Global Insurance Compliance

Arranging Multinational Insurance Programmes

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2008
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1. Introduction

Almost all companies buy insurance, but the type and amount of insurance cover purchased will vary according to the risk profile and risk appetite of the business. Insurance is purchased to protect assets and income streams; to protect the assets of directors and officers of the company; to pay compensation to third parties in the event of a claim against the company, and because, in certain circumstances, it is a legal obligation. Mandatory insurances vary from territory to territory, but will usually include Employers Liability or Workers Compensation and Third Party Motor Insurance.

The Employers’ Liability (Compulsory Insurance) Act 1969 requires all employers to take out insurance in respect of liability to employees for bodily injury or disease sustained during employment in Great Britain.

The Federal Employees’ Compensation Act (FECA) provides compensation benefits to civilian employees of the United States for disability due to personal injury sustained while in the performance of duty. The Act also provides for compensation for employment-related disease. Benefits available to injured employees include rehabilitation, medical, surgical and necessary expenses. FECA provides compensation to dependents if the injury or disease causes the death of an employee.

Insurance provides a substitute or complement to government social security programmes. “Workers Compensation can relieve pressure on social insurance systems, preserving government resources for essential social welfare.”1 In addition, terms and conditions in contracts either with customers or suppliers may specify the purchase of insurance.

The JCT² forms of contract employed in the construction industry provide a suite of clauses which specify that insurance must be purchased for specific risks arising from the building works:

- Death and personal injury to contractors’ employees
- Death and personal injury to third parties
- Damage to property
- Damage to the Works and site materials
- Damage to existing structures and their contents

Many products and services are only sold if adequate liability insurance is available to cover any claims for negligence. Insurance cover may be a precondition for engaging in a particular activity.
The Riding Establishment Act 1970 requires the establishment owner to hold a current insurance policy which provides insurance against liability for any injury sustained by those who hire a horse from him for riding and those who use a horse in the course of receiving from him, in return for payment, instruction in riding and arising out of the hire or use of a horse as aforesaid and which also insures such persons in respect of any liability which may be incurred by them in respect of injury to any person caused by, or arising out of, the hire or use of a horse as aforesaid;  

Because of the high risk of new business failure, venture capitalists often make funds available only if tangible assets and the entrepreneurs’ lives are adequately insured. Insurance also underpins business activity by enhancing the creditworthiness of customers; banks and other creditors typically insist that the loan collateral be insured or they will not make the loan or will charge higher interest rates.

Private Finance Initiatives (PFI) and Public Private Partnerships (PPP) can only obtain funding if the insurance provision, taken out by the private contractor, meets the requirements of the lender.

The cost of natural catastrophes and man made disasters may have reduced during 2006, however, this is mainly due to the locations where the majority of these incidents occurred. The perceived threat of climate change appears to be bringing unpredictable weather conditions to all parts of the globe (witness the floods in the UK in 2007), and this exposes multinational companies perils in hitherto unexpected locations.

Liability exposures are correspondingly increasing, the consumer lobby in both the UK and the US is increasingly litigious. The US style class actions have appeared in Europe and prominent lawyers from the US are establishing branches within the UK and Europe with the express intention of launching class actions.

Corporate scandals have led to new regulations such as Sarbanes Oxley in the US and a plethora of corporate governance regulations in the UK and Europe. Indeed, the increasing focus on corporate governance is one of the main reasons why the issue of global insurance has become so dominant in recent times.

Implementing a global programme takes a considerable amount of time and effort. Multinationals have to establish and assess the risks to which they are exposed, determine their risk appetite and then decide how best to finance those risks they do not wish to retain. Insurance is a common risk financing option and ensuring that all aspects are compliant is complex. Purchasing suitable insurance in all territories is a time consuming and problematic process because insurance regulations are different in each territory,
insurance taxes are different in each territory and risk exposures are continually increasing and developing in response to external and internal factors. Commerce clearly transcends national boundaries and arranging appropriate insurance to cover ever growing risk exposures and comply with legal regulations is no easy matter. How then, do risk managers implement an insurance programme which is effective, efficient and compliant?

This paper aims to address the complex issue of arranging insurance programmes for companies with multinational insurances. It considers the basic requirement for insurance, the risk exposures with which multinationals are faced and the issues which surround insurance purchase worldwide. The various options for structuring multinational programmes will be discussed against the background of the various issues leading to the conclusion that there is no optimum structure which is applicable to all multinationals. Each company must address its own exposures, corporate structure, and policy requirements and use the options available to compile a structure which provides the best fit.
2. Risk Exposures

Managing risks can be complicated for firms operating in multiple jurisdictions. The operating environment will differ both in terms of the physical and legal environment from one jurisdiction to another as will the magnitude and scope of the economic consequences.

2.1 Property Risks

Natural and man made catastrophic events can have a serious and detrimental effect on the balance sheet and profit and loss account. In the event of such a catastrophe, insurance will relieve the pressure on cash flow and reduce volatility. Swiss Re’s research records a total of 136 natural and 213 man-made disasters in 2006.

![Number of events 1970-2006](image1)

Figure 1: Number of Events 1970 – 2006
Source: Swiss Re: Facts and Figures on Global Insurance

Natural catastrophes and man made disasters claimed 31,000 lives worldwide, with earthquakes causing the most fatalities. 6,600 lives were lost in Indonesia where one earthquake triggered a tsunami; storms and floods caused a further loss of 11,800 lives. The value of property claims dropped below the long term average in 2006, this reduction was mainly due to the regions in which the events occurred having low insurable values. The windstorm season in both the US and Europe passed with no expensive losses and no regions with high monetary values were hit by earthquakes.

![Insured losses 1970-2006](image2)

Figure 2: Insured Losses 1970 – 2006
Source: Swiss Re: Sigma No 2/2007 Natural catastrophes and man made disasters in 2006
Man-made disasters cost a total of 8,700 lives mainly in the shipping industry, but 940 lives were lost in aviation accidents and fires and explosions cost more than 900 lives.

According to the United Nations, this loss situation is likely to be aggravated by the facts of global warming. Their report claims that the global average temperature in 2006 was higher than the mean of the years 1961 – 1990 with the northern hemisphere affected more than the southern hemisphere. Record temperatures affected many parts of the world in terms of both extreme heat and extreme cold. Current thinking by many climatologists is that extreme forms of weather will extend to parts of the world that have hitherto been unaffected. This may well lead to an increase in claims as regions with high insurable values fall victim to natural disasters. As a result multinationals may be faced with claims from territories where historical trends would indicate that there is only a low risk of loss.

2.2 Liability Exposures
Multinationals are increasingly vulnerable to new and more aggressive forms of legal activism:
- the shift by non-governmental organisations away from attacking to exploiting legislation;
- the emergence of highly profitable class actions in US;
- the arrival of a new generation of lawyers many of whom put correcting social and environmental injustice ahead of salary and career development.

Multinational companies are facing continuing legal action for past and future impacts resulting from corporate actions which are now perceived to be irresponsible. In addition, causes of action, standards of evidence and procedural rules that courts either tolerate or require are all shifting to provide a new legal landscape in which businesses must now operate. Corporate scandals including, Parmalat, Enron and Worldcom have fostered a mistrust of industry leading to a demand for greater corporate accountability through new standards of governance, new disclosure requirements, and transparent accounting rules.

The Sarbanes-Oxley Act is a United States federal law in response to a number of major corporate and accounting scandals including those affecting Enron, Tyco International, Peregrine Systems and WorldCom. These scandals resulted in a decline of public trust in accounting and reporting practices. The legislation is wide-ranging and establishes new or enhanced standards for all U.S. public company boards, management, and public accounting firms. The Act requires the Securities and Exchange Commission (SEC) to implement rulings on requirements to comply with the new law.
The consumer lobby is increasing in strength in many jurisdictions, and class actions, once the preserve of the US, are threatening to emerge in the UK and Europe spurred on by several European Union Directives.

On April 11, 2007, Royal Dutch Shell agreed to pay $352.6 million to non-U.S. investors who bought Shell shares outside the U.S., in connection with the company’s 2004 oil resources accounting scandal. According to the *Times (London)*, the agreement is “thought to represent the largest ever class action settlement in Europe.” The agreement is subject to the approval of the Amsterdam Court of Appeals as well as to “agreed opt-out provisions.”

Managing liability risks is now a global phenomenon; Swiss Re (2004) reports that liability claims in the largest 10 non-life insurance markets worldwide reached US$84bn in 2002 of which US$67bn was from the US market alone. The US liability system is now twice as expensive as those of other developed countries with liability claims accounting for 2.2% of GDP.

<table>
<thead>
<tr>
<th>Claims incurred In 2002</th>
<th>General Liability</th>
<th>Total non-life</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>USD billions 2002</td>
<td>average loss rate 1997-2000</td>
</tr>
<tr>
<td>US</td>
<td>98.7</td>
<td>99.7%</td>
</tr>
<tr>
<td>Canada [1]</td>
<td>1.3</td>
<td>72.5%</td>
</tr>
<tr>
<td>Germany</td>
<td>4.2</td>
<td>95.1%</td>
</tr>
<tr>
<td>UK [1]</td>
<td>3.1</td>
<td>99.0%</td>
</tr>
<tr>
<td>France</td>
<td>2.6</td>
<td>113.2%</td>
</tr>
<tr>
<td>Italy</td>
<td>2.3</td>
<td>102.0%</td>
</tr>
<tr>
<td>Japan [2]</td>
<td>1.5</td>
<td>93.7%</td>
</tr>
<tr>
<td>Australia [3]</td>
<td>0.9</td>
<td>124.2%</td>
</tr>
<tr>
<td><strong>10 Countries [4]</strong></td>
<td><strong>93.9</strong></td>
<td><strong>98.2%</strong></td>
</tr>
</tbody>
</table>

Figure 3: Liability Claims incurred in 2002
Source: Swiss Re: Sigma No 6/2004, The Economics of Liability losses – insuring a moving target

Directors and Officers Liability (D&O) and Errors and Omissions Insurance (E&O) lines of business have suffered from severe claims costs arising from securities class actions and a number of high profile industry scandals including mutual fund late trading, back dating stock options and a multitude of mis-selling allegations against financial services institutions. Developments to employment law in the US and Europe are affecting Employment Practices Liability with a raft of claims resulting from wrongful termination, discrimination and sexual harassment.

