The Insurance and Reinsurance Law Review

Editor
Peter Rogan

Law Business Research

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EDITOR'S PREFACE

It is hard to overstate the importance of insurance in personal and commercial life. It is the key means by which individuals and businesses are able to reduce the financial impact of a risk occurring. Reinsurance is equally significant: it protects insurers against very large claims and helps to obtain an international spread of risk. Insurance and reinsurance plays an important role in the world economy. It is an increasingly global industry, with the emerging markets of Brazil, Russia, India and China developing apace.

The insurance and reinsurance industry is remarkably resilient. In recent times it has been severely tested, but has passed the test on every occasion. Three examples spring to mind. As a lawyer steeped in the London market the first is the source of some personal pride. In the late 1980s and early 1990s the Lloyd's market suffered enormous losses arising largely as a result of a combination of asbestosis and pollution-related claims and the market practice, prevalent at the time, of placing inter-syndicate excess of loss retrocession in respect of catastrophe losses, commonly known as the London Market Excess of Loss (LMX) spiral. Those losses ultimately led to a plethora of litigation and forced many Lloyd's Names to cease underwriting. The scale of the losses also affected the solvency and liquidity of Lloyd's.

In 1996 Lloyd's implemented a reconstruction and renewal (R&R) plan, a complex market restructuring. Ultimately Equitas was established to reinsure and run off the 1992 and prior years' liabilities of the Names. In November 2006 National Indemnity Company, a member of the Berkshire Hathaway Group, reinsured all the liabilities of Equitas and Resolute Management Services Ltd, another member of the Berkshire Hathaway Group, took over responsibility for the run-off. On 25 June 2009 the English High Court approved the transfer of the 1992 and prior business of the Names to Equitas with the effect that, as a matter of English law, Lloyd's Names no longer have any liability for the 1992 and prior years' losses. This restructuring has been extremely successful in enabling Lloyd's not only to continue operating but to improve and enhance the service it provides. Lloyd's is today undoubtedly the world's leading market for internationally traded insurance and reinsurance.

The second test of the insurance and reinsurance market was the financial crisis of 2008–2009. While there were some high-profile casualties, in general the industry was able to withstand events better than other financial institutions, certainly better than the banks. With the exception of specialist lines such as directors' and officers' (D&O) and trade credit insurance, insurers and reinsurers suffered relatively little exposure to the financial market losses. The traditional insurance and reinsurance sectors were largely onlookers. Indeed I would go further and suggest that they arguably helped to provide a stabilising effect, given the nature of their business model and in particular a conservative investment approach. If the crisis has triggered a more stringent regulatory regime for financial services generally that is no bad thing, but it should not be forgotten that insurance activity neither led to, nor was unduly affected by, that crisis.

Finally, the natural catastrophes and man-made disasters of 2011 and 2012 have caused not only human tragedy and loss of life but also enormous insured losses. A 28 March 2012 study by Swiss Re (based on data from its *sigma* database) revealed that, altogether, natural catastrophe insured losses came to around US$110 billion, while losses from man-made disasters were around US$6 billion, making 2011 the second-highest catastrophe loss year ever for the insurance industry. 2012 was dominated by weather-related events in the United States, most notably Hurricane Sandy. On 19 December 2012, again based on *sigma* data, Swiss Re estimated that insurance losses arising from the catastrophic events of the year were set to reach approximately US$65 billion. The figure is of course moderate compared with 2011 but Swiss Re notes that it is above the average of the past 10 years.

The events of 2011 and 2012 provided significant challenges for the insurance and reinsurance industry for a number of reasons – one being the sizeable impact they had on manufacturing around the world, something that had not fully been appreciated in advance. However, the industry proved to be highly effective in overcoming these challenges. Despite losses on a historic scale and a difficult economic climate, it played a key role in bringing financial relief to populations, businesses and governments suffering from the effects of the disasters.

Events such as these test not only insurers and reinsurers but also the rigour of the law. From the English perspective, the Lloyd's Insurance and Reinsurance Reports, issued almost monthly, are never short of material to fill their pages. Insurance and reinsurance disputes provide a never-ending array of complex legal issues and new points for the courts and arbitral tribunals to consider. Taking the natural catastrophes as an example, these have thrown up issues of causation, claims notification, cooperation and control, the effect of 'follow the settlements' provisions and aggregation, to name but a few.

There are many insurance and reinsurance publications available. However, in this increasingly globalised industry there is a need for a source of reference that analyses recent developments in the key jurisdictions on a comparative law basis. This volume, to which leading insurance and reinsurance practitioners around the world have made valuable contributions, seeks to fulfil that need. I would like to thank all of the contributors for their work in compiling this volume.

