (art. 2464 para 1 CCQ). The rule is softened somewhat for life insurance (art. 2441 para 1; art. 2443 para 1; and art. 2443 para 2 CCQ).

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

common law and civil law (Québec): Yes.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

common law

As a matter of common law, the insured is required to have an *insurable interest* in the subject matter of the insurance contract, otherwise the contract will be found to be void. However, the requirement for an insurable interest is modified somewhat by statute throughout the common law jurisdictions such that in the case of life insurance and accident and sickness insurance, an insurable interest is not required if the insurance is group insurance or if the person whose life is insured has consented in writing to the insurance being placed on his or her life (or, in the case of accident and sickness insurance, if the person insured has consented in writing to the insurance). In the case of life insurance as well as accident and sickness insurance, certain relationships are statutorily deemed in all common law jurisdictions to give rise to an insurable interest (e.g., a person is stated to have an insurable interest in the person's child).

With life and accident and sickness insurance, the *insurable interest* need only exist at the time of the insurance contract took effect, and the rights of an owner or beneficiary are not affected by the subsequent termination of his or her insurable interest in the life insured (e.g., life insured ceases to be an employee or spouse of the policy owner). With indemnity insurance (e.g., property or liability insurance), the insurable interest generally needs only exist at the time of the loss.

civil law (Québec)

Under Québec civil law, the rules regarding *insurable interest* are similar to those of the other Canadian provinces. The insured is required to have an *insurable interest* in the subject matter of the insurance contract.

In the case of insurance of persons, art. 2418 CCQ provides that

> "in individual insurance, a contract is null if at the time the contract is made the client has no insurable interest in the life or health of the insured, unless the insured consents in writing."

Certain relationships are statutorily deemed to give rise to an insurable interest such as those based on family ties, on employment relations or a somewhat looser "pecuniary or moral interest" (art. 2419 CCQ).

In property insurance, a person has an insurable interest in a property where the loss or deterioration of the property may cause him direct and immediate damage. It is necessary that the insurable interest exist at the time of the loss but not necessary that the same interest have existed throughout the duration of the contract (art. 2481 CCQ). The insurance of a property in which the insured has no insurable interest is null (art. 2484 CCQ).

Any stipulation which derogates from the rules of the CCQ on *insurable interest* is null (art. 2414 CCQ).

As is the case under the common law system, *insurable interest* need only exist at the time that the insurance contract took effect for life and accident and sickness insurance (art. 2418 CCQ) while it need only exist at the time of the loss for property insurance (art. 2484 para 2 CCQ).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

common law

The insurable interest is required to attach to the policyholder. This having been said, it is possible at least insofar as property is concerned, for an insured who has an insurable interest in a portion of an insured item to purchase valid insurance for the insurable interest of a third party provided that the purported insured also intends to obtain insurance covering the third-party's insurable interest and the wording of the particular contract of insurance does not otherwise preclude such coverage or limit recovery to the applicant's own interest only.

civil law (Québec)

The insurable interest is also required to attach to the policyholder under Québec Civil Law.

For property insurance, a person has an insurable interest if the loss or deterioration of the property would cause him direct and immediate damage (art. 2481 CCQ). This rule should not be understood as meaning that someone could not have proper property insurance for property belonging to someone else. Courts have ruled that as long as the insured would sustain a direct and immediate damage, the insurance contract will be valid. For example, one of the co-owners in a condominium complex could purchase insurance for the other co-owner's parts, in so far as they could sustain direct and immediate damage; when someone has made a promise to purchase, an insurable interest can exist.

In insurance of persons, as explained under Section 4 above, a contract is null if at the time the contract is made, the client has no insurable interest in the life or

health of the insured, unless the insured consents in writing (art. 2418 CCQ).

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

common law

Although it is a common element of insurance that the risk assumed by an insurer will be mitigated by the simultaneous or proximate insuring of a larger number of similar risks (and although it is necessary to the continuing solvency of any particular insurer), there is no express statutory obligation to do so. As well, such mitigation may be a relevant factor or indicium in the determination of whether a particular contract is one of insurance.

civil law (Québec)

As in other Canadian jurisdictions, there is no express provision in the CCQ which would require that the risk assumed by an insurer be mitigated by the simultaneous or proximate insuring of a larger number of similar risks. The element of "sharing of risk" is a factor to be taken into account in the determination of whether a particular contract is one of insurance.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

common law

In the common law provinces and territories, there is one statutory definition of insurance, with the second part of such definition being applicable to life insurance and other forms of contingency insurance – see Section 1 above.

civil law (Québec)

The general definition of an insurance contract found in art. 2389 CCQ applies to all types of insurance (see Section 1 above). However, the CCQ also provides for specific definitions for the main types of insurance contracts in the class of insurance of persons and in the class of damage insurance.

For example, life insurance and certain types of annuities are defined at art. 2393 CCQ as follows:

> **2393**: Life insurance guarantees payment of the agreed amount upon the death of the insured; it may also guaranty payment of the agreed amount during the lifetime of the insured, on his surviving a specified period or on the occurrence of an event related to his existence.
>
> Life or fixed-term annuities transacted by insurers are assimilated to life insurance but remain also governed by the chapter on Annuities. However, the rules in this chapter relating to unseizability apply to such annuities with priority.

Damage insurance is defined at arts. 2395 and 2395 CCQ as follows:

> **"2395**: Damage insurance protects the insured from the consequences of an event that may adversely affect his patrimony.
>
> **"2396**: Damage insurance includes property insurance, the object of which is to indemnify the insured for material loss, and liability insurance, the object of which is to protect the insured against the pecuniary consequences of the liability he may incur for damage to a third person by reason of an injurious act.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

common law

Contracts of gambling and chance are not considered a type of insurance contract in Canada. Superficially, an insurance contract resembles a contract of gambling or chance. In both cases, one party to the arrangement pays a small sum of money to another party for the chance of receiving a larger sum of money from that other party if a particular event occurs. However, upon deeper analysis, the two types of contracts have fundamentally different purposes. An insurance contract is made to avoid risk, while a gambling contract is made to profit from risk. The first protects against a risk that already exists (and is thus considered to be socially beneficial) and transfers it to the insurer, while the second creates a new risk where none existed before and, therefore, there can be no *transfer* of risk since one did not previously exist.

Another distinction between these two types of contracts relates to the concept of "insurable interest". Subject to what is stated in the answer to question 4 above, a contract is not enforceable as an insurance contract unless the insured has an insurable interest in the subject matter of the insurance. Such an interest does not exist in contracts of gambling and chance. Canadian courts will interpret the insured as having an insurable interest if the uncertain event which is contemplated in the contract is adverse to the interest of the insured. In contracts of gambling and chance, apart from the secondary effects which may flow from

the contract itself, the uncertain event contemplated does not affect the insured at all.

civil law (Québec)

The above analysis is equally applicable to the civil law regime. Specifically, contracts of gambling and chance are referred to as contracts of "gaming and wagering" under the CCQ (arts. 2629 and 2630 CCQ) and are not considered a type of insurance contract.

Despite being treated together, "gaming and wagering" are not considered to be the same thing. On the one hand, gaming implies an attempt to obtain a certain result in an environment where there is some randomness. The parties can have some or lots of control over the occurrence of the event. The parties agree to remit money or a good to the party who obtains the result in question, such as winning a game of poker. On the other hand, wagering implies a divergence of opinion between the parties, and an agreement to remit money or a good to the party whose opinion about a certain fact turns out to be right, such as, for example, the date of birth of Elvis Presley.

Insurance is distinguishable from both "gaming and wagering". Gaming allows for a certain level of control over an outcome, although the degree of control varies. This is different from a contract of insurance in that the loss incurred by a policyholder is outside the control of the policyholder. As well, the environment pursuant to which insurance operates is not one that is random. In fact, premiums for insurance are usually determined based on the probability of a certain event occurring (if not for that particular policyholder then for someone within the same "group" as the policyholder). Wagering is based on the correctness of someone's opinion about a certain fact. No event needs to happen between the wager and the winning. In insurance, however, unless an event occurs, which causes someone a loss, nothing will ensue.

Finally, perhaps the most important distinction is that insurance aims to compensate for a loss and is not zero-sum in nature, whereas the objective of both gaming and wagering contracts is to provide the "winner(s)" with a net gain and the "loser(s)" with an uncompensated loss.

ii) Warranty, guaranty or any other surety contracts

common law

Warranty: Warranty is an assurance of quality, variety, quantity or title of goods or, to the extent applicable, services. Such a warranty given by a manufacturer or seller, and provided that the contract does not also indemnify against loss or damage from an external risk or peril, constitutes a true warranty and is not considered insurance. Although there is some disagreement on the point, a warranty given by a person who has no connection with the subject of the warranty (either as manufacturer, seller or wholly-owned subsidiary of the manufacturer or seller) – a so-called "third party warranty" – would appear to constitute insurance in the common law jurisdictions of Canada, since it would appear to have all of the constituent elements thereof, even if the warranty relates solely to a manufacturing defect.

British Columbia has attempted to end any debate on this last issue in respect of certain goods by adding to its insurance legislation definitions of "product warranty insurance" and "vehicle warranty insurance" as well as by introducing a restricted list of exemptions thereto (i.e., manufacturers, sellers and certain others are expressly exempt and are not considered insurers). Alberta has also attempted to do the same, but by simply adding definitions of "equipment warranty insurance" and "product warranty insurance" to its insurance statute. However, in Alberta it should be noted that a third party warranty offered on a "home appliance" (as defined in the legislation) where the total consideration payable for the insurance does not exceed CAD 200, would not need to be issued by an insurer licensed to conduct business in that province and would not need to otherwise comply with its insurance legislation.

civil law (Québec)

Warranty: Except for certain types of warranty as more fully described below, a warranty is not considered insurance in Québec. The CCQ has numerous provisions dealing with warranties. A warranty applies first and foremost in the context of a sale (arts. 1716, 1723, 1732 and 1733 CCQ). However, it can also exist in other contexts where rights are transferred, as in the case of an assignment of a claim (art. 1639 CCQ) or rent agreement (art. 1854 CCQ), amongst others.

Unlike British Columbia, Alberta and Saskatchewan, Québec specifically excludes product warranties from regulation under the *Act respecting Insurance* (Québec) (the "Québec Insurance Act"). Instead, the sale of product warranties is regulated in Québec under the *Consumer Protection Act* (Québec). Under this legislation, a permit is required in order to provide extended warranties on automobiles, motorcycles and other prescribed classes of property.

However, certain types of warranties are considered as insurance in Québec. More specifically, the *Autorité des marches financiers* (the "AMF"), which is the regulator of Québec incorporated insurance companies and of extra-provincial insurance companies licensed to conduct insurance business in the province of Québec, has stated in various notices published in 2009 and 2010[4] that it considered as insurance "vehicle replacement cost warranties" and two other products relating to vehicles namely, "marking

[4] AMF notice dated 27 March 2009 respecting vehicle replacement cost warranties, AMF notice dated 30 April 2010 respecting products relating to vehicles generally and AMF notice dated 30 April 2010 respecting GAP warranties.

warranties" and "GAP warranties", if certain conditions are met. As explained in the AMF notice relating to vehicles generally, a product that relates to a vehicle is considered insurance if the product is (i) offered on the sale or lease of a vehicle or one of its components or parts; and (ii) gives the right to an indemnity upon the occurrence of a risk covered in the contract (e.g. loss, theft, accident, vandalism) in exchange for the price of purchasing the protection. In the AMF's view, all the criteria necessary for a product to be considered insurance are present in such products: (i) the payment of a benefit; (ii) upon the occurrence of a risk; (iii) for a consideration. The difference between an insurance product and a warranty is that insurance protects the consumer from risk while a warranty protects the consumer from defects in quality. However, the AMF further explains that a product providing for (i) reimbursement of its cost; and (ii) cancellation of the contract in the event that the good sold does not work effectively is not an insurance product.

common law

Guaranty: A traditional or true guaranty is a secondary undertaking given by one person (i.e., the guarantor) to answer for the payment of a debt or the performance of an obligation made by another person (i.e., the original obligor), should such original obligor default in that payment or performance in first instance. More simply, a true guaranty has been said to be a secondary undertaking by one person to answer for the default of another. With insurance, and leaving aside the issue of primary versus excess insurance coverage, the insurer's obligation is a primary one. A true guaranty also differs from a contract of insurance in that with insurance, the risk is fortuitous whereas in the case of a guaranty, the risk is prone to be in the control of the original obligor, either wholly or at least partially.

This having been said, three provinces have recognized "guaranty insurance" as a class of insurance under which the so-called *insurer* undertakes to perform an agreement or discharge an obligation if the person liable to perform or discharge it fails to do so[5], and most common law jurisdictions in Canada have recognized the class of "surety insurance" and have defined it as including, among other things, insurance under which the insurer undertakes to guaranty the due performance of a contract or undertaking. As with the definition of insurance itself, these definition are inordinately wide as all guarantees could fit within them whether it be a simple guaranty by a parent of the debt, lease or other obligation of a child or the guaranty by a parent corporation of the debt of a subsidiary under a commercial loan. As a rule of thumb, what distinguishes guarantees that are intended to be regulated via statute as insurance from those that are not, is that in the former case the guarantor issues the guaranty as a vocation and *not* merely incidental to some other non-insurance business, activity or relationship. In a particular case, a court would use certain rules of statutory interpretation to distinguish between guarantees that are intended to be regulated via statute as insurance from those that are not.

civil law (Québec)

Guaranty: Under Québec civil law, true guarantees are governed by Chapter XII of the CCQ dealing with "suretyship". Art. 2333 CCQ provides that

> "suretyship is a contract by which a person, the surety, binds himself towards the creditor, gratuitously or for remuneration, to perform the obligation of the debtor if he fails to fulfil it."

The three following differences between insurance and guaranty (or suretyship) should be noted. (1) A guaranty (or suretyship) can be gratuitous, whereas insurance never is (the policyholder always pays a premium to the insurer); (2) a guaranty (or suretyship) is necessarily a tripartite contract, whereas insurance can be between two parties alone; and (3) when the surety pays the creditor after the debtor has failed to fulfill her obligations, the surety will expect to be reimbursed by the debtor, whereas in insurance, the payment by the insurer does not normally give a recourse to the insurer against the policyholder.

Like in other common law provinces, Québec has recognized the class of "surety insurance" and has defined it in Section 19 of the Québec Insurance Regulation as

> "insurance whereby the insurer undertakes to guaranty the performance of an obligation or the payment of a penalty or indemnity for default on the part of the debtor. It does not include credit insurance, credit protection insurance or hypothec insurance, which are distinct classes."[678]

[5] Or to pay money upon such failure or in lieu of such performance or discharge.

[6] Section 20 of the Québec Insurance Regulations provides that "insurance in the "credit insurance" class is insurance whereby the insurer undertakes to indemnify an insured creditor against loss resulting from failure on the part of a debtor to repay the insured creditor. This class does not include protection for claims secured by hypothec."

[7] Section 21 of the Québec Insurance Regulations provides that "insurance in the "credit protection insurance" class is insurance whereby the insurer undertakes to indemnify a creditor against loss resulting from failure on the part of an insured natural person owing a debt to the creditor to repay the latter by reason of insufficient income, up to the amount of the debt."

common law

Suretyship: In the common law jurisdictions of Canada, the distinction between a contract of guaranty and a contract of suretyship is somewhat nebulous if it exists at all. Furthermore, any effort to isolate the similarities and differences between insurance and suretyship in the common law sense is, to a certain extent, an academic exercise as a result of the fact that "surety insurance" is a statutorily defined class of insurance not only federally, but also in ten[9] of the thirteen provincial and territorial jurisdictions of Canada. The federal definition is reproduced as follows and is identical or nearly identical to the corresponding definition in such other ten jurisdictions:

> "surety insurance" means insurance under which an insurer undertakes to guaranty the due performance of a contract or undertaking or the payment of a penalty or indemnity for any default.

Two other provinces[10] also regulate surety contracts as insurance, but there by virtue of the definition of insurance itself, taken together with the definition of "guaranty insurance" as a recognized class of insurance. As indicated above, guaranty insurance is generally defined as an undertaking to perform an agreement or discharge on obligation if the person liable to perform or discharge it fails to do so, or to pay money upon such failure or in lieu of such performance or discharge.

As a result of the breadth of these definitions, a court will not consider all arrangements which satisfy the particular definition as being subject to the insurance legislation of the applicable jurisdiction. If the particular contract fits the definition and, as a rule of thumb, if the surety issues the contract as a vocation and *not* merely incidental to some other non-insurance business, activity or relationship, then it is likely that a court would find that the issuer needs to be licensed as an insurer (*i.e.,* needs to be a duly constituted insurance company and licensed to conduct the class of surety insurance or guaranty insurance, as the case may be, in the jurisdiction) and otherwise comply with the applicable insurance legislation of the jurisdiction. Accordingly, surety bonds of various types including, without limitation, performance bonds, bid bonds, and labor and material payment bonds (payment bonds), would all need to be issued by an appropriately licensed insurer. In a particular case, a court would use certain rules of statutory interpretation to distinguish between surety arrangements that are intended to be regulated via statute as insurance from those that are not.

civil law (Québec)

As explained in our response for "guaranty" above, suretyship is defined under art. 2333 CCQ. However, the Quebec Insurance Regulation also provides for a class of surety insurance.

i) Financial contracts such as hedging contracts/swaps/derivatives

common law and civil law (Québec)

While insurance contracts by federally or provincially licensed insurers are carved out of the definition of derivative under the *Derivatives Act* (Québec) and proposed *CSA Model Rule 91-301 Derivatives: Product Determination*, there is no similar carve-out for derivatives from the definition of insurance under provincial insurance statutes. Generally most derivatives do not have the characteristics necessary to be considered contracts of indemnity because derivatives do not require either party to have an insurable interest in the underlying interest of the derivative. However, the statutory definitions of insurance also include contracts which involve the payment upon the occurrence of a certain event. As indicated above, there is an issue with the breadth of the definitions of insurance in Canadian statutes and the application thereof to various financial instruments. Most derivatives do not fall under the various classes of insurance defined under federal and provincial legislation, but credit derivatives do resemble guaranty insurance (which is a recognized form of insurance in some provinces). Most commentators have stated that it is likely that courts would find another means to distinguish between a legitimate credit derivative and guaranty insurance, however this is by no means certain and there is no case law or official commentary on the topic. Despite this possible issue, there is a well developed Canadian credit derivatives market whose participants are not licensed as insurance companies and have no intention to obtain such licenses.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

common law

As explained earlier, the regulation of insurance contracts is an exclusive provincial jurisdiction. The definition of "insurance" and "business of insurance" are broadly similar across the Canadian jurisdictions and similar to those found in the US. There is little Canadian case-law although there is an Ontario Court

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[8] Section 22 of the Québec Insurance Regulations provides that "insurance in the "hypothec insurance" class is insurance whereby the insurer undertakes to indemnify an insured creditor against loss resulting from failure on the part of a debtor to repay a loan secured by a movable or immovable hypothec."

[9] British Columbia, Alberta, Manitoba, Ontario, New Brunswick, Nova Scotia, Newfoundland and Labrador, Yukon, Northwest Territories, and Nunavut.

[10] Saskatchewan and Prince Edward Island. Manitoba has recognized both a class of "surety insurance" as well as "guaranty insurance".

of Appeal decision that looks at the evil that the insurance legislation addresses in determining whether the activity or contract is insurance that requires to be regulated as such. A few cases address the insurance boundary line as more fully described in 8(ii) above as does some of the provincial insurance legislation in the area of product warranties. The provincial regulators have some discretion in applying the legislative definition to factual situations and some are more willing to exercise their discretion than others. All legislation contemplates exemption by Regulation and there are instances of these exemptions in some Provinces. Obtaining an exemption Regulation is in part a political/policy matter informed by the insurance regulator.

Another consideration is whether the location of the risk or the location of the insurance activity is the determining factor. The federal insurance regulator takes the view that it is the latter[11]. The provincial regulators focus on the location of the risk although certain insurance (financial guaranty, for example) is traditionally obtained by Canadian companies on foreign markets without the insurance contract being subject to Canadian insurance regulation.

civil law (Québec)

As explained in our response to question 8, certain types of contracts such as extended warranties who meet the characteristics of insurance contracts are not considered insurance contracts. Instead, they are governed by the *Consumer Protection Act* (Québec). Other types of insurance, such as funeral expenses insurance, are currently not allowed in Québec (art. 2442 CCQ)[12] while being allowed in other Canadian provinces.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

common law

The insurance boundary has elements of this. In addition to the issue of warranties (see response to question 9 above), activities with an element of risk transfer that, in the past, the courts have found not to be insurance included motor clubs, annuities, not for profit religious organization activities. In the case of the latter two, the province(s) passed legislation to expressly include them in the insurance regulatory scheme. As mentioned in the response to question 9, at least one court has analyzed the issue in terms of determining the evil that the insurance legislation was designed to address and comparing it to the activity in issue.

civil law (Québec)

A close legal or economic nexus to a non-insurance transaction will often be the reason for a contract or product not to be considered as insurance. In our response to question 9 regarding warranties, we explained that while product warranties are not considered insurance in Québec, certain types of warranties such as insurance vehicle replacement cost warranties, marking warranties and GAP warranties, are considered insurance products if certain conditions are met. In the AMF's view, all the criteria necessary for a product to be considered insurance are present in such types of products: (i) the payment of a benefit; (ii) upon the occurrence of a risk; (iii) for a consideration. Again, the difference between an insurance product and a warranty is that insurance protects the consumer from risk while a warranty protects the consumer from defects in quality.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

common law

An insurer is required to be licensed when it undertakes a contract made or deemed to be made in that province.

A contract of insurance (except, in certain cases, for a contract of life insurance) is deemed to be made in a province where the contract insures a person domiciled or resident in that province at the time the contract is made, or the subject-matter of the contract is property that is or will be located in the province. In certain provinces, the contract may also qualify as being made in the province if it is signed, countersigned, issued or delivered in the province or committed to the post office or to any person and to be delivered to the insured, his assign or agent in the province.

In general, an insurer is also required to be licensed to insure risks in a province when it carries on business in that province. Apart from undertaking a contract made or deemed to be made in a province, "carrying on business" typically includes:

i) having a physical presence in the province, in the insurer's own name or in the name of an agent or other representative;

ii) being listed in a telephone or similar directory for any part of the province.

iii) making or causing to be made in the province any solicitation for insurance;

iv) issuing or delivering in the province any policy of insurance;

[11] OSFI Advisory Notice on "Insurance in Canada of Risks ", revised May 2009

[12] Section 48 of *Bill 8, An Act amending the Securities Act and other Legislative Provisions* (2009, chapter 25), which has not come into force yet, proposes to amend the CCQ by adding a new art. 2441.1 which would allow for funeral expenses insurance in Québec.

v) directly or indirectly in the province collecting or receiving or negotiating any premium for a contract of insurance;

vi) inspecting any risk or adjusting any loss in the province under a contract of insurance; or

vii) prosecuting or maintaining in the province any action or proceeding in respect of a contract of insurance.

Contracts of reinsurance only may be entered into by licensed or unlicensed entities. In Nova Scotia, there is no statutory exemption from licensing; however it appears that, as long as no insuring activities ("carrying on business") take place in the province, no licensing requirements would be triggered for reinsurers.

civil law (Québec)

An insurer is required to be licensed as "insurer" when it undertakes an insurance contract made or deemed to be made in the province of Québec or when it carries on the business of insurance in Québec. The insurer must also be registered as a "firm" under *An Act Respecting the Distribution of Financial Products and Services* (Québec) (the"Québec Distribution Act") in order to distribute the insurance products to consumers through duly registered insurance agents or brokers. Certain exemptions from the licensing requirements under the Québec Distribution Act exist for the following persons:

- Persons who, on behalf of an employer, a union, a professional order or an association or professional syndicate constituted under the Professional Syndicates Act (chapter S-40), secure the adhesion of an employee of that employer or of a member of that union, professional order, association or professional syndicate in respect of a group contract in insurance of persons or a group annuity contract;[13]
- Members of a mutual benefit association that does not guaranty the payment of a benefit upon the occurrence of a risk who offer policies for the mutual benefit association;[14]
- Actuaries who, in pursuing activities as an actuary, offer insurance products in group insurance of persons or group annuities are not group insurance representatives.[15]

Market intermediaries known as "distributors" are also exempt from the licensing requirements to sell insurance products. A distributor is defined as a person who, in pursuing activities in a field other than insurance, offers, as an accessory for an insurer, an insurance product which relates solely to goods sold by the person or secures a client's adhesion in respect of such an insurance product.[16] The following types of products are deemed to be insurance products which relate solely to goods:

- Travel insurance;
- Vehicle rental insurance, where the rental period is less than four months;
- Credit card and debit card insurance;
- Replacement insurance, that is, property insurance under which the insurer guarantees the replacement of the insured vehicle or insured parts.

The Québec Distribution Act also provides that debtor life, health, employment insurance and investor life insurance are deemed to be insurance products which relate solely to goods and to which clients adhere. It also provides that other insurance products may be authorized by the AMF to be distributed through distributors. Insurers are thus expressly permitted to sell insurance products through distributors such as travel agents, banks and trust companies. Both the distributor and the insurer have obligations of disclosure to the client. They must also comply with various approval and filing requirements with the AMF .

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

common law

An unlicensed underwriter acting without a license is, upon conviction, guilty of an offence under the applicable insurance legislation of the applicable province/territory. While the penalties range among jurisdictions, financial penalties are up to CAD 1,000,000 and up to two years imprisonment. In certain jurisdictions, directors and officers of the corporation have liability for prosecution, even if the corporation itself is not prosecuted or convicted. Similar types of offences and penalties exist for marketing insurance without the appropriate license.

A foreign insurer undertaking insurance in Canada without a federal order (registration) in contravention of the ICA is also be liable to fines under the ICA of up to CAD 5,000,000.

civil law (Québec)

The Québec Insurance Act and the Quebec Distribution Act also provide that an unlicensed underwriter acting without a license under said statutes

[13] Section 3 of *An Act Respecting the Distribution of Financial Products and Services* (Québec)

[14] Idem

[15] Section 4 of *An Act Respecting the Distribution of Financial Products and Services* (Québec)

[16] Section 408 of *An Act Respecting the Distribution of Financial Products and Services* (Québec)

is, upon conviction, guilty of an offence and subject to the payment of fines and penal proceedings.

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

common law

Most insurance companies in Canada are governed by the ICA. The ICA restricts the business and powers of a Canadian insurance company regulated by the OSFI (15(2)). A company is prohibited from engaging in or carrying on any business other than financial services (440(1)), and, except as authorized by the ICA, may not deal in goods, wares or merchandise or engage in any trade or other business (441(3)). Therefore, essentially, a Canadian insurer is not permitted to engage in non-insurance business activities unless those activities are authorized under the ICA.

The term "financial services" is not formally defined in the ICA. However, the ICA clarifies certain types of activities that a company may engage in and which therefore are *not* prohibited. These include (i) acting as a financial agent, receiver, liquidator or sequestrator, (ii) providing investment counseling services and portfolio management services, and (iii) issuing payment, credit or charge cards and, in cooperation with others (including financial institutions), operating a payment, credit or charge card plan (440(2)).

Additionally, the ICA clarifies that a company may (i) act as an agent and provide consulting or appraisal services in respect of real property, (ii) hold, manage and otherwise deal with real property, (iii) subject to certain restrictions, provide information processing services in Canada, (iv) promote merchandise and services to holders of payment, credit or charge cards issued by the company, (v) subject to certain restrictions, sell lottery and urban transit tickets, and (v) act as a custodian of property. There are a number of additional powers to engage in services, primarily relating to information technology, that in certain instances are subject to the prior written approval of the Minister (441(1)).

Subject to the consent of the Minister, a company may carry on activities that are "reasonably ancillary to the business of insurance carried on by the company", including:

- Providing safety and risk prevention services;
- Operating rehabilitation and training and development centers;
- Providing computer systems to independent brokers and agents;
- Providing support to independent insurance brokers and agents; and
- Operating repair and appraisal centers (441(1)(h)).

Further, a life company may engage in specialized business management or advisory services, subject to any prescribed terms and conditions ((441(1)(1.1)). Finally, a company may act as agent for any person in respect of the provision of services provided by a financial institution, an entity in which the company is permitted to have a substantial investment or a prescribed entity (442(1)).

In short, an OSFI regulated Canadian insurance company is prohibited from engaging in non-insurance activities unless those activities are "financial services" or are otherwise authorized by the ICA as set out above.

The ICA also contains extensive restrictions upon insurance companies holding substantial investments in entities that carry on certain non-insurance activities. The ICA provisions, in some cases, prohibit it, in some cases require control and in others require regulatory approval.

civil law (Québec)

A Québec insurer may not acquire directly or through a partnership or legal person it controls more than 30 per cent of the assets or the voting rights attached to the shares of a legal person, or more than 30 per cent of the assets or the voting rights attached to the shares of a cooperative or other similar legal person whose head office is situated outside Québec. The voting rights may not enable the insurer to elect more than one-third of the directors of the legal person.[17] Notwithstanding this rule, an insurer may (1) acquire directly all or part of the shares of a legal person that only carries on activities similar to those the insurer is authorized to carry on; and (2) acquire all or part of the shares of a legal person in such cases as are determined by government regulation. Except in the case of a professional order, an insurer may acquire shares of a legal person through a holding company.[18]

Section 38 of the Québec Insurance Regulation provides that an insurer may acquire the shares of a legal person:

i) whose principal activity is the purchase, management, sale or leasing of immovables;

ii) whose principal activity is the offering of shares in investment portfolios, the making of loans and investments, factoring, leasing, the offering of computing services or actuarial advisory services;

iii) whose principal activity is complementary to the distribution of certain insurance products

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[17] Section 244.1 of the Québec Insurance Act

[18] Section 244.2 of the Québec Insurance Act

such as travel assistance, legal assistance and road assistance; or

iv) whose activities are those of a firm within the meaning of the Québec Distribution Act or that offers financial products and services outside Québec.

Québec insurers are also prohibited from owning directly or indirectly more than 20 per cent of the shares of a brokerage firm or voting rights attached to its shares.[19]

14. **Do the terms and conditions of insurance contracts need to be**

i) **submitted to the regulator as a kind of formal requirement or**

ii) **approved by the regulator prior to entering into effect?**

common law

Automobile insurance policies are strictly regulated and are typically issued in standard form, subject to changes in regards to levels of coverage and additional coverage.

Other types of insurance contracts do not require regulatory approval.[20]

civil law (Québec)

Automobile insurance policies are strictly regulated and are issued in standard form.

The AMF requires a copy of the proposed insurance policies and riders with the application for a new license or with an application to amend an existing license to add a new class of insurance but otherwise, insurers do not need regulatory approval for other types of insurance contracts.

Impact of Qualification – Law of Contracts

15. **Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?**

common law

Insurance contracts issued by a non-licensed party will contravene Canadian insurance statutes. Generally, if a statute is silent on the issue of contracts that contravene its provisions, contracts that do so are considered illegal and therefore may be voidable. As a result, a policyholder who is party to an insurance contract with a non-licensed insurer would be able to terminate the contract if he chose to do so. However, the non-licensed insurer would likely not be able to terminate the contract because there is an exception to the general rule of illegal contracts being void which would work against the non-insured insurer. In respect of that exception, the modern approach of Canadian courts is to allow enforcement of an illegal contract if refusal to enforce the contract would produce a harmful effect on the party for whose protection the law that makes the contract illegal exists.

In the context of insurance, courts have held that the purpose of the licensing requirement in insurance statutes is to protect policyholders (by ensuring that only desirable persons carry on the business of insurance). Therefore, whether an insurance contract with a non-licensed insurer will be considered enforceable will depend upon whether the policyholder would be harmed by voiding the contract and whether enforcement is in line with the protection of the policyholder. Since it is difficult to imagine a scenario where a policyholder would not be harmed by an attempt by an unlicensed insurer to void the contract, practically, it would appear that a policyholder would always be able to enforce an insurance contract with a non-licensed insurer.

If a court holds a contract void by way of illegality, the plaintiff will not be able to recover damages unless he can maintain an independent cause of action (an action that does not rely upon the illegal contract for its advancement). Generally, a plaintiff also cannot recover money or property transferred under an illegal contract, but there are certain exceptions to this rule as well. One exception that is particularly relevant to policyholders is as follows: if the illegal contract contravenes a statute that was passed to protect a class of persons of which the plaintiff is a member, the plaintiff will be allowed to recover the money or property transferred under the contract. Therefore, since insurance statutes are passed to protect policyholders, a policyholder to an illegal insurance contract will be able to recover the premiums previously paid under the contract. However, this exception will not apply if the policyholder contracted knowing of the illegality.

civil law (Québec)

Like any contracts executed under Québec laws, an insurance contract may be annulled by a court based on a defect of consent, which may be vitiated by error, fear or fraud (arts. 1399 CCQ and following). If the error is induced by fraud (art. 1401 CCQ), the victim can ask for a variety of recourses:

> **1407:** A person whose consent is vitiated has the right to apply for annulment of the contract; in the case of error occasioned by fraud, of fear or of lesion, he may, in addition to annulment, also claim damages or, where he prefers that the contract be maintained,

[19] Section 148 of the Québec Distribution Act

[20] Provincial regulators occasionally ask to see a copy of policies when an insurer applies for a new license or for an amended license authorizing the issuance of a new class of policies.

apply for a reduction of his obligation equivalent to the damages he would be justified in claiming.

An insurance contract issued by a non-licensed party will contravene the Québec Insurance Act and the Québec Distribution Act which may result in the non-licensed party being convicted of an offence or subject to the payment of penalties under said statutes. (Please see our response to question 12 above).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

common law

While prudential issues (e.g. governance, solvency) relating to Canadian-domiciled insurance companies and to Canadian branches of foreign insurance companies are typically regulated by the ICA in the case of federal insurers and foreign insurers operating Canadian branches, the regulation of insurance activities, including insurance contracts, (and the governance and solvency of provincially incorporated insurers), is a provincial/territorial matter. Accordingly, in addition to the various relevant regulations thereunder, the legislation applicable to insurance contracts in Canada are:

- *Insurance Act* (Ontario)
- *Insurance Act* (British Columbia)
- *Insurance Act* (Alberta)
- *The Saskatchewan Insurance Act* (Saskatchewan)
- *The Insurance Act* (Manitoba)
- *Insurance Contracts Act* (Newfoundland and Labrador)
- *Insurance Act* (Prince Edward Island)
- *Insurance Act* (Nova Scotia)
- *Insurance Act* (New Brunswick)
- *Insurance Act* (Nunavut)
- *Insurance Act* (Yukon)
- *Insurance Act* (Northwest Territories)

civil law (Québec)

The most important statutes pertaining to insurance under the civil law of Québec are the following:

1. *Civil code of Québec*, in particular arts. 2389-2628 contained in Chapter XV;

2. *An Act Respecting Insurance* and the regulation adopted thereunder;

3. *An Act Respecting the Distribution of Financial Products and Services* (and related regulations);

4. *Supplemental Pension Plans Act*;

5. *Automobile Insurance Act*; and

6. *Consumer Protection Act*.

Furthermore, the AMF provides for various guidelines with respect to insurance.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

According to Article 10 of the 1992 Statute, the common law

Yes. Such statutes typically require certain mandatory inclusions in insurance policies, such as certain mandatory statutory conditions and certain information applicable to the insurance (e.g., name of insurer, name of insured, name of beneficiary, amount of premium, date the insurance takes effect, date insurance terminates).

In some provinces/territories, certain classes of insurance (typically including automobile, fire, and accident and sickness insurance) have their own set of statutory conditions.

Automobile insurance policies are typically issued in a standard prescribed form, with certain minimum coverage levels. In some provinces (British Columbia, Saskatchewan, Manitoba, Québec), a government insurance company is the primary automobile insurer.

civil law (Québec)

Yes. As mentioned in our response to question 1 above, the general principles of contracts contained in the CCQ apply to insurance contracts subject to the considerable limitations contained in the Chapter XV of the CCQ on insurance. For example, art. 2414 CCQ provides that any clause in non-marine insurance contract which grants the client, the insured, the participant the beneficiary or the policyholder fewer rights than are granted by the provisions of Chapter XV on insurance is null.

The CCQ provides that the essential elements of an insurance contract are (i) the risk; (ii) the duration of the protection; (iii) the premium; and (iv) the payment. A contact implies the acceptance of an offer (art. 1386 CCQ). This rule is also true for insurance contracts. However, in the case of insurance contracts, the CCQ considers that the offer is made by the client (to become the policyholder) and not by the insurer. Therefore, the contract is formed when the insurer accepts to cover the risk (art. 2398 CCQ).

No formality is required for the formation of the contract, which could be formed orally. However, the insurer should remit a copy of the policy to the policyholder (art. 2400 para 1 CCQ). It should be noted that in cases where there are important discrepancies (in particular on the risk covered, the amount of the premium or the amount of the coverage) between the offer made by the policyholder and the acceptance by the insurer, the insurer has not accepted the risk, and

no contract is formed until the policyholder accepts the changes. In order to be able to oppose these changes to the policyholder, the insurer needs to bring such changes to the attention of the policyholder in a distinct document, failing which, the offer first made by the policyholder would prevail (art. 2400 para 2 CCQ).

In addition, regulations dictate what information should be provided by the insurer to the policyholder[21]. The information to be provided by the insurer or the insurance representative is consistent with what is required under the common law provinces.

For life insurance, three more conditions have to be respected for the contract to be formed: (i) the insurer must accept the offer as such; (ii) the client must pay the first premium; and (iii) there must not be a change in the insurability of the risk since the application was signed (art. 2425 CCQ).

For accident and sickness insurance, the contract is formed when the policy is delivered to the policyholder (art. 2426 CCQ).

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

common law

Yes. While each province/territory has its own unique governance of the market conduct of insurers, such statutes typically require certain mandatory inclusions in insurance policies, such as certain mandatory statutory conditions and certain information applicable to the insurance (e.g., name of insurer, name of insured, name of beneficiary, amount of premium, date the insurance takes effect, date insurance terminates).

In some provinces/territories, certain classes of insurance (typically including automobile, fire, and accident and sickness insurance) have their own set of statutory conditions, while certain other classes of insurance are entirely exempt from the statutory conditions.

Automobile insurance policies are typically issued in a standard prescribed form, with certain minimum coverage levels. In some provinces (British Columbia, Saskatchewan, Manitoba, Québec), a government insurance company is the primary automobile insurer.

civil law (Québec)

Article 1436 CCQ provides protections against clauses which are illegible or incomprehensible to a reasonable person if they are found in a contract of adhesion. A contract of adhesion is defined as a contract in which the essential stipulations have been imposed by one party to the other and where such stipulations were not negotiated (art. 1379 CCQ). In addition, art. 1437 CCQ provides important protections against abusive clauses.

The Consumer Protection Act (Québec) provides for some protections with respect to insurance, such as the prohibition of refusing credit to consumers due to the fact that no insurance is purchased through the merchant (s. 111); the right of the consumer to fulfill, through his own insurance, an insurance requirement of a credit contract (s. 112 para 1); the obligation of the merchant to inform the consumer of the afore-mentioned right (s. 112 para 2); the obligation of the merchant to remit a copy of the insurance contract for both life and health insurance (s. 113) and for insurance subscribed for in the context of a contract of credit (s. 114).

Furthermore, various statutes and regulations also provide for certain consumer protection obligations. Most notably, several regulations adopted under the Québec Distribution Act provide for the types of information / disclosure that an insurer or a representative of an insurer must provide when offering insurance to consumers and the *Charter of the French Language* provides for the obligation to provide brochures to Québec based consumers in the French language under no less favorable terms than those provided for in the English versions.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Utmost Good Faith

In Canada, as in many jurisdictions, contracts of insurance are subject to the legal doctrine of *uberrimae fidei,* which means ''utmost good faith''. According to this doctrine, any material misrepresentation by the insured or failure by the insured to disclose material information to the insurer at the time of entering into the contract of insurance will entitle the insurer to avoid liability. This obligation goes further than ensuring that the information provided is accurate. It also requires full and voluntary disclosure by the applicant of any relevant information, whether or not the insurer specifically asks for it. In Québec, this principle of ''utmost good faith'' is found in art. 2408 CCQ.

At the same time, insurers also owe a duty of good faith to their customers, and this duty is an implied term of the contract of insurance. Courts in Canada have determined that this obligation to act in good faith is separate from the insurer's obligation to compensate its insured for a loss covered by the policy. Accordingly, breach of an insurer's obligation to act in good faith is a separate or independent wrong giving rise to a cause of action against the insurer.

Regulation of Insurance Contracts and Market Conduct

The majority of insurers in Canada are federally incorporated or federally licensed as a branch and, as such, their solvency is regulated by OSFI, the federal

[21] *Regulation respecting information to be provided to consumers (Québec)*

prudential insurance regulator. However, insurance contracts and the marketing and sale of insurance products (market conduct) are regulated by the Canadian provinces and territories. As explained earlier, this is a result of the separation of powers under Canadian constitutional law and case law determining that insurance contracts fall under ''property and civil rights''. In Québec, as mentioned above, the regulatory authority is the AMF.

Specific Consumer Protection Provisions

As indicated above, the statutes of many Canadian provinces and territories contain specific provisions that are designed to protect consumers of insurance from inappropriate practices by insurers. In addition to requirements with respect to the provision of information, the Ontario legislation, for example, includes a regulation that prescribes a series of acts as ''unfair or deceptive'' which are prohibited. Examples include:

- Misrepresentation of any of the terms, benefits or advantages of any contract of insurance;
- Any false or misleading statement as to the terms, benefits or advantages of any contract of insurance;
- Any incomplete comparison of any contract of insurance with that of any other insurer for the purpose of inducing a lapse or surrender of a contract of insurance;
- Making the issuance of a policy of automobile insurance conditional on the insured purchasing another insurance policy; and
- Use of a document in place of a form approved for use by the Superintendent.

Under the Ontario *Insurance Act*, the Superintendent of Financial Services has broad investigative powers to determine if an insurer has committed an unfair or deceptive act or practice, as well as the power, subject to the right to a hearing, to issue a cease and desist order enjoining the insurer's actions, including its engagement in the business of insurance altogether. Pursuant to recent amendments in Ontario, these matters are now also subject to the administrative monetary penalty regime which is designed to further encourage regulatory compliance and prevent financial benefit from violations. Under the *Act respecting Insurance (Québec)*, the AMF has similar investigative powers.

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

Yes, there is a statutory definition of both "insurance activity" ("actividad aseguradora"), as an economic phenomenon, and an "insurance contract" per se. Both are interrelated. "Insurance activity" is defined in the Insurance Market Act (enacted in 2008, *Ley Reguladora del Mercado de Seguros*, art. 7) as requiring the following elements:

- To accept the transfer of "insurable risk";
- To someone who acts as an insurer;
- In exchange for payment of a price ("premium");
- With the purpose of dispersing the risk among similar risks in order to bear the economic cost.

Meanwhile, an "insurance contract" is defined in the Insurance Contracts Act (enacted in 2011, *Ley Reguladora del Contrato de Seguro*, art. 3) as requiring the following elements:

- Insurer obligated to indemnify insured for a loss, or pay capital or perform some other obligation;
- In exchange for payment of a premium;
- In the event of the occurrence of an event the risk of occurrence of which is insured.

2. **Does an insurance contract require an element of uncertainty? Please describe.**

Yes. The Insurance Market Act requires "insurable risk" (art. 2), which the Insurance Contracts Act (art. 40), in turn, defines as the possibility of occurrence of a future and uncertain event that does not depend on the will of the insured. It then specifies that events that are certain to occur and those that are physically impossible are not insurable risks, nor are wagers.

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

Yes. See answer 1 above.

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?**

Yes. The Insurance Contracts Act specifically requires "insurable interest" and defines it as a licit interest that the loss not occur.

5. **Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?**

Generally, the requirement is that the "insured" has an insurable interest. However, the insured is not necessarily the policyholder (understood as the person who takes out the insurance contract) nor is he necessarily the beneficiary (understood as the person to whom the obligation of the insurer is owed in the event of a loss). Where the policyholder is not the insured, special rules apply. In property and casualty, insurable risk will be any sort of economic interest. In personal lines, if the policyholder is not the insured the law recognizes insurable interest in the life of persons to whom the policyholder owes or can legally request alimony support, persons whose death or disability can cause direct economic loss, persons who have an emotional bond (assuming the insured agrees), and employees.

6. **Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?**

Yes, see answer 1 above. It does affect the classification as "insurance activity", for which a license issued by the government is required. It is not expressly mentioned in the definition of "insurance contract".

7. **Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?**

No.

Distinction from Similar Types of Contracts and Exemptions

8. **Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.**

i) **Contracts of gambling and chance**

Yes, they are similar, but expressly excluded as insurance. Gambling is not prohibited but gambling contracts (and debts) are unenforceable in court.

ii) Warranty, guaranty or any other surety contracts

Where warranty or guaranty contracts are sold by someone acting as an insurer *en masse* and where rates are set based on actuarial principles equivalent to those used in insurance, the contract is considered "insurance" and must be sold by authorized insurers. However, where a person issues a personal guaranty to secure an obligation on an individual basis it is not insurance.

iii) Financial contracts such as hedging contracts/swaps/derivatives

In principle, they are not considered insurance. They have their own set of regulations issued by CONASSIF, the national financial services umbrella regulator. However, due to the broadness of the definitions of "insurance activity" and "insurance contract" (see answer 1 above), the issue may arise in the future.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

There is one main exemption related to assistance services. Although assistance services (such as home assistance, roadside assistance, travel assistance, etc.) sometimes meet all of the criteria listed in answer 1 above, there is a specific ruling issued by the Insurance Superintendent exempting some assistance services from regulation as insurance under certain criteria, for example that pricing is not established following actuarial principles and that the services are provided through use of the assistance company's own infrastructure (not hired-out).

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

No.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Yes. A license issued by the Insurance Superintendent is indispensable to act as risk-taker ("insurer") in an insurance contract.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

The risk-taker faces the following consequences:

- Fine of up to 1,000 times the "base salary" established for Costa Rican government workers (approximately USD 500,000).
- Inability to obtain a license from the Superintendent if the above fine is unpaid.
- Eventually, criminal prosecution for fraud. (There is no specific criminal statute governing this type of fraud. The Insurance Superintendent is of the position that selling insurance without a license falls within the general fraud statute. This remains to be seen in practice.)

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

Yes. Insurers may not engage in any other activity that is not "insurance activity" (see answer 1 above). This a statutory requirement.

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

Although the letter of the law establishes a simple "file and use" system regarding insurance contract forms and rates, in practice and under applicable regulations the system has been turned into a prior approval system.

Impact of Qualification – Law of Contracts

15. <u>Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?</u>

The contract itself is not void. The policyholder is entitled to claim whatever damages it can show under the contract.

16. <u>Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.</u>

Yes. There is an extensive Insurance Contracts Act that governs the general aspects of insurance contracts, as well as the particulars of certain kinds of insurance (e.g., fire, liability, transportation, life, health, etc.).

17. <u>Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.</u>

Yes. Insurance contracts must be made in writing, though no specific medium is required (even electronic media are valid). The contract must be

made in Spanish. The Insurance Contracts Act's provisions are deemed imperative and thus an insurer cannot contract out of those provisions, except where the Act expressly permits it to do so. The law provides for many specific rules applicable to insurance generally and to specific types of insurance as well. The law includes the minimum content that an insurance policy must have.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes. Consumer protection notions heavily influence the Insurance Market Act and the Insurance Contracts Act, among them:

- A statutory definition of the *in dubio pro* insured principle.
- Provisions that are imperative (insurers cannot contract out of most provisions of the law).
- Standard rules applicable to contracts of adhesion (for example, the use of *contra proferentem* rule in the event of contract ambiguity).
- Significant pre-contract information disclosure requirements relative to the proposed contract, the insurer, and the intermediary if applicable (including disclosure of intermediary commission levels).
- Formal requirements to make exclusions in contracts clearly visible and distinguishable from the rest of the policy text.
- Significant scrutiny by the insurance regulator during the policy form and rate filing process, including preventive correction of possibly abusive or misleading contract terms.
- Special rules applicable to insureds under group policies.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Not at this time.

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ANNE BUHL BJELKE

Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

There is no statutory or case law-based definition of an insurance contract. However, the generally accepted definition of an insurance contract under Danish insurance law is:

> "An agreement for the transfer of an economic risk of the occurrence of an uncertain event in exchange for a fee, which is calculated on the statistical basis of the distribution of this risk on a multitude of insurances contracts.[1] "

Although case law on this particular issue is sparse, courts are considered to apply the said definition of an insurance contract.[2]

The reason why such definition is not contained in the primary piece of legislation on insurance contracts, the Danish Insurance Contracts Act[3], is that the preparatory commission for the Act found that codifying an exact definition in the Act would deprive the concept of its flexibility. The commission considered jurisprudence a more suitable authority to develop such a definition.[4]

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. Part of the definition and a central element in what may be considered an insurance contract is the transfer of a risk incidental to an uncertain event. It is also assumed that the event has to be one of which the insurer has no control.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes. A contract which does not provide for the transfer of a risk is not considered an insurance contract under Danish law.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Yes. An essential element of insurance against loss or damage under Danish law is that the insured must have an insurable interest in the subject matter insured. According to Section 35 of the Danish Insurance Contracts Act, an insurable interest is any legal interest which may be economically assessed in terms of value. E.g. insurance against the risk of criminal fines is not a legal interest.

As for life, accident and disability insurances, it is possible to enter into insurance contracts even though the policyholder has no economic interest in the subject matter of the insurance.[5] However, for life insurance where the policyholder is different from the person against whose death insurance is taken out, consent of the concerned individual is required in order to enter into an insurance contract where the insurance company undertakes to pay out more than collected premiums with accrued interest in case of the person's death.[6]

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

It can be attributable to a third party. Under Danish law, an insurance contract concerning the interest of a third-party may be entered into if the insured carries the risk of loss or damage to the subject matter or if the insurance concerns property in which multiple parties have an interest.[7] By statute, property insurance is deemed to cover all with an in rem interest in the subject matter of the insurance,

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[1] *Ibid*.

[2] The Danish Supreme Court decision of 29 January 1985, published in the Danish weekly law reports in 1985, p. 205. See also Ivan Sørensen, Forsikringsret, p. 37.

[3] In Danish *Forsikringsaftaleloven*, Consolidated Act No. 999 of 5 October 2006.

[4] Ivan Sørensen, Forsikringsret, 5th Ed., 2010, Jurist- og Økonomforbundets Forlag, p. 35, Henning Jønsson & Lisbeth Kjærgaard, Dansk Forsikringsret, 9th Ed., 2012, Jurist- og Økonomforbundets forlag, p. 60, and Preben Lyngsø, Forsikringsaftaleloven med kommentarer, 4th Ed., 1992, Jurist- og Økonomforbundets forlag, pp. 33-34.

[5] Sections 97 and 119 of the Danish Insurance Contracts Act and Jønsson, p. 457 et seq.

[6] Section 55 of the Danish Financial Business Act (In Danish *lov om finansiel virksomhed*).

[7] Section 54 of the Danish Insurance Contracts Act, Ivan Sørensen, Forsikringsaftaleloven med kommentarer, 1st Ed., 2000, Forlaget Thomson, p. 149, and Jønsson & Kjærgaard, Dansk Forsikringsret, p. 583 et seq.

including but not limited to the owner of the property. Property insurance is therefore deemed made out with respect to any other owner or lien holder of the property insured.

It is also possible to insure the interest of a third party with regard to liability insurance, e.g. if the standard terms designate a non-specific group of entities or people, as is the case with for instance vehicle insurance in which case the standard terms and conditions designate "any who legally uses the vehicle, allows it to be used or is the driver of it" as an insured under the contract.[8]

Group policies usually designate a parent company as the policyholder and all its subsidiaries and controlled companies as the insured. Even though the parent company is the sole policyholder and the only explicitly named insured under the policy, all companies qualifying as subsidiaries as per the terms of the policy are covered.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The definition of an insurance contract under Danish law (see above under question 1) contains a requirement that the fee charged for the assumed risk is statistically calculated based on a multitude of insurance contracts. By this definition, the risks assumed under an insurance contract are to be mitigated by a large number of similar risks.

However, some contracts whereby the risk is not directly mitigated by the insurer assuming a large quantity of similar risks may qualify as insurance contracts. This is the case with for instance credit insurances, which in nature somewhat resemble guarantees.[9]

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Although the Danish Insurance Contracts Act does not contain a definition of life insurance, just as it does not contain a definition of insurance contracts in general, no distinction is made between life insurance and non-life insurance with regard to the definition of the agreement as an insurance contract.[10]

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Although gambling and chance transactions contain the exchange of the risk of a certain outcome for a fee, the person entering into a gambling or chance agreement is doing so for the purpose of financial gain. Contrary to this, a person taking out insurance does so with the intention of insuring his interest in the subject matter of the insurance contract, not for financial profit. Under Section 39 of the Danish Insurance Contracts Act, the insured under a non-life insurance has no legal standing in claiming any amount in excess of what is required to cover the damage, loss or injury incurred.

ii) Warranty, guaranty or any other surety contracts

Although similar in terms of the outcome of the individual contract, warranties, guarantees and sureties differ from insurance contracts in that the risk assumed with warranties, guarantees and sureties is calculated on a transaction-to-transaction basis and not by offering a large quantity of similar contracts as an insurance company does when offering insurance.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Some financial contracts share similarities with insurance contracts, namely that the outcome of the contract is uncertain and that the contract entails an assumption of risk by one of the parties in exchange for a fee.

Similar to gambling and chance transactions as described above, financial contracts and insurance are markedly different from the perspective of the insured. An insurance contract is entered into by the insured with a view to establishing economic protection and certainty against the risks of life and to restoring the physical and financial ability of the

[8] Jønsson & Kjærgaard, Dansk Forsikringsret, p. 583 *et seq.*

[9] Danish Supreme Court decision published in the Danish weekly law reports, UfR 1991.523, Ivan Sørensen, Forsikringsaftaleloven med kommentarer, p. 33, and Peter Blok, Kreditforsikring – forsikring eller kaution?, published in the Danish weekly law reports, UfR.1992B.25.

[10] Ivan Sørensen, Forsikringsaftaleloven med kommentarer, p. 31-32.

insured to its pre-event state. A financial contract, on the other hand, is entered into by the customer with the purpose of financial gain or hedging on a transaction-to-transaction basis. No clear distinction or case law exists on this.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Generally, any contract meeting the requirements of insurance contracts is deemed as such under Danish insurance law.

As for some types of contracts, such as subscription contracts whereby a company undertakes the maintenance of the subscriber's property, it remains somewhat uncertain whether the contract, when entered into by a company which does not engage in insurance business, may be deemed an insurance contract.[11] Due to the fact that such contracts are generally not considered to contain an assumption of risk of an unknown or unpredictable event, subscription contracts are in all likelihood not insurance contracts under Danish insurance law.[12] It is also unclear whether credit insurance/surety should be considered an insurance contract or a guaranty.[13] In addition hereto, warranties on goods may in some circumstances constitute an insurance contract.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

No. Contracts meeting the requirements of an insurance contract are deemed as such.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Under Section 11 of the Danish Financial Business Act[14], a license is required in order to do insurance business in Denmark. Insurance business is characterized as entering into contracts meeting the requirements of the generally accepted definition of an insurance contract as the risk-assuming party.[15]

If an entity without a license enters into insurance contracts, such contracts are voided by the Danish Financial Supervisory Authority.

12. What are the legal consequences for the risk-taker acting without license?

If the Danish Financial Supervisory Authority[16] determines that a business enters into insurance contracts as an insurer without a license, the Authority will order the activity to cease and that all premiums are returned to the would-be insured.[17]

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

There is no complete prohibition against non-insurance business, but licensed insurance companies are only allowed to enter into business listed in the Danish Financial Business Act.[18] These are: (1) Activities which are considered ancillary to insurance business, (2) other business to ensure or wind up previously entered into commitments and activities with an intention to participate in the restructuring of companies, and (3) other activities carried out through joint ownership of a non-financial services company if the insurance company does not, directly or indirectly, control the business or is part of the same group of companies.

Ancillary activities are to be construed in conjunction with the authorized business of the company and may not assume a scale where they become the dominant activity of the insurance company. The Danish Financial Supervisory Authority is authorized to order that ancillary activities be hived off.[19]

The wind-up and restructuring of commitments previously entered into is intended to allow insurance companies to take part in the restructuring of companies, but it is not possible to set a firm limit on the duration of the insurance company's involvement. The insurance company has to notify the Danish

[11] Decisions rendered by the Danish Eastern High Court, the Danish weekly law reports, UfR 1945.627, UfR 1947.441, UfR 1953.630, UfR 1955.194 and UfR 1966.488. See also Ivan Sørensen, Forsikringsaftaleloven med kommentarer, p. 33 *et seq.*

[12] Lyngsø, Forsikringsaftaleloven med kommentarer, p. 35.

[13] See Question 6 above.

[14] In Danish: *Lov om finansiel virksomhed*, Consolidated Act No. 705 of 25 June 2012.

[15] See above under Question 1.

[16] In Danish: *Finanstilsynet*.

[17] See Merete Hjetting, Thomas Kjøller, Marianne Simonsen and Malene Stadil, Lov om finansiel virksomhed, 1st Ed., 2007, p. 82 *et seq.*, with reference to a decision of the Danish Financial Supervisory Authority published in the 1985 Annual Report of the Authority, p. 33.

[18] See Sections 24-26 of the Act.

[19] Section 24(2) of the Danish Financial Business Act.

Financial Supervisory Authority of any such participation.[20]

The ability of insurance companies to carry out business through joint ownership with non-financial corporations is intended to allow insurance companies to adapt to the structural developments and thereby ensure the highest possible yield.[21]

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

It is not a requirement under Danish insurance law that the insurer submits insurance contracts to a regulator.

ii) approved by the regulator prior to entering into effect?

Approval by a regulator is not a requirement for the insurer to use the terms and conditions in insurance contracts.

As a general rule, the insurer is free to draft the terms of insurance contracts. However, there are certain requirements as to the individual insurance contract by which the insurer has to abide.[22]

In addition to the requirements applying to specific types of insurance contracts, mandatory provisions contained in regular legislation, such as the Danish Marketing Practices Act (in Danish markedsføringsloven), also have to be observed by the insurance company when drafting its terms and conditions.[23]

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

If an insurance contract is entered into by a non-licensed party, the contract may be declared null and void by the Danish Financial Supervisory Authority. See above under Questions 11 and 12.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes. The primary piece of legislation is the Danish Insurance Contracts Act which applies to insurance contracts entered into by an insurance company. Parts of the Danish Insurance Contracts Act are mandatory whereas other parts may be deviated from by agreement.

The Danish Insurance Contracts Act does not apply to reinsurance. However, for similar issues and contracts not directly governed by the Danish Insurance Contracts Act, the Act may apply by analogy.[24]

Furthermore, for specific types of insurance contracts (usually mandatory insurance), mandatory requirements apply, including but not limited to;

Fire insurance: as per the requirements stipulated in Section 60 of the Danish Financial Business Act.

Mandatory[25] insurance for dogs: as per the requirements stipulated in Order No. 485 of 25 September 1984.

Mandatory[26] liability insurance for insurance agents and insurance brokers: as per the requirements stipulated in Order No. 1390 of 22 December 2008.

Mandatory[27] liability insurance for auditors and accountants: as per the requirements stipulated in Order No. 661 of 26 June 2008.

Mandatory[28] motor liability insurance: as per the requirements stipulated in Order No. 579 of 6 June 2007.

Mandatory[29] workers' compensation insurance: as per the requirements stipulated in the Danish Consolidated Act on Worker's Compensation.

Liability insurance for practicing Danish lawyers is not mandated by statute. However, the Danish Administration of Justice Act stipulates that all Danish lawyers are members of the Danish Bar and Law

[20] Section 25 of the Danish Financial Business Act.

[21] Hjetting and others, Lov om finansiel virksomhed, p. 164 *et seq.*

[22] Jønsson & Kjærgaard, Dansk Forsikringsret, p. 113.

[23] *Ibid.*

[24] Lyngsø, Forsikringsaftaleloven med kommentarer, p. 35.

[25] Section 8(2) of the Danish Dog Act, in Danish *Hundeloven*.

[26] Section 20 of the Danish Insurance Mediation Act, in Danish *Forsikringsformidlingsloven*.

[27] Section 3 of the Danish Act on Approved Auditors and Audit Firms, in Danish *Revisorloven*.

[28] Section 105 of the Danish Road Traffic Act, in Danish *Færdselsloven*.

[29] Section 48 of the Danish Consolidated Act on Worker's Compensation, in Danish *Lov om arbejdsskadesikring*.

Society[30], and the bylaws of the Society prescribe a duty to take out liability insurance.[31]

The regulatory framework for insurance business in Denmark is primarily contained in the Danish Financial Business Act.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Generally, no requirements exist in respect of form for an insurance contract.

With regards to content, the legal requirements referred to under Question 16 often lay down a minimum coverage and terms in respect of termination, run-off, reinstatement and legal effects of misrepresentation and lack of payment of premium.

Also see below under Question 18 concerning consumer protection.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes. Both the Danish Insurance Contracts Act, the Danish Financial Business Act, executive orders issued on the basis of these two acts as well as the Danish Insurance Mediation Act contain certain requirements with respect to insurance contracts targeting consumers as well as rules on the conduct of insurance companies towards consumers.