Disability Discrimination Claim

MNO Corporation is located in California. Ellen worked in the office for over six years. During the last year, she informed MNO that she had developed degenerative disc disease and submitted medical notes noting that she could not sit for long periods of time. Ellen had a two hour commute to the office and could not sit in a car for that length of time.
She requested to telecommute as reasonable alternative. MNO did not believe that Ellen could perform her duties from home and denied her request. MNO then fired Ellen as they did not believe she would be able to perform the essential functions of her job and they needed someone in the office who could. Ellen filed a lawsuit alleging disability discrimination in violation of the California Fair Employment and Housing Act. The matter went to trial and the jury found in favour of Ellen

Award amount: $45,000 damages $225,000 attorney fees

2.3 Legal Liability

Traditionally, liability rules in civil law have been based on the notion of fault, with the person at fault who has caused injury or damage to another person responsible for compensating the damaged party, providing that the act was deliberate or due to a lack of care or attention. There has been an increasing trend towards no-fault liability; with liability based on causation, rather than negligence, a person becomes liable to pay compensation for an act irrespective of intent or neglect. In extreme cases, liability based on causation is not subject to the existence of any irregularities or malfunction. Thus, the mere existence of a link between a facility or object and the loss event is sufficient to create a liability.

The development of asbestos litigation is one example of the trend towards both liability based on causation and an attack on “deep pockets”. Initial lawsuits were directed against the manufacturers of asbestos, but once these sources of compensation were exhausted, lawyers turned against the companies that had used asbestos in any shape or form, including contractors and building owners and occupiers. In addition, claims have been filed by claimants with little or no current disability bundled together with stronger claims into class actions.

In the US, under civil law insured companies may be subject to punitive and exemplary damages being added to normal damages in cases where behaviour is deemed to be reprehensible or egregious. In 2002, punitive damages were awarded in 3-4% of bodily injury claims but the amounts vary considerably with many high profile cases of extreme punitive damages being awarded. Although these may be overturned on appeal the cost involved in so doing are considerable. A recent judgment in the US has sought to achieve a more reasonable balance between compensatory and punitive damages.

Insurance can also fund employment benefits, for example private health insurance, protect the personal assets of Directors and Officers and protect the business in the event of the death of a key member of staff. Insurance can promote financial stability as businesses that incur substantial uninsured losses may suffer major financial reverse or even failure. The loss in value of the owners’ stake in the business occasioned by an uninsured loss, means the firm’s future contribution to the economy is reduced or eliminated. Employees
lose jobs, suppliers lose business, customers forgo the opportunity to buy from the firm and government loses tax revenues. Stability provided by insurance encourages individuals and firms to invest and create wealth.

Many regulated industries (telecommunications, utilities) remain subject to regulatory oversight and have a higher demand for insurance. Rates charged to customers have to include estimates of expected costs including loss costs and will rely on insurers loss distributions. Premium loadings can be included in rate filings and can be passed onto customers.

Given the increasing concentration and complexity of risks which face multinationals in both the physical and legal arena, it is crucial that a well-considered strategy is developed and implemented for global insurance purchase. This strategy should identify the insured’s international issues and contemplate a solution to as many of these as possible. In an ideal world, multinational companies would arrange the insurances of its international subsidiaries centrally in the country of its headquarters or in a country where they have access to a sophisticated risk management and insurance community. This provides central control of insurance purchase, a standardised approach to risk management / loss control, familiar policy terms, a common language, avoidance of gaps or duplication of cover, consolidation of insurance purchase and significant leverage in the purchasing arena through economies of scale.
3. Issues affecting the purchase of multinational insurance

3.1 Global Insurance Market

Foreign markets can offer great potential, but carry risks that are compounded by legal, linguistic, cultural, economic and political differences. This is true of many aspects of multinational business, but is particularly applicable to the worldwide insurance market. In truth, there are so many different idiosyncrasies that it is probably not even accurate to describe the international insurance arena as one market.

Worldwide insurance premiums amounted to USD 3,723 billion in 2006, about 7.7% of global economic value generation (GDP). According to the Swiss Re sigma study, growth in total premium volume accelerated further to 5% (adjusted for inflation). Real premium growth in the emerging markets of 16% continued to outpace the growth of 4% experienced in the industrialised countries. The industrialised countries spent about 9% of the gross domestic product on insurance in 2006, while in the emerging markets this ratio varies from 1.4% in the Middle East and Central Asia to 4.7% in Africa. Global non-life business grew by 1.5%, below the growth in GDP. This figure, however, masks a sharp divergence in performance between the industrialised world, which saw only tiny growth of 0.6%, and the robust 11% delivered by emerging markets. In the industrialised world however, downward pressure on premium rates, particularly in non-catastrophe lines of business, was the salient feature of the market and could not be offset by higher demand. Strong underwriting discipline and the absence of major catastrophes delivered record profits in 2006.

![Figure 4: Developments in the major insurance markets in 2006](source)

3.2 Demand for Global Insurance Solutions

Whilst a global approach to insuring risk is not a twentieth century phenomenon, "One of the earliest forms of global programme ....... insured the safe return of a vessel or fleet," there has, however, been an increasing trend towards the globalisation of insurance programmes in recent times. The expansion of the risk management discipline and its increasing importance as a corporate function is one factor that has contributed to the development of global programmes. "In many multinational firms, risk management has evolved from a narrow insurance buying function to the broader role of identifying, analysing, financing and monitoring all forms of risk exposure on a global basis – in some cases involving both “pure” and “speculative” forms of risk. As the function has gained greater influence at the corporate level, many organisations have moved to centralise risk management responsibilities”.

Whilst multinational companies are increasingly looking to centralise their risk management programmes, there are a considerable number of factors that make insurance abroad different from domestic insurance in the United Kingdom. A country’s laws, attitudes and economic conditions, as well as the political and natural environment, combine to make insurance purchase unique in each territory. Requirements to insure certain assets and activities, compulsory participation by domestic insurers, and premium taxes are obvious examples of laws which directly affect insurance. Tax laws, liability rules, and workers’ compensation statutes also have a considerable impact.

<table>
<thead>
<tr>
<th>China</th>
</tr>
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<tbody>
<tr>
<td>Under Chinese law, non-admitted insurance is expressly prohibited. An insurer must be licensed by the China Insurance Regulatory Commission (the “CIRC”) under Article 71 of the China Insurance Law before it can write insurance in or from China. Similarly, Article 7 imposes a complementary obligation upon potential insureds which provides that: “Legal persons and other organisations which require insurance within the territory of the People’s Republic of China shall acquire such insurance from insurance companies within the territory of the People’s Republic of China.” If a non-admitted insurer writes insurance in China, the CIRC, may confiscate any illegal income obtained from the activity and impose fines on the offending company (up to five times the amount of illegal income obtained). There are, however, no explicit penalties set out for breach by a Chinese insured of Article 7. In addition, non-admitted contracts of insurance are deemed void under Article 52(5) of the China Contract Law and are unenforceable by either party in China.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Hong Kong</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-admitted insurance is permitted in Hong Kong, save in relation to a small number of mandatory forms of insurance such as motor and employee compensation insurance. A Hong Kong resident company may, obtain cover for locally based risks from foreign</td>
</tr>
</tbody>
</table>
There are, however, indirect restrictions upon offshore insurers on their ability to cover Hong Kong risks. In addition, there are express restrictions on Hong Kong authorised insurance brokers’ ability to recommend and place cover with unauthorised underwriters. Under section 8 of the Insurance Companies Ordinance, no person may carry on any class of insurance business in or from Hong Kong without being authorised by the Hong Kong Insurance Authority (the “IA”).

### 3.3 Insurance Regulation

Every country has an agency charged with overseeing and supervising its insurance marketplace. The task of co-ordinating the work of national insurance regulators falls to the International Association of Insurance Supervisors (IAIS). This body represents over 100 jurisdictions and is charged with promoting cooperation among national insurance supervisors, setting international standards for insurance regulation and supervision and coordinating work with other financial services regulators.

The fundamental law regulating insurance is generally contained in one or two act(s), supplemented by subsidiary legislation or by another act regulating insurance activities in each jurisdiction. In addition, legislation can be found in civil codes, commercial codes, insurance contract law and laws regulating the social security system. In some jurisdictions, essential rules can also be found in the central bank legislation or the constitution.

Insurance in Hong Kong is regulated by the Insurance Companies Ordinance (Chapter 41), which came into effect on 30 June 1983. A new Building Management (Insurance) Regulation will require incorporated property owners to arrange third party liability insurance with a minimum indemnity limit of HKD 10mn for the common parts of the building. This is due to commence in late 2007.

The quasi fiduciary nature of insurance and its importance to the overall public interest is the reason why governments worldwide have sought to protect insurance buyers against the natural information imbalance which exists between insurance buyers and sellers. The insurance laws in many territories prescribe the protection of policyholders’ interests as a key objective of insurance regulation and supervision. Individual consumers and small businesses may not know enough to even make appropriate inquiries as they negotiate for insurance and can be easy prey for unscrupulous insurance sellers.

In the UK the Insurance Law Reform: Law Commission Review is considering a number of reforms including:

A redefining of the materiality test for non-disclosure/misrepresentation.
Allowing insurers to claim damages from brokers for breach of brokers’ independent duty of disclosure to insurers in the placing process. In the case of consumers or small policyholders, linking insurers’ entitlement to reject a claim for breach of warranty to demonstrating that the breach has caused or contributed to the loss.

With the privatisation and deregulation of insurance markets, there is an increased risk of insurer insolvency. Regulators are challenged with creating a competitive market whilst ensuring that the insurers maintain adequate solvency levels. Within the EU the ongoing Solvency 2 project is aiming to set appropriate and consistent solvency margins across all member states.

Solvency 2 is a fundamental review of the capital adequacy regime for the European insurance industry that aims to establish a revised set of EU-wide capital requirements. These requirements should help supervisors protect policyholders' interests more effectively by making prudential failure less likely – reducing the probability of consumer loss or market disruption.¹⁹

Whilst the key objectives of insurance laws and regulations are to protect the policyholders’ interests and to monitor solvency, other goals include ensuring confidence in the functioning of the insurance sector, maintaining insurance market stability, ensuring the availability of insurance to purchases, retaining insurance premiums within the country, and channelling them into the local capital market. These regulations avoid unnecessary loss of foreign exchange either through the purchase of insurance/reinsurance from abroad or through the remittance of funds abroad by foreign or foreign-owned insurance companies. The barriers to entry and restrictive market practices are also implemented by governments to achieve political and economic results. By prohibiting foreign insurers, the local market is allowed to develop to a stage where it is able to compete with the large multinational insurers. Purchases from locally established insurance firms invest funds locally, whereas cross border purchases usually result in little or no investment in the country where the risk is situated. Cross border trade might not result in the creation of local insurance expertise or technology transfer to the local market and hence is less beneficial in terms of human resource development to the country.
3.3.1 Regulation of Brokers

Almost all jurisdictions have some form of regulation relating to the business of insurance intermediation. In most jurisdictions, the vast majority of insurance policies are not sold by the insurers themselves, but by intermediaries. This chapter contains a brief overview of the rules of jurisdictions relating to insurance intermediaries. In particular, attention is paid to the distinction between agents and independent intermediaries, the regulatory requirements for intermediaries and the supervision of intermediaries.

