



Portfolio Transfers and Commutation - Alternatives to Run-Off

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I. Portfolio Transfers

To distinguish between:

1. Primary Insurer
2. Reinsurer

I. Portfolio Transfers

1. Primary Insurer

1.1 Prerequisites of Portfolio Transfers

1.2 Legal Consequences of Portfolio Transfers

1.3 Liability in Connection with Portfolio Transfers

I. Portfolio Transfers

1.1.1 Prerequisites of Portfolio Transfers (Primary Insurer)

- ✓ Regulated in Section 13 Insurance Supervision Act (ISA)
(Versicherungsaufsichtsgesetz, VAG)

To distinguish between:

1. Prerequisites of inland transfer (para. 1)
2. Prerequisites of transfer within the EEA (para. 2)
3. Specific Prerequisites (para. 3 and 4)

I. Portfolio Transfers

1.1.1 Prerequisites of Portfolio Transfers (Primary Insurer)

- ✓ Authorization of Supervisory Authority of the involved insurance undertakings (para.1 cl. 1)
- ✓ Prerequisites of Authorization (para. 1 cl. 2):
 - a) Interests of the insureds preserved
(„*Belange der Versicherten gewahrt*“)
 - b) Permanent satisfiability („*Dauerhafte Erfüllbarkeit*“) given

I. Portfolio Transfers

1.1.1.1 Prerequisites of Inland Transfers (Primary Insurer)

a) Interests of the insureds preserved

- No definition by law

Reason: Concretized by more than one hundred years of judicature of the highest courts

I. Portfolio Transfers

1.1.1.1 Prerequisites of Inland Transfers (Primary Insurer)

- Federal Administrative Court (BVerwG (st. Rspr.):
- *„An insufficient preservation of the interests of the insureds is given if interests of insureds requiring protection are impaired and if these impairments, under consideration of the entirety of the involved interests and of the particularities of the class of insurance, have to be considered as inadequate and as so serious, that an intervention by the public authority is justified.“*
(„Eine nicht ausreichende Wahrung der Belange der Versicherten ist dann gegeben, wenn schutzwürdige Interessen der Versicherten beeinträchtigt werden und diese Beeinträchtigung unter Berücksichtigung der Gesamtheit der beteiligten Interessen und der Besonderheiten des betreffenden Versicherungszweiges als unangemessen anzusehen ist und so schwer wiegt, dass ein Eingreifen der Behörde gerechtfertigt ist.“)

I. Portfolio Transfers

1.1.1.1 Prerequisites of Inland Transfers (Primary Insurer)

- It is crucial, whether the situation of the insureds changes significantly to the worse.
- Comparison between the situation of the insureds before and after the portfolio transfer.

I. Portfolio Transfers

1.1.1.1 Prerequisites of Inland Transfers (Primary Insurer)

- a) Permanent satisfiability given
 - Reference to Sections 89 et seq. ISA (Sections 122, 294 para. 4)
 - Hereby reference to solvency requirements of the acquiring insurance undertaking

I. Portfolio Transfers

1.1.1.2 Prerequisites of Transfers within the EEA (Primary Insurer)

- ✓ Authorization of Supervisory Authority of the transferring insurance undertaking (para.2 cl. 1)
- ✓ Prerequisites of authorization (para. 2 cl. 2):
 - Prerequisites of para. 1 cl. 2 fulfilled
 - Interests of the insureds preserved
 - (permanent satisfiability given)
 - Solvency certificate of the supervisory authority of the acquiring insurance undertaking
 - Approval of the supervisory authority of the location of the risks (Belegenheit der Risiken)
 - Consultation of the supervisory authority of the EEA-country in case of transfer of portfolio of a branch

I. Portfolio Transfers

1.1.1.3 Specific Prerequisites (Primary Insurer)

- Transferring insurance undertaking is a mutual insurance company (Versicherungsverein auf Gegenseitigkeit, VVaG; para. 3):
 - Appropriate payment for the loss of membership
 - Exception: Acquiring insurance undertaking is also a mutual insurance undertaking

- Insurance contracts with surplus participation (Überschussbeteiligung; para. 4):
 - For example: Life insurances
 - Surplus participation of the insureds of the transferring insurance undertaking and of the acquiring insurance company must not be lower after the transfer

I. Portfolio Transfers

1.2 Legal Consequences of Portfolio Transfers

- Section 13 para. 7 ISA:
 - Publication in the Federal Gazette (Bundesanzeiger; cl. 1)
 - Information of the insured by the acquiring insurance undertaking about (cl. 2)
 - Reason/occasion
 - Details (Ausgestaltung)
 - Consequences, in particular about
 - Change of supervisory authority
 - Change with regard to claims against a protection scheme in case of insolvency of the insurance undertaking