Consumer insurance is defined under Danish law as insurance contracts where the insured predominantly acts outside his business sphere when entering into the insurance contract.[32]

Chapter 1A[33] of the Danish Insurance Contracts Act contains consumer protection regulation, including a prohibition against the insurance company seeking out the consumer at home, at the consumer's workplace or any other place where access is ordinarily restricted. The chapter also includes provisions on specified information to be provided by the insurance company to the consumer prior to entering into the contract as well as provisions on the right of the consumer to cancel an insurance contract within a specified period of time (free-look cancellation).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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[30] Section 143 of the Danish Administration of Justice Act, in Danish *Retsplejeloven.*

[31] Section 61 of the bylaws.

[32] Section 57(2) of the Danish Financial Business Act.

[33] Sections 34 and 34a-34m.

France

SCP Bouckaert Ormen Passemard Sportes

ALEXIS VALEÇON[1]

Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

Neither the Civil Code, nor the Insurance Code precisely defines an insurance contract or an insurance transaction. Article 1964 of the Civil Code does, however, provide the following definition:

> "An aleatory contract is a reciprocal agreement whose effects, as to advantages and losses, either for all the parties, or for one or more of them, depend on an uncertain event.
>
> Such are:
>
> Insurance contracts;
>
> Bottomry bonds;
>
> Gaming and betting;
>
> Contracts for life annuity."

And Article 1104 of the Civil Code draws the following distinction between commutative and aleatory contracts:

> "A contract is commutative where each party binds himself to transfer or do something that is considered the equivalent of what is transferred to, or done for, him.
>
> Where the equivalent consists in a chance of a gain or loss for each party, depending on an uncertain event, the contract is aleatory."

Some specific features of an insurance contract however can be highlighted as follows:

Insurance is usually defined by French legal writers as a transaction by which an insurer promises, in consideration for the payment of a premium, performance for the benefit of another person in the event of occurrence of a fortuitous insured event (J. Kullmann (dir), *Lamy Assurances 2013*, No 2).

The two main criteria are, therefore, the payment of a premium and the existence of an uncertain event that makes the contract aleatory.

In addition, an insurance transaction is based on the principle of risk-sharing, which enables insurers to provide coverage at a reasonable cost.

Finally, insurance contracts are governed by the principle of consensualism, which means that the simple agreement of the parties without any further formalities is sufficient to form a contract. A written document is not a condition of validity of the contract; it merely serves for evidentiary purposes.

2. **Does an insurance contract require an element of uncertainty? Please describe.**

As stated above, uncertainty is a key element of an insurance contract in French law. France's highest ordinary court, the Cour de Cassation, considers that uncertainty is the essence of an insurance contract (Cass., 1st Civ. Div., 4 November 2003, appeal on a point of law No 01-14942).

Uncertainty in an insurance contract is so important that, in its absence, either the insurer or the policyholder may seek avoidance of the contract.

Uncertainty may relate either to the occurrence of a fortuitous event (e.g. a fire), or to the date on which an insured event will occur (e.g. in a life insurance policy, the time of the insured's death is uncertain).

Uncertainty presupposes that the materialization of the insured risk or the date of occurrence of the insured event must not be 'potestative', i.e. dependent on the free will of one of the parties.

It should be mentioned that in two major asbestos cases, the Cour de Cassation construed the concept of uncertainty broadly, by holding that for the purposes of liability policies covering employers of asbestos victims, the uncertainty could lie in the outcome of legal proceedings against such employers (Cass., 2nd Civ. Div., 14 June 2006, appeal on a point of law No 05-13090; Cass., 2nd Civ. Div., 14 June 2012, appeal on a point of law No 11-16958). Since the outcome of [all] legal proceedings is uncertain *per se*, this would imply that all liability policies contain an element of uncertainty. French legal writers have highly criticized the Cour de Cassation's position and suggested that it was based solely on considerations of expediency (see, e.g., A. Valençon, *Lamy Assurances Actualités*, No 203, p. 1 ff, J. Kullmann, *Revue générale du droit des assurances*, No 2006-3, p. 711).

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

Under French law, a transfer of risk from one party to another is not required for a contract to qualify as insurance contract. Indeed, the insured person remains the party at risk (i.e. the person on whose life, health, integrity or status the insurance is taken out), whereas the insurer only commits itself to covering the risk (J. Kullmann (dir), *Lamy Assurances 2013*, Nos 2 and 37)

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance**

1 The author thanks Stéphanie Simon, associate, for her help in the preparation of this contribution.

contract (usually called 'insured interest')?

Generally speaking, the purpose of requiring an insured interest is to avoid speculation on risks: the insured and/or the policyholder must have an interest in the non-occurrence of the insured risks. An insured interest is assessed in different ways depending on the type of insurance involved.

i) An insured interest is considered an essential element of non-life insurance. Article L121-6 of the Insurance Code provides that

> "[a]ny person who has an interest in safeguarding property may have it insured. Any direct or indirect interest in the non-occurrence of a risk may be covered by insurance."

Consequently, in property insurance, the insured interest corresponds to the adverse effect that the occurrence of the risk might have on the insured person's assets, and is therefore mainly a pecuniary interest.

ii) An insured interest is not regarded as an essential element of life insurance. The main requirement for the validity of a life insurance contract is that a risk exists on a human being. Article R321-1 of the Insurance Code defines life insurance transactions are those whose performance depends on the lifespan of an individual. Consequently, the only requirement for such transactions to be valid is that uncertainty exists as to the lifespan of the policyholder (Cass., mixed bench, 23 November 2004, appeal on a point of law No 01-13592).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Article L112-1[2] of the Insurance Code provides for insurance on behalf of others, known as "insurance for whom it may concern" or "omnibus insurance", as follows:

> "Insurance may be contracted on behalf of whom it may concern. The clause shall be valid as insurance for the benefit of the policyholder and as a provision in favor of a third party for the benefit of the known or contingent beneficiary of the said clause."

Such insurance aims at protecting the insured interest of a party or parties other than, or in addition to, the policyholder, regardless of the reason for taking out such insurance, provided that it is lawful.

French law accepts the insured interest need only be determinable at the time of purchasing the insurance, in which case it will be identified when a loss occurs (J. Kullmann (dir), *Lamy Assurances* 2013, No 36). This may be the case, for instance, for omnibus insurance taken out by a building owner on behalf of his contractors.

Furthermore, in a life insurance contract, the policyholder instructs the insurer to pay the insurance proceeds to a third-party beneficiary on the policyholder's death (Insurance Code, art. L132-1[1] *et seq.*). If no beneficiary is designated, the insurance proceeds accrue to the policyholder's estate (Insurance Code, art. L132-11).

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

As previously stated, insurance is based on the principle of risk-sharing: "the contribution of many to the misfortune of few" (F. Ewald, *L'Etat Providence*, Ed. Grasset, 1986). Since insurance contracts are aleatory contracts, insurers need to use probability theorems to assess their risk exposure, but, in French law, this is merely a supervisory and actuarial issue, not a criterion for characterizing an insurance contract.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

A life insurance contract is defined as a contract covering a risk that depends on human lifespan. Apart from the subject matter, the definition of a life insurance contract does not differ from that of a non-life insurance contract. The difference between life and non-life insurance contracts lies mainly in the rules governing them.

Indeed, several provisions of the Insurance Code do not apply to life insurance contracts. E.g:

- Article L113-2[1] concerning the payment of the premiums;
- Articles L113-2[3] and L113-4 concerning the reporting of new circumstances that have the effect of either increasing the risk or creating new risks;
- Article L113-8 concerning fraudulent misrepresentation.

It should also be mentioned that insurance companies, unlike reinsurance companies, may not be licensed for both life and non-life business (Insurance Code, art. L321-1[3]).

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

As previously stated, Article 1964 of the Civil Code lists contracts of gambling and chance ("gaming and betting") along with insurance contracts, bottomry contracts and life-annuity contracts as examples for aleatory contracts.

Insurance contracts are, however, different from contracts of gambling and chance, in that the former are designed to protect against hazards, whereas the latter consist in speculating on hazards. Insurance contracts contemplate a possible loss, whereas contracts of gambling and chance contemplate a possible gain and consequently involve no risk within the meaning of insurance law (M. Provost, *La notion d'intérêt d'assurance*, LGDJ 2009, p. 42 ff).

ii) Warranty, guaranty or any other surety contracts

In 1952, French banks objected to the possibility or permitting insurance companies to issue surety bonds. France's highest administrative court, the Conseil d'Etat, held that since surety bonds involved no uncertainty, because the risk of default was 'potestative' (i.e. dependent on the free will of one of the parties), they could be offered only by undertakings operating in the banking sector (*Renaudin arbitration*, Conseil d'Etat, 6 October 1952).

European Directive 73/240/ECC of 24 July 1973 nevertheless gave insurance companies the right to underwrite contracts of suretyship.

It is important to distinguish between contracts of direct suretyship and contracts of indirect suretyship. The former are 'potestative', because the insured debtor can decide whether to pay or not, whereas the latter are designed to afford insurance protection to the surety, whose risk remains uncertain. Even though insurance companies are now permitted to offer direct suretyship insurance (Insurance Code, art. R321-1[15]), the corresponding contracts do not meet the main criterion for an insurance contract, namely, uncertainty. French legal authors therefore consider that contracts of direct suretyship, unlike contracts of indirect suretyship, are not insurance contracts.

iii) Financial contracts such as hedging contracts/swaps/derivatives

- On the one hand, according to a relatively recent decision of the Cour de Cassation (Cass. Com. Div., 12 July 2011, appeal on a point of law No 10-16873), life insurance contracts cannot be equated with financial instruments.
- On the other hand, in 2004, the Cour de Cassation was asked to recharacterize investment-linked life insurance contracts (*contrats d'assurance-vie de placements*), under which the policyholder pays a premium (which is, in fact, his savings) to the insurer for investment and, in return, the insurer must pay back the amount, together with investment income earned, to the policyholder (or his designated beneficiaries) on a pre-agreed date.

  The characterization of these contracts as insurance contracts was challenged before the Cour de Cassation, because, unlike life insurance contracts, they involve no risk depending on the lifespan of the policyholder: they are simply investment plans.

  The Cour de Cassation refused, however, to recharacterize them. Taking the view that they qualify as aleatory contracts under Article 1964 of the Civil Code, the court maintained their characterization as insurance contracts (Cass., mixed bench, 23 Nov. 2004, appeal on a point of law No 02-17507).

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

The main reason why a contract that apparently meets the characteristics of an insurance contract would not be treated as such is lack of uncertainty. An insurance contract containing no element of uncertainly might be either re-characterized and treated as another type of contract, or declared void.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

Under French Law, a transaction that meets all the requirements of an insurance contract (i.e. uncertainty, payment of a premium and, to a certain extent, risk-sharing) should be qualified as such, irrespective of its possible connection with a non-insurance transaction.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

A risk-taker can enter into an insurance contract on the basis of the license granted to it by the French prudential supervisory authority, *Autorité de Contrôle Prudentiel* (ACP), created by Ordinance No 2010-76 of 21 January 2010.

In this regard, an insurance company that wishes to be authorized to write insurance in France must

comply with the licensing procedure prescribed in Articles L321-1 to L321-3 and R321-1 to R321-12 of the Insurance Code.

A license may be granted conditionally or unconditionally, or refused, by the ACP, which bases its decision on the following criteria: the extent and suitability of the technical and financial means that the applicant plans to implement; the integrity, expertise and experience of the applicant's managers; and the applicant's shareholding structure and shareholder status. In case of refusal, the applicant can challenge the decision before France's highest administrative court, the Conseil d'Etat.

Licenses are granted to insurance and reinsurance companies for specific classes of business. Applicants must choose among the 26 classes listed in Article R321-1 of the Insurance Code. As previously mentioned, insurance companies, unlike reinsurance companies, may not be licensed for both life and non-life business (Insurance Code, art. L321-1[3]).

12. What are the legal consequences for the risk-taker acting without license?

Unlicensed insurance companies cannot do business in France, or they will incur sanctions provided by article L310-26 *et seq.* of the Insurance Code, which include fines (from EUR 4,000 to EUR 300,000 in specific cases) and imprisonment for up to three years.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Insurance companies are subject to the principles of exclusivity and specialty induced by Articles L.321-1[2] and R.321-1[1] of the Insurance Code. Pursuant to these principles, insurance companies may not engage in any business other than classes of insurance business for which they are licensed. There are, however, several exceptions:

- First, an insurance company can act as intermediary and write insurance contracts on behalf of other insurance companies with which it has an agreement. In this case, the insurance company is an agent and does not assume the risk.
- Second, the principle of exclusivity does not bar an insurance company from entering into transactions that are not, strictly speaking, insurance transactions, e.g. tontines, funding transactions, management of collective pension funds, or participation in group retirement plans.

Furthermore, according to Article L322-2-2 of the Insurance Code:

> "Transactions other than those referred to in Articles L310-1 [insurance and capitalization contracts] and L310-1-1 [reinsurance treaties] and Article L341-1 of the Monetary and Financial Code may be carried out by the firms referred to in Articles L310-1 and L310-1-1 only if they are of limited importance in relation to the firm's business as a whole."

The Cour de Cassation considers, however, that contracts entered into in violation of the above provision are not void (Cass., Com. Div., 7 April 2009, appeal on a point of law No 07-189074, comm. J. Kullmann, *Revue générale du droit des assurances*, No 2009-04, p. 1282; M. Marly, *Recueil Dalloz* 2009, p. 2731).

Pursuant to Article L612-39 of the Monetary and Financial Code, the Enforcement Commission of the ACP can impose one or more of the following disciplinary sanctions, commensurate with the seriousness of the violation:

> "1. A warning;
>
> 2. A reprimand;
>
> 3. A prohibition on carrying out certain transactions and any other restriction on the carrying on of the activities;
>
> 4. The temporary suspension of one or more senior managers or, in the case of an electronic money institution engaged in hybrid activities, of the individuals declared responsible for, respectively, the management of the payment service activities or the electronic money issuance and management activities, with or without the appointment of a provisional administrator;
>
> 5. The removal from office of one or more senior managers or, in the case of a payment institution engaged in hybrid activities, of the individuals declared responsible for, respectively, the management of the payment service activities or the electronic money issuance and management activities, with or without the appointment of an interim administrator;
>
> 6. A partial withdrawal of approval;
>
> 7. Complete withdrawal of approval or delisting of the approved persons, with or without the appointment of a liquidator.
>
> The duration of the sanctions referred to in paragraphs 3 and 4 cannot exceed ten years."

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Insurance companies do not need to submit the terms and conditions of their insurance contracts to, or have those terms approved by, the ACP.

The ACP was, however, created to license and supervise insurance (and reinsurance) activities, and may therefore oversee the terms and conditions of insurance contracts.

Indeed, under Article L612-1 of the French Monetary and Financial Code, the ACP can supervise the entire course of the business engaged in by insurance companies, from the promotion of the insurance products offered by them to the terms and conditions of their insurance contracts.

The ACP can carry out on-the-spot or documentary checks.

Depending on the results of its investigations into a company, the ACP may:

- Issue a warning to the company, if the ACP considers that the behavior of the company could be detrimental to its customers' interests;
- Serve the company with formal notice to take appropriate steps to comply with its obligations;
- Provide consumers with any information that the ACP deems appropriate;
- Publish the sanctions imposed;
- Order the company to withdraw any document contrary to life insurance regulations, on pain of a sanction.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Pursuant to Article L310-2 of the Insurance Code, insurance contracts issued by unlicensed insurers shall be null and void. The nullity however, is not effective against policyholders or beneficiaries of policyholders who entered into the contract in good faith.

Insurance contracts issued by unlicensed insurers may be contested by the policyholder or an insured party. If the policyholder or insured party establishes that the nullity of the contract caused him to suffer a loss, the issuer of the contract may be held liable in tort under Article 1382 of the Civil Code ("Any act whatever of man that causes damage to another obliges him by whose fault it occurred to make reparation"). The policyholder and/or the insured would therefore be entitled to claim damages (Cass., 2nd Civ. Div., 28 Feb. 2013, appeal on a point of law No 11-28247).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Generally speaking, most of the provisions of the Insurance Code are a matter of public policy and hence mandatory. In particular, Article L111-2 clearly restricts the parties' contractual freedom to a few provisions.

The Insurance Code also lays down specific duties to provide information and documents both during the pre-contractual phase and during the continuance of the contract.

In particular, pursuant to Article L112-2 of the Insurance Code, prior to the conclusion of the contract, the insurer must provide the insured with an information sheet (*fiche d'information*) giving particulars of the premium and the policy limits and describing the functioning over time of occurrence-based coverage, the functioning over time of claims-based coverage and the consequences of a succession of contracts with different bases for triggering coverage.

The insurer must also provide the insured with a copy of the draft contract and the attachments thereto, or a booklet on the contract precisely describing the coverage and exclusions and the insured's obligations. The draft will not be binding on the insured or the insurer, since only the policy or the cover note will prove their agreement.

Provisions designed to protect policyholders, insureds and beneficiaries may not be varied or excluded by agreement.

In addition, specific obligations have been established by case law. For instance, the Cour de Cassation considers that the two-year limitation period for insurance claims provided for in Article L114-1 of the Insurance Code is unenforceable if the wording of Article L114-1 is not quoted in the insurance contract. In a decision dated 3 September 2009 (appeal on a point of law No 08-13094), the Cour de Cassation added, on the basis of Article R112-1 of the Insurance Code, that insurers must specify the specific causes of interruption of the two-year limitation period, on pain of unenforceability of the clause; and, in a recent decision, the Cour de Cassation extended the requirement to the ordinary causes of interruption of the limitation period (Cass., 2nd Civ. Div., 18 April 2013, appeal on a point of law No 12-19519).

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

In general, insurance contracts must be written in French and in clear print. Article L112-3 of the Insurance Code, nevertheless, provides:

> "(…) when, pursuant to Articles L181-1 and L183-1, the parties to the contract have the possibility of applying a law other than French law, the documents referred to in the first paragraph of this article may be written in a language other than French. The choice of a language other than French shall be made by mutual agreement of the parties and, except if the contract covers major risks as defined in Article L111-6, upon the policyholder's unilateral written request.
>
> When the parties to the contract do not have the possibility of applying a law other than French law, the said documents may nevertheless, by mutual agreement of the parties and upon the policyholder's sole written request, be written in the language, or one of the official languages, of the State of which he is a national (…)"

Moreover, Article L112-4 of the Insurance Code provides that policy clauses that stipulate nullities, forfeitures or exclusions shall be valid only if they appear in very clear print.

Finally, insurance contracts must also comply with the requirements of Articles L112-4, L113-12 and R112-1 of the Insurance Code:

- Article L112-14 provides that the policy must specify, in particular, the nature of the insured risks, the starting point and period of coverage and the policy limit;
- Article L113-12 provides that the policy must specify the duration of the contract and the terms applicable to termination;
- Article R112-1 provides that the policy must specify, in particular, the duration of the mutual undertakings made by the parties, the terms of tacit renewal of the policy, the policyholder's duty of disclosure, the two-year limitation period for insurance claims and the causes of interruption of the said period.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

With respect to the specific case of insurance offered to consumers or non-professionals, Article L133-2 of the Consumer Code provides that the contract terms "must be set out and written in a clear and comprehensible manner." Moreover, "in case of doubt, they are to be interpreted in the sense most favorable to the consumer or non-professional" (Cass., 2nd Civ. Div., 20 Dec. 2012, appeal on a point of law No 11-27225).

More generally, a court cannot interpret a clause that is clear and precise; this prohibition also applies to the questionnaire submitted by the insurer to the insured (Cass., 2nd Civ. Div., 28 June 2012, appeal on a point of law No 11-20793). Article L113-1 of the Insurance Code specifies that exclusion clauses must be "express and limited," failing which the insurer would be unable to enforce the clause and would have to cover the loss (Cass., 3rd Civ. Div., 26 Sept. 2012, appeal on a point of law No 11-19117). Any exclusion clause that needs interpreting necessarily does not comply with Article L113-1 of the Insurance Code (Cass., 2nd Civil Div., 12 Apr. 2012, appeal on a point of law No 10-20831).

In the event of contradiction between a clause contained in the general terms and conditions of a contract and a clause contained in the special terms and conditions of the contract, the latter will prevail (Cass.,1st Civ. Div., 9 Feb. 1999, appeal on a point of law No 96-19538).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Generally speaking, the French insurance and reinsurance market is solid, despite the current financial and economic crisis. French insurers are making large investments in French industrial companies: in 2012, investment in companies for the first time exceeded EUR 1,000 billion, i.e. 56 per cent of insurers' assets (according to FFSA, the French Federation of Insurance Companies, http://www.ffsa.fr/sites/upload/docs/application/pdf/201301/assurance_francaisebilan2012.pdf).

In addition, major changes will be introduced into French insurance law when France transposes Directive 2009/138/EC of 25 November 2009 on the taking-up and pursuit of the business of insurance and reinsurance ("Solvency II"). The deadline for transposition of Solvency II was originally 31 October 2012 but has been postponed to 30 June 2013. Solvency II aims at unifying the regulation of insurance in the European Union, especially with respect to the level of provisions for losses that insurance companies must have in order to reduce the risk of insolvency. Solvency II will soon imply substantial changes in the regulation of insurers and reinsurers operating in the European Union.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

A definition of an insurance contract is neither provided for in the German Civil Code (BGB) nor in the German Insurance Contract Act (VVG). However, the German Insurance Contract Act describes the typical obligations under an insurance contract as follows:

> "The insurer undertakes to cover a certain risk of the policyholder or a third party by paying a benefit upon occurrence of the agreed insured event. The policyholder is obligated to pay the agreed contribution (insurance premium) to the insurer." (Section 1 of the German Insurance Contract Act).

German courts have established certain criteria which must be met in order to qualify a contract as an insurance contract. Pursuant to the respective case law, a contract qualifies as an insurance contract, if someone is

- under the legal obligation to perform certain services against payment in case of;
- the occurrence of an uncertain future event, if;
- the assumed risk is spread between a number of persons threatened by the same peril and the assumption of risk is based on the calculation on the grounds of the law of the large numbers, and if;
- the assumption of risk constitutes an independent obligation of contract and not only a subsidiary obligation.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes, the criterion of uncertainty is a key element of an insurance contract. An uncertain future event is given if it is uncertain whether and when the event occurs, or in case of a certain event, whether it occurs in a specific period of time (e.g. life insurance). If the element of uncertainty did not exist, an insurance contract would either be economically impracticable or resemble a financing agreement. In order to ensure the element of uncertainty the policyholder may not voluntarily make the uncertain event happen without forfeiting the insurance cover.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

A transfer of risk from one party to the other is not part of the general definition of an insurance contract (see under number 1. above). However, as it can be concluded from the general definition, the insurer undertakes to cover a certain risk of the policyholder or a third party. Likewise the German definition puts one party under the legal obligation to perform certain services in case of an uncertain event occurring, which is an indirect way of describing a risk transfer. In fact, an insurance contract without a transfer of risk from the one party to the other is thus not conceivable. However, the risk does not need to transfer from the policyholder: e.g. in case of a bond insurance the policyholder remains liable towards the insurer, while the bond insurance relieves the beneficiary from the policyholder's credit risk.

With regard to finance reinsurance contracts (*Finanzrückversicherungsverträge*), the criterion of transfer of risk is provided for by supervisory law. These contracts usually have a financing function and would thus have to be booked as a liability for accounting purposes. In order to avoid misuse and to ensure proper accounting, a sufficient risk transfer is required according to the statutory definition of a finance reinsurance contract: A finance reinsurance is an insurance under which the total economic assumed risk, which incurs from the assumption of a material actuarial risk as well as from the risk regarding its duration, exceeds the sum of the insurance premium for the total duration of the insurance contract by a limited but material amount (sufficient risk transfer), (i) factoring in interest (present value) or (ii) warranting by the contractual provisions that the economic results are balanced out between the parties for the duration of the contract in order to establish a targeted risk transfer (Section 121 e of the German Insurance Supervision Act).

From the perspective of supervisory law, the criterion of a sufficient risk transfer has an important meaning; if a contract lacks the sufficient risk transfer, the provisions of the German Insurance Supervision Act and in particular the provisions regarding reinsurance are not applicable. As a consequence, possible accounting benefits do not apply either.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

The insured interest can be defined as a relation of value of a legal subject to a certain asset, the impairment of which is economically detrimental to the same. Pursuant to statutory law, the policyholder is not obligated to pay the insurance premium if there is

no interest to be insured at the time of commencement of the insurance cover (Section 80 para 1 of the German Insurance Contract Act).

The exact scope of the requirement of an insured interest is, however, disputed in the legal literature. Most authors hold that at least in the field of indemnity insurance the specific risk covered by the insurance policy must be clearly described. This basically means that the insured needs to have an interest in the subject matter of the insurance contract. Thus, in indemnity insurance contracts, an insured interest is essential.

Whereas the insured party needs to have an insured interest in the area of indemnity insurance, an insured interest does exist from a dogmatic point of view, but has no relevance in the field of fixed-sum insurance and in particular in life insurance contracts. The reason behind this is that the concept of fixed-sum insurance has been established for cases in which a specific damage or, *inter alia*, a preceding concrete interest is not quantifiable.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

The insured interest can be attributed to the policyholder as well as to a third party.

The most relevant example is the insurance for the account of a third party, where the policyholder concludes the insurance contract not in his own name but for the account of a third party (Section 43 para 1 of the German Insurance Contract Act). In this case, the third party is eligible to the insurance benefit but does not necessarily need to be named as a beneficiary (*Bezugsberechtigter*). The third may either be named in the insurance policy or, alternatively, it may be concluded by way of interpretation that the insurance contract has been made for the purpose of the insured interest of the third person.

An insurance contract can also cover the insured interest of the policyholder as well as the insured interest of a third party at the same time. If the circumstances do not indicate that the insurance contract is concluded to the benefit of a third party, it is deemed to have been made for the policyholder's own account.

Further, in life insurance contracts the insured interest is attributable to the beneficiary and in liability insurance contracts to the injured person (*Geschädigter*). In life insurance contracts, the beneficiary needs to be named as such.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

According to the widely recognized definition of an insurance contract, the assumption of risk is based on the calculation on the grounds of the law of the large numbers. However, this element is mainly relevant for matters of supervisory law, in particular with regard to the activity to carry on insurance business as well as with regard to the due calculation of the insurance premium. To this end, one could say that the payment of premium is an inherent part of an insurance contract, as otherwise the risk could not be spread. Therefore, the matter is mainly a supervisory and actuarial issue; for the law of insurance contracts, the element of mitigation by simultaneous insurance of a large number of risks is generally irrelevant. The criterion may, however, still be used for the purpose of distinction between insurance contracts and other similar contracts.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

The general definition of an insurance contract does not make a distinction between life-insurance and non-life insurance. Regarding life insurance, the general definition of an insurance contract can however be specified: Under a life insurance policy, the insurer undertakes to cover the economical risk of the beneficiary deriving from the uncertainty and unpredictability of human life by making a monetary payment which becomes due upon the death of the insured person.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

A contract of gambling and chance has certain similarities to an insurance contract (it puts one party under the obligation to perform certain services in case of an uncertain event occurring). Whereas the purpose of an insurance contract is to secure an existing risk which is independent from the actual contract, in a contract of gambling and chance an artificial risk is established. The goal of the gambler is not to protect itself from a certain event but to take advantage of such event occurring in order to make a benefit. Therefore, in a contract of gambling and chance the element of an insured interest is missing.

ii) Warranty, guaranty or any other surety contracts

Warranty:

A warranty contract is usually connected to another contract, which relates to the object for which the warranty granted. The most prominent example is a warranty under a contract for the sale of goods, which relates to a certain product. Such warranty is granted if a sales contract on the respective product is entered into and can be modified in such contract. Contrary to that, an insurance contract is usually concluded independently from another contract.

Guaranty/Suretyship:

A guaranty contract in the sense of a financial guaranty is comparable to an insurance contract as it serves as a security for a certain risk, *i.e.* the risk that the debtor does not fulfill his obligations vis-à-vis the creditor when due. While a bank which provides financial guarantees does not conclude an insurance contract but conducts banking business and is thus regulated by the German Banking Act, an insurance company may also provide comparable guarantees, but will be regulated under the Insurance Supervision Act.

In the legal literature it is discussed that the element of collective risk mitigation is missing, and therefore turns the guaranty business towards a banking business; banks potentially lay more weight on the likelihood of the individual risk while insurers spread it over the group of similar cover holders.

All of the above types of contracts have in common that they constitute unilateral obligations (*einseitig verpflichtender Vertrag*) under German law, whereas an insurance contract implements bilateral obligations. However, this feature does not provide a meaningful distinction as in commercial reality a counterparty would not issue a warranty/guaranty/suretyship without receiving a benefit.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Similar to insurance contract, financial contracts such as hedging contracts, swaps and derivatives have the purpose to cover a certain risk, namely the risk of price fluctuations. However, the aforementioned financial contracts must have a relation to a certain futures market that enables the conclusion of a counter transaction at any time. Such a market does not exist with respect to insurance contracts. In an insurance contract the balance of risk rather takes place within a mutually supportive group.

Moreover, derivatives single out a certain risk position (e.g. weather conditions, currency exchange rates, interest rates etc.) which make them detached from an underlying transaction. This risk position can then be traded individually. Thus, the neither party of the derivative must have an interest in the underlying transaction, which means that there is no insured interest with any of them. Hence, a derivative may not be regarded as insurance product.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Yes, the contracts described under no. 8. above in principle meet the characteristics of insurance contracts, but are not treated as such for different reasons: A warranty contract does not constitute an insurance contract as it is connected to a sale of goods or similar transaction. A financial guaranty/suretyship cannot be qualified as an insurance contract, because it is a typical activity conducted by financial and not insurance institutions.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

Yes, as already stated under nos. 8.(i) and 9. above, a warranty contract in principle meets the characteristics of an insurance contract but is not qualified as such due to the close legal and economical nexus between the warranty and the underlying contract on the sale of the product.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

In order to conduct the insurance business, a license of the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*) is required (Section 5 para 1 of the German Insurance Supervision Act).

12. What are the legal consequences for the risk-taker acting without license?

Conducting insurance business without a license constitutes a criminal offence pursuant to Section 140 para 1 no.1 and 2 of the German Insurance Supervision Act. A person who carries on unpermitted insurance activities can be held liable to imprisonment for a term up to five years or to a fine, the amount of which is determined in accordance with the sentencing principles of criminal law. Under German law, only natural persons can be held liable under criminal law, thus the responsible persons acting for and on behalf of the risk taker would be held liable.

Further, a person who concludes an insurance contract for an undertaking that does not have the required license commits an administrative offence (*Ordnungswidrigkeit*), which is punishable by a fine of up to EUR 50,000 (Section 144a para 1 no. 1 of the German Insurance Supervision Act).

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, beyond insurance business, insurance undertakings are only permitted to carry on such other business which is directly related to it (Section 7 para 3 of the German Insurance Supervision Act). The reason behind such prohibition is to protect the insured against financial risks on the insurer's side which might arise from non-insurance activities. The exact scope of the prohibition has to be determined on the basis of an objective economic approach. The following examples can be given:

- Banking activities: Banking activities must generally not be conducted by insurance companies. However, there are certain exemptions for life insurance companies, which may for example under certain conditions enter into capitalization transactions and part of the guaranty business.
- Capital participations in other companies: A capital participation in non-insurance companies (for example asset management companies) is not deemed as non-insurance business. A subsidiary of an insurance undertaking may also provide non-insurance related services, if the financial risks associated therewith are limited to the funds of such subsidiary.
- Capital investments: Capital investments in equities which qualify for the restricted assets (*gebundenes Vermögen*) according to the respective provisions of supervisory law do qualify as insurance business.
- Supporting contracts: Insurance undertakings may generally enter into supporting transactions and, for instance, take on loans to this effect. Insurance companies may, however, not provide financial security such as guarantees suretyships to the benefit of the creditor of one of its subsidiaries as this might affect the interests of the insured.
- Futures, options and financial instruments: Dealings in futures, options and other financial instruments may only be entered into if these are to serve as hedge against price and interest rate risks in connection with existing assets or contemplated purchases of securities, or if any additional return is to be generated on existing securities (Section 7 para 3 of the German Insurance Supervision Act).
- Insurance companies may not, as a rule, take out loans.

14. **<u>Do the terms and conditions of insurance contracts need to be</u>**

i) **<u>submitted to the regulator as a kind of formal requirement or</u>**

ii) **<u>approved by the regulator prior to entering into effect?</u>**

Unlike in earlier days, as a general rule, the terms and conditions of insurance contracts neither need to the submitted to the Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*) nor do they need to be approved by it prior to entering into effect. Instead, German supervisory law provides for a comprehensive information concept vis-à-vis the insured (Section 10 of the German Insurance Supervision Act).

However, regarding certain types of insurances, i.e. in particular health insurance, compulsory insurances and death benefit funds, the general terms and conditions need to be submitted to the Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*) together with the application for the insurance license (Section 5 para 3 no. 2, para 5 no. 1 of the German Insurance Supervision Act).

Impact of Qualification – Law of Contracts

15. **<u>Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?</u>**

According to the prevailing opinion, an insurance contract entered into by a non-licensed party is not considered null and void by law but legally valid. However, the policyholder may avoid the contract pursuant to Section 119 para 2 of the German Civil Code, if he was mistaken about the fact that the risk-taker holds a license to conduct insurance business and if he would not have entered into the contract had he known that the insurer acts without a license.

The policyholder may also claim damages under the law of torts pursuant to Section 823 para 2 of the German Civil Code in connection with Section 140 para 1 of the German Insurance Supervision Act, provided that he can prove that he has suffered damage from the fact that the insurance contract was concluded without the insurer having the respective license. However, as the insurance contract is valid - provided that the policyholder does not decide to avoid the contract - the risk-taker is obligated to fulfill his obligations under the contract.

16. **<u>Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.</u>**

Detailed provisions on the rights and obligations of both the insurer and the policyholder are contained in the German Insurance Contract Act. The code contains mandatory provisions, so-called semi-mandatory provisions and non-mandatory provisions: Mandatory provisions cannot be waived (neither to the

benefit, nor to the detriment of the policyholder), whereas semi-mandatory provisions are such provisions which may be waived but not to the detriment of the policyholder. The remaining non-mandatory provisions of the German Insurance Contract Act may be waived.

Besides the German Insurance Contract Act, the German Insurance Supervision Act contains several provisions which have an effect on the insurance contract, for example the provisions on the transfer of portfolio (*Bestandsübertragung*) (Section 14 *et seq.* of the German Insurance Supervision Act). Such provisions are occasionally referenced by the German Insurance Contract Act.

Further, where the German Insurance Contract Act does not contain any specific provisions which are *lex specialis* to the general provisions of the German Civil Code, the German Civil Code is applicable to insurance contracts. Moreover, the German Civil Code contains a few provisions relating to insurances (for instance provisions on the obligation of the usufructuary to provide for insurance, Section 1045 *et seq.* of the German Civil Code).

Other German statutes occasionally contain provisions on insurance contracts, as for example the German Commercial Code, which mentions transport insurance policies (Section 363 para 2 of the German Commercial Code) or the Mandatory Insurance Act (*Pflichtversicherungsgesetz*) which deals with mandatory motor vehicle liability insurance.

17. <u>Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.</u>

As regards the conclusion of an insurance contract, the general provisions of the German Civil code apply. However, the Insurance Contract Act contains a number of supplementary provisions, such as consulting and information duties (see below under no. 18).

As a general rule, a certain form is not required for the conclusion of an insurance contract. Therefore, it is generally possible to conclude an insurance contract even through the internet, however, for reasons of evidence, insurance contracts are usually concluded in writing. Moreover, for the insurance policy and certain aspects in connection with the conclusion of the contract (for example the fulfillment of information duties of the insurer), text form is required (Section 126 b of the German Civil Code). In life insurance contracts, the approval of beneficiary third insured party is required which needs to be made in writing (Section 150 para 2 of the German Insurance Contract Act).

The content of an insurance contract is generally subject to the agreement between the parties, however general statutory limits apply (in particular invalidity due to a violation of mandatory law or violation of the general good). Moreover, the German Insurance Contract Act contains mandatory provisions which cannot be waived to the detriment of the policyholder, for example the following provisions:

- A statutory right to the benefit of the policyholder who has the right to withdraw from the insurance contract under certain conditions (Section 8 *et. seq.* of the German Insurance Contract Act);
- specific provisions on the term and termination of insurance contract (Section 11 of the German Insurance Contract Act);
- provisions with regard to limitation of claims under the insurance contract (Section 14 of the German Insurance Contract Act);
- termination rights of the policyholder in case of an increase of the insurance premium (Section 40 of the German Insurance Contract Act).

In addition to the mandatory provisions of the German Insurance Contract Act and the general provisions of the German Civil Code, statutory requirements regarding the content of an insurance contract exist for certain types of insurance. The following examples can be given:

- With regard to mandatory insurances such as motor vehicle liability insurance, the content of such contracts is stipulated by statutory law. This applies in particular to the minimum insurance amount, which is contained in the respective statutes.
- Insurance undertakings which provide substitutive health insurance (*i.e.* health insurance which is suitable to substitute compulsory health insurance), are obligated to provide a uniform basis policy under which insurance benefits are comparable to the nature, scope and amount of statutory health insurance (Section 12 para 1a of the German Insurance Supervision Act)
- According to statutory law, directors and officers liability insurance policies to the benefit of the members of the management board need to contain a deductible (Section 93 para 2 sentence 3 of the German Stock Corporation Code).

18. <u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>

Pursuant to Section 7 of the German Insurance Contract Act in connection with the information regulation relating thereto, the insurance undertaking has certain information obligations vis-à-vis the policyholder, prior to the conclusion of the insurance contract as well as during the term of the contract.

The information duties of the insurer prior to the conclusion of the contract can be summarized as follows:

- Submission of the terms of contract, including the general terms and conditions of insurance;
- information on the identity of the insurance undertaking (in particular address and corporate information);
- information on nature and scope of the insurance formation, on the exact amount of the insurance premium, including additional costs and payment information;
- information on the commencement, the term and termination of the insurance, including termination rights and information on the statutory right to withdraw;
- information on the applicable law, the competent forum and on the competent supervisory authority.

Additional information is required under life insurance, disability insurance, accident insurance and health insurance contracts.

Insurance undertakings are required to submit a product information leaflet (*Produktinformationsblatt*) to consumers which has to contain all information of particular importance for the conclusion or the performance of the insurance contract, such as a description of the insured risks and information on the exclusion of risks and on obligations of the policyholder.

During the term of the insurance, the insurer has to provide information on changes and amendments regarding the insurance contract (for example changes in the general terms and conditions, changes of the insurance premium or changes with regard to the term of the contract).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

No.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

According to Section 536 (1) of Act IV of 1959 on the Hungarian Civil Code (the "Hungarian Civil Code"), on the basis of an insurance contract, the insurer obliges itself to pay a certain amount of money or to provide another service in the case of the occurrence of a particular event in the future (insurance event), while the insured obliges itself to pay a premium.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. As a general Hungarian insurance law principle, only such risk can be insured which may only happen in the future and the occurrence of which in the future is uncertain. By way of example, the occurrence of a person's death is certain; however, the date of the death is uncertain.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

According to Section 4 of Act LX of 2003 on Insurers and Insurance Activities (the "Hungarian Insurance Act"), insurance activity is a commitment based on an insurance contract, legal provision or membership, in the course of which the insurer organizes a group of people who are exposed to the same or similar risks (risk group), assesses the measurable risks that can be insured by mathematical and statistical means, collects premium as consideration for its commitment, creates specific reserves, assumes the risks stipulated and provides contractual services. On the basis of the above, an insurance contract requires the transfer of risk from the insured to the insurer.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

According to Section 545 (1) of the Hungarian Civil Code, if the insured interest ceases to exist before the insurance contract becomes effective, the insurance contract shall not enter into effect. According to Section 545 (2) of the Hungarian Civil Code, if the insured interest ceases to exist when the insurance contract is already effective, the insurance contract shall terminate on the last day of the affected month. On the basis of the above, a valid and effective insurance contract requires the insured party to have an insured interest.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

It is not required that an insured interest attaches to the party entering into the insurance contract, i.e. it can be attributable to a third party. Such third party does not have to be the beneficiary under the insurance contract. According to Section 547 (1) of the Hungarian Civil Code, a third party may enter into an insurance contract on behalf of the insured. On the basis of the Hungarian Civil Code, in an insurance contract, four different legal positions may be designated, i.e. the insurer, the contracting party (i.e. the person entering into the insurance contract), the insured (i.e. the person in relation to whom the insured event may occur) and the beneficiary (i.e. the person who receives the insured amount).

According to Section 548 of the Hungarian Civil Code, property insurance contracts can be concluded only by such person who is interested in the protection of the affected property or who enters into the insurance contract in favor of an interested person.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

Yes, it is necessary and relevant. According to Section 4 of the Hungarian Insurance Act, when assuming risk, the insurer organizes a group of people who are exposed to the same or similar risks (risk group) as well. Pursuant to subSections 7 and 8 of Section 3 (1) of the Hungarian Insurance Act, the insurance branches and insurance classes are determined on the basis of the risks undertaken and their criteria. According to Section 117 and 118 of the Hungarian Insurance Act, insurers are obliged to create reserves on the basis of the undertaken risks which are supervised by the Hungarian Financial Supervisory Authority (the "HFSA") from the aspect of actuarial issues. If the insurer does not comply with the above regulatory requirements, such non-compliance will not cause the contract to be reclassified, i.e. such contract will remain an insurance contract; however, the insurer will face regulatory sanctions.

7. Does the definition of an insurance contract differ between life insurance and

non-life insurance (obviously apart from the subject matter)?

The general definition of insurance contract set out in our answer to question 1 above applies to both life and non-life insurance. However, there are several differences in the main criteria and requirements of certain types of insurance contracts. By way of example, according to Section 560 (1) of the Hungarian Civil Code, beneficiaries of a life insurance contract are limited to the following:

i) Person named in the contract;

ii) Holder of a bearer insurance policy;

iii) Successor of the insured if no beneficiary was named in the insurance contract and bearer policy has not been issued.

In addition, the Hungarian Civil Code sets out special provisions for property insurance, liability insurance, life insurance, accident insurance differentiating between the conditions of certain types of insurance contracts.

According to the Hungarian Insurance Act, the main branches of insurance are defined as life insurance and non-life insurance triggering different regulatory requirements.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Gambling is a specifically regulated area under Hungarian law. Gambling activities may only be carried on by the Hungarian State or on the basis of a valid license or concession granted by the Hungarian State. According to Section 204 (1) of the Hungarian Civil Code, claims originating from gambling or betting cannot be enforced in a court procedure, unless such activities were carried out on the basis of such license. While insurance and gambling have specific features in common, e.g. both types of contracts focus on future contingent events, the main distinctive feature is that while the purpose of an insurance contract is to aim to avoid or mitigate the risks of damages or other possible adverse event in the future, the aim of a gambling contract is to gain money or any other financial benefit through the occurrence of certain incidental future conditions.

In addition, Hungarian law recognizes types of contracts with certain elements of uncertainty, e.g. support contracts or annuity contracts, where one of the parties provides support or a specific sum of money on a regular basis to the other party until the other party's death. The parties may set out that the party providing support or annuity receives certain assets of the beneficiary. The element of uncertainty in such contracts is the time of the death of the beneficiary. The main distinctive element between such contracts and an insurance contract is that while insurance contracts aim to avoid or mitigate the risks, the purpose of support contracts or annuity contracts for consideration is that the party providing services may gain financial benefit from an early death of the other party. In addition, support contracts or annuity contracts are not subject to license under Hungarian law.

On the basis of the above, contracts of gambling and chance cannot be regarded as a type of insurance contract.

ii) Warranty, guaranty or any other surety contracts

According to Section 306 of the Hungarian Civil Code, in the case of a defective performance, the obligee is entitled to enforce certain warranty rights. The conditions of the guaranty rights are set out in Section 248 of the Hungarian Civil Code: If a guaranty is provided under a contract or legal provision for the performance in conformity with the contract, the guarantor shall be released from liability during the guaranty period if it is able to prove that the cause of defect occurred after its performance. Other security contracts, e.g. security deposit, contractual penalty, bank guaranty, stipulation of forfeiture of right, suretyship, lien, mortgage, floating charge etc. are set out in the Hungarian Civil Code as independent legal instruments which are, as opposed to insurance contracts, always directly linked to the non-performance or defective performance of a civil law contract and are, generally speaking, not subject to license.

iii) Financial contracts such as hedging contracts/swaps/derivatives

According to subSections 14 to 16 of Section A) of Annex 1 of the Hungarian Insurance Act, insurance contracts can be concluded for the insurance of risks originating from the following insurance classes: credit, suretyship, guaranty and various financial losses. The definition of financial contracts such as hedging contracts/swaps/derivatives is set out in Act CXX of 2001 on the Capital Market. These financial contracts are not regulated independently in the Hungarian Civil Code since these have the characteristics of sale and purchase contracts, supply contracts, exchange contracts, loan agreements etc. The only similarity between insurance contracts and the above mentioned financial contracts is the existence of an uncertain event in the future, in connection with which the contracts are concluded.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

We are not aware of any such exception or exemption.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

n/a

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

According to Section 5 (1) of the Hungarian Insurance Act, insurance activity can be carried out within the territory of Hungary subject to a license issued by the HFSA. According to Section 5 (2) of the Hungarian Insurance Act, an insurance company having its registered seat in an EU Member State may carry out insurance activity as a cross-border service or through its Hungarian branch within the territory of Hungary provided that it is entitled to do so under a license issued by the competent authority in the country of its establishment.

12. What are the legal consequences for the risk-taker acting without license?

According to Section 196 (1) of the Hungarian Insurance Act, a fine may be imposed on an insurer or on the managing director thereof by the HFSA, if they carry on an insurance activity as risk-takers without a valid license. According to Section 62 (1) of Act CLVIII of 2010 on the HFSA, the fine imposed on such risk-takers may amount from HUF 100,000 to HUF 2,000,000,000 subject to the circumstances of the infringement. In addition to establishing such fine, the HFSA is also entitled, among others, to prevent the insurer from continuing the performance of its insurance activity. According to Section 298/D of Act IV of 1978 on the Criminal Code, any person, who performs insurance activity without a license required by law, commits the crime of unauthorized financial activity which is to be punished with up to 3 years imprisonment. On the basis of Sections 5-6 of Act CIV of 2001 on punitive measures against legal entities, if the above crime results in or is intended to provide illegal financial benefit for the insurer, its activities may be restricted for a period of between 1 and 3 years or a fine may be imposed on the insurer, the amount of which is equal to the triple of the benefit acquired or intended to be acquired.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

According to Section 5 (5) of the Hungarian Insurance Act, insurance companies may not perform any other business activities in addition to insurance activities and activities directly related to insurance activities. According to Section 5 (6) of the Hungarian Insurance Act, among others, the following activities are deemed directly related to insurance activities:

i) management and investment of the insurance company's own assets;

ii) intermediation of financial services;

iii) mortgage lending;

iv) securities lending and securities borrowing;

v) services related to the operation of the insurance activity provided by an insurer to its subsidiary or parent company, or to a company in which it has a share.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

The terms and conditions of the insurance contracts applied by an insurer do not have to be (i) submitted to the HFSA as a kind of formal requirement or (ii) approved by the HFSA prior to entering into effect. However, Section 96 (1) of the Hungarian Insurance Act sets out the minimum requirements of the content of insurance contracts. In addition to the above, the HFSA may request the provision of any information from the insurance company, e.g. the submission of the applicable terms and conditions of its insurance contracts on the basis of Section 171 (1) of the Hungarian Insurance Act.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

As indicated in our answer to question 11 above, insurance activities which cover the conclusion of an insurance contract can only be performed subject to a license issued by the HFSA. On the basis of the above and according to Section 200 (2) of the Hungarian Civil Code, an insurance contract if concluded with an insurer that does not have an HFSA license, is null and void since it is in breach of the applicable laws. If the policyholder suffers any damages from the invalidity of the insurance contract due to the fact that it is null and void, the policyholder may claim compensation for their damages in accordance with the general tort law provisions of the Hungarian Civil Code.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

The following acts, setting out the main requirements, are directly applicable to certain insurance contracts within the territory of Hungary:

i) Act LXII of 2009 on Compulsory Motor Vehicle Liability Insurance;

ii) Act CLIX of 2007 on Reinsurance;

iii) Act LX of 2003 on Insurers and Insurance Activities;

iv) Act XCVI of 1993 on Voluntary Mutual Insurance Funds and

v) Act IV of 1959 on the Hungarian Civil Code.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

According to Section 537 (1) of the Hungarian Civil Code, the conclusion of insurance contracts is subject to a written form. The contract shall also come into existence, if the insurer does not respond to an offer within 15 days. In such a case, the insurance contract shall be created with retroactive effect to the date on which the offer was received by the insurer or its representative. According to Section 538 (1) of the Hungarian Civil Code, the written agreement or the insurer's acceptance may be replaced by the issuance of an insurance policy (certificate, insurance stamp).

Section 96 (1) of the Hungarian Insurance Act sets out the minimum content requirements of the insurance contracts. Among others, the insurance contract must set out the following terms:

i) insurance event, exclusions;

ii) procedure and deadline for reporting insurance events;

iii) services provided by the insurer (way, time, conditions of performance);

iv) rights and obligations of the insured party;

v) limitation of claims;

vi) address of the insurance company, branch etc.

According to Section 96 (4) of the Hungarian Insurance Act, the termination right of the insured party cannot be excluded.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

According to Sections 166-167/A of the Hungarian Insurance Act, insurers are obliged to inform their clients about the terms and conditions of the insurance contracts to be concluded and on the main details of their company. As indicated in our answer to question 14, Section 96 (1) of the Hungarian Insurance Act sets out the minimum content requirements of insurance contracts. In addition, the HFSA conducts a procedure in accordance with Act XLVII of 2008 on the Prohibition of Unfair Business Practices against Consumers in the case of any infringement of the consumer's rights in the course of insurance activities. Such procedure of the HFSA can be initiated ex officio or by a consumer. Furthermore, according to Section 167/B of the Hungarian Insurance Act, insurers are obliged to handle the complaints of their clients in a fair and correct manner.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

a) Insurance is primarily governed by the Insurance Act 1938, the Insurance Regulatory and Development Authority Act, 1999(IRDA) and the Indian Contract Act 1872.

b) An insurance contract has not been defined under any statute in India.

c) The general meaning of an "insurance contract" can be derived from various case laws. The courts have held a contract of insurance as primarily a contract of indemnity.[1] An insurance policy has been described as the exclusive record of the insurance contract and the parties are bound by the terms of the policy.[2]

d) A typical insurance contract would have all the legal requirements for a contract mentioned under the Indian Contract Act 1872, and also certain additional requirements.

e) The four essentials of a contract of insurance are:[3]

i) Definition of the risk;

ii) Duration of the risk;

iii) Premium;

iv) Amount of insurance.

f) The further legal requirements are:

i) Utmost good faith;[4]

ii) Insurable Interest.

g) One class of insurance has been defined by statute: contract of marine insurance. This has been defined as an agreement whereby the insurer undertakes to indemnify the assured, in the manner and to the extent thereby agreed, against marine losses, that is to say, the losses incidental to marine adventure.[5]

2. **Does an insurance contract require an element of uncertainty? Please describe.**

a) An Insurance contract, being a contingent contract, has the element of uncertainty. A contingent contract is based on an uncertain future event, however if the event becomes impossible, the contract will become void.[6]

b) A valid insurance contract requires the insurer to accept significant insurance risk from another by agreeing to compensate that person if a specified uncertain future event adversely affects the insured.[7]

c) Premium is the consideration which the insured pays to the insurer for agreeing to undertake the risk and premium or cost of insurance is based upon the relative risk or hazard involved. The insurer must take on risk for a valid insurance contract.[8]

d) The occurrence of the risk in an insurance contract is uncertain, and in case of life insurance the time of the risk is uncertain, and therefore the element of uncertainty exists.

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

Yes. One of the essential elements, as mentioned above, for the identification of an insurance contract is "risk". "Insurance risk" is defined as "risk, other than financial risk, transferred from the holder of a contract to the issuer of the insurance policy.[9] A contract that exposes the issuer to financial risk without significant insurance risk is not an insurance contract. No

[1] Assambrook Exports Ltd v Export Credit Guarantee Corporation of India Ltd, AIR 1998 Cal 1. This is not so for life insurance.

[2] Principles of Insurance Law, M.N Srinivasan 18th Edition 2006

[3] State Bank of India v Agents & Manufacturers, AIR 1998 Del 84

[4] Satwant Kaur Sandhu v New India Assurance Company 2010(1)ALLMR(SC)974

[5] Section 3, Marine Insurance Act 1963

[6] Sharadprasad v Sikandar, AIR Nag 15

7 As per the Indian Accounting Standard on Insurance Contracts http://www.mca.gov.in/Ministry/pdf/Ind_AS104.pdf

8 S.R. Kharidia and Ors v Max New York Life Insurance Co. Ltd and Ors, AIR 2009 Guj 57

[9] As per the Indian Accounting Standard on Insurance Contracts http://www.mca.gov.in/Ministry/pdf/Ind_AS104.pdf

contract is said to be entered into between the parties unless the insurer has taken steps to underwrite the risk and issue the policy to the insured, mere submission of a proposal form and payment of first premium does not conclude an insurance contract.[10]

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

The insured party must have an interest in the property, life or liability, which is the subject matter of the insurance. This is known as "insurable interest" and the absence of this will render the contract as a contract of wager which is void as under Section 30 of Indian Contract Act 1872.[11]

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

a) Under the Insurance Act 1938, a policyholder is defined as "a person to whom the whole of the interest of the policy-holder in the policy is assigned once and for all, but does not include an assignee thereof whose interest in the policy is defeasible or is for the time being subject to any condition. As mentioned above, the policyholder must have an insurable interest in the subject matter of the insurance contract.

b) As regards insurable interest being attributable to a third party:

i) It is mandatory for every motor vehicle owner to get a third party insurance cover as per the Motor Vehicles Act 1988.[12] The third party is not a direct beneficiary, as the policy covers the insured's liability for death or disability of third party loss or damage.

ii) The Public Liability Insurance Act, 1991 provides for immediate relief to persons affected by accidents occurring while handling any hazardous substance. The owner of the premises dealing with the hazardous substances (i.e., the 'controller of the hazardous substance') must take out 'public' insurance policies and any person who suffers the harm is allowed to claim under the insurance contract.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

a) It is not so necessary.

b) The law of larger numbers is based on probability. It is relevant to the insurer to apply this law to predict the chances of a risk. The application of the law of large numbers is relevant to insurers to predict losses accurately as the risk is spread over a large group. However, it is not necessary that the risk will be mitigated.[13]

c) In India, group insurance can be seen as an application of the law of larger numbers. It is the coverage of a homogeneous group, by an insurer who drafts a single policy for the entire group.

d) It is a supervisory and actuarial issue.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

a) Under the Insurance Act 1938, "life insurance business" has the following meaning "the business of effecting contracts of insurance upon human life, including any contract whereby the payment of money is assured on death (except death by accident only) or the happening of any".

b) Although "life insurance" is not defined under any statute in India, the interpretation given to it can be understood by the definition given to it in Halsbury's Law of England[14] which was the meaning taken in an Indian case.[15] It is defined as comprising any contract in which one party agrees to pay a given sum upon the happening of a particular event contingent upon the duration of human life, in consideration of the immediate payment of a smaller sum or certain

[10] S.R. Kharidia and Ors v Max New York Life Insurance Co. Ltd and Ors, AIR 2009 Guj 57

[11] Swaminathan v Jayalakshmi Amma, 1987 (2) KLT 292

[12] Section 146,Motor Vehicles Act

[13] www.actuariesindia.org

[14] Halsbury's Laws of England, 3rd Edn. Vol. 22, p. 273

[15] Chandulal Harjivandas, Jamnagar v Commissioner of Income Tax, Gujarat AIR 1967 SC 81

equivalent periodical payments by another part.

c) Life insurance is not a contract of indemnity while non-life insurance is a contract of indemnity.

d) Also, in a life insurance contract, insurable interest is required only at the time when the policy is affected and need not continue thereafter.[16] Unlike the insurable interest in a general insurance contract, which requires the insurable interest to exist at the commencement and execution of the policy to the occurrence of the loss.

e) The risk in a life insurance contract is certain, unlike in other insurance contracts, as death is certain. However, the occurrence of this risk is where the element of uncertainty lies.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Contracts of gambling and chance are not treated as contracts of insurance.

Even though Contracts of insurance and contracts of gambling and chance are contingent in nature, as dealt with under Question no. 4, any contract of insurance by way of wager is void. In a contract of insurance, the insurer promises, in return for a premium to pay the insured money on the happening of an uncertain event adverse to the interest of the insured.

If an insurer binds himself to indemnify the insured, the payment made by the insurer in this respect, cannot be said to be based on stake.[17]

ii) Warranty, guaranty or any other surety contracts

Contracts of warranty, guaranty, and surety are not regarded as types of insurance contracts. A contract of guaranty is a contract to perform the promise or discharge the liability of a third person in case of his default. A contract of insurance as described under Question no. 1 is a contract of indemnity which promises to indemnify the insured.

A contract of guaranty unlike a contract of insurance is not based on utmost good faith, but is based on the strictest rule of law.[18]

The creditor, the principal debtor and the guarantor are three parties in a contract of guaranty whereas there are only two parties to a contract of insurance, the insurer and the insured.

Contracts of insurance are generally matters of speculation in which the insurer has to know about the nature of the risk from the insured. In a contract of guaranty, the guarantor is aware of the risk that he is going to assume.

iii) Financial contracts such as hedging contracts/swaps/derivatives

A derivative includes a contract which derives its value from the prices, of underlying securities.[19] These financial contracts do not necessarily require insurable interest and barring certain classes would constitute wagers and be unenforceable.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Yes: warranty contracts and surety bonds.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

Not applicable.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Yes. No person can carry on any class of insurance business in India unless authorized to do so through a certificate of registration under the authority regulating the class of insurance business he intends to carry on with.[20]

Even an insurance agent needs to procure a license to act on behalf of the insurer.[21]

12. What are the legal consequences for the risk-taker acting without license?

[16] Dalby v. India and London Life Assurance Co (1854), 15 C. B. 365

[17] Northern India General Insurance Co. Ltd. V. Kanwarjit Singh Sobti, AIR 1973 ALL 357

[18] Suresh Narain v. Akhauri AIR 1957 PAT 256

[19] Section 2 (ac) (B), Securities Contracts (Regulations) Act, 1956

[20] Section 3 (1), The Insurance Act, 1938

[21] Section 42, The Insurance Act, 1938

If the insurer fails to furnish any document, statement, account, return or report to IRDA or to comply with the directions like procuring the certificate of registration, as mentioned above, the insurer shall be liable to a penalty not exceeding INR 5,000 for each such failure and punishable with fine.[22]

A penalty which may extend INR 500 can be imposed on a person acting as an insurance agent, on behalf of the insurer without a license.[23]

A penalty which may extend to INR 5,000 can be imposed on a firm or company acting as an insurance agent, without a license.[24]

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

The registration that is granted to the insurer to carry on the business of insurance can be cancelled by the authority governing the specified class of insurance if the insurer carries on any business other than that of insurance.[25] A company carrying on life insurance business cannot carry on non-life insurance business.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Yes as every new policy type requires to be filed and approved though that can be by way of negative approval. It is not required to submit the insurance contract every time it is entered into.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

It will be null and void. The policyholder would be entitled to claim damages by seeking redressal under the Consumer Protection Act 1986.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes

1. PRIMARY ACTS

a) Isurance Act, 1938

b) Insurance Rules, 1939

c) Insurance Regulatory and Development Authority Act, 1999 and the notifications and circulars issued there under.

2. SECONDARY ACTS

a) The Life Insurance Corporation Act, 1956

b) The General Insurance Business (Nationalization) Act, 1982

c) Motor Vehicles Act, 1988[26]

d) Marine Insurance Act, 1963

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Yes they do.

1. LIFE INSURANCE and GENERAL INSURANCE

a) As per *IRDA (Protection of Policyholders Interests) Regulations, 2002*, detailed content has been laid down for Life Insurance[27] and General Insurance contract.[28]

b) To name a few with regards to Life Insurance:

i) Name of the plan governing the policy and the terms and conditions;

ii) Benefits payable and contingencies upon which they are payable;

iii) The date of commencement of risk and the date of maturity;

iv) Any special clauses or conditions, such as, first pregnancy clause, suicide clause etc.

c) To name a few with regards to General Insurance contract:

i) The name(s) and address(es) of the insured and of any bank(s) or any other person

[22] Section 102, read with Section 103, The Insurance Act 1938

[23] Section 42 (7), The Insurance Act, 1938

[24] Section 42 (8), The Insurance Act, 198

[25] Section 3 (4) (h), The Insurance Act, 1938

[26] Chapter XI, Motor Vehicles Act, 1988

[27] Regulation 6, IRDA (PPHI) Regulation, 2002

[28] Regulation 7, IRDA (PPHI) Regulation, 2002

having financial interest in the subject matter of insurance;

ii) Perils covered and not covered;

iii) Action to be taken by the insured upon occurrence of a contingency likely to give rise to a claim under the policy;

iv) Full description of the property or interest insured.