Regulations for intermediaries wishing to conduct business, including the requirement for intermediaries to be approved, licensed or registered by the insurance authority or, in some cases, by another authority are laid down in virtually all jurisdictions. In many cases, incorporation in the jurisdiction is required for the intermediary.

UK insurance intermediaries must be authorised by the Financial Services Authority

Insurance intermediaries are not allowed to conduct business in Japan without a licence from the Financial Services Agency. 20

Many different regulatory requirements apply to intermediaries in the various jurisdictions and in general, tied agents are subject to fewer requirements than independent intermediaries. Most requirements relate to the intermediary’s professional competence and good reputation, the requirement to have compulsory liability insurance and to provide certain information to the supervisor. Requirements such as the separation of clients’ money or solvency and capital requirements and a small number of jurisdictions additionally require intermediaries to participate in a guarantee fund. The areas in which jurisdictions apply regulatory requirements to intermediaries most frequently are set out in the table below.
In the large majority of jurisdictions the supervision of intermediaries is conducted by the insurance supervisor; in a small number, another institution is responsible for supervision. Almost all jurisdictions provide supervisors with the possibility of applying sanctions to intermediaries with the imposition of fines being the most common, although suspension or withdrawal of the licence of intermediaries is the most severe penalty which can be imposed.

### 3.4 Insurance Licensing

Insurance is a specific and complex field of commercial activity and no country permits foreign insurers completely unrestrained market access. Most jurisdictions require new entrants to be subject to approval or registration by the supervisory authority. Legislation exists in most countries, to a greater or lesser degree, prohibiting the purchase of insurance from insurers who are not licensed to transact insurance business within that territory. Financial penalties and in severe cases, imprisonment can result from the failure to comply.

The conduct of direct insurance business through cross border business of foreign companies is not allowed in nearly of 60% jurisdictions, a third of which do not allow foreign companies to carry out business through a branch. It is usual for licenses to be granted for an unlimited amount of time; however, a few jurisdictions impose a time restriction on licenses. Licensing is subject to payment of a fee on initial submission and on renewal. The granting of the licence may be dependent on the economic conditions prevalent in the territory at the time of application.

The relevant insurance supervisory authority will issue the licence and will state the extent to which the insurer can operate in the territory. The licence will include the classes of business, details of legislative and regulatory requirements and, where applicable, adherence to tariff rates and compulsory reinsurance.
The most common legal forms admissible for insurance companies are public limited companies/companies limited by shares, mutual associations and private limited companies. A foreign insurer can supply insurance services to local markets by setting up a subsidiary company. While the conversion of an existing branch to local company status may be viewed by many international insurers as part of an evolutionary development, in that the growth of business necessitates greater decentralisation of control, premature pressure to set up a local company can discourage supply altogether. Apart from the question of viable size, political risks associated with deploying extra capital may not be justifiable.

Chinese capital requirements are unusual in the sense that each branch must be separately capitalised. Minimum capital must be fully paid-up in cash. Capital requirements are the same for life and non-life and vary only with the geographical spread of a company's operations. Current capital requirements, effective from June 2004, are as follows:

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nationwide licence</td>
<td>CNY200m</td>
</tr>
<tr>
<td>Capital per branch</td>
<td>CNY 20m</td>
</tr>
<tr>
<td>Maximum capital (nationwide licence plus 15 branches)</td>
<td>CNY500m</td>
</tr>
</tbody>
</table>

Solvency Margin
According to Article 99 of the Insurance Law, net retained premiums may not exceed four times a company's capital and surplus. In addition to this general requirement, specific solvency margins were introduced in March 2000.

Reserve Requirements
Non-life insurers are required to establish unearned premium reserves and loss reserves. Outstanding loss reserves must represent the full settlement cost of both reported and incurred but not reported claims. Claims reserves must be established on a gross basis and may not be discounted for the time value of money.

Insolvency
The CIRC operates an "early warning system" based on the relationship between an insurance company's actual solvency margin and its required solvency margin which allows it varying degrees of financial and managerial control over a failing company.

Policyholder Protection
All companies are obliged to deposit 20% of their paid-up capital with a bank designated by the CIRC as a guarantee in case of insolvency. In addition the CIRC has established life and non-life policyholder protection funds financed by levies on insurers' premium income.

In most jurisdictions, the licensing requirements for domestic insurers and foreign companies seeking local licensing is the same or very similar. Information is required about
the company owners, directors and managers; the nature of risks the company intends to cover and basic financial information are also important to the licensing procedure.

**European Union**

There are unique cross border regulations which apply to insurers who operate within the European Union. The First Non-life Insurance Directive, (1973), introduced freedom of establishment giving EU insurers the right to establish branches and subsidiaries in other member states. This was followed by the Second Non-life Insurance Directive in 1988 which introduced Freedom of Services, and meant that an insurer in one member state could supply services to residents of other member states without the need to be established in that territory. The Third Non-Life Insurance Directive brought together measures in first two directives into Single Licence concept which means that any insurer can set up a subsidiary or branch in another member state, or provide cross border services, without the need for authorisation in each territory (only in the parent country).

For a multinational with operations in various European countries the use of an insurer in an EU country means it can have policies issued on an admitted basis throughout the EU. Directives have allowed multinationals to set up Captives in the EU for issuing policies in all the EU territories where it has operations. The Third Directive allows the law of the contract to be decided freely so that a programme using an insurer in the home territory to insure subsidiaries in other member states can use the law of the parent companys’ country for the contract. The administration and regulatory burden has been reduced by Single Licence system in EU but separate policies still have to be issued for each country.

Despite relaxation and liberalisation of many aspects of international trade, the tendency to retain the proceeds of insurance transactions onshore, either by compelling nationals to use local insurers or by controlling the remittances from licensed foreign insurers to their overseas principals, looks likely to continue.

**3.5 Insurance Policy Conditions**

Regulating and supervising the contractual relationship between the policyholder and the insurance company is an important element of policyholder protection. The role which product control plays in insurance supervision varies considerably between jurisdictions. In many jurisdictions, the policy conditions of an insurance contract have to comply with the general contract, commercial or common law as well as insurance supervision and insurance contract law. In several jurisdictions there are further laws or supervisory authorities’ decrees applicable to insurance contracts. Furthermore, the insurance industry in several jurisdictions has laid down its own codes of conduct on drafting policy conditions with which insurers have to comply.
Policy conditions are mandatory in a considerable number of jurisdictions, either in part or whole. Motor vehicle third party liability and other insurance policies for third party liabilities related to other vehicles such as vessels, aircrafts, motorboats and railways, but also related to specific activities or risks such as brokerage, construction and environment, travel agencies and hunting, as well as for all other compulsory insurance policies.

Regulators and supervisory authorities influence the characteristics of insurance products. In some cases products require full prior approval and in others, systematic notification, notification on request or other control measures. Insurance products are subject to prior approval by the supervisor in about one third of the jurisdictions and to systematic notification in another third of the jurisdictions. In about half of the jurisdictions insurance products have to be notified to the supervisor on request. In quite a number of jurisdictions the supervisor may require such notification even if they are subject to prior approval or systematic notification already. In about 15% of the jurisdictions insurance products are not controlled by the supervisor at all.

Wherever insurance products are controlled by the supervisory authority, the controlling measures refer not only to the first version of the policy conditions but also to all changes during the term of the insurance contract.

### 3.6 State Control and Provision of Insurance

There remain a few jurisdictions where the provision of some or all insurance is provided by a state insurer, such as in Cuba, Iran, Myanmar and North Korea. In these cases all the compulsory classes must be insured with the state insurer. Alternatively the state may provide cover which is unavailable in the commercial market. This can be seen in many markets with the provision of government "pools".
In the UK, Pool Re was created to insure commercial property and business interruption following the terrorism exclusion brought in by insurers following sustained terrorist activity. Pool Re provides cover above a certain limit and is funded by contributions from insureds with the UK government acting as the reinsurer of last resort.

The multi-national corporation has to contend with the desire of governments that insurance be placed with licensed insurers or locally organised companies and when considering a global policy it is necessary to examine any restrictive legislation to determine the extent to which it must be complied with. Unfortunately the insurance laws and regulations in several countries are not clearly set out or readily available. Foreign firms encounter transparency problems in countries where insurance authorities have broad discretionary powers as foreign insurers have no clear understanding of the market or operational and market conduct requirements.

3.7 Premium / Tariff Control

Insurance supervisors in many jurisdictions are keen to have to influence or at least oversee insurance premiums. The pricing of an insurance contract can be influenced either by controlling the structure and financial elements of the premium tariffs or by fixing the premium rates or setting a certain margin binding the insurance companies. Premium rates and the structure of premium tariffs are regulated by the supervisory law in more than 45% of jurisdictions and in several jurisdictions also by several other laws such as insurance contract law, general contract, commercial or common law, and other laws or by supervisory decrees. There are many instances of the insurance industry or other private institutions laying down codes of conduct or guidelines in the matter. When there is regulation regarding premium rates there is usually regulation regarding the structure of premium tariffs. In most jurisdictions this is undertaken by the supervisory law and/or by decrees of the supervisory authority.

Kazakhstan

Statutory tariffs exist in respect of both premium rates and limits of liability for all compulsory classes of insurance.

The compulsory classes are:
- motor third party liability insurance
- agricultural insurance
- accident to passengers on public transport
- civil responsibility of notaries, auditors and travel agents
- third party liability in respect of hazardous goods and activities
- employers' liability.
3.8 Insurance Taxes

Insurance Premium Tax(es) (IPT) are becoming a major concern for insurers, brokers and insureds. When policies are written across more than one jurisdiction IPT and other parafiscal taxes may be due in each country. Failure to account for these taxes correctly could lead to significant penalties and interest charges, as well as payment of the unpaid tax, for any of the parties involved. Governments worldwide are always looking to maximise any available tax revenues. Subsidiaries of foreign companies are attractive targets of potential revenue enhancement. Insurance taxes vary enormously around the world, there is no common level of tax worldwide, nor is there agreement as to what constitutes insurance premium tax.

<table>
<thead>
<tr>
<th>Tax Type</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stamp Duty</td>
<td>A single amount payable per policy</td>
</tr>
<tr>
<td>Fire brigade tax</td>
<td>Levied on fire insurance premiums towards the cost of fire brigades</td>
</tr>
<tr>
<td>Withholding tax</td>
<td>May be in the form of income tax, with a percentage of the premium treated as income and taxed as such,</td>
</tr>
<tr>
<td>Excise tax</td>
<td>Charged on premiums paid to foreign insurers.</td>
</tr>
<tr>
<td>VAT/Goods and services Tax</td>
<td>Usually a percentage of the total premium, may be recovered whereas premium tax is non-recoverable.</td>
</tr>
</tbody>
</table>

Tax liability rules differ between countries and are in some cases contradictory, ambiguous or conflict. Responsibility to account for and pay insurance premium tax to the tax authorities lies with different parties in different countries. Some territories have different levels of premium tax for different classes of business. In the United States, each state will impose its own level of premium taxes.

