



AUGUST 2007

## In-sure

This month's roundup of developments affecting the insurance industry sees the European Commission's draft Directive for Solvency II and its call for further advice from CEIOPS. Also in this issue, the HM Treasury consults on the implementation of the Reinsurance Directive

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### Market round up

#### Insurance Claims could top £3bn

Insurers face more than £3bn of claims from the floods in June and July, forcing up the cost of insurance and raising questions about its availability, analysts have warned. The Association of British Insurers said it had received 8,000 claims from the flooding over the past 72 hours. Its initial estimate of the insurance losses from the deluge over recent days is £500m, taking total claims from the summer flooding to at least £2bn. The Government has so far paid out £14m to areas hit by the June flooding and promised another £10m for last week's victims. (*Financial Times*, 25 July 2007) - [Back](#)

#### Insurers Enlist Third-Party Asset Specialists

From AIG in the US, to Allianz of Germany, Italy's Assicurazioni Generali, Axa of France and the UK's Prudential, Standard Life, Scottish Widows and Norwich Union, insurers have scaled the heights of the asset management industry. But a growing minority of insurers are turning their backs on this approach and outsourcing their asset management needs, creating a potentially lucrative market for the investment industry given the scale of insurance assets, estimated at \$15,000bn (£7,500bn). The trend is largely attributed to the ever rising complexity of asset management as well as a perceived need to squeeze higher returns from assets. While some insurers are reacting to this by outsourcing all of their asset management, others are retaining responsibility for their fixed-income assets, but outsourcing risk-seeking mandates, where they may lack the relevant expertise. (*Financial Times*, 2 July 2007) - [Back](#)

#### Firms Change the Way they sell PPI

The Financial Services Authority (**FSA**) announced on its website that major finance firms have agreed to change the way they sell payment protection insurance (**PPI**) over the internet. Those firms have been offering



loans on their website whereby PPI was automatically included by techniques like "pre-ticked" boxes. The consumer did not have to make an active decision to buy PPI. The agreed change now provides that the consumer makes an active decision.

This agreement is the latest in a series of initiatives by the FSA to improve sales standards in the PPI market. Earlier this year the FSA and a number of trade associations reached an agreement on greater fairness and transparency with regard to refunds of single premium PPI policies. Other measurements include proposed changes to the Insurance Conduct of Business rules which aim to improve selling practises on PPI and other protection products. (Source: FSA) - [Back↑](#)

## EU Insurance Shift 'will hit US'

The biggest overhaul of EU insurance regulation in 30 years will boost the competitiveness of European groups against rivals from abroad and set a benchmark for the rest of the world, the European Commission claimed. The new regime, known as Solvency II, will allow insurers to match the amount of capital they have to hold to cover their liabilities with the true risks they face. This will benefit large and diversified insurers such as Allianz, Axa and Aviva. (*Financial Times*, 11 July 2007) - [Back↑](#)

## Insurance Plan Predicted to Spark Mergers

Sweeping new European legislation could spark a wave of merger and acquisition activity in the insurance industry. The new regime, known as Solvency II, will overhaul the rules that determine how much buffer capital insurers must hold. It will seek to match the capital more closely to the risks they face, and will replace a patchwork of local regulations with harmonised rules designed better to protect policyholders. Solvency II will allow large groups to reduce their provisions in line with the lower risk arising from diversification, potentially freeing up billions of euros in capital for more profitable investments. (*Financial Times*, 10 July 2007) - [Back↑](#)

## New Chief Executive for the FSA

On 20 July 2007 Hector Sants replaced John Tiner as chief executive of the FSA. Mr. Sants previously worked as managing director of the FSA's wholesale and institutional markets business unit which he joined in May 2004. Please click [here](#) for a copy of the press release. - [Back↑](#)

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## General Legal Issues

### The Regulatory Reform (Financial Services and Markets Act 2000) Order 2007

This Order reforms the law by amending various provisions of the Financial Services and Markets Act 2000 (**FSMA**) with the result that a firm or individual may succeed to the business of a predecessor firm without obtaining a new authorisation if they succeed to the whole or substantially the whole of the business of the former firm. It also makes amendments with the result that the FSA is only required to consult the firm's home state regulator before giving a permission under Part IV of FSMA to a person connected with a firm authorised in another Member State. Please click [here](#) for a copy of the Order. - [Back↑](#)

### European Parliament Adopts Implementing Directives in Relation to Reinsurance and Direct Insurance

The European Parliament adopted on the 10 July 2007, the following measures which confer implementing powers on the Commission:

- European Parliament legislative resolution of 10 July 2007 on the proposal for a directive of the European Parliament and of the Council amending Directive 2005/68/EC relating to reinsurance, as regards the implementing powers conferred on the Commission; and
- European Parliament legislative resolution of 10 July 2007 on the proposal for a directive of the European Parliament and of the Council amending Directive 92/49/EEC on the coordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance, as



regards the implementing powers conferred on the Commission .