2. MARINE INSURANCE

The form of the policy has been laid down in the Schedule to the Marine Insurance Act, 1963 along with the content identified under Section 25 of the act.[29]

A marine policy must specify

i) the name of the assured, or of some person who effects the insurance on his behalf;

ii) the subject- matter insured and the risk insured against;

iii) the voyage, or period of time, or both, as the case may be, covered by the insurance;

iv) the sum or sums insured;

v) the name or names of the insurer or insurers.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes. Specific provisions as per Insurance Act, 1938 for life insurance contracts:

- Right to Nominate the beneficiary;[30]
- Notice of options available to the assured on the lapsing of a policy;[31]
- Supply of copies of proposals and medical reports;[32]
- Policy not to be called in question on ground of mis-statement after two years.

Other provisions for protection in respect to insurance contracts:

- Consumers may seek redressal from the grievance cell of respective insurers and upon their failure to respond, may approach the office of *Insurance Ombudsman* which is an independent body created by Government of India[33] with the purpose of quick disposal of the grievances of the insured customers by conciliation.
- Under Consumer protection Act, 1986[34] the insurance is covered within the definition of services. The aggrieved party may seek redressal from appropriate consumer forum for deficiency in services rendered by the insurers.
- IRDA Protection of Policyholders' Interests (PPHI) Regulations 2002 stipulates Turnaround Times (TAT) for various services that an insurance company has to render to the consumer. Also they lay down guidelines for Grievance redressal by the insurers.[35]

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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[29] Section 25, Marine Insurance Act,1963

[30] Section 39, Insurance Act, 1938

[31] Section 50, Insurance Act, 1938

[32] Section 51, Insurance Act, 1938

[33] G. S. R. 670(E) dated 11-11-1998

http://www.irda.gov.in/ADMINCMS/cms/NormalData_Layout.aspx?page=PageNo233&mid=7.1; http://www.gbic.co.in/notifications.html

[34] Section 2(o), Consumer Protection Act , 1986

[35] Insurance Regulatory and Development Authority, GUIDELINES FOR GRIEVANCE REDRESSAL BY INSURANCE COMPANIES, Ref: 3/CA/GRV/YPB/10-11 27th July, 2010

Ireland

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

There is no statutory definition of a "contract of insurance" under Irish law, nor are there specific rules for the formation of an insurance contract beyond the general principles of contract law and the duty of utmost good faith: both parties have an overriding duty to disclose all material facts to the other before the contract is made. Accordingly, it is necessary to consider the common law definition of a "contract of insurance" which is derived from case law, some of considerable antiquity. Irish legislation does not specify the essential legal elements of an insurance contract and the courts have considered it on a case-by-case basis. At common law, the leading authority on what constitutes an insurance contract is *Prudential Assurance v Inland Revenue* [1904] 2 KB 658 (the "Prudential Case") which is of persuasive authority in Ireland.

Channell J provided a useful definition of a "contract of insurance" as follows:

> "…a contract for the payment of a sum of money, or for some corresponding benefit…to become due on the happening of an event, which event must have some amount of uncertainty about it, and must be of a character more or less adverse to the interest of the person effecting the insurance."

From this definition we can extract a number of key elements that may be required when assessing whether a contract is one of insurance or not, including an element of uncertainty:

i) There must be a *contract*;

ii) that provides some *monetary payment* or corresponding *benefit*;

iii) on the happening of an *adverse*;

iv) and uncertain *event*;

v) for the consideration of some *premium*.

The leading Irish authority is *International Commercial Bank plc v Insurance Corporation of Ireland plc* [1991] ILRM 726 ("International Commercial Bank Case"). In distinguishing an insurance contract from a contract of guaranty, Blayney J applied the judgment of Romer LJ in *Seaton v Heath* [1899] 1 QB 782 ("Seaton v Heath") and listed the main characteristics of an insurance contract as follows:

- Generally the insured must have an insurable interest in the subject matter of the insurance policy;
- there is a payment of premium;
- the insurer undertakes to pay the insured party in the event of the happening of the insured risk;
- the risk must be clearly specified;
- the insurer will indemnify the insured against any actual loss (indemnification).

There is no legal difference under Irish law between an insurance contract and a reinsurance contract.

2. Does an insurance contract require an element of uncertainty? Please describe.

As stated above, Irish legislation does not provide a test for the existence of an insurance contract. However, it is possible to derive a test from the Prudential Case which would be of persuasive authority in Ireland. One of the key elements listed by Channell J in assessing whether a contract is one of insurance or not is the happening of an event, "which event must have some amount of uncertainty about it".

As regards an uncertain event, Channell J stated that:

> "There must be either uncertainty whether the event will happen or not, or, if the event is one which must happen at some time, there must be uncertainty as to the time at which it will happen."

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

One of the key elements of the definition of an "insurance contract" as set down by Channell J in the Prudential Case is that the insurer undertakes to pay the insured party in the event of the happening of the insured risk which risk must be clearly specified. There must therefore be a clearly identified risk upon the occurrence of which the insurer will indemnify the insured against any actual loss.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

As per the elements listed in the International Commercial Bank Case, a primary distinguishing characteristic of an insurance contract from other types of contracts is the presence of an insurable interest. The insured must have a sufficient interest in

the subject matter of the insurance to make it valid; one man cannot insure another man's property. In the case of a life assurance contract, the interest in question must be in the life or lives assured. Irish law does not provide a standard definition of what constitutes an "insurable interest", and the legal test for the interest required varies depending on the nature of the insurance policy under consideration.

In MacGillivary on Insurance Law, the author states that the nature of insurable interest is as follows:

> "Insurable interest may be described loosely as the assured's pecuniary interest in the subject matter of the insurance" (12th edition, Sweet & Maxwell, paragraph 1-013, page 9).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Although Irish common law did not historically require an insurable interest to be present for a contract of insurance to be enforceable, subsequent statutory developments aimed at counteracting fraud, gambling and criminal destruction of lives and property did. It is clear however, in relation to life policies, that Irish law retains an insurable interest requirement by way of the English Life Assurance Act 1774 (the "1774 Act"). The 1774 Act established the requirement that an insurable interest must be present in respect of life and certain other forms of insurance policies. The provisions of the 1774 Act were extended to Ireland by virtue of the Life Assurance (Ireland) Act 1866 (the "1866 Act") but only as regards life assurance policies.

Section 1 of the 1774 Act requires that the person(s) for whose use, benefit, or on whose account a policy is made shall have an interest. Section 2 requires the name(s) of such person(s) to be inserted in the policy, so that no one should "acquire clandestinely an interest in a policy on the lift of another*".* If the policy is made for the benefit of someone other than the life assured, and he possesses a valid interest in the life, the policy will nonetheless be unlawful if he is not named therein. As stated in *Lucena v Crauford* (1806) BOS & Pul (NR) 269, the insured must bear some relationship to the insured thing whereby he / she stands to benefit by its safety or be prejudiced by its loss or by incurring liability.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

This is not necessary or relevant under Irish insurance law.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

As stated above, Irish legislation does not provide a definition of an "insurance contract", in respect of life insurance or non-life insurance. The Prudential Case offers some guidance on the key elements required when assessing whether a contract is one of insurance or not. The Prudential Case was cited with approval by the Court of Appeal in the more recent case of *Fuji Finance Inc. v Aetna Life Ins. Co. Ltd.* [1995] Ch 122, 130. The Court of Appeal reviewed both the provisions of the 1774 Act and relevant case law which considered various essential aspects of insurance contracts (*Flood v Irish Provident Assurance Co. Ltd* [1912] 2 Ch. 597, *Joseph v Law Integrity Insurance Co. Ltd* [1912 2 Ch. 581, *Gould v Curtis* [1913] 3 KB. 84).

As regards life insurance contracts, the Court was satisfied that the formulation of a test in respect of the existence of contracts of insurance on life involved the existence of an obligation on the insurer to pay a sum or money or other benefit which is payable on an event which is uncertain, either as to the timing or as to its happening at all and that event must be dependent on the duration of human life. This decision and the early case law on which it was based is of strong persuasive authority in Ireland and the Irish Courts would likely define a life assurance contract as a contract providing for the payment of a benefit that is expressed to be contingent on human life (i.e. on death or survival).

Accordingly, the definition of a "contract of insurance" provided by Channell J in the Prudential Case must therefore be qualified in respect of life assurance as an event such as survival (and the consequent payment of a benefit under a life policy) could clearly not be described as "adverse". This element of Channell J's formula can therefore be disregarded in certain cases and need not be regarded as an imperative component of the test in respect of contracts of life assurance.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Contracts of gambling are not defined under Irish law, however, contracts of gaming which are akin in some respects to contracts of gambling are governed by the Gaming and Lotteries Act 1956. Section 36 of the Gaming and Lotteries Act states that every contract by way of gaming or wagering is void. Section 36(2)

provides that no action shall lie for the recovery of any money or thing which is alleged to be won or to have been paid upon a wager or which has been deposited to abide in the event on which a wager is made.

Gaming

Although there is no definition as to what is meant by a "contract of gaming" or a "contract of wagering", "gaming" is defined in Section 2 as "playing a game (whether of skill or chance or partly of skill and partly of chance) for stakes hazarded by the players." The Gaming and Lotteries Act expressly prohibits all gaming, except that which is specifically provided for under the terms of the Act. "Unlawful gaming" is defined in Section 4 as any kind of gaming:

- "in which by reason of the nature of the game, the chances of all players, including the banker, are not equal; or
- in which any portion of the stakes is retained by the promoter or is retained by the banker otherwise than as winnings on the result of the play; or
- by means of any slot machine."

Wagering

A definition of "wagering" is not contained in the Gaming and Lotteries Act. However, a wagering contract typically involves two persons who hold opposite views about a future uncertain event and agree that one of them shall pay the other a sum of money or some other agreed stake dependent upon the outcome or determination of that future event. The parties must have no other interest in the contract apart from the sum of money or other stake which they stand to win or lose. The purpose, intention and context in which a transaction is entered into will be considered in determining whether a contract is in fact a wagering contract and therefore unenforceable.

ii) Warranty, guaranty or any other surety contracts

Contract of Guaranty

In the International Commercial Bank Case, the leading Irish authority on distinguishing an insurance contract from a contract of guaranty, Blayney J applied the judgment of Romer LJ in Seaton v Heath which states that there is no hard and fast rule for distinguishing a contract of insurance from a contract of guaranty. Romer LJ identified the principal factor which distinguishes a contract of insurance from a contract of guaranty as being that contracts of insurance are generally contracts of speculation, where the person desiring to be insured has means of knowledge as to the risk and the person giving insurance has not. Contracts of guaranty, by contrast, are not typically issued by a surety following an explanation given to him of the nature of the risk by the creditor, but are often issued at the instigation of the debtor.

For a contract to be one of insurance, it is essential that the insurer undertakes an obligation to pay. Thus, a contract whereby the "insured" only acquires a right to require the insurer to consider his claim is not one of insurance. The contract must be one where the insurer undertakes to pay money or moneys worth to the insured on the occurrence of a specific event.

Using words such as "insurance" or "guaranty" does not determine the status of the contract. Instead, the status of the contract is determined by "its substantial character and how it came to be effected". Referring to a document as a "policy" indicates that it is intended to be a contract of insurance but is not conclusive as to its status. For example, in *Kreglinger and Fernau Ltd v Irish National Ins. Co. Ltd* [1956] I.R. 116, a document guaranteeing performance of a contract of sale by the vendors was held to be a contract of insurance whilst a performance bond guaranteeing the performance of a contract by a building contractor was held to be a contract of guaranty in *Trade Indemnity Co. v Workington Harbour and Dock Board* [1937] A.C. 1.

Extended Warranty

Although the Central Bank has not issued any view or guidance on extended warranty schemes, in the recent case of *Re Digital Satellite Warranty Cover Ltd & Ors* [2011] EWHC 122(CH), the England and Wales Court of Appeal clarified that extended warranties could be regarded as insurance contracts. The appellants were engaged in the business of providing extended warranty contracts under which they agreed to repair and replace customers' television dishes, digital boxes and associated equipment in the event of breakdown, malfunction or damage caused by external forces. The respondent, the FSA, argued that the warranties were contracts of general insurance, within the meaning of the FSMA (Regulated Activities) Order (2001 SI 2001/3544), being "contracts which provided insurance against the risk of loss attributable to the insured incurring unforeseen expense".

The High Court of England and Wales held that the warranties were contracts of general insurance which provided cover against the risk of the insured incurring expense in the form of the cost of repair or replacement of the equipment. Although this is a decision of the England and Wales Court of Appeal, the ramifications of the decision in Ireland are, as yet, unclear. However, the decision is likely to be of persuasive authority before the Irish Courts and may have implications for those persons engaged in similar activities in this jurisdiction.

iii) Financial contracts such as hedging contracts/swaps/derivatives

The definition of "financial contracts" is contained in Section 1 of the Netting of Financial Contracts Act, 1995 and has been extended by Statutory Instrument 214 of 2000 as well as the Markets in Financial Instruments and Miscellaneous Provisions Act, 2007. The broad definition includes, interest-rate contracts, foreign-exchange contracts, contracts relating to one

or more of equities, bonds, gold, precious metals other than gold, and commodities other than precious metals, or a combination of them, consisting of one or more of, for example, swaps, spot contracts, futures or options. In order for a contract to fall within the definition of a "financial contract" it must consist of at least one of the various limbs set out in that definition.

Section 3(2) of the Insurance Act 1936 states that:

> "A financial contract within the meaning of the Netting of Financial Contracts Act 1995 is not, and it taken never to have been, a contract of insurance for the purposes of –
>
> a) the Insurance Acts 1909 – 2002, or
>
> b) regulations in force under those Acts, or
>
> However, this subSection does not have effect if the financial contract provides for any benefit that may accrue to a party to the contract to be conditional on the occurrence of a loss or detriment to which the party is required to be exposed under the contract."

There is a strong argument to be made therefore that where a "financial contract" is not a "contract of insurance" for the purpose of the Insurance Acts 1909 to 2000 or the regulations made thereunder, it is not a "contract of insurance" as a matter of Irish law. Nonetheless, it is important for each type of financial contract to be examined on a case by case basis in this regard.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

No such exceptions or exemptions exist under Irish law. However, it is clear from a review of the elements of an insurance contract listed in the Prudential Case that it is possible for these elements to be present in contracts that are not traditionally regarded as insurance contracts. For example, as set out at Question 8 above, a contract of guaranty possesses the elements of an insurance contract as identified by Channell J in the Prudential Case. It provides for the payment of a monetary amount to the beneficiary by the guarantor on the occurrence of a borrower default (which is an uncertain event that is adverse to the beneficiary) and there may be a guaranty fee paid in respect of this. It is clear law however that a guaranty agreement is not a contract of insurance at common law. A similar analysis can be conducted in respect of warranties/indemnities given in share purchase agreements.

Similarly, certain forms of financial instruments may also be categorized as insurance contracts. For example, in a sample credit derivative contract, one party (Party A) agrees with another party (Party B), to pay a sum of money to Party A, in return for a premium, on the happening of a future specified contingency. Credit derivative contracts do not require the protection buyer to hold the portfolio of securities the subject of the contract, so that Party B would not need to hold bonds issued and the contract could be entirely speculative.

Therefore the approach generally adopted by lawyers is to conclude that credit derivative contracts are not contracts of insurance since all of the elements identified in the Prudential Case do not exist. It is important to note however that this point has not been considered by the courts to date in either Ireland or the UK.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

In Ireland, complex structured finance transactions that resemble insurance contracts must be carefully examined on a case by case basis in order to determine if such arrangements constitute an insurance contract. If found to be an insurance contract, the issuer of the contract is required under the legislation governing the authorization of insurance companies in Ireland, to be authorized to "carry on the business of non-life [or life] insurance". Failure to hold such an authorization renders the undertaking and its directors and officers liable to prosecution for breaches of the relevant legislation. The legislation is silent however as to the consequences of lack of authorization for any unauthorized contracts of insurance.

The UK courts held in *Phoenix General Insurance v Halvanon Insurance Limited* [1985] that such policies were not enforceable by the suppliers but that the insured party could elect to enforce the contract. Irish Courts have considered the enforceability of contracts of insurance effected in circumstances where the supplier was not authorized to effect a policy of insurance and appear to differ in their approach. Although there is no specific Irish case on the facts, in *Whitecross Potatoes (International) Limited v Raymond Coyle* [1978], the court found that a contract made by a supplier without the relevant license to do so was enforceable. It is not clear however if this will extend to contracts of insurance.

Irish courts do not generally tend to re-characterize contracts as insurance contracts as a matter of course. Judicial authorities indicate that as long as commercial arrangements made by parties are not a sham, the Irish court will generally not attempt to re-characterize a contract because a transaction has an economic resemblance to another form of transaction.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

A party as a risk-taker cannot enter into an insurance contract unless it is authorized to conduct insurance business. At the outset, it should be noted that Ireland has adopted all of the EU insurance directives

(i.e. the non-life Directives and the Consolidated Life Directive) (the "EU Insurance Directives"). Irish legislation provides that an insurer is not permitted to carry on the business of, as the case may be, life assurance (Regulation 6(1) of the European Communities (Life Assurance) Framework Regulations 1994 (the "Life Framework Regulations")) or non-life insurance (Regulation 6(1) of the European Communities (Non-Life Insurance) Framework Regulations 1994 (the "Non-Life Framework Regulations")) unless it is authorized by either the Central Bank of Ireland (the "Central Bank") or by the competent authority of another EEA Member State. The Central Bank is the competent authority in Ireland having responsibility for the regulation of the Irish insurance industry. In this regard, from an insurance regulatory perspective, the Central Bank is responsible for the authorization and ongoing supervision of insurers.

Where an insurer is authorized by the competent authority of another EEA Member State, it may write insurance business directly in Ireland in reliance on the passporting provisions contained in the EU Insurance Directives. Insurance business may be written by that insurer on a freedom of services and/or a freedom of establishment basis.

Insurers established in countries outside the EEA may write types of railway, aviation and marine insurance, including carrier's liability, in Ireland subject to the satisfaction of solvency requirements and confirmation that they are authorized to underwrite risks in the applicable classes of non-life insurance under the Non-Life Framework Regulations. Insurance covering accident and motor vehicle liability may be written by these insurers where it relates to the insurance of marine or aviation passengers or carriers' liability.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

As discussed above in response to Question 11, both the Life Framework Regulations (life assurance) and the Non-Life Framework Regulations (non-life assurance) stipulate that an undertaking must not carry on the business of insurance unless it is authorized to do so.

Both the Life Framework Regulations and the Non-Life Framework Regulations provide that an undertaking that fails to comply with any provision of the regulations (including the requirement to be authorized to carry on insurance business) is guilty of an offence and is liable on summary conviction to a maximum fine of EUR 1,900 (one thousand, nine hundred Euros). Where the offence is committed by a body corporate and is proved to have been, in particular, committed with the consent or connivance on the part of a director, manager, secretary or other officer of the body corporate, such individual(s) will also be guilty of an offence. The Central Bank is empowered to take a prosecution for an offence.

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

Yes, a prohibition exists preventing authorized insurers from entering into non-insurance business. Consistent with the terms of the EU Insurance Directives, both the Life Framework Regulations and the Non-Life Framework Regulations expressly provide that an insurer must limit its operations to the business of insurance and to operations directly arising therefrom, to the exclusion of all other commercial business. It should also be noted that an authorized non-life insurer may not carry on the business of life assurance. However, an authorized life assurer may conduct certain limited classes of non-life insurance business (Class 1: *Accident* and Class 2: *Sickness*) where authorized to do so.

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

No, under Irish law the terms and conditions of insurance contracts do not need to be (i) submitted to the Central Bank or (ii) approved by the Central Bank prior to entering into effect. Both the Life Framework Regulations and the Non-Life Framework Regulations expressly provide that the Central Bank must not require the prior approval or systematic notification of general and special policy conditions. However, in accordance with the Life Framework Regulations and the Non-Life Framework Regulations, the Central Bank may require notification, in particular of the general and special policy conditions for the purposes of verifying compliance by the insurer with laws, regulations and administrative provisions concerning insurance contracts.

Impact of Qualification – Law of Contracts

15. <u>Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?</u>

It is clear under Irish legislation (the Life Framework Regulations and the Non-Life Framework Regulations) that it is a statutory offence for an undertaking to carry on insurance business without being authorized to do so. However, the legislation is silent as to consequences for a contract of insurance that was issued by an unauthorized insurer. In so far as we are aware, to date there has been no reported Irish case which has considered the legal consequences for such an insurance contract.

Therefore, it is difficult to say whether the insurance contract would be legally valid, null and void or capable of being avoided by either party. However, it may be reasonable to hold the view that where the legislature has failed to spell out the consequences of entering into a contract of insurance with an unauthorized insurer, it is not to be assumed that the contract would be invalid.

Until quite recently, a statutory provision (which has been repealed) under the Insurance Act 1936 made it unlawful for any person to enter into a contract of insurance with a company or a person who was not duly authorized to effect contracts of insurance.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

In Ireland, there exists only a limited body of legislation which is specifically applicable to insurance contracts (in contrast to insurance business). These include, in particular, the 1774 Act (as discussed above in response to Question 1) and the Marine Insurance Act 1906. In Ireland, many of the key features of the law concerning insurance contracts derive from long-established principles and judge made law (as discussed above in response to Question 1). Regard should also be had to the consumer protection requirements discussed below in response to Question 18.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Generally, the legal provisions and statutes applicable specifically to insurance contracts do not set out requirements regarding either the form or content of an insurance contract. In reality, insurers will usually have standard policy conditions for each product that they issue. Such policy conditions will have developed on basis of industry norms as well as case law involving contractual clauses. However, policies of mandatory insurance (e.g. motor insurance and solicitors' professional indemnity insurance) must meet certain legislative requirements (see Section 62 of the Road Traffic Act 1961 with respect to motor insurance and Regulation 3 of The Solicitors Acts 1954 to 2008 (Professional Indemnity Insurance) Regulations 2011 with respect to solicitors' professional indemnity insurance).

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes, consumer protection provisions exist under Irish legislation which applies to insurance contracts.

Some of these provisions derive from EU law (e.g. implementation of the Unfair Terms in Consumer Contracts Directive and the Distance Marketing of Consumer Financial Services Directive), while other provisions that are designed to protect consumers derive from domestic law (e.g. The Sale of Goods and Supply of Services Act 1980 and the Consumer Protection Act 2007). For example, the Sale of Goods and Supply of Services Act 1980 prohibits the provision of false or misleading information to consumers and it requires the supplier of a service to have the necessary skill to provide the service and exercise due care and diligence in carrying out the service.

The Central Bank's Consumer Protection Code 2012 (the "CPC") applies to regulated financial service providers (including insurers) carrying on business in Ireland. The CPC contains a comprehensive framework designed to protect consumers in dealings with financial service providers. The provisions of the CPC are binding on regulated financial service providers and the Central Bank can administer sanctions for a contravention of the CPC. Chapter 2 of the CPC sets out twelve general principles which all regulated financial service providers (including insurers) must abide by in all dealings with customers. These include, in particular, the requirements to act honestly, fairly and professionally in the best interests of customers and the integrity of the market and to make a full disclosure of all relevant material information, including all applicable charges, in a way that seeks to inform the customer.

Other areas of the CPC which are of relevance to insurance contracts include Chapter 3 (dealing with premium handling and contact with consumers), Chapter 4 (specifying the information that must be provided to consumers before entering into a contract), Chapter 5 (knowing the consumer and assessing the suitability of the product) and Chapter 7 (dealing with rebates and claims processing).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

In 2012, the Irish Law Reform Commission published a consultation paper examining insurance contracts in Ireland. This consultation represented the first systemic review of insurance contract law in Ireland since the foundation of the Irish State in 1922. In the consultation paper, the Law Reform Commission examined whether the following principles and rules concerning insurance contracts would benefit from statutory consolidation:

i) The concept of "insurable interest";

ii) the duty of disclosure placed on the insured;

iii) the nature and scope of pre-contractual misrepresentation by the insured;

iv) the nature and effect of "warranties" in insurance contracts and their connection with "basis of contract" clauses;

v) the relationship between exclusions in insurance contracts and the general law on unfair terms;

vi) formalities (including specific terms that need to be drawn to the insured's attention);

vii) the duty of utmost good faith in insurance contract law;

viii) the rights of third parties; and

ix) the remedies available for breach of the contract.

The Law Reform Commission set out its provisional recommendations in the consultation paper. The period of consultation is closed. In 2013 the Law Reform Commission is expected to issue its final report on the findings.

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Definition of an Insurance Contract

1. <u>Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.</u>

According to Section 1 of the Insurance Contract Law, 1981 (hereinafter: "the Insurance Contract Law"): "An insurance contract is a contract between an insurer and an insured, which obliges the insurer, in consideration of premiums, to pay insurance benefits to the beneficiary upon the occurrence of the insured event."

As can be seen from the above definition, the main legal requirements for an insurance contract include:

- The existence of a contract;
- The parties to the contract: the insured and the insurer;
- The content of the contract: in consideration of premiums paid by the insured, the insurer undertakes to pay insurance benefits to the beneficiary upon the occurrence of an insured event.

The term "insured event" is not defined under the Israeli Law, however, the courts have ruled that the purpose of an insurance contract is to protect the insured from a risk which may or may not occur, and thus there must be some uncertainty as to the occurrence of the event.

2. <u>Does an insurance contract require an element of uncertainty? Please describe.</u>

One of the basic elements of an insurance contract is the uncertainty regarding the occurrence of the insured event. The uncertainty refers to the occurrence of the insured event or to the timing of the insured event (in life insurance).

Based on the uncertainty element, the Israeli courts have ruled that there is no policy coverage for property damage which was expected to occur under normal circumstances, such as natural wear and tear or as a result of an inherent vice (for example: Civil Appeal 172/98 *Sela v. Solel Boneh)*.

In addition, according to court rulings and Israeli scholars, damages resulting from an insured's intentional act will not be considered as uncertain from the insured's point of view, and thus they will not be covered under the policy (see for example, S. Veller, *Insurance*, Vol. I, p. 184 – 185).

Another implication of the uncertainty requirement is reflected in Section 16 of the Insurance Contract Law, according to which an insurance contract which provides coverage for a risk which, at the time the contract was entered into, has already ceased to exist or has already occurred, is void.

In Civil Appeal 1530/02 *Menora Ins. Co.* v. *Yuvalim* the Supreme Court referred to Section 16 when discussing the existence of policy coverage under a professional liability policy which was on claims made basis and included a retroactive date. In the said case, the claim – which was filed during the insurance period – arose from a demand letter which was sent to the insured prior to his entry into the insurance contract. The Supreme Court ruled that once a demand letter was sent to the insured, the filing of a court claim became almost certain, and thus the court claim which arose from the demand letter is not covered under the Policy. The Supreme Court stated:

> "… the parties to the insurance contract are not prevented from entering into an insurance contract which applies retroactively. Nevertheless, the basic principle of insurance is that there cannot be insurance for a certain damage… the element of uncertainty as to the occurrence of the insured event is an important basis of any insurance contract.
>
> The element of risk and uncertainty must be met also in policies which provide the insured's retroactive coverage… the meaning is that policies of this kind indeed provide retroactive coverage, however the coverage applies only to insured events which, at the time the insurance contract was entered into, none of the parties knew that they occurred".

3. <u>Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?</u>

According to Israeli court rulings, the purpose of an insurance contract is to transfer the risk from the insured to the insurer. As stated by the Supreme Court: "A key element in understanding the term insurance is the risk element. Insurance is a mechanism for transferring and allocating the risk that damage will occur " (Criminal Appeal 37/07 *Moshe Pereg v. the State of Israel*, also see: Civil Appeal (Central Dist. Court) 6749-08-07 *Shoshana Zerug v. Harel Ins. Co. Ltd.*)

4. <u>Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?</u>

Insurance Contract Law does not directly refer to the "insured interest" requirement; nevertheless, the law conditions the payment of insurance benefits on the

existence of damage which was caused to the insured or to the beneficiary (Section 55).

Israeli Courts interpreted the law very broadly and determined that as long as the insured suffered certain damage as a result of the insured event, the insured will be entitled to policy coverage, even if the insured is not the owner of the property. The Israeli courts referred to a large range of economic and legal interests which entitle an insured to insurance benefits.

In Civil Appeal 188/84 *Zur Ins. Co. Ltd. v. Hadad* the Supreme Court addressed the "insured interest" issue, in respect of an insured who purchased a vehicle insurance policy which covered a car which the insured already paid for, however was expected to gain ownership of only after its arrival to the car agency. The car was driven to the agency by an agency representative, and was involved in a car accident during the journey. The insurer claimed that the insured had no insurance interest in the car, and thus suffered no damage as a result of its loss. The Supreme Court rejected this argument and stated:

> "…the damage should be caused to the insured or the beneficiary; however this does not mean that the property has to be owned by one of them. Indeed, there are many cases in which a person insures another person's property due to his liability for it, and in case it is lost or damaged he will need to compensate the owner, and thus will suffer damage. There may also be circumstances in which a person insures property since he has an interest that the property will be transferred safely, in order to enable him to gain ownership over the property after its arrival".

In respect of life insurance, the Insurance Contracts Law determines that in cases where the person whose life is insured is not a party to the insurance contract, the contract requires the written consent of that person. This provision is based on the assumption that a person will not agree that his life will be insured by a party who has no connection with him.

5. <u>Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?</u>

Pursuant to Section 55 of the Insurance Contract Law, indemnification under a property insurance contract will be "for damage caused to the insured or the beneficiary by loss of or damage to the insured property". Accordingly, property insurance can apply only in cases where the insured (the policyholder) or the beneficiary under the policy suffered damage.

However, according to court rulings, the scope of coverage provided under the policy can exceed the actual damage suffered by the policyholder or the beneficiary, and can derive from the damage caused to a third party which is not named under the insurance contract. For example, in M.C.A. 5449/97 *Migdal Ins. Co. Ltd. v. Menora Ins. Co. Ltd.* the court ruled that a transporter of property is entitled to purchase an insurance policy which also covers the owner's interest in the property. This is allowed even though such an interest is broader than that of the transporter, despite the owner not being named under the policy.

6. <u>Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?</u>

The legal definition of "insurance contract" requires the contract to be between an insurer and an insured. Insurance Contract Law does not define the term "insurer", and does not refer to the need of an insurer to assume a large number of similar risks. Nevertheless, there were scholars who opined that only an insurer which spreads the risk by contracting with a large number of insured parties can be considered as an "insurer", and thus only a contract signed with such insurer can be considered as an insurance contract (S. Veler, *Insurance*, Vol. 1, p. 174; Y. Elias, *Insurance Laws*, Vol. 1, p. 20.).

There is a definition of the term "insurer" in the Supervision Over Financial Services (Insurance) Law, 1981 (hereinafter: "the Supervision Law"), however the relevance of this definition to the Insurance Contracts Law is questionable.

According to the Supervision Law, an insurer is whoever received an insurer's license pursuant to the Supervision Law. In order to receive an insurer's license, the applicant must present a business plan which will refer, inter alia, to the proposed premiums and payments to be collected from the insured parties and the actuarial assumptions that served as the basis for setting the premium tariff. The Commissioner of Insurance will not provide an appellant a license unless he is convinced of its financial stability and that the business plan is reasonable. In this respect, the Commissioner of Insurance will examine the number of risks expected to be assumed by the insurer and their effect on the insurer's global risk.

7. <u>Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?</u>

No. Life insurance is included in the general definition of "insurance contract" set in the Insurance Contract Law.

The said law determines that in life insurance "the insured event is the death of the insured or their

attaining a specific age or another event in their life other than an accident, sickness or disability".

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Section 32 of the Contracts Law (General Part), 1973 determines that, in general, contracts of gambling and chance are not enforceable under Israeli Law. A contract of gambling and chance is a contract in which "a party may win some benefit, where winning depends on fate, guesswork or a chance occurrence, rather than on understanding or ability".

Contrary to a gambling contract the purpose of which is to win some benefit, an insurance contract is meant to indemnify the insured for its damages. As mentioned above, Section 55 of the Insurance Contracts Law states that indemnification under a property insurance contract will be for damage caused to the insured or the beneficiary.

In M.C.A. 5449/97 *Migdal Ins. Co. Ltd. v. Menora Ins. Co. Ltd*, the Supreme Court stated that the purpose of Section 55 was to avoid contracts of gambling pretending to be insurance contracts.

ii) Warranty, guaranty or any other surety contracts

Section 14(a) of the Supervision Law prohibits the carrying on of insurance business in Israel without a license granting permission to do so. The term "carrying on of insurance business" is defined as "entering into insurance contracts commercially except for the granting of a guaranty for a commodity or for a service which is incidental to the main business of the guarantor".

It is unclear from the above definition whether a warranty or guaranty contract is considered as an insurance contract, and there is no Supreme Court precedent which referred to this issue. Nevertheless, the accepted opinion among scholars and lower court rulings is that warranty and guaranty contracts should not be considered as insurance contracts (U. Yadin, *Insurance Contracts Law*, 1981, p. 23; E. Zamir, Contraction Contract Law, 1974, p. 162; Civil File (Magistrate Court Tel Aviv) 182492/02 *Auto Glass Ltd.* v. Tiyuley Gili).

The distinction between insurance contracts and warranty or guaranty contracts is not always clear.

When dealing with a guaranty given by a service or product provider for the service/product provided, the main distinction is based upon the nature of the risk assumed: In cases where the risk arises from reasons controlled by the service or product provided, the transaction will be considered as guaranty. However, in cases where the risk arises from reasons beyond the parties' control –the transaction transferring the risk will be classified as insurance (A. Brener, *Insurance*, p. 54).

Another relevant distinction is between insurance and product or service guaranty/warranty provided by a third party (other than the manufacture or the original service provider). There were scholars who suggested that the classification should be based on the benefit obtained by the "insured" under the contract: when the benefit is monetary, the contract should be considered as "insurance" however when the benefit is service or a product, then the contract should not be considered as such (see for example E. Zamir, ibid).

The more common opinion is, that the classification of a transaction as "insurance" other than as warranty, guaranty or other surety contract should be made according to the purpose and nature of the transaction: a transaction the main purpose of which is to transfer risk from one party to the other will be considered as insurance while a contract the main purpose of which is to provide a service will not be classified as such (Civil File (Magistrate Court Tel Aviv) 182492/02 *Auto Glass Ltd. v. Tiyuley Gili*).

A similar classification (even though for other purposes) was applied in Civil File (Dist. Court - Tel Aviv) 2738/99 *Shimon Shabi v. Pelephone Communication Ltd.* The court ruled that a cellular company which provided repair services to its consumers should not be considered as an insurer, since the purpose of the services it provided, other than the consumer's satisfaction, was to assure that its consumers had an available product to accept and make telephone calls at all times. The main purpose of the services provided in that case was not the transfer of risk, but rather to promote the main business of the provider – selling cellular products.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts which are meant to transfer credit risks have characteristics similar to insurance contracts. Nevertheless, there is no reference in the Israeli Law or court rulings to the distinction between such financial contracts and insurance contracts.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

There is no specific exception or exemption in the Insurance Contract Law which determines that a contract which meets the characteristics of an insurance contract law will not be treated as such. It should be noted, however, that there are several insurance contracts which were excluded from most provisions of Insurance Contract Law (reinsurance,

marine insurance, aviation insurance and other branches determined by the Minister of Justice).

As mentioned above, in respect of the license requirement directed to a person carrying on insurance business, according to Section 14(a) of the Supervision Law, this requirement does not apply "for the granting of a guaranty for a commodity or for a service which is incidental to the main business of the guarantor".

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

See answer 9.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Yes. Section 14 of the Supervision Law prohibits carrying on of insurance business in Israel without a license granting permission to do so.

12. What are the legal consequences for the risk-taker acting without license?

A risk-taker acting without license can be exposed to criminal proceedings which may result in payment of fines or imprisonment (up to three years).

In addition, if such risk-taker made misrepresentations towards third parties, it can also be exposed to civil liability for the damages caused as a result of the misrepresentations.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

There are many limitations on the investments allowed to an insurer. The Supervision Over Insurance Business Regulation (Means of Investment of the Capital and Funds of an Insurer and the Management of its Liability), 2001 determines that investment by an insurer can be made only in accordance with the limitations set under the said regulations. The limitations refer to the nature of the assets in which an insurer may invest, and to the maximum share of each investment.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

According to the Supervision Law, to receive an insurer's license, the applicant shall submit details to the Commissioner of Insurance regarding the insurance programs it wishes to sell, including the full policy wording. In addition, any new insurance program or any change to an existing program must be notified in advance to the Commissioner of Insurance.

In several insurance fields (such as life insurance, personal accident insurance, and employers' liability insurance), any new insurance program or change in an existing program requires the approval of the commissioner. In some of these fields the program will be considered as approved if the commissioner did not object thereto within 30 days from the date on which the new program was submitted.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

According to Israeli scholars, an insurance contract issued by a non-licensed party should not be considered void, since such a conclusion contradicts the main purpose of the Supervision Law. The purpose is to protect insured parties from insurers who will not be able to fulfill their financial obligation towards the insured. Therefore, if the insured was not aware of the fact that the insurer is non-licensed, he should be granted the possibility to enforce his rights against the insurer (S. Veler, *Insurance*, Vol. 1., p. 173).

In any case, under Contract Law (General Part), 1973 if the insured was not aware of the fact that the "insurer" had no license, the insured may terminate the contract and is entitled to restitution of the premiums it paid or to compensation for the damages suffered as a result of the "insurer's" breach of contract/misrepresentations. Such claim for damages can be based also on the Tort Ordinance [New Version].

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes - The Insurance Contract Law.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

The Israeli Insurance Contract Law sets several requirements as to the form and content of an insurance contract as follows:

- Duty to provide the full policy wording to the insured - Section 2 of the Insurance Contract Law provides that the insurer must provide the insured with the full policy wording,

detailing the parties' rights and obligations (unless the insurance is in a field where according to the practice no written policy is issued). As long as the policy was not provided to the insured, the terms which will apply to the parties are the terms of the policy which was submitted by the insurer to the Commissioner of Insurance.

- The duty to emphasize policy exclusions - According to Section 3 of the Insurance Contract Law, terms intended to exclude or limit an insurer's liability must be detailed close to the subject to which it relates or must be emphasized in the policy. An insurer will not be entitled to rely on any limitation or exclusion which was not properly emphasized.

- Attachment to the policy – the insurer must attach to the policy a copy of the insured's response to the proposal form. A response which was not attached to the policy cannot be relied on by the insurer.

- The policy terms cannot contradict the cognitive provisions of the Insurance Contract Law – the law includes various provisions which cannot be stipulated against, including the insurer's remedies in case of non-disclosure, the insurer's remedies in case the insured did not incur safety measures required by the insurer, the insurer's duty upon receipt of a notification regarding the occurrence of the insured event etc.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

The Insurance Contract Law is consumer-oriented, and was drafted based on the premise that there is an inherent inequality between the insurer and the insured which should be rectified by the law. This principle is reflected in various law provisions, including:

- Duties imposed on the insurer intended to achieve transparency and assure that the insured is aware of its rights – As mentioned above, insurers are required to provide the insured with the full policy wording and to emphasize the policy exclusion. The Israeli courts added, that under certain circumstances, an insurer is also required to assure that the insured is aware of the policy terms and to draw the insured's attention to any change in the policy wording (Civil Appeal 4819/92 *Eliahu Insurance Co. v. Yashar Menashe*,).

- The insured's disclosure duties and the insurer's remedies in cases of non-disclosure - The Insured's disclosure duty requires them to reply completely, and in a straightforward manner to questions presented to the insured concerning material matters. In addition the law prohibits the insured from concealing information with fraudulent intent concerning material matters. This duty was recognized by the Supreme Court as the duty to initiate disclosure also in cases where the insured was not asked to do so (see for example: 282/89 *Shmuel Rotenberg v. Clal Insurance Company Ltd.*, and Civil Appeal 10-64/03 *Eliahu Insurance Co. Ltd. v. Estate of Rachel Piementa*).

  According to the Insurance Contract Law failure by an insured to fulfill its disclosure duties does not automatically release the insurer from liability. If the insurer discovered after the insured event occurred, that an insured breached its disclosure duties, then the insurer's liability may be reduced. The rate of reduction is proportionate to the additional premium which would have been requested by the insurer had it been aware of the true situation.

- The insurer's remedies in case of late notification - According to the Insurance Contract Law, an insured is obliged to notify the insurer of the occurrence of an insured event immediately upon becoming aware thereof. However, an insurer will be entitled to reduce its liability based on the breach of the insured's obligation, only if and to the extent that the timely notification would have enabled the insurer to reduce its liability.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

As can be seen, the Israeli insurance law is meant to protect the insured's rights to reduce the imbalance between insured parties and insurers, and to provide the insured with an advantage against the power, information and resources of the larger insurer.

Despite the above, it is very rare to find any distinction made by the law or the courts, between consumer insurance and commercial insurance. The pro-insured provisions of the Insurance Contracts Law equally apply to an individual insured party who purchased a vehicle insurance policy and to a financial institution which purchased a Bankers Policy.

Several Israeli scholars have pointed out the need to distinguish between consumer insurance and commercial insurance; however to date there have not been any significant steps taken in this direction. One can hope that the Israeli legislator will act in order to limit the ability of large commercial entities to take advantage of benefits which were meant to protect individuals who were insured.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

Under article 1882 of the Civil Code The insurance is the contract by means of which the insurer, against the payment of a premium, undertakes to repay the insured party, within the agreed terms, the damage caused to the insured party by an event, or to pay a capital or an annuity, subject to the verification of an event affecting the human life". The main criteria of an insurance contract are on one side the payment of the premium (by the insured or the policyholder) and on the other side the payment (by the insurer) of the indemnity (for non-life insurance), of the capital or of an annuity (for life insurance contracts). More in detail in non-life insurance contracts, we have an indemnification function ("funzione indennitaria"): the insurer has the obligation to indemnify the insured party only if the event covered by the insurance contract occurs and only to the extent of the damage effectively suffered by the insured as a consequence of the event; whereas in life insurance contracts, we have a security function: the obligation of the insurer is due in any case on the basis of the premium paid and there is no need to verify the existence of a damage or of a need by the insured party, his heirs, or of the beneficiary of the insurance policy (the insurance contract is based not only on a statistical forecast but also on a financial hypothesis, which implies the capitalization of the premiums paid).

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes, insurance contracts require an element of uncertainty, which could be better defined as the "risk" related to the possible occurrence of an event. In non-life insurance contracts, the risk is the possible occurrence of a harmful event (fire, theft, unfulfillment of an obligation undertaken by a debtor, etc.). In life insurance contracts the event to which the obligation of the insurer is linked is the death or the survival of a natural person (the risk covered is that of a possible need in the future). In this respect, please note that under article 1895 of the Civil Code an insurance contract is null and void if the risk never existed or if it terminated before the execution of the contract.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

The main scope of an insurance contract is the transfer of the risk (which is an essential element of the insurance contract) from the insured to the insurer (please refer to articles 1882 and 1895 of the Civil Code).

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

An "insured interest" is only required in non-life insurance contracts. The scholars defined the insured interest as the economic relationship that links the insured good and the insured party, so called economic interest. Under article 1904 of the Civil Code, which applies only to non-life insurance contracts, if the insured interest does not exist, the insurance contract is null and void.

On the contrary, the law does not require an interest in life insurance contracts. In the latter we may have an economic interest when the insurance covers the life of the insured party, and a legal interest when it covers the life of a third party (the authorization of the third party is required under article 1919 of the Civil Code), but – by way of an example – there are no requirements by law if the payment of the capital is due upon survival.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Under Italian law a third party can enter into an insurance contract in the name and on behalf of an insured party, because he represents it, or because he has a joint or indirect interest to the insurance contract. Namely this is possible, when the third party (i) represents the insured person on the basis of a power of attorney or as a legal representative (e.g.: the parent or the tutor of a minor, the legal tutor of an interdict or incapacitated) or (ii) has a joint interest to the insurance contract (e.g.: he is the lessee of a real estate, the holder of an usufruct on the property). In such case the policyholder can also be the beneficiary.

Furthermore a third party may enter into an insurance contract when he has an indirect interest to the insurance contract (e.g.: the person in charge of the shipping of certain goods or of their deposit). In this case the insurance is called "assicurazione per conto altrui" (insurance on behalf of a third party) or "assicurazione per conto di chi spetta" (insurance on behalf of whom it concerns), when the third party is not aware of the name of the owner of the insured goods (e.g.: when goods are sold various time during transportation).

The policyholder having an indirect interest to the insurance contract shall fulfill all the obligations provided by the same, except for those that can only be fulfilled by the insured party. As the insurance direct interest belongs to the insured person, to this latter belong the rights provided by the contract, including the right to the indemnity (he shall be the beneficiary). The third party cannot request the insurer to fulfill the contract unless he has obtained the consent of the insured party. The third party however has a privilege vis-à-vis the insured party for the amount paid to the insurer as premium and/or for the costs for preserving goods.

Another relevant hypothesis is that of the insurance contract entered by the policyholder (who shall also be the insured party) in favor of a third party (beneficiary) who has right to the capital or annuity (in life insurance contracts). In life contracts the interest of the policyholder to enter into the contract in favor of the third party is presumed. On the contrary, as a general rule, non-life insurance contracts in favor of a third party are not allowed as the allocation of the indemnity to a person who is not the holder of the insured interest is in conflict with the indemnification function of the contract, however if the insured party has an interest to said allocation (e.g.: in favor of the bank which has issued a loan and has a pledge on a property), the annotation on the policy of a binding appendix (“appendice di vincolo“) in favor of the third party is allowed.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the ‘law of the large numbers’)? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

Italian law requires that the risk assumed by the insurer be mitigated by the simultaneous insurance of similar risks (“law of the large numbers”). In general terms, the insurer risks are classified in 18 non-life and six life risks (Article 2 of the Private Insurances Code (“PIC”)). Upon execution of an insurance contract, the insurer has the following main obligations: (i) to record the insurance contract in its accountings and allocate the premium collected among the technical reserves; (ii) to maintain an adequate solvency margin; (iii) to have and maintain in place a technical organization which shall be able to neutralize the risks. For each of the above risks the insurer is required to adopt a number of actions aimed to mitigate the risks (i.e.: it shall resolve the execution of one or more passive reinsurance contracts pursuant to the provision (“circolare”) no. 574/2005 issued by the Italian supervisory regulator (Ivass).

The above obligations also affect the classification of the contract as an insurance contract. In this respect, please note the following: (a) the carrying out of non-life and life insurance activity is reserved to insurers (insurance companies) which has to meet a large number of requirements to be enrolled as such; (b) an insurance contract stipulated by a risk taker who is not a licensed insurer or is an insurer banned from the execution of new insurance contracts by Ivass is null and void and cannot be qualified as an insurance contract. Should this be the case, the agreement may be classified as a different type of contract (e.g.: contract of gambling or perpetual annuity).

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No as mentioned article 1882 of the Civil Code has set forth a unique definition; please refer to the answer to question 1 above.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Contracts of gambling and chance have similarities to insurance contracts, however they are not regarded as insurance contracts, regardless of the definition the parties have given to the contract.

The main difference between the two types of contracts is the fact that in insurance contracts, the risk of the insured party/policyholder pre-exists to the execution of the contract, whilst in gambling and chance contracts, the party creates the risk of damage by executing the contract. From a different standpoint, the reason of the contract differs; in the insurance contract the policyholder/insured party executes it in order to prevent himself (the insured party) from the consequences of a possible negative event, whereas in gambling and chance contracts the party is attracted by the possible gain and bets on the outcome of an event: there is no indemnification function.

Another relevant difference is the fact that, pursuant to article 1462 of the Civil Code, the rules that allow the risk taker to terminate the contract for excessive burden of the obligation do not apply to gambling and chance contracts, as they are classified as “contratti aleatori” (aleatorius contracts), whether similar rules, as provided by articles 1898 and 1926 of the Civil Code, apply to insurance contracts.

ii) Warranty, guaranty or any other surety contracts

As warranty, guaranty or any other surety contracts, these are not regarded as insurance contracts, nor do the provisions applicable to the latter apply to warranty, guaranty or other surety contracts. In

general terms, these contracts allow the creditor to have a second debtor: the creditor can choose its debtor unless the guaranty contract provides differently. Nonetheless, certain provisions applicable to guaranty contracts may apply to insurance contracts unless the parties have excluded such application. As an example this may happen with an insurance guaranty contract ("contratto di assicurazione fideiussoria") where the insurer undertakes to pay an amount to the beneficiary in case a third party does not fulfill its obligation vis-à-vis the beneficiary. In these contracts, according to the Supreme Court the insurer - pursuant to article 1956 and 1957 of the Civil Code - may have the right to refuse payment to the beneficiary in certain cases (if the beneficiary has granted a credit to the third party, without the permission of the insurer, even if he was aware that the financial situation of the third party may have implied its default; the insurer is solely responsible even after the expiration of the main obligation provided that the creditor has duly sued the debtor in due course).

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts such as hedging contracts, swaps and derivatives may have an insurance function, but are not classified as insurance contracts.

The Scholars agree on the fact that swap and interest swap do not constitute an insurance transaction. In this respect, please note that even if a risk is transferred from one party to another in these contracts, one of the essential elements of the insurance contract is missing, as the amount due to the risk taker (premium) is not identified on the basis of statistics laws and is not an insurance contract split in accordance with mutuality rules.

Furthermore, while in insurance contracts the risk is borne by the insurer, in swap contracts, the risk of fluctuation of the benchmark is borne by both parties, depending on the negative or positive fluctuation.

As to credit derivatives contracts, insurers sometimes use these to transfer the risks insured to third parties, as an alternative to traditional reinsurance contracts. In this respect, insurers are able to transfer the risk of credit default from one party to another, without assigning the ownership of the underlying credit and by keeping the relationship with insured parties. As an example in credit default swap contracts, the protection seller (SPV), against payment of a fee, undertakes to execute a predetermined payment in favor of the protection buyer (insurer), subject to the occurrence of an uncertain future event that expresses the deterioration in the credit profile of a third party (the insurer risk). These securitizations may concern both insurance and financial risks.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

No in principle there are no exceptions or exemptions applicable because, as mentioned, even if contracts meet all the characteristics of an insurance contract they will not be classified and treated as such, and will be null and void, if the risk taker is not licensed or is a banned insurer. An exception may be the case in which the insured party deemed the risk taker as a licensed insurer, in which case the contract may be voidable ("contratto annullabile") upon request of the insured party.

Furthermore, as mentioned above, certain rules provided only for insurance contracts do not apply to these "non-insurance transactions" that are classified as "aleatorius contracts": the rules provided by articles 1828 and 1926 (only for life insurance contracts) of the Civil Code setting forth the remedies provided for the insurer, in the case the fulfillment of the obligation became too onerous.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

No, a close legal or economic nexus does not provide for an exception.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Yes, under Italian law to qualify an insurance contract, the risk taker shall be an insurer duly licensed by Ivass and the license ("autorizzazione") shall be fully in force. Namely, pursuant to article 1883 of the Civil Code, the insurance activity can be exercised only by a public entity or by an S.p.A. ("joint stock company") complying with the rules set forth by special laws. Moreover, as mentioned, pursuant to article 167 of the PIC, an insurance contract stipulated by a non-licensed risk-taker or by an insurer that has been banned from the execution of new insurance contracts by the Italian Regulator (Ivass) is null and void.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

Pursuant to article 305 of the PIC anyone pursuing the insurance business without license shall be punished with imprisonment from 2 to 4 years and with a penalty varying from EUR 20,000 to EUR 200,000.

Pursuant to article 265 of the PIC, upon Ivass' proposal the Minister of Production Activities states the compulsory winding up ("liquidazione coatta amministrativa") of the risk taker without license. In case there are reasonable grounds for suspecting that a risk taker pursues the insurance business without license, Ivass shall also inform: (i) the Court which will adopt the measures provided by article 2409 of the Civil Code (a number of measures to protect the interests of the creditors/insured parties); and (ii) the public prosecutor.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, licensed insurance companies cannot enter into non-insurance business. The ratio of this rule is to preserve the carrying out of insurance techniques and procedures from other activities, in other words any premium, reserve and in general, assets collected or formed in the exercise of the insurance activities, shall be reserved to the insured business and to the satisfaction of the insured parties. The law allows the insurer to carry out only activities that are connected or instrumental to the insurance business. In this respect, the investment of technical reserves and of the free equity of the insurer, the direct management of insurance agencies (so called “agenzie in economia”), the reinsurance of the risk assumed, the activities concerning the management of integrative health and pensions’ insurance products (within the limit provided by law) are considered “connected activities”. On the contrary are defined as instrumental those activities whose nature is ancillary to the insured business. In this respect, within the limit of the free equity (formed by the assets that are not tied-up to the coverage of the technical reserves), insurers may also purchase interests (or even the control) in other companies even if they are not carrying out the insurance business. To this end, by way of example, the Supreme Court (order no. 30174 dated 30 December 2011) has recently clarified the following principles: (i) insurers are prohibited from carrying out non-insurance activities but not the single non-insurance acts; (ii) the release of a guaranty in favor of a third party is not forbidden unless it is continuous and in favor of an undetermined number of subjects; (iii) as far as insurers are allowed to purchase participations in non-insurance companies, they shall be able to guaranty the debts of such companies vis-à-vis third parties.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

No, the terms and conditions of insurance contracts shall not be submitted to the regulator (Ivass) for prior approval or as a kind of formal requirement.

Nonetheless, according to article 186 of the PIC an insurer may request Ivass to make a preliminary inquiry on the compliance of the informative note and of the insurance contract with the information requirements set forth by articles 185 and following of the PIC (please refer to answer 18 below). Ivass’s reply is due within 60 days and in such period the insurer shall not distribute the insurance product; the documents sent are deemed compliant if Ivass does not reply within the above term.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

As mentioned above, pursuant to article 167 of the PIC, an insurance contract stipulated by a risk taker who is not a licensed insurer, or as an insurer has been banned from the execution of new insurance contracts by the Italian regulator (Ivass), is null and void. The nullity and voidability of the insurance contract can only be claimed by the policyholder or by the insured party (so called “nullità relativa”) and, once acknowledged, implies the reimbursement of the premiums paid. In any case the indemnifications paid or due by the risk-taker to the insured party and/or to other parties having right to the indemnification cannot be claimed back. Damages can also be requested.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes, insurance contracts are mainly regulated by the Civil Code and by certain Sections of the PIC. To this end article 165 of the PIC, entered into force on 1 January 2006, clarifies that the rules of the Italian civil code apply to insurance contracts unless they are in conflict with the PIC rules (“lex specialis derogat legi generali”). In particular, the following specific provisions apply to insurance contracts:

- Articles from 1882 to 1932 of the Civil Code;
- Articles from 165 to 181 of the PIC, Title XII, “Rules relevant to insurance contracts”;
- Articles from 182 to 187 of the PIC, Title XIII, “Disclosures of operations and policyholder’s protection”.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

In theory under Italian law there is no form requirement for insurance contracts: article 1888 of the Civil Code requires the written form of an insurance contract only as a proof of evidence, but in practice, the insurance contract is always stipulated in written form as a pre-formulated standard contract drafted by the insurer not amendable by the insured party or the policyholder. To protect the interests of the insured parties, the legislator has therefore set a number of rules as follows, which indirectly require the written form:

- Under article 166 of the PIC stating that “the contract and any other document delivered by the insurer to the policyholder shall be

drawn up in a clear and exhaustive manner" and that "clauses providing, forfeitures, nullities or limitations to the guarantees or which set forth charges on the policyholder or the insured party, shall be shown in highlighted fonts";

- Under article 1888, par. 2 of the Civil Code stating that the insurer is obliged to provide the policyholder with the insurance policy or any document signed by the same;
- Under article 127 of the PIC, applicable to compulsory insurance against civil liability in respect of the use of the motor vehicles and crafts ("assicurazione obbligatoria contro la responsabilità civile per la circolazione dei veicoli a motore o dei natanti") which sets forth the obligation for the insurer to issue an insurance certificate.

Moreover, please consider that article 1889 of the Civil Code clarifies that an insurance written proposal addressed to the insurer will remain valid for a period of 15 days (30 days in case a visit of the doctor is required to provide the insurance) starting from the date of delivery of the proposal to the insurer or the date in which the proposal is delivered to the courier.

As to the content of an insurance contract, its essential elements are those provided for any contract by articles 1325 and following of the Civil Code. Namely, an insurance contract shall contain at least the following elements:

i) the identification of the risk to be covered by the insurer (as mentioned, article 1895 of the Civil Code provides the nullity and voidness of an insurance contract if the risk has never existed or if the risk is terminated before the execution of the contract);

ii) the identification of the good or person to which the insurance refers;

iii) the identification of the insurance interest (only for non-life insurance contracts). As mentioned above pursuant to article 1904 of the Civil Code if the insured interest does not exist, the insurance contract is null and void;

iv) the identification of the duration of the insurance contract (only for non-life insurance contracts). In this respect, please note that pursuant to article 1899 of the Civil Code, the insurance starts at 2400 hours of the date on which the agreement is stipulated and ends at 2400 hours of the last day of the duration period as indicated in the insurance contract; if the insurance contract is automatically renewed, each new renewal period cannot exceed two years;

v) the limitation of the obligations of the parties to the contract; in this respect the contract shall identify forfeitures, nullities or limitations to the guarantees or charges on the policyholder or the insured party (article 166 of the PIC);

vi) the amount of the premium. Under article 1901 of the Civil Code (applicable only to non-life insurance contracts), if the policyholder does not pay the premium or the first installment of the same, the insurance will remain suspended up to 2400 hours of the date in which the payment is made. The same rule applies in case of default of payment of the next premiums, or portion of it. Furthermore, the insurance contract is terminated by law, within 6 months starting from the date on which the premium was due, unless the insurer claims for its payment.

It should also be stressed that article 1932 lists a number of principles that cannot be derogated unless the derogation is in favor of the insured party; in this respect, please consider *inter alia* the following provisions:

- The minimum duration of an insurance contract proposal sent by the insured party to the insurer (article 1887 of the Civil Code);
- the insurer loses the right to request that the insurance contract be declared null and void if after three months from the date the insurer became aware of the unfair declarations or omissions of the policyholder acting with fraud or with gross negligence; a similar rule applies in case the policyholder acted without fraud or gross negligence, in such a case the insurer has the right to withdraw only within 3 months from the date it was informed of the unfair declarations/omissions (Articles 1892 and 1893 of the Civil Code);
- the provisions of articles 1892 and 1893 of the Civil Code apply also to the beneficiary (insured party) of an insurance contract executed on behalf of a third party (please also refer to answer 5 above);
- the obligation of the insurer to reduce the premium starting from the next payment in case it has been informed that the insured risk was lower than agreed (article 1897 of the Civil Code);
- the insurer loses the right to withdraw from the insurance contract after one month from the date it has been informed that the insured risk was higher than agreed (Article 1898 of the Civil Code);
- in case of automatic renewal of an insurance contract, the duration of the renewal period cannot exceed two years pursuant to article 1899 of the Civil Code (please refer to Answer 17 (iv) above);

- pursuant to article 1901 of the Civil Code the insurance contract remains suspended up to 2400 hours of the date in which the policyholder pays the same (up to 2400 hours of the fifteenth day after the expiration of the payment date in case of renewal); the agreement is terminated by law if the insurer does not claim the payment of the premium; in any case the insurer will only have right to the payment of the premium and of the costs borne (no damages);
- the insured party's right to sue the insurance agent in lieu of the insurer for obligations connected to the duties the agent would have executed on behalf of the insurer (article 1903, 2nd par. of the Civil Code);
- the costs borne by the insured party to avoid or reduce the damage are paid by the insurer proportionally to the insured value when compared to the value at the time of the event, even if the amount of such costs exceeds the insured amount or in case of poor results, unless the insurer proves that the costs incurred by the insured party were made in an unreasonable way (article 1914, 2nd par. of the Civil Code);
- if the insured party negligently omits to inform the insurer of the event or to act in order to safeguard the insured goods, the insurer can reduce the indemnity proportionally to the damage suffered (article 1915, 2nd par. of the Civil Code);
- with respect to an insurance contract against civil liability, the costs borne to counterclaim against the damaged person are paid by the insurer up to an amount equal to 1/4 of the insured amount; in case the amount due to the damaged person exceeds the insured value, legal costs are split among the insurer and insured party on the basis of their respective interest; the insured party sued by the damaged party can request the insurer to intervene in the relevant proceeding (article 1917, par. 3 and 4, of the Civil Code);
- with respect to a life insurance contract, should the insured party change its activity or profession, the insurance contract remains valid under the same terms and conditions executed by the insurer ; if this is not the case, the insured party shall notify the insurer within 15 days from the date of the change; the insurer in turn may withdraw from the insurance contract, reduce the insured value or increase the premium; the insured party has 15 days to accept or refuse the proposal (no reply means acceptance); the insurer however has the right to the premium related to the current insurance duration period; the insured party maintains the right to the reimbursement of the capital (article 1926 of the Civil Code).

18. <u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>

Articles 117 to 120 and from 182 to 187 of the PIC set forth a number of rules to be followed by the insurers and/or the insurance intermediaries distributing insurance contracts concerning duties and responsibilities versus insured parties, including pre-contractual obligations, rules to avoid conflicts of interests and ensure transparency and an informed consent by the insured party, obligations in terms of asset segregation and fulfillment of payment obligations.