Examples of Premium Taxes

<table>
<thead>
<tr>
<th>Country</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Japan</td>
<td>nil</td>
</tr>
<tr>
<td>US</td>
<td>0.5% - 6% depending upon policy class and state</td>
</tr>
<tr>
<td>Singapore</td>
<td>5%</td>
</tr>
<tr>
<td>South Africa</td>
<td>14%</td>
</tr>
</tbody>
</table>

In addition, the responsibility for the payment of premium taxes may not be clear, is it the insurer, the insured or the broker/agent who must pay in each country?

In China the insurer is responsible for collecting the taxes from the insured and passing them to the tax authorities.  
In Kuwait the insured is responsible for paying premium tax directly to the tax authorities.  
In Kenya premium tax is collected by the insurer and passed to the tax authorities, whereas stamp duty is paid directly by the insured.
Collating and interpreting this information is a mammoth task and monitoring, understanding and responding to this shifting legal and regulatory environment is crucial to transparent, compliant and sustainable risk management and global insurance coverage. In addition, legislation and regulation operate within a changing landscape. The European Economic Area (EEA) has its own specific rules, however, outside the EEA rules vary by country.

**European Union**

Within the European Union, the Direct tax directive on mutual assistance, adopted on 26 April 2004 is designed to speed up the flow of information between tax authorities of Member States. The Directive which relates to direct taxation (income tax, company tax and capital gains tax), together with Insurance Premium Tax, enables Member States to coordinate their investigative action against cross-border tax fraud and carry out more procedures on behalf of each other.

**United States**

Within the United States, a Federal excise tax is imposed where premiums are paid to non-US insurer for US risks, although a number of countries (including the UK) have double taxation treaties with the US which excludes them from the Federal Excise Tax.

The type of programme and classes of insurance will determine the different tax issues which apply, either local policy taxes, premium not qualifying for tax relief or payment of claims being treated as unearned income. Local taxes must be paid whether insurance is admitted or not but if non-admitted has been purchased and taxes are paid, this might trigger an investigation as to the legality of the policy.

**Non-admitted insurance is permitted in Canada, however, under the Excise Tax Act, all Canadian corporations that place insurance with a non-licensed insurer or through a broker outside Canada must pay federal excise tax to the Canadian Revenue Agency (CRA). The Excise Tax Act is particularly pertinent if the insured in a subsidiary of a non-Canadian parent where coverage is under a non-admitted programme with no locally admitted policy. The tax will still apply even if the subsidiary has paid premium allocations to the parent company or subsidiary.**

The increasing complexity and hardening of the licensing, tax and legal environments have raised foreign premium tax accountability to new heights.

The *Kvaerner* ruling, (first heard in the Dutch Supreme Court in 1999) specifically addressed the premium tax applicability of the Dutch exposures of a UK based professional indemnity policy, ruling that premium tax must be paid in the country where the risk is located. While
it pertained specifically to professional lines, Kvaerner has ramifications across multiple lines; global insurance solutions that were once considered compliant may now be deemed illegal.

Kvaerner plc –v- Staatssecretaris van Financien

Kvaerner is a multinational company that was fined by the Dutch tax authorities for not paying Insurance Premium Tax (IPT) in the Netherlands on a non-admitted programme arranged out of the UK.

The ECJ judgment released on June 14, 2001 concerned the definition of "establishment" under Art 2(d) of the Second Non-life Directive (88/357/EEC), which includes the location of risk rules member states may apply when imposing local taxes on insurance contracts.

Before the Kvaerner case, many U.K. insurers and insureds had few concerns about overseas taxes. They simply looked at the apportionment of the risks insured when deciding whether part of the premium could be exempted from U.K. IPT. After the European Court of Justice (ECJ) hearing and its judgment in 2001, insurers became more alert to the business issue of overseas premium taxes and any related exposures.

Lloyds has actively responded to the Kvaerner ruling and has expanded the concept to jurisdictions outside of the EU area. Policies from Lloyd’s have unique territorial coverage extensions that automatically give all policyholders de facto admitted policy status in all territories for which Lloyds holds licenses. This requires the policyholder to pay local taxes.

The extension of the Mutual Assistance Directive (Dir.77/799) to taxes on insurance premiums is a problem for non-compliant insurers and insureds not only in relation to current and future multi-national risks, but also in relation to past non-reporting and under-declaring of premium taxes. Moreover, the recently announced International Tax Enforcement Arrangements (ITEA) are likely to extend these powers outside the E.U. They allow the UK to enter into bilateral and multilateral arrangements for the exchange of information in relation to direct and indirect taxes and mutual assistance in their collection. Existing powers covering double taxation of income, capital gains and inheritance taxes are repealed, and replaced by a single power to make arrangements with other territories for the exchange of information, service of documents and assistance in both direct and indirect tax collection. The scope of HMRC powers remains the same. The range of taxes they can be applied to is wider. HMRC can now obtain information for all treaty partners, regardless of whether the U.K. has a domestic tax interest in the information.
Claims paid locally from a non admitted insurer may be subject to corporation tax. An insurer may pay a non-admitted claim either directly into the country in question or in the country where the master policy is issued. If local payments are detected and the non-admitted insurance was arranged in violation of the law, then the claim payment may be subject to tax assessment, and fines and penalties may be imposed. If a claim payment made in the UK relates to an overseas operation, then the Inland Revenue may assess the payment as subject to tax and the corporate rate (30%) would be applied.

Tax Liability Clause
If the insurer is unable to pay any loss in the country where the loss occurs, because of local law or otherwise, such loss will be paid in the master policy country. In the event of such loss payment, the Insurer will also pay the Insured an additional amount required to offset any tax(es) on income as a result of the local tax(es) on income payable by the Insured in the county of payment, which accrues because of such payment. Any additional amount shall be reduced to the extent of any reduction in tax(es) on income as a result of local tax treatment of the loss in the country where the loss occurred.\textsuperscript{25}

The inclusion of an appropriate tax liability clause in any master policy wording where non-admitted insurance is anticipated can alleviate these costs even though fines and penalties would not obviously be included.

When a claim payment is received in the master policy country, getting the funds to the country can be challenging and may result in additional charges and penalties.

The tax regime of a country and the attitude of revenue authorities towards non-admitted insurance will help shape the programme where the multinational buyer is looking for the most tax efficient and tax friendly programme. The aim must be to comply with local taxation but to try to reduce the impact of such taxes in countries where the rate is particularly high.
4 Multinational Insurance Programme Structures

There are a number of ways in which a multinational company can structure its insurance programme, from a loose collection of unrelated, local policies to the most sophisticated alternative risk financing or a variety of combinations which fall between the two.

4.1 Locally admitted programme

An admitted policy is issued by an insurance company that is licensed in the country in which the insured and/or the risk is domiciled. A locally admitted programme involves all the insurance being purchased from local carriers according to local customs and regulations. Premium payments and loss payments are made in the local currency and the policy contract would be subject to the local legal system. Cover is likely to be specifically tailored to the territory and be compliant with local regulations, tariffs, policy forms and taxes; premiums are likely to be tax deductible. Most countries prefer the placement of insurance to remain with local insurers, irrespective of whether they are a local company or a subsidiary of a foreign group. The admitted insurer does not have to be a local domestic insurer; foreign insurers and multinational insurers can also be admitted if they are licensed by the supervisory authority to conduct insurance business in the territory.

The governing legislation relating to non-admitted insurance in Brazil is article 6 of Decree Law 73/66, which states that a risk located in Brazil can only be insured outside of Brazil if coverage is not available in the country or if the coverage contravenes public interest. Authorisation to use an external insurer is made on a case by case basis, depending on interest and guarantees presented by the broker or the insurance company. The penalty for any entity found placing non-admitted insurance, co-insurance or reinsurance in Brazil or abroad is equal to the sum insured or reinsured. Additionally, it is illegal to remit money abroad to pay the premium of non-admitted policies and consequently no money can be officially received in Brazil as indemnity of non-admitted policies. If a master policy is taken out overseas by the headquarters of a multinational company with a coverage extension to all subsidiaries worldwide, (i.e. D&O), the Brazilian legislation will not allow nationalization of foreign capital from insurance indemnities.

4.1.1 Benefits of Admitted Programmes

Compliance with local laws, good citizenship

Many countries have severe restrictions relating to the use of non-admitted insurance with an outright ban imposed in some countries.
China, India, Indonesia, Japan, Korea, the Philippines, Taiwan, Thailand and most other Asian countries similarly restrict the sale by and purchase from non admitted companies; the exceptions are Hong Kong, Malaysia and Singapore. Consumers within the EU may purchase insurance from EU insurers in other member states, and EU insurers may solicit insurance in all EU countries.28.

Purchasing locally admitted insurance means that the multinational has purchased insurance from insurers authorised to do business in that country issuing policies that are compliant with local laws. Purchasing admitted insurance provides the multinational with the benefit of knowing that all the policies are compliant from governance and corporate citizen perspective. The risk of fines and penalties from not purchasing admitted insurance is eliminated with the admitted policies. The purchase of compulsory insurances with an admitted insurer will also minimise any risk of the policyholder being left without cover in the event of insolvency as they may be entitled to state protection.

**Access to local pools**

Some territories require the compulsory cession of certain perils to national insurance where the risks are deemed too difficult for local insurance market to cover. Purchasing admitted insurance gives insureds access to local government pools

There is a Brazilian Nuclear Risks Pool (CBRN) and any nuclear risk written by a domestic insurance company must be transferred to the pool

**Tax deductibility of premiums paid locally**

Premium payments may also be eligible for tax relief as buying from an admitted insurer means that there should be less of a problem regarding tax deductibility.

**Claims payments income**

Insurance purchased from an admitted insurer allows claims to be paid in full without any complications regarding their taxable status. The payment of premiums in the local territory allows for easier transactions and reduces the effects of exchange rate fluctuations. An admitted policy allows claims to be paid in full in the local currency without any complications regarding their taxable status, and in the local currency alleviating any currency restrictions or exchange rate losses.