Peter Rogan
Ince & Co
London
April 2013

Chapter 15

MALTA

Matthew Bianchi[1]

I INTRODUCTION

Malta has long been seen as an attractive centre for the financial services industry and as a result there has been political awareness that financial services should be one of the pillars of Malta's economy. This sector now accounts for around 12 per cent of Malta's gross domestic product.

The Maltese financial services industry has grown rapidly over the years, particularly from the early 1990s. The industry benefited largely from Malta's accession to the EU in 2004, mainly due to the ability of local licensees to passport throughout the EU. Malta's accession to the EU put it on a level playing field with all other EU Member States, with most of the financial services legislation and regulation being harmonised across the EU.

The insurance industry has been no exception. In fact, over the past couple of years, the local industry has grown from seven local insurers to approximately 54 licensed insurance undertakings authorised in terms of the Insurance Business Act.[2] These comprise 37 non-life insurers, eight life insurers, two composite insurers, seven reinsurers, and 10 affiliated insurance undertakings (eight of which are protected cell companies).[3]

Malta's legislative, regulatory and taxation framework offers Maltese insurance participants several benefits. Malta's full EU membership grants an insurer or insurance intermediary the right to 'passport' their licence and allows them to carry on insurance

1 Matthew Bianchi is a partner at Ganado Advocates. The author would like to thank Elaine Sultana, Ylenia Grech and Beppe Sammut for their contributions to this chapter.

2 1998, Chapter 403 of the Laws of Malta.

3 The Malta Financial Services Authority, 2011 Annual Report, available at www.mfsa.com.mt/Files/Publications/Annual%20Reports/MFSA%20Annual%20Report%202011.pdf.

business directly on a services or establishment basis in 30 European countries (27 EU and three EEA Member States) by following a notification procedure[4] to the Malta Financial Services Authority ('MFSA').

Malta is the only full EU Member State to offer protected cell legislation.[5] The protected cell company ('PCC') provides insurers with the opportunity of writing business while benefiting from the efficiencies that the PCC structure offers, by cells sharing in the capital base of the PCC, and benefiting from the economies of scale and scope that arise through the common management of the PCC carried on by the core. Furthermore, Malta is the only full EU Member State that has in place regulations that cater for incorporated cell companies.[6]

Malta's regulatory regime also recognises the particular nature of affiliated insurance undertakings (captives) and provides these undertakings with shorter application processing times and with certain derogations.[7] Malta also has in place the necessary regulatory framework to cater for insurance intermediaries, namely, insurance managers, brokers, agents and tied insurance intermediaries.

Malta's re-domiciliation regulations allow insurers to seamlessly transfer their seat to or out of Malta, without any break in the company's corporate existence or the need to re-execute any insurance policies or other contracts.

Malta also has in place an extensive double taxation treaty network that covers over 60 countries including the United Kingdom, France, Germany, Italy and the United States, and the Maltese government is actively pursuing additional treaties with particular emphasis on income arising from financial services. Furthermore, another benefit from a taxation perspective is that all insurance policies issued by Maltese insurance companies insuring risks that are situated outside Malta are exempt from Maltese stamp duty or any other form of Maltese insurance premium tax. Maltese company, insurance and fiscal law implement all the relevant EU regulations and directives, and is also based on tried and tested UK legal principles.

The MFSA is the single regulator of investment services, insurance, banking, pensions and trustee services in Malta, and also houses the International Taxation Unit and the Company Registrar. This provides a 'one-stop shop' for all market participants and ensures coordination between these different regulators. The approach of the MFSA is known to be firm but flexible and encourages informal discussion at all levels with all applicants, market participants and any other interested persons.

4 European Passport Rights for Insurance and Reinsurance Undertakings Regulations, 2004, Subsidiary Legislation ('SL') 403.14.

5 Companies Act (Cell Companies Carrying on Business of Insurance) Regulations, 2010, SL 386.10 ('PCC Regulations').

6 Companies Act (Incorporated Cell Companies Carrying on Business of Insurance) Regulations, 2010 SL 386.13 ('ICC Regulations').

7 The Insurance Business (Companies Carrying on Business of Affiliated Insurance) Regulations, 2003 ('Affiliated Regulations'), SL 403.11 and Insurance Rule 21 of 2007 on Business of Affiliated Insurance ('Affiliated Rules').