Under article 120 of the PIC, insurance intermediaries shall provide customers (potential insured parties) with information, before the signing of the contract or renewal with amendments of the same, by clarifying: a) whether they give the advice on the basis of a fair analysis and large number of contracts available on the market (to be able to offer or recommend an insurance product adequate to the policyholder's needs according to the information provided by the latter); b) whether they offer insurance products under a contractual obligation with one or more insurers and in any case they shall provide their names. In any case prior to the signing of the contract the insurance intermediary shall illustrate the main characteristics of the contract and the obligation undertaken under the same by the insurer. More detailed provisions are set forth by Ivass' regulations.

Under article 183 of the PIC, before the signing and for the duration of the contract, insurers and intermediaries shall always:

a) behave with diligence, fairness and transparency towards policyholders and insured persons;

b) acquire from policyholders the information necessary to evaluate their insurance or pension needs and act in such a manner that they are always appropriately informed ("suitability rule");

c) make arrangements so as to identify and prevent – where reasonably possible – conflicts of interest and, in case of conflict, make policyholders aware of the possible adverse effects, and anyhow manage these conflicts so as to exclude any detrimental consequences for policyholders;

d) achieve an independent, sound and prudent financial management and take adequate measures to safeguard the rights of policyholders and insured persons.

Furthermore, according to articles 117 and following of the PIC the amounts paid to the intermediaries and

those belonging to insurers or needed to compensate damages shall be paid in a segregate account. Intermediaries may however be exonerated from such obligation if they provide a bank guaranty. To protect the consumer/insured party on such bank account lawsuits, seizures or pledges by creditors, except those of insured parties or insurers, are not admitted. Moreover payments in cash to insurance intermediaries are only admitted for non-life insurance premium if the amount is lower than EUR 500; premium payments made by policyholders acting in good faith to the insurance intermediary or to its co-workers, are considered as made directly to the insurer.

Another provision relevant for the protection of customers/insured parties is that of article 119 of the PIC which sets forth the joint responsibility of insurers for losses caused by certain insurance intermediaries (those directly employed by the insurers, so called “produttori”, banks and financial intermediaries acting as insurance intermediaries and their co-workers), even if such losses are caused by criminal offences committed by the latter.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

With reference to aspects of the Italian jurisdiction that could be of interest for this project, please consider the following:

- The insurance of economic risks, such as coverage of the shares or bonds value, outcome of a speculative transaction, etc., is not allowed (Ivass regulation no. 29);
- a factual defect of the Italian insurance market is the fact that insurers are not willing to execute insurance contracts to cover certain insurable risks, even if they are permitted by the law (e.g.: we found that damages directly caused by a storm are not insured unless they are related to agricultural risks);
- after the Lehman Brothers crash, the counterpart’s risk of the index linked insurance contract is fully endorsed to the insurer (pursuant to regulation no. 35 of Ivass).

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Japan

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Preamble:

The Insurance Act of Japan (Act No. 56 of 2008, as amended; the "Insurance Act") and the Insurance Business Act of Japan (Act No. 105 of 1995, as amended; the "IBA") are the primary laws governing insurance matters in Japan.

The Insurance Act is a special-purpose contract law enacted to regulate various aspects of insurance contracts. It addresses the formation, effect, performance and termination of contracts for non-life insurance, life insurance and fixed-benefit accident and health insurance (with reinsurance being categorized as non-life insurance for this purpose). The Insurance Act contains default provisions, setting forth rights and obligations between parties that may be altered through contractual agreement, as well as compulsory provisions that are mandatorily applicable to one or both parties to any covered contract.

The IBA provides for the regulation and supervision of insurance business. This regulation and supervision applies to Japanese insurance companies, as well as foreign insurers and so-called "small amount" and "short term" insurance providers operating in Japan. The provisions of the IBA can be divided by subject matter into the following three general groups:

a) provisions for the regulation and supervision of companies engaged in the insurance business;

b) provisions for the incorporation and organization of insurance companies; and

c) special measures for policyholder protection.

Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

Article 2(1) of the Insurance Act defines an "Insurance Contract" as a contract, regardless of title, under which one party undertakes to provide a benefit (which, in the case of life insurance contracts and fixed-benefit accident and health insurance contracts, is limited to the payment of money) to the other party in the event of certain contingencies, while such other party undertakes to pay a premium determined based on the likelihood of such contingencies.

In addition, Insurance Contracts are further classified into non-life, life and fixed-benefit accident and health insurance contracts under Articles 2(6), (8) and (9) of the Insurance Act, respectively. The specific definitions are as follows:

Non-life insurance contracts include Insurance Contracts under which insurers undertake to provide compensation for damages suffered due to the occurrence of specified fortuitous accidents (Art. 2(6)).

Life insurance contracts include Insurance Contracts under which insurers undertake to pay fixed amounts in connection with the survival or death of insured individuals (other than contracts which fall within the definition of fixed-benefit accident and health insurance, below) (Art. 2(8)).

Fixed-benefit accident and health insurance contracts are defined to include Insurance Contracts under which insurers undertake to pay fixed amounts based on injury or illness suffered by insured individuals (Art. 2(9)).

2. Does an insurance contract require an element of uncertainty? Please describe.

Non-life insurance contracts, as defined in the Insurance Act (see our response to question 1 above), require an element of uncertainty. More specifically, the occurrence of the insured event must generally be uncertain at the time of entry into the insurance contract. (The term "fortuitous", which appears in the definition of non-life insurance contracts is construed by Japanese courts and legal scholars to mean that the occurrence of the insured events must be uncertain at the time of the conclusion of the contract.) Japanese legal scholars generally agree that life insurance contracts and fixed-benefit accident and health insurance contracts also require the element of uncertainty, but this is not expressly required in their respective definitions under the Insurance Act.

In the light of the above principle, retroactive insurance (i.e., insurance covering contingencies which may have occurred prior to entry into the insurance contract, or prior to the policyholder application) is only valid in very restricted circumstances.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

There is no express statutory requirement in Japan that a contract must provide for a transfer of risk in order to be recognized as an Insurance Contract. In practice, however, based on the definitions presented in response to question 1 above, such transfer of risk is a necessary characteristic of Insurance Contracts.

[1] The authors would like to acknowledge, with thanks, the assistance of Tomoki Debari, William Segal and Huan Lee (Henry) Tan.

More specifically, as explained above, the term Insurance Contract is defined as a contract under which one party undertakes to provide a benefit to the other party in the event of certain contingencies, while such other party undertakes to pay a premium determined based on the likelihood of such contingencies. Through the substantive effect of this definition, Insurance Contracts, accordingly, are contracts through which one party transfers the risk of certain contingencies to another party.

The premiums paid in consideration of such transfer, as also noted above, are required to be determined on the basis of the likelihood of occurrence of the specified contingencies. This in turn means that insurance premiums payable under Insurance Contracts must reflect the risks transferred thereunder.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Article 3 of the Insurance Act requires insured parties in non-life insurance contracts to have an "insurable interest" in order for such contracts to be effective. Article 3 of the Insurance Act further requires such "insurable interest" to be susceptible to financial evaluation (i.e., to be capable of being evaluated in monetary terms). In addition, Japanese legal scholars have generally taken the view that an interest will constitute an insurable interest only if it satisfies the following requirements:

a) certainty of existence (an interest that does not exist at the outset of an insurance contract may constitute an insurable interest, provided that such interest is certain to arise subsequently); and

b) legality (no illegal interest may constitute an insurable interest; e.g., a non-life insurance contract in which the insurable interest is in smuggled goods, such as narcotics, cannot be established).

Insurable interests are not required in connection with Insurance Contracts for life insurance and fixed-benefit accident and health insurance.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

As stated in our response to question 4 above, insurable interests are required only in the case of non-life insurance. Under Article 8 of the Insurance Act, the insurable interest need not attach to the policyholder himself/herself in the event that the insurable interest attaches to a party other than the policyholder , however, such a party must be the beneficiary under the insurance contract.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

There is no provision of the Insurance Act or the IBA, which expressly makes classification as an Insurance Contract contingent on risk mitigation through applicability of the law of large numbers. In practice, however, the Financial Services Agency of Japan (the "FSA"), which serves as Japan's insurance regulatory authority, ensures through a combination of supervisory and actuarial requirements that holders of insurance business licenses in Japan operate so as to benefit from the law of large numbers.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Please refer to our response to questions 1 and 4 above for definitions of and distinctions between non-life insurance contracts and life insurance contracts.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Gambling is prohibited in Japan under Article 185 of the Criminal Code of Japan (Act No. 45 of 1907, as amended). The Insurance Act and the IBA do not expressly define the differences or relationship between Insurance Contracts and contracts relating to gambling and chance. Insurance Contracts, however, are not deemed to fall within the definition of contracts relating to gambling and chance, and the Insurance Act incorporates certain measures intended to preclude Insurance Contracts being utilized for the purpose of gambling.

In the case of non-life insurance, Article 3 of the Insurance Act requires the existence of an insurable interest (as mentioned above), and Insurance Contracts are also subject to a non-codified but judicially recognized "non-profit principle". Both of these are intended to have the effect of preventing the use of insurance contracts for gambling purposes. The non-profit principle, generally recognized by Japanese courts and legal scholars, nominally prohibits insureds from making a profit from insurance

proceeds, which is deemed unacceptable from a public interest perspective; but the scope and effect of this prohibition is unclear.

In the case of life insurance, Article 38 of the Insurance Act provides that a life insurance contract under which the insured is different from the policyholder will become effective only with the insured's consent. This requirement is also intended as a gambling prevention measure.

ii) Warranty, guaranty or any other surety contracts

The Insurance Act and the IBA do not expressly define the differences or relationship between Insurance Contracts and warranties, guaranties or any other surety contracts.

Warranty

Warranties, such as those provided by distributors or manufacturers of products, are very similar to insurance contracts, in that the distributor or manufacturer offers repair services if required and receives premiums in consideration for assuming this contingent risk. Providers of warranties, however, are in some cases shielded from the requirement to obtain an insurance business license pursuant to the Comprehensive Guidelines for the Supervision of Small-amount and Short-term Insurance Providers issued by the FSA (the "FSA Guidelines").

More specifically, Section III-1-1 of the FSA Guidelines provides that the FSA shall determine whether offering of services on a contingent basis in relation to accidents, in consideration of fees payable in advance, will fall within the definition of "insurance business" and therefore require an insurance business license. Such determination is made taking into account various matters, such as whether the services have previously been recognized as being different from insurance transactions.

Section III-1-1 of the FSA Guidelines also expressly provides that provision of contingent repair services for purchased products, which are provided to customers incidentally to the manufacture and/or sale of such products, will not fall within the definition of "insurance business".

Guaranty/surety

Insurance Contracts and guaranties/sureties are deemed by applicable Japanese law to constitute different types of transactions, subject to differing requirements and restrictions. Entities entering into guaranties/sureties need not be licensed to engage in the insurance business.

iii) Financial contracts such as hedging contracts/swaps/derivatives

The Insurance Act and the IBA do not expressly define the differences or relationship between Insurance Contracts and hedging contracts, swaps and/or derivatives.

Insurance Contracts and hedging contracts, swaps and derivatives are deemed by applicable Japanese law to constitute different types of transactions, subject to differing requirements and restrictions. Entities engaging in hedging contracts, swaps and/or derivatives transactions need not be licensed to engage in the insurance business.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Article 2 of the IBA expressly excludes certain risk-underwriting businesses from the types of business requiring an insurance business license. Such risk-underwriting businesses include, (1) businesses governed by other legislation; (2) the business of risk-underwriting by certain entities for the benefit of their constituent members; and (3) the businesses of underwriting risks relating to 1,000 persons or less.

Section III-1-1 of the FSA Guidelines also excludes provision of congratulatory or condolence payments from business requiring an insurance business license, provided that (i) such payments are generally and widely recognized as common practice in society and (ii) the amounts paid are reasonable in light of common sense. (This "reasonable in light of common sense" limitation is stipulated in Section III-1-1 of the FSA Guidelines to be subject to a maximum amount of JPY 100,000.)

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

As indicated in our response to question 8(ii) above, Section III-1-1 of the FSA Guidelines provides that provision of contingent repair services for purchased products, which are provided to customers incidentally to the manufacture and/or sale of such products, do not fall within the definition of "insurance business" requiring an insurance business license.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Article 3 of the IBA requires that any person wishing to engage in the insurance business in Japan must obtain an insurance business license, of which two types are available, namely the life-insurance business license and the non-life insurance business license. Pursuant to Article 185 of the IBA, a foreign insurer will generally be required to establish a branch in Japan and obtain an insurance business license before engaging in insurance business in Japan. However, Article 186 of the IBA permits foreign insurers to directly underwrite certain types of insurance (such as reinsurance and marine insurance) without establishing branches in Japan and without obtaining insurance business licenses.

12. What are the legal consequences for the risk-taker acting without license?

Pursuant to Article 315 of the IBA, a risk-taker who is required to obtain an insurance business license in Japan but fails to do so may be subject to imprisonment for up to three years and/or a fine of up to JPY 3 million. A company, the representatives, agents or employees of which engage in insurance business when such company does not hold an insurance business license may also be subject to a fine of up to JPY 3 million.

Please also refer to our response to question 15 below for legal consequences vis-à-vis insurance contracts underwritten by unlicensed insurance providers.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Article 100 of the IBA prohibits any company holding an insurance business license in Japan from conducting any business other than the following:

a) the business of underwriting insurance and investing assets, such as insurance premiums received (i.e., the inherent business of insurance companies);

b) businesses which are incidental to the inherent business of insurance companies referred to in item 1) above (e.g., provision of guarantees, and underwriting and distribution of Japanese government bonds (the latter is in fact unrelated to such inherent business, but by tradition is a business conducted by insurance companies in Japan));

c) businesses stipulated under the IBA (e.g., the sale of investment funds), provided that engagement in such businesses does not preclude the relevant insurance company's engagement in the inherent business of insurance companies referred to in (a) above; and

d) businesses in which insurance companies are specifically permitted to engage under relevant laws other than the IBA.

Insurance companies wishing to engage in businesses described in (b) through (d) above may be subject to additional permission or licensing requirements under legislation other than the IBA.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Article 4 of the IBA requires every applicant for an insurance business license to attach general policy conditions to its written application. The applicant must also attach to such written application a statement of business procedures in relation to the proposed insurance business (including special provisions of insurance contracts). These documents must conform to the requirements of the IBA.

An insurance company wishing to modify its general policy conditions or any special provision stipulated in its statement of business procedures generally will be required under Article 123 of the IBA to obtain authorization from the FSA. As an exception, an insurance company may modify its general policy conditions or the special provisions in its statement of business procedure by giving advance notification to the FSA, if such modifications relate to certain types of corporate insurance (commercial lines of insurance such as employee pension insurance and marine insurance) specified in Article 83 of the Ordinance for Enforcement of the IBA (Ordinance No. 5 of the Ministry of Finance of 1996, as amended) (the "Ordinance for Enforcement").

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Neither the Insurance Act nor the IBA specifies whether an Insurance Contract issued by an unlicensed party is legally valid or capable of being annulled by either party, and this issue is not addressed in recognized legal scholarship or precedents. Generally speaking, violation of the IBA (including underwriting activities by an unlicensed party) will not affect the validity of the relevant Insurance Contract.

Notwithstanding this, if a party violates the IBA by underwriting Insurance Contracts without an insurance business license and thereby prejudices the interests of consumers (e.g., by including provisions in such Insurance Contracts which are harmful to policyholders), such Insurance Contracts may be deemed invalid or capable of being annulled by consumers under the Consumer Contract Act (Act No. 61 of 2000, as amended; the "Consumer Contract Act") or by court application of principles of equity.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

As described in the preamble to this questionnaire, the Insurance Act and the IBA are the primary laws governing insurance matters in Japan. Some other laws that apply to insurance transactions are described below.

1. Regulatory Laws

While the IBA sets forth a comprehensive regulatory regime with respect to the insurance business, the Ship Owner's Mutual Insurance Union Act of Japan (Act No. 177 of 1950, as amended) is an additional source of insurance and reinsurance law relating specifically to mutual-aid type hull insurance and liability insurance for ship owners. In addition, the Agricultural Co-operatives Act of Japan (Act No. 132 of 1947, as amended), the Fishery Co-operatives Act of Japan (Act No. 242 of 1948, as amended), the Small and Medium-Sized Enterprise Co-operatives Act of Japan (Act No. 181 of 1949, as amended) and the Consumer Co-operatives Act of Japan (Act No. 200 of 1948, as amended) regulate insurance-like businesses (i.e., mutual aid programs) operated by co-operative associations. Furthermore, the Japanese government, formerly, engaged directly in the life insurance business (through so-called "postal life insurance" (*kampo*) arrangements), and in this connection was regulated by the Postal Life Insurance Act of Japan (Act No. 68 of 1949, as amended). Both postal life insurance and the related legislation were abolished in connection with Japan's postal service privatization in 2007.

2. Private Laws

2.1. Special Private Laws

While the Insurance Act constitutes a "general" private law with respect to insurance contracts, "special" private laws providing for the formation, effect, performance or termination of insurance contracts may override the provisions of the Insurance Act. In the field of non-life insurance, provisions of the Commercial Code of Japan (Act No. 48 of 1899, as amended; the "Commercial Code") regarding marine insurance, as well as the Automobile Liability Security Act of Japan (Act No. 97 of 1955, as amended), the Act on Liability for Oil Pollution Damage of Japan (Act No. 95 of 1975, as amended) and the Act on Compensation for Nuclear Damage of Japan (Act No. 147 of 1961, as amended) serve as "special" private laws. No "special" private laws exist in the field of life insurance or fixed benefit accident or health insurance.

2.2. Application of General Private Laws

Insurance contracts constitute a particular type of contract, and accordingly general private laws broadly applicable to all contracts, such as the Civil Code of Japan (Act No. 89 of 1896, as amended) and the Commercial Code, will apply thereto, except for matters expressly provided in the Insurance Act. Other applicable general private laws include the Consumer Contract Act and the Act on Sales, etc. of Financial Products (Act No. 101 of 2000, as amended; the "Act on Sales, etc.").

17. **<u>Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.</u>**

1. Form

The Insurance Act does not impose specific requirements with respect to form or procedural requirements in connection with the formation of insurance contracts. Although Article 6 of the Insurance Act requires insurers to deliver certain documents to policyholders upon conclusion of insurance contracts, effectiveness of such contracts is not subject to compliance with this requirement. In addition, the Insurance Act does not impose specific procedures in connection with applications to enter into insurance contracts. Accordingly, verbal applications (for example) theoretically may be effective. In practice, however, insurance companies in Japan will not accept applications unless made utilizing a prescribed form.

2. Contents

Under Article 9 of the Ordinance for Enforcement, general terms of insurance are required to include the following matters:

a) events triggering insurance payments;

b) factors rendering the insurance contract invalid;

c) events or factors releasing the insurer from its obligations under the insurance contract;

d) methods of determining the scope of obligation of the insurer, and the timing of performance thereof;

e) disadvantages imposed on the policyholder or the insured in the event of any breach of their obligations under the insurance contract;

f) events triggering partial or complete termination of the insurance contract, and rights and obligations of the parties upon such termination; and

g) in the event that any policyholders are entitled to policy dividends, the scope of such entitlement.

Please also refer to our response to question 14 above regarding the required regulatory procedures for the implementation and amendment of general policy conditions and the statement of business procedures (including special provisions of insurance contracts).

18. **<u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>**

Under Article 300 of the IBA, licensed insurance companies and their officers and insurance sales forces and insurance agents, as well as insurance

brokers and their officers and employees, are prohibited, in connection with concluding any insurance contract or engaging in any insurance solicitation activity, from making false statements or omitting any important matter relating to such insurance contracts.

The Consumer Contract Act and the Act on Sales, etc. also impose obligations of explanation on insurance product providers (Article 4 and Article 3, respectively). In addition, case law and scholarly views indicate that insurers may owe explanatory obligations to policyholders and insureds based on the Civil Code, violation of which may result in insurer liability for contractual or tort damages. The basis for these judicial and scholarly positions is the widely held view that there is generally a knowledge and information gap between insurers and policyholders/insureds in insurance transactions, and that therefore insurers' explanations may crucially affect decision-making by policyholders/insureds.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

No.

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

What constitutes a "contract of insurance" is not specifically defined under Malaysian law. Like any contract, an insurance contract is subject to the Malaysian Contracts Act 1950, but no particular form is required for a contract of insurance. Section 2 of the Insurance Act 1996 ("IA 1996") provides that a policy of insurance need not be embodied in or evidenced by an instrument.

It is noteworthy that the Malaysian Court of Appeal has in *Dancom Telecommunication (M) Sdn Bhd v Uniasia General Insurance Bhd [2008] 6 MLJ 52* and *Mary Colete John v South East Asia Insurance Bhd [2010] 2 MLJ 222* cited with approval the statement of principle by Megarry VC in *Medical Defence Union Ltd v Department of Trade [1980] 1 Ch 82* at pp 89–90 on the requirements of a contract of insurance:

> "First, the contract must provide that the assured will become entitled to something on the occurrence of some event. … Second, the event must be one which involves some element of uncertainty. … Third, the assured must have an insurable interest in the subject matter of the contract."

2. **Does an insurance contract require an element of uncertainty? Please describe.**

The Court of Appeal in *Dancom Telecommunication (M) Sdn Bhd v Uniasia General Insurance Bhd [2008] 6 MLJ 52* and *Mary Colete John v South East* Asia Insurance Bhd [2010] 2 MLJ 222 has answered this question in the affirmative (see quotation above).

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

A contract of insurance is, in effect, the transfer of risk from the assured/insured to the underwriting member/insurer, in consideration of a premium paid by the assured to the underwriting member. Whilst the requirement of transfer of risk has not been considered by the Malaysian courts, it is implicit in insurance contracts. This is, in fact, an essential feature of insurance (see *Malcolm Clarke, "The Law of Insurance Contracts" (4th Ed) at p.10)* and it is likely that if called upon to determine the point, a Malaysian court would find likewise.

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?**

The Court of Appeal in *Dancom Telecommunication (M) Sdn Bhd v Uniasia General Insurance Bhd [2008] 6 MLJ 52* and *Mary Colete John v South East Asia Insurance Bhd [2010] 2 MLJ 222* has answered this question in the affirmative (see quotation in answer to Question 1 above).

It would appear that where insurance with respect to goods is taken out by a person without interest in the said goods, the contract would likely be construed as a wager rather than a contract of insurance. In Malaysia, agreements by way of wager are void under Section 31(1) of the Contracts Act 1950.

5. **Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?**

The insured interest may, in some cases, be attributable to a third party. This is, for example, where the insured is legally responsible for the said third party, for instance, in a relationship of employer and employee or principle and agent (see *Williams v Baltic Insurance Association of London Ltd. [1924] 2 KB 282*). In such cases, the third party need not be the beneficiary under the insurance contract.

In cases of life insurance, insurable interest may lie with a third party (e.g. the life of one's spouse, the life of a child or ward being under the age of majority at the time the insurance is effected; the life of the insured's employees; etc) by a statutory legal presumption under Section 152(2) of IA 1996.

6. **Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?**

Under Malaysian insurance law, the 'law of the large numbers' has no legal significance and is merely an actuarial issue. However, under Section 57(1) of IA 1996, a licensed insurer may enter into reinsurance arrangements which are "consistent with sound insurance principles." The licensed insurer shall produce for the Bank's assessment particulars of the reinsurance arrangement, as the Bank may require in keeping with Section 57(2) of IA 1996.

7. **Does the definition of an insurance contract differ between life insurance and**

non-life insurance (obviously apart from the subject matter)?

Life insurance or "life business" is defined under Section 2 of IA 1996 as, inter alia, the business of undertaking liability under a life policy.

Section 4 IA 1996 distinguishes the two different classes of insurance business as follows:

a) life business, which in addition to all insurance business concerned with life policies shall include any type of insurance business carried on as incidental only to the life insurer's business; and

b) general business, which means all insurance business which is not life business.

It would, therefore, appear that apart from the subject matter insured, the definition of an insurance contract for both classes of insurance business is similar.

For completeness, it is noteworthy that Section 16 of the Financial Services Act 2013 (which has been passed but not yet in force) provides that a licensed insurer may not carry on both life insurance business and general insurance business.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

The similar characteristic shared between an insurance contract and a contract of gambling and chance (also called a 'contract of wager') is that both contracts are dependent upon the happening or occurrence of an uncertain event.

Nevertheless, contracts of wager are void by virtue of Section 31(1) of the Contracts Act 1950. The distinguishing feature between a genuine insurance contract and a contract of wager is that the latter is usually where the person insuring does not have an insurable interest in the property/subject matter insured.

ii) Warranty, guaranty or any other surety contracts

Like insurance contracts, warranties, guarantees and other surety contracts are generally also contracts of indemnity. However, this is where the similarities end. Insurance contracts may be distinguished from warranties, guarantees and other surety contracts on the basis that:

a) guarantees are discharged by any compromise between creditor and debtor and are not subject to the doctrine of good faith. The distinction has been emphasized in *The Zuhal K [1987] 1 Lloyd's Rep. 151* per Sheen J.:

"Contracts of guaranty are between persons who are in positions of creditor, debtor and surety. The surety assumes the obligation to make good the default of the principal debtor either for a fee or even without a fee from motives of friendship towards the debtor. There is not usually any bargaining between the guarantor and the creditor; nor is there a payment made by the creditor. On the other hand an insurer engages to pay a loss incurred by the insured in the event of a certain contingency occurring";

b) moreover, insurance contracts are construed strictly in favor of cover (see *Youell v Bland Welch & Co Ltd [1992] 2 Lloyd's Rep 127*) as opposed to guarantees which are construed strictly against the creditor (see *Blest v Brown (1862) 4 De G F & J 367*).

iii) Financial contracts such as hedging contracts/swaps/derivatives

The similarity between financial contracts and insurance contracts generally is the uncertainty of the occurrence/ happening of an event. However, financial contracts are distinct from insurance contracts as is implicit under Section 7 of the IA 1996 which prohibits certain annuity or investment-linked insurance business. Moreover, financial contracts are not subject to the requirement of utmost good faith as in insurance contracts.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

No such exceptions or exemptions exist under Malaysian law.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

n/a (see answer to Question 9 above)

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Insurance business may not be conducted unless it is undertaken by a licensed insurer (see Section 9(1) IA 1996). The license to conduct insurance business is granted and supervised by Bank Negara Malaysia, i.e. the national bank. An individual is only permitted to insure property or liability with an insurer if it is a licensed general insurer (see Section 140 IA 1996).

12. What are the legal consequences for the risk-taker acting without license?

Any risk taker or person who carries on insurance business without a license may be subject to criminal penalties set out under Section 9(1) IA 1996 as follows:

- Insurer – Imprisonment for ten years or MYR 10,000,000 or both.
- Insurance broker – Imprisonment for three years, MYR 3,000, or both.
- Adjuster – Imprisonment for one year or MYR 1,000,000 or both.
- Financial adviser – Imprisonment for two years, MYR 2,000,000, or both.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

The prohibition of licensed insurance companies from entering into non-insurance business is provided for under Section 28 of IA 1996 where it states that:

> "(1) Except with the prior written approval of the Bank, a licensee shall not carry on any activity in or outside Malaysia, otherwise than in connection with or for the purposes of its licensed business."

"Licensed business" for this purpose is defined under Section 2 of the Act as "insurance business, insurance broking business, adjusting business or financial advisory business" whilst the scope of "insurance business" is outlined in Section 4 of the Act as including life business, general business and reinsurance of liabilities.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

The terms and conditions of insurance contracts need not be submitted as a formal requirement nor do they have to be approved. However, pursuant to Section 149(1) IA 1996, a licensed insurer shall submit the proposal form and policy for the time being in use or to be used by the insurer once written notice is received which is required by the bank. Thus, the regulator, i.e. Bank Negara Malaysia, retains overall supervisory jurisdiction and licensed insurers may be required to submit the terms and conditions as and when the Bank deems fit.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Pursuant to Section 140 of IA 1996, no person shall insure or cause to be insured property or liability with an unlicensed insurer except with the prior written approval of the Bank. A person who is unlicensed is prohibited from carrying on insurance business under Section 9 of IA 1996.

As such, a contract of insurance issued by a non-licensed party is illegal and void ab initio both under Section 24 of the Contracts Act 1950 and the common law, i.e. 'ex turpi cause non oritur actio' (from a dishonorable cause an action does not arise).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

These are, inter alia, the Insurance Act 1996, the Insurance Regulations 1996, the Contracts Act 1950, the English Life Assurance Act 1774 and the English Marine Insurance Act 1906.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

An Insurance contract, like any other contract, is governed under the Contracts Act 1950 and its basic elements are offer, acceptance, consideration, the intention to create legal relations and the legal capacity to enter into a contract. It is formed when there is unconditional acceptance of the offer (*Borhanuddin bin Haji Jantara v American International Assurance Co Ltd. [1987] 1 MLJ 22*).

An insurance contract commonly takes the form of an insurance policy which includes a cover note (*Chop Eng Thye Co v Malaysia National Insurance Sdn Bhd [1977] 1MLJ 161*). Nothing in the Insurance Act 1996 provides for the formalities in constituting an insurance contract, which can be formed orally or be partly oral and partly in writing, except for a marine insurance contract under the English Marine Insurance Act 1906.

The required content of an insurance contract is outlined in Regulation 44 of the Insurance Regulation 1996 which includes the following:

i) name of policy owner;

ii) address of policy owner;

iii) policy number, cover note number or certificate number;

iv) class of insurance;

v) subject matter of insurance;

vi) period of insurance;

vii) perils insured;

viii) sum insured; and

ix) gross premium.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

The existing provisions under the Insurance Act 1996 is consumer-friendly, as exemplified by provisions such as Section 147 IA 1996 (a licensed insurer shall not dispute liability due to misstatement of age) and Section 151 IA 1996 (the knowledge of an authorized person/agent of the licensed insurer shall be deemed to be the knowledge of the licensed insurer).

Bank Negara Malaysia, the regulator of the insurance industry, has also issued various guidelines to the insurance industry in Malaysia in recognition of the need to address unfair practices e.g. the *Guidelines on Unfair Practices in Insurance Business, BNM/RH/GL/003-6* (by prohibiting the insurer from engaging in any act or omission that constitutes an unfair practice in the business of insurance) and the *Guidelines on Claims Settlement Practices (Consolidated), BNM/RH/GL/003-9* (by setting timeframes for each stage of the claims process to ensure claims are processed within the time limit stipulated to avoid delays in the settlement of claims).

These Guidelines are subsidiary legislation, having legislative effect and force of law, hence require judges to take judicial notice of the Guidelines and the standards set thereby with regard to issues of fair dealing and fair treatment of consumers (see *Diana Chee Vun Hsai v Citibank Berhad [2009] 5 MLJ 643).*

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

English common law and equity apply under Malaysian insurance law by virtue of Section 3 of the Civil Law Act 1956 and English statutes (eg. Life Assurance Act 1774 and Marine Insurance Act 1906) likewise apply directly under Section 5 of the Civil Law Act 1956.

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

Article 7:925 paragraph 1 of the Dutch Civil Code ("DCC") defines an insurance contract. The legal requirements for an insurance contract are:

- a contract that includes:

i) an obligation that the insurer undertakes towards the other party to make one or more payments, which may also be payment in kind (Article 7:926 (1) DCC);

ii) an obligation of the policyholder to undertake to pay a premium;

iii) an uncertainty for the parties whether, when or up to what amount payment must be made, or even how long payment of the agreed payment of premium will last.

- Insurance has to be either an indemnity insurance or a benefit insurance. The essential difference between an indemnity insurance and a benefit insurance is that an indemnity insurance ("schadeverzekering", Article 7:944 DCC) covers the actual damage, whereas a benefit insurance ("sommenverzekering", Article 7:964 DCC) disburses a fixed payment in case of loss, regardless of the actual inflicted damage.

- Benefit insurances are permitted for insurance of a person (Art. 7:925 paragraph 2 DCC) and for insurance so designated by Regulation only.[1] Benefit insurances are nearly always life insurances. Life insurances are governed by Article 7:975 DCC. Specific types of life insurances are: life insurance on the condition of death, funeral expenses and benefits in kind, and savings-life insurances.[2]

2. **Does an insurance contract require an element of uncertainty? Please describe.**

Article 7:925 paragraph 1 DCC explicitly mentions uncertainty as a constitutive element. The element of uncertainty manifests itself in four dimensions: uncertainty as to whether the insurer ever owes payment, the moment payment would be owed, the amount of such payment and the duration of possible periodical payments.[3]

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

The legal definition does not specify transfer of risk as a prerequisite for an insurance contract. Whether it should be considered a legal requirement is debated among scholars.[4] As of yet, there is insufficient indication that transfer of risk has acquired the status of a separate legal requirement, but most scholars seem to agree that it may have value as a(n) (implied) distinctive feature of insurance contracts.

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?**

In indemnity insurance, the existence of a (future) insured interest seems implied by the definition of Article 7:944 paragraph 1 DCC, that describes an indemnity insurance as an insurance for loss of, or damage to, property which the insured could suffer.[5]

[1] At January 1, 2013 no Regulation applied: J.H. Wansink, N, van Tiggele-van der Velde, 'Burgerlijk Wetboek, Boek 7: bijzondere overeenkomsten, Titel 17, Section 1', in: J.H. Wansink, R.Ph. Elzas, J. Borgesius, *Tekst & Commentaar: Verzekeringsrecht*, (Deventer: Kluwer 2013), p. 69-70.

[2] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering,* (Deventer: Kluwer 2012), p. 533-535.

[3] J.H. Wansink, N, van Tiggele-van der Velde, 'Burgerlijk Wetboek, Boek 7: bijzondere overeenkomsten, Titel 17, afd. 1', in: J.H. Wansink, R.Ph. Elzas, J. Borgesius, *Tekst & Commentaar: Verzekeringsrecht*, (Deventer: Kluwer 2010), p. 2.

[4] B.M. Jonk-van Wijk, M. de Boer, 'Wanneer is er sprake van een verzekering?', *Tijdschrift voor Financieel Recht*, 2012/7-8, p. 243, also citing F.H.J. Mijnssen, Scheltema, *Algemeen deel van het schadeverzekeringsrecht*, Alphen aan den Rijn: Samsom 1998, 2010, p. 21.

[5] R. Zwitser, "Verzekerbaar belang in handelskoop", *Nederlands tijdschrift voor handelsrecht* 2013/3, p. 138.

Also, the indemnity principle of Article 7:960 DCC implies that an insured interest has to exist in order to receive payment, since insurance compensation may not place the insured in a clearly more advantageous position than before the realization of the insured risk. However, most Dutch scholars agree that a tangible insured interest at the conclusion of the contract is not a prerequisite for an insurance contract to be valid.[6]

In benefit insurance, the former Dutch civil code specifically required an insured interest for the validity of the insurance contract. The present Dutch Civil Code does not stipulate such express requirement. Nonetheless, a material or idealistic (reasonable) interest in the insurance is still believed to be a prerequisite.[7] Case law has determined that if a benefit insurance lacks an insured interest at conclusion, the contract might still qualify for a (valid) contract of gaming or wagering.[8] In other situations the contract is void. [9]

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

As a default rule, an insurance contract covers only the interests of the insured (Article 7:946 (1) DCC). However, the insured interest may be attributed to a third party by designation of the third party as an insured or beneficiary in the insurance contract (Article 7:946 (1) DCC). It is also possible to attribute the insured interest to both the policyholder and a third party. Even if a third party is not explicitly mentioned as the beneficiary, a reasonable interpretation of the insurance contract can lead to the recognition of a third party as the beneficiary.[10]

There is a supplementary condition for third parties that wish to rely on indemnity insurances. The insured third party, or beneficiary, acquires a right to payment only by accepting his designation (Article 7:945 DCC).

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

Any natural or legal person can enter into an insurance contract that fulfills the criteria of Article 7:925 DCC. It is not required that the insurer mitigates his risk by assuming a larger number of similar risks. However, if a (legal or natural) person enters into multiple insurance contracts, this will soon qualify as conducting an insurance business. An insurance business requires a license and is supervised, which implies actuarial supervision as well. Subsequently, in practice, the 'law of the large numbers' will be relevant for insurers in a professional capacity.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

The general definition of an insurance contract does not differentiate between life and non-life insurance. A life assurance qualifies as a benefit insurance within the meaning of article 7:925 DCC. However, life assurance is also defined separately in article 7:975 DCC: "Life assurance is the benefit insurance taken out in connection with life or death, on the understanding that accident insurance is not considered to be life assurance."

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

A benefit insurance has a clear resemblance to a contract of gaming or wagering. Nevertheless, there are two essential differences.

[6] M.L. Hendrikse, H.J.G. van Huizen, J.G.J. Rinkes, *Verzekeringsrecht praktisch belicht*. Deventer: Kluwer, 2011, p. 360-362.

[7] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 554.

[8] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 556.

[9] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 556.

[10] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 335-336.

Firstly, an insurance contract covers an already existing risk and/or interest, irrespective of the contract. Contrarily, the conclusion of a contract of gaming or wagering actually creates the interest (risk of loss).[11]

Secondly, unlike contracts of gaming or wagering, the principle of legitimate expectations forms part of the character of insurance contracts. Insurance contracts are therefore 'uberrimae fidae', and contracts of gaming or wagering are not.[12]

Thirdly, the Betting and Gaming Act draws a distinction between life insurances and contracts of gaming or wagering by explicitly excluding valid life insurance contracts from the scope of the Act. However, benefit insurances without an insured interest can qualify as contracts of gaming or wagering according to case law based on the former Dutch Civil Code.[13]

ii) Warranty, guaranty or any other surety contracts

Dutch law does not recognize the Anglo-Saxon division of warranty and guaranty. A so-called contract of guaranty ("garantie-verbintenis") probably comes closest to warranty.[14] The guaranty provides security for property, just like indemnity insurance. In case the guarantor defaults, the guaranty has a fixed right to performance of the guaranteed standard, suspension of own performance, rescission of the contract and/or the right to damages.[15] Nonetheless, the difference with an insurance contract is that a guaranty generally serves to provide security against specified defaults of the guarantor or guaranteed product itself, whereas an insurance contract typically provides security for damage to property or a person by a larger range of agreed causes. Also, a guarantor is typically not entitled to periodical payments. Moreover, since the guarantor is generally responsible for the guaranteed performance, he is able to influence whether he will be indebted to the guaranty. Insurers, on the contrary, will mostly have little influence on the occurrence of the circumstances that trigger payment.

A contract of surety ("borgtocht") is based on Article 7:850 paragraph 1 DCC whereby one party (the surety) agrees with another party (the principal obligor) to perform the obligation of a third party (the obligee), if the obligee fails to perform his agreement with the principal obligor. The contract of surety guarantees the principal obligor's performance. He is therefore insured against possible non-performance of the obligee. In that sense the contract of surety may resemble a contract of insurance. However, the contract of surety always involves three parties. Also, the contract is dependent on the obligation of the obligee (Article 7:851 (1) DCC). If the obligee performs, the contract of surety seizes to exist.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Derivatives are financial instruments which value is dependent upon the value of another property right or object.[16] There are three types of derivates: "opties, termijncontracten en swaps", roughly taking the shape of options, hedges and swaps. Similarly to insurance contracts, they mitigate future insecurities and cover risk. However, whereas the above mentioned financial contracts are used to secure any devaluation of (publicly traded) capital, insurers may only compensate actual damages or pay fixed amounts in contractually defined events. Also, these financial contracts do not necessarily have to be subscribed to a natural or legal person by name, and can be exchanged freely at stock markets. Contrarily, although insurance contracts are generally interchangeable, the transfer of the insured rights involves a specified instrument, notification and permission of the insurer (Article 3:94 (1) DCC). It is possible that the right to transfer the insured right is excluded in the insurance policy.[17]

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

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[11] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 555-557.

[12] M.L. Hendrikse, H.J.G. van Huizen, J.G.J. Rinkes, *Verzekerin*

gsrecht praktisch belicht, Deventer: Kluwer, 2011, p. 6.

[13] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 556.

[14] R.D.J.L. Tjittes: 'Contracteren: Veelvoorkomende misverstanden bij het gebruik van Anglo-Amerikaanse termen in internationaal contracteren. *Tijdschrift voor de contractspraktijk* (2), 2008, p. 41.

[15] G.T. de Jong, in C.J.H. Brunner *et al.*, *Verbintenissenrecht algemeen*, derde druk, Deventer: Kluwer, 2011, p. 166.

[16] R.M. Wibier, 'Opties en andere derivaten in het vermogensrecht', in: S.E. Bartels, A.J. Verdaas, R.J. van der Weijden, *Effecten en vermogensrecht*, Deventer: Kluwer, 2011, p. 323.

[17] J.H. Wansink, N. Van Tiggele-van der Velde & F.R. Salomons, *Mr. C. Asser's Handleiding tot de beoefening van het Nederlands Burgerlijk Recht. 7. Bijzondere overeenkomsten. Deel IX. Verzekering.* Deventer: Kluwer 2012, p. 661-663.

Such an exemption applies to reinsurance contracts which, although they meet the criteria of insurance contracts, are exempted from the legal provisions applicable to insurance contracts in Title 17 of Book 7 (Article 7:927 DCC).

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

The Betting and Gaming Act draws a distinction between contracts of gaming or wagering and insurance, by explicitly excluding valid life insurance contracts from the scope of the Act (Article 2).

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

The legal provisions on insurance contracts do not set requirements for the capacity of an insurer. Any natural or legal person can therefore enter into an insurance contract without permission or a license. However, when a (natural or legal) person enters into multiple contracts as insurer, it will soon qualify as professional or corporate conduct within the meaning of Article 1:1 of the Financial Supervision Act ("FSA"). To conduct an insurance business, the law requires authorization of the Dutch Central Bank (Article 2:27 (1) and Article 2:48 FSA). Whether a license is required, therefore depends on the legal status of the insurer.

12. What are the legal consequences for the risk-taker acting without license?

Conducting an insurance business within the meaning of Article 1:1 FSA without a license qualifies as an criminal offence under Article 1 paragraph 2 of the Economic Offences Act (in conjunction with Articles 2:27 (1) and 2:48 (1) FSA). It is punishable by a custodial sentence (up to two years if the offence is committed intentionally; six months if not committed intentionally), community punishment or a fine up to EUR 19,500. Additionally, it may lead to seizure of profits or goods, temporary deprivation of rights, suspension of business, appointment of an administrator, publication of the court decision and obligations to right the misconduct and compensate (financial) consequences (Article 7 Economic Offences Act).

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Insurance companies are prohibited from conducting other businesses - including insurance business - than the type of insurance business they are licensed to provide (Article 3:36 (1) FSA). However, there are a few exceptions. Insurers may conduct commercial activities outside the insurance business, if those activities follow from their insurance business (Article 3:36 (2) (a) FSA), on the condition that no appreciable risk arises to the soundness of the insurer and the interests of the insured. According to the legal history of the Article, an insurer may for example give out mortgages or act as an intermediary for banking products. [We note that the legal history dates back to 2005 / 2006, before the credit crisis.] Moreover, life insurers that have a permission to conduct their business are allowed to conduct the business of funeral expenses and benefits in kind insurer without express permission. According to paragraph subSection b of paragraph 2, life insurers, funeral expenses and benefits in kind insurers, and non-life insurers are permitted to conduct reinsurance businesses without express permission, as long as so conducted within the respective area they are permitted to conduct their business in.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

No.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Insurance contracts concluded by non-licensed professionals or corporate parties are not rendered null ipso facto, and cannot, solely on that ground, be subject to annulment (Article 1:23 FSA). Since the contract is in principle valid, the policyholder can enforce the duties under the contract or claim compensation for breach of contract. In addition, an insurance undertaking convicted of contracting without an insurance may be ordered to perform under the insurance, to undo the illegal action or to right the misconduct otherwise and compensate the (financial) consequences thereof (Article 8 (c) of the Economic Offenses Act).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Title 17 of Book 7 of the Dutch Civil Code specifically regulates insurance contracts. Health insurances are additionally regulated in the Healthcare Insurance Act. Pension and saving funds are additionally regulated in the Pension and Saving Funds Act, the Sectoral Pension Funds (Obligatory Membership) Act 2000 and/or Occupational Pension Scheme (Obligatory Membership) Act.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Insurance contracts do not have a prescribed form - they may even be verbal. However, the law obliges the insurer to issue a signed document, i.e. the policy, in which the terms of the contract are confirmed, as soon as possible. There is an exception to this obligation if the nature of the contract justifies a different practice, or the policyholder has no interest in the issue of a policy (Article 7:932 DCC).

For the legal requirements for insurance contracts, please see question 1.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Part 3, title 5 of book 6 on General Terms and Conditions is applicable to insurance contracts. If the general terms and conditions are considered unreasonably onerous for the other party, or the user has not given the other party a reasonable opportunity to take note of them, the general terms and conditions may be subject to annulment by the other party (Article 6:233 DCC). These grounds for annulment may not be invoked by (reasonably) large corporations (Article 6:235 DCC). For consumers, natural persons not acting (in relation to) in a corporate or professional capacity, lists of provisions that are generally or presumably unreasonably onerous are provided by the law (Article 6:236 and 6:237 DCC).

The FSA and Market Conduct Supervision (Financial Institutions) Decree also set standards and requirements for expertise and reliability of insurance undertakings and financial and legal certainty of the insurance products. Also, insurance undertakings have to inform the potential policyholder about all costs, risks, obligations and rights and the general nature of the contract (Article 4:20 FSA and Articles 57 and 60 of the Market Conduct Supervision (Financial Institutions) Decree. The information requirements are strict and comprehensive. They partially depend on the type of insurance provided. Information requirements also exists during the course of the insurance (Article 4:20 FSA and 70 Market Conduct Supervision (Financial Institutions) Decree). Finally, insurance undertakings have a general duty of care towards their policyholders.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

The Insurance Act 2003, which is the law of Nigeria, does not define what an insurance contract is. The interpretation provision of the Act only says that "Insurance" includes "assurance". In a number of cases, the Nigerian courts have widely defined Insurance Contract as

> "contracts whereby one person called the insurer undertakes in return for the agreed consideration called the premium, to pay another person called the assured, a sum of money, or its equivalent, on the happening of a specified event". (See: Kayode v. Royal Exchange Assurance (1955-56) W.R.NL.R. 154).

2. Does an insurance contract require an element of uncertainty? Please describe.

From the above case law definition of Insurance Contracts, there must be an element of uncertainty. In the case of life assurance where death is certain, the time of death must remain uncertain before a business of insurance can be consummated.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Going by the judicial definition the insurer must assume the risk as being transferred and should not be based on the discretion of the insurer.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Under the Common Law principle and incorporated into Nigerian Statute no insurance contract is to be made on a life without an insurable interest (see Sections 56-58 of Insurance Act 2003).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Whilst it is essential that the insured interest attaches to the policyholder, the Nigerian regime allows a situation whereby, under the customary law and Islamic law, one person assumes responsibility for the maintenance and care of the other even though the relationship is not through blood line.

It also goes without saying that Compulsory Insurance Contracts are essentially meant to protect the third party, e.g. the third party motor vehicle insurance policy.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

In practice, insurers are allowed to reinsure part of their risks with a view to mitigating their risk. This is purely an actuarial issue and not necessarily a classification of insurance contracts.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

The general judicial definition of Insurance does not distinguish between a life and non-life Insurance save for the purposes of classification.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

The requirement of insurable interest which do not need to exist in gambling contracts makes gambling quite distinct from insurance even though there is an element of uncertainty in the two transactions.

ii) Warranty, guaranty or any other surety contracts

An insurance Contract is essentially a primary contract between two or more parties while a classical contract of warranty, guaranty or surety is a collateral or secondary contract between parties.

iii) Financial contracts such as hedging contracts/swaps/derivatives

The elements of direct premium and indemnity between the insured and the insurers distinguish an

insurance contract from a financial contract. The contracts of hedging, swaps and derivatives are entered into on behalf of subscribers, who may or may not know the products the funds are being invested in or the underlying assets the profit interests are paid from.

The other significant difference is the fact that profit taking (in form of interest and yield) is the essential element of investment in hedging, swap and derivatives, whereas the insurance contracts are based essentially on recompensation for a loss that may or may not happen.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

It is significant to note that regardless of the similarity in characteristics, insurers must be registered and be subject to the regulatory authority before such a transaction can be approved. (See: Sections 3 and 4 of the Insurance Act 2003). In other-words, a performance bond issued by an insurer may be treated as a contract of insurance whereas a bank guaranty given by a commercial bank may be viewed as banking product rather than an insurance product issued by a bank even though the two contracts are similar in nature.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

As explained above, it is the institution issuing the product that matters, and not necessary the product that is being issued.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Yes.

12. What are the legal consequences for the risk-taker acting without license?

The contract will be illegal having regard to the combined effect of Sections 3, 4 and 85 of the Insurance Act 2003.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

There seem to be a subtle prohibition if one goes by the general principle of the law. In practice however, such non-insurance business is usually done through a subsidiary company. In the same vein, Section 16 of Insurance Act requires insurers to obtain prior approval of the regulatory authority before a new product is introduced into the market.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Section 7 (g) of the NAICOM Act requires the regulatory Commission to approve standards, conditions and warranties applicable to all classes of insurance business.

Apart from the above industry standard setting, it is not generally required that individual terms and conditions of insurance contracts need to be submitted to the regulatory authority except in a situation of foreign reinsurance where the local insurer has to justify non availability of capacity of local companies in terms of size and complexity.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

If it is proved that the insurer is not licensed, such a contract can be avoided for lack of capacity and/or on the principle of illegality.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

i) Section 6 (1) (d) of the Insurance Act 2003 provides that the regulatory authority must ensure that the proposal forms, terms and conditions or policies are satisfactory and acceptable before registering insurers;

ii) Section 16 of the Insurance Act 2003 also requires a prior approval of insurance products before being introduced to the insuring public;

iii) National Insurance Commission Act 1969 (otherwise known as NAICOM Act);

iv) Nigerian Council of Registered Insurance Brokers Act 2003;

v) Motor Vehicles (Third Party Insurance) Act 1950;

vi) Third Parties (Rights Against Insurers) Act 1956;

vii) Marine Insurance Act, Cap M2 LFN 2004;

viii) S. 50 of Nigeria Oil & Gas Industry Content Development Act, 2010 which restricts the placement of offshore insurance without the approval of the regulatory body.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

There is no statute that contains specific provision for all the requirements of an insurance contract. S. 54 of Insurance Act, however mandates that the proposal form or application for insurance must be drawn up in such a manner as to elicit such information as the insurer considers material before accepting the application for the insurance risk and any information not specifically requested shall be deemed not to be material.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

i) Section 15 specifies a maximum of 60 days whence the insurance policy or contract must be delivered to the insured after the payment of premium;

ii) Section 55 of Insurance Act provides some kind of comfort to the insured in the sense that the insurer cannot avoid a contract of insurance unless the breach of term, whether a warranty or a condition, is material and relevant to the risk or loss insured;

iii) Section 78 of the Insurance Act establishes a security fund where the insured or third party beneficiary of the insurance claim could be paid in the event the insurer is insolvent or the regulatory authority has cancelled its license.

In the same vein, where there is a breach of a term of an insurance, the insurer shall not be entitled to repudiate the whole or any part of the contract or claim on the grounds of the breach unless:

i) The breach amount to fraud; or

ii) It is a breach of fundamental term of the contract;

iii) One of the statutory functions of the regulatory Commission is to protect insurance policyholders and beneficiaries and third parties to insurance contracts. (See Section 7 (h) of NAICOM Act, 1969.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Generally, the nature of contract of insurance conforms to Common Law principles for the formation of contracts.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

The definition of the insurance contract has been provided for in article 805 § 1 of the Act of 23 April 1964 – the Civil Code (Journal of Laws of 1964, No. 16, item 93, as amended) ("Polish Civil Code"). According to the above-mentioned provision, by insurance contract, the insurer, within the scope of activity of its enterprise, commits to the specified performance (benefit) in the case of the occurrence of the accident envisaged in the contract, and the policyholder commits to pay the premium. Insurance contracts are regulated under the Polish Civil Code in the provisions of articles 805 to 834. It should be noted, however, that those provisions do not constitute a comprehensive and full regulation of this matter. Regulations on the content of insurance contracts are also provided in other legal acts, e.g. in the Act of 22 May 2003 on Insurance Activity (unified text, Journal of Laws of 2010, No 11, item 66, as amended) ("Insurance Activity Act").

The contract may be qualified as an insurance contract provided that it meets the specific criteria determined in the Polish Civil Code and other legal acts. Firstly, the insurance contract must be concluded between an insurance company and a policyholder. The main obligation of the insurance company regards the coverage of the envisaged accident in the contract with a benefit. The policyholder is liable for the payment of the insurance premium. The provisions of the law provide for a specific regulation of the content of the insurance contract. For further details please refer to item 17 below.

2. Does an insurance contract require an element of uncertainty? Please describe.

According to the Polish regulations on insurance contracts the element of uncertainty relates to the occurrence of the insured event. Provisions of Polish law do not provide for detailed characteristics of the insured event, the occurrence of which is subject-matter of the specified insurance contract. Applicable regulations only provide that the accident must be specified in the insurance contract. Moreover, the accident should be random and possible to occur in the future (article 805 § 1 and 806 of the Polish Civil Code).

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

The economic literature defines insurance as a method of protection against the effects of a fortuitous event, involving a transfer of risk to the institution providing insurance cover. Although, the definition of an insurance contract is provided for in the Polish Civil Code, it does not directly mention the transfer of risk; in every insurance relationship the insurance company underwrites a given risk.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

According to certain representatives of the legal doctrine, the insured interest is one of the so-called essentialia negotii (essential elements) of an insurance contract. It shall be outlined however, that legal regulations do not provide directly for the requirement to demonstrate existence of the insured interest in order to effectively conclude an insurance contract. However, in relation to non-life insurance, Article 821 of the Polish Civil Code provides that

> "Property insurance may cover any property interest which is not unlawful and which may be assessed in money."

The insured interest is mainly the legal concept developed by the representatives of the doctrine of insurance law. The issue is more complicated, as insurance interest shall be defined in a different way in case of life and non-life insurance. Also, in case of group insurance contracts, the insurance interest has a specific meaning.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

As stated above, the legal regulations do not provide for any definition of the insured interest (except for the above-cited Article 821 of the Polish Civil code) and it is mainly the concept of legal doctrine. Accordingly, it is difficult to provide any specific answer.

For the purpose of providing an exemplary opinion, some representatives of the legal doctrine state that the insured interest is the value, which can be expressed in money that may be lost by the policyholder. In an insurance contract concluded on the account of a third party, value may be lost not by the policyholder but by the insured. It is not likely that the insurance interest could be attached to any other

entity, not being a policyholder, an insured or a beneficiary.

We would like to draw your attention to the fact that the analyzed concept is disputed among the representatives of the legal doctrine. The above-mentioned view is only one of many possible opinions. As it was mentioned above, this issue is not directly regulated in the respective provisions of law. Thus, it seems that it is not possible to indicate, which opinion of the legal doctrine representatives is the most accurate.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The above question is rather an actuarial than a legal issue. Naturally, each insurance company concludes insurance contracts on a large scale, as this is the main way of splitting the risk and making the insurance activity profitable. As far as legal regulations are concerned, it is sufficient if an insurance company is a party to only one insurance contract.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

In principle, the Polish Civil Law provides for a general definition of an insurance contract indicated in the answer 1 above. Generally, the Polish Civil Code does not provide for a separate complex definition for life and non-life insurance contract. The main difference in this regard relates to the benefit which should be paid out by the insurer:

i) in property (non-life) insurance – specific compensation for the damage caused by an accident in the contract;

ii) in personal insurance (including life insurance) – agreed sum of money, annuity or other benefits in case of occurrence of specific event in life of the insured person (in particular death, accident, reaching certain age).

Apart from the definition and regulations of a general character, the provisions of Polish law provide for a specific regulation of personal and property insurance contracts.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

The Polish Gambling Law Act states that a game of chance means a game played for prize where the prize can be cash or article prize and where the outcome of the game is conditional on chance and the conditions of the game are prescribed by game regulations. The Gambling Law Act also provides for the list of specific games of chance.

It seems that it is very difficult to provide any comparison of the game of chance and an insurance contract, as the legal construction and the nature of these relationships is entirely different.

The legal doctrine provides in a certain context a comparison of gambling/game of chance (in general, without reference to current regulations of Gambling Law Act) and an insurance contract. According to certain legal doctrine representatives, the main differences relate to:

a) their function;

b) the interest of the party in materialization of the particular event;

c) the economic purpose related with the amount of the possible damages/prize.

Please be advised however, that the above list is only of an exemplary character.

ii) Warranty, guaranty or any other surety contracts

In principle, in the Polish legal system the insurers are entitled to issue insurance guaranties in order to secure the economic interest of the beneficiary. As the Polish law does not provide for any specific regulations on insurance guaranty, its content and mechanisms are mainly a result of market practice and legal doctrine's view. This is the reason why it is difficult to determine the legal differences between the insurance guaranties and insurance contracts.

The Insurance Activity Act provides that the conclusion of contracts of insurance guaranty is a type of insurance activity. However, the above does not mean that the insurance guaranty is a type of insurance contract. Some legal doctrine representatives claim that the insurance guaranty should not be regarded as a type of insurance contract and should be rather deemed as an undefined type of contract.

iii) Financial contracts such as hedging contracts/swaps/derivatives

In principle, there are no complex regulations on the content of such contracts/financial instruments in the provisions of the Polish law that could be subject to comparison with the provisions on the insurance contract. The content of such contracts/financial

instruments is mostly a result of the market practice. In addition, there are many different forms of the above contract/financial instruments available on the market. According to the opinion of some legal doctrine representatives, in some cases the function of the above contracts/financial instruments relates with the intention of the investor to mitigate the risk connected with its activity. However, it seems that except for this surficial similarity, the legal structure and mechanisms of insurance contracts and the above-mentioned contracts/financial instruments do not have any other important similarities.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Polish law does not provide for any specific regulations in this respect.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

n/a

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

According to the Insurance Activity Act, the insurance activity can only be conducted by insurance companies, which possess the relevant license issued by Polish Financial Supervision Authority (Komisja Nadzoru Finansowego – "KNF"). The Insurance Activity Act provides for two types of insurance activity: life (branch I) and non-life insurance (branch II). A life insurance company cannot conduct non-life insurance activity and vice versa. The license can be issued for all groups of insurance related to a given branch or only to a part of them, subject to the request of the founder of the insurance company.

The Insurance Activity Act specifies that the insurance activity shall be understood as insurance acts performed in connection with insurance cover offered and provided against the risk of occurrence of the effects of chance events. Acts of insurance are inter alia entering into insurance contracts, insurance guaranty contracts or commissioning authorized insurance intermediaries to enter into the same, likewise performing the same. Also the Polish Civil Code states that

> "by a contract of insurance *the insurer, within the scope of activity of its enterprise*, shall assume the obligation to effect the specified performance in case of the occurrence of the accident envisaged in the contract, and the policyholder shall assume the obligation to pay the premium".

Specific regulations relate to insurance companies form the EU Member States, which conduct insurance activity in Poland on the basis of freedom of services or freedom of establishment within the EU. Such companies do not require a separate license to conduct insurance activity in Poland, but are obliged to notify the KNF (through their domestic regulator) of their intention to conduct such activity.

12. What are the legal consequences for the risk-taker acting without license?

The Insurance Activity Act provides for penal sanctions in respect of unauthorized performance of insurance acts. These regulations state that "Whoever performs insurance acts or pursues reinsurance activity without the required permit shall be liable to a fine, a penalty of restriction of liberty or deprivation of liberty of up to 2 years". The same sanction applies also to natural persons acting on behalf of a legal person.

In case where the insurance company concludes insurance contracts not included in the scope of its insurance license, also the supervisory measures can be imposed by the KNF. The KNF may inter alia impose a financial penalty on the members of the management board of the insurance company, impose financial penalty on the insurance company, suspend the performance of duties by members of the management board, apply to a competent body of the insurance company for a recall of a member of the management board or recall of a procuration granted. The KNF may also withdraw, by decision, the license to pursue insurance activity in respect of one or more groups of insurance.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, the Insurance Activity Act directly states that an insurance company cannot perform any activity other than insurance activity and an activity directly related thereto (there are minor exceptions described below). Insurance activity is defined by enlisting the activities, which are treated as insurance acts within the meaning of the Insurance Activity Act. There is no definition of activities "directly related to insurance activity". The Insurance Activity Act provides for few exceptions from the above general prohibition, stating that apart from insurance activity, the insurance company can:

i) perform reinsurance activity (provided that it is properly licensed to conduct such activity);

ii) mediate in the name and for the benefit of subjects performing banking operations (as specified in the Polish Banking Law), when entering into contracts within the scope of performing those acts;

iii) mediate in the transfer and repurchase of participation units of investment funds or participation titles in foreign funds, open-end investment funds with their seats in EU Member States and open-end investment funds with their seats in OECD Member countries not being EU Members States on the basis laid down in the Act on Investment Funds;

iv) perform services connected with the securing of the documents connected with the entering into and carrying out insurance contracts.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

In principle there is no general obligation to submit the GTC to the supervisory authority in order to formally implement them on the market. The Act on pension and insurance supervision and on Insurance Ombudsman provides for the obligation for insurance company to submit the GTC within 14 days from the day of its placing on the market to the Insurance Ombudsman. However, failure to comply with this obligation will not result in invalidity of the GTC.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

As stated above, the insurance activity may be performed only by an insurance company on the basis of a license granted by the supervision authority (KNF). The Insurance Activity Act indicates that the conclusion of insurance contracts is an insurance activity. That means that an insurance contract may not be concluded by a non-licensed entity. Also the Civil Code directly states that by insurance contract, the insurer, within the scope of activity of its enterprise, commits to the specified performance (benefit) in the case of the occurrence of the accident envisaged in the contract.