**Local servicing of claims and coverage issues**

With a locally admitted policy, servicing is by the local insurers’ offices and a local broker or agent is usually provided. Local managers are have a local contact and are easily able to provide changing property values and other updated information. This will enable the adjustments that are required in insurance coverage to be amended more quickly. Local insurers have a much better understanding of the risks in their country, and more
experience in terms of underwriting those risks. Certain classes of business (such as Workers Compensation) require a high level of local servicing are usually best placed locally so that the most efficient service can be obtained. Local representatives will understand coverage nuances and local practices and be able to design more appropriate programmes.

**Local language**
The contract is written in the language of the local country and will be easily understood by local management.

**Local financing and other business activities**
Business activities such as contracts, banking, and property ownership and tenancy may require purchase of admitted insurance, admitted insurers can provide local certificates of insurance.

**Local control**
Local management tend to favour this approach as it provides them with the control over the structure and placement of their insurance programme and allows them to make decisions about deductibles, the scope of any additional services provided, out of pocket expenses and other terms and conditions.

### 4.1.2 Drawbacks of Admitted Programmes

**Higher costs**
If the group is buying on an international basis, the fragmented nature of insurance buying means that it will not be able to benefit from economies of scale and in particular bulk purchase, for which very competitive rates may be available. It is difficult to achieve pricing efficiencies if each local operation is negotiating its own insurance premium, while some subsidiaries may be able to negotiate better pricing terms and wider covers than others, the sum of all the local insurance premiums may well be greater than the cost of insurance purchased centrally. Compliance with tariff rates, the lack of competitive market or underwriting sophistication and the lack of corporate leverage may lead to higher rates and make admitted insurance more expensive than non-admitted.

**Less broad coverage**
The scope of cover available to each local subsidiary will vary from territory to territory and policy wordings will vary considerably according to local market practice and regulatory constraints. The limits available will depend upon the capacity of the local market and in many cases these restrictions will not be acceptable to a multinational which requires consistent policy structures and level of cover. Local insurance practices may be unfamiliar and conditions of contract may be less favourable or easily understood resulting in non-standard conditions and increasing the possibility of coverage gaps and underinsurance. In
countries where 100% insurance to value (coinsurance) is required, underinsurance can subject loss settlements to penalties.

**Corporate risk retention strategy**
Local coverage programmes may run counter to corporate policy, making corporate risk management strategy difficult to implement. If corporate philosophy is to retain significant amounts of loss through large deductibles or self insured retentions, the local market may not offer such insurance programmes. Business practices in many countries do not favour large retentions and may not be encouraged by local insurance industry, regulators or business partners.

**Local premium taxes**
Admitted insurance is subject to local premium taxes which as we have seen vary according to territory and policy class.

**Insufficient local services / knowledge**
There may not be the same level of technical knowledge within insurers or brokers in smaller jurisdictions where the insurance market is not yet fully developed. Local risk control services, risk surveyors or loss adjusters may not be as easily obtainable as in more developed industrial nations.

**Legal Issues**
Legal systems vary around the world, as does the way in which businesses are treated by the courts, these will all have an impact on policy and claims disputes. Any dispute on policy wording will be decided in the country of the subsidiary not the country of the parent which may not provide the most favourable jurisdiction or be easily accessible to the corporate parent and its lawyer.

**Financial solvency / capacity issues**
Whilst the regulation of insurers worldwide is increasing, there are still many markets where finding a local admitted insurer that has the required financial security and is acceptable to the parent may be difficult as the availability of meaningful solvency regulation, financial statements and insurer rating services varies widely. Other major drawbacks can include limited knowledge of insurance markets on the part of local management, the possibility of reduced emphasis on risk control, and the potential for very large losses that can negatively affect the subsidiary’s financial operation.

**No central control**
The fragmented nature of admitted insurance for a multinational company means that there is no central control. The restraints on the local market and the lack of sophistication at the local level of insurance purchase might lead to over-insurance or underinsurance, gaps in
coverage, poor wordings, restrictive conditions and warranties. Policies written in different languages may be difficult to evaluate and manage by central risk management.

4.2 Non-admitted programme

A non-admitted policy is issued by an insurance company in a country in which it is not licensed and / or a country outside of the risk domicile Typically it is a policy which is issued in one country that cover exposures in other countries. Policies would not be issued in the local country, rather one policy would be issued in the territory where the insurance was purchased. Premium payments and loss payments are made in the currency where the policy is issued and the policy contract would be subject to that legal system. Cover is likely to be designed according to corporate risk management standards.

4.2.1 Benefits of Non-admitted programmes

Potentially lower costs
This option should achieve a more favourable premium result, because a single insurer prices all coverage on a global basis. There is also the likelihood that coverage will be duplicated from one policy to the next, resulting in higher overall costs. Cheaper premiums are available through bulk buying and pooling of retentions. Insurers’ administrative savings in terms of time, cost, and economies of scale mean cheaper premiums.

Broader and uniform coverages
From the corporate viewpoint non-admitted insurance provides a broader, standard level of coverage and addresses certain exposures, such as global interdependencies that may not be covered under locally admitted policies. The multinational may also obtain greater leverage in negotiating a broader policy wording than may be available under admitted insurance policies particularly as the risk is spread over many territories. Extended coverage or other extraneous perils may be added some of which may not be known or available in local markets. The policy can be issued with an “open limit” reducing the danger of the insured acquiring new values at a different locations and being without protection until confirmed, perhaps weeks later.

Management
Non-admitted insurance has the advantage of enabling risk managers to purchase insurance for all operating companies according to corporate standards. The level of cover required in each class and the conditions of cover can be mandated worldwide. With admitted insurance this uniformity of cover and limits is virtually impossible to obtain, as certain types of insurance are unavailable in some territories, or may be too expensive or too restrictive. A uniform level and scope of cover is especially important for multinationals where there is a high degree of inter-related exposures. Multinational cover through a non-admitted insurer can therefore provide cover for such risks in a way that would not be possible with local insurers. It is easier to ensure that there are no gaps in cover across the whole group with
non-admitted insurance as well as no overlapping insurance. Communication between subsidiaries and the parent can be poor and lead to gaps in cover or inappropriate limits where the local unit is left to arrange its own cover. It makes sense to integrate policy wording to ensure appropriate coverage in the event of physical damage in one location that results in a business interruption elsewhere in the corporate family.

**Common currency**
Non admitted premiums will be payable in the home country currency as will losses. This use of a single currency eliminates the risk of exchange fluctuations. Claims can be paid to the parent company, which has control of the funds and can use them as it wishes. It is possible that the parent may not wish to rebuild a factory, for example, but may use the funds elsewhere in the group.

**Choice of insurer**
The choice of non-admitted insurer is clearly much greater than for a local admitted insurer as markets in the developed world are stronger and more diverse. It will also be easier to assess the financial security of a non-admitted insurer which is usually domiciled in a highly regulated jurisdiction with sophisticated rating agencies.

**Common language**
A non-admitted policy can be written in the language of the parent company, and include common wordings and clauses to ensure that the cover is the same worldwide, as well as being easily understandable and leaving less room of errors and omissions.

**Legal issues**
Non admitted policies administered in the home country mean that any coverage disputes are subject to the home country’s legal system and courts which are familiar.

**Claims handling**
Claims can be handled by a single team who understand the intricacies of the policy wording and apply it uniformly across all jurisdictions. Claims can be paid to the parent company providing control over the funds and decisions as to where to deploy them.

**4.2.2 Drawbacks of Non-admitted Programmes**

**Prohibited by local laws**
On the negative side, non-admitted insurance is illegal in many countries despite the number of deregulation and liberalisation measures around the world. Deregulation and the removal of state monopolies do not necessarily mean that non-admitted insurance will be allowed. Many countries which have deregulated and have competitive insurance markets still do not allow non-admitted insurance.
According to Article 186 of the Insurance Business Law, "no foreign insurer without a branch office in Japan may effect insurance contracts (other than those specified by a cabinet ordinance) on persons having residence or place of abode in Japan or property situated there or vessels or aircraft of Japanese nationality" without obtaining the prior permission of the Minister of Finance.29

The penalties for non-compliance with local insurance regulations vary, they consist of severe fines and, in some cases, the imprisonment of local directors. Even in territories where the use of non-admitted insurers is permitted, there may be penalties attached such as higher premium taxes or service charges.

In Indonesia, if company based in Europe proposes to debit its subsidiary in Indonesia for insurance arranged by them and is found to have breached the regulations, they face a tax penalty based on the following:

- **Tax Law No 7/1993** (as amended by Law No 10/1994) states insurance and/or reinsurance premium paid to an overseas company is subject to a deduction of 20% from the estimated net income.

- **Decree No624/KMK/0401994** states the estimated net income (paid overseas) will be taxed.

According to Article 21, Chapter II of Insurance Law 2/1992, a person or persons responsible for transacting non-admitted insurance may be subject to imprisonment for up to 15 years and a fine not exceeding IDR 2.5bn (USD 257,667).30

**Lack of tax deductibility**

Non-admitted insurance may not qualify for tax relief. Where premiums are paid to an unlicensed insurer, transactions may not be considered as insurance and local revenue may not allow the premiums to be tax deductible.

Unless special dispensation is granted by the Indonesian regulatory authority for a buyer to insure direct overseas, premiums cannot be deducted by a company as a business expense.

**Taxes on premium payments**

Where non-admitted insurance is legal, there may be a requirement to pay higher insurance taxes, tariffs may be higher or there may be a requirement to reinsure all or an element of non-admitted policies with a domestic reinsurer to ensure that at least some of the premium remains in the country. In some countries there is a compulsory requirement to cede all or a portion of business to the state reinsurer.
In the Philippines, all non-life insurers are obliged by law to offer National Re up to 10% of their reinsurance treaties which the company may, at its discretion, accept or decline.

**Taxes on claims payments**
Claim payments may be viewed as unearned income by local revenue authorities rather than an insurance claim and subject to tax both in the country of claim and in the home country. Suitable tax liability clauses need to be negotiated (or at least option priced) for covers where non-admitted insurance is likely. Even where claims receipts from abroad are allowed, some countries adopt a deliberate policy of administrative delays to try to discourage such policies. Claims settlements can become more complex without local cover and the assistance of local insurer representatives.

In Indonesia, a buyer may be exposed to taxation on any compensation paid by an overseas insurer which is treated as unearned income.

**Lack of local service**
Where there is no local insurer and no local broker this can mean a loss of control for local service, assessment of risk and claims investigations as all communication is undertaken from a distance or by sending in personnel who are not directly familiar with the circumstances.

**4.3 Combination Programmes**
Combination programmes comprise a mixture of local admitted policies and a supporting non-admitted Difference in Conditions (DIC) and Difference in Limits (DIL) policy. This may take the form of purchasing the widest available coverage in the local admitted market with the DIC/DIL policy providing any additional coverage deemed necessary by the parent company. Alternatively, locally admitted insurance may be purchased for compulsory classes only supported by a more extensive non DIC/DIL policy. The local policies may be purchased from local admitted insurers, and then reinsured with a captive where legally permissible. The captive has the option of retaining some or all of the risk, or reinsuring with the commercial reinsurance market.