As a growing financial services centre Malta also offers many other benefits. Malta is consistently leading as one of the most cost-efficient domiciles for insurance undertakings. As an ideal location, Malta is only one hour ahead of GMT and only a short flight away from mainland Europe. Malta provides insurance companies with top professional services as most of the top international insurance managers have all been established in Malta since its accession to the EU, and the Big Four audit firms all have an establishment in Malta. Finally, Malta also offers a multilingual and well-educated workforce, with a modern and top ICT communications system and network.

II REGULATION

i General

The Maltese insurance regime is mainly regulated by the Insurance Business Act and the Insurance Intermediaries Act.[8] While the former regulates the activities of underwriters the latter regulates the activities of insurance brokers, managers, agents and tied insurance intermediaries. These two laws set out, *inter alia*, the general provisions that apply to the relevant insurance participants ranging from authorisation, prudential supervision, conduct of business and the powers of the MFSA.

The Insurance Business Act and the Insurance Intermediaries Act are supplemented by regulations promulgated under and in terms of the two laws and by detailed rules issued by the MFSA. The regulations and MFSA insurance rules act as detailed rules that have legislative force for all authorised entities, and provide market participants with a comprehensive and complete set of directives that apply during the application process as well as on an ongoing basis.

Insurance companies are incorporated as limited liability companies, bringing into play the Companies Act[9] and the regulations issued thereunder. The Companies Act acts as the main legislation that regulates all limited liability companies under Maltese law. The memorandum and articles of association of the insurance undertaking, the role and duties of directors, rules regarding share capital and transfer of shares, winding up and restructuring of insurance undertakings, *inter alia*, are all regulated by the Companies Act. In fact, the protected cell company and incorporated cell company are both regulated and catered for by regulations issued under and in terms of the Companies Act.

The Civil Code[10] is also relevant for certain matters relating to the business of insurance. The Civil Code plays an important role as it is the substantive law that applies to the law of insurance contracts, obligations of insurance companies, the agent-principal position and security interests.

There are other specific legislations that deal with particular areas of insurance, including the Motor Vehicles Insurance (Third-Party Risks) Ordinance,[11] the Merchant

8 2006, Chapter 487 of the Laws of Malta.

9 1995, Chapter 386 of the laws of Malta.

10 1870, Chapter 16 of the Laws of Malta.

11 1947, Chapter 104 of the Laws of Malta.

Shipping (Insurance for Maritime Claims) Regulations[12] and the Civil Aviation (Insurance Requirements for Air Carriers and Aircraft Operators) Order,[13] which set out compulsory insurance for motor vehicles, ships and aircraft respectively.

When pieced together, these various pieces of legislation ensure that Malta has in place a comprehensive and complete legislative and regulatory regime for insurance undertakings and insurance intermediaries.

ii The Insurance Business Act

Insurance and reinsurance undertakings and captives (referred to as 'affiliated' insurance undertakings under Maltese legislation) in Malta are all regulated by the Insurance Business Act, which caters for the authorisation and supervision of insurance business in Malta. The Insurance Business Act is largely modelled on UK statute and implements the requirements of the EU Consolidated Life Insurance Directive[14] and the three Non-Life Insurance Directives.[15]

The carrying on of insurance business is a regulated activity and MFSA approval is required prior to any person carrying on such activity. In terms of the Insurance Business Act, 'no person shall carry on, nor hold itself out as carrying on, in or from Malta, business of insurance unless authorised by the competent authority.'[16] The same Act defines the business of insurance as the 'effecting and carrying out of contracts of insurance'.[17]

Under Maltese law, non-admitted insurance is very exceptional and largely limited to reinsurance, 'large risks', or contracts of insurance entered into with the approval of the MFSA or the responsible minister, in each case with the involvement of a Maltese broker licensed in terms of the Insurance Intermediaries Act.[18]

Any person interested in establishing an insurance, reinsurance or affiliated insurance undertaking has to file an application with the MFSA and go through the authorisation process. While for insurance undertakings the Insurance Business Act sets

12 2012, SL 234.50.

13 2005, SL 449.41

14 Directive 2002/83/EC of the European Parliament and of the Council of 5 November 2002 concerning life assurance, as amended.

15 First Council Directive 73/239/EEC of 24 July 1973 on the coordination of laws, regulations and administrative provisions relating to the taking-up and pursuit of the business of direct insurance other than life assurance; Second Council Directive 88/357/EEC of 22 June 1988 on the coordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance and laying down provisions to facilitate the effective exercise of freedom to provide services and amending Directive 73/239/EEC; and Council Directive 92/49/EEC of 18 June 1992 on the coordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance and amending Directives 73/239/EEC and 88/357/EEC (Third Non-Life Insurance Directive).