As regards contracts concluded by non-licensed entities, the legal doctrine indicates that any insurance contracts concluded by such entities should be declared as null and void, due to the fact that such contracts would be contrary to binding provisions of the law. The parties to such contract are not assigned with any rights or obligations from such agreement. This includes the claim of the non-licensed entity concerning the payment of the insurance premium by the policyholder, or the claim of the latter concerning the payment of insurance benefit. This does not exclude other types of contractual liabilities if the contract concluded can be treated as a different type of a contract, such as a guaranty or any other kind of obligation.

However, there may be also cases where a non-licensed entity concludes the insurance contract with a Polish entity without any active presence in Poland (e.g. the contract is concluded via insurance broker with a foreign insurer). In such cases the Polish law does not provide for a clear answer as to whether such contracts are admissible and valid. Such cases should be analyzed case be case taking all relevant circumstances, such as the place of concluding the contract and the applicable law, into account.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

The general provisions on insurance contracts are stipulated in the Polish Civil Code. This regulation also provides for a specific regulation concerning personal and property insurance contract.

Some specific provisions are stipulated in other legal acts. As an example, the elements that should be covered by the general terms and conditions or life insurance contracts are stipulated in the Insurance Activity Act.

As regards mandatory insurance, there are numerous legal acts, which provide for specific regulations regarding the conditions of such contracts. Such regulations are usually not extensive (e.g. minimum guaranty sum), however, they somehow influence the content of the insurance contract.

Statutory laws regarding insurance contracts or insurance activity are also included in various legal acts, including tax and accountancy acts.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

The legal provisions on insurance contracts do not provide any requirement for the form of the insurance contract. The law only requires that the conclusion of an insurance contract should be confirmed by a document, usually a policy. This, however, does not require a written form. The law does not indicate the requirements towards the content of the policy, except for the policies issued by foreign insurers conducting activity on the territory of Poland through Freedom of Services or Freedom of Establishment.

As regards the content of an insurance contract, the legal regulations are more complex. The conditions of the particular insurance product are in most cases stipulated in a standard form, i.e. general terms and conditions of insurance ("**GTC**"). The Insurance

Activity Act provides for a catalogue of items, which should be covered by the GTC:

i) the type and subject of insurance;

ii) the conditions for changing the sum insured or the sum guaranteed, if general insurance conditions provide for such change;

iii) rights and obligations of each of the parties to the insurance contract;

iv) the scope of liability of the insurance company;

v) for property insurance, the method of measuring the size of damage;

vi) the method of establishing the amount of damages or another benefit, if general insurance conditions provide for derogation from general rules;

vii) the method of establishment and payment of the insurance premium;

viii) the method and manner of premium indexation, if the general insurance conditions provide for such indexation;

ix) the procedure and conditions of amending an insurance contract concluded for an indefinite period;

x) the circumstances and time-limits of termination of the contract by each of the parties, as well as the procedure and conditions of the termination, if the general insurance conditions provide for such termination.

The Insurance Activity Act provides also for specific regulations on the content of life insurance contracts and unit-linked products. As regards life insurance products, the insurance company is obliged to include in the insurance contract:

i) the definition of individual benefits;

ii) the amount of premiums corresponding to individual basic and additional benefits;

iii) rules for the determination of benefits due under the contract, in particular the manner of calculating and granting bonuses, discounts and the share in the insured's profits, determining the technical rate, indicating the surrender value and the sum insured in the event of changing the insurance contract to a paid-up one, provided they are guaranteed, determining the costs and other charges levied by the insurance company at the payment of benefits;

iv) a description of these factors in the methods of calculation of the technical provisions that may influence a change in the amount of the benefit from the insurance company;

v) the indication of provisions which regulate the taxation of benefits from insurance the company.

In case of unit-linked products, the insurance company is obliged to specify or include the following in insurance contracts:

i) the list of unit-linked insurance funds offered;

ii) the rules for the determination of benefits and surrender value, including the rules for the redemption of units of the unit-linked insurance fund and the time-limits for their exchange for cash, and payment of benefits;

iii) the rules for investing the assets of the unit-linked insurance fund, which include in particular the profile of assets being part of such fund, the criteria of assets selection and the principles of their diversification and other investment restrictions;

iv) the rules and time-limits for valuation of the units of unit-linked insurance fund;

v) the rules for the determination of the amount of costs and all other charges deducted from insurance premiums or from unit-linked insurance funds;

vi) the rules for the allocation of insurance premiums to units of unit-linked insurance funds, in particular in the scope specified in items (iv) and (v) above, and the time-limit for converting premiums into units of such fund.

It should be also taken into account that certain provisions of the Polish Civil Code will apply to all insurance contracts, even if the parties regulate certain issues otherwise in the insurance contract of the general terms and conditions. E.g. if the parties regulate in the insurance contract that the benefit will be paid by the insurer within 60 days, such provision will not be binding, since the Polish Civil Code provides that the standard period, when the insurer is obliged to pay the benefit, cannot be longer than 30 days, unless payment is not possible due to certain objective reasons (e.g. lack of necessary documentation).

18. <u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>

Yes, the Polish regulations provide for a consumer protection with respect to insurance contracts.

According to the Polish Civil Code, the regulations concerning the consumer protection of the persons concluding a contract with a standard form should *apply to the concluded* insurance contracts. The above-mentioned provisions stipulate that provisions of a contract concluded with a consumer, which have not been individually agreed with him, should not be

binding thereupon, if his rights and duties have been stipulated in conflict with good customs and in flagrant violation of his interest (wrongful contractual provisions). The Polish Civil Code provides also for an exemplary catalogue of wrongful contractual provisions. The particular contract provisions are declared as a wrongful contractual provision by a court and are subsequently published in the Register of Wrongful Contractual Provisions maintained by the President of the Competition and Consumer Protection Office. Further to the Polish Civil Code, the consumer shall be deemed to be any natural person who performs acts in law which are not directly connected with his economic or professional activity.

The above rule applies also to the insurance contracts concluded on another person's account (where policyholder and insured are not the same person) to the extent to which the contract refers to the rights and duties of the insured.

The consumer protection related with insurance contracts derives in some cases also from the regulations on practices infringing collective consumer interests and unfair commercial practices. Depending on the case (e.g. in case of distributing insurance via the Internet, on-line) also additional obligations aimed at protection of the consumer may apply.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

We believe that most important issues have been addressed above.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

The definition of an insurance contract is set out in Section 1 of the Spanish Insurance Contract Act 1980 (ICA). It provides that through the insurance contract the insurer undertakes the responsibility to indemnify, within the limits agreed, against the risks of uncertain damaging events befalling the insured or to pay a certain capital, an annuity or other obligations as agreed, in exchange for a premium. Case law has described an insurance contract as a commercial contract, consensual, bilateral, onerous and aleatory (Decision of the Supreme Court of 27 November 1991, RJ 1991\8496).

The essential elements of an insurance contract are risk, the insurable interest and the indemnity principle in casualty insurance.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. The risk is by definition a future and uncertain event, the materialization of which depends on chance. The risk is a fundamental element of the insurance contract to the point that, generally speaking, the insurance contract is null and void if at conclusion there was no risk or the loss had occurred (Section 4, ICA).

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Insurable interest is another fundamental element of the insurance contract. The insured or policyholder must have an insurable interest with the subject-matter of the insurance at the moment of conclusion of the contract. Section 25 of ICA makes void all casualty insurance contracts in which there is no interest of the insured upon the conclusion of the contract to the indemnification of the loss.

Legal doctrine and case law have clarified that the insurable interest must also exist during the life of the contract and at the time of the loss (Ley de Contrato de Seguro, dir. Fernando Sánchez Calero, Editorial Aranzadi, 2010, page 602 and Decisions of the Supreme Court of 31 January 2005 [RJ 2005\1078], and 23 March 2006 [RJ\2006\6292]).

In addition, Spanish doctrine and case law have declared that the basis of the indemnity principle is in fact the existence of an interest, since there can be no loss without an interest (Sánchez Calero, Op cit, page 613, and Decision of the Supreme Court of 7 October 1986 [RJ\1986\5331]).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Under Section 7 of ICA, the policyholder can take the insurance for his account or for the account of a third party- Where the policyholder acts for his account, he would have the dual position of the policyholder and insured, whilst in the second case –where he acts for the account of a third party- he would only be the policyholder.

The rights arising out of the contract, namely the right to collect the indemnity from the insurer, will pertain to the insured or, as the case may be, the beneficiary (Section 7, ICA). This provision is included in the general part of the ICA, so in principle it would apply to all types of insurances, either casualty (indemnity) or personal (namely, life). In a contract of indemnity, it is the insured who has the insurable interest and is entitled to receive the indemnity from the insurer precisely as a consequence of the loss sustained in such interest. In fact, Section 8.2 of ICA requires that the holder of the insurable interest is specified in the contract and this is the insured. In contracts of indemnity, precisely in virtue of the indemnity principle, it is argued that, as a general rule, it would not be possible to appoint a beneficiary other than the insured simply because the beneficiary does not have an insurable interest which entitles him to receive the indemnity.

The beneficiary has a proper function in personal insurance, namely life, in which an economic interest is not required as in the contract of indemnity.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The insurance industry is able to calculate their estimated losses based on previous statistics and applying to its data the law of large numbers. These calculations are part of the actuarial technique.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

The ICA distinguishes between casualty insurance and personal insurance and establishes general and particular provisions for each type of insurance.

Under the ICA, the main difference between personal insurance (namely, life, accidents and health) and casualty insurance (fire, theft, surety, credit, civil liability, among others) is the different nature of the obligation assumed by the insurer. Pursuant the Section 1 of ICA, the obligation assumed by the insurer can be expressed in two different ways: the obligation to indemnify, or to pay a certain capital, an annuity or other obligations as agreed. The latter is used in the ICA when referred to personal insurance.

As a general rule, in personal insurance, the insurance cannot have an indemnity function, but only as providing the agreed financial benefits, since in personal insurance an insurable interest is not required as it is in casualty insurance.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Both insurance contracts and gambling contracts are aleatory. However, while in gambling the risk of loss is created by the bettor, insurance is intended to indemnify the insured in respect of the risk of loss to an interest he already possessed. Consequently, based on that principle, Section 25 of ICA makes void all casualty insurance contracts in which there is no interest by the insured in the indemnification of the loss upon the conclusion of the contract.

ii) Warranty, guaranty or any other surety contracts

Under Spanish law, by the guaranty, the guarantor undertakes to perform the payment obligation of the debtor, if the latter fails to perform its obligation to the creditor (Section 1822 of the Spanish Civil Code).

Surety insurance is regulated in Section 68 of ICA, which provides that the insurer shall indemnify the creditor for loss suffered by the insured upon breach of the policyholder's legal or contractual obligations.

Spanish case law has made clear that surety and guaranty are two distinct contracts. The Supreme Court has declared that in surety contracts, unlike security contracts, the insurer does not undertake to perform the obligation of the main debtor, but to compensate the creditor for the damage (Decisions of the Supreme Court of 19 May 1990 [RJ 1990\3741], and 12 March 2003 [RJ 2003\2572]).

In addition, the guarantor's obligation under the guaranty is secondary to the primary obligation that the debtor has to the creditor under the underlying contract. On the contrary, an insurer's obligation is primary (Decision of the Supreme Court of 13 December, 2000 [RJ 2000\10438]).

iii) Financial contracts such as hedging contracts/swaps/derivatives

Both financial contracts such as credit default swaps (CDSs) and surety insurance are generally used to provide protection from the failures of debtors. Unlike the insurance contract, in the CDSs, the payment obligation of the seller is irrespective of whether the buyer (the payee of a fee or premium) of the CDS has suffered a loss. Further, CDSs are not intended to protect an insurable interest of the buyer, which is an essential principle under the ICA.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

No.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

No.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Yes. Under Section 5 of the Law for the Regulation and Supervision of Private Insurances 2004 (LRSPI), a person shall not conduct insurance activities in Spain unless authorized to do so.

An insurance company authorized by the Dirección General de Seguros y Fondos de Pensiones (Directorate General for Insurance and Pension Funds, DGIPF) is, as far as Spanish law is concerned, entitled to cover risks located anywhere in the world to the extent that this geographical scope would have been indicated in the program of activities and approved. Authorization to operate will be valid throughout the EEA (the so-called single passport).

Insurers based in the EEA who are duly authorized to write business in their countries will be entitled to carry out business in Spain under either the freedom of establishment regime (as a branch) or the freedom to provide services regime. Foreign insurers other than EEA companies are required to obtain an authorization from the Ministry for the Economy and Competitiveness if they wish to set up a branch in Spain.

12. What are the legal consequences for the risk-taker acting without license?

As stated, a person shall not conduct insurance activities in Spain unless authorized to do so (Section 5 of LRSPI). Breaching this requirement is considered a very serious infraction and punishable with the following relevant penalties: public advertising of the infraction; and/or a fine of one per cent of its capital (or between EUR 150,000 and EUR 300,000 if one per cent of capital is less than EUR 150,000).

Policies issued by non-authorized insurers are null and void by law. However, the effects can differ from the general civil rules on nullity of contracts: if no loss has occurred, the insured is not required to pay the agreed premium or has the right to recover any premium paid. However, if a loss which would otherwise have been covered had the policy been valid occurs before the premium is returned, the non-authorized insurer may keep the premium, but would be required to pay an indemnity the quantum of which would be determined in accordance with the void policy terms. The insured may also claim any other relevant damages sustained by reason of the void policy. Both the company and the directors or officers that permitted the policy to be issued shall be jointly and severally liable for those obligations.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Under Section 4.1 of the LRSPI, insurers are prohibited from carrying out the following transactions: those lacking a technical actuarial basis; any commercial activities other than those specific to the insurance business, unless they involve collaboration with non-insurance companies for the distribution of their services; and insurance mediation activities as defined in the Private Insurance and Reinsurance Mediation Act 2006.

LRSPI provides that the prohibited transactions are null and void by operation of the law.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Models of policies are neither subject to approval, nor have they to be submitted systematically to the DGIPF (Section 25, LRSIP). Nevertheless, models of compulsory insurance (third-party motor insurance, hunters, nuclear, auditors and arbitrators, amongst others) must be at the disposal of the DGIPF.

The DGIPF, however, has the power to request the presentation of the policies models at any time in order to check the fulfillment of applicable Spanish laws and to prohibit the use of a given policy wording if the wording breached the law. A special procedure is established for these purposes.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Please see our answer to Question 12.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes, the three most important statutes are the Insurance Contract Act 1980, the LRSPI and the Commerce Code concerning marine insurance.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Under the ICA, the insurance contract and any amendments or supplements must be formalized in writing whether on paper or other durable medium that enables it to be stored, easily retrieved and reproduced without changing the contract or the relevant information. Further, the insurer has the duty to hand out the insurance policy or at least a provisional document attesting coverage to the policyholder. This is for purposes of proof only.

Apart from certain information that the insurer must provide to the insured prior to entering into the contract, there are certain minimum content requirements for insurance contracts as set forth in Section 8 of ICA:

- Full names of the parties, and their domicile, as well as the named insured and beneficiary, as the case may be;
- If the policyholder purchases cover on his behalf or on behalf of another person (the insured);
- Nature of the risk covered;
- Designation, as the case may be, of the insured objects and their location;
- Insured sum or scope of cover;
- Amount of premium, surcharges and taxes;
- Maturity of premium, place and form of payment;
- Duration of contract, with indication of day and hour in which its effects begin and expire; and,

- Name of the agent intervening in the contract, if any.

Aside from contracts involving so called large risks where party autonomy operates fully, thus affording more flexibility, the conditions of the insurance contract must be clearly and precisely drafted, and signed by the insured (there are special rules for electronic contracts). Further, clauses which limit or restrict the rights of the insureds must be highlighted and written in bold letters, and explicitly accepted by the policyholder or insured (Section 3, ICA). Otherwise, the clause may be null and void. It is required to include a statement that the policyholder or insured has read the limitative clauses, if any, and agrees to them.

Extreme care should be taken when incorporating legal concepts and principles from other jurisdictions into Spanish policies. Such principles might mean little or nothing in Spain and, even worse, they can lead to misinterpretations.

See in this regard our answer to Question 18 below on Contracts Standard Conditions and consumers and users legislation.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Firstly, all the provisions of the ICA are mandatory in nature which means that the parties cannot depart from them, save that the law itself provides otherwise. However, clauses that benefit the insured shall be permissible and valid.

Further, pursuant to Section 60 of LRSPI, prior to entering into the contract, the insurer must provide to policyholder with the following information:

- The applicable law to the contract.
- The different channels, internal and external, available for claims related to the insurance contract and procedures.
- The Member State and the supervisory authority in charge of controlling the insurer's activity.
- Its registered address.

This information must be provided in the policy itself or in the cover note.

The Contracts Standard Conditions Act 1998 may apply both to consumers and non-consumers where all or part of the terms of the agreement are not negotiated individually and are intended to be incorporated into a plurality of contracts. This is particularly relevant for so called collective or group insurances.

The Act applies to those standard conditions included in contracts which are subject to Spanish law. It will also apply to contracts subject to a foreign law where the contracting party has bound itself in the Spanish territory and has its habitual residence in this territory.

For these conditions to be deemed valid, accepted and incorporated into the contract, the following requirements must be met:

- The drafter must inform the other party of the existence of such standard conditions and provide it with a copy of same.
- The party that adheres to the contract must accept the conditions explicitly; and
- The contract must make reference to the general conditions and be signed by the parties thereof.

In connection with these rules, it should be also noted that any doubts arising when interpreting these clauses shall be resolved in favor of the non-drafter, i.e., the law introduces the "contra proferentem" rule. This is a variation of the general interpretation rule which provides that the interpretation of obscure clauses should not favor the party that caused such obscurity, i.e., the drafter of the clause (Section 1288, Civil Code).

Further, under the consumers and users legislation, all unfair (abusive) terms are void (Restated Text of the Law for the Defence of Consumers and Users, 2007).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

The policyholder's duty of disclosure prior to the conclusion of the contract:

Under Article 10 of ICA, the policyholder is subject to the duty, prior to the conclusion of the contract, to disclose to the insurer, pursuant to the questionnaire submitted by the insurer, all the circumstances known by the policyholder that may be relevant for the evaluation of the risk. The policyholder will be relieved from said duty if the insurer does not submit a questionnaire or, submitting it, there are circumstances that may be relevant for the evaluation of the risk but are not covered in the questionnaire.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

No, there is no definition in Swedish statutory law with regard to an insurance contract. However, according to Swedish legislative preparatory works and Swedish legal literature the main characteristics of an insurance contract are the following: The contract must comprise a transfer of risk to the insurer from the insured where the insurer, in consideration of a premium, takes on the risk that a particular uncertain event (an insured event) occurs. If an insured event occurs, the insurer shall pay the insured a sum of money that has been determined in advance.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes, the event that the insurance is designed to cover must to some extent be uncertain. The element of uncertainty is therefore of importance to all forms of insurance. When such element is missing, e.g. when damage occurs with some frequency or is associated with a particular business and the cost is known, this is a factor that reduces the likelihood that the contract is to be considered an insurance contract.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes. The risk transferred to the risk-taker cannot be too minimal. The Swedish Supreme Administrative Court has ruled that a contract with a risk component of only 0.1 per cent of the value of the assets placed in a life insurance savings product (in Swedish referred to as a "capital insurance"), was too small for the contract to be considered an insurance contract under Swedish law. The ruling was neither affected by the fact that the risk-taker had labeled the contract a "capital insurance" contract nor by the fact that in the risk-taker's jurisdiction, such contracts were in fact considered insurance contracts. In another case, the Supreme Administrative Court held that a contract with a risk equivalent to one per cent of the value of the assets, qualified as an insurance contract.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Yes, if the insured party has no interest whatsoever in the subject matter of the contract, the contract will most likely not be considered insurance (see also regarding gambling, Section 8 (i) below). Further, this interest must be "lawful", which means that an insurance contract may not provide cover for e.g. criminal operations.

However, the insured interest does not have to be an interest of a financial kind. Under Swedish law, it is possible to obtain insurance for events that incur purely non-financial damage. An example is accident insurance covering personal injuries, where the insured is entitled to insurance compensation for pain and suffering that follow the accident.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

No, the insured interest does not have to be linked to the policyholder, and may be attributable to a third party.

This third party may be an "explicit" beneficiary under the insurance contract, meaning that the insurance contract stipulates that the third party shall be entitled to insurance compensation in case of an insured event occurring. This is the case e.g. where a company is the policyholder of a directors and officers liability insurance that provides cover for third parties, i.e. the directors and officers of the company.

Further, there may also be "implicit" beneficiaries that are entitled to insurance compensation based on certain rights or interests which the third party has in the insured property. The beneficiary is "implicit" since he/she may have a right to insurance compensation even if that right is not stipulated in the insurance contract. For example, under the Swedish Insurance Contract Act (the "ICA"), unless the parties to the insurance contract have agreed otherwise, an insurance contract which covers the value of real property or the value of fixed or personal property applies also to the benefit of (i) any third party which has a secured interest in the policyholder's protected ownership right, ground lease, or chattel mortgage, but not a maritime lien or aviation lien; and (ii) any third party who bears the risk for the property in connection with its transfer.

Under ICA, it is possible to pledge insurance for the policyholder's debt with the effect that any insurance compensation shall be paid by the insurer directly to the mortgagee.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

No, under Swedish law it is not necessary for an insurer to mitigate a particular risk by insuring a larger number of similar risks. The risk assumed may well be mitigated by the insurance of other types of risks, as long as the insurer holds technical reserves that equal the funds required to cover all reasonably expected claims that may occur under all the insurance contracts issued by that insurer.

However, it is normally relevant that a risk assumed by the insurer is mitigated by the simultaneous insurance of a larger number of similar risks, as this makes it easier for the insurer to predict claim outcome for that type of risk.

7. <u>Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?</u>

No, the definition does not differ between life and non-life insurance. In fact, there are insurance contracts that comprise both life and non-life components, e.g. payment protection insurance (PPI), which generally covers for example death, sickness (life) and unemployment (non-life).

Distinction from Similar Types of Contracts and Exemptions

8. <u>Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.</u>

i) Contracts of gambling and chance

Contracts of gambling and chance are not regarded as types of insurance contracts. When making a distinction between these types of contracts and insurance contracts, the purpose of the contract is of interest.

The purpose of an insurance contract is to provide cover for an insured interest, while the purpose of contracts of gambling and chance is to speculate in specific events occurring.

Parties of contracts of gambling and chance enter into the contract with the purpose of making money through speculation and neither party has an interest that needs to be protected by way of risk-transfer.

For example, a contract which pays one of the parties a sum of money in case it rains on a particular day, may either constitute an insurance contract or a contract of gambling depending on the purpose of the contract.

If the party receiving money under the contract in case it rains has organized an outdoor event on the day in question and the event has to be cancelled because of the rain, leading to that party having to compensate e.g. ticketholders, the contract may constitute an insurance contract in view of the insurable interest.

However, if the party receiving money in case it rains has no implicit interest whether it rains or not, but merely speculates that it will rain, the contract will likely be considered a contract for gambling.

Nonetheless, in some cases it is difficult to draw the line between contracts of gambling on the one hand and contracts of insurance on the other and there is no clear legal distinction between the two types of contract.

ii) Warranty, guaranty or any other surety contracts

Warranties and guarantees comprise most of the characteristics of an insurance contract. However, warranties normally include certain elements that distinguish them from insurance contracts. Warranties provided by a manufacturer of a certain product often cover damage which is relatively predictable, such as wear-out failure or defective material (please see Section 2 above in relation to the element of uncertainty). Furthermore, the guarantor's undertaking is often to restore the product to working order and not to pay monetary compensation.

Surety contracts such as bank guarantees also comprise most of the characteristics of an insurance contract, but are not considered insurance contracts under Swedish law.

An example of a warranty that comprise many of the characteristics of an insurance contract, but is not regarded as such under Swedish law, is the motor vehicle damage warranty (please see Section 9 below).

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts may generally be designed in a way which makes them very similar to insurance contracts, in particular hedging contracts and credit derivatives. The purpose of entering into such contracts may be equivalent to the purpose of entering into an insurance contract, i.e. mitigate/transfer a risk.

However, financial contracts can also be entered into purely with the purpose of speculation e.g. to speculate in the price fluctuation of a commodity, which differentiate such contracts from insurance contracts.

There are no clear legal definitions of these types of contracts and there is no case law to clarify the situation. Thus it may be difficult to distinguish these types of contracts from insurance contracts.

Ultimately, the question whether a contract should be considered a financial contract or an insurance contract may be decided by examining the parties that have entered into the contract. If the contract is entered into by an insurer, it is likely that it will be considered an insurance contract, whereas e.g. a

credit derivative might not be considered an insurance contract if one of the parties is a bank licensed to issue financial contracts.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

Yes, such exemption exists in relation to motor vehicle damage warranty, which is commonly used within the Swedish automotive market (originally introduced by Volvo). In addition to wear-out failure and defects in materials, the motor vehicle damage warranty covers more uncertain events, such as car damage due to accidents or vandalism, etc. The motor vehicle damage warranty is by design very similar to an insurance contract, but is still regarded by the Swedish legislature as a warranty. It has been stated in legislative preparatory works that the car manufacturer has the best opportunity to determine a balance between the car's quality and the risk of damage and defects. Thus, it has been considered appropriate that the car manufacturer is responsible for the warranty. It is these considerations that have been decisive in the design of the warranty, rather than the characteristics (such as risk calculation and assumption of risk etc.) typical in relation to insurance business. Further, the fact that the motor vehicle damage warranty follows the ownership of the car and not the person signing the warranty, is also relevant for the exemption being available. It has been stated that motor vehicle warranties provided by an operator who is independent from the vendor/car manufacturer are usually considered to be insurance contracts.

Re-insurance contracts are by definition considered to be insurance contracts and fall within the scope of the Swedish Insurance Business Act ("IBA") and the Solvency II-Directive, but outside the scope of ICA. Credit insurance is another type of contract that falls within the scope of IBA, but outside the scope of ICA. There are also categories of insurance that fall within the general definition, but outside the ICA as well as IBA. An example of the latter is social insurance provided by the government.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

Please see Section 9 above and the exemption in relation to the motor vehicle damage warranty.

Please note that contracts which pool risks within the same group of companies e.g. contracts entered into by a captive insurance company, are considered insurance contracts under Swedish law. Captive insurance companies need to be licensed to perform insurance business (see Section 11 below).

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Under IBA, a party that is to enter into insurance contracts as a risk-taker on a commercial scale may only do so if that party has obtained a license to perform insurance business. However, if a risk-taking party in a one-off situation and on a non-commercial scale enters into a contract that could be characterized as an insurance contract *per se*, it is probable that such an action would not constitute insurance business subject to license requirement.

A party that wishes to enter into a contract as a risk-taker may seek a preliminary ruling from the Swedish Financial Supervisory Authority (the "SFSA") on whether the planned operation constitutes insurance business.

Only limited liability companies, mutual insurance companies and insurance associations may be granted license to perform insurance business. Licenses to perform insurance business are issued by the SFSA.

12. What are the legal consequences for the risk-taker acting without license?

If a risk-taker performs insurance business without a license, the SFSA shall issue an order to the risk-taker to cease its operations. In this order the SFSA may resolve that the company or association be liquidated. The order may be combined with conditional fines.

If the risk-taker acting without a license is a company or association, a court shall, upon request from the SFSA, decide that the company or association is to be liquidated.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, under IBA, an insurance company may not carry on any other business than insurance business and business related thereto.

There is virtually no case law which sheds light on the scope of the prohibition. In practice, if an insurer is uncertain whether a planned operation is prohibited or not, the insurer may contact the SFSA for clarification.

An example of business related to insurance business is management of the assets of the insurance company. If an insurance company for example has invested some of its funds in real estate, the insurance company may manage the real estate assets and e.g. let property, invest in real estate development etc. This means that the scope of business related to insurance business in fact can be quite wide as long as it is within the scope of the insurance company's asset management.

14. Do the terms and conditions of insurance contracts need to be

i) **submitted to the regulator as a kind of formal requirement or**

ii) **approved by the regulator prior to entering into effect?**

Under Swedish law, an insurer's terms and conditions do not have to be neither submitted nor approved by the regulator. Thus, there are no formal requirements on how the terms and conditions of an insurance contract are to be drafted.

Nonetheless, insurance terms and conditions which, in comparison with mandatory provisions of ICA, are to the detriment of the policyholder or its assignee, or to the detriment of the insured, shall be without effect in respect of any such party. Most mandatory provisions of ICA are only applicable to consumer insurance, but there are also a few mandatory provisions with respect to non-consumer insurance.

Further, terms and conditions that in some respect are unreasonable in relation to the insured may be set aside by a court in legal proceedings between an insurer and an insured.

Also, the Swedish Market Court may find that insurance terms and conditions used by an insurer are inequitable against consumer. If the Market court finds terms and conditions to be inequitable, it may order the insurer to stop using such terms and conditions. This order may be combined with conditional fines. Typically, cases involving inequitable terms and conditions are brought to the Market Court by the Swedish Consumer Ombudsman (*Sw: Konsumentombudsmannen*), which is a governmental body with the purpose to safeguard consumer interests.

Impact of Qualification – Law of Contracts

15. **Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?**

An insurance contract is legally binding between the parties even though the insurer is a non-licensed party. However, the policyholder may be entitled to prematurely terminate the insurance contract if the "insurer" has operated without a license or if the insurance company's license has been withdrawn during the policy term. In the latter situation, the policyholder may also be entitled to claim damages.

The policyholder may terminate an insurance contract prior to the conclusion of the policy term, where the insurance company commits a material breach of its obligations pursuant to ICA or the insurance contract.

A material breach by an insurance company under other relevant legislation than ICA may also be considered a material breach of the insurance contract. Therefore, a breach of e.g. IBA (such as issuing insurance without a license) may in some cases constitute cause for termination of the insurance contract prior to the conclusion of the policy term. According to Swedish legal literature, such termination likely requires that the insured party shows that the insurer's actions have led to a substantial risk for harm or damage to the insured.

If the policyholder was aware that the "insurer" was operating without a license when the insurance contract was issued, the policyholder will most likely not be entitled to prematurely terminate the contract.

The policyholder is also entitled to terminate the insurance policy with immediate effect where the insurance company is no longer entitled to market and issue new insurance contracts relating to risks located in Sweden (either because the company never had a license or because a license has been revoked), unless the insurance company posts security for the fulfillment of the contract, immediately following a demand therefor.

If the insurance policy is terminated pursuant to said provision, the policyholder and other parties who suffer loss due to such termination are entitled to claim damages.

16. **Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.**

In Sweden, insurance contracts are mainly governed by ICA. The ICA comprises rules regarding insurance periods, renewal of insurance contracts, termination of insurance contracts, the insurer's duty to inform the policyholder, payment of premiums etc.

In addition, there are other statutes on specific insurance types such as motor vehicle liability insurance and insurance relating to construction errors. There are also provisions on insurance contracts in other fields of law, such as environmental legislation.

There are also provisions in the Swedish Income Tax Act, establishing the criteria for an insurance contract to constitute "pension insurance" (see Section 19 below).

Further, insurance contracts are regulated by Swedish general contract law.

17. **Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.**

Under Swedish law, there are no legal requirements with regard to the form of insurance contracts. However, there are some provisions governing the insurer's duty to inform the policyholders. Certain information must be presented to the insured in written form, in particular where the policyholder is a consumer (see Section 18 below).

There are mandatory provisions of ICA, which set out requirements with regard to content of insurance contracts issued to consumers. For example, the policy term of a non-life insurance contract shall not exceed one year, unless there are specific reasons for a longer policy term.

18. <u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>

Yes, under ICA an insurer is obliged to provide information to the customer prior to issuing the insurance. The information must aim at facilitating the customer's assessment of the insurance cover and choice of insurance. The information must, to the extent possible, be provided in a document or in another readable and durable form which is available to the customer. The information must be clear and unambiguous and written in Swedish. There are also SFSA regulations that specify how information must be provided. At the request of the customer, the information may be provided in another language. The pre-sale information shall, in a simple manner, set forth the principal contents of the insurance terms and conditions, which the customer needs to be aware of in order to assess the cost and scope of the insurance policy. Important limitations regarding the insurance coverage shall be set forth clearly.

Further, information about the terms and conditions must be provided to the insured once the insurance contract has been concluded.

19. <u>Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?</u>

In Sweden it is common to use group insurance when a defined group of people, e.g. members of an organization, wishes to obtain insurance for the same type of risks. Under Swedish law, group insurance can be divided into main two types; voluntary group insurance and mandatory group insurance. In voluntary group insurance, members of the group are free to affiliate themselves to the insurance giving each member an individual insurance policy, while mandatory insurance members are automatically insured under the same insurance policy.

The motor vehicle damage warranty described in Section 9 above is specific for Sweden and the exception has its basis in a Swedish Supreme Court ruling from the 1950's. The warranty comprises most of the characteristics of an insurance contract and it is plausible that if the warranty had been designed today it would be considered an insurance contract and not a warranty. However, the Supreme Court ruling still stands and motor vehicle damage warranties are therefore not considered insurance contracts.

It could also be of interest to know that in Sweden, it is common to use life insurance contracts as a way of saving for retirement. Such insurance contracts are called "pension insurance". Pension insurance can be provided under both employment schemes and private schemes.

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

There is no definition of an insurance contract in statutory law, neither in the Swiss Federal Act on Insurance Contracts ("ICA") nor in the Swiss Federal Act on Insurance Supervision ("ISA"). The Swiss Federal Supreme Court ("SFSC") has defined a contract of insurance as a contract under which an insurer promises an economic performance to an insured (or a third person) in case of the realization of a risk in exchange for payment of a premium. (e.g., Swiss Federal Supreme Court Decision ("SCD") 124 III 382, no. 6f). The basic defining elements of an insurance contract are thus the transfer of risk against payment. Furthermore, the SFSC has established two additional requirements, which are particularly relevant from an insurance supervisory law perspective, but might also have to be considered in the context of an insurance contract law analysis: (i) the requirement that the insurance contract must be an autonomous or independent agreement and (ii) the requirement that the insurer compensate the risks according to the laws of statistics. Consequently, according to the practical definition elaborated and constantly used in case law for decades (e.g. in SCD 58 I 259, no. 2; 107 Ib 56, no. 1b; 114 Ib 247, no. 4a; SFSC decision 4P.52/2000, no. 3a/bb) the concept of insurance in Swiss law rests upon the following five elements:

i) Risk or danger: Risk may be defined as a future event whose occurrence is both uncertain and in fact possible. There must be either uncertainty as to whether the future event will occur at all or uncertainty as to when the future event will occur (incertus an or incertus quando, see SCD 92 I 133, no. 4).

ii) Performance by the insured (i.e. premium payment): The premium is, in principle, the price the insured pays in exchange for the performance by the insurer in the event that the insured risk materializes. Although the Swiss Federal Supreme Court often uses the term "performance by the insured", it is also possible that the premium is not paid by the insured, but e.g. by a policyholder or another person differing from the insured (e.g. SFSC decision 2C_410/2010, no. 3.2).

iii) Performance by the insurer: The contract must include the obligation of the insurer (and thus the right of the insured) to perform to the insured or a beneficiary differing from the insured in case the insured risk materializes. Usually, the insurer pays to the insured an amount of money, but performance may also consist in a payment in kind, in the waiver of a claim against the insured or in any other conduct or benefit in favor of the insured or according to his will, including omissions (SCD 76 I 370, no. 4). According to more recent legal literature, performance may also consist in the rendering of services (Helmut Heiss/Ulrike Mönnich, in: Hsu/Stupp (eds.), Basler Kommentar zum Versicherungsaufsichtsgesetz, Basel 2013, art. 2 N 27; for the legal protection insurance, see art. 161 Swiss Federal Ordinance on Insurance Supervision ("ISO") (emphasis added): "Under a legal protection insurance contract, an insurance undertaking assumes the obligation, in exchange for a premium, to reimburse costs resulting from legal matters or to provide services in connection with such matters").

iv) Independence of the operation: This means that the insurance agreement must not be a mere modality or subsidiary agreement of a non-insurance contract, but must have a certain independent importance. E.g., a clause in a credit agreement whereby the creditor waives his right to the repayment of the outstanding loan in case of the debtor's death does not have independent importance and, therefore, does not yet result in a qualification of the agreement as an insurance contract (regarding warranties see question 8 (ii)).

v) Compensation of risks according to the laws of statistics (systematic business activity): Case law has not developed one single definition for this element. Instead, various court decisions have emphasized different criteria, namely the systematic business activity (SCD 58 I 262, no. 6; 114 Ib 247, no. 4), the distribution of risk according to the law of large numbers (SCD 58 I 262, no. 6; 107 Ib 61, no. 5; SFSC decision 2C_410/2010, no. 3.4), the consideration of the principles of statistics, at least implicitly (SCD 2C_410/2010, no. 3.4) and the requirement that the earnings equal or supersede the expenses (SCD 92 I 132, no. 3). In legal literature, the view prevails that an undertaking may not free itself from insurance supervision by not complying with the principles of statistics and insurance mathematics (see e.g. Heiss/Mönnich, op. cit., art. 2 N 37). Further, the Supreme Court

has held that it is not necessary that the business activity must be based on insurance mathematics (SCD 92 I 132, no. 3; 107 Ib 61, no. 5; SFSC decision 2C_410/2010, no. 3.4). Therefore, if an undertaking intends to assume a large number of similar risks, the element of compensation of risks according to the laws of statistics is likely to be given.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes, of the five elements, in principle, required for the qualification of a contract as an insurance contract (see above in the answer to question 1) the element of risk or danger includes the element of uncertainty: Risk may be defined as a future event whose occurrence is both uncertain and in fact possible (see also the further remarks in the answer to question 1); it depends on the factors of the probability and the potential magnitude of the event.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes, an insurance contract needs to provide for a transfer of risk from one party to another. This follows from the qualifying elements of a "risk or danger" and a "performance by the insurer" (see above, question 1, elements 1 and 3): The risk is transferred from the insured to the insurer by the promise of performance of the insurer in case the risk materializes. The prevailing view among scholars is that this transfer of risk against the payment of a premium (see above, question 1, element 2) are the core elements (i.e. *essentialia negotii*) of the insurance contract (see e.g. STEPHAN FUHRER, Schweizerisches Privatversicherungsrecht, Zurich 2011, N 2.5). Without a transfer of risk, there is no insurance contract.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

It is controversial in legal literature whether the subject matter of an insurance contract is someone's "interest" or "economic interest" in the non-occurrence of an event (the so-called "theory of interest", *Interessenlehre*) or whether the subject matter of an insurance contract is simply a physical object, a person or certain assets ("theory of objects", *Gegenstandslehre*) and the concept of an "interest" thus superfluous (in favor of the theory of interest e.g. Fuhrer, *op. cit.* (question 3), N 4.8 et seq.; in favor of the theory of objects e.g. Christian Boll, in Honsell/Vogt/Schnyder (eds.), Basler Kommentar zum Versicherungsvertragsgesetz, Basel 2001, art. 48 N 3 *et seq.*, and Christian Boll/Andrea Stadelmann Stöckli, in Honsell et al. (eds.), Basler Kommentar zum Versicherungsvertragsgesetz, Nachführungsband, Basel 2012, art. 48 ad N 4, both with further references). However, this debate can be left aside at least as far as the qualification of an agreement as an insurance contract is concerned. This is because representatives of both sides of the controversy agree that the protection of an abstract interest is not sufficient, i.e. there must be a tangible and valid economic interest and the occurrence of the insured event must have a negative economic impact on the policyholder, insured or beneficiary.

This rule also applies to fixed sum insurance contracts. Under these contracts, the insurer undertakes to perform upon the occurrence of a triggering event (e.g. the disability or death of the insured), irrespectively of whether this triggering event has caused any loss or damage. Nevertheless, there still must be a economic interest of the policyholder, insured or beneficiary in order to distinguish it from contracts of gambling and chance (see also below, question 8 (i)).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

No, it is not required that the insured interest attaches to the policy holder. E.g., the following constellations are possible (Fuhrer, *op. cit.* (question 3), N 14.7):

- The policyholder can take out an insurance policy where the triggering event is the harm (a) to an insured different from the policyholder or (b) to such insured's property, but the policyholder receives the insurer's performance, i.e. the policyholder is the beneficiary of the policy, but the danger is attached to someone else.

  E.g., a contractor can take out a contract works insurance policy (*Bauwesenversicherung*). Here, the contractor insures his interest in the builder-owners building: Under Swiss property law, the unfinished building belongs to the builder-owner (because the ownership in the building is attached to the ownership in the real property), but if the unfinished building is damaged, the contractor will have to repair the damage at his own expense based on the contract for work and labor (except if the builder-owner is responsible for the damage).

  However, the law provides for restrictions to this type of insurance in the area of life insurance to avoid or reduce the potential risk of criminal acts inflicted by the policyholder on the insured. According to art. 74 para. 1 ICA, the insurance on the life of another person is null and void if the person whose death shall be insured did not

consent in writing prior to the conclusion of the contract.

- The policyholder can take out an insurance policy where the triggering event is the harm (a) to an insured different from the policyholder or (b) to such insured's property, but whereby a third person, the beneficiary, receives the insurer's performance. In this constellation, the policyholder protects the interest of another person and the danger is attached to yet another person.

  E.g., a mother (i.e. policyholder) takes out an insurance policy that pays an amount to her children (i.e. beneficiaries) in the event of death of their father (i.e. insured).

  Consent restrictions apply to life insurances according to art. 74 para. 1 ICA as mentioned above (i.e. the insured person must give his prior written consent).

- The policyholder can take out an insurance policy where the triggering event is the harm (a) to an insured different from the policy holder or (b) to such insured's property and the insured receives the insurer's performance, i.e. the policyholder protects someone else's interest and the danger is attached to that person.

  E.g., a mother (i.e. policyholder) takes out an insurance policy that pays a capital amount to her children (i.e. insured and beneficiaries) in the event of their disability; or a carrier (i.e. policyholder) takes out a transport insurance policy for the benefit of the owner of the transported goods (i.e. insured and beneficiary).

- The policyholder can take out an insurance policy where the triggering event is the harm to the policyholder or his property, but where someone else receives the insurer's performance as beneficiary, i.e. the policyholder protects someone else's interest, but the danger is attached to himself.

  E.g. a parent (i.e. policyholder/insured) takes out an insurance policy that pays an amount to his spouse and kids (i.e. beneficiaries) in case of his death.

6. <u>Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?</u>

The "law of the large numbers" or element of compensation of risks according to the laws of statistics is predominantly an insurance supervision requirement (see question 1, element 5). This means that, as a general matter, it cannot be deducted from the fact that an undertaking does not apply the law of large numbers to diversify or compensate the risks under the contracts with its counterparties that such contracts would not qualify as insurance contracts from an insurance contract law perspective. The element of compensation of risks may however serve as an additional criterion in the qualification of a contract in that a contract offered by an undertaking fulfilling all the elements outlined in question 1 (and which is subject to FINMA insurance supervision) in its usual conduct of business is likely to qualify as an insurance contract.

7. <u>Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?</u>

No, but there are different statutory rules applying to life insurance contracts, such as art. 36 para. 3 ICA, which states that if the policyholder withdraws from a life insurance contract, he may claim back the policy reserve. Further, art. 73-96 ICA contain special provisions regarding personal insurance, e.g. stating:

- That the insurance on the life of another person is null and void if the person whose death shall be insured did not consent in writing prior to the conclusion of the contract (art. 74 ICA; see also above, question 5);

- That subject to existing pledges, neither the policyholder's insurance claim nor the beneficiary's insurance claim are subject to debt enforcement proceedings in favor of the policyholder's creditors if the policyholder's spouse or descendants are the beneficiaries of the insurance policy (art. 80 ICA).

Distinction from Similar Types of Contracts and Exemptions

8. <u>Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.</u>

i) Contracts of gambling and chance

The difference between an insurance contract and a contract of gambling and chance is that the parties to an insurance contract intend to protect an (economic) interest of the policyholder (or insured or beneficiary), i.e. the insurance contract offers protection against the possibility of future damage or loss. A well-known example to illustrate the difference between a gambling contract and an insurance contract is the "insurance" that was taken out in medieval times for the event that the pope should die prior to an agreed upon date. The "insured" would suffer no damage or loss by the occurrence of the "insured" event. Thus,

such a contract does not protect an economic interest of the contractual counterparty and is therefore not an insurance but a gambling contract (Fuhrer, *op. cit.* (question 3), N 4.12)

ii) Warranty, guaranty or any other surety contracts

Warranties, guaranties or other surety contracts, can, depending on the individual case, often be distinguished from an insurance contract by application of the element of "independence of the operation" (see above, question 1, element 4). Warranties or guaranties are often modalities or subsidiary agreements of non-insurance contracts (such as sales contracts) and do not qualify as independent or autonomous agreements. Therefore, they do not qualify as insurance contracts.

In SCD 107 Ib 54, the Swiss Federal Supreme Court had to qualify a 12 month warranty of a producer of motor oil additives, covering the costs for reparation of the motor and the gearing mechanism. The warranty was sold and upheld under the condition that the motor oil additives were used in the car, but the warranty was not restricted to damage caused by the motor oil additives. The Swiss Federal Supreme Court decided that this warranty was an independent operation and therefore an insurance contract. The reason was that the warranty could have been sold independently from the motor oil additives and that the prize of the warranty (CHF 140; paid by partnering garages) was higher than the prize of the motor oil additives themselves (CHF 73).

In many cases, a warranty, guaranty or surety contract can be qualified as an independent operation and may fulfill all of the five elements that define an insurance contract (see above, question 1). It is therefore difficult to distinguish these contracts from insurance contracts. These difficulties arise in particular with regards to surety contracts issued by banks. The law does not differentiate between banking contracts and insurance contracts and there are no clear-cut criteria to make this distinction. In these cases, an important, but not necessarily conclusive, indication for either a banking or an insurance contract is whether the contract has been concluded by a licensed bank or by a licensed insurance undertaking.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Similar to the surety contracts as referred to above, financial contracts may contain all elements of an insurance contract, especially if the counterparty enters into a contract for hedging purposes. Here too, there are no clear-cut criteria to distinguish between financial contracts and insurance contracts and the decision may be strongly influenced by the question of whether a financial institution or an insurance undertaking has entered into the contract.

Similar considerations apply in connection with risk transfer contracts entered into between (re-)insurance companies and special purpose vehicles which in turn emit (direct or indirect) cat bonds. Such contracts must likely be deemed not to constitute reinsurance contracts on the basis that the relevant special purpose vehicle is not a licensed reinsurance company (Christian Schaal, Risikotransfer durch Katastrophenanleihen, Zurich 2010, p. 44).

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

As stated under question 8 (ii) and (iii), there are contracts that fulfill all the five requirements of an insurance contract but may not qualify as insurance contracts under a holistic view taking into account all the circumstances of the case.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

De facto, yes. There are no clear-cut criteria to distinguish between banking/financial contracts and insurance contracts. Therefore, a qualification may be strongly influenced by the question whether the seller of the protection or product is a bank (or another type of financial market participant) or an insurance undertaking (see also questions 8 and 9).

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Yes, in principle, any insurance undertaking subject to ISA must obtain a license from FINMA in order to engage in the business of insurance (art. 3 para. 1 ISA). The following insurance undertakings are e.g. excluded from Swiss insurance supervision and must therefore not obtain a FINMA license (art. 2 para. 2 ISA):

- Insurance undertakings domiciled in a foreign country that only engage in reinsurance in Switzerland;
- Insurance businesses, to the extent that they are subject to specific supervision under federal laws or laws of the cantons, e.g. occupational pensions institutions (registered in the register of occupational pension plans), mandatory health insurance or insurance business of building insurers of certain cantons.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

A risk-taker willfully carrying out an activity requiring a license without having obtained such license is liable to a custodial sentence of up to three years or to a monetary penalty (art. 44 para. 1 of the Swiss Financial Market Supervisory Act ("FINMASA")).

Persons acting negligently are liable to a fine of up to CHF 250,000 (art. 44 para. 2 FINMASA). In addition, such sanctions might e.g. affect the fit and proper test requirement should the sanctioned person be or intend to be in the board or executive management position of a financial institution subject to prudential supervision.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Yes, according to art. 11 para. 1 ISA, an insurance undertaking may only engage in insurance business or types of business that are directly related to insurance business. FINMA can approve the conduct of other types of business if they do not endanger the interests of the insured (art. 11 para. 2 ISA).

Insurance undertakings that have obtained a specific license within the subset of life insurance licenses are allowed to conclude capitalization contracts, i.e. contracts without insurance coverage for any biometric risks (Appendix 1 of the ISO, classification A.6), although such capitalization contracts strictly speaking do not qualify as insurance contracts. The insurers that conclude such contracts remain under insurance supervision and do not fall under banking supervision. Such capitalization contracts may, however, not be labeled as insurance contracts. Furthermore, apart from these capitalization contracts, insurance undertakings engaging in primary life insurance may, in addition, only engage in accident and health insurance (art. 12 ISA) but not in any other types of insurance.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

In principle, there are no such submission or approval requirements, except e.g. for the insurance of all risks in occupational pension plans and for the supplementary insurance to the mandatory health insurance (art. 4 para. 2 lit. r ISA). However, in the area of natural hazards insurance (*Elementarschadenversicherung*), FINMA still reviews the premiums (art. 33 para. 3 ISA) and the Federal Council (*Bundesrat*) has the authority to specify the terms of insurance if it deems this necessary (art. 33 para. 5 ISA). Further, FINMA specifies the reference rate for life insurance policies with an interest rate guaranty (art. 121 ISO) and has issued a circular defining, inter alia, the minimal requirements for life insurance tariffs (FINMA-Circular 08/40, Life insurance, no. 6-57).

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

As a general rule, contracts are only null and void if the rule that has been breached by the (conclusion of the) contract explicitly foresees the nullity of the contract or if such consequence follows from the intention and purpose of the rule that has been breached (SCD 134 III 442, no. 2.2; 119 II 224, no. 2). If one of the parties was not allowed to enter into a certain contract, this will in principle not render the contract null and void (e.g. SCD 117 II 50, no. 2 c). Therefore, if an insurance contract is issued by a non-licensed party, the contract will under Swiss private law not be null and void, but in principle valid and binding upon the parties. However, the insured may, depending on the circumstances of the individual case, be entitled to reject the obligation due to fundamental error (*Grundlagenirrtum*: art. 24 para. 1 no. 4 Swiss Code of Obligations ("CO")) or deceit (*absichtliche Täuschung*: art. 28 para. 1 CO) and may in such context be entitled to claim damages, e.g. based on *culpa in contrahendo.*

It is further worth noting that article 36 paragraph 1 ICA grants a right of withdrawal to the policyholder in the event that an insurance undertaking's license is revoked by FINMA. The policyholder is in such case entitled to reimbursement of the surplus premium or life insurance policy benefits, as the case may be, and may further be entitled to claim damages (art. 36 para. 2-4 ICA).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes, the Federal Act on Insurance Contracts of 2 April 1908 (SR 221.229.1). Where the ICA does not contain a provision, the CO applies (art. 100 para. 1 ICA).

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Form

The validity of the insurance contract is not subject to compliance with any particular form, though the application for an insurance policy and acceptance by the insurer are customarily produced in writing. However, the insurer must issue a (written) policy to the insured stating the rights and duties of the parties (art. 11 ICA).

Content

Under article 3 ICA an insurer must inform the insurance taker prior to the execution of the insurance contract about the identity of the insurer and the key

elements of the contract, including, e.g., the insured risks, the scope of insurance coverage, the premiums due and any other duties of the policyholder, the duration and options for terminating the contract and (particularly with regard to life insurance) the methods, principles and bases for calculating and distributing the surplus profits.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

The ICA contains a list of mandatory provisions of the ICA that cannot be amended by the parties of an insurance contract (art. 97 ICA) and a list with articles that can only be amended in favor of the insured (art. 98 ICA). However, while not all of the provisions in these two lists specifically favor the insured, at least some of them clearly aim to protect the counterparty of the insurance undertaking, such as art. 3 and 11 ICA described above under question 17 and art. 33 ICA ("If not stated otherwise in this Act, the insurer is liable for all events that display the characteristics of the risk for which the insurance was taken out unless the contract excludes particular events from the insurance in a precise and unambiguous way"). Furthermore, general rules of Swiss civil procedure law and private international law impose restrictions regarding the choice of forum and choice of law in the context of contractual relationships with consumers.

Art. 40 *et seq.* ISA refer to registration requirements and other obligations of insurance intermediaries. The main purpose of these provisions is to protect the insured.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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General Information on Turkish Law

Turkey is a member of the continental law system and legislation is the principle and primary source of law with its letter and spirit. In the absence of any rule in the legislation and the rule of custom (defined as unwritten rules existing for a time immemorial and continuously observed and which are considered as "opinion necessitates"), the judge must decide as he was himself the legislator. This rule does however not mean that the rules which the judge sets up are to have the force of a general legislative enactment and therefore binding in the sense of legislation. Doctrine and court judgments constitute secondary and supporting but important sources of law in guiding the judge and in providing an understanding of the meaning and proposed application of the legislation and also in the functioning of the judge as a quasi legislator.

With respect to private law, *only* judgments of the *General Assembly of Joint Chambers of the High Court of Appeals* are legally binding on inferior courts. The number of these decisions however is limited. Other decisions of the High Court of Appeal or local courts are not legally binding on inferior courts and the courts rendering them. However courts in practice tend heavily to take decisions of the High Court of Appeals into consideration in giving their judgments.

The responses below are therefore based on the provisions of relevant legislative texts, the insurance doctrinal views and Turkish High Court of Appeal precedents.

Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

The sixth Book of the Turkish Commercial Code dated 13.01.2011 and numbered 6102 ("the TCC") which is an integral part of the Turkish Civil Code (dated 22 November 2001 and numbered) introduces provisions with respect to insurance contracts. The first Part of the Insurance Book includes general provisions applicable to all insurance contracts, indemnity insurances and personal insurances. The second Part of the Book is divided into two Chapters. The first chapter is with respect to Indemnity Insurances and is in turn provided in two Sections "property insurances" and "third party liability insurances". The second Chapter is with respect to Personal insurances and is divided into three Sections i.e. "life insurances", "accident insurances" and "health and sickness insurances".

Article 1401 of general insurance provisions gives a definition of both indemnity and personal insurances:

> "A. Insurance Contract
>
> I. Basic Notions
>
> 1. Definition
>
> (1) An insurance contract means a contract under which the insurer undertakes, in exchange for a premium, to indemnify a loss caused by the occurrence of a danger, risk, harming an interest measurable in monetary terms of a person concerned or to effect payment or to fulfill other performances based on the lifetime or upon occurrence of certain events in the course of the lifetime of one or several persons."

The first part of the above definition is with respect to indemnity insurances and the second part to personal insurances (i.e. life, accident, and health and sickness insurances).

Article 1402 of the general insurance provisions provides a separate definition for "mutual insurance stating that

> "Under mutual insurance, several persons mutually undertake to indemnify the loss incurred by one of them as a result of the occurrence of a defined risk. Only cooperative companies are entitled to carry on mutual insurance."

Under Article 1487 of the TCC there is a specific definition with respect to life insurances:

> "A. Life Insurance
>
> I. Definition
>
> (1) Under a life insurance contract, the insurer undertakes, in exchange for a premium, to pay a fixed sum to the policyholder or a person designated by the policyholder upon the death or survival of the insured."

The TCC does not provide any definition with respect accident and health and sickness insurances but introduces some provisions with respect to their subject matter and content. With respect to the definition of life insurance see question 7 below for further information.

With respect to *indemnity insurances*, the following can be identified as the main criteria of an insurance contract considering the above statutory definition of Article 1401, various other provisions of the TCC, insurance doctrinal views and court of Appeal precedents:

i) An insurable interest measurable in monetary terms

The TCC in its definition under article 1401 cited above does not define "interest" but refers to an interest measurable in monetary terms.

The general provision of article 1408 of the TCC provides as follows:

A. Insurance Contract

II) General Rules

3. Lack of Insurable Interest

(1) The insurance contract shall be null and void if no insurable interest existed at the time of the conclusion of the contract. If the interest, which existed at the time of conclusion, ceased to exist within the contract period, the insurance contract becomes null and void immediately.

See question 4 below for further explanations on insurable interest.

ii) Risk:

The definition of the TCC includes "risk", i.e. danger which leads to harm to the insured interest. Article 1421 of the general provisions of the TCC explicitly refers to the obligation of the insurer to "carry the risk." The insurer's obligation to indemnify is subject to the occurrence of the identified risk(s) and the occurrence of a loss as a result of the occurrence of such risk(s). A risk is however only insurable where it is coincidental, i.e. a risk the occurrence and/or the time of occurrence of which is uncertain.

iii) Insurance Sum

Insurance sum is the maximum amount to be paid by the insurer to the insured (subject to the limit of the insured value and the actual loss in indemnity insurances).

iv) Insurance Premium:

Premium is the consideration paid by the policyholder for the transfer of risk to the insurer. Article 1421 of the TCC provides that

"Unless otherwise contracted liability of the insurer starts at the time of actual payment of the premium or the first installment. The insurer's liability in case of carriage of goods in transit and by sea starts at the conclusion of the contract."

2. <u>Does an insurance contract require an element of uncertainty? Please describe.</u>

As explained above one of the elements of an insurance contract is the provision of cover in case of occurrence of a risk. A risk within the meaning of insurance is an event which is coincidental, the occurrence and/or the time of occurrence of which is uncertain. Where the time or the period of occurrence of a risk is known, such risk cannot be insured. Risks which have already occurred or which are impossible to occur are not insurable unless the insurer and the policyholder (and the insured if he is aware of the insurance) do at the conclusion of the insurance contract not know about such occurrence or impossibility.

3. <u>Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?</u>

The heading of the general insurance provision of 1421 regarding the obligations and duties of the parties to an insurance contract provides for "the insurer's obligation to carry the risk".

III. Duties and Obligations of the Parties.

1. Duties and Obligations of the Insurer

a) The Obligation to Carry the Risk

aa) General

1421: (1) Unless otherwise contracted liability of the insurer starts at the payment of the premium or the first installment. The insurer's liability in case of carriage of goods in transit and by sea starts at the conclusion of the contract.

Accordingly, depending on the type of the insurance contract, the risk is transferred to the insurer as soon as the contract is concluded or the premium paid.

4. <u>Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?</u>

Article 1408 cited above under question 1 provides clarity that the lack of insurable interest not only at the time of the conclusion of the contract but at any stage will result in invalidity of the contract. Provisions to the contrary will render the insurance contract invalid.

The TCC does not provide for a definition of insurable interest but provides under Article 1401 that the insurable interest shall be measurable in monetary terms. According to settled doctrinal views and practice it is recognized that an insurable interest consists of proprietary, intellectual or personal rights and receivables which are measurable in monetary terms and capable of enforcement by legal action. No interest can be insured unless it is legitimate and legal.

5. <u>Is it required that an insured interest attaches to the policyholder (i.e. the party</u>

entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Article 1453 of the TCC on Property Insurance provides that any one who has an interest in the non-occurrence of the risk can insure such interest. Article 1454 (1) of the TCC further provides that a policyholder can insure the interest of a third party by disclosing or not disclosing the identity of that third party. In such case the third party will be the insured who in principle will have the rights arising from the insurance contract.

There is no requirement for the policyholder to have a direct or indirect interest in order to insure the interest of a third party. This is reflected in the provision of article 1455 of the TCC on property insurances providing that

> "If a person having insurable interest only in a part of a property or right over a property takes out insurance for more than its share, the exceeding part of the insurance shall be deemed to have been made in favor of those with the same kind of interest on the property as the policy holder."

The same principles apply with respect to third party liability insurances whereby a policyholder can take out insurance for the benefit of a third party and the interest does not need to attach to the policyholder.

With respect to life insurances, article 1490 of the TCC provides that the policyholder can take out insurance on its own life or on the life of another person (person subject of the risk) against death or survival. In the case of insurance on the life on another person it is required that the beneficiary has an interest in the survival of that person.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The law of large numbers does not affect the classification as an insurance contract and is an actuarial issue.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Article 1401 of general insurance provisions applicable to all types of insurances gives a definition of both indemnity and personal insurances. With respect to personal insurances the relevant provision states:

> "A. Insurance Contract
>
> I. Basic Notions
>
> 1. Definition
>
> (1) An insurance contract means a contract under which the insurer undertakes, in exchange for a premium, ……………… to effect payment or to fulfill other performances based on the lifetime or upon occurrence of certain events in the course of the lifetime of one or several persons. "

The Chapter on Personal Insurances of the Insurance Book of the TCC is divided into three Sections, i.e. "life insurances", "accident insurances" and "health and sickness insurances".

Article 1487 of the TCC introduces a specific definition for life insurances:

> "Under a life insurance contract, the insurer undertakes, in exchange for a premium, to pay a fixed sum to the policy holder or a person designated by the policy holder upon the death or survival of the insured."