A Controlled master programme comprising local admitted policies for all overseas operating companies, supplemented by a Difference in Conditions policy purchased by the corporate risk management department from one insurer who has licensed operations in each of the required territories. The local insurance subsidiary insures the risk, collects the premium, deals with the taxes, issues the policy and pays the losses, but the risk is reinsured back to the insurers lead office.
Under these programmes all premiums and losses are paid, (to the fullest extent possible), in the countries where the exposures are located. The DIC policy is written according to corporate coverage standards to fill the gaps. Risk retentions can be accomplished using a captive insurer or other deductible funding mechanisms.

The rapid globalization of business has led to an increase in the number of international companies purchasing an integrated global insurance programmes. In order to cover its operations worldwide this involves master policies in the home jurisdiction and local policies issued in various other jurisdictions where the policyholder operates. The combined programme, however, may remedy many of the problems of the previous two approaches by using a combination of non-admitted policies where possible and admitted policies where the local regulations insist upon it or where penalties or taxes make it the only viable option. It has the advantage of providing a centralized, uniform insurance programme negotiated with one lead carrier meeting corporate standards, as well as the benefit of having local policies issued to each operating company that also meet, or come close to meeting, corporate criteria. Control can be centralised without compromising local regulations or breaking local law. These types of programme, however, require careful underwriting, experienced claims handling and extensive coordination among business units in different countries and can be complicated to administer. It is also worth noting that whilst non-admitted insurance is illegal in the vast majority of territories, excess policies and DIC/DIL are permitted in many more territories. Many combined programmes work on the basis that local cover needs to be broadened in order to provide the appropriate and chosen level of protection for the group as a whole.

The master/local international insurance programs can be structured in a variety of forms.

1. Locally admitted insurance provides the widest available coverage supported by a non-admitted DIC/DIL. In this combination, each subsidiary purchases the broadest possible cover which is available in the local market and any additional cover which the parent requires is provided by the master DIC/DIL policy purchased centrally. This ensures that the subsidiaries comply with all local regulations and pay premium tax. Premiums and the majority of claims are paid in the local currency thus eliminating the problems which occur with currency fluctuations and the importation of currency under a non-admitted policy. Local management are able to retain the benefit of local insurers who understand the local market, policy wordings, legal system and the detailed workings of the subsidiary, yet the DIC/DIL provides the uniformity and level of cover for the parent and includes the widest possible wording.

2. Locally admitted insurance is purchased for the compulsory classes only supported by a non-admitted DIC/DIL or master programme. The subsidiary, in this combination, purchases just the compulsory classes of insurance or provides the minimum cover available
to comply with the regulations. The DIC/DIL cover is purchased by the parent to provide the majority of the worldwide cover. This has the advantage of complying with local regulations, but provides the parent with a greater element of control. In this scenario it is possible that more claims will require payment from the master programme and whilst we have already noted that there is a greater acceptance of DIC/DIL policies, the possibility of facing currency fluctuations is greater under this combination.

3. Local admitted insurance reinsured through a captive insurer. The subsidiary purchases insurance policies from local admitted insurers, who then reinsure as much premium as is legally permissible to the parent’s captive insurance company. Central control is managed through tying all the various national policies into a single programme through the captive although tight controls are required to ensure the timely remittance of premiums and payment of claims. The captive has the option of retaining the risk or reinsuring with the commercial reinsurance market, depending upon the risk tolerance of the captive.

4. Under a controlled master programme the corporate parent uses one international insurer and its network of subsidiaries and its affiliates to structure the international programme. The insurer is commonly known as master policy insurer or lead insurer. The subsidiaries or affiliates are licensed in the countries of operation assisting in the issuing of admitted policies and providing claims and other policy related services. Locally admitted contracts issued by that insurer or through its local representatives which, ideally at least, duplicate or approximate the global master policy’s wording as closely as possible. Local conditions determine the scope of local coverage, and minimum amounts may be purchased if tariff rates are high and coverage restricted. Global insurance programmes typically involve interaction between the Master policies issued in the home country and local policies issued in other countries in which the policyholder operates. These policies may contain different conditions, terms and exceptions particularly where the local policy wording has to be filed and approved by a local insurance supervisor or regulator. In many instances, the insurer issuing the master policy will arrange for the local policies to be issued by it subsidiaries or by affiliated insurers affiliated over which it has control. In other instances, however, a local policy will be issued by an unaffiliated insurer, because of policyholder preference, absence of an affiliated insurer in a particular country or local regulatory requirements.

4.3.1 Benefits of Combination Programmes

Compliance
This process is able to operate even in strictly regulated markets as the local insurer can act as fronting insurer and then reinsure (to the fullest extent legally possible) with the master insurer.
Costs
The controlled master programme provides account leverage; one global, volume
discounted premium negotiated by the risk manager with one insurer often resulting in
better terms and conditions and claims negotiations. Premium savings can be realised by
minimizing duplicate coverage and consolidated purchasing.

Broader cover
There is a stronger likelihood that the insurer will offer more flexible terms with respect to
form and coverage because its spread of risk is greater.

Premium Tax
As premiums and losses often can be paid in the countries where the exposures exist, it is
generally tax neutral, insurance premium taxes will be paid, but premiums will be tax
deductible. Where pricing terms and terms and conditions are flexible, purchasing locally
the broadest coverage available will be more appropriate. A broad admitted contract may
provide the greatest tax benefit and local accountability and its premium may more
accurately reflect local experience. The lead insurer is able to coordinate the programme
through its international subsidiaries and affiliates. The centralising of underwriting involves
the detailed analysis of all the exposures, loss experience and pricing and the centralising of
claims administration and other services such as loss control allows a consistent approach to
be implemented.

Corporate Risk Management
A centralised approach is more likely to realise corporate risk management goals including a
consistent risk management strategy. The global programme can use additional risk
financing options that incorporate incentives for loss control through cost allocation and
allow for various deductible levels to offer local managers more decision authority. The risk
manager’s corporate perspective can enhance the allocation process, requiring local
subsidiaries to bear only what they are financially capable of sustaining. The Risk Manager
must also be aware of Transfer Pricing issues. Transfer pricing rules generally require
premiums to be allocated on an arm’s length basis in accordance with the location of the
risk.

Uniformity of cover
By providing cover for all exposures, gaps in cover which existed under the differences in
terms and conditions under local polices can be eliminated. Multinational international
operations may be interdependent; a disruption in one facility can interrupt others. By fully
integrating the domestic and overseas exposures in a global master programme, any gaps
in coverage are eliminated.
Claims handling
This type of programme provides a standardised approach to global claims handling and risk control efforts, while permitting local claims payments in local currencies and ensuring that local engineering codes are followed.

4.3.2 Drawbacks of Combination Programmes
Full integration of local and overseas exposures is not without its shortcomings and challenges.

Implementation
Global programmes are very time-consuming to put together. Collating information on all the risks of the subsidiaries requires time and expense as well as the cooperation of all the operating units. Board level support is essential to implement the international programme and ensure its successful operation. Communication is essential to ensure every party involved in the programme fully understands their participation and role. Local intransigence and attempts to retain autonomy can provide difficulties for the global programme.

Documentation
Reinsurance documentation and fronting agreements are very lengthy documents and require significant input from insurers, risk managers, brokers and legal advisers to ensure they correctly reflect the arrangements in place.

Cost
The cost savings which appear to be inevitable when combining a number of programmes can not necessarily be guaranteed. Local subsidiaries may benefit from competition and from long standing relationships.

Aggregate Limits
In programmes where there is a single annual aggregate limit, the total amount payable under the entire global programme is specified by the master policy. Claims payments under any part of the global programme erode the limits of the master policy and have a direct impact on the cover remaining under all local policies and the master policy. If the limits are exhausted with a loss or losses anywhere, then cover is exhausted under the entire programme, despite the fact that, on face value, limits are still available under the terms of the other local policies.

For example, if a claim arose under a Malaysian local policy exhausting both the limit of that policy at £25,000 and the limits of the master DIL policy at £50,000, then no cover would be available under any other local policy anywhere in the world. In such circumstances, disputes could arise in another jurisdiction where a claim was filed under a local policy but had not been paid by the time the Malaysian claim was resolved.
In the US and many other jurisdictions, strict adherence to policy terms and conditions is expected. If such a position was litigated in the US courts, any ambiguity may be construed against the insurer under the doctrine of *contra proferentum*.

**Interaction between master and local Policies**

It is also possible that, regardless of the intent of both parties, as expressed in the master policy, the local policy must be given independent effect and its limits cannot be eroded by other payments. In the US this argument may be based on regulatory or public policy or on the rights of third parties, i.e. claimants, who may be deemed to have acted in reliance on the coverage apparently provided by the local policy. Each local policy, therefore, should reference that it forms part of a global programme and that cover available under the local policy is part of and subject to the limits and other terms of the global programme detailed in the master policy. In addition to traditional coverage disputes about the meaning of individual policy provisions, global programmes may result in coverage disputes about the scope or interaction of master/local policies, and differences in conditions or applicable limits.

**ENDORSEMENT - UNDERLYERS ISSUED IN ADDITION TO MASTER POLICY-DIC**

Where foreign underlyer policies have been issued in addition to and in conjunction with this policy at the request of the policyholder, and where any claim or loss is covered under any foreign underlyer policy but such claim or loss is not covered pursuant to the terms and conditions of this policy, then the liability of the insurer shall be strictly limited to such foreign underlyer policy with respect to such claim or loss, including with respect to the limit of liability specified under such policy. The insurer shall under no circumstances also be liable under this policy with respect to such claim or loss and shall not be liable to provide the same or similar cover under this policy other than in accordance with the terms and conditions of this policy.

**ENDORSEMENT TO BE ATTACHED TO UNDERLYER POLICIES**

Notwithstanding any provision to the contrary in this policy the insurer shall be under no obligation to make a payment to any insured if and to the extent that the result of that payment being made would otherwise be that the insured’s aggregate liability under and for the period of the UK Worldwide Policy would exceed the Worldwide Master Aggregate Limit of Liability.

The inclusion of policy exclusions or other critical provisions in the local policy that are not referenced in the master policy may give rise to additional problems. If the master policy does not contain a provision stating that its coverage is under the same terms as that provided by the Local policy, an insured could argue that the master policy should respond to a claim otherwise excluded under the local policy.
For example, if the U.S. local policy contains a pollution exclusion clause, as most US general liability policies do, but the master policy is silent as to coverage for pollution, an insured could argue that, even if a pollution claim is excluded by the local policy, the master policy should respond to provide coverage for such a claim. If the master policy contains a difference-in-conditions provision, the argument for pollution coverage would be strengthened even if that was not the intent of the parties.