16 Insurance Business Act, Article 6(1).

17 Ibid, Article 2(1).

18 Insurance Intermediaries Act, Article 31.

out a six-month period within which the MFSA has to consider an application,[19] the time period for affiliated insurance undertakings[20] and reinsurance undertakings is three months.[21]

Insurance and reinsurance companies have to satisfy minimum capital requirements upon incorporation and on an ongoing basis, referred to as the minimum guarantee fund.[22] The value depends on the class of business being undertaken and whether the undertaking is established as a direct insurer, reinsurer or affiliated insurance undertaking. The own funds requirements vary from €1.2 million for an affiliated reinsurance undertaking, to €3.7 million for general business, up to a maximum of €7.4 million for combined long-term, general insurance and reinsurance.[23]

All insurance and reinsurance companies are required to maintain at all times a margin of solvency[24] and adequate technical provisions[25] as set out in the Insurance Business (Assets and Liabilities) Regulations.[26] These must at all times be covered by admissible assets, which must be diverse. The solvency test for non-life insurers in Malta follows the Solvency I regime.

iii The Insurance Intermediaries Act

The Insurance Intermediaries Act implements the Insurance Mediation Directive[27] and establishes the legal and prudential framework for the regulation of insurance intermediaries' activities in Malta. This Act caters for the regulation of insurance brokers, insurance managers, insurance agents and tied insurance intermediaries. Any person carrying out the activities of a broker, manager, agent or tied insurance intermediary in Malta shall require prior MFSA approval.[28] At present there are 17 insurance agents, 27 insurance brokers (one of which is established as a PCC), 15 insurance managers (one of which is established as a PCC) and over 155 tied insurance intermediary established as companies. Insurance intermediaries are able to benefit from the passporting regime[29] and are therefore capable of passporting through the provision of services or by establishing a branch in all 30 EU and EEA countries.

The definition of insurance intermediaries' activities refers to the 'introducing, proposing or carrying out other work preparatory to the conclusion of contracts of

19 Insurance Business Act, Article 7(6).

20 Affiliated Regulations, Regulation 4(2).

21 Insurance Business Act, Article 7(8).

22 Insurance Business Act, Article 16.

23 Insurance Rule of 1 of 2007 on Own Funds of Companies Carrying on Business of Insurance.

24 Insurance Business Act, Article 14.

25 Ibid, Article 17.

26 2007, SL 403.16.

27 Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation.

28 Insurance Intermediaries Act, Article 6.

29 European Passport Rights for Insurance Intermediaries Regulations, 2005, SL 403.18.

insurance', and includes the conclusion of such contracts, assisting in the administration and performance of such contracts, in particular in the event of a claim.[30]

As their name implies, insurance brokers are referred to as persons who bring together persons seeking insurance and insurers, who play a role in the conclusion of insurance contracts and who assist in the administration and performance of these contracts (including claims handling).[31]

Insurance agents are persons appointed by an insurance undertaking to be its agent with the authority to enter into contracts of insurance on behalf of the company.[32] Tied insurance intermediaries are defined as persons carrying on insurance intermediary activities for or on behalf of one or more insurance companies in the case of insurance products that are not in competition. These persons may collect premiums or amounts intended for the policyholder, however they cannot make any insurance commitments towards or on behalf of the public.[33]

Insurance managers can provide services either to an insurer or to an insurance broker. In the former case, an insurance manager can accept an appointment from an insurer to manage any of its business and may have the authority to enter into contracts of insurance on behalf of the insurer. Insurance managers may also accept an appointment from an insurance broker with certain limitations specified in the law.[34]

The Insurance Intermediaries Act allows insurance intermediaries to be established as companies or alternatively, individuals can apply for enrolment into the brokers, managers or agents list maintained by the MFSA.[35] Furthermore, insurance brokers and managers can also be set up as PCCs. Each enrolled insurance intermediary must have an individual (usually a director if the enrolled person is a company) who is registered in the managers, brokers or agents register, as the case may be.[36] In all cases, whether it is the enrolment of an intermediary in the relevant list or the registration of an individual insurance intermediary in the relevant register, the MFSA has three months in which to decide on an application for authorisation.[37]

Insurance managers, brokers and agents are all required to satisfy applicable own fund requirements.[38] Brokers and agents have to satisfy the fixed own funds amount of approximately €60,000.[39] The minimum own funds required to be held by managers ranges from €17,000 to €60,000 depending on whether the manager is managing solely

30 Insurance Intermediaries Act, Article 2(1).

31 Ibid. Schedule to the Act.

32 Ibid.

33 Ibid.

34 Ibid.

35 Ibid, Article 9.

36 Ibid. Article 7.

37 Ibid. Article 13(5).

38 Ibid. Article 10(1)(a)(iv) and Insurance Intermediaries Rule 1 of 2007 on the Own Funds of Persons Enrolled in the Agents List, Managers List or Brokers List Carrying out Insurance Intermediaries Activities.

39 Ibid.

affiliated insurance undertakings and whether the manager has binding authority to enter into insurance contracts on behalf of the insurers.[40] Brokers, agents and managers (when they have binding authority to enter into insurance contracts) are also required to satisfy further conduct of business requirements, including rules regarding monies held in a fiduciary capacity,[41] compliance with rules regarding advertising[42] and disclosure of information to policyholders[43] and others.

iv 'Affiliated' or captive insurance

Captives, referred to as 'affiliated insurance undertakings' under Maltese insurance legislation, are defined as insurance undertakings registered in Malta to carry on business 'restricted to risks originating with shareholders or connected undertakings or entities'.[44] The wide definition adopted by Maltese legislation means that Maltese affiliated insurance undertakings can do much more than simply write the risks of their parent company. Maltese affiliated insurance undertakings may write risks originating from a range of persons, including their parent, associated or group companies, or individuals having a majority ownership and members of a particular trade,[45] among others. On the contrary, affiliated reinsurance is restricted solely to parent and group undertakings.[46]

Affiliated insurance undertakings benefit from certain derogations. The statutory limit for the MFSA to grant a licence to an affiliated insurance undertaking is decreased from six months to three months.[47] There are certain relaxations of the applicable publications that are required to be made in terms of the law for the publication of accounts[48] and transfer of a business.[49]

v Protected cell companies

Maltese legislation allows insurers, reinsurers, affiliated insurance undertakings, insurance managers and insurance brokers to be created as traditional limited liability companies or as protected cell companies. There are a number of PCCs already established in Malta that offer the operators of the cell the option of creating a segregated cell that can write insurance business, rather than setting up a stand-alone insurance undertaking. This is cost-effective, particularly for smaller operations wishing to write specific lines of business.

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40 Ibid.

41 Insurance Intermediaries Act, Article 20 and Insurance Intermediaries Rule of 2007 Monies Held in a Fiduciary Capacity.

42 Insurance Intermediaries Rule 5 of 2008 – Insurance Intermediaries Advertisement and Other Promotional Activities.

43 Insurance Intermediaries Rule 3 of 2007 – Disclosure of Information for Clients.

44 Affiliated Rules, First Schedule, Rule 2.

45 Ibid.

46 Ibid. Second Schedule.

47 Affiliated Regulations, Regulation 4(2).

48 Ibid. Regulation 4(3).

49 Ibid. Regulation 4(5).

A PCC is a regular trading company that can create one or more cells for the purpose of segregating and protecting the cellular assets from each other and from the 'core' assets of the company. This enables promoters to come together within the PCC framework and to share overhead costs while being protected from each others' liabilities. Alternatively, a single promoter can write separate lines of business from separate cells, thus segregating each line of business. A cell is created through the issue of cell shares, which allows cell owners to receive the profits of the cell by way of cell share dividends.[50]

Cellular assets attributable to a cell are only available to satisfy the liabilities of that cell and as a rule no recourse can be had to its assets by any creditor of another cell or of the core.[51] Generally, however, cellular creditors also have a right of secondary recourse to core (non-cellular) assets of the PCC, but only once cellular assets of that particular cell to which the liability is attributable have been fully exhausted.[52] Where the PCC is authorised as an affiliated insurance undertaking or to carry out business of reinsurance, the PCC may enter into agreements with creditors limiting recourse solely to the cellular assets of the PCC.[53]

Authorisation for the establishment of a PCC is subject to the time periods established under the Insurance Business Act, and depends on whether the PCC is being established as a direct insurer (six months) or reinsurer/captive (three months). Each cell forming part of the PCC will also require authorisation by the MFSA. The authorisation process and licence application for a cell is similar to that for the PCC with certain minor exceptions that cater for the fact that the cell is a part of an already authorised insurance company.

As the PCC is one legal entity[54] it is the PCC as a whole and not each individual cell that has to satisfy the minimum guarantee fund requirements. However, each cell would need to satisfy the required margin of solvency for the business written through the cell and those requirements relating to technical provisions.

Cells in a PCC, even though they do not have separate juridical personality, are treated as separate entities for fiscal purposes as though each cell were a limited liability company.

vi Incorporated cell companies

The incorporated cell company ('ICC') form has evolved from the PCC concept. ICCs are regular companies that may create incorporated cells in accordance with the ICC Regulations. Incorporated cells are themselves limited liability companies with separate legal personality.[55] ICCs and incorporated cells may only be established to carry on business of insurance, reinsurance or business of affiliated insurance.

50 PCC Regulation, Regulation 10.
51 Ibid. Regulation 13.
52 Ibid. Regulation 14.
53 Ibid. Regulation 15.
54 Ibid. Regulation 3(2)(a).
55 ICC Regulations, Regulation 10.

The general principles on the establishment and governance of companies apply to incorporated cells, albeit with significant relaxations. Most notably, an incorporated cell may be established as a single-member company;[56] a corporate company secretary may be appointed,[57] and the rules set out in the Companies Act on financial assistance do not apply.[58]

Unlike cells in PCCs, incorporated cells are separate legal entities with distinct legal patrimony to the ICC itself. On this basis, each incorporated cell will be required to satisfy own funds and solvency capital requirements in its own right. Since each incorporated cell is a separate legal entity, there is less risk that creditors of an incorporated cell seek recourse to the ICC or to any other incorporated cell forming part of the same ICC when compared to the PCC structure.

III INSURANCE AND REINSURANCE LAW

i Sources of law

The Maltese legal system can be described as a 'mixed legal system' having its foundations in both civil law and the English common law. Even though the Maltese legal framework boasts of such a mix, Malta has not inherited the common law doctrine of precedence and courts of law are free to interpret the law applying to similar situations in a different manner. Since its accession to the EU, Malta is also required to apply regulations and transpose directives of the EU within its legal system.

The elements of contracts under Maltese law are governed by the civil law doctrines found in the Civil Code, while common law has influenced mainly commercial law. In this respect, the principles of insurance contracts within the Maltese legal framework are a blend of civil and common law tradition, as will be explained in more detail below.

ii Making the contract

All contracts under Maltese law must satisfy certain essential elements in order to ensure their validity, these being capacity of the parties, free consent of the parties, lawful consideration and subject matter. If these prerequisites are not satisfied, the contract will not exist and will not be valid.

Another inherent element to the contract is formality. Generally, a contract can be concluded verbally. However, there are instances where the law would specifically require the agreement to be concluded in writing. The Civil Code distinguishes between two kinds of writing: private writing and public deed. The public deed is the most solemn form of agreement and is drawn up by a notary public and attributed public faith thereto. Such writing is deemed to be proof of its contents. The requirement of formalising an agreement through a public deed is applicable for a limited number of contracts, especially in the case of commercial transactions.

56 Ibid. Regulation 14.

57 Ibid.

58 Ibid.

Finalising a contract depends also on how and when it comes into existence. A contract is the unity of two or more consents and this can be broken down into two processes: the offer and the acceptance. For an offer to be valid, it must be expressed clearly in order to be capable of acceptance. On the other hand, acceptance must match the offer in all its elements. Once the offer and acceptance are united, the contract comes into existence.

These principles are therefore intrinsic elements to contracts of insurance. As explained above, common law custom has influenced the commercial Maltese legal system, including contracts of insurance. Thus, together with the Civil Code elements, the common law principles of insurable interest and utmost good faith are also applied to contracts of insurance under Maltese law. Insurable interest arises where a person stands to suffer a direct financial loss if the risk against which insurance cover is requested occurs. Insurable interest is not defined under Maltese law, however the Civil Code lists instances where insurable interest is presumed in the case of life insurance – spouses and dependents, life of employers and employees, etc.[59] Utmost good faith applies where the parties seeking insurance cover are required to disclose all material facts to the insurer. Maltese law generally attributes good faith to contracts; thus in the case of insurance contracts, the law has embraced this added tranch.

It is also pertinent to make reference to the definition of an insurance contract as found in the Insurance Business Act. The Act defines an insurance contract as:

> *An agreement whereby an insurer agrees, for a consideration, to pay to or for the account of the insured a sum of money or other consideration whether by way of indemnity against loss, damage or liability or otherwise, on the happening of a specified event which involves an element of uncertainty as to when or whether it will take place.*[60]

In terms of this definition a contract of insurance requires the following elements: legal entitlement for the insured to claim payment from the insurer when the specified event occurs; uncertainty as to when or whether the specified event will occur; lack of control with respect to both the insured and the insurer regarding the occurrence of the specified event; and the payment of money or money's worth by the insurer to the insured on the happening of the specified event.

iii Interpreting the contact

The Civil Code regulates rules of interpretation of a contract quite comprehensively. The general rule is that there shall be no room for interpretation where the terms of the agreement are clear and words in the agreement are attributed the meaning attached to them by usage at the time of the agreement.[61] If the literal meaning differs from the common intention of the parties, as clearly evidenced by the whole of the agreement, then preference will be given to the intention of the parties.[62] Interestingly, where there

59 Civil Code, Article 1712A.

60 Insurance Business Act, Article 2(1).

61 Civil Code, Article 1002.

62 Ibid. Article 1003.

is doubt, the agreement shall be interpreted against the insurer and in favour of the insured.[63]

iv Agency

Agency is generally dealt with by the Civil Code under the rules of mandate and it is defined as the act whereby one person gives to another the power to carry out something on the mandator's behalf.[64] This contract can only be perfected once the mandatary has accepted the contract. Agency is also dealt with in the Commercial Code,[65] whereby it is classified into two parts: general mandate and mercantile mandate. In the case of agency the agent acts on behalf of the principal, and any acts that the agent carries out and are within the authority granted to him or her by the principal shall have effects, whether positive or negative in relation to the principal.

The notion of principal-agency plays an important role in relation to insurance brokers, agents, managers and tied insurance intermediaries in terms of the Insurance Intermediaries Act. Moreover, insurers can appoint agents other than agents licensed within the terms of the Insurance Intermediaries Act, to act on their behalf and subject to regulatory requirements.

IV DISPUTE RESOLUTION

i Jurisdiction and choice of law

Choice of law in contractual obligations is regulated by the Rome I Regulation.[66] The parties to an insurance contract that falls within the ambit of Article 7(3) of Rome I are given a limited choice as to which applicable law can be chosen to regulate the relationship, chosen from a list of laws provided for under the Regulation. These are the following:

a the law of any Member State where the risk is situated at the time of conclusion of the contract;

b the law of the country where the policyholder has his or her habitual residence;

c in the case of life assurance the law of the Member State of which the policyholder is a national;

d for insurance contracts covering risks limited to events occurring in one Member State other than the Member State where the risk is situated, the law of that Member State; or

e where the policyholder pursues a commercial or industrial activity or a liberal profession and the insurance contract covers two or more risks that relate to those activities and are situated in different Member States, the law of any of the

63 Ibid. Article 1009.

64 Ibid. Article 1856.

65 1857, Chapter 13 of the Laws of Malta.

66 Regulation (EC) No. 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations ('Rome I').

Member States concerned or the law of the country of habitual residence of the policyholder.

In certain circumstances contemplated under Rome I, if the Member States prefer to grant greater freedom of the choice of law applicable to the insurance contract, the parties may take advantage of that freedom.

Where the parties have not chosen the applicable law, the insurance contract will be governed by the law of the Member State where the risk is situated at the time of the conclusion of the contract. Rome I only applies to insurance contracts covering risks that are situated inside the territory of a Member State.

Provisions relating to the formal requirements required by Maltese law, whose requirements will govern the insurance contract in substance under Rome I, are also contemplated under the Civil Code.[67] These will apply in the event that Maltese law is applicable to govern the validity and effects of the insurance contract.

The Brussels I Regulation[68] regulates the jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, and has particular sections that deal with the jurisdiction for insurance contracts that are applicable in Malta. An insurer may be sued in the courts of the EU Member State where it is domiciled or of the EU Member State where the plaintiff is domiciled if the actions are brought by the policyholder, the insured or a beneficiary. In respect of liability insurance or insurance of immoveable property, the insurer may, in addition, be sued in the courts of the place where the harmful event occurred.

ii Litigation

In Malta the Code of Organisation and Civil Procedure[69] regulates the procedure relating to the institution of court proceedings by one party to an insurance contract against the other. Generally speaking, a procedure by sworn application is required to institute a case. The defendant would then have 20 days from the date of service of the claims of the plaintiff within which it may file its sworn reply. The court that has jurisdiction will subsequently order the parties to appear before it on the day appointed, in order to show cause why the claim contained in the sworn application should or should not be allowed.

An appeal against the judgment delivered by the first instance court may be entered by means of an application that is to be filed within 20 days from the date of delivery of the judgment by the first instance court.

iii Alternative dispute resolution

Apart from the possibility of instituting proceedings in court, Maltese law additionally grants the parties to an insurance contract the possibility of resorting to various forms of alternative dispute resolution. These include arbitration, mediation and conciliation.

67 Civil Code, Article 1712I.

68 Council Regulation (EC) No. 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters ('Brussels I').

69 1855, Chapter 12 of the Laws of Malta.

iv Arbitration

Arbitration is undoubtedly the most popular form of alternative dispute resolution resorted to by the parties to an insurance contract in Malta. The main advantages underlying arbitration proceedings are that the proceedings are usually cheaper and speedier.

According to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards,[70] each contracting state to the Convention shall recognise an agreement under which the parties to an insurance contract undertake to submit to arbitration of a particular country to solve any differences. Under Maltese law, arbitration is governed by the Arbitration Act[71] and the rules issued thereunder. These provide rules both for domestic and international arbitration. International arbitration is governed by the UNCITRAL Model Law implemented in the First Schedule to the Arbitration Act.

There are two types of arbitration: mandatory arbitration and voluntary arbitration. Mandatory arbitration emanates from the schedules to the Arbitration Act. An example of claims that are subject to mandatory arbitration in Malta are motor vehicle claims. On the other hand, voluntary arbitration may be resorted to if there is a clause provided for in the insurance contract or in a separate agreement. If the parties agree to the insertion of such a clause in the insurance contract or agreement, then, provided that this clause is valid in terms of the applicable law governing the contract, the parties cannot validly institute proceedings in court to seek a remedy.

In relation to the right of the parties to appeal against an award handed down by the arbitral tribunal, in the case of mandatory arbitration, the parties may appeal to the Maltese Court of Appeal in certain limited circumstances contemplated under the Arbitration Act. On the other hand, in the case of voluntary arbitration, if the parties to the insurance contract expressly excluded such a right of appeal, the decision of the arbitrator will be final and the parties will not be entitled to appeal to the Maltese Court of Appeal.

In the past the constitutionality of mandatory arbitration was the subject of controversy in a number of cases such as *H Vassallo & Sons Ltd v. AG, Water Services Corporation & Enemalta Corporation* (2011).[72] In this case the court ruled, *inter alia*, that the requirements for security of tenure were not satisfied by the arbitral tribunal and therefore the mandatory arbitration proceedings were held to be anti-constitutional. The Constitutional Court largely agreed with the judgment handed down by the first instance court and stated that if the parties do not agree to refer the dispute to arbitration access to the courts should still be available.

70 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958).

71 1998, Chapter 387 of the Laws of Malta.

72 Constitutional Court composed of Mr Justice Albert J Magri (Acting President), Mr Justice Geoffrey Valenzia and Mr Justice Tonio Mallia, 30 September 2011.

v Mediation

In Malta, mediation, both domestic and international, is governed by the Mediation Act.[73] According to the Act, mediation proceedings may be resorted to by the mediation parties in three circumstances: voluntarily, following an order by a court, or by law.

The Malta Mediation Centre provides the parties to an insurance contract where mediation is opted for by the parties with a forum where they may refer, or be referred to, in order to resolve their dispute through the assistance of a mediator. The parties, or one of them with the explicit consent of the other, may request that the content of a written agreement resulting from mediation be made enforceable subject to the provisions contemplated under the Code of Organisation and Civil Procedure.

Although Maltese law provides the parties to an insurance contract with the possibility of resorting to this form of alternative dispute resolution, in practice mediation proceedings are rarely resorted to.

vi Conciliation

Conciliation implies that the parties to a dispute may use a conciliator whose function will be to meet the parties separately in an attempt to resolve their differences. The conciliation process has no legal standing and the conciliator usually has no authority to seek evidence or call witnesses. The conciliator usually does not hand down any decision in writing and neither does he or she make an award.

Similarly to mediation, conciliation proceedings are not often resorted to in relation to insurance contracts.

V YEAR IN REVIEW

i Regulatory developments and Solvency II

As an EU Member State, Malta will be required to implement the Solvency II Directive.[74] At present there is much uncertainty regarding the planned implementation of the Solvency II Directive. While full implementation of the Directive has been postponed until 2014 (and possibly later should the implementation of the Omnibus II Directive be delayed further), the European Insurance and Occupational Pensions Authority ('EIOPA') has issued a statement confirming that certain parts of Pillars II and III of the Solvency II Directive should be implemented prior to the full implementation date of Solvency II. EIOPA has set out a 'comply or explain' procedure for all Member States in relation to the implementation of the relevant parts of the Directive.

With this in mind, the MFSA has already issued certain guidance notes