Different from indemnity insurances the limit of indemnity is not restricted by the amount of the actual loss but by a fixed sum predetermined in the insurance contract. Therefore the payment to be made by the insurer is called insurance sum rather than insurance indemnity. The risk element in life insurances and all personal insurances relate to elements of human life.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

The Turkish Code of Obligations introduces provisions on gambling and betting, but does not define them. Similar to insurance contracts there is an element of uncertainty and risk, and an undertaking to pay subject to the occurrence of a certain event, and in some cases an element of "pooling" as in the case of insurance.

The purpose of gambling is, on the other hand, enrichment, subject to the realization of a condition, whereas insurance in principle covers and aims to indemnify a loss of an insurable legitimate interest (except for life insurance) and provides assurance against risks. There is no element and aim of losing or winning, as in gambling, and no enrichment of the insured. Contracts of gambling also involve an element of betting whereas there is no such element in insurance contracts. A pre-requirement for the obligation of the insurer to pay only arises where there is a loss whereas this is not the case in gambling.

The presence of the requirement of a legitimate insurable interest on the subject matter of the contract does not exist in contracts of gambling and chance. One of the elements of an insurable interest is regarded as "legal enforceability" as explained under question 1 above. Although contracts of gambling and chance can validly be entered, receivables arising from these contracts are not protected by the law in that they cannot in principle be enforced by court mechanisms (except for provisions of special laws such as the National Lottery.)

Under Turkish law insurance cannot cover losses arising from risks which have been caused intentionally by the policyholder (or the insured) whereas the risk element in gambling is willfully caused by the parties.

ii) Warranty, guaranty or any other surety contracts

Warranty and Extended Warranty

Although both warranty and insurance undertake to cover certain losses arising from certain events, in a warranty, the underlying idea is that the manufacturer (seller etc.) is guaranteeing durability of its products. On the other hand, with an insurance policy, there is not necessarily a focus on guaranteeing specific engineering and quality of a product. A warranty promises indemnity against defects in the article sold, while insurance in principle indemnifies against loss or damage resulting from perils outside of and unrelated to defects in the article itself. A major difference between a warranty and insurance is that a warranty is collateral to the main purpose of the underlying contract and is not a contract itself whereas the undertaking of the insurer is not collateral. Except for extended warranties the warranty is not given against a consideration for premium but is a duty of the manufacturer arising directly from the law.

Extended warranties although they may take various forms, may be more similar to insurance than warranties due to the fact that they constitute contracts mutually obligating the parties of the contract. There is no regulation on the nature of extended warranties (and the Insurance General Directorate of the Treasury is working on a regulation) and to the knowledge of the authors no court of appeal decision discussing this. However, where if the risk covered by the warranty contract is exclusively one relating to the parts and workmanship involved in the product itself, and if the contract is issued either by the manufacturer or by a dealer in connection with a specific sale, the contract should not be defined as insurance.

Guaranty Contracts

Guaranty contracts are not defined by any statute under Turkish law. Turkish doctrinal views and the High Court of Appeal classify certain guaranty contracts as a "promise of a third person's act" provided under article 128 of the Turkish Code of Obligations. According to article 128, a person who undertakes an action of a third party, is liable for the loss occurred as a result of non - realization of that action.

On the basis of prevailing doctrinal views and High Court of Appeal precedents they can be defined as contracts whereby the guarantor, with the purpose of soliciting the guaranty to a certain action or transaction and/or with the purpose of providing assurance, undertakes entirely or partially risks of these actions or transactions and promises to indemnify the guaranty in case of failure of the underlying actions or transactions or the debtor in the underlying relationship.

Both guaranty and insurance contracts have the purpose of providing assurance and undertaking of a risk. However, the very purpose of many of the guaranty contracts is soliciting the guaranty to a certain act or transaction whereas there is no such aim in an insurance contract.

In insurance contracts the insurer is undertaking to carry the risk and to indemnify the loss in consideration of a premium whereby in principle the guarantor does not have a claim for a consideration from the guaranty although there may be guaranty contracts providing otherwise. Although in certain insurance contracts the risk of failure of fulfillment of an obligation by a third party can be covered, insurance is unlikely to provide cover for a receivable based on e.g. an invalid underlying contract, whereas the guarantor's obligation is in principle independent of validity, possibility etc. of the underlying relationship.

In principle an insurance contract also cover risks arising from fault of the policyholder except for willful acts, there may be arguments to the effect that the guarantor's liability may be deleted or mitigated where the risk occurs as a result of the fault of the guaranty.

Whereas the right of subrogation of the insurer who provides cover to the insured is a fundamental principle of indemnity insurances, the right of subrogation of the guarantor to the third party whose act was guaranteed may or may not exist depending on specific circumstances.

Surety Contracts

Another type of contract provided under article 581 of the Turkish Code of Obligations is Surety Contracts whereby the surety undertakes towards the creditor of a third party debtor liability for losses arising from default of such debtor. Main difference from a guaranty contract is that the obligation of the surety is collateral unlike the obligation of the guarantor (whereby the guarantor's undertaking is independent of e.g. validity of the underlying contract). This is also one of the differences between a surety contract and insurance.

Surety is in principle not given for a consideration, and this is not a requirement for a surety contract,

whereas the insurer receives a premium in order to carry the risk.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts such as derivates (forwards, futures, options and swaps) may obviously take various forms and can be complex however in outline they can be considered similar to insurance in that they may involve elements such as a promise to pay a sum of money on the happening of an event, protection against risks, risk sharing and transfer of risk.

Insurance contracts provide persons exposed to certain risks with financial protection against the consequences of the occurrence of specified risks, many of which cannot be expressed in terms of market prices. In case of insurance, funds are collected from policyholders and invested in financial or other assets which are held as technical reserves to meet future claims arising from the occurrence of the events specified in the insurance policies i.e. insurance manages event risk primarily by pooling, not the trading of risk. The insurer assumes not only the risk of a loss, but distributes the risk across many of the risk pooling—is absent in many of these derivative transactions.

In case of insurance the occurrence of the risk triggers the obligation of the insurer to pay indemnity i.e. it is a pre-condition for payment, whereas e.g. in a forward or future contract, it is in fact not the occurrence of a risk which triggers the obligation to pay but the underlying contract.

Another established principle of insurance law different from derivative transactions is the concept of indemnity, as a result of which a person cannot recover more under an insurance contract than the loss incurred (except for life insurances). A pre-requirement for the insurer's obligation to pay is the occurrence of a loss, whereas in derivative contracts there is no such requirement. Derivative transactions are also entered for the purpose of assurance but also speculation and arbitrage.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

No.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

No.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

The framework of regulation of the insurance sector is provided by the Turkish Insurance Act numbered 5684 and dated 14 June 2007 ("the Insurance Act"). According to the provisions of the Insurance Act, before incorporation, insurance companies (which must be in the form of a joint stock company or in the case of mutual insurance in the form of a co-operative company), unlike regular companies, must obtain approval from the Ministry of Customs and Trade and have their draft articles of association approved. This is a pre-condition to incorporation. To operate as an insurance company, the company must apply after incorporation to the Undersecretariat of the Treasury for obtaining a license for operation in each insurance license class. The licenses are to be registered with the Trade Registry and published in two leading newspapers published nationally.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

Within one year at the latest, an insurance company upon incorporation (i.e. registration with the relevant Trade registry) must make its application for insurance license. Companies failing to do so, it will loose their right to use "insurance" in their commercial names. According to article 35/1 of the Insurance Act, insuring without a license is subject to criminal penalties of imprisonment of three to five years and criminal monetary fines corresponding to a minimum of six hundred days to a thousand days. This fine is calculated by multiplying the full number of days subject to penalty with the monetary amount fixed per day. The court decides on the value of the amount of the daily fine (between twenty, and a at most TR 100 per day) according to personal and financial conditions of the offender.

Also, failure to register the license with the relevant trade registry and to comply with the relevant publication requirements is subject to administrative fines of TR 48,000 (ca EUR 3,225.- as of 17 June 2013) due to the provision of article 34 of the Insurance Act.

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

Article 3 of the Insurance Act, provide that insurance (and reinsurance) companies to operate in Turkey are prohibited from engaging in transactions other then insurance transactions and businesses directly related to insurance.

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

According to the Regulation on the Incorporation and Operation of Insurance and Reinsurance Companies dated 24 August 2007 and numbered 26623 require insurance and reinsurance companies and branches of foreign insurance and reinsurance companies to submit their products and policies in their application for relevant insurance licenses.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

According to Article 1401 of the Turkish Commercial Code, relevant articles of the Turkish Code of Obligations with respect to gambling and betting shall apply to insurance contracts concluded with an unlicensed company in the knowledge of this deficiency. (However, this provision does not apply to insurance contracts concluded with insurance companies that are not resident in Turkey.)

According to relevant provisions of the Code of Obligations, a contract of gambling and betting comes validly into effect and parties can perform under the contract. However receivables arising from gambling and betting cannot be subject to any legal action, i.e. cannot be legally enforced.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Turkey is a member of the continental law system and legislation is the principle and primary source of law. The sixth Book of the Turkish Commercial Code which is an integral part of the Turkish Civil Code introduces provisions with respect to insurance contracts. The first Part of the Insurance Book includes general provisions applicable to all insurance contracts, indemnity insurances (property and third party liability) and personal insurances (life, accident, health and sickness). Where there is no relevant provision in the Commercial Code, relevant applicable provisions of the Turkish Code of Obligations shall be applicable.

The Turkish Insurance Code is primarily related to regulation and supervision but also includes certain provisions with respect to insurance contracts such as form, or insurance arbitration.

There are also special Acts such as the Highway Traffic Act, Turkish Civil Aviation Act, Financial Leasing Act etc., which contain requirements and provisions with respect to relevant insurance contracts.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

The formation of an insurance contract is in principle not subject to any formal requirement for validity but to the general rules of contract formation provided by the Turkish Code of Obligations. Article 1424 of the general insurance provisions of the TCC provides that the insurer shall deliver the insurance policy duly signed by authorized persons within twenty four hours from the conclusion of the contract if the insurance contract is concluded by the insurer or its agent, otherwise within fifteen days. The insurer shall be liable for losses arising from late delivery of the policy. Where no policy is delivered the proof of the existence of the contract is subject to the general provisions of proof.

According to article 1425 of the TCC on the content of an insurance policy, an insurance policy shall set out the respective rights of the parties, provisions with respect to default, general conditions and special conditions if any. The policy shall be drafted in such way to facilitate easy reading.

Article 11 of the Insurance Act provides that special conditions of an insurance policy shall be in compliance with the relevant general conditions predetermined by the Undersecretary of the Treasury. This does not however mean that general conditions cannot be amended by special conditions subject to the mandatory provisions of the law. Article 11 further states that risks that are not covered shall explicitly be shown in the policy and that the lack of such explicit exclusion shall render a presumption of cover. Article 11 of the Insurance Act also provides that no foreign language words can be used in an insurance policy. Before the introduction of the Insurance Act the Turkish Court of Appeal used to give affect to internationally utilize standard wording in a foreign language attached to policies. The authors are not aware of any precedents interpreting the new provision of the Act and its effects.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

A consumer within the definition of the Turkish Consumer Act is a natural or legal person who receives, uses or benefits from services or goods without a commercial or professional purpose. In that respect, although not all insured persons would fall under the legal definition of a consumer, certain aspects of the legislation confer them a consumer – like protection.

One of the primary aims of the Turkish Insurance Act has been expressed as the protection of economic interests of insured parties through various regulations. The Insurance Act explicitly refers to advertising and communication of products and prohibits any misleading behavior and unfair competition in this regard. The Act provides that such

cases shall be referred to the Advertising Board established due to the provisions of the Turkish Consumer Act. Where the insured is also a consumer especially Article 6 of the Consumer Act based on the EC Counsel Directive 93/13 on unfair terms in consumer contracts shall be applicable. Article 6 provides among others that a contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer. Such unfair terms are not binding on the consumer.

There is a specific regulation based on the Insurance Act on the duty of insurers (and their agents) to supply policyholders with sufficient information regarding the scope, terms and conditions, operation and other relevant circumstances during the negotiation and before the conclusion of the contract, and developments which may affect the interest holders during the policy period. This is introduced with the aim of increasing awareness of policyholders at all stages before and after formation of contracts and imposes on insurance companies a duty to provide policyholders with certain notices and an pre – contractual information form. Upon request ensured parties and beneficiaries (in life insurances) must be supplied with the same type of information.

Also, the TCC introduces provisions with respect to the duty of the insurer to properly inform the insured of the insurance conditions before and during policy period and requires the insurer to provide a separate information form giving the above referred information.

Certain mandatory and semi – mandatory provisions of the TCC also provide protection in that they cannot be amended by contract or amended contrary to the interests of the insured and the policyholder.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

It would be worth mentioning that the Turkish Commercial Code referred to in this paper quire recently entered into force in 30 June 2012. The insurance Section of the TCC is much wider in scope and attempts to provide clarity in terms of both law and terminology controversial under the Insurance Book of the old Commercial Code of 1956 which was highly insufficient to meet the dynamic needs of today’s insurance industry. For the first time in Turkish insurance law, a specific Section on third party liability insurances has been introduced by a Code. The German Versicherungsvertragsgesetz (Insurance Contracts Act) of 30 May 1908 as amended the German and English insurance general conditions were taken as primary and secondary sources of reference in the drafting. Developments in the insurance laws of Germany, France, England, and Switzerland were also considered. It is however yet to be seen how the courts will interpret the new provisions of the Code.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

1.1 In English law, there is no general statutory definition of an insurance contract and it is left to the courts to determine whether a contract is a contract of insurance. There have been relatively few decisions of the English courts which have dealt with whether a contract is a contract of insurance. The decisions have generally described what a contract of insurance does but have been very careful not to define what is (and what is not) a contract of insurance.

1.2 However, notwithstanding the above, we have been left with a relatively well settled description of a contract of insurance. The case of *Prudential Insurance Co v Commissioners of Inland Revenue [1904] 2 K.B. 658* sets out that a legally enforceable contract of insurance is one under which a provider undertakes:

i) in consideration of one or more payments;

ii) to pay *money or provide a corresponding benefit* to a recipient;

iii) in response to a defined event;

iv) the occurrence of which is *uncertain* (either as to when it will occur or as to whether it will occur at all); and

v) which is adverse to the interest of the recipient (in that she/he must possess an *insurable interest* in the subject matter insured).

1.3 Arguably, the most important features of a contract of insurance are those in bold; that the insurer provides money or a corresponding benefit in response to an uncertain event in respect of which the insured has an insurable interest. Additionally insurance contracts must contain an element of risk - and this is relevant to each of the characteristics above.

1.4 The Financial Conduct Authority ("FCA"), which is one of the authorities responsible for regulation of insurance in the UK, has issued guidance in The Perimeter Guidance Manual ("PERG") on the identification of contracts of insurance. PERG 6 explains that the FCA will apply the following principles, after applying the principles set out in the *Prudential* case, in considering whether a contract constitutes a contract of insurance:

i) The FCA will attach more weight to the substance, rather than form, of the contract;

ii) The provider and customer's intention is unlikely to be relevant; and

iii) The contract will be characterized as a whole (following *Fuji Finance Inc. v Aetna Life Insurance Co. Ltd* [1997] Ch. 173 (CA)).

2. Does an insurance contract require an element of uncertainty? Please describe.

2.1 Yes. A contract of insurance must be a contract based on an uncertain event. A contract of insurance is a contract against a contingency and not a certainty.

2.2 The benefits under an insurance contract must be payable on the occurrence of an event which is uncertain in terms either of *if* it will happen or *when* it will happen (*Prudential Insurance Co v Commissioners of Inland Revenue*). There must always be an element of uncertainty. In the case of indemnity insurance (insurance against fire, theft etc.), the uncertainty is whether there will be a loss at all. In the case of life insurance, the uncertainty relates to the date that it will occur (*Gould v Curtis [1913] 3 KB 84*).

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

3.1 Yes. The transfer of risk is an essential element to a contract of indemnity insurance. One of the determining factors of whether a contract is one of indemnity insurance is whether a risk is being transferred by the insured to the insurer. Indeed, the "assumption of risk" by the insurer is used by the FCA as a descriptive feature of all contracts of insurance (see PERG 6.6.2G).

3.2 The general principle that a transfer of risk is necessary for a contract of insurance is easier to apply to indemnity contracts that are contracts of general insurance which cover the risk of loss. There is not always a transfer of risk from the insured to the insurer in the case of long term insurance contracts such as life insurance, however the English courts have still found that these kinds of contracts are classified as insurance even though there is no assumption of risk from the insurer.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

4.1 Yes. An "insurable interest" is an essential element to a contract of insurance. It has been loosely defined as the "insureds pecuniary interest in the subject matter of the insurance". The principles behind the concept of insurable interest are mainly concerned with ensuring that a person who cannot suffer a loss is prevented from insuring in the first place. The requirement of an insurable interest in a contract of insurance is simply another way of expressing the fact that an insurance contract must be a contract against the risk of loss.

4.2 There is no single overriding general rule of English law which requires the insured to have an insurable interest in the subject matter insured under the policy. The need to possess an insurable interest is based on a series of independent statutory and common law principles. These apply differently to the various classes of insurance contract. An insured party must possess an insurable interest in the subject matter either (a) because this is a requirement of the particular contract of insurance in order for it to be enforceable; or (b) because it is stipulated by statute as a condition of the policy in order to be legally valid. Various statutes refer to the concept of insurable interest in order to determine whether a particular contract is a legal contract of insurance.

4.3 For certain types of insurance contract the requirement for an insurable interest derives from statute. An insurable interest is required under life insurances and certain other contingency insurances under the Life Assurance Act 1774. An insurable interest is required in marine insurance because of the Marine Insurance Act 1906. (The provisions in these statutes override any provision to the contrary in the policy). Otherwise, the requirement for an insurable interest is derived from case law.

4.4 Other than in the context of marine insurance, there is no statutory definition of insurable interest. The concept has been developed by the courts.

4.5 For there to be an insurable interest an insured must have an existing right. A hope or expectation of a future right or benefit is not sufficient to constitute an insurable interest. The most widely quoted definition of insurable interest is that of Lawrence J in *Lucena v Craufurd (1806) 2 B & PNR 269,* which speaks of insurable interest in terms of financial interest in the subject matter insured:

i) The insured must have a genuine interest in the subject matter;

ii) The insured must be prejudiced if anything adverse happens to it; and

iii) The insured's interest can be partial, or at least not necessarily whole.

4.6 The cases defining the concept of insurable interest could be summarized as showing that an insurable interest exists if: the insured has legal or equitable title to the subject matter; or if the insured is in possession of the subject matter; or if the assured is not in possession of the subject matter but may either be responsible for, or suffer loss in the event of, any damage to the subject matter (*Feasey v Sun Life Assurance Co. of Canada [2003] Lloyd's Rep IR 637*).

4.7 Whilst this is the strict legal position, there are examples where the insurable interest is less easily identified, for example group life assurance and key man insurance, which are often taken out by an employer and written as life assurance. It could be argued that an employer only has an insurable interest in the lives of its employees to the extent of the employee's notice period and as such it would be more appropriate for these policies to be written as general financial loss policies. However, in reality these issues are unlikely ever to be tested in the courts because these anomalies are accepted in the insurance industry and insurers always honor the policies. See also the *Feasey* case, which applied a less strict analysis to the insurable interest for a policy on many lives over a substantial period.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

The insurable interest does not have to attach to the policyholder, but the insured must possess an insurable interest in the subject matter insured under the policy. Therefore if the insurable interest attaches to a third party, that third party must be a beneficiary under the insurance contract.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance

contract or is it merely a supervisory and actuarial issue?

6.1 The legal classification of the contract as a contract of insurance is not affected by whether or not the insurer enters into any other contracts. However, the diversification of risk across many contracts may result in the insurer being required to hold a lower amount of reserves against its future liabilities under each contract, so insurers will generally try to achieve such diversification.

6.2 There is an exclusion from the requirement to be authorized as an insurance intermediary where the insurance mediation activities are carried on in relation to a "large risks contract of insurance" where the risk is situated outside of the EEA (see Article 72D of the Regulated Activities Order SI 2001/544) ("Regulated Activities Order 2001")). However, this does not affect the interpretation of that contract as a contract of insurance; it merely affects the authorization requirements of the intermediary performing activities in relation to that contract.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

7.1 No. The description of what constitutes a contract of insurance in the *Prudential* case applies to both life insurance and non-life insurance. However, life and non-life insurance contracts differ in their contractual characteristics. In non-life insurance contracts, the insurer will usually contract to indemnify the insured for what he or she may actually lose and therefore on the happening of certain events of loss, the insurers' liability will arise. Life insurance in contrast is a contract of contingency insurance where the insurer undertakes to pay out on the occurrence of an event regardless of the loss of the insured.

7.2 Furthermore, the timing required for the insurable interest under the policy differs slightly between life and non-life insurance contracts. For a life insurance policy, the policyholder must have an insurable interest at the date of the policy (otherwise the policy is illegal) but not necessarily thereafter (*Dalby v India and London Life Assurance Co. (1854) 15 CB 365*). In contrast, the assured need not possess an insurable interest at the date of creation for a non-indemnity insurance policy. The value of the policy is fixed at the outset.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Gambling contracts are regarded as distinct from insurance contracts. They are governed by the Gambling Act 2005 ("GA 2005") and are defined in Section 3 GA 2005 as contracts for gaming (playing a game of chance), betting and participating in a lottery.

Pre GA 2005, contracts for bets (or wagers) were void and unenforceable, while insurance contracts were legal. Therefore, historically, it was important to distinguish between the two. Under s 335 GA 2005, lawful gambling contracts are now enforceable but the distinction between gambling and insurance remains.

A wager is defined as a contract in which the risk of loss is created by making the bet itself. The sole interest of each party was the stake he will win or lose (*Carlill v Carbolic Smoke Ball Co. Ltd. [1892] 2 QB 484*). Comparatively, a contract of insurance is described as protecting the assured from a risk of loss to an interest he possesses independently of the conclusion of the insurance contract (*Wilson v Jones (1867) LR 2 Ex 139*). Therefore, the existence or otherwise of an insurable interest is the key difference between a gambling and insurance contract.

As gambling contracts are not a type of insurance contract, they are not subject to the regulatory regime under the Financial Services and Markets Act 2000 ("FSMA").

ii) Warranty, guaranty or any other surety contracts

Warranty

On the face of it, providers of warranties could be said to be providing insurance as many warranties have all the attributes of an insurance contract. In its guidance, the FCA draws a distinction, however, between contracts of insurance on the one hand and manufacturers' and retailers' warranties on the other. The distinction is based on the fact that, in the case of a warranty of this type, the provider is not assuming any risk: the warranty is simply a means of the seller complying with its contractual, tortious or statutory obligations to the purchaser (as to the quality of the goods or services) which it would have in any event as a consequence of the sale. The warranty is seen as an adjunct of the contract of sale, and not as a freestanding contract of insurance.

The FCA's guidance is, therefore, that a warranty provided by a retailer or manufacturer in consideration of the purchase price of the goods or services and which is of the same nature as a seller or supplier's usual obligations as regards the quality of the goods

or services is unlikely to be an insurance obligation in substance - (PERG 6.7.8G).

The FCA is unlikely to classify a contract containing a simple manufacturer's or retailer's warranty as a contract of insurance, if the FCA is satisfied that the warranty does no more than crystallize or recognize the obligations that are of the same nature as a seller's or supplier's usual obligations as regards the quality of the goods or services – (PERG 6.7.9G).

If the seller or manufacturer assumes additional risk by extending its obligations beyond those they would have in any event as a result of the sale, then there is a risk that the FCA could classify the arrangement as insurance.

Additional issues arise in circumstances where there is (i) a separate payment for the warranty and/or (ii) where the warranty is provided by a third party (ie, it is not provided by the seller) (PERG 6.7.11(1)G). These could both be indicators of a contract of insurance.

Third parties do not owe existing duties to the customer (in connection with the sale) and therefore if they provide the warranty they assume risk to which they would not otherwise be subject. This can be the case even when the third party is part of the same group as the seller or manufacturer – (PERG 6.7.13G).

Extended warranties are also at risk of being classified as insurance because they extend the usual obligations of a seller or a manufacturer in terms of scope, content or duration – (PERG 6.7.11(2)G).

<u>Guaranty and surety contracts</u>

Surety contracts are to be distinguished from insurance contracts. A surety contract promises to see that the debtor's obligation is performed; whereas an insurance contract promises to indemnify the insured if the debtor fails to perform his obligation (*Moschi v Lep Aire Services Ltd [1973] AC 331*). The insurer has an independent obligation to pay a new debt that may differ from the original debt in amount and timing.

It can be difficult to distinguish between a guaranty and insurance contract as the difference is circumstantial. The case of *Seaton v Heath [1899] 1 QB 782* provides helpful indicators:

i) Motive of Parties

An insurer is likely to write the business for money, whereas a guarantor will undertake the responsibility through a private arrangement for perhaps no consideration.

ii) Manner of Dealings

An insurer often deals with an insured, through a broker, rather than directly with the debtor. A surety is often approached by the principal debtor directly.

iii) Means of Knowledge

Insurance is subject to the duty of utmost good faith and the insurer relies on the insured to disclose all the material facts. A surety will usually be aware of the risks he is assuming.

Guarantees and insurance contracts may be distinguished by examining their effect, construction and terms. It is an important distinction to make because of the following reasons:

iv) A guaranty must be evidenced in signed writing (s 4 Statute of Frauds 1677), whereas a contract for non-marine insurance can be made orally;

v) Unlike an insurance contract, a guaranty is void or discharged if the corresponding principal debt is void or discharged;

vi) A guarantor who pays out has a right of action against the debtor in their own name. Whereas following payment, an insurer is merely entitled to be subrogated to the rights of the insured;

vii) The court will usually construe a guaranty against the creditor and insurance in favor of cover; and

viii) Unlike an insurance contract, providing a guaranty is not a regulated activity and is therefore not subject to the FSMA regulatory regime.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts are distinct from insurance contracts.

As discussed above, insurance contracts protect against the risk of loss for an insurable interest. Financial contracts differ from insurance contracts in that:

i) The payment obligation is not conditional on the payee sustaining loss; and

ii) They do not seek to protect an insurable interest.

Where the contract provides for payment whether or not loss occurs and irrespective of the risk of loss, it is not a contract of insurance. The addition of an element of pure risk may also be enough to distinguish financial contracts (or investments) from insurance.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

No. Please see above for all relevant exceptions.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

10.1 The classification of a contract as a contract of insurance does not provide for an exception arising from a close legal or

economic nexus of that contract to a non-insurance transaction.

10.2 However, depending on the circumstances it may be possible avoid a contract of insurance arising by the use of a waiver term in a non-insurance contract, instead of a collateral contract of insurance.

10.3 A contractual waiver is a term of a non-insurance agreement, for example a loan agreement or a hire agreement. The waiver term may be optional and, if so, may involve an additional cost for the customer. The waiver term will stipulate that all or part of the customer's obligations under the contract (for example an obligation to make a repayment on the loan or an obligation to pay for any damage to the hire vehicle/equipment) is waived (often upon the occurrence of an uncertain event, for example in the case of a loan waiver term upon accident, sickness or involuntary unemployment of the customer).

10.4 The agreement on the part of the contracting party, such as the bank or hire company, to waive an obligation is not a contract of insurance. Rather it is a variation of the customer's contractual terms. As such an arrangement would not involve an insurance company, save that it would of course be possible for the contracting party (ie the bank or hire company) to insure against the risk of the waiver being invoked by a customer.

Impact of Qualification – Supervisory law

Insurance companies are dual regulated in the UK. The Prudential Regulation Authority ("PRA") is responsible for the authorization and prudential regulation of insurers, while the Financial Conduct Authority ("FCA") is responsible for ensuring good market conduct.

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

11.1 Yes. Section 19 of FSMA provides for a "general prohibition" which states that no person may carry on a regulated activity unless they are authorized or exempt. Entering into a contract of insurance as risk carrier would constitute the regulated activity of effecting and carrying out contracts of insurance as principal (Article 10(1) and (2) Regulated Activities Order 2001).

11.2 "Effecting" contracts of insurance has been taken to include the preparatory process of negotiating insurance business as well as the confirmation of cover *(Stewart v The Oriental Fire and Marine Insurance Company Ltd [1985] QB 988)*. Whereas "carrying out" insurance covers activities after the insurance contract has been made, such as premium collection, claims handling and settlement and payment of claims *(Stewart, Scher v Policyholders Protection Board [1994] 2 AC 57)*.

11.3 Therefore, unless one of the limited exclusions apply (for which see articles 11 and 12 of the Regulated Activities Order 2001), authorization from the PRA as an insurer is necessary in order to enter into an insurance contract as principal. It is not possible to become exempt by becoming an Appointed Representative for the activity of effecting and carrying out contracts of insurance (see the FCA's guidance in SUP 12.2.7G). Before granting authorization, the PRA must also obtain the consent of the FCA. Insurers must take care to comply with the regulations for both the PRA and FCA.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

12.1 It is a criminal offence for an unauthorized person to perform a regulated activity without permission (see s 23 FSMA). This could result in (1) 6 months imprisonment or a GBP 5,000 fine on summary conviction; or (2) two years imprisonment and/or a fine on conviction on indictment.

12.2 It is a statutory breach for an authorized person to perform a regulated activity for which it does not have permission (see s 20 FSMA). This could result in disciplinary action by the PRA and/or the FCA.

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

Yes. Insurers cannot carry on any commercial business other than insurance and activities directly arising from that business (see Rule 1.5.13 of the Prudential Sourcebook for Insurers ("INSPRU")).

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

No. Currently, FCA pre-approval is not required for an insurance product, however the FCA will scrutinize an insurer's product governance by looking at how the product is designed, operates and sold. The FCA has powers to make product intervention rules to prevent harm to customers.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

15.1 Where the contract of insurance is effected by an authorized person whose permissions do not include effecting and carrying out contracts of insurance, the contract is not void or unenforceable except in specified situations. In certain prescribed situations the contravention is actionable by a person who suffers loss as a result, subject to the defenses applicable to actions for breach of statutory duty (s 20 FSMA).

15.2 Where the contract of insurance is effected by an unauthorized person, it is unenforceable against the other party. The other party is entitled to recover any money paid under the agreement and compensation for any loss sustained as result of having parted with the premium (s 26 FSMA).

15.3 As noted above, it is a criminal offence for an unauthorized person to enter into a contract of insurance. It would be advisable for such an unauthorized person to consider whether this gives rise to any money laundering issues.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

16.1 As the legal system in England and Wales is a common law system, we do not have a comprehensive code governing insurance contract law. There are countless statutes that affect contracts of insurance. There is also a great deal of case law which has developed insurance contract law principles in this jurisdiction.

16.2 Therefore the following is a non-exhaustive list of some of the legislation which applies to the formation of insurance contracts in England and Wales:

i) Marine Insurance Act 1906; and

ii) Life Assurance Act 1774

16.3 Furthermore, the following statutes are some examples of statutes affecting the interpretation and regulation of insurance (ie by regulating the way in which insurers are permitted to operate, market and sell insurance):

i) Financial Services and Markets Act 2000; and

ii) Consumer Insurance (Disclosure and Representations) Act 2012.

16.4 The Combined FCA and PRA Handbook is another important source of regulation affecting insurers and insurance intermediaries.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

17.1 No. Neither statute nor the common law requires a contract of insurance to be in any particular form.

17.2 As described in question 1 above, the *Prudential* case describes the minimum requirements for an insurance contract, namely that the contract must specify the premium and the uncertain event regarding an insurable interest. However, there are no specific terms required. Example provisions that would normally be included in an insurance contract include:

i) Duration of risk;

ii) Rate of premium;

iii) Amount and subject matter of insurance; and

iv) The insurer's usual terms.

17.3 However, where the insurance contract is with a consumer (ie a person acting for purposes outside of his trade or profession) there are minimum content and disclosure requirements in the Insurance Conduct of Business Sourcebook ("ICOBS"), and it is a key principle that the policy (as well as any other communication with a customer) is clear, fair and not misleading.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Combined FCA and PRA Handbook

18.1 The key source of regulation with regard to contracts of insurance with consumers is ICOBS in the Handbook. This seeks to ensure that all communications are clear, fair and not misleading. It sets out the minimum information requirements required by the Distance Marketing Directive and the Electronic Commerce Directive. It also makes it mandatory for the firm to provide certain disclosures about itself, its services and its remuneration. A firm must take reasonable steps to ensure that a customer is given appropriate information about the contract of insurance in good time and in a comprehensible form so that the customer can make an informed decision about the arrangements proposed.

18.2 Furthermore, the Handbook incorporates guidance on the FCA's approach to the Unfair Terms in Consumer Contracts Regulations 1999 (SI 1999/2083), which applies to consumer contracts which have not been individually negotiated – see the Unfair Contract Terms Regulatory Guide ("UNFCOG").

Consumer Insurance (Disclosure & Representations) Act 2012

18.3 Previously, consumers were required to volunteer all material facts to insurers in accordance with the duty of utmost good faith. However, since the Consumer Insurance (Disclosure & Representations) Act 2012 came into force on 6 April 2013 consumers are no longer obliged to volunteer material facts. Instead, the onus is on the insurer to ask questions. The consumer must take reasonable care to answer the insurer's questions fairly and accurately and not to make a misrepresentation.

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

No.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

In California, insurance code ("Ins. C.") §380 defines an insurance contract as a

> "written instrument, in which a contract of insurance is set forth, is the policy."

The insurance policy is

> "an agreement by which one person for a consideration promises to pay money or its equivalent […] on the destruction, death, loss, or injury of someone or something by specified perils." *California Physicians' Serv. v. Garrison (1946) 28 C2D 790, 803-804.*

In determining whether a person is engaged in the business of insurance, California considers two tests as persuasive: the assumption of risk of loss by a party not previously exposed to it; and the existence of indemnity, rather than service, as the principal object of the subject agreement. These tests are applied on a case-by-case basis in order to determine whether the business of insurance is being transacted

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. Pursuant to Ins. C. §22, insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event.

Also, §250 states that

> "any contingent or unknown event, whether past or future, which may damnify a person having an insurable interest, or create a liability against him, may be insured against."

Insurance is designed to protect against contingent or unknown risks of harm, not risks that are certain or expected, or harm that has already occurred. *Prudential-LMI Comm'l Ins. v. Sup. Ct. (1990) 51C3d 674, 695.*

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes.

> "Essential to insurance is the element of shifting of the risk of loss, subject to contingent or future events, by legally binding agreement." *Richardson v. GAB Business Serv. Inc. (1984) 161 CA3d 519, 523*. To qualify a contract as an insurance contract courts analyze whether

> "that shifting of risk or something else to which it is related in the contract is the principal object and purpose." *Title Ins. Co. v. State Bd. of Equalization (1992) 4 C4th 715, 726.*

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Yes. Pursuant to Ins. C. §280, if the insured has no insurable interest, the contract is void. California defines an insurable interest as

> "[e]very interest in property, or any relation thereto, or liability in respect thereof, of such a nature that a contemplated peril might directly damnify the insured is an insurable interest." *(Ins. C. §281)*

Pursuant to Ins. C. §286,

> "[an] interest in property insured must exist when the insurance takes effect, and when the loss occurs, but need not exist in the meantime; and interest in the life or health of a person insured must exist when the insurance takes effect, but need not exist thereafter or when the loss occurs."

Thus, the insured must have a direct pecuniary interest in the property and must be exposed to a pecuniary loss in the event of its destruction. *Ann* Burns v. California Fair Plan, 152 Cal. App. 4th 646, *651 (Cal. Ct. App. 2007).*

Pursuant to Ins. C. §282, an insurable interest in property may be any of the following:

- An existing interest;
- An inchoate interest founded on an existing interest; or
- An expectancy, coupled with an existing interest in that out of which the expectancy arises.

The insurer is the only party who can raise the question of insurable interest. *Countrywide Home Loans, Inc. v. Tutungi (1998) 66 Cal. App. 4th 727*.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Under California law, an insurance contract is void if the insured party does not possess an insured interest. Accordingly, under California law, a third party such as a life insurance beneficiary must have an "insurable interest," meaning he/she has an

interest in the insured person remaining alive and is not entering into a transaction for the purpose of making money off the insured's death. In 2009, the California Legislature amended the state's Insurance Code to prohibit the assigning of a beneficial interest in a life insurance policy to a party without an insurable interest. California courts found that

> "[t]he purpose of California's insurable interest requirement for life insurance is to prevent third parties from purchasing insurance on a person as to whom they have no insurable interest and thereby enter into a 'wager contract' on the insured's life." *The Lincoln Life and Annuity Co. v. Jack Teren Ins. Trust, No. D056373 (Cal. Ct. App., 4th Dist., Div. 1 May 17, 2011).*

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

No. This is purely an actuarial issue. The law of large numbers is a statistical concept that relates to probability. It is one of the factors insurance companies use to determine their rates. Insurance companies use the law of large numbers to lessen their own risk of loss by pooling a large enough number of people together in an insured group.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No. Life insurance policy is defined by Insurance code §101 and is a contract obligating an insurer to pay a sum of money to a designated person(s) upon the death of another. As with insurance generally, a life insurance contract is valid if the owner has an insurable interest in the life of the insured.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Under California law, a policy executed by way of gambling or wagering is void. Insurance is distinctly different because the requirement of an insurable interest in the policy removes the policy from any definition of gambling. The purpose of the insurable interest doctrine is an attempt to control wagering, fraud, and moral hazards.

ii) Warranty, guaranty or any other surety contracts

Although it is true that "surety insurance" is defined as a class of insurance in Ins. Code § 105, surety contracts are not treated as insurance for all purposes. *Cates Cost., Inc. v. Talbot Partners (1999) 21 C4th 28, 51*. We can isolate many differences. Under a contract of suretyship, one is called upon to answer for the debt, default of another and the risk of loss remains with the principal. Another difference deals with the fact that because the surety has the right to recover from the principal, the most basic element of insurance, transfer of risk, is absent.

Surety insurance under California law includes surety bonds, Fidelity insurance, Crime insurance, Payment bonds, and Performance bonds.

iii) Financial contracts such as hedging contracts/swaps/derivatives

The basic form of credit derivative, known as a "credit default swap" (CDS), is a simple contract through which a lender can protect against the risk of default by paying premiums to a third party who agrees to compensate the lender in the event of default by the underlying borrower. The apparent similarity to typical insurance products, like property or life insurance, has caused some politicians and analysts to argue that credit derivatives are a form of insurance and should be regulated as such. But the fact that an instrument has similarities or provides insurance against loss is not enough to warrant regulating it as "insurance." Indeed, Ins. C. § 12100 (h) defines "Credit default swap" as an agreement referencing credit derivative definitions published by the International Swap and Derivatives Association, Inc., or otherwise acceptable to the commissioner, pursuant to which a party agrees to compensate another party in the event of a payment default by, insolvency of, or other adverse credit event in respect of, an issuer of a specified security or other obligation; provided that the agreement does not constitute an insurance contract and the making of the credit default swap does not constitute the transaction of insurance.

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

No. We have not identified any law that would prevent a contract that satisfies the definition of "insurance" under Ins. C. § 380 and § 381 from being treated as such.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

None.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Pursuant to Ins. C. §700, an insurer can transact a class of insurance business in California only if it has been first admitted for that class. Thus, insurance companies that seek to do business in California must apply and be reviewed by the Department of Insurance to determine whether or not they should be given the authority to sell insurance in California. Moreover, Ins. C. §680 provides that

> "[a]n insurer shall not transact any class of insurance which is not authorized by its charter."

However, Ins. C. §1760 states that

> "[a] home state insured may negotiate and effect insurance to protect himself, herself, or itself against loss, damage, or liability with any nonadmitted insurer."

Nonadmitted insurer means insurers that are not licensed the State of California (called surplus lines carriers.) Surplus line insurance policies are sold by "nonadmitted" carriers through licensed "surplus line brokers." Nonadmitted does not mean nonregulated. The only way that a nonadmitted foreign or alien insurer can transact business in California is through a California surplus line broker. An entire chapter 14 of the California Insurance Code is devoted to the subject of surplus line brokers whose business consists of placing insurance with nonadmitted insurers under certain conditions. For example, a surplus line broker may solicit and place insurance for a person whose home state is California with nonadmitted insurers only if that insurance cannot be procured from insurers that are admitted for the particular class of insurance and that actually write that particular type of insurance in California. Ins. C §1763(a). Additionally, the surplus lines broker should conduct a diligent search to establish a prima facie evidence that among admitted insurers three of them that actually write the particular type of insurance in this state have declined the risk, or that fewer than three admitted insurers actually write the particular type of insurance. Ins. C §1763(b).

In order to comply with NRRA, on 15 July 2011, Governor Brown signed AB 315 which became effective 21 July 2011. Accordingly, California updated its insurance code to be consistent with the provisions of NRRA. This included the adoption of the nonadmitted insurer eligibility requirements for California home state insureds. Under the amended Ins. Code §1765.1, a broker may place surplus line insurance for California home state insureds with eligible carriers that have met the standards set forth in that code Section.

This new law also created a List of Approved Surplus Lines Insurers (LASLI). The LASLI List contains the names of nonadmitted carriers that have been reviewed and approved by the California Department of Insurance (CDI) for surplus line insurance in California. Nonadmitted carriers on the LASLI List are actually "admitted" insurance carriers, in a state or domicile other than California. LASLI is a voluntary list and insurers may opt off the list. As a result, there may be nonadmitted insurers that are not on LASLI but pursuant to the NRRA and Ins. C. §1765.1, are nonetheless eligible for use by surplus line brokers, as long as the broker has determined at the time of placement that the insurer meets specific eligibility criteria.

12. What are the legal consequences for the risk-taker acting without license?

Transacting insurance business in California in willful violation of the licensing requirement is punishable either as a felony or a misdemeanor punishable by imprisonment in the state prison, or in a county jail not exceeding one year and/or a monetary fine of up to USD 100,000. Ins. C §700(b).

Moreover the policies issued by unlicensed insurance company are not void and insured can sue for benefit of the policy written by the unlicensed insurer. *Medina v. Safe-Guard Products, 164 CA4th 105, 110*.

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

There is an important distinction between what a regulated insurance entity can do and what an affiliate of a regulated insurance entity can do. In California, domestic insurers and reinsurers are only permitted to carry on activities that are reasonably incidental to the insurance business, whereas their non-insurer affiliates are permitted to carry on non-insurance business.

Statutes may prohibit or restrict certain activities pursued by insurance companies. Thus, some insurers are prohibited from writing more than a single type of insurance. As an example, mortgage insurers, and title insurers cannot transact any other class of insurance than that for which they are authorized (Ins. C. §12441 & §12360).

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Pursuant to the California voters' enactment of Proposition 103 in 1988, premium rates for all California property-casualty lines, except workers compensation and ocean marine, must be filed with and approved by the CDI. Ins. C. §1850.4 et seq. The elected Insurance Commissioner is required by law to reject excessive premium increases. An initiative that

should qualify for the 2014 ballot is underway to extend the pre-approval requirement to health insurance premiums. Moreover, individual long-term care insurance policy must be approved by the DOI and have all of the consumer protections required under California law.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

By statute, an insurer is a "person who undertakes to indemnify another by insurance." Ins. C. §23. Pursuant to this definition, a person issuing a contract of insurance is qualified as an insurer. Those insurers/insurance companies are required to obtain licenses from the Department of Insurance (DOI) in order to transact insurance business in California. Ins. C. §700. However, an insurance company's violation of California's licensing requirements does not void its insurance contracts. The insured can sue for benefits under a policy written by an unlicensed insurer. *Medina v. Safe-guard Products, 164 CA4th 105, 110*. Also, an insurer's violation of California's licensing requirements may be grounds an insured to rescind a policy and recover premiums paid. However, rescission requires an offer to restore benefits received under the contract. Civ. C. §1691(b). Finally, an aggrieved policyholder may sue an unlicensed insurer under the Unfair Competition Law (Bus.&Prof. C. §17200) for restitution of premiums or commissions paid.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

California law contains legal provisions applicable to the insurance contract (i.e. insurance policy) in Part 1 "The contract" at Sections 100 to 679.73.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Pursuant to Insurance code §381, A policy shall specify:

a) The parties between whom the contract is made.

b) The property or life insured.

c) The interest of the insured in property insured, if he is not the absolute owner thereof.

d) The risks insured against.

e) The period during which the insurance is to continue.

f) Either:

i) A statement of the premium, or

ii) If the insurance is of a character where the exact premium is only determinable upon the termination of the contract, a statement of the basis and rates upon which the final premium is to be determined and paid.

Pursuant to Ins. C. §386, an insurance policy must bear the signature of the insurance company president or vice president, or, on their absence, any two directors, and must be countersigned by the corporate secretary.

In some cases, statutory definition of terms may be read into an insurance contract or may supersede conflicting definitions (e.g. definition of cause of loss – Ins. C. §530.)

Additionally, some statutes limit the coverage that may be provided by insurance policies:

- No coverage for future unlawful act – Civil C. §2773;
- No waiver of insurable interest requirements – Ins. C. §287;
- No coverage for willful acts – Ins. C §533;
- No coverage for the payment of fine or penalties – Ins. C. §533.5(a);
- No duty to defend criminal actions or in false advertising or unfair competition proceedings in which fine are sought by the Attorney General or any district attorney, county counsel, or city prosecutor – Ins. C §533.5(b).

Finally, statutes may regulate the content of certain types of group insurance such as group life insurance (Ins. C. §10202-10209), group disability insurance (Ins. C. §10270), and group health insurance (Ins. C. §10125).

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Certain coverage terms and conditions are mandated by law for consumer protection such as for fire insurance (California Standard Form Fire Insurance Policy – Ins. C. §2071), disability insurance (Ins. C. §10350-10350.12), liability insurance (Ins. C. §11580(b)(2)), automobile insurance (insured may waive or limit uninsured motorist benefits in an automobile insurance policy only in writing and signed by the name insured – Ins. C. §11580.2(a)(3)), and worker compensation coverage for household employees in personal liability insurance (Ins. C. §11590-11593)

Where a policy provision is mandated by statute, policies that do not contain the required provision will be enforced as if they did.

Statutes may require in some instance that policies contain a special notice of restriction or limitation of coverage (e.g. professional liability insurance policies written on claims-made basis – Ins. C. §11580.01).

Consumers are also protected by the Fair Claims Settlement Practices regulations (Ins. C. §790.03(h)). Ins. C. § 2695.4 provides that

> "[e]very insurer shall disclose to a first party claimant or beneficiary, all benefits, coverage, time limits or other provisions of any insurance policy issued by that insurer that may apply to the claim presented by the claimant."

19. <u>Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?</u>

None.

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Definition of an Insurance Contract

1. <u>Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.</u>

Yes. Under Conn. Gen. Stat. § 38a-1(10), "insurance" means "any agreement to pay a sum of money, provide services or any other thing of value on the happening of a particular event or contingency or to provide indemnity for loss in respect to a specified subject by specified perils in return for a consideration." Conn. Gen. Stat. § 38a-1(10) further provides that

> "[i]n any contract of insurance, an insured shall have an interest which is subject to a risk of loss through destruction or impairment of that interest, which risk is assumed by the insurer and such assumption shall be part of a general scheme to distribute losses among a large group of persons bearing similar risks in return for a ratable contribution or other consideration."

This definition is an apparent codification of the Supreme Court of Connecticut's definition of "insurance" in *Day v. Walsh*, 132 Conn. 5, 11 n.1 (1945). There, the Supreme Court of Connecticut stated that a contract of insurance is distinguishable by the presence of the following five elements:

i) The insured possesses an interest of some kind susceptible of pecuniary estimation, known as an insurable interest;

ii) The insured is subject to a risk of loss through the destruction or impairment of that interest by the happening of designated perils;

iii) The insurer assumes that risk of loss;

iv) Such assumption is part of a general scheme to distribute actual losses among a large group of persons bearing similar risks; and

v) As consideration for the insurer's promise, the insured makes a ratable contribution to a general insurance fund, called a premium.

Day v. Walsh, 132 Conn. 5, n.1 (1945); *see also Golf Mktg. Worldwide, LLC v. State Ins. Dep't,* 2004 Conn. Super. LEXIS 926 *9 (Conn. Super. Ct. 2004).

2. <u>Does an insurance contract require an element of uncertainty? Please describe.</u>

Yes. Connecticut courts have recognized that one of the primary axioms of insurance is that it is intended to cover only the risk of unknown loss. *Maher & Williams v. Ace Am. Ins. Co.*, 2010 U.S. Dist. LEXIS 91934 *41 (D. Conn. 2010), *citing* Lawyers Professional Liability: A Primer on Prior Knowledge, 30 The Brief 29, 35 (Fall 2000).

> "Insurance policies cover only those losses that are caused by 'fortuitous' events . . . insurance is not available for losses that the policyholder knows of, planned, intended, or is aware are substantially certain to occur." *Sports Domain, LLC v. Max Specialty Ins. Co.*, 2011 Conn. Super. LEXIS 3187 *8 (Conn. Super. Ct. 2011); see also *Eisenhandler v. Twin City Fire Ins. Co.*, 2011 Conn. Super. LEXIS 2694 *10 (Conn. Super. Ct. 2011) ("one may not obtain insurance for a loss already in progress, or for a loss that the insured either knows of, planned, intended, or is aware is substantially certain to occur.")

3. <u>Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?</u>

Yes. Conn. Gen. Stat. § 38a-1(10) provides that

> "[i]n any contract of insurance, an insured shall have an interest which is subject to a risk of loss through destruction or impairment of that interest, which risk is assumed by the insurer . . ."

The Supreme Court of Connecticut has determined that under Conn. Gen. Stat. § 38a-1(10), insurance is "the assumption of another's risk for profit." *Doucette v. Pomes, 247 Conn. 442, 456 (1999).* Further, Connecticut courts have acknowledged that the transfer of risk is generally considered to be an "essential element" of an insurance relationship. *Esposito v. Simkins Indus.*, 286 Conn. 319, 334 (2008) ("[the] transfer of risk . . . is generally considered to be an essential element of an insurance relationship"), *citing Doucette v. Pomes*, 247 Conn. at 459 (1999); *see also Orthopaedic Specialty Group P.C. v. Pentec, Inc.*, 2011 Conn. Super. LEXIS 2383 *23 (Conn. Super. Ct. 2011) ("a policy of insurance transfers all or a portion of a loss exposure to an insurance company in exchange for a premium"); *Golf Mktg. Worldwide, LLC v. State Ins. Dep't*, 2004 Conn. Super. LEXIS 926 *13-14 (Conn. Super. Ct. 2004) (insurer's assumption of insured's risk in return for compensation is the "essence" of an insurance transaction).

4. <u>Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?</u>

Yes. Conn. Gen. Stat. §38a-1(10) provides, in pertinent part:

> "[i]n any contract of insurance, an insured shall have an interest which is subject to a risk of loss through destruction or impairment

> of that interest . . ." Conn. Gen. Stat. §38a-1(10); *see also Calabrese v. New London County Mut. Ins. Co.*, 1997 Conn. Super. LEXIS 3147 *4 (Conn. Super. Ct. 1997) ("It is now almost universally held . . . that an insurable interest is necessary to the validity of a policy, no matter what may be the subject matter, and that if no insurable interest exists, the contract is void"), *citing* 3 G. Couch, Insurance (2d Ed. 1984) 24:1, p. 8; *accord McLaughlin v. Am. Empire Ins. Co.*, 1992 Conn. Super. LEXIS 2808 *9 (Conn. Super. Ct. 1992) ("public policy requires the existence of an insurable interest in order to prevent fraud and to avoid the making of wagering contracts where there is no actual economic interest in the subject which the law recognizes").

Under Connecticut law, any person has an insurable interest in property "by the existence of which he receives a benefit, or by the destruction of which he will suffer a loss," whether or not he has any title in, or lien upon, or possession of the property itself. *Calabrese v. New London County Mut. Ins. Co.*, 1997 Conn. Super. LEXIS 3147 *4 (Conn. Super. Ct. 1997), *quoting Plum Trees Lime Co. v. Keeler*, 92 Conn. 1, 7 (1917). To ascertain whether a party possesses an insurable interest, the crucial question is whether the insured will be directly and financially affected by the loss of the property insured. *Plum Trees Lime Co. v. Keeler*, 92 Conn. at 8 (1917). According to the Supreme Court of Connecticut,

> "[t]he loss must not be indirect or sentimental, but direct and actual…. This opens a wide field and the decisions take an extensive range with a growing tendency to expand rather than to contract the scope of the term." *Id.*

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Under Connecticut law, a policyholder must possess an insurable interest. Conn. Gen. Stat. §38a-1(10); *see also Calabrese v. New London County Mut. Ins. Co.*, 1997 Conn. Super. LEXIS 3147 *4 (Conn. Super. Ct. 1997). A policy may benefit a third party who lacks an insurable interest in the subject matter of the insurance if the insurance contract is made in good faith. See, e.g., Allen v. Hartford Life Ins. Co., 72 Conn. 693, 696 (1900) (while an insured may take out a life insurance policy intending to benefit a third party who lacks an insurable interest in the life of the insured, such action must be taken in good faith; in the absence of good faith, such contract amounts to a mere device that enables the payee to speculate upon the hazard of the life insured, and is void as against public policy); *accord PHL Variable Ins. Co. v. Charter Oak Trust*, 2012 Conn. Super. LEXIS 1218 *18 (Conn. Super. Ct. 2012).

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

Yes. Conn. Gen. Stat. § 38a-1(10) provides that

> "[i]n any contract of insurance, an insured shall have an interest which is subject to a risk of loss through destruction or impairment of that interest, which risk is assumed by the insurer and such assumption shall be part of a general scheme to distribute losses among a large group of persons bearing similar risks . . ."

The Supreme Court of Connecticut has stated that an insurer's assumption of risk, as part of a general scheme to distribute actual losses among a large group of persons bearing similar risks, is a necessary element of insurance that distinguishes insurance contracts from other somewhat similar transactions. *Day v. Walsh*, 132 Conn. 5, 12 (1945).

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No. Under Conn. Gen. Stat. § 38a-1, "life insurance" is defined as "insurance on human lives and insurances pertaining to or connected with human life." Connecticut courts have applied the requirements of Conn. Gen. Stat. § 38a-1(10), which defines "insurance," to life insurance contracts. *See, e.g., PHL Variable Ins. Co. v. Charter Oak Trust*, 2012 Conn. Super. LEXIS 1218 *14 (Conn. Super. Ct. 2012); *see also Day v. Walsh*, 132 Conn. 5, 12 (1945).

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Insurance contracts and contracts of gambling both involve wagering. However, a contract of insurance is distinguishable from a contract of gambling or chance because an insurance contract requires that an insured have an insurable interest in the matter insured. Conn. Gen. Stat. §38a-1(10); *see also Calabrese v. New London County Mut. Ins. Co.*, 1997

Conn. Super. LEXIS 3147 *4 (Conn. Super. Ct. 1997). Where the insured does not possess an insurable interest in the matter insured, the policy is merely a wager policy, and is void as against public policy. *Fuller v. Metro. Life Ins. Co.*, 70 Conn. 647, 675 (1898); *PHL Variable Ins. Co. v. Charter Oak Trust*, 2012 Conn. Super. LEXIS 1218 *15-16 (Conn. Super. Ct. 2012) ("[i]t is generally agreed that mere wager policies, that is, policies in which the insured party has no interest whatever in the matter insured, but only an interest in its loss or destruction, are void, as against public policy"), *citing Connecticut Mut. Life Ins. Co. v. Schaefer*, 94 U.S. 457, 460 (1877).

ii) Warranty, guaranty or any other surety contracts

Connecticut courts have recognized that there are common law differences between surety contracts and contracts of insurance. *Travelers Cas. v. F&F Mech. Contrs., Inc.*, 2001 Conn. Super. LEXIS 1283 *9 (Conn. Super. Ct. 2001); *Blakeslee Arpaia Chapman, Inc. v. U.S. Fid. and Guar. Co.*, 11 Conn. L. Rptr. 169, 8 (Conn. Super. Ct. 1994). First, the presence of a third party in a surety contract creates a basic difference from insurance contracts. A tripartite relationship

> "is always present in a surety contract, while an insurance contract in itself never creates a tripartite relation analogous to the suretyship relation." *Blakeslee Arpaia Chapman, Inc.*, 11 Conn. L. Rptr. 169, 8 (Conn. Super. Ct. 1994), *quoting Meyer v. Bldg. & Realty Serv. Co., 209 Ind. 125, 133 (1935)*. Second, in the context of a surety bond, the premium is usually paid by the principal, although the obligee is the party receiving the protection of the bond. *Id.* Finally, unlike in the usual insurance context, a party who purchases a performance or payment bond does not do so to protect himself from a loss. Id. Therefore, although surety contracts are sometimes treated as a form of insurance, these differences distinguish such surety contracts from contracts of insurance and necessitate caution in applying the rules of insurance. *Id.*

iii) Financial contracts such as hedging contracts/swaps/derivatives

Under Connecticut law, an insured must have an "insurable interest" in the subject of an agreement to render the agreement an "insurance contract." Conn. Gen. Stat. §38a-1(10); *see also Calabrese v. New London County Mut. Ins. Co.*, 1997 Conn. Super. LEXIS 3147 *4 (Conn. Super. Ct. 1997). Hedging contracts, swap agreements and other financial contracts share some similarities with insurance contracts. *See, e.g., Pursuit Partners, LLC v. UBS AG*, 2009 Conn. Super. LEXIS 2313 *22-23 (Conn. Super. Ct. 2009) ("At its most basic, a credit default swap is similar to an insurance contract. . . . [t]he swap provides the buyer with protection and coverage against specific risks in exchange for a periodic fee paid to the counterparty who 'buys' that risk"). However, such financial contracts generally do not require that the buyer have an interest in the subject matter of the contract that could be adversely affected by the occurrence of a specified event. Indeed, such financial contracts generally do not require that the buyer have any interest in the subject matter of the contract whatsoever. We have not identified any Connecticut statute, regulation or case law that directly addresses whether such contracts constitute contracts of insurance within the meaning of Conn. Gen. Stat. §38a-1(10). However, because Connecticut law requires that an insured possess an "insurable interest" in the subject of an insurance contract, it does not appear that most financial contracts would constitute contracts of insurance.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

We have not identified any law that would prevent a contract that satisfies the definition of "insurance" under Conn. Gen. Stat. § 38a-1(10) from being treated as such.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

Not applicable.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

In general, under Connecticut law, an insurance company may not carry out any insurance business, including the making of any insurance contracts, until it has obtained a license issued by the Insurance Commissioner of the State of Connecticut. Conn. Gen. Stat. §§ 38a-41(a); 38a-271(a). To obtain a license, an insurance company must make an application to the Commissioner setting forth the line or lines of business that it seeks authorization to write. Conn. Gen. Stat. §§ 38a-41(a). An insurance company's application must also include: (1) a certified copy of the insurer's charter or articles of association; (2) evidence that the insurer has complied with the laws of the jurisdiction under which it is organized; (3) a statement of its financial condition; and (4) evidence of good management in such form as is required by the Commissioner. *Id.* An applicant must also demonstrate an orderly pattern of growth in its marketing territories in the geographic region and an expertise in marketing and servicing the lines of insurance it desires to write. Finally, it must submit evidence of its ability to provide timely claims settlement. Id.; *see also* Regs., Conn. State Agencies § 38a-41-3 (setting forth detailed requirements for an

application for license to transact insurance business in Connecticut). If the information furnished is satisfactory to the Commissioner and the insurer has complied with all other requirements of the law, the Commissioner may issue a license to the insurance company permitting it to do business in Connecticut. *Id*.

Surplus lines insurance presents an exception to the general rule requiring licensure in Connecticut. Pursuant to Conn. Gen. Stat. § 38a-741(a), the Commissioner maintains a list of those lines of insurance for which coverage is generally unavailable from licensed insurers in Connecticut. Under Conn. Gen. Stat. § 38a-794(a), a licensed insurance producer in Connecticut may apply for and obtain a surplus lines broker's license, pursuant to which the producer may procure insurance policies from insurers not authorized to transact business in Connecticut where such coverage cannot can be placed through licensed insurers in the Connecticut market.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

Conn. Gen. Stat. § 38a-278 provides for the imposition of penal sanctions under certain circumstances. Under Conn. Gen. Stat. § 38a-278(a),

> "[a]ny unauthorized insurer who does any act of an insurance business as set forth in [Conn. Gen. Stat.] Section 38a-271 shall be fined not more than fifty thousand dollars."

Conn. Gen. Stat. § 38a-271 provides, in relevant part:

> Unless otherwise indicated, as used in Sections 38a-27, and 38a-271 to 38a-278, inclusive, "insurer" includes all corporations, . . . and individuals engaged as principals in the business of insurance . . . Any of the following acts effected in this state by mail or otherwise is defined to be doing an insurance business in this state: (1) The making of or proposing to make, as an insurer, an insurance contract; . . . (3) the taking or receiving of any application for insurance; (4) the receiving or collection of any premium . . .; (5) the issuance or delivery of contracts of insurance to residents of this state or to persons authorized to do business in this state; . . .

Conn. Gen. Stat. § 38a-271(a). Conn. Gen. Stat. § 38a-272 provides that

> "[n]o person or insurer shall directly or indirectly do any of the acts of an insurance business set forth in subSection (a) of [Conn. Gen. Stat.] Section 38a-271 except as authorized by the general statutes."