**Modifications to policy wordings**

If the provisions of the Local policy are changed while the coverage is in effect and the same changes are not reflected in the master policy (or vice versa), a dispute may arise as to which policy language applies. Care must be taken to make sure that any changes to the policy terms and conditions are accurately (and consistently) addressed in both documents.

If the master policy contains provisions that modify or restrict policy terms under the local policy and the local policy does not contain a programme clause expressly referencing the master policy and stating that the local policy is subject to the terms and conditions of the master, further problems may arise. If this is the case, as with master policy monetary limits discussed above, the insured can argue that the Local policy is entirely independent from the master policy. US regulatory requirements may restrict the enforceability of master policy terms and may make difficult the express subordination of the US local policy to the terms of the master policy.

Careful underwriting is essential to ensure that the intent of the parties is clear from the face of the master and local policies and both policies read as a whole. Explicit clauses should be inserted in both the master and the local policies establishing the interaction between the two policies, particularly regarding limits and trigger of coverage issues. Exclusions set forth in one policy that are intended to apply to both policies should be contained in both policies (or at least cross-referenced) and where changes are made under either policy, care should be taken to ensure the changes are appropriately and consistently reflected in both policies.

A contractual mechanism should be included to assure that any payment under a local policy that exceeds the intended scope of the overall coverage may be recouped from the corporate parent either through the master policy or more appropriately through a separate agreement such as an indemnity agreement, although this will need careful drafting to ensure it does not create additional problems on a D&O Policy.
Indemnification
In Malaysia, any provision, whether contained within the company’s Articles of Association or in any contract exempting any director from or indemnifying him against any liability for negligence, default, breach of duty or breach of trust is void.\textsuperscript{32} If the Directors and Officers Liability policy is exhausted (as discussed above) there may still be an obligation for an insurer to pay out due to strict adherence to policy terms and conditions being enforced. The insurer would invoke the indemnity agreement in force between the insurer and the insured, however, this may be construed as circular indemnity (the insurer pays the director and the insured pays the insurer) and also deemed to be void.

Claims handling
In addition, care must be taken with administering claims arising under global programs to minimise coverage disputes. Instructions and procedures for handling global claims in applicable claims handling manuals must be carefully drafted. Designated, experienced, trained claims handlers should oversee these claims to ensure that all the claims are appropriately apportioned to the correct policy and payments are made through the appropriate channels. Claims under local policies which attach to a master should be automatically flagged and the master policy must be immediately identified and the terms of both policies evaluated. Open and appropriate communication between claims and underwriting personnel and the principal insured and its broker or consultants is essential.
5 Insurer Requirements

5.1 Administration
The administration of a global risk management programme requires local service, global loss control services, global claims service, and sophisticated information technology. The most efficient programmes typically involve both a global broker and a global carrier. The choice of insurer is very important to the success of the global programme; there are very few insurers who are capable of implementing such a programme and many have to rely on arrangements with other insurers in countries where the multinational does not operate or where the insurer cannot provide the right level of service. An insurer with international expertise can offer peace of mind as companies expand in new territories.

5.2 Local Knowledge / Technical skills
The insurer needs to have a good understanding of the local market, including the legal system, economic climate, language and customs. Local representation can provide current information on the insurance requirements in each country and critical information on changes in legal and economic environment. As we have already discussed, the political and economic landscape in foreign countries creates difference business risks for companies. The insurer needs to be able to provide specialised products or a portfolio of products to address these issues.

The multinational products must be supported by a network of experienced service providers who can issue the policies, collect premiums, pay taxes, handle claims and provide loss control services. In addition, the multinational insurer must have financial stability and the commitment of senior management to remain in the multinational market for the long term. Multinational companies need to be able to rely on the financial security of the insurer, particularly in areas where the claims may not materialise or develop for several years.

The insurer should also be able to provide consistent worldwide technical services including physical risk control, engineering reports, business interruptions surveys, workers compensation assessments and statistical claims analysis which comply with local regulations and can also relate to the multinationals risk management strategy.

5.3 Ability to write excess covers
The insurer needs to have the ability to provide excess or umbrella covers in countries where there are restrictions, such as a lack of capacity, restrictive wordings, compulsory cessions or tariffs and the capability to cede as much by way of reinsurance as possible after taking account of local legal restraints. If the local polices can be reinsured back to the multinational insurer, this provides the uniformity of cover.
5.4 Cost

Reduced administration and bulk purchase should make competitive pricing available through a multinational insurer, although fronting fees, reinsurance premiums, engineering costs and claims handling costs must be factored into the overall costs. The insured will require the flexibility to allocate the premium to local operations according to its own allocation model. Given the various regulations which surround multinational insurance the insurer will need to be able to replicate this flexibility. Given that there are relatively few insurers who are capable of providing such a worldwide programme, it is possible that there may be a degree of monopolistic or oligopolistic charges included in the rates.

Exchange controls, currency fluctuations and inflation all have an impact on the payment of claims between the master insurer, the local insurer, the parent company and the subsidiary. It is essential for the insured and its subsidiary that claims are handled quickly and efficiently, comply with local regulations yet are acknowledged to be part of a global programme.

5.5 Structure

The multinational insurer must be structured to co-ordinate centrally the worldwide package and to be in a position to make decisions on fronting fees, underwriting, handling costs and claims settlements even where there may be disagreements with insurers’ local subsidiary. The local offices need to balance the flexibility to adapt cover to the particular needs of the local subsidiary whilst fulfilling the parent company’s requirements. Consistency and uniformity of service provision are high on list of insureds’ requirements. The insurer must exercise a high degree of control over its local offices whilst allowing for local servicing to respond in a timely and appropriate matter to subsidiary concerns.

If the insured uses a captive as part of the global programme it is essential that the premiums are transferred to the captive as soon as possible. Some territories impose exchange control, reserve withholding restrictions and financial penalties on reinsurance premiums which are passed out of the country to risk funding mechanisms. The best multinationals will provide a guaranteed cash flow programme which provides interest penalty payments if deadlines are missed.
6 Broking Service Requirements

Given the complex nature of international insurance it is difficult for corporate risk management departments to manage the worldwide insurance programme. A global broker, therefore, has a crucial role assisting in the implementation and ongoing management of a multinational programme. The use of such a broker specialising in global business with the ability to provide risk management resources in all the jurisdictions where the client operates can add value to the multinational insurance programme.

6.1 Operating Protocols

Operating a multinational insurance programme requires a clear set of operating protocols and uniform documentation. These need to be created by the broker and the corporate risk manager to ensure they are delivering the information the multinational corporation needs, when they need it.

Operating protocols and service plans should include:

- A summary of the insurance programme
- Details of the multinationals’ local business activities and contacts
- An agreed service plan outlining the responsibilities of the broker’s global and local office
- Details of reporting requirements e.g. for local acquisitions and changes in exposure
- Claims reporting and handling procedures, including any third party claims administrators or loss adjusters
- Loss Control requirements
- Details of responsibility for local lines of insurance outside the scope of the multinational insurance programmes
- A timetable for gathering exposure information
- An approved method of remuneration
- Details of any transitional arrangements

6.2 Broker Network

The broker must have a network matching the domestic and international territories of the multinational client and must control, direct and execute the business philosophy and initiatives for the multinational through their network. Through this network the broker can provide expert knowledge on insurance markets, the legal system and admitted policy wordings in each jurisdiction, provide advice on options for self insurance or use of a captive, provide claims handling expertise and supply loss control surveyors and other associated services.

The co-ordinating office has the task of implementing the corporation’s risk and insurance strategy, it is the hub which drives service distribution and updates all local offices in the
network. Effective coordinating offices need to be part of a core insurance team, staffed by professionals skilled in the technical aspects of insurance and risk as well as the nuances of international business. The multinational insurance programme is managed from the hub ensuring that all local policies are in place. It implements and monitors the service plan, and advises on service issues as requested by the local offices. The directives issued by the multinational client should be communicated around the world as an extension of insurance and risk management department fulfilling a liaison function between the global servicing team and corporate risk management department.

Functions of the central office:

- Identify the buyers’ needs, understand the buyers’ business and international management
- Collect and collate underwriting data from local operations
- Design the master programme including excess covers in terms of wordings and limits
- Design the programme at local level, including assessment of admitted –v- non-admitted insurance, compulsory insurances or cessions
- Establish retention levels at both group and local subsidiary level
- Assist in the identification and selection of multinational insurers
- Communicate to their network, ensuring they are aware of programme structure and operations,
- Establishing authority over local (non-owned) brokers
- Collect premiums and claims payments
- Assist with premium allocation
- Monitor the programme including premium flow,
- Issue the multinational policy documents
- Hold regular review meetings
- Encourage direct contact between buyer and insurer / reinsurer
- Assess insurer security
- Provide information on legislative / regulatory changes in different countries around the world
- Undertake a risk financing audit
- Provide technical services such as risk identification and loss control surveys
- Provide advice to find solutions to common problems such as rigidity of tariff regimes, taxation regulations, compulsory cessions, poor local risk management standards, opposition from local partners
- Deal with legislative restraints and the problem of internal politics

Functions of the local broker

- Understand the multinational programme and corporate philosophy
• Arrange the local covers according to requirements of the programme such as scope and limits of cover
• Provide a full local service including collection of local premiums and local claims payments
• Report to the central broker on relevant developments and changes in risk profile such as major changes in asset or turnover values, new products and processes, any acquisitions or divestments and any new locations

The broker is tasked with ensuring communications are aligned in content, timing and focus as it is essential to ensure that messages travelling from global centres to local operations (either brokers or insurers) are the same to avoid confusion.

The efficient implementation of insurance programmes requires a clear statement detailing that control should rest with the co-ordinating office, which can then enforce its authority throughout the network. The co-ordinating office needs to have the authority to mandate that the service level agreed with the global risk manager takes precedence over local service models and the local broker needs to recognise the role and authority of the co-ordinating office and execute their part of the global plan according to the client’s request and service standards

**6.3 Remuneration**

The level and basis of remuneration should be agreed between the client and the co-ordinating brokers’ office. All services should be detailed and allocated between the co-ordinating office and the co-ordinating office to ensure there is clarity and that the fee charged is a fair reflection of the services provided and the resource required to perform the services.