Please click [here](#) for a copy of the proposal relating to reinsurance and click [here](#) for a copy relating to direct insurance other than life assurance. - [Back↑](#)

## Insurance Premium Tax (IPT): Review of the tax Representative Provisions

A consultation on the Insurance Premium Tax (IPT) tax representative provisions for overseas insurers which considers whether there is a need for the appointment of an IPT tax representative; the possibility of introducing an IPT registration threshold; and seeks evidence on the use of the current IPT extra statutory concession which gives insurers providing mixed-risk policies exemption from IPT where specific de minimis requirements are met. A seminar is planned for late September to give interested parties the opportunity to hear the background to the consultation. (Source: *HM Revenue and Customs, 26 July 2007*) Please click [here](#) for a copy of the Consultation Paper. - [Back↑](#)

## Market Reform Group Published Letter sent to CEOs of all London Market Brokers and Insurers

The Market Reform Group (MRG) published on its website a letter sent to CEOs of all London Market brokers & insurers. The letter gives an overview of the process made on the three reform priorities for 2007 as agreed between the Lloyd's Market Association, London Market Insurance Brokers' Committee, International Underwriting Association of London and Lloyd's.

On the "Contract Certainty and Legacy" priority MRG concluded that achievement is consistently above the 90% target and that they are reducing the outstanding stock of legacy policies in line with the targets shared with the FSA.

On the "Electronic Claims" priority, Lloyd's market has only just achieved the target of 30% of new, in-scope claims being processed electronically using the Insurers' Market Repository (IMR).

The target for the electronic accounting and settlement priority of take-up of electronic processing for Accounting and Settlement (A&S) was missed by more than 20%.

MRG agreed that it will continue to work to support increased use of the IMR or both A&S and ECF and that it will disseminate data on firms' performance on A&S and ECF to all firms. Please click [here](#) for a copy of the letter. - [Back↑](#)

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## Regulatory Developments

### Solvency II Draft Directive Published

The European Commission adopted a proposal entitled "concerning the taking-up and pursuit of the business of Insurance and Reinsurance, to introduce a new solvency capital and supervision framework for insurers and reinsurers". This draft directive known as Solvency II aims to establish a single insurance market that allows insurers to operate throughout the EU and to establish and provide services freely. At the same time it tries to secure an adequate level of consumer protection. These goals are achieved by a common prudential framework, founded on three generations of life and non-life Directives, harmonising essential rules. According to the European Commission approximately three quarters of the new Directive consist of a codification of the 14 existing Insurance Directives. The European Commission also announced that the date by which the new Directive has to be implemented by the EEA Member States is postponed by two years to 2012.

The current solvency regime was widely criticised as delivering too little harmonisation among the EEA Member States which finally hampered the functioning of the Single Market. An overhaul of the existing Directives has also become necessary after many stakeholders concluded that the current regime disregarded major areas which could influence the solvency of an insurance undertaking like position risk, operational risk etc. Other points of criticism included the presumption that capital requirement alone could lead to a level playing field and that diversification was not recognised as a mean to mitigate risk.

As compared with existing legislation the proposal brings the following innovations:



□ an "Economic Risk-Based Approach" introduces a system that reflects the true risk profile of (re-) insurance undertakings by moving away from a "one-model-fits-all" to entity specific requirements.

□ the "Total Balance Sheet" approach also takes account of the asset-side risks that could influence the solvency of an (re-) insurance undertaking by including market risk and operational risk in the determination of the required capital.

□ the "Own Risk and Solvency Assessment" (ORSA) – Article 44, is an internal assessment process within the undertaking. At the same time it is also a supervisory tool for the supervisory authorities which must be informed about the results of the undertaking's ORSA.

□ under the "Supervisory Review Process" (SRP) – Article 36, supervisory authorities review and evaluate the strategies, processes and reporting procedures established by insurers and reinsurers to comply with this Directive as well as the risks the undertaking faces or may face and its ability to assess those risks. In order to ensure the efficiency of the SRP, supervisory authorities will have appropriate tools that enable weakness and deficiencies to be identified and remedied.

□ Public Disclosure - Articles 50 to 55 requires undertakings to a far greater extent than currently is the case to disclose annually a report covering essential and concise information on their solvency and financial condition. This proposal aims to bring market discipline which finally ensures the soundness and stability of insurers. (Source: *EU press release*).

Please click [here](#) for a copy of the draft Directive. - [Back](#)

## European Commission Calls for further Advice on the Solvency II Project

Following the adoption of the Framework Directive Proposal for Solvency II, the European Commission asked the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) for further advice to move on to the next stage (Phase 3) of the Solvency II project. In a letter to CEIOPS the Commission expressed its intention to have "any

*necessary implementing measures and supervisory guidance in place at least 18 month before the new regime becomes operational, in order to give the industry enough time to prepare for the new solvency regime."*

(Source: *European Commission*) - [Back](#)

## HM Treasury Consultation Paper on the Implementation of the Reinsurance Directive

This consultation document focuses on the changes to UK legislation, mostly FSMA and related secondary legislation, which have become necessary to complete the implementation of the Reinsurance Directive (Directive 2005/68/EC). Many provisions in the Reinsurance Directive are the same as or similar to those in the direct insurance directives, which have already been implemented, changes are only required in a limited number of areas where differences occur. These are principally in terms of passporting, where the process is much more straightforward in the case of the Reinsurance Directive, and provisions in the FSMA in which a distinction is drawn between reinsurers and insurers, particularly in relation to Part VII FSMA concerning the transfer of insurance portfolios.