As discussed above, Conn. Gen. Stat. § 38a-41(a) requires that an insurance company must obtain a license from the Insurance Commissioner of the State of Connecticut before conducting any insurance business. Accordingly, an insurer that issues an insurance contract without a license will be subject to a fine up to USD 50,000 under Conn. Gen. Stat. § 38a-278(a).

Further, Conn. Gen. Stat. § 38a-278(b) provides that in addition to the penalty provided in Conn. Gen. Stat. § 38a-278(a), any insurer violating Conn. Gen. Stat. §§ 38a-27 or 38a-271 to 38a-278

> "shall be fined two thousand five hundred dollars for the first offense and an additional two thousand five hundred dollars for each month during which any such person or insurer continues such violation." *See Golf Mktg. Worldwide, LLC v. State Ins. Dep't*, 2004 Conn. Super. LEXIS 926 *11 (Conn. Super. Ct. 2004) (where golf marketing company and its president contracted to assume a sponsor's risk that a golfer would have a hole-in-one at the sponsor's event in exchange for the payment of a premium without a license to issue insurance, company and its president engaged in unauthorized insurance activities in violation of Conn. Gen. Stat. §§ 38a-272 and 38a-271 and were properly fined pursuant to Conn. Gen. Stat. § 38a-278(a) and (b)).

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

It does not appear that Connecticut law prohibits a licensed insurance company from entering into non-insurance business. Con. Gen. Stat. § 38a-271, which sets forth the activities included in the definition of an "insurance business," specifically includes "any other transactions of business in this state by an insurer." Con. Gen. Stat. § 38a-271(8). Although Conn. Gen. Stat. § 38a-41 imposes limitations on the type of insurance in which certain insurers may engage, it does not include any prohibition against transacting non-insurance business.

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

Connecticut law requires that most types of insurance contracts be filed with and approved by the Insurance Commissioner of the State of Connecticut prior to issuance. Conn. Gen. Stat. § 38a-676(c), for example, requires that the form of any insurance policy or contract that is subject to Conn. Gen. Stat. §§38a-663 to 38a-696, which includes most types of property and casualty insurance, be filed with the Commissioner prior to issuance. The specific procedures to be followed by any insurer that is

required to file a copy of a form pursuant to Conn. Gen. Stat. § 38a-676 are set forth under Regs., Conn. State Agencies § 38a-676-2. Under Regs., Conn. State Agencies § 38a-676-3(c), the Insurance Department must review and either approve or disapprove such a form within thirty days after it is accepted for review.

Likewise, Conn. Gen. Stat. § 38a-430(a) provides that no life insurance policy may be delivered or issued for delivery until a copy of the applicable form has been filed with and approved by the Commissioner. Section 38a-430-2 of the Regulations of Connecticut State Agencies sets forth the specific procedures to be followed by an insurer that is required to file a copy of a form pursuant to Conn. Gen. Stat. § 38a-430. Under Regs., Conn. State Agencies § 38a-430-3(c), the Insurance Department must review and either approve or disapprove such a form within seventy-five days after it is accepted for review. Finally, health insurance policy forms must also be filed with and approved by the Commissioner prior to issuance pursuant to Conn. Gen. Stat. § 38a-481(a). The specific procedures to be followed by any insurer that is required to file a copy of a form pursuant to Conn. Gen. Stat. §§ 38a-481(a) are set forth under Regs., Conn. State Agencies § 38a-481-2. Under Regs., Conn. State Agencies §§ 38a-481-3(c), the Insurance Department must review and either approve or disapprove such a form within seventy-five days after it is accepted for review.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Under Conn. Gen. Stat. §38a-275, an insurance policy issued by an unlicensed insurer would be unenforceable by the insurer. *See* Conn. Gen. Stat. § 38a-275 ("any contract . . . entered into by an unauthorized insurer in violation of [Conn. Gen. Stat.] Sections 38a-27 and 38a-271 to 38a-278, inclusive, shall be unenforceable by such insurer"); *see also* Conn. Gen. Stat. § 38a-272 ("[n]o person or insurer shall directly or indirectly do any of the acts of an insurance business set forth in subSection (a) of [Conn. Gen. Stat.] Section 38a-271 except as authorized by the general statutes");

Conn. Gen. Stat. § 38a-41(a) (in order to conduct any insurance business, an insurance company must obtain a license from the Insurance Commissioner of the State of Connecticut). However, at least one Connecticut trial court has held that even where an insurance policy is issued by an unlicensed insurer, it is nonetheless a legal contract if both parties are willing to be bound by it. *Travelers Cas. & Sur. Co. v. Didato*, 2008 Conn. Super. LEXIS 2468, *6-7 (Conn. Super. Ct. 2008).

Conn. Gen. Stat. § 38a-275 further states that if an unauthorized insurer fails to pay any claim or loss within the provisions of an insurance contract,

> "any person who assisted or in any manner aided directly or indirectly in the procurement of such insurance contract shall be liable to the insured for the full amount of such claim or loss pursuant to the provisions of such insurance contract."

In *Trez v. Int'l Water Safety Found.*, 2010 Conn. Super. LEXIS 1574 (Conn. Super. Ct. 2010), an insurance agency and insurance agent procured insurance for an insured with an insurance carrier not licensed to do business in Connecticut. The court found that so long as the insured's loss was "within the provisions" of the insurance policy, Conn. Gen. Stat. § 38a-275 provided authority for a claim by the insured against the agent and agency for damages. Id. at *5. In reaching its decision, the court explained that under Connecticut law, the agents had an obligation to place the business of a prospective insured with insurance companies licensed to do business in Connecticut. *Id.* at *13-14.

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes. The Connecticut Insurance Code is codified at Conn. Gen. Stat. § 38a-1 et seq. The Connecticut Insurance Regulations are codified in the Regulations of Connecticut State Agencies at § 38a-8-1 *et seq.*

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Yes. The Connecticut legislature has enacted the Insurance Plain Language Act, Conn. Gen. Stat. § 38a-295 et seq. The Insurance Plain Language Act generally provides that insurance policies must be printed using a 10-point type, at minimum, and must conform to certain height and style requirements set forth under Regs., Conn. State Agencies §§ 38a-297-3 and 38a-297-4. In addition, policy forms for automobile, dwelling, life and health insurance must conform to other "readability" requirements, including: (i) the use of Section titles captioned in boldface type or which otherwise stand out significantly from the text; (ii) the avoidance of unnecessarily long, complicated or obscure words, sentences or paragraphs; and (iii) the inclusion of a table of contents or an index of the principal Sections of the policy if the policy exceeds three pages or three thousand words. Conn. Gen. Stat. § 38a-297(a); Conn. Gen. Stat. § 38a-299(a).

Several Sections of the Connecticut Insurance Code and Connecticut Insurance Regulations set forth additional requirements as to the form and content of certain types of insurance contracts. Conn. Gen. Stat. § 38a-307, for example, sets forth the standard form

of fire insurance policy in Connecticut. Section 38a-334-1 of the Regulations of Connecticut State Agencies describes required areas of coverage in automobile liability insurance policies. With respect to health insurance policies, Conn. Gen. Stat. § 38a-482 sets forth a number of requirements to which insurers must adhere, including that such policies must: (i) set forth the exceptions and reductions of indemnity, either with the provision to which they apply or under a caption such as "EXCEPTIONS" or "EXCEPTIONS AND REDUCTIONS"; (ii) identify each form, including riders and endorsements, by a form number in the lower left-hand corner of the first page thereof; and (iii) purport to insure only one person, except in limited circumstances. Section 38a-327-3, finally, sets forth a number of minimum standards applicable to claims-made liability insurance policies.

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes. The Connecticut Unfair Insurance Practices Act, Conn. Gen. Stat. § 38a-815 et seq. (CUIPA), prohibits unfair methods of competition and unfair or deceptive acts or practices in the business of insurance. Under Conn. Gen. Stat. § 38a-816, “unfair methods of competition” and “unfair and deceptive acts or practices” in the business of insurance include conduct such as: (i) misrepresenting the benefits, advantages, conditions or terms of any insurance policy; (ii) committing any act of boycott, coercion or intimidation resulting in the unreasonable restraint of, or monopoly in, the business of insurance; and (iii) engaging in unfair claim settlement practices, including failing to adopt and implement reasonable standards for the prompt investigation of claims and misrepresenting pertinent facts or insurance policy provisions relating to coverages at issue. Conn. Gen. Stat. § 38a-816(1), (4), (6). Under CUIPA, the Insurance Commissioner of the State of Connecticut may conduct hearings into violations of CUIPA and order an insurer to cease and desist as well as to pay a monetary penalty. Conn. Gen. Stat. § 38a-817. The Commissioner may order payment of a fine of not more than USD 5,000 for each act or violation but not to exceed an aggregate penalty of USD 50,000, unless the insurer knew or reasonably should have known that it was in violation of CUIPA. Conn. Gen. Stat. § 38a-817(b). The Commissioner may also suspend or revoke an insurer’s license and order restitution of any sums shown to have been obtained by an insurer in violation of CUIPA. *Id.*

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Most federal and Connecticut state courts have determined that the Connecticut Unfair Insurance Practices Act, Conn. Gen. Stat. § 38a-815 *et seq.* (CUIPA), does not provide a private cause of action. *See, e.g., Traylor v. Awwa*, 899 F. Supp. 2d 216, 226 (D. Conn. 2012) (“CUIPA does not provide a private cause of action”); *Smith v. Geico Gen. Ins. Co.*, 2009 Conn. Super. LEXIS 941 *7 (Conn. Super. Ct. 2009) (“this court joins the majority of Superior Courts in holding that CUIPA does not provide a private right of action”); *cf. Lee v. AIG Cas. Co.*, 2013 U.S. Dist. LEXIS 10579 (D. Conn. Jan. 2013) (“there is debate as to whether a private cause of [action] exists under CUIPA”), *citing Western World Ins. Co. v. Architectural Builders of Westport, LLC*, 520 F. Supp. 2d 408, 411 (D. Conn. 2007). However, the Supreme Court of Connecticut has expressly held that a violation of CUIPA may be pursued by a private party under the Connecticut Unfair Trade Practices Act, Conn. Gen. Stat. § 42-110b (CUTPA). *Mead v. Burns*, 199 Conn. 651, 663 (1986) (a “private cause of action [exists] under CUTPA to enforce alleged CUIPA violations”). To sustain a CUIPA cause of action under CUTPA, a plaintiff must allege conduct that is proscribed by CUIPA. *Nazami v. Patrons Mut. Ins. Co.*, 280 Conn. 619, 625 (2006). As discussed above, an act or practice is prohibited under CUIPA if it is

> “any trade practice which is defined in [Conn. Gen. Stat.] Section 38a-816 as, or determined pursuant to [Conn. Gen. Stat.] Sections 38a-817 and 38a-818 to be, an unfair method of competition or an unfair or deceptive act or practice in the business of insurance.” Conn. Gen. Stat. Ann. § 38a-815. Where the defendant is an insurer who has been accused of violating CUTPA through an unfair claim settlement practice, as defined in Conn. Gen. Stat. § 38a-816(6), the plaintiff must allege that the “defendant has committed the alleged wrongful acts with such frequency as to indicate a general business practice.” *Traylor v. Awwa*, 899 F. Supp. 2d 216, 226 (D. Conn. 2012), *quoting Quimby v. Kimberly Clark Corp.*, 28 Conn. App. 660, 672 (1992).

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Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

Yes. The Illinois insurance code does not contain a definition of "insurance." However, the Illinois Department of Insurance has used the common law definition enunciated in *Griffin Systems, Inc. v. Washburn,* 153 Ill. App. 3d 113 (1st Dist. 1987) to determine whether a particular product constitutes insurance. In Griffin Systems, the court adopted a four-pronged definition of insurance: (1) a contract or agreement between an insurer and an insured which exists for a specific period of time; (2) an insurable interest possessed by the insured; (3) consideration in the form of premium paid by the insured to the insurer; and (4) assumption of the risk by the insurer whereby the insurer agrees to indemnify the insured for potential pecuniary loss to the insured's property resulting from certain perils. 153 Ill. App. 3d at 116.

2. **Does an insurance contract require an element of uncertainty? Please describe.**

Yes. An insurance contract requires that a covered loss must have resulted from a "fortuitous event." *Johnson Press of America, Inc. v. Northern Ins. Co. of New York,* 339 Ill. App. 3d 864, 871 (1st Dist. 2003). "Fortuitous" means "happening by chance or accident, or occurring unexpectedly or without known cause." *Id.* at 872 (citing *Black's Law Dictionary* 664 (7th ed. 1999)). The Restatement of Contracts also defines a fortuitous event as "an event that, as far as the parties are aware, is dependent on chance." *Id.* (citing Restatement of Contracts § 291, Comment A (1932)).

The question of whether a loss was fortuitous is a legal question for a court to determine. *Id.* (citing *Mattis v. State Farm Fire & Cas. Co.,* 118 Ill. App. 3d 612, 621 (5th Dist. 1983)). "An all-risk policy covers only those losses that were actually *risked* by the parties. A loss that was, so far as the parties knew, an inevitable certainty at the time of contracting is not fortuitous and will not be covered by the resulting contract." *Id.* (citing *Crete-Monee School Dist. 201-U v. Indiana Ins. Co.,* 2000 WL 1222155 (N.D. Ill. 2000) (citing Mattis, 118 Ill. App. 3d at 621)) (emphasis in original).

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

Yes, as described in the response to question one above, an assumption of risk, or transfer of risk, is a necessary element for an insurance contract. Specifically, there must be an "assumption of the risk by the insurer whereby the insurer agrees to indemnify the insured for potential pecuniary loss to the insured's property resulting from certain perils." *Griffin Systems,* 153 Ill. App. 3d at 116. Risk is the essence of an insurance contract. *E.g., St. Paul Fire & Marine Ins. Co. v. Lefton Iron & Metal Co.,* 296 Ill. App. 3d 475, 482 (5th Dist. 1998). The United States Court of Appeals for the Seventh Circuit has noted, "[t]he essential attribute of an insurance company under Illinois law, and the attribute prompting deference to state regulation, is the assumption of a third party's risk for a premium." In re Estate of Medcare HMO, 998 F.2d 436, 445 (7th Cir. 1993).

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?**

Yes, one of the requirements for an insurance contract is an "insurable interest." *See Griffin Systems*, 153 Ill. App. 3d at 116. In order to collect under an insurance agreement, one must have an insurable interest in the insured item. *Reznick v. Home Ins. Co.,* 45 Ill. App. 3d 1058, 1060-61 (1st Dist. 1977). However, Illinois does not have a statutory definition of insurable interest and instead relies on common law. *Id.* at 1061. In *Lieberman v. Hartford Fire Ins. Co.,* 6 Ill. App. 3d 948, 949 (1st Dist. 1972), the court relied on Couch on Insurance 2d § 24:13, which explains that "[g]enerally speaking, a person has an insurable interest in property whenever he would profit by or gain some advantage by its continued existence and suffer loss or disadvantage by its destruction." This is the common law definition that most courts adhere to today. *See, e.g., Murphy v. State Farm Fire & Cas. Co.,* 978 N.E. 2d 649, 652 (1st Dist. 2012).

Further, a party may have an insurable interest in property, even if that party does not actually possess the property or even own it. *Hawkeye-Security Ins. Co. v. Reeg,* 128 Ill. App. 3d 352, 354-55 (5th Dist. 1984). "It is enough if one claiming an insurable interest holds such a relation to the property that its destruction by the peril insured against involves a pecuniary loss to him." *Id.* at 355. Courts have held that the determination of whether an insurable interest existed should be determined "at the moment of loss and should not be determined by speculating about

[1] This summary is not intended, and is not provided, as legal advice. No duty shall arise between the authors and any reader of this material.

future, uncertain events." *Murphy,* 978 N.E. 2d at 653 (citing *Miller v. New Jersey Ins. Underwriting Ass'n,* 188 N.J. Super. 175, 189 (N.J. Super. Ct. App. Div. 1983)).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

This issue arises mostly in the context of life insurance policies. Generally, a life insurance policy cannot be sold to or be procured by a person who has no insurable interest in the life of the insured. *Bajwa v. Metropolitan Life Ins. Co.,* 333 Ill. App. 3d 558, 567 (1st Dist. 2002). "Illinois law has long required that the procurer of an insurance policy on the life of another must have an insurable interest in the other's life." *Id.* (citing *Guardian Mut. Life Ins. Co. of New York v. Hogan,* 80 Ill. 35, 39 (Ill. 1875); *Hawley v. Aetna Life Ins. Co.,* 291 Ill. 28, 30 (Ill. 1919) (stating, "courts have uniformly held that one having no insurable interest in the life of another cannot procure a policy of insurance on such life, and the policy so procured is void at its inception.")).

This concept is based on public policy, "which forbids a person with no interest in the continuation of a life to obtain insurance on that life." *Id.* (citing *Colgrove v. Lowe,* 343 Ill. 360, 363 (Ill. 1931) ("Public policy forbids one person who has no interest in the continuance of the life of another from speculating on that life by procuring a policy of insurance.")).

However, "while it has long been the established law of Illinois that the purchaser of an insurance policy must have an insurable interest in the insured's life, it has also long been held that 'one may insure his own life for the benefit of another having no insurable interest therein.'" *Bajwa v. Metropolitan Life Ins. Co.,* 208 Ill.2d 414, 420 (Ill. 2004) (citing Bajwa*,* 333 Ill. App. 3d at 568). Accordingly, Illinois courts distinguish between the requirement that the policyholder have an insurable interest and a requirement that the beneficiary have an insurable interest. Bajwa, 333 Ill. App. 3d at 568 (citing Hawley, 291 Ill. at 30 ("[C]ourts have uniformly held that one having no insurable interest in the life of another cannot procure a policy of insurance on such life . . . This court has also held that one may insure his own life for the benefit of another having no insurable interest therein.") This means that under Illinois law, while there is a requirement that the individual procuring a policy must have an insurable interest, there is no requirement that the ultimate beneficiary have such an insurable interest. *Id.*

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

When determining whether a party has engaged in the business of insurance, or whether a contract at issue is a contract of insurance, Illinois courts consider the "spreading of risk" (i.e., the law of large numbers) to be a significant factor of consideration. Illinois courts have recognized that "[i]nsurance is based upon the theory of spreading risk among many policyholders." *State Farm Mut. Auto. Ins. Co. v. Fisher*, 315 Ill. App. 3d 1159, 1163 (Ill. App. Ct. 2000) (citing *Group Life & Health Ins. v. Royal Drug Co.*, 440 U.S. 205, 211 (1979)). In *Homeward Bound Servs., Inc. v. Ill. Dept. of Ins.*, 365 Ill. App. 3d 267, 277 (Ill. App. Ct. 2006), the court upheld the Illinois Department of Insurance's finding that an assisted living provider engaged in the business of insurance pursuant to its "Assisted Living Service Agreement," due in part to the provider's admission that it was able to substantially discount its services based upon the calculation that customers did not normally receive all the care that was specified in their plans (and, accordingly, the risk was spread among the customers).

As discussed further in response to Question 8, the Illinois Court of Appeals has distinguished warranties and service contracts from contracts of insurance by noting, in part, that insurance policies are based on the distribution of risk among many customers.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Life insurance contracts "involve[] the payment of stated amounts, known as premiums, by the insured over a period of years, in return for which the insurer creates an immediate estate in a fixed amount in the event of the insured's death." *In re Ellis,* 274 B.R. 782, 786 (Bkrtcy. S.D. Ill. 2002) (citing 1 John A. Appleman & Jean Appleman, Insurance Law & Practice, § 84, at 295 (1981)).

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Gambling contracts that may be valid under foreign law have not been enforced in Illinois because such contracts are contrary to Illinois public policy. *Potomac Leasing Co. v. Chuck's Pub, Inc.,* 156 Ill. App. 3d 755, 759-60 (2d Dist. 1987) (citing *Thomas v. First National Bank,* 213 Ill. 261 (Ill. 1904)). "While at one time gambling contracts in insurance were

permitted, the modern view is to the contrary. Now it is practically the uniform rule that one must have an insurable interest and a loss before one can collect on a policy of insurance. This rule is based on public policy." *Beman v. Springfield Fire & Mar. Ins. Co.,* 303 Ill. App. 554, 561 (1st Dist. 1940).

ii) Warranty, guaranty or any other surety contracts

Warranties and Service Contracts

The Illinois Court of Appeals discussed the factors distinguishing warranties, service contracts, and insurance in *Griffin Systems,* 153 Ill. App. 3d at 117-18. The court described "warranty" as a company's agreement to repair or replace a product that it sold to a customer, and a "service contract" as a company's agreement to repair or replace a product that it built. *Id.* at 117. The court noted that, for warranties and service contracts:

> No third parties are involved nor is there a risk accepted which the company, because of its expertise, is unaware of. Through a warranty or service contract, a company simply guarantees that its own product will perform adequately for a period of time.
>
> Insurance policies, on the other hand, are generally issued by third parties and are based on a theory of distributing a particular risk among many customers.

Id. at 118. The court concluded that a mechanical service contract, provided by a corporation that sold automobile parts, wherein the corporation agreed to cover repairs but did not actually make the repairs was an indemnity agreement whereby the corporation agreed to indemnify its customers for potential losses arising from the breakdown of the customer's vehicle and, therefore, was a contract of insurance. *Id.* at 119. Subsequent case law, and enactment of the Illinois Service Contract Act (see below) broadened the definition of service contract to potentially encompass any agreement to repair or replace, regardless of who manufactured or sold the product. 215 ILCS 152/5 (2013); *Morton Int'l, Inc. v. Sequa Corp.*, No. 01 C3402, 2001 WL 897562, at *2 (N.D. Ill. Aug. 8, 2001).

In 1998, Illinois enacted the Service Contract Act, 215 ILCS 152/1, *et seq.*, which provides that service contract providers complying with the Act are not subject to the Illinois Insurance Code. The Act "sets forth a statutory framework under which a service contract provider can do business in Illinois and not be treated as an insurance company." *In re Auto. Prof'ls., Inc.*, 370 B.R. 161, 168 (Bk. N.D. Ill. 2007). The Act defines a service contract as:

> … [A] contract or agreement whereby a service contract provider undertakes for a specified period of time, for separate and identifiable consideration, to perform the repair, replacement, or maintenance, or indemnification for such services, of any automobile, system, or consumer product in connection with the operational or structural failure due to a defect in materials or workmanship, or normal wear and tear, with or without additional provision for incidental payment or indemnity under limited circumstances, for related expenses, including, but not limited to, towing, rental, and emergency road service ...

215 ILCS 152/5 (2013). Service contracts may provide for services approved by the Director of Insurance, if not inconsistent with other provisions of the Act. *Id.*

Service contracts expressly covered by the Act include contracts for the repair or replacement of tires or wheels, or both, on a motor vehicle damaged as the result of coming into contact with road hazards, and the repair, replacement, or maintenance of property damage resulting from power surges and accidental damage from handling. *Id.* The Act expressly *excludes* contracts (i) of limited duration that provide for scheduled maintenance only; (ii) for fuel additives, oil additives, or other chemical products applied to the engine, transmission, or fuel system of a motor vehicle; and (iii) for the repair or replacement, or both, of damage to the interior surfaces of a vehicle, or for repair or replacement, or both, of damage to the exterior paint or finish of a vehicle, although such coverage may be offered in connection with the sale of a protective chemical, device, or system (as further described in the Act). *Id.*

To qualify, a service contract provider must have first dollar insurance coverage for its service contracts, meet certain reserve requirements, or have a net worth of at least USD 100,000,000. 215 ILCS 152/15.

Sureties and Guaranties

The transaction of the business of insurance in Illinois includes "[t]he making of or proposing to make, guarantor or surety, any contract of guaranty or suretyship as a vocation and not merely incidental to any other legitimate business of the guarantor or surety." 215 ILCS 5/121-3.

iii) Financial contracts such as hedging contracts/swaps/derivatives

Section 5/ILCS 126.31 of the Illinois Insurance Code regulates transactions in derivatives by Illinois domestic property/casualty insurance companies, among other kinds of insurers. Section 126.31 provides that an insurer may engage in derivative transactions under certain conditions. Section 126.31(A) provides that an insurer may use derivative instruments to engage in hedging transactions and certain income generation transactions, subject to certain limitations.

Derivative instrument means an agreement, option, instrument or a series or combination thereof: (a) To make or take delivery of, or assume or relinquish, a

specified amount of one or more underlying interests, or to make a cash settlement in lieu thereof; or (b) That has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests. Derivative instruments include options, warrants used in a hedging transaction and not attached to another financial instrument, caps, floors, collars, swaps, forwards, futures and any other agreements, options or instruments substantially similar thereto or any series or combination thereof and any agreements, options or instruments permitted under rules adopted under Section 126.8.

Separately, it is important to note that in 2010, the federal Dodd-Frank Wall Street Reform and Consumer Protection Act ("the Dodd-Frank Act") provided that swaps could not be subject to regulation as an insurance product by any state. PUB. L. NO. 111-203, §722(b) (2010).

9. Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?

The *Griffin Systems* holding teaches that a service contract could be recognized as insurance in Illinois. As noted by the court in *In re Auto. Prof'ls., Inc.*, 370 B.R. at 176 discussing *Griffin Systems*, "before the [Service Contract] Act was enacted, Illinois law classified service contracts as insurance contracts, so service contract providers would most likely have been considered insurers." The Service Contract Act therefore gives rise to an exception.

10. Does a close legal or economic nexus to a non-insurance transaction provide for such exception?

See specific regulation under the Service Contract Act discussed above.

Impact of Qualification – Supervisory law

11. Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?

Yes, absent a specific exemption (e.g., surplus lines, reinsurance), no person or company may transact the business of insurance, including entering into an insurance contract as the risk-taker, or insurer, unless it has received a certificate of authority from the Illinois Department of Insurance. 215 ILCS 5/24. It is unlawful for any company to enter into a contract of insurance as an insurer, or to transact insurance business in Illinois, without a certificate of authority from the Director. 215 ILCS 5/121(1).

As noted above, one of the exceptions includes surplus lines insurance, for which the Illinois Code provides specific directives, including those applicable to surplus lines producers 215 ILCS 5/445 and domestic surplus lines insurers, 215 ILCS 4/445a.

It should be noted that the Dodd-Frank Act, among other things, limits states' abilities to regulate certain types of cross-border insurance, including surplus lines. *See* PUB. L. NO. 111-203, §§ 501 et seq. Specifically, the Dodd-Frank Act changes the status quo with respect to non-admitted insurance (including surplus lines) and provides that a non-admitted insurer is only regulated by the regulator of the insured's home state: "[e]xcept as otherwise provided in this Section, the placement of non-admitted insurance shall be subject to the statutory and regulatory requirements solely of the insured's home State." 15 U.S.C. § 8202(a) (formerly at PUB. L. NO. 111-203, § 522). This Section, which became effective in July 2011, should simplify the process of providing insurance on a non-admitted basis.

12. What are the legal consequences for the risk-taker acting without license?

Any company that violates the prohibition against transacting insurance without a license as provided in 215 ILCS 5/121(1) is guilty of a business offense and

> "shall be required to pay a penalty of not less than $100 nor more than $1,000 for each offense, to be recovered in the name of the People of the State of Illinois by the State's Attorney of the county in which the violation occurs and the penalty so recovered shall be paid into the county treasury. Each day in which a violation occurs shall constitute a separate offense." 215 ILCS 5/121(3).

> "The failure of a company to obtain a certificate of authority shall not impair the validity of any act or contract of such company and shall not prevent such company from defending any action in any court of this State, but no company transacting insurance business in this State without a certificate of authority shall be permitted to maintain an action in any court of this State to enforce any right, claim or demand arising out of the transaction of such business until such company shall have obtained a certificate of authority." 215 ILCS 5/121(4).

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

As provided in the Insurance Code,

> "[n]o company shall be authorized to transact any kind or kinds of business other than those enumerated in its respective class, or classes, except as otherwise specifically provided . . . but any company, upon complying with all applicable provisions of this Code, may be authorized to transact all or any part of its business on the basis of reinsurance, except that no certificate of

> authority shall be limited in whole or in part to reinsurance unless the restriction as to such reinsurance is expressed in the articles of incorporation of said company." 215 ILCS 5/5(2).

The Code provides that "[a] domestic company may engage directly in any of the following businesses:

a) rendering investment advice;

b) rendering services related to the functions involved in the operation of its insurance business including, but not limited to, actuarial, loss prevention, safety engineering, data processing, accounting, claims, appraisal and collection services;

c) acting as administrative agent for a government instrumentality which is performing an insurance function for a health or welfare program;

d) reinsuring the business of title insurance companies, provided such domestic company if organized as a stock company shall have capital and surplus of not less than USD 5,000,000 and if organized as a domestic mutual or reciprocal company have surplus of not less than USD 5,000,000;

e) any other business activity reasonably complementary or supplementary to its insurance business; either to the extent necessarily or properly incidental to the insurance business the company is authorized to do in this State or to the extent approved by the Director . . ."

215 ILCS 5/9.

14. **<u>Do the terms and conditions of insurance contracts need to be</u>**

i) **<u>submitted to the regulator as a kind of formal requirement or</u>**

ii) **<u>approved by the regulator prior to entering into effect?</u>**

Pursuant to Illinois insurance law, all policy forms must be filed with the Director of Insurance prior to issue or delivery.

Specifically, Section 143 of the Insurance Code provides that no company transacting life, accident and health insurance may issue or deliver a policy (or certificate of insurance) or use an application blank until the

> "form and content of such policy, certificate, evidence of coverage, endorsement, rider, bylaw or other matter incorporated by reference or application blank has been filed electronically with the Director . . ." 215 ILCS 5/143(1).

The Director must then approve or disapprove the policy or form within 60 days after submission. *Id.* The Director can withhold approval if the policy or form contains provisions which

> "encourage misrepresentation or are unjust, unfair, inequitable, ambiguous, misleading, inconsistent, deceptive, contrary to law or the public policy of [Illinois], or contains exceptions and conditions that unreasonably or deceptively affect the risk purported to be assumed in the general coverage of the policy." *Id.*

All policy forms for casualty, fire and marine insurance must also be filed with the Director. 215 ILCS 5/143(2). The Director may also require that any generally used riders, endorsements, certificates, application blanks, and other matter incorporated by reference in any policy or contract be filed for approval. *Id.* In the event that the Director finds that any of the policy forms violate the Insurance Code; contain inconsistent, ambiguous, or misleading clauses; or contain exceptions and conditions that will unreasonably or deceptively affect the risks that are purported to be assumed by the policy, the Director will order the company to discontinue the use of such forms. *Id.* However,

> "[n]othing in this subSection [of the Insurance Code] shall require a company transacting [casualty, fire and marine insurance] to obtain approval of these forms before they are issued nor in any way affect the legality of any policy that has been issued and found to be in conflict with this subSection . . ." *Id.*

Additionally,

> "[n]o policy of insurance against loss or damage from the sickness, or from the bodily injury or death of the insured by accident shall be issued or delivered to any person in this State until a copy of the form thereof and of the classification of risks and the premium rates pertaining thereto have been filed with the Director." 215 ILCS 5/355.

Impact of Qualification – Law of Contracts

15. **<u>Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?</u>**

The Insurance Code provides that

> "[t]he failure of a company to obtain a certificate of authority shall not impair the validity of any act or contract of such company and shall not prevent such company from defending any action in any court of this State, but no company transacting insurance business in this State without a certificate of authority shall be permitted to maintain an action in any court

> of this State to enforce any right, claim or demand arising out of the transaction of such business until such company shall have obtained a certificate of authority." 215 ILCS 5/121(4).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes, 215 ILCS 5/1 et. seq. and ILL. ADMIN. CODE tit. 50, § 101.10 *et seq.* govern insurance generally.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

See the response to Question 14.

Credit Life Insurance and Credit Accident and Health Insurance

> "Each individual policy or group certificate of credit life insurance, and/or credit accident and health insurance shall, in addition to other requirements of law, set forth, the name and home office address of the insurer, and the identity by name or otherwise of the person or persons insured, the rate or amount of payment, if any, by the debtor separately for credit life insurance and credit accident and health insurance, a description of the amount, term and coverage including any exceptions, limitations or restrictions, and shall state that the benefits shall be paid to the creditor to reduce or extinguish the unpaid indebtedness and, wherever the amount of insurance may exceed the unpaid indebtedness, that any such excess shall be payable to a beneficiary, other than the creditor, named by the debtor or to his estate." 215 ILCS 5/155.56(b).

Accident and Health Insurance

Pursuant to 215 ILCS 5/357.1, all accident and health policies delivered or issued for delivery in Illinois must contain the provisions set forth in 215 ILCS 5/357.2 through 215 ILCS 5/357.13 in the words which appear in those specified Sections (unless alternative wording has been approved by the Director of Insurance and the alternative wording is not less favorable to the insured or beneficiary in any respect). These statutory provisions include provisions that relate to the policy constituting the entire contract (§ 357.2), a time limit on certain defenses (§ 357.3), grace periods (§ 357.4), reinstatement (§ 357.5), notice of a claim (§ 357.6), claim forms (§ 357.7), proofs of loss (§ 357.8), the time for payment of claims (§ 357.9), delay in payment of claims (§ 357.9a), payment of claims (§ 357.10), physical examinations and autopsy (§ 357.11), legal actions (§ 357.12), and change of beneficiary (§ 357.13).

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Yes, Illinois prohibits improper claims practices, which include (a) knowingly misrepresenting to claimants and insureds relevant facts or policy provisions relating to coverages at issue; (b) failing to acknowledge with reasonable promptness pertinent communications with respect to claims arising under its policies; (c) failing to adopt and implement reasonable standards for the prompt investigations and settlement of claims arising under its policies; (d) not attempting in good faith to effectuate prompt, fair and equitable settlement of claims submitted in which liability has become reasonably clear; (e) compelling policyholders to institute suits to recover amounts due under its policies by offering substantially less than the amounts ultimately recovered in suits brought by them; (f) engaging in activity which results in a disproportionate number of meritorious complaints against the insurer received by the Insurance Department; (g) engaging in activity which results in a disproportionate number of lawsuits to be filed against the insurer or its insureds by claimants; (h) refusing to pay claims without conducting a reasonable investigation based on all available information; (i) failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed; (j) attempting to settle a claim for less than the amount to which a reasonable person would believe the claimant was entitled, by reference to written or printed advertising material accompanying or made part of an application or establishing unreasonable caps or limits on paint or materials when estimating vehicle repairs; (k) attempting to settle claims on the basis of an application which was altered without notice to, or knowledge or consent of, the insured; (l) making a claims payment to a policyholder or beneficiary omitting the coverage under which each payment is being made; (m) delaying the investigation or payment of claims by requiring an insured, a claimant, or the physicians of either to submit a preliminary claim report and then requiring subsequent submission of formal proof of loss forms, resulting in the duplication of verification; (n) failing in the case of the denial of a claim or the offer of a compromise settlement to promptly provide a reasonable and accurate explanation of the basis in the insurance policy or applicable law for such denial or compromise settlement; (o) failing to provide forms necessary to present claims within 15 working days of a request with such explanations as are necessary to use them effectively; (p) failing to adopt and implement reasonable standards to verify that a repairer designated by the insurance company to provide an estimate, perform repairs, or engage in any other service in connection with an insured loss on a vehicle

is duly licensed under Section 5-301 of the Illinois Vehicle Code; (q) failing to provide as a persistent tendency a notification on any written estimate prepared by an insurance company in connection with an insured loss that Illinois law requires that vehicle repairers must be licensed in accordance with Section 5-301 of the Illinois Vehicle Code; and (r) engaging in any other acts which are in substance equivalent to any of the foregoing. 215 ILCS 5/154.6.

However, Illinois courts have held that this provision does not give rise to a private cause of action by a policyholder against an insurer, but is instead to be enforced by the Director of Insurance. *Area Erectors, Inc. v. Travelers Prop. Cas. Co. of Am.*, 981 N.E.2d 1120, 1127 (Ill. App. Ct. 2012); *American Serv. Ins. Co. v. Passarelli*, 752 N.E.2d 635, 638 (Ill. App. Ct. 2001). If a company is found, after a hearing, to have engaged in improper claims practices, the Director is required to order the company to cease such practices and has the discretion to suspend the company's certificate of authority and/or impose a civil penalty of up to USD 250,000. *See* 215 ILCS 5/154.8.

A private cause of action for policyholders does exist pursuant to 215 ILCS 5/155, which provides an extra-contractual remedy to the policyholder where there is in issue the liability of an insurer or the amount of loss payable under a policy, or an unreasonable delay in settling a claim, and it appears to the court that such action or delay is vexatious and unreasonable. See, e.g., Area Erectors, Inc., 981 N.E.2d at 1127 (noting that Section 155 was enacted by the legislature to provide a remedy to an insured who encounters difficulties when an insurer withholds policy benefits). Pursuant to this provision, a policyholder may be awarded reasonable attorneys' fees, other costs, and an amount not to exceed (1) 60 per cent of the amount the court or jury finds the policyholder is entitled to recover against the insurer; (2) USD 60,000; or (3) the excess of the amount which the court or jury finds the policyholder is entitled to recover over the amount, if any, which the insurer offered to pay in settlement of the claim prior to the action. 215 ILCS 5/155(1).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Not applicable.

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

In Massachusetts, the term "insurance contract" is defined by statute. An insurance contract is "an agreement by which one party for a consideration promises to pay money or its equivalent, or to do an act valuable to the insured, upon the destruction, loss or injury of something in which the other party has an interest." Mass. Gen. Laws c. 175, § 2. The statutory definition of "insurance contract" does not differ substantially from the common-law definition. *Attorney Gen. ex rel. Monk v. C. E. Osgood Co.*, 249 Mass. 473, 476 (1924), *citing Commonwealth v. Wetherbee*, 105 Mass. 149 (1870); *Claflin v. U.S. Credit Sys.*, 165 Mass. 501 (1896).

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. Massachusetts courts recognize the "known loss" doctrine, which precludes insurance coverage for losses known to the insured at the time the insured purchases an insurance policy. *Keyspan New Eng., LLC v. Hanover Ins. Co.*, 24 Mass. L. Rep. 511 (Mass. Super. 2008), *citing SCA Servs., Inc. v. Transp. Ins. Co.*, 419 Mass. 528, 532 (1995). It is well-settled under Massachusetts law that "the basic purpose of insurance is to protect against fortuitous events and not against known certainties." *SCA Servs.*, 419 Mass. at 532 (1995). When parties enter into a contract of insurance, they "wager against the occurrence or nonoccurrence of a specified event; the carrier insures against a risk, not a certainty." *Id., citing Bartholomew v. Appalachian Ins. Co.*, 655 F.2d 27, 29 (1st Cir. 1981). Once the risk is eliminated, the contract for insurance "no longer exists." Id.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes. Massachusetts courts have construed the definition of "insurance contract" set forth under M.G.L. c. 175, § 2 as requiring the transfer of risk. *See, e.g., Cellilli v. Cellilli*, 939 F. Supp. 72, 77 (D. Mass. 1996); *New England Mut. Life Ins. Co. v. Harvey*, 82 F. Supp. 702, 706 (D. Mass. 1949); *see also Liability Investigative Fund Effort v. Massachusetts Med. Prof'l Ins. Ass'n*, 418 Mass. 436, 447 (1994) (explaining that insurance involves the shifting of risk from insured to insurer).

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Yes. To create a valid insurance contract, the insured must have an "insurable interest" in the subject of the contract at the time of the formation of the contract and at the time of the loss. *Queen v. Vermont Mut. Ins. Co.*, 32 Mass. App. Ct. 343, 345 (1992), *citing Clinton v. Norfolk Mut. Fire Ins. Co.*, 176 Mass. 486, 489 (1900). The policy underlying this requirement is that it is "unwholesome" to wager on insurance losses. *Id., citing* Couch, Insurance § 24.1, at 8-11 (2d ed. 1984). Massachusetts courts have recognized, for example, that betting on the destruction of someone else's property "could be a temptation to make the damaging event come true." Id.

With respect to property insurance, persons have an insurable interest if they receive a tangible benefit from the insured property or if they will suffer a loss by reason of its destruction. *Queen v. Vermont Mut. Ins. Co.*, 32 Mass. App. Ct. at 345-46 (1992) (finding that beneficiaries of real estate trust had an insurable interest in the trust corpus because they had a tangible interest in preserving the assets that benefited them). An insured "may have an insurable interest in property in which he has no title whatever, legal or equitable." *Womble v. Dubuque Fire & Marine Ins. Co.*, 310 Mass. 142, 144 (1941) (finding that even a somewhat tenuous continuing right to possession may suffice to afford an insurable interest); *see also Quigley v. Bay State Graphics*, 427 Mass. 455, 463 (1998) (explaining that a tenant may have an insurable interest in a leasehold under certain circumstances). With respect to life insurance, a person has an insurable interest in his own life and the lives of others that are of "some real interest to him." *In re Caron*, 305 B.R. 614, 616-617 (Bankr. D. Mass. 2004) (a person cannot take out insurance on the life of a total stranger, or someone "who is not so connected with him as to make the continuance of his life of some real interest to him."), *citing Connecticut Mut. Life Ins. Co. v. Schaefer*, 94 U.S. 457, 460 (1876) (finding that mere wager policies, where the insured party has no interest whatever in the matter insured, are void as against public policy).

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

Under Massachusetts law, an insurance contract is void if the policyholder does not possess an insured interest in the subject of the contract. *Womble v. Dubuque Fire & Marine Ins. Co.*, 310 Mass. 142, 144 (1941); O'Neill v. Queen Ins. Co., 230 Mass. 269, 270 (1918). A third party, such as a beneficiary, may also have an insurable interest in the subject matter of the

insurance contract, but no such interest is required unless there is evidence that the contract was intended as a wagering contract. *Potvin v. Prudential Ins. Co.*, 225 Mass. 247, 251 (1916) ("in the absence of any evidence indicating that the transaction was intended as a wagering contract, it is not necessary that the beneficiary or assignee should have an insurable interest"); *see also Bacon v. Federal Kemper Life Assur. Co.*, 400 Mass. 850, 854 (1987) (with respect to life insurance, Massachusetts law does not require that a beneficiary have an insurable interest in an insured's life); *accord Strachan v. Prudential Ins. Co.*, 321 Mass. 507, 509 (1947).

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

Massachusetts courts recognize that the spreading of risk is one of the primary purposes of insurance. *See, e.g., Van Arnam v. GSA*, 332 F. Supp. 2d 376, 394 (D. Mass. 2004) ("a principal purpose of insurance is to reduce one's risk of liability by spreading the cost among a large number of insureds, only a small number of whom will actually suffer a loss"); *United States Liab. Ins. Co. v. Selman*, 70 F.3d 684, 690 (1st Cir. 1995) (recognizing that insurance serves a socially advantageous purpose of risk-spreading); *Liab. Investigative Fund Effort v. Massachusetts Med. Prof'l Ins. Ass'n*, 418 Mass. 436, 447 (1994) ("insurance . . . involves not just the shifting of risk from insured to insurer, but also risk-sharing among insureds"); *Bonnano v. Harvard Pilgrim Health Care*, 11 Mass. L. Rep. 25 (Mass. Super. Ct. 2000) (insurance is meant "to spread the risk"). However, Massachusetts law imposes risk-spreading requirements only on certain types of mutual insurance companies that do not satisfy certain capital and surplus requirements prescribed by law. M.G.L. c. 175, § 90A. For such companies, Massachusetts law requires that either four hundred or eight hundred separate risks are subscribed for and entered on a company's books, depending on the type of loss insured against. Id. Beyond these requirements, risk-spreading does not affect the classification of an insurance contract.

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No. The definition of "insurance contract" set forth under M.G.L. c. 175, § 2 "is intended to be comprehensive of all kinds of insurance, including life, fire, accident, fidelity, health, title, and liability . . ." *Attorney Gen. ex rel. Monk v. C. E. Osgood Co.*, 249 Mass. 473, 476 (1924); *see also New England Mut. Life Ins. Co. v. Harvey*, 82 F. Supp. 702, 705 (D. Mass. 1949) (M.G.L. c. 175, § 2 applies to contracts for life insurance).

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Insurance contracts and contracts of gambling both involve wagering. *SCA Servs., Inc. v. Transp. Ins. Co.*, 419 Mass. 528, 532 (1995) (parties who enter into an insurance contract "wager against the occurrence or nonoccurrence of a specified event"). However, a contract of insurance is distinguishable from a contract of gambling or chance because an insurance contract requires that an insured have an insurable interest in the matter insured. *Queen v. Vermont Mut. Ins. Co.*, 32 Mass. App. Ct. 343, 345 (1992). Where the insured does not possess an insurable interest in the matter insured, the policy is merely a wager policy, and is void as against public policy. *Conn. Mut. Life Ins. Co. v. Schaefer*, 94 U.S. 457, 460 (1877) ("mere wager policies -- that is, policies in which the insured party has no interest whatever in the matter insured, but only an interest in its loss or destruction -- are void, as against public policy"); *King v. State Mut. Fire Ins. Co.*, 61 Mass. 1, 5 (1851) ("to make a policy valid, and enable the assured to recover a loss, he must have an interest in the subject, when the contract is made, and when the loss occurs . . . otherwise it is a wager policy, and void"); *see also New Ponce Shopping Ctr. v. Integrand Assur. Co.*, 86 F.3d 265, 268 (1st Cir. P.R. 1996) ("[r]equiring an insurable interest as a prerequisite to recovery prevents gambling through insurance policies.")

ii) Warranty, guaranty or any other surety contracts

Massachusetts courts distinguish contracts of insurance from arrangements of guaranty and surety based on the nature of the risk assumed by, and the potential liability of, the insurer or guarantor/surety. In the context of an insurance contract, the risk is controlled only by chance or nature. *FDIC v. Ins. Co. of N. Am.*, 105 F.3d 778, 785 (1st Cir. 1997). In guaranty and surety arrangements, on the other hand, the risk tends to be at least partially in the control of the promisor, creditor, or debtor. *Id.* at 785-786, *citing* 1 Russ & Segalla, Couch on Insurance 3d § 1:18 (1995). Further, with respect to potential liability, an insurer, upon the occurrence of the contingency, "must bear the ultimate loss," while a surety "is entitled to indemnity in case the surety is compelled to perform." *Id.* at 786. The Massachusetts legislature has determined that surety bonds are not insurance

contracts. *See* Mass. Gen. Laws c. 175, § 107 ("[t]he bonds on which such company becomes surety shall not be deemed insurance contracts as defined in [M.G.L. c. 175,] Section two"); *see also Gen. Elec. Co. v. Lexington Contracting Corp.*, 363 Mass. 122, 124 (1973) (finding that a surety bond is not an insurance contract).

iii) Financial contracts such as hedging contracts/swaps/derivatives

In Massachusetts, an "insurance contract" is defined as "an agreement by which one party for a consideration promises to pay money or its equivalent, or to do an act valuable to the insured, upon the destruction, loss or injury of something in which the other party has an interest." M.G.L. c. 175, § 2. An insured must have an "insurable interest" at the time of the formation of the insurance contract and at the time of the loss. *Queen v. Vermont Mut. Ins. Co.*, 32 Mass. App. Ct. 343, 345 (1992). Although hedging contracts, swap agreements and other financial contracts share some similarities with insurance contracts, financial contracts generally do not require that the buyer have an interest in the subject matter of the contract that could be adversely affected by the occurrence of a specified event. Indeed, such financial contracts generally do not require that the buyer have any interest in the subject matter of the contract whatsoever. We have not identified any Massachusetts statute, regulation or case law that directly addresses whether financial contracts constitute contracts of insurance within the meaning of M.G.L. c. 172, § 2. However, because Massachusetts law requires that an insured possess an "insurable interest" in the subject of an insurance contract, it does not appear that most financial contracts would constitute contracts of insurance.

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

We have not identified any law that would prevent a contract that satisfies the definition of "insurance contract" in M.G.L. c. 172, § 2 from being treated as such.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

Not applicable.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Under Massachusetts law, a domestic insurance company (defined as an insurance company incorporated or formed in Massachusetts) may not make or issue an insurance contract until it has obtained a certificate from the Massachusetts Commissioner of Insurance. M.G.L. c. 175, § 32. Massachusetts General Laws c. 175, § 32 provides, in relevant part, that no such certificate shall be issued until the Commissioner is satisfied that the insurance company: (i) has complied with Massachusetts law; (ii) has adopted a proper system of accounting; (iii) has employed a competent accountant, claim manager and underwriter, and (iv) is generally without liabilities, except for certain approved expenses. Id. To be eligible for such a certificate, the insurance company must file with the Massachusetts Division of Insurance of an affidavit signed by the officers of the company stating the amount of expenses incurred in the company's formation and stating that the company has no outstanding liabilities except organizational expenses and any liabilities to stockholders for the amount paid in for shares of stock. M.G.L. c. 175, § 4. The Commissioner may, in his discretion, refuse to issue a certificate to any company if he believes that the granting of such a certificate would be prejudicial to the public interest. M.G.L. c. 175, § 32.

Likewise, a foreign insurance company (defined as an insurance company formed by an authority of any state or government other than Massachusetts) may not make or issue an insurance contract until it has obtained a license from the Massachusetts Commissioner of Insurance. M.G.L. c. 175, § 151. To obtain a license, a foreign insurance company must file with the Commissioner a certified copy of its charter or deed of settlement, a statement of its financial condition, and a power of attorney appointing the Commissioner or his successor its true and lawful attorney upon whom all lawful processes in any legal proceeding against it may be served. *Id.* A foreign insurance company must also satisfy the Commissioner that: (i) it is fully and legally organized under the laws of its state or government to do the business it proposes to transact; (ii) it has the combined amounts of capital and surplus required or prescribed by the Commissioner for the classes of business it proposes to transact; (iii) it has made a deposit with the state treasurer or with the proper board or officer of some other state in exclusive trust for the benefit and security of all its policyholders in the United States; (iv) it has made a deposit with the state treasurer in exclusive trust for the benefit and security of its policyholders in Massachusetts; (v) any capital, surplus, guaranty fund or guaranty capital and assets, other than contingent, are well invested and available for the payment of losses in Massachusetts; (vi) the company is in a sound financial condition; (vii) the company's business policies, methods and management are sound and proper; and (viii) that it insures in a single risk wherever located an amount no larger than ten percent of its surplus to policyholders. *Id.*

Surplus lines insurance presents an exception to the general rule requiring licensure in Massachusetts. A "surplus lines" insurance company is neither an insurer organized under Massachusetts law nor a foreign corporation admitted to transact insurance business in Massachusetts. *See Church of Christ v.*

St. Paul Surplus Lines Ins. Co., 22 Mass. App. Ct. 407, 408 (1986). Under M.G.L. c. 175, §§ 168 and 168A, a person may receive a license as a special insurance broker to negotiate, in very limited circumstances, contracts to provide insurance on property or interests located in Massachusetts where coverage ordinarily would be unavailable. *Id.; see also Orion Ins. Co. v. Shenker*, 23 Mass. App. Ct. 754, 759 (1987). Insurance may be written by such specially licensed brokers with surplus lines companies only when the full amount of insurance required to protect the property or interests for which coverage is sought is not procurable from among Massachusetts or admitted foreign insurance companies. *Church of Christ*, 22 Mass. App. Ct. at 408 (1986).

12. What are the legal consequences for the risk-taker acting without license?

An insurance company that transacts business without a license in Massachusetts may be subject to prosecution by the Attorney General, District Attorney or Commissioner of Public Safety and may face penal sanctions. Massachusetts General Laws c. 175, § 3 provides that "[n]o company shall make a contract of insurance upon or relative to any property or interests or lives in the commonwealth, or with any resident thereof… except as authorized by [M.G.L. c. 175]… or except as otherwise expressly authorized by law." M.G.L. c. 165, § 3. Massachusetts General Laws c. 175, § 3A, confers broad authority on the Commissioner of Insurance to "administer and enforce" the provisions of M.G.L. c. 175. See *Hartford Acci. & Indem. Co. v. Comm'r of Ins.*, 407 Mass. 23, 28 (1990). M.G.L. c. 175, § 3A further provides that "[i]f upon complaint, examination or other evidence exhibited to [the Commissioner], he is of opinion that any provision…has been violated, he shall forthwith report the facts to the attorney general, to the proper district attorney or to the commissioner of public safety, who shall cause the offender to be prosecuted therefor." M.G.L. c. 175, § 3A; *see also Attorney Gen. ex rel. Monk v. C. E. Osgood Co.*, 249 Mass. 473, 477 (1924) (where company's issuance of an insurance contract violated M.G.L. c. 175, § 3, attorney general obtained injunction and company was required to pay costs). Pursuant to M.G.L. c. 175, § 189, a company that transacts insurance business without a license in Massachusetts may also be subject to a fine of $50 to $500. M.G.L. c. 175, § 189. ("A company or any officer or agent thereof who makes, issues or delivers a policy of insurance…in violation of [c. 175] shall, except as otherwise provided, forfeit not less than fifty nor more than five hundred dollars").

13. In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.

Under M.G.L. c. 175, § 47A, a domestic insurance company may engage directly in any of the following businesses: (a) rendering investment advice; (b) rendering services related to the functions involved in the operation of its insurance business including, but not limited to, actuarial, loss prevention, safety engineering, data processing, accounting, claims, appraisal and collection services; (c) acting as administrative agent for a government instrumentality which is performing an insurance function or is responsible for a health or welfare program; or (d) any other business activity reasonably complementary or supplementary to its insurance business, either to the extent necessarily or properly incidental to the insurance business that the insurer is authorized to perform, or to the extent approved by the Commissioner of Insurance. M.G.L. c. 175, § 47A. A domestic insurance company may not, however, act for another insurer as insurance agent, insurance broker, special insurance broker, or public insurance adjuster. *Id.*

Massachusetts law does not expressly prohibit a foreign insurance company from transacting non-insurance business. However, a foreign insurance company may only transact the kind of business that is specified in its charter and in its license. M.G.L. c. 175, § 152.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Yes. Massachusetts General Laws c. 175, § 2B provides that no policy form of insurance shall be issued to more than fifty policyholders until a copy of the policy form has been on file with the Commissioner of Insurance for thirty days. M.G.L. c. 175, §2B. Under M.G.L. c. 175, § 193F, the Commissioner may extend the thirty-day period by giving written notice of the extension to the insurance company before the expiration of the initial thirty-day period. M.G.L. c. 175, § 193F. If the form does not comply with Massachusetts law, the Commissioner should so notify the company in writing, specifying the reasons for his opinion. M.G.L. c. 175, § 2B. Unless the policy form has been affirmatively approved or disapproved during the thirty-day period or any extension thereof, it will be deemed approved at the conclusion of the period. Id. Once the applicable period has elapsed, affirmative approval of the Commissioner is not required before issuance of the policy form. M.G.L. c. 175, § 2B.

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Under Massachusetts law, an insurance policy issued by a non-licensed party is valid and binding on the company that issued it. M.G.L. c. 175, § 193. Massachusetts General Laws c. 175, § 193 provides that where a policy of insurance is issued in violation of M.G.L. c. 175, the policy "shall be valid and binding upon the company issuing it, and the rights, duties and obligations of the parties thereto shall be determined by [M.G.L. c. 175]." The purpose of this rule is to protect the insureds. *Clarendon Nat'l Ins. Co. v. Amica Mut. Ins. Co.*, 441 Mass. 248, 256 (2004). Although an insurer may be held to pay a fine as penalty for the issuance of a policy without proper license, we have identified no Massachusetts case in which a policyholder has recovered damages in connection with the issuance of an insurance policy by an unlicensed company. *See* M.G.L. c. 175, § 189. ("A company or any officer or agent thereof who makes, issues or delivers a policy of insurance … in violation of [c. 175] shall, except as otherwise provided, forfeit not less than fifty nor more than five hundred dollars").

16. <u>Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.</u>

Yes. The Massachusetts Insurance Code is codified at Mass. Gen. Laws c. 174A to c. 178A. The Massachusetts Insurance Regulations are codified in the Code of Massachusetts Regulations at 211 CMR 1:00 *et seq.*

17. <u>Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.</u>

Several Sections of M.G.L. c. 175 set forth requirements as to the form and content of certain insurance contracts. M.G.L. c. 175 § 99, for example, requires that in every fire insurance policy issued in Massachusetts, the words "In case of fire notify the company or its local agent at once in writing" must be printed or stamped on the policy's filing-back. M.G.L. c. 175, § 99, Seventh. M.G.L. c. 175, § 99 further requires that all fire insurance policies must include the following language: "notwithstanding any provision to the contrary of any general or special law, the company shall, before paying any claim for loss or damage to real property, other than owner-occupied one, two, three, or four family dwellings, from any hazard, where the amount of the loss payable under the policy equals or exceeds USD 5,000, first require the claimant to submit to the insurer a certificate of municipal liens from the collector of taxes of the city or town wherein such property is located." *Id.* at Fourteenth.

Likewise, M.G.L. c. 175, § 113A requires that motor vehicle liability policies contain a variety of provisions, including that: (i) if the company shall cease for any reason to be authorized to transact business in Massachusetts the insured shall, if he has paid the premium as aforesaid, be entitled to a return premium; (ii) the policy, the written application therefor, if any, and any rider or endorsement, shall constitute the entire contract between the parties; and (iii) no statement made by the insured or on his behalf, either in securing the policy or in securing registration of the motor vehicle or trailer covered thereby, no violation of the terms of the policy, and no act or default of the insured, either prior or subsequent to the issuance of the policy, shall operate to defeat or avoid the policy so as to bar recovery within the limit provided in the policy by certain judgment creditors. M.G.L. c. 175, § 113A (3)-(5). Similarly, M.G.L. c. 175, § 108 governs the contents of accident and sickness insurance policies. It provides that each such policy issued to any person in Massachusetts must contain the following provisions, among others: (i) "After two years from the date of issue of this policy no misstatements, except fraudulent misstatements, made by the applicant in the application for such policy shall be used to void the policy or to deny a claim for loss incurred or disability as defined in the policy commencing after the expiration of such two-year period;" (ii) "Written notice of claim must be given to the insurer within twenty days after the occurrence or commencement of any loss covered by the policy, or as soon thereafter as is reasonably possible;" and (iii) "No action at law or in equity shall be brought to recovery on this policy prior to the expiration of sixty days after written proof of loss has been furnished in accordance with the requirements of this policy." M.G.L. c. 175, § 108, 3(a)(2), (5), (11).

18. <u>Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.</u>

Yes. Mass. General Laws c. 176D, § 2 prohibits insurance companies from engaging in "unfair or deceptive" acts or practices in the business of insurance. Under M.G.L. c. 176D, § 3, "unfair or deceptive" acts or practices in the business of insurance include conduct such as: (i) misrepresenting the benefits, advantages, conditions, or terms of any insurance policy; (ii) making or permitting any unfair discrimination between individuals of the same class and of essentially the same hazard in the amount of premium, policy fees, or rates charged for any policy or contract of accident or health insurance or in the benefits payable thereunder, or in any of the terms or conditions of such contract; and (iii) refusing to pay claims without conducting a reasonable investigation based upon all available information. M.G.L. c. 176D, § 3(1), (7), (9). Generally, M.G.L. c. 176D is enforceable only by the Massachusetts Commissioner of Insurance. *Foisy v. Royal Maccabees Life Ins. Co.*, 241 F. Supp. 2d 65, 68 (D. Mass. 2002), *citing Thorpe v. Mut. of Omaha Ins. Co.*, 984 F.2d 541, 544 n.1 (1st Cir. 1993). However, an individual insured may bring an action for damages under the Massachusetts consumer

protection act, M.G.L. c. 93A, where an insurer commits an “unfair claim settlement practice” as defined under M.G.L. c .176D, §3(9). *See* M.G.L. c. 93A, § 9(1) (“Any person whose rights are affected by another person violating the provisions of clause (9) of Section three of chapter one hundred and seventy-six D may bring an action . . . for damages . . . .”). Under M.G.L. c. 176D, §3(9), “unfair claim settlement practices” include conduct such as: (i) failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies; (ii) failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed; and (iii) failing to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear. M.G.L. c. 176D, §3(9)(b), (e)-(f).

Although M.G.L. c. 176D is generally enforceable only by the Massachusetts Commissioner of Insurance, the Commissioner may order that restitution be made by an insurer or its agent to any claimant who has suffered actual economic damage as a result of a violation of M.G.L. c. 176D. M.G.L. c. 176D, § 7. Further, in any action to recover on an insurance policy, a court may award punitive damages, in addition to the amount of the claim, not to exceed 25 per cent of the claim if the court finds that the party seeking to recover on the insurance policy has been damaged by a violation of §§ 3 or 4 of M.G.L. c. 176D that has been determined as such by the Commissioner. *Id.*

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Massachusetts General Laws c. 175, § 224 carves out an exception to the provisions of Massachusetts General Laws Chapter 175 for large commercial policyholders. Under M.G.L. c. 175, § 224, the provisions of Chapter 175 do not apply to property or casualty insurance policies issued to “large commercial policyholders” to the extent that the provisions relate to the “regulation of policy form and content and the filing, approval and fixing and establishing of rates.” M.G.L. c. 175, § 224. Pursuant to M.G.L. c. 175, § 224, a “large commercial policyholder” is the holder of a property or casualty insurance policy that is a corporation, partnership, trust, sole proprietorship or other business or public entity, has aggregate property and casualty insurance premiums of USD 30,000 excluding workers' compensation, which has certified that it elects to be treated as a large commercial policyholder and understands the limited regulatory oversight that the election connotes, and has certified that it meets two of the following criteria:

(1) net worth of USD 10,000,000;

(2) net revenue or sales of USD 5,000,000;

(3) more than 25 employees per individual company or more than 50 employees per holding company aggregate;

(4) nonprofit or public entity with an annual budget or assets of USD 25,000,000 or more;

(5) municipality with a population of 20,000 or more; or

(6) retains a risk manager who shall be a full-time employee or a person retained by a large commercial policyholder, either of which shall be licensed and shall be 1 of the following: (i) a certified insurance counselor; (ii) a chartered property and casualty underwriter; (iii) an associate in risk management; (iv) a certified risk manager; or (v) a licensed insurance advisor in property and casualty insurance.