In case of change of the authority responsible for the financial supervision: Right of the insured to terminate the insurance contract (Limitation period: 1 month from the disclosure by the insurance undertaking) (cl. 3); duty of disclosure of the acquiring insurance undertaking (cl. 4)

I. Portfolio Transfers

1.3 Liability in Connection with Portfolio Transfers (Primary Insurer)

- ✓ Liability issues in particular in case of insolvency of the transferring insurance undertaking after portfolio transfer
 - if portfolio transfer motivated by threatening insolvency and assets are transferred in the interest of the insureds, third parties may be disadvantaged

I. Portfolio Transfers

1.3 Liability in Connection with Portfolio Transfers (Primary Insurer)

- ✓ Rights of contestation have to be considered:
 - Insolvency administrator may generally contest pursuant to Sections 129 et seq. Insolvency Act (Insolvenzordnung, InsO) if creditors are disadvantaged;
 - Single creditors may contest pursuant to Sec. 1 et seq. Act on Contestation (Anfechtungsgesetz, AnfG)

I. Portfolio Transfers

1.3 Liability in Connection with Portfolio Transfers (Primary Insurer)

- ✓ Rights of contestation may be excluded because
 1. Section 14 ISA old version was created for the restructuring of distressed insurers
 - => this intention would be devalued if the acquiring insurance undertaking were in danger of being exposed to additional liability
 2. Section 419 German Civil Code (Deutsches Bürgerliches Gesetzbuch, BGB), according to which claims could also be brought against the acquirer, has been abolished
 - => the legislator considered the co-liability of the acquirer as overvaluation of creditor protection

I. Portfolio Transfers

2. Reinsurer

- ✓ Regulated in Section 166 ISA

To distinguish between:

1. Prerequisites of Transfer (para. 1)
2. Specialty: Transfer to Insurance Undertaking with connection to third country (para. 2)

I. Portfolio Transfers

2.1 Prerequisites of Transfer (Reinsurer)

- ✓ Approval by BaFin (para. 1 cl. 1)
- ✓ (Only) Prerequisite of Approval (para. 1 cl. 3):
 - Solvency Certificate of Supervisory Authority of acquiring insurance undertaking
- ✓ Only control of plausibility by BaFin
 - ✓ Publication in Federal Gazette (para. 1 cl. 5)
 - ✓ Written information of the insurers by acquiring insurance undertaking

I. Portfolio Transfers

2.2 Particularity: Transfer to Insurance Undertaking with Connection to Third Country (Reinsurer)

- ✓ Acquiring insurance undertaking must (according to para. 2 cl. 1) be
 - branch of primary insurer of a third country
 - or
 - branch of reinsurer of a third country

I. Portfolio Transfers

2.2 Particularity: Transfer to Insurance Undertaking with Connection to Third Country (Reinsurer)

- ✓ Approval by BaFin (para. 2 cl. 1)
- ✓ (Only) Prerequisite of approval (para. 2 cl. 2):
 - Proof of solvency margin by acquiring branch
 - If solvency is supervised by EEA-member state,
then solvency certificate of supervisory authority of EEA-member state
(para. 2 cl. 3)

I. Portfolio Transfers

2.3 Portfolio Transfer – Pros & Cons in Comparison to Internal Run-Off

✓ Pros:

- ✓ Finality
- ✓ Release of capital/reserves, personnel
- ✓ Strategic adjustment of business

✓ Cons:

- ✓ Transfer = (singular) effort
- ✓ Approval process with supervisory authority
- ✓ Possible liability in case of faulty transfer of portfolio

II. Commutation

1. Definition

Process, by which the insurer agrees with its reinsurer – or a reinsurer with its retrocessionaire – by way of conclusion of a commutation agreement upon the **finalization of the reinsurance relationship.**

II. Commutation

2. Definition

- **Formal termination** of the reinsurance contract per se,
- Normally **termination of a liability period** of the reinsurer exceeding the contract period and
- Settlement of the losses occurred within the liability period.

II. Commutation

3. Effects

Legal: Finalization of all rights and duties of both parties at the agreed point in time

Factual: Loss reserves exit, as far as reserves exist

II. Commutation

4. Pros & Cons

Pro: Legal Finality

Cons: Legal disputes may arise (e.g. scope of commutation may be unclear in case of unclear description of commuted business – General Clause vs. List of contracts)

Thank you very much for your attention!

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