The brokers remuneration must be equitably distributed between the co-ordinating office and the local offices to fairly represent the client’s understanding of assignment, activity and responsibility. This is a sensitive area which must be handled correctly to fairly compensate and incentivise the brokers local offices. Without such incentivisation, there is a risk that the local broker may be more interested in looking after the interests of the buyer’s local operation than the parent company. This can aggravate internal disagreements caused by the programme between the parent company and local operation. In extreme situations, the local broker will see the local operation as its primary client and may back them against the centralising of insurance buying or even oppose the programme in order to gain favour with its local client.
7 Conclusion

Arranging appropriate multinational insurance to cover ever growing risk exposures against a background of diverse and complex legal and tax regulations is no easy task. There are a myriad of rules and regulations which dictate how insurance is written, who can write insurance, on what terms and conditions insurance can be written, who can act as an intermediary and what taxes or other charges must be paid in addition to the premium. Whilst global business would appear to be operating in a ever decreasing world, due to the advances in technology, insurance does not appear to be following this trend. It is an industry which still presents huge barriers to entry (capital requirements, licensing regulations etc), and imposes these in a different form in each jurisdiction where the insurer may wish to operate. There are only a few insurers, (i.e.) AIG, Chubb, ACE, Zurich who have the capability and commitment to write insurance on a truly multinational basis.

Implementing a global programme takes a considerable amount of time and effort. Multinationals have to establish and assess the risks to which they are exposed, determine their risk appetite and then decide how best to finance those risks they do not wish to retain. Insurance is a common risk financing option and ensuring that all aspects are compliant is complex.

The use of purely non-admitted insurance, whilst still being cost effective option providing consistency of cover and central control, is probably reducing in appeal and appropriateness. The plethora of corporate governance regulations worldwide makes the use of non-admitted fraught with dangers. Most jurisdictions have always prohibited non-admitted insurance but have not enforced the regulations with any vigour and in the past it has been common practice for risk managers to use this form of insurance, particularly for classes such as D&O or Crime. With Sarbanes-Oxley, the landmark Kvaerner tax case, which clearly defined insurance tax liability for the European Union, and other regulatory and legislative developments in many jurisdictions, the use of non-admitted may no longer be an acceptable option for a multinational who wants to demonstrate good governance and be a good corporate citizen. Indeed for the Directors of multinational companies, the consequences of not doing so may range from fines and penalties to imprisonment. In addition, governments worldwide are looking to maximise their revenue. Subsidiaries of foreign companies are likely to be targets of revenue enhancement and may be subject to a higher risk of scrutiny from tax authorities. Potential tax liabilities are now an important risk for buyers of non-admitted insurance.

Where coverage has been arranged on a non-admitted basis, complications arise due to the absence of local documentation. An insurer may elect to pay a non-admitted claim either directly into the country in question or in the country (UK) where the master policy is issued. If local payments are detected and the non-admitted insurance was arranged in
violation of the law, then the claim payment may be subject to tax assessment and fines and penalties may be imposed. If the payment is made into the UK, then it is subject to Corporation Tax at 30%, thus significantly reducing the claim payment.

Of even more concern are overseas claims made under the Directors and Officers Liability policy. In jurisdictions where it is illegal for the company to indemnify its directors, the director would expect to look to his D&O policy for assistance with defence costs. If the policy cannot respond because non-admitted insurance is also illegal, the Director is left without financial recourse.

would be likely to be more cost effective in terms of premium and time to purchase a local insurance policy in each country of operation. The advantages to this approach include regulatory compliance, since most countries prohibit purchasing insurance from unlicensed insurers, the use of a local broker who can serve local needs and interpret coverage terms and conditions. The disadvantages include having different terms and conditions, different limits of cover, which may not be adequate, restricted insurance expertise and having little or no leverage in trying to obtain better terms and pricing due to relatively small premiums for each local policy.

To provide some consistency, DIC/DIL policy can be purchased on a non-admitted basis which will “drop down” to provide insurance in the event the country does not require locally purchased (admitted) insurance. This policy would also sit in excess of the local limits in those countries where locally admitted insurance must be purchased and can provide broader terms and conditions than typically available locally. Advantages of this approach include the confidence that all countries have consistent terms and conditions; overall cost reductions may be available by limiting the purchase of local insurance to those countries where admitted insurance is mandatory. A disadvantage of this approach may be the risk of a fine or penalty if the DIC/DIL policy is used as primary coverage, or and excess layer has to act as a primary layer due to erosion of the primary layer, in a country that prohibits non-admitted insurance or where DIC/DIL is itself illegal.

Companies with major international operations the most efficient and effective option is to purchase a master controlled programme with the local admitted insurance being written by the master controlled programme insurer. This provides an almost seamless global insurance programme (always remembering that in some jurisdictions, some classes must be placed locally), ensuring maximum coordination between local policies and the master policy. This arrangement maximises purchasing leverage in negotiating the best terms and pricing for the corporation and eliminates the administrative hassle of dealing with tacit renewals with various expiry dates. Premium negotiation and claims payments are centralised with one point of contact and the cover is consistent worldwide.
With this type of programme, it is very important to have a highly competent team to oversee the global programme and a partnership with an insurance carrier that can write local insurance in all the relevant countries. Communication is the key to establishing and monitoring a successful global programme with effective operating protocols established between local offices, insurers and brokers.

The multinational insurance world is a diverse and complex one with separate and diverse rules and regulations operating in each and every jurisdiction and in order to maximise the responsiveness of a global programme the multinational should review its global profile to see which countries prohibit non-admitted coverage or impose restrictions or additional taxes on the use of non-admitted coverage. The requirements need to be mapped against the countries which cause the greatest concern in terms of size of existing operations, strategies for growth, strength of insurance regulator etc. Ultimately each company must carefully evaluate its unique business and tax situation prior to deciding upon a global insurance structure, and seek legal and technical advice when selecting insurance partners, implementing the programme, and negotiating coverage details. The optimum programme structure should take into account the business environment of each territory together with the covers which must be placed locally, the taxation implications, and the limits and deductibles required in each territory to ensure a match with the financial capabilities of the operating company and compliance with local regulations.

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17 IAIS Regulation document
18 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
19 FSA Website
20 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
21 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
22 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
23 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
24 Mutual Assistance Directive
25 Willis Webcast
26 RIRG – Establishing an effective multi-national insurance programme
27 Global implications
28 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
29 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
30 Aon’s Global Insurance Guide, powered by AXCO Insurance Information Services
Contra proferentem is a rule of contractual interpretation which provides that a term which is found to be ambiguous should be construed against the party which imposed its inclusion in the contract. That is, the preferred interpretation will be the one most favourable to the party upon whom its inclusion was imposed. Or, more accurately against (the interests of the party who imposed it). The rule only applies if, and to the extent that, the clause was included at the unilateral insistence of one party without having been subject to negotiation by the counter-party.

Malaysia: Companies Act 1965 Section 172 (1)
# Glossary of Insurance Terms

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Admitted Insurance</td>
<td>Refers to a policy(ies) that is issued by a locally licensed Insurer in the country where the property or risk is located.</td>
</tr>
<tr>
<td>Captive Insurer</td>
<td>This usually is an insurance company formed to insure the risks of its owner (parent company).</td>
</tr>
<tr>
<td>Compulsory Insurance</td>
<td>Refers to coverage required by law. Such coverages must be written on an admitted basis in the country of insured operations.</td>
</tr>
<tr>
<td>Controlled Master Programme</td>
<td>Refers to a program wherein all policies and their terms and conditions are agreed centrally with a worldwide Insurer(s) and supported by underlying (admitted where required and/or desired) policies issued in each country where the Insured operates.</td>
</tr>
<tr>
<td>Difference-in-Conditions</td>
<td>Refers to a policy or clauses in property insurance which 'wrap around' basic perils provided by local primary policies so as to include, as an example, the perils of earthquake, flood, collapse, etc. The use of a DIC policy or clause in the Master Policy provides worldwide consistency of terms and conditions.</td>
</tr>
<tr>
<td>Difference-in-Limits</td>
<td>This wording is mostly found in the Master Policy and provides excess limits over locally admitted underlying policies bringing them to a predetermined uniform level within the Controlled Master Program (CMP).</td>
</tr>
<tr>
<td>Fronting (Company)</td>
<td>In international insurance, this refers to a locally admitted Insurer ceding the local risk, less any retention - fronting fee - and/or taxes, to its Reinsurer.</td>
</tr>
<tr>
<td>Global Programme</td>
<td>Refers to a worldwide insurance program which includes the parent company's domicile. As opposed to a Controlled Master Program (CMP) which covers mostly only the foreign operations of a multinational company.</td>
</tr>
<tr>
<td>Guarantee Endorsement</td>
<td>In non-restricted countries, achieving the terms, conditions and coverage of the Master Policy is not a problem; however, rather than translating each and every policy to be sure it agrees with the Master, a Guarantee Endorsement should be endorsed so that all its provisions apply locally regardless of the local terms and conditions.</td>
</tr>
<tr>
<td>Local Policy</td>
<td>An admitted insurance policy issued in the country where the risk exposure exists to support a controlled master or global insurance programme. The policy is issued to comply with admitted insurance regulations and duplicates portions of the coverage provided by the master policy.</td>
</tr>
<tr>
<td>Term</td>
<td>Description</td>
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</tr>
<tr>
<td>Master Policy</td>
<td>An original, complete insurance policy contract that is issued by an insurer with the understanding that certificates of insurance or underlying policies will be issued to others.</td>
</tr>
<tr>
<td>Non-Admitted Insurance</td>
<td>Insurance which is not provided by a locally admitted (licensed) Insurer in a given country or state.</td>
</tr>
<tr>
<td>Punitive / Exemplary Damages</td>
<td>Punitive damages (termed exemplary damages in the United Kingdom) are damages not awarded in order to compensate the plaintiff, but in order to reform or deter the defendant and similar persons from pursuing a course of action such as that which damaged the plaintiff.</td>
</tr>
<tr>
<td>Self Insurance</td>
<td>Protecting one's self or company by putting aside money to pay for otherwise insurable and predictable losses. To purchase insurance for these types of losses would cost more because in addition to the premium charged, Insurers charge for their overhead, selling, general and administrative charges plus any premium taxes.</td>
</tr>
<tr>
<td>Tariff Rate</td>
<td>Refers to standard rates set by a rating bureau, Government Authority, or associations of Insurers for a particular line of coverage. In some countries and/or markets, tariff rates are strictly enforced and in others, they act as guidelines.</td>
</tr>
<tr>
<td>Tax Liability Endorsement</td>
<td>This endorsement should be made part of a Controlled Programs' Master Policy. It provides that if a valid foreign claim must be paid in the USA (other countries should check their tax laws for applicability), Insurer(s) will pay any income tax the Insured will incur as a result of the claim payment.</td>
</tr>
<tr>
<td>Workers' Compensation</td>
<td>Workers' compensation provides insurance to cover medical care and compensation for employees who are injured in the course of employment, in exchange for mandatory relinquishment of the employee's right to sue their employer for the tort of negligence.</td>
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Bibliography


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<thead>
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