M.G.L. c. 175, § 224.

A policy issued pursuant to M.G.L. c. 175, § 224 must also contain certain disclosures and notifications. M.G.L. c. 175, § 225. For example, a policy issued pursuant to § 224 must contain the following disclosure notice: “The policy applied for is not subject to all insurance laws that apply to other commercial lines products and may contain significant differences from a policy that is subject to all insurance laws.” *Id.* The disclosure notice should also include a policyholder's acknowledgement statement, to be signed and dated by the first named insured before the effective date of coverage, which states: “I hereby acknowledge that I have read the above disclosure notice and have received a copy of the same.” Id. The first named insured shall sign and date a similar notice before each renewal of the policy, except if there are no material changes to the policy. *Id.*

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

Yes. Under New York Insurance Law ("NYIL"), an insurance contract is

> any agreement or other transaction whereby one party…is obligated to "confer benefit of pecuniary value" upon another party…dependent upon the happening of a fortuitous event in which [such other party] has, or is expected to have at the time of such happening, a material interest which will be adversely affected by the happening of such event.[1]

"Fortuitous event," in turn, means any occurrence which is, or is assumed by the parties to be, "to a substantial extent" beyond the control of either party.[2]

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes. As described in Item 1., the definition of "insurance contract" depends on the occurrence of a "fortuitous" event, which means an event beyond the control of the parties.[3]

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

It seems implicit in the definition of "insurance contract" that risk must be transferred insofar as value is transferred upon the occurrence of a contingent event.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

In general, yes. As described in more detail below, for property-casualty policies, insurable interest must exist at any time there is an attempt to claim benefits under the contract. For life policies, the insurable interest requirement is more limited. Insurable interest must be present at policy inception only, but there must be no "intent" at policy inception that the policy benefits a person without insurable interest. More specifically:

Under the general definition of "insurance contract," the person entitled to insurance protection under the contract must have a "material interest" which will be "adversely affected" by a contingent event.[4]

No property-casualty insurance contract issued in, or on property located in, the state of New York is enforceable except by a person having an insurable interest in the property insured.[5] For these purposes, "insurable interest" includes any "lawful and substantial economic interest in the safety or preservation of property from loss, destruction or pecuniary damage."[6]

In the context of life, accident and health insurance, no person may "procure" an insurance contract on another person unless the benefits under such contract are payable to the person insured or to a person having, "at the time when such contract is made," an "insurable interest" in the person insured.[7]

"Insurable interest" for these purposes means

- in the case of persons closely related by blood or by law, a "substantial interest engendered by love and affection," or
- in the case of other persons, a "lawful and substantial economic interest" in the continued life, health or bodily safety of the person insured, "as distinguished from an interest which would arise only by, or would be enhanced in value by, the death, disablement or injury of the insured."[8]

Historically under New York law, a life policy could be taken out on one's own life without any requirement that the beneficiary have insurable interest.[9] Similarly, in 2010, the New York Court of Appeals (the state's highest court) ruled that where a person obtained a policy on his own life with the intent to immediately assign it, the policy would be valid.[10] This decision, however, applies only retrospectively insofar as the New York legislature adopted comprehensive life settlement legislation in 2009, proscribing so-called "stranger-originated life insurance" (the practice of initiating the issuance of an

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[1] NYIL §1101(a)(1).

[2] NYIL §1101(a)(2).

[3] Id.

[4] NYIL §1101(a)(1).

[5] NYIL §3401.

[6] Id.

[7] NYIL §3205(b)(2).

[8] NYIL §3205(a)(1).

[9] NYIL §3205(b)(1).

[10] *Kramer v. Phoenix Life Ins. Co. et al.*, 15 N.Y. 3d 539, 940 N.E. 2d 535 (2010).

insurance policy for purposes of on-selling it to an investor).[11]

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

For property-casualty policies, as explained above, insurable interest relates to the property or risk insured, rather than the person owning the property at the time of policy inception. In other words, we understand New York law to require that a policyholder have insurable interest in the particular property or risk at the time that such holder makes a claim under the policy. If the policyholder has no insurable interest at such time (even if the policyholder once did have such an interest), the insurer should have a valid defense to payment.[12]

As discussed in the previous item, in the context of life insurance, generally:

- A person can procure a policy on his own life as long as
  - it is at the person's own "initiative"[13] and
  - such person does not have an "intent" to transfer the policy, once issued, to someone with no insurable interest.[14]
- A person can obtain insurance on the life of another person only if the benefits are payable to someone with insurable interest in the life of such other person.[15]

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The extent to which risks are pooled does not have any direct statutory bearing on whether a contract is characterized as insurance. However, the fact that insurance is generally written over a large and diversified body of risks (in order to distribute the risk of loss more evenly) has been cited as a major distinguishing characteristic of insurance.[16]

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

No.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

New York law defines "gambling" as risking something of value upon the outcome of a "contest of chance" (defined as a game in which chance is a material determinant in the outcome) or a "future contingent event not under his control or influence, upon an agreement or understanding that he will receive something of value in the event of a certain outcome."[17] Despite textual similarities between the definitions of "gambling" and "insurance" in New York law (e.g., the role of chance and a transfer of risk), an insurance contract may be distinguished from gambling insofar as insurance depends on an insurable interest. Courts construing New York law have affirmed that a purported insurance policy issued on the life of a stranger is a kind of "wagering contract" that is void as against public policy.[18] (In other words, public policy disfavors the creation of contracts that confer a monetary benefit on the death of a third person.) As discussed above and below, the boundary between insurance contracts with the requisite insurable interest and other types of arrangements (whether legal or not) where insurable interest is deemed lacking has not always been clear.

ii) Warranty, guaranty or any other surety contracts

New York insurance law specifies that "making or proposing to make" such a contract "as a vocation and not merely incidental to any other legitimate business or activity" of the person constitutes "doing an insurance business" in New York.[19] A contract so

[11] N.Y. Laws 2009, ch. 499, §11, codified at NYIL §7815.

[12] NYIL §3401.

[13] NYIL §3205(b)(1).

[14] NYIL §7815.

[15] NYIL §3205(b)(2).

[16] *See, e.g., Lerner v. Lerner*, 120 A.D. 2d 243 (Appel. Div. 2d Dept., 1986).

[17] NY Penal Law §225.00(2).

[18] *See, e.g.*, Life Product Clearing v. Angel, 530 F. Supp. 2d 646 at 652 (SDNY, 2008); Kramer at 539.

19 NYIL §1101(b)(1)(A).

made is an insurance contract.[20] In interpretive guidance, the Office of General Counsel of the New York Insurance Department (the "NYID")[21] has indicated that a warranty

> relates in some way to the nature or efficiency of a product or service. Commonly, the warrantor agrees to repair or replace a product that fails to perform properly, such as a contract covering a defect in materials or workmanship, or a contract otherwise covering the breakdown of the product. Where the maker of a contract has a relationship to the product or service, or does some act that imparts knowledge of the product or service to the extent of minimizing, if not eliminating, the element of chance or risk contemplated by [the definition of "insurance contract" under New York law], then the contract is a warranty. Where there is no relationship or act, the maker of the contract undertakes an obligation involving a fortuitous risk, which is an insurance contract. If the maker is not licensed as an insurer, the contract would be issued in violation of [New York's licensure requirement].[22]

iii) Financial contracts such as hedging contracts/swaps/derivatives

Historically the NYID took the position that a financial instrument such as an interest rate or credit default swap should not be considered insurance despite arguably "conferring value upon the occurrence of a fortuitous event." The principal rationale on which this conclusion was based was the fact that payment under such a contract is not triggered by *loss* of a party but rather by an objectively verifiable event such as a default on an obligation of a third person.[23] In 2008 the NYID revised its guidance, indicating that a swap might be characterized as an insurance contract if the protection buyer has a "material interest" in the obligation that triggers payment under the swap.[24] In other words, even where a swap is payable based on a default rather than a "loss," the contract could be an insurance contract if the holder owns the obligation triggering the swap and therefore, in effect, does incur a loss when a default occurs.

On 20 November 2008, the NYID indicated that it was delaying its application of these guidelines on swaps in light of expected Federal initiatives addressing derivatives.[25] The Dodd-Frank Wall Street Reform and Consumer Protection Act, a landmark Federal law adopted in 2010, essentially mooted this issue by providing that no swap could be subject to regulation as an insurance product by any state.[26]

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

Strictly speaking, no. As noted above, a warranty, guaranty or surety contract is an insurance contract only if made as part of the issuer's "vocation" and not as incidental to some other activity.[27]

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

No.

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

Yes. A license is required to issue an insurance contract.[28]

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

A person issuing an insurance contract without a license is subject to a penalty of USD 1,000 for the first violation and USD 2,500 for each subsequent violation, "in addition to any other penalty provided by law."[29]

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance</u>

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20 NYIL §1101(a)(3).

21 Now known as the Department of Financial Services.

22 NYID General Counsel Opin. 2-29-96 (Feb. 29, 1996).

23 NYID General Counsel Opin., June 16, 2000, available at 2000 NY Insurance GC Opinions LEXIS 144.

24 NYID Circular Letter No. 19 (2008). See also Press Release of New York Gov. David Paterson dated September 22, 2008 indicating that such Circular Letter "establish[es]" that where the protection buyer owns the underlying obligation of a credit default swap, the swap is an insurance contract. The Circular Letter itself is more circumspect, stating only that the NYID would address this issue at a future time.

25 First Supplement to Circular Letter No. 19 (2008), Nov. 20, 2008.

26 111 Public Law 203, §722(b).

27 NYIL §1101(a)(3).

28 NYIL §1102(a).

29 *Id.*

business? If yes, please briefly explain the scope of such prohibition.

Strictly speaking, no. The myriad regulatory requirements imposed on insurers, however – regulating investment holdings, market conduct, payment of dividends to corporate affiliates, advertising, permitted products and corporate governance, among other things – would make it difficult as a practical matter, and undesirable as commercial matter, to conduct non-insurance businesses through an insurer.

14. Do the terms and conditions of insurance contracts need to be

i) submitted to the regulator as a kind of formal requirement or

ii) approved by the regulator prior to entering into effect?

Property-casualty policies are subject to prior filing and approval, although rates can be used upon filing, without having to wait for formal approval ("file and use").[30] For life policies, policies are subject to prior approval, and some but all not rates (including credit life, certain group life coverages, credit accident and health and certain others) must also be approved prior to use.[31] For rates on other lines of life insurance, file-and-use is available.[32] Health policies are subject to form and rate approval. [33]

Certain larger commercial risks can be insured in New York free of rate and form filing and approval requirements. The two general ways in which such coverages can be written are the so-called "Free Trade Zone" for risks above a certain premium amount or certain enumerated unusual risks[34] and excess line coverage, which is coverage from non-admitted insurers where coverage cannot be procured from New York-licensed carriers.[35]

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

An insurance policy that does not conform to regulatory requirements of the New York insurance law is generally enforceable against the insurer.[36]

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

Yes. Article 31 of NYIL governs insurance contracts generally. Article 32 governs life, accident and health contracts, while Article 34 regulates property-casualty contracts.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Yes. Generally, subject to specific types of policies and required provisions, life policies must contain provisions regarding the following:

- grace periods for payments of premium;
- incontestability after two years;
- premium adjustment in the event of a misstatement of age;
- calculation of divisible surplus accruing on the policy;
- any applicable mortality table, interest rate and method used in calculating cash surrender values and any paid-up nonforfeiture benefits available under the policy;
- policy loan availability and permitted terms;
- applicable installment or annuity payments available under the policy;
- reinstatement;
- premium refund in the event of policy surrender;
- any applicable guaranteed mortality, expense and interest factors;
- nonforfeiture of benefits;
- non-guaranties of dividends and certain additional amounts;
- minimum guarantied interest rates applicable to the policy;
- in the case of group life, certain rights of certificate-holders to information from the policyholder;

30 NYIL §2305(a), §2310(a).

31 NYIL §3201.

32 *Id.*; General SERFF Guidelines for Form Filings (NY Dept. of Financial Services, Life Bureau), available at www.dfs.ny.gov/insurance/serflife.htm.

33 NYIL §3231.

34 NYIL Art. 64.

35 NYIL §2118.

36 NYIL §3103.

- payments to and determination of beneficiaries;
- policy conversion provisions applicable to the holder;
- in the case of group life, rights of new employees to participate in the policy; and
- certain required renewal terms.[37]

Individual accident and health insurance policies must include, in general, the following:

- explanation of the consideration due in respect of the contract;
- effective and termination dates, including termination based on change in family status, age and occupation;
- identification of persons covered and provisions regarding rights of unmarried dependents;
- provisions allowing insurers certain information rights from insureds;
- no "undue prominence" given to any portion of text;
- description of policy exceptions;
- certain administrative identifiers of the policy (file numbers etc.);
- no provision purporting to make any portion of the charter, rules, constitution or by-laws of the insurer a part of the policy unless such portion is set forth in full in the policy;
- a statement regarding status as a qualifying retirement facility;
- suspension for active military duty;
- a statement that the contract embodies all of the rights of the parties;
- provisions regarding claims, proof of loss and benefits;
- rights of the insurer to examine the health of an insured or make an autopsy;
- provisions governing legal actions;
- provisions regarding changes in beneficiaries;
- provisions regarding the effect on coverage of having other insurance in-force;
- provisions in connection with relationship between income and coverage; and
- exclusions for intoxicant- or narcotic-caused conditions.[38]

Property-casualty policies generally are required to have a provision that, in the event of a pending claim for damage to real property, the insurer will upon request furnish to the insured a written estimate of damages which the insurer has independently prepared for its own purposes, or had prepared on its behalf for its own purposes, specifying all appropriate deductions, within 30 days after the request or preparation, whichever is later.[39] Additional detailed and coverage-specific requirements are imposed on various types of policies and risks such as fire[40], liability[41], windstorm[42] and specialty lines such as title insurance[43] and financial guaranty.[44]

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Many, if not most, of the provisions described in item 17 are designed to protect consumers from terms or conditions that may be regarded as abusive or to compensate for the perceived imbalance in commercial bargaining power between insurer and insured. Additional specific examples of contract requirements that are motivated by consumer protection include New York's requirement that policies be "readable and understandable"[45] and the provision that no misrepresentation of an insured may void any contract of insurance unless it is so "material" that knowledge of the actual facts would have led to a refusal by the insurer to issue the coverage.[46]

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

n/a

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37 NYIL §3203, §3220.

38 NYIL §3217.

39 NYIL §3407-a.

40 NYIL §3404.

41 NYIL §3420.

42 NYIL §3445.

43 NYIL §6409.

44 NYIL §6905.

45 NYIL § 3102.

46 NYIL §3105(b)(1).

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Definition of an Insurance Contract

1. Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.

Under Texas law, "[i]nsurance is a contract by which one party, for consideration, assumes a particular risk on behalf of another party and promises to pay him a certain or ascertainable sum of money on the occurrence of a specified contingency." *In re Allstate Mut. Ins. Co.*, 209 S.W.3d 742, 745 (Tex. App.—Tyler 2006, no pet.). The Texas Supreme Court has recognized that the foundation of insurance is "risk distribution." *In re Tex. Ass'n of School Boards, Inc.*, 169 S.W.3d 653, 659 (Tex. 2005). "Insurance companies are in the business of spreading losses across the premiums they receive." *Concierge Nursing Ctrs., Inc. v. Antex Roofing, Inc.*, --- S.W.3d ---, 2013 WL 1912342, at *5 (Tex. App. – Houston [1st. Dist.] May 9, 2013).

The essential terms and elements of a contract of insurance on which the parties' minds must meet include:

- the rate of the premium
- the duration of the policy
- the nature of the risk
- the description of the property or person or interest to be insured and its location
- the amount of insurance

E.g., Hines v. Liberty Life Ins. Co., Slip Copy, 2013 WL 310320, at *16 (W.D. Tex. Jan. 25, 2013) (citing 45 TEX. JUR. 3d, Insurance Contracts and Coverage §19); *see also Export Ins. Co. v. Herrera*, 426 S.W.2d 895, 898 (Tex. App.—Corpus Christi 1968, writ ref'd n.r.e.) (identifying subject matter, rate of premium, amount, and duration as necessary elements of insurance contract).

Other than for regulatory purposes, Texas courts have held that an insurance policy or contract, and the validity of a binder, contract to insure, or contract of insurance, will be recognized regardless of its informality. *See, e.g., Howard v. Burlington Ins. Co.*, 347 S.W.3d 783, 790 (Tex. App.—Dallas 2011) (noting that binder is enforceable insurance contract pending issuance of policy and generally provides coverage equivalent to contemplated policy); *Riner v. Allstate Life Ins. Co.*, 131 F.3d 530, 534 (5th Cir. [Tex.] 1998) (noting, "Texas law recognizes that a receipt and temporary insurance agreement can create a binding contract to provide temporary insurance.") However, a quote is *not* an insurance contract; it is merely an offer to make a contract of insurance. Howard, 347 S.W.3d at 789. Any doubts as to whether an agreement provides temporary coverage, or is merely a conditional promise to consider the insurance application, will be resolved in favor of coverage. Riner, 131 F.3d at 534.

As discussed further at No. 14 below, insurers doing business in Texas are required to use policies and endorsements approved by the Texas Department of Insurance ("TDI"). *Urrutia v. Decker*, 992 S.W.2d 440, 443 (Tex. 1999). Policies covered by these requirements include: life, health, and accident insurance policies, TEX. INS. CODE ANN. §§ 1701.051, et. seq.; title insurance policies, TEX. INS. CODE ANN. § 2703.002; and certain types of liability, casualty, and property insurance, including general liability insurance, residential and commercial property insurance, financial guaranty insurance, personal and commercial automobile insurance, and fidelity, guaranty and surety bonds other than criminal court appearance bonds, TEX. INS. CODE ANN. §§ 2301.001 et. seq.

2. Does an insurance contract require an element of uncertainty? Please describe.

Yes, under Texas law, the existence of risk - or "fortuity"—generally is essential to a contract of insurance. *E.g., In re Tex. Ass'n of School Boards, Inc.*, 169 S.W.3d at 658-59; *Two Pesos, Inc. v. Gulf Ins. Co.*, 901 S.W.2d 495, 501 (Tex. App. - Houston [14th Dist.] 1995, no writ). Texas applies the "fortuity doctrine" to bar coverage for damages that the insured knew of when he or she entered into an insurance policy. *Scottsdale Ins. Co. v. Travis*, 68 S.W.3d 72, 75 (Tex. App. - Dallas 2001, pet. denied). The "fortuity doctrine" precludes coverage for both a "known loss" and a "loss in progress." *Id.* A "known loss" is one the insured knew had occurred prior to making the contract; a "loss in progress" occurs when the insured is, or should be, aware of an ongoing, progressive loss at the time of contracting. *Id.*

In Texas, it also is contrary to public policy for an insurance company to knowingly assume a loss that occurred prior to making the contract. *Two Pesos, Inc.*, 901 S.W.2d at 501-02.

3. Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?

Yes, under Texas law, "risk-shifting is the purpose of insurance." *Fairfield Ins. Co. v. Stephens Martin Paving, L.P.*, 246 S.W.3d 653, 673 (Tex. 2008)

[1] This summary is not intended, and is not provided, as legal advice. No duty shall arise between the authors and any reader of this material.

(Hecht, J., concurring). The Texas Supreme Court has recognized that "[t]he payment of the premium by the insured and the assumption of a specified risk by the insurer are essential elements to a contract of insurance …the consideration to be valued is the undertaking of the risk that insured losses might occur." *In re Tex. Ass'n of School Boards, Inc*., 169 S.W.3d at 658-59.

4. Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called 'insured interest')?

Yes, under Texas law, this generally is called an "insurable interest." The insurable interest requirement is intended to "discourage the use of insurance for illegitimate purposes." *Valdez v. Colonial County Mut. Ins. Co*., 994 S.W.2d 910, 914 (Tex. App.—Austin 1999, pet. denied).

Although insurable interest is an essential characteristic of all insurance contracts, under Texas law, "it is necessary to distinguish between property insurance and life insurance in defining what constitutes an insurable interest." *Stillwagoner v. Travelers Ins. Co*., 979 S.W.2d 354, 361 (Tex. App.—Tyler 1998, no pet.). Because property insurance is based upon the principle of indemnity, if the insured has no insurable interest, the policy is invalid and the insured cannot recover under the policy. *Id.* In contrast, a beneficiary's lack of an insurable interest does *not* invalidate a life insurance policy. *Id.* Where life insurance benefits are paid to a beneficiary without an insurable interest, the beneficiary holds the proceeds for the benefit of those entitled by law to receive them. *Id.* at 358.

Property

Generally, with respect to property, an insurable interest exists when the insured "derives a pecuniary benefit or advantage by the preservation and continued existence of the property or would sustain a pecuniary loss from its destruction." *Valdez*, 994 S.W.2d at 914. An insurable interest in property is not dependent upon ownership or possession of the property but, "[i]f a claimant cannot suffer any pecuniary loss or derive any benefit from the property, he has no insurable interest." *Id.* The Texas Windstorm Insurance Association Act specifically defines an "insurable interest" to include "any lawful and substantial economic interest in the safety or preservation of property from loss, destruction, or pecuniary damage." TEX. INS. CODE ANN. § 2210.201.

An insurable interest in property must exist both at the time of the issuance of the insurance and at the time of the loss. *Highlands Ins. Co. v. City of Galveston*, 721 S.W.2d 469, 471 (Tex. App.-Houston [14th Dist.] 1986, writ ref'd n.r.e.)

Life

It is against public policy in Texas to allow anyone who has no insurable interest to be the owner or beneficiary of life insurance. *Mayo v. Hartford Life Ins. Co*., 220 F. Supp. 2d 794, 798 (S.D. Tex. 2002), *affirmed and remanded by* 354 F.3d 400 (5th Cir. 2004); *Stillwagoner*, 979 S.W.2d at 358. A putative beneficiary or owner only has an insurable interest in the life of another where the beneficiary is: (1) so closely related by blood or affinity that he wants the other to continue to live, irrespective of the monetary considerations; (2) a creditor; or (3) one possessing a reasonable expectation of pecuniary benefit or advantage from the continued life of another. *Mayo*, 220 F. Supp. 2d at 798; *Stillwagoner*, 979 S.W.2d at 361 (quoting *Drane v. Jefferson Standard Life Ins. Co*., 161 S.W.2d 1057, 1058-59 (Tex. 1942)).

With respect to life insurance, Texas law provides that a beneficiary "who is designated in a life insurance policy has an insurable interest for the face amount of the policy and is entitled to collect that amount." TEX. INS. CODE ANN. § 1103.002. An individual applying for a policy on his or her own life may "designate in writing in the application for the policy any individual" as beneficiary, owner, or both. *Id.* at § 1103.054. An individual also may designate a third party to submit an application on his or her behalf, or consent to the designation of a third party as a beneficiary or owner, but this consent must be in writing. *Id.* at § 1103.056.

5. Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?

See discussion at No. 4 above.

6. Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the 'law of the large numbers')? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?

The "spreading" of a policyholder's risk has been identified as a primary element of an insurance contract. *Vesta Ins. Co. v. Amoco Prod. Co*., 986 F.2d 981, 986 (5th Cir. [Tex.] 1993). The Texas Court of Appeals has observed:

> ... [T]o be insurable the risk must be measurable in quantitative terms for which purpose the law of large numbers and the theories of probability and chance are employed. The law of large numbers is based on the observation that the larger the number of instances taken, the closer the result approaches the theoretical probability, and, as applied to insurance, that means the probability of loss. Carried to the ultimate this means to have converted the probability of

> loss into "expectation of loss" or value of the risk. Thereby is determinable the consideration to be charged ...

Conn. Gen. Life Ins. Co. v. Shelton, 611 S.W.2d 928, 930 (Tex. App. - Fort Worth 1981, writ ref'd n.r.e.). The *Shelton* court further noted that, for a risk to be insurable, it "must be genuine, must exist for large groups of people, and its existence must be recognized by a sufficient number of people to warrant the establishment of organization(s) to insure it."

Unique agreements are an exception. "When the agreement is unique, the insured's risk is transferred to an insurer who bears it alone, but when the agreement is a standard policy offered by an insurer to the general public, the insured's risk is, in a real sense, borne by the insurer's policyholders as a group, from whose pool of premiums all claims must be paid if the insurer is to remain in business." *Fairfield Ins. Co.*, 246 S.W.3d at 673-74 (Hecht, J., concurring).

7. Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?

Texas does not provide a statutory definition for "life insurance;" however, Texas does provide some specific statutory definitions related to life insurance. For instance, a "life insurance company" is a corporation authorized under a charter to engage in business involving the payment of money or another thing of value conditioned on the continuance or cessation of human life or involving an insurance, guaranty, or contract for the payment of an endowment or annuity. TEX. INS. CODE ANN. § 841.001(9).

"Wholesale, franchise, or employee life insurance" means a term life insurance plan under which a number of individual term life insurance policies are issued to a selected group at a rate that is lower than the rate shown in the issuing insurer's manual for an individually issued policy of the same type issued to an insured of the same class.

"Industrial life insurance" means life insurance under which the premiums are payable: (1) weekly; or (2) less often than weekly but at least monthly, if the face amount of insurance coverage provided by the policy is $1,000 or less. TEX. INS. CODE ANN. § 1151.001.

"Credit life insurance" means insurance on the life of a debtor in connection with a specific credit transaction. TEX. INS. CODE ANN. § 1153.003.

Distinction from Similar Types of Contracts and Exemptions

8. Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.

i) Contracts of gambling and chance

Insurance contracts are distinguished from contracts of gambling and chance (which generally are unenforceable) by the existence of an "insurable interest" in the subject matter of the contract. *See, e.g., Fairfield Ins. Co.*, 246 S.W.3d at 674 (Hecht, J., concurring). The Texas Supreme Court has described an insurance agreement as an "aleatory contract; that is, a contract in which a promise is conditioned on the happening of a fortuitous event, an event of chance." *In re Tex. Ass'n of School Boards, Inc.*, 169 S.W.3d at 658. Similarly, a wager has been defined as a contract by which two or more parties agree that a sum of money or other thing shall be paid or delivered to one of them on the happening of an uncertain event. *Herndon v. State,* 543 S.W.2d 109, 121 (Tex. Crim. App. 1976). However, under Texas law:

> It is generally agreed that mere wager policies - that is, policies in which the assured party has no interest whatever in the matter insured, but only an interest in its loss or destruction - are void, as against public policy.

Fairfield Ins. Co., 246 S.W.3d at 67 (Hecht, J., concurring); *see also Stillwagoner*, 979 S.W.2d at 363 (life policy on lower-level employee rejected as a "wagering contract" where the employer demonstrated *no* insurable interest).

ii) Warranty, guaranty or any other surety contracts

<u>Warranties</u>

Warranties generally are not considered contracts of insurance though they may contain all the essential elements of an insurance contract. *Rayos v. Chrysler Credit Corp.*, 683 S.W.2d 546, 548 (Tex. App.—El Paso 1985, no writ). A warranty is issued to provide protection against defects or failures in a product, whereas an insurance policy is issued to provide reimbursement or indemnity based on an accident or occurrence unrelated to any defect or failure in the product. *Id.* In determining whether an agreement is a warranty or an insurance contract, the question is whether, looking at a plan of operation as a whole, service rather than indemnity is the principal object and purpose of the agreement. *Id.*

<u>Service contracts</u>

Although distinguished from insurance, service contracts also have attracted legislation and are regulated in Texas. For example, Texas passed the Service Contract Regulatory Act ("SCRA"), Texas Occupations Code, Chapter 1304. The SCRA defines a service contract as an agreement for separately stated consideration (in addition to the price of the product) "under which a provider agrees to repair, replace, or maintain a product or provide

indemnification for the repair, replacement, or maintenance of a product, for operational or structural failure or damage caused by a defect in the materials or workmanship or by normal wear." TEX. OCC. CODE ANN. § 1304.003(a)(1)-(2). A service contract may also provide for: "(1) incidental payment or indemnity under limited circumstances, including towing, rental, and emergency road service; (2) the repair or replacement of a product for damage resulting from a power surge or for accidental damage incurred in handling the product; or (3) identity recovery, as defined by [TEX. OCC. CODE ANN. §] 1306.002, if the service contract is financed under Chapter 348 of 353, Finance Code." TEX. OCC. CODE ANN. § 1304.003(a)(1)-(2).

The SCRA exempts certain contracts, such as, for example, "a warranty" as defined by the act[2], and where conditions are met, service contracts sold by a motor vehicle dealer[3].

Assuming all conditions of the SCRA are met, service contracts may be issued by a "provider", that is "contractually obligated to a service contract holder under the terms of the contract." TEX. OCC. CODE ANN. § 1304.002(7). Service contracts may also be issued by a "seller" that, unlike the provider, is not contractually obligated to the service contract holder (consumer). TEX. OCC. CODE ANN. § 1304.002(8-a). "Marketing, selling, offering for sale, issuing, making, proposing to make, and administering a service contract" are exempt from "the Insurance Code and other laws of this state regulating the business of insurance." TEX. OCC. CODE ANN. § 1305(3). The Executive Director of the Texas Department of Licensing and Regulation ("TDLR") investigates and enforces the SCRA. TEX. OCC. CODE ANN. § 1304.051.

Other acts of note are the Residential Service Company Act, TEX. OCC. CODE ANN. § 1303.001 *et seq.*, under the authority of the Texas Real Estate Commission, and the Identity Recovery Service Contract Regulatory Act, TEX. OCC. CODE ANN. § 1306.001 *et seq.*, under the authority of TDLR.

Guaranty and surety contracts

Making or proposing to make, as a guarantor or surety, a guaranty or suretyship contract as a vocation and not merely incidental to another legitimate business or activity of the guarantor or surety, constitutes conducting the business of insurance in Texas. TEX. INS. CODE ANN. § 101.051(b)(2). Surety bonds and related instruments are governed by TEX. INS. CODE ANN. §§ 3503.001 et. seq.

However, as recognized by the Texas Supreme Court, the "business of insurance" means different things in different Sections of the Texas Insurance Code and surety contracts are not covered by all provisions of the code. *See Dallas Fire Ins. Co. v. Tex. Contractors Surety & Cas. Agency*, 159 S.W.3d 895, 896 (Tex. 2004) (concluding that former Texas Insurance Code article 21.21 (private action for unfair and deceptive acts or practices) could not be applied to surety business in light of the unique characteristics of suretyship and absent clear legislative directive to the contrary). The Texas Supreme Court has noted:

> [T]he characteristics of suretyship are different from those of insurance. Insurance involves the pooling and spreading of risk of the insureds, with no right of indemnity possessed by the insurer. Suretyship, on the other hand, allows a surety full rights of indemnity against its principal.

Great Am. Ins. Co. v. N. Am. Mun. Util. Dist. No. 1, 908 S.W.2d 415, 424 (Tex. 1995).

iii) Financial contracts such as hedging contracts/swaps/derivatives

Financial contracts (or investment contracts) generally are governed by the Texas Securities Act, which expressly excludes insurance contracts. "Hedging" is a method used to protect one's investment or an investor against loss by making balancing or compensating contracts or transactions. *Black v. Shor*, --- S.W.3d ---, 2013 WL 1687537, at *10 n.3 (Tex. App. - Corpus Christi Apr. 18, 2013). The term "derivative" refers to "financial instruments whose performance is derived in whole or in part from the performance of an underlying asset (such as a security index of securities). *Laborers Nat'l Pension Fund v. N. Trust Quantitative Advisors, Inc.*, 173 F.3d 313, 318 (5th Cir. [Tex.] 1999). A "swap" is a form of derivative, where counterparties exchange cash flows of one party's financial instrument for those of the other party's financial instrument. *See id.*

Contracts relating to hedging, swaps, and derivatives generally are classified as "investment contracts" under Texas law. Texas courts employ the same test articulated by the U.S. Supreme Court to determine whether an arrangement qualifies as an "investment

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[2] A "warranty" is defined as "an undertaking made solely by the manufacturer or importer of a product or the seller of a product or service that: (A) guarantees indemnity for a defective part, mechanical or electrical breakdown, or labor cost or guarantees another remedial measure, including the repair or replacement of the product or the repetition of service; (B) is made without payment of additional consideration; (C) is not negotiated or separated from the sale of the product or service; and (D) is incidental to the sale of the product or service." TEX. OCC. CODE ANN. § 1304.004(a)(2).

[3] A contract will be exempted under the act when "sold by a motor vehicle dealer on a motor vehicle sold by that dealer, if the dealer: (A) is the provider; (B) is licensed as a motor vehicle dealer under Chapter 2301; and (C) covers its obligations under the service contract with a reimbursement insurance policy". TEX. OCC. CODE ANN. § 1304.004(b)(6).

contract" (*i.e*., the Howey test). *E.g., H.E. Searsy v. Commercial Trading Corp*., 560 S.W.2d 637, 640 (Tex. 1978); *Caldwell v. State*, 95 S.W.3d 563, 566-67 (Tex. App. - Houston [1st Dist.] 2002, pet. ref'd) An investment contract requires: (1) the investment of money; (2) a common enterprise; (3) expectation of profits; (4) solely from the efforts of others. *H.E. Searsy*, 560 S.W.2d at 640; *Caldwell*, 95 S.W.3d at 566-67 "Investment contracts" are included in the definition of securities under the Texas Securities Act, and governed by securities law. *H.E. Searsy*, 560 S.W.2d at 639-40; *Caldwell*, 95 S.W.3d at 566-67.

The Texas Securities Act expressly *excludes* insurance contracts from the definition of a "security," noting:

> [T]his definition shall not apply to any insurance policy, endowment policy, annuity contract, optional annuity contract, or any contract or agreement in relation to and in consequence of any such policy or contract, issued by an insurance company subject to the supervision or control of the Texas Department of Insurance when the form of such policy or contract has been duly filed with the Department as now or hereafter required by law.

TEX. REV. CIV. STAT. art. 581-4(A); *see also Griffitts v. Life Partners, Inc*., No. 10-01-00271-CV, 2004 WL 1178418, at *3-4 (Tex. App. - Waco May 26, 2004) (rejecting argument that life insurance policies constitutes securities).

In 2010, the federal Dodd-Frank Wall Street Reform and Consumer Protection Act ("the Dodd-Frank Act") provided that swaps could not be subject to regulation as an insurance product by any state. PUB. L. NO. 111-203, §722(b) (2010).

9. <u>Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?</u>

As discussed further above, a "warranty" may contain all the essential elements of an insurance contract, but service - rather than indemnity - will be the principal objective of the contract. See *Rayos*, 683 S.W.2d at 548.

10. <u>Does a close legal or economic nexus to a non-insurance transaction provide for such exception?</u>

n/a

Impact of Qualification – Supervisory law

11. <u>Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?</u>

A party may not directly or indirectly do an act that constitutes the business of insurance, as provided by the Texas Insurance Code, except as authorized by statute. TEX. INS. CODE ANN. § 101.102(a). However, with respect to insurance of a subject that is resident, located, or to be performed in Texas, the Texas Insurance Code does not prohibit an act performed outside Texas - including the collection of premiums - by a party authorized to do business in Texas, if the transaction and insurance contract otherwise comply with law. TEX. INS. CODE ANN. § 101.102(b).

However, surplus lines insurance allows a person who seeks to insure a Texas risk but is unable to obtain that insurance from a Texas-licensed insurer to seek the insurance from an insurer that is not licensed in Texas but is an "eligible" surplus lines insurer. TEX. INS. CODE ANN. § 981.001. An insurer is an "eligible" surplus lines insurer if it meets certain minimum capital and surplus requirements outlined in the insurance code. TEX. INS. CODE ANN. §§ 981.002(1), 981.057.

Surplus lines insurance *must* be obtained through a licensed Texas agent. If surplus lines insurers do not place their surplus lines insurance through a licensed Texas agent, they are engaging in unauthorized insurance. *Strayhorn v. Lexington Ins. Co*., 128 S.W.3d 772, 785 (Tex. 2004). "Only an insurer who receives premiums on independently procured insurance on which a premium-receipts tax has been paid is excepted from this liability." *Id.*

It should be noted that the Dodd-Frank Act, among other things, limits states' abilities to regulate certain types of cross-border insurance, including surplus lines. *See* PUB. L. NO. 111-203, §§ 501 et seq. Specifically, the Dodd-Frank Act changes the status quo with respect to non-admitted insurance (including surplus lines) and provides that a non-admitted insurer is only regulated by the regulator of the insured's home state: "[e]xcept as otherwise provided in this Section, the placement of non-admitted insurance shall be subject to the statutory and regulatory requirements solely of the insured's home State." 15 U.S.C. § 8202(a) (formerly at PUB. L. NO. 111-203, § 522). This Section, which became effective in July 2011, should simplify the process of providing insurance on a non-admitted basis.

On 28 February 2013, the Texas Legislature introduced a bill (S.B. 951) intended to amend state law relating to surplus lines insurance to conform to federal law, following the passage of the Dodd-Frank Act. S.B. 951 amends the Texas Insurance Code (§§ 981.001 et seq.) to apply statutory provisions regulating surplus lines to insurance provided to an insured whose home state is Texas, removing provisions that previously restricted application to the insurance of a subject that is resident, located, or to be performed in Texas and to insurance that is obtained, continued, or renewed through negotiations or an application wholly or partly occurring or made within or from within Texas or through premiums wholly or partly remitted directly or indirectly from within Texas.

S.B. 951 defines "home state," with respect to an insured, as the state in which the insured maintains the insured's principal residence if the insured is an individual; the state in which the insured maintains the insured's principal place of business if the insured is not an individual; the state to which the greatest percentage of the insured's taxable premium for an insurance contract that covers risk is allocated if 100 percent of the insured risk is located outside of the state in which the insured maintains the insured's principal residence or principal place of business, as applicable; or, for an affiliated group, the home state of the member that has the largest percentage of premium attributed to it under the insurance contract. The bill redefines "surplus lines insurance" to remove the condition that the insurance coverage be for a subject that is resident, located, or to be performed in Texas.

After being passed by the Texas Legislature, S.B. 951 was signed into law by the Governor on June 14, 2013, to be effective immediately.

12. <u>What are the legal consequences for the risk-taker acting without license?</u>

<u>Civil Penalty</u>

An insurer that acts without a license is subject to a civil penalty of up to USD 10,000 for each act of violation and for each day of violation. TEX. INS. CODE ANN. § 101.105(a). The Insurance Commissioner may request that the attorney general institute a civil suit in a district court in Travis County for injunctive relief to restrain an insurer from continuing a violation or threat of violation. TEX. INS. CODE ANN. § 101.105(b).

Criminal Penalty

An insurer that intentionally, knowingly, or recklessly acts without a license commits a felony of the third degree. TEX. INS. CODE ANN. § 101.106(a) & (b).

<u>Administrative Penalty</u>

The TDI may impose an administrative penalty on a person licensed or regulated under the code who violates a provision of the Texas Insurance Code or any other Texas insurance law. TEX. INS. CODE ANN. § 84.021. The penalty for a violation may not exceed USD 25,000, unless a greater or lesser penalty is specified by the Texas Insurance Code or another Texas insurance law. TEX. INS. CODE ANN. § 84.022(a). The amount of the penalty shall be based on:

(1) The seriousness of the violation, including: (A) the nature, circumstances, extent, and gravity of the violation; and (B) the hazard or potential hazard created to the health, safety, or economic welfare of the public;

(2) The economic harm to the public interest or public confidence caused by the violation;

(3) The history of previous violations;

(4) The amount necessary to deter a future violation;

(5) Efforts to correct the violation;

(6) Whether the violation was intentional; and

(7) Any other matter that justice may require.

Tex. Ins. Code Ann. § 84.022(b).

13. <u>In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.</u>

An insurer authorized to engage in the insurance business in Texas may be a member of an insurance holding company system, but must register with the Commissioner of Insurance. TEX. INS. CODE ANN. § 823.051. Texas statute provides that "[i]t is consistent with the public interest and the interest of policyholders to permit insurers to:

(1) engage in activities that would enable the insurers to make better use of management skills and facilities;

(2) have free access to capital markets that could provide funds for insurers to use in diversification programs;

(3) implement sound tax planning conclusions; and

(4) serve the changing needs of the public and adapt to changing conditions of the social, economic, and political environment, so that insurers are able to compete effectively and to meet the growing public demand for institutions capable of providing a comprehensive range of financial services.

Tex. Ins. Code Ann. § 823.001(a). The TDI regulates insurance carriers and their relationships with affiliated entities. The TDI monitors the financial condition and risk profiles of holding company systems or groups of affiliates, recognizing that risks posed by non-insurance operations can potentially spread to insurance companies and negatively impact their financial condition.

14. <u>Do the terms and conditions of insurance contracts need to be</u>

i) <u>submitted to the regulator as a kind of formal requirement or</u>

ii) <u>approved by the regulator prior to entering into effect?</u>

"Insurers doing business in [Texas] are required to use policies and endorsements approved by our State Board of Insurance." *Urrutia v. Decker*, 992 S.W.2d 440, 443 (Tex. 1999). Policies covered by these requirements include:

- Life, health, and accident insurance policies, TEX. INS. CODE ANN. §§ 1701.051, et. seq.;

- Title insurance, TEX. INS. CODE ANN. § 2703.002; and

Certain types of liability, casualty, and property insurance, including general liability insurance, residential and commercial property insurance, financial guaranty insurance, personal and commercial automobile insurance, and fidelity, guaranty and surety bonds other than criminal court appearance bonds, TEX. INS. The Texas Supreme Court has held that an unapproved endorsement or clause that conflicts with an approved provision in a standard form policy is unenforceable. *Urrutia*, 992 S.W.2d at 443. Insurance sold through a policy *not* approved by the TDI is voidable rather than void, and the insured may elect to rescind the policy or to accept it and be bound by the agreed terms. *Id*.

Any agreement to issue insurance policies that have not been approved by the TDI is illegal. *Oakes v. Aetna Cas. & Surety Co.*, 551 S.W.2d 504, 506 (Tex. App.—Amarillo 1977, writ ref'd n.r.e.).

Impact of Qualification – Law of Contracts

15. Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?)?

Under Texas law, an insurance contract entered into by an unauthorized party is unenforceable by that party, *e.g., Ware v. Heath*, 237 S.W.2d 362, 363-64 (Tex. App. - Fort Worth 1951, no writ) (denying lender right to recover alleged balance where court concluded that charges related to waiver due to sickness or death amounted to a contract of insurance in violation of states regulations), and a person who in any manner assisted directly or indirectly in the procurement of the contract is liable to the insured for the full amount of a claim or loss under the terms of the contract if the unauthorized insurer fails to pay the claim or loss. TEX. INS. CODE ANN. § 101.201(a).

This Section does not apply to insurance procured by a licensed surplus lines agent from an eligible surplus lines insurer as defined by Chapter 981 and independently procured contracts of insurance, as described in TEX. INS. CODE ANN. § 101.053(b)(4) that are reported and on which premium tax is paid in accordance with Chapter 225 or 226. TEX. INS. CODE ANN. § 101.201(b).

16. Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.

As the Texas Supreme Court has observed, "[The Texas] Insurance Code is somewhat different from Texas's other statutory codifications in that it is not a formal, unified Code containing uniform definitions." *E.g., Tex. Dept. of Ins. v. Am. Nat'l Life Ins. Co.*, --- S.W.3d ---, 2012 WL 1759457, at *4 (Tex. May 18, 2012). Significant statutes applicable to insurance contracts in Texas include: consumer protection statutes, *see* TEX. INS. CODE ANN. §§ 541.001, et. seq. (Deceptive, Unfair and Prohibited Practices) *and* TEX. INS. CODE ANN. §§ 542.001, et. seq. (Unfair Claim Settlement Practices); life insurance and annuities-related statutes, *see* TEX. INS. CODE ANN. §§ 1101.001, et. seq.; health and accident insurance-related statutes, TEX. INS. CODE ANN. §§ 1201.001, et. seq.; property and casualty insurance-related statutes, *see* TEX. INS. CODE ANN. §§ 1801.001, et. seq.; and title insurance statutes, see TEX. INS. CODE ANN. §§ 2501.001, et. seq.

17. Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.

Insurers doing business in Texas are required to use policies and endorsements adopted or approved by the TDI. *Urrutia v. Decker*, 992 S.W.2d 440, 443 (Tex. 1999). Following are specific statutory requirements for certain lines of insurance:

Accident and Health Insurance

The Texas Insurance Code specifies certain terms that must be included in an accident and health insurance policy, including: a statement of the consideration for the policy; the time of the policy's effectiveness and termination; the persons insured; any exceptions to or reductions of indemnity for the policy; the form number; incorporation of or reference to other documents; notification that the policy is returnable for a refund; notice of limitations on the termination of coverage for a child based on age; and required definitions. TEX. INS. CODE ANN. §§ 1201.051-065.

The Texas Insurance Commissioner may adopt rules prohibiting specific individual accident and health insurance policy provisions not specifically authorized by statute that the Commissioner determines are unjust, unfair, or unfairly discriminatory to the policyholder, an insured under the policy, or a beneficiary. TEX. INS. CODE ANN. §§ 1201.102.

Automobile Insurance

A personal automobile insurance policy form must comply with applicable state and federal law, and may not be used unless the form is written in plain language, such that it achieves the minimum score established by the Texas Insurance Commissioner on the Flesch reading ease test (or an equivalent test selected by the Commissioner) or (if permitted by the Commissioner) conforms to the language requirements in a National Association of Insurance Commissioners model act relating to plain language. TEX. INS. CODE § 2301.053.

Each form for a personal automobile insurance policy must provide the coverages mandated under Texas Insurance Code, Chapter 1952, Subchapters C

(Uninsured or Underinsured Motorist Coverage) and D (Personal Injury Protection Coverage), unless the coverages are rejected by the named insured in the manner provided by those subchapters. TEX. INS. CODE § 2301.053(b).

A contract or agreement that is not written into an application for personal automobile insurance coverage and the personal automobile insurance policy is void, violates the Texas Insurance Code, and constitutes grounds for the revocation of an insurer's certificate of authority to write personal automobile insurance in Texas. TEX. INS. CODE § 2301.054.

A personal automobile insurance policy, or any similar policy form adopted by the Texas Insurance Commissioner or filed for approval by the Commissioner, that covers liability arising out of ownership, maintenance, or use of a motor vehicle of a spouse who is otherwise insured by the policy *must* contain a provision to continue coverage for the spouse during a period of separation in contemplation of divorce. TEX. INS. CODE § 1952.056. An insurer *may not* deliver or issue for delivery in Texas an automobile insurance policy that provides payment on final conviction of the named insured for loss for a covered motor vehicle seized by federal or state law enforcement officers as evidence in a case against the named insured under Chapter 481, Health and Safety Code, or under the federal Controlled Substances Act (21 U.S.C. §§ 801 et seq.). TEX. INS. CODE § 1952.057.

Individual Life Insurance

An individual life insurance policy form must contain a number of statements and provisions, as outlined at 28 TEX. ADMIN. CODE. §§ 3.101 et. seq., including but not limited to (1) a provision that premiums are payable in advance; (2) a provision that all statements made by the insured, absent fraud, shall be representations and not warranties; and (3) a provision that the policy, or policy and application, shall constitute the entire contract between the parties.

Residential Property Insurance

A residential property insurance form must comply with applicable state and federal law, and may not be used unless the form is written in plain language, such that it achieves the minimum score established by the Texas Insurance Commissioner on the Flesch reading ease test (or an equivalent test selected by the Commissioner) or (if permitted by the Commissioner) conforms to the language requirements in a National Association of Insurance Commissioners model act relating to plain language. TEX. INS. CODE § 2301.053.

Windstorm and Hail Insurance in a Designated Catastrophe Area

A policy form or printed endorsement form (for residential or commercial property insurance) may provide for a contractual limitations period for filing suit on a first-party claim under the policy. TEX. INS. CODE § 2301.010(b). The contractual limitations period may not end before the earlier of: (1) two years from the date the insurer accepts or rejects the claim; or (2) three years from the date of the loss that is the subject of the claim. *Id.* Such a policy or endorsement may also contain a provision requiring that a claim be filed with the insurer not later than one year after the date of the loss that is the subject of the claim, unless good cause for the delay has been shown. TEX. INS. CODE § 2301.010(c).

A provision contrary to SubSection (b) or (c) is void. TEX. INS. CODE § 2301.010(d). If a provision is voided pursuant to TEX. INS. CODE § 2301.010(d), the voiding of the provision does not affect the validity of other severable provisions of the policy.

An insurer using a policy form or endorsement form that includes a provision described by SubSection (b) or (c) shall, at the time the policy or endorsement is issued or renewed, disclose in writing to an applicant or insured the contractual limitations or claims filing period, as applicable, in the policy or endorsement. TEX. INS. CODE § 2301.010(f).

To encourage authorized insurers to write windstorm and hail insurance, the TDI may approve policy or contractual provisions other than those described by SubSections (b) and (c) that are consistent with sound underwriting and insurance principles, and meet other relevant statutory requirements. TEX. INS. CODE § 2301.010(e).

18. Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.

Consumer Protection Provisions

The Texas Insurance Code contains a number of consumer protection provisions.[4] Consumer protections that have been put in place include:

[4] *See, e.g.*, Chapter 521 (Consumer Information and Complaints); Chapter 522 (Consumer Information in Spanish); Chapter 523 (Market Assistance Program for Residential Property Insurance); Chapter 524 (Health Coverage Awareness and Education Program); Chapter 541 (Unfair Methods of Competition and Unfair or Deceptive Acts or Practices); Chapter 542 (Processing and Settlement of Claims); Chapter 543 (Prohibited Practices Related to Policy or Certificate of Membership); Chapter 544 (Prohibited Discrimination); Chapter 545 (HIV Testing); Chapter 546 (Use of Genetic Testing Information); Chapter 547 (False Advertising by Unauthorized Insurers); Chapter 548 (Insurer Insider Trading and Proxy Regulation); Chapter 549 (Prohibited Practices Relating to Property Insurance); Chapter 550 (Prohibited Practices Relating to

- Toll-free telephone numbers. An insurance company whose gross annual premium receipts collected in Texas are more than USD 2,000,000.00 a year is required to establish a toll-free telephone number to provide information about policies to consumers and to accept complaints from policyholders. Tex. Ins. Code Ann. §§ 521.101, 521.102.
- Claims reporting. An insurer may not report to a claims database (i.e., a database used by insurers to share, among insurers, claims histories or damage reports concerning covered parties) information regarding an inquiry about coverage by an insured under an automobile or residential property policy *unless and until* the insured actually files a claim under the policy. Tex. Ins. Code Ann. §§ 563.101, 563.102.
- Written Statement of Reasons for Cancellation, Declination, or Nonrenewal. Whenever an insurer cancels, declines coverage, or fails to renew a policy of insurance, including liability and property and casualty policies, the insurer must fully explain the decision in a written statement and specifically state: (1) the precise incident, circumstance, or risk factors applicable to the applicant or policyholder that violate guidelines; (2) the source of information which was relied on regarding the incident, circumstance, or risk factors; and (3) specify any other information deemed relevant by the Commissioner of Insurance. Tex. Ins. Code Ann. § 551.002.
- Limitation on Actions in Other State Courts. No action or legal proceedings based upon a contract of insurance between a foreign or alien insurance company and a Texas resident, which was entered into in Texas, may be brought in or transferred to a court in another state without the consent of the Texas consumer. Tex. Ins. Code Ann. § 982.305.
- "Consumer bill of rights." The public insurance counsel's powers and duties include a directive to adopt a "consumer bill of rights" for each "personal line of insurance" to be distributed upon the issuance of policies to policyholders. Tex. Ins. Code Ann. § 501.156. Policy forms which describe the "Bill of Rights" are routinely provided with automobile and homeowners/renters insurance policies.

Private Cause of Action for the Insured

Chapter 541 of the Texas Insurance Code provides a private cause of action to an insured against an insurer for unfair or deceptive insurance practices. An insurer can be liable for deceptive insurance practices if the insurer engages in acts or practices that violate:

1. Texas Insurance Code chapter 541, subchapter B, which prohibits:

a) Unfair competition activities, including, but not limited to, defamation; boycott, coercion, and intimidation; false financial statements; unfair discrimination; and use of deceptive names, words, or slogans. TEX. INS. CODE ANN. §§ 541.053-55, .058(b) & .059(a).

b) False advertising and specific misrepresentations, including, but not limited to, making a statement misrepresenting the terms of a policy, the benefits or advantages promised by a policy, or the dividends or share of surplus to be received on a policy. TEX. INS. CODE ANN. §§ 541.051 & 541.052.

c) Misrepresentations about an insurance policy, including, but not limited to making untrue statements of material fact; leaving out material facts so that other statements are rendered misleading, making misrepresentations of law, and not disclosing any matter required by law to be disclosed. TEX. INS. CODE ANN. § 541.061.

d) Unfair settlement practices, including, but not limited to, misrepresenting a material fact or policy provision relating to coverage at issue***;*** not attempting in good faith to effectuate a prompt, fair, and equitable settlement of a claim with respect to which the insurer's liability has become reasonably clear***;*** failing to promptly provide to a policyholder a

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Payments); Chapter 551 (Practices Relating to Declination, Cancellation, and Nonrenewal of Insurance Policies); Chapter 552 (Illegal Pricing Practices); Chapter 553 (Enforcement of Insurance Policies Regarding Holocaust Victims); Chapter 554 (Burden of Proof and Pleading); Chapter 555 (Failure to Satisfy Judgment); Chapter 556 (Unfair Methods of Competition and Unfair Practices by Financial Institutions); Chapter 557 (Insured Property Subject to Security Interest); Chapter 558 (Refund of Unearned Premium); Chapter 559 (Credit Scoring and Credit Information); Chapter 560 (Prohibited Rates); and Chapter 562 (Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Regarding Discount Health Care Programs); Chapter 563 (Practices Relating to Claims Reporting); Chapter 601 (Privacy); Chapter 602 (Privacy of Health Insurance Information); and Chapter 651 (Financing of Insurance Premiums); Chapter 701 (Insurance Fraud Investigations); Chapter 703 (Covered Entity's Antifraud Action); Chapter 704 (Antifraud Programs); Chapter 705 (Misrepresentations by Policyholders); Chapter 706 (Identity Theft Insurance); and Chapter 751 (Market Conduct Surveillance).

reasonable explanation of the basis in the policy, in relation to the facts or applicable law, for the insurer's denial of a claim or offer of a compromise settlement of a claim. TEX. INS. CODE ANN. § 541.060.

2. The Texas Deceptive Trade Practices Act ("DTPA"), which prohibits false, misleading, or deceptive acts and practices, including, but not limited to:

a) Representing that goods or services have characteristics or benefits that they do not have. TEX. BUS. & COMM. CODE ANN. § 17.46(b)(5).

b) Representing that an agreement confers or involves rights, remedies, or obligations that it does not have, or that are prohibited by law. TEX. BUS. & COMM. CODE ANN. § 17.46(b)(12).

c) Failing to disclose information concerning goods or services which was known at the time of the transaction when such failure to disclose such information was intended to induce the consumer into a transaction into which the consumer would not have entered had the information been disclosed. TEX. BUS. & COMM. CODE ANN. § 17.46(b)(24)

d) Generally engaging in unconscionable courses of action while handling an insurance claim. TEX. BUS. & COMM. CODE ANN. § 17.50(a)(3). The DTPA defines an "unconscionable action" as an act or practice which, to a consumer's detriment, takes advantage of the lack of knowledge, ability, experience, or capacity of the consumer to a grossly unfair degree. TEX. BUS. & COMM. CODE ANN. § 17.45(5).

e) Violating the provisions of the Texas Insurance Code. TEX. BUS. & COMM. CODE ANN. § 17.50(a)(4).

19. Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?

Under Texas law, an insurance policy provision that states that (1) a misrepresentation, including a false statement, made in a proof of loss makes the policy void or voidable; or (2) false statements made in the application for the policy or in the policy make the policy void or voidable, has no effect and is not a defense in a suit brought on the policy. TEX. INS. CODE ANN. §§ 705.003(a) (Misrepresentation in Proof of Loss or Death); 705.004(a) (Misrepresentation in Policy Application).

To void an insurance policy for misrepresentation, the insurer must plead and prove: (1) the insured's making of a representation; (2) the falsity of the representation; (3) reliance on the misrepresentation by the insurer; (4) the intent to deceive on the part of the insured in making the misrepresentation; and (5) the materiality of the misrepresentation. TEX. INS. CODE ANN. §§ 705.003(b); 705.004(b); *Texas Farm Bureau Mut. Ins. Co. v. Rogers*, 351 S.W.3d 103, 107 (Tex. App. - San Antonio 2011) (no pet.); *Temcharoen v. United Fire Lloyd's*, 293 S.W.3d 332, 341 (Tex. App. - Eastland 2009) (pet. denied); *see also Medicus Ins. Co. v. Todd*, --- S.W.3d ---, 2013 WL 1928519 at *4 (Tex. App.—Dallas May 10, 2013) (noting, "Although [Section 705.004] does not expressly require the insurer to prove the insured's intent to deceive, the Texas Supreme Court has imposed that requirement.")

In determining the materiality of the misrepresentation, the key consideration is whether the insurer would have accepted the risk if the true facts had been disclosed. *Rogers*, 351 S.W.3d at 107. It is a question of fact whether a misrepresentation made in the application for a policy or in the policy itself was material to the risk or contributed to the contingency or event on which the policy became due and payable. TEX. INS. CODE ANN. §§ 705.004(c). In order to void coverage, the insured's false representation must have been made willfully and not as the result of inadvertence or mistake. Temcharoen, 293 S.W.3d at 341.

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Template

This template, accompanied by explanations of the purpose of each question, was sent to contributors to the project in May 2013. Responses were received in during the summer of 2013, followed by an editing process that was carried out in close cooperation with the contributors and concluded in September with the publication of this report.

Definition of an Insurance Contract

1. **Is there a definition in your jurisdiction with regard to an insurance contract, based on either statutory or case law? Please summarize the legal requirements for an insurance contract by identifying the main criteria.**

2. **Does an insurance contract require an element of uncertainty? Please describe.**

3. **Does an insurance contract need to provide for a transfer of risk from the one party to another to be recognized as an insurance contract?**

4. **Does the insured party need to have an economic, legal or any other interest in the subject matter of an insurance contract (usually called ‘insured interest’)?**

5. **Is it required that an insured interest attaches to the policyholder (i.e. the party entering into the insurance contract) or can it be attributable to a third party? In the later case, must this third party be the beneficiary under the insurance contract?**

6. **Is it necessary or relevant that the risk assumed by the insurer will be mitigated by the simultaneous insurance of a larger number of similar risks (called also the ‘law of the large numbers’)? If yes, does it affect the classification as an insurance contract or is it merely a supervisory and actuarial issue?**

7. **Does the definition of an insurance contract differ between life insurance and non-life insurance (obviously apart from the subject matter)?**

Distinction from Similar Types of Contracts and Exemptions

8. **Please consider whether an insurance contract has similarities to the following contractual arrangements existing under the laws of your jurisdiction. Please describe if these are regarded as a type of insurance contract or, if not, what the distinction is.**

   (i) Contracts of gambling and chance

   (ii) Warranty, guaranty or any other surety contracts

   (iii) Financial contracts such as hedging contracts/swaps/derivatives

9. **Do exceptions or exemptions exist to the effect that contracts, which in principle meet the characteristics of an insurance contract, are not treated as such?**

10. **Does a close legal or economic nexus to a non-insurance transaction provide for such exception?**

Impact of Qualification – Supervisory law

11. **Can a party as risk-taker enter into a contract with qualifies as insurance contract only on the basis of a permission/license?**

12. **What are the legal consequences for the risk-taker acting without license?**

13. **In the laws of your jurisdiction, is there a prohibition for licensed insurance companies to enter into non-insurance business? If yes, please briefly explain the scope of such prohibition.**

14. **Do the terms and conditions of insurance contracts need to be (i) submitted to the regulator as a kind of formal requirement or (ii) approved by the regulator prior to entering into effect?**

Impact of Qualification – Law of Contracts

15. **Would a contract of insurance issued by a non-licensed party be legally valid or null and void or can it be avoided by either party (e.g. is the policyholder entitled to terminate or contest the contract? Is the policyholder entitled to claim damages?).**

16. **Are there specific legal provisions or statutes applicable to insurance contracts in your jurisdiction? Please identify.**

17. **Do these legal provisions or statutes contain for legal requirements with regard to form and the content of an insurance contract? If yes, please outline these requirements.**

18. **Do your laws provide for consumer protection with respect to insurance contracts, e.g. by establishing information or other requirements? If yes, please briefly describe.**

19. **Is there anything else you would like to add with respect to your jurisdiction that could be of interest to this project?**