HM Treasury proposes a risk-based approach to implement the provisions. As a consequence, some current exemptions from Part VII FSMA for transfers of reinsurance business, for example, will not be maintained in their entirety, it is not proposed to apply the full Part VII Court approval process in all cases. The HM Treasury also intends to introduce a requirement for publication of transfers of reinsurance in line with current UK provisions applying more generally. This will be low cost but will help improve certainty of process. (Source: *HM Treasury – Proposals to implement the Reinsurance Directive*). Please click [here](#) for a copy of the Consultation Paper. - [Back](#)

## CEIOPS publishes Consultation Paper on the Establishment of a Mediation Mechanism between Insurance and Pensions Supervisors

Following an invitation by the ECOFIN Council to explore the conditions for the establishment of a mediation mechanism and where appropriate to test such a mechanism in the insurance field in 2008, CEIOPS published a Consultation Paper on the establishment of a Mediation Mechanism between Insurance and Pensions Supervisors.



This consultation paper provides a design for a CEIOPS mediation mechanism and sets out the basic principles and the key features of the mechanism as formalised in the annexed draft Protocol.

The mediation mechanism which only deals with issues of cross-border nature, is a peer mechanism aiming at improving the cooperation and convergence amongst CEIOPS Members and non-CEIOPS national Authorities competent under the relevant sectoral directives (referred to insurance, occupational pensions, reinsurance and intermediaries). Comments are welcome by email (Secretariat@ceiops.org) by 5 October 2007, indicating the reference "CEIOPS-CP-01/07". (Source: CEIOPS) Please click [here](#) for a copy of the Consultation Paper. - [Back↑](#)

## CEIOPS publishes progress report on supervisory convergence

Following an official request by the EU Financial Services Committee, CEIOPS published an Interim Progress Report on the current position in its initiatives towards increasing convergence in supervisory practices in the field of insurance and occupational pensions. The report has three parts addressing:

- fostering supervisory convergence and cooperation,
- enhancing the cost-efficiency of the EU insurance supervisory regime and
- improving cross-border supervision.

Please click [here](#) for a copy of the report. - [Back↑](#)

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## Corporate News

### Money Laundering Regulations 2007

On 25 July 2007 HM Treasury published the Money Laundering Regulations 2007. Subject to Parliamentary approval, these Regulations will take effect from the 15 December 2007. The Regulations build on responses to HM Treasury's January 2007 consultation.

In summary the new regulation will

- provide more detailed obligations regarding customer due diligence, for example, explicit requirements for firms to undertake ongoing monitoring of business relationships and for firms to identify not just the customer but the beneficial owner of the customer;
- require firms to vary customer due diligence and monitoring according to the risk of money laundering or terrorist financing;
- require firms to take enhanced customer due diligence measures in higher risk situations, while allowing firms to take reduced identification measures for specific situations with a lower risk of money laundering;
- allow firms to rely on certain other firms for undertaking customer identification; and
- clarify the arrangements for the supervision of firms, including those that will be supervised for the first time.

Please click [here](#) for a copy of Money Laundering Regulations 2007. - [Back↑](#)

## Case Summaries

### C v D (2007)

An insured was entitled to an anti-suit injunction preventing the insurer from challenging a London arbitration award in United States proceedings because the attempt to invoke the jurisdiction of another court was a breach of the contract to arbitrate, the agreement to refer and the agreement to the curial law. QBD (Comm) (Cooke J) 28/6/2007. - [Back↑](#)

### HIH Casualty & General Insurance Ltd v JLT Risk Solutions Ltd (Formerly Lloyd Thompson Ltd) (2007)

An insurance broker was under a duty, after placing reinsurance, to alert the reinsured to matters of potential concern on coverage, but in the circumstances the reinsured had failed to prove that its loss had been caused by the broker's breach of duty. CA (Civ Div) (Auld LJ, May LJ, Longmore LJ) 12/7/2007. - [Back↑](#)



# ADDLESHAW GODDARD

[Tyco Fire & Integrated Solutions \(UK\) Ltd \(Formerly Wormald Ansul \(UK\) Ltd\) v Rolls-Royce Motor Cars Ltd \(Formerly Hireus Ltd\) \(2007\)](#)

A contractor was entitled to recover compensation in respect of damage or loss arising from a specified risk, namely the escape of water from a pipe on a sprinkler system installed by it in a car assembly plant, where the employer was, on the true construction of the contract in question, required to insure in joint names of employer and contractor against that risk but had failed to do so. Provision for joint insurance in the contract

had the effect of displacing the contractor's liability for negligence or breach of contract in relation to the damage. QBD (TCC) (Judge Gilliland QC) 29/6/2007 - [Back↑](#)

If you wish to discuss any of the above, or for more information, please contact one of the Insurance and Reinsurance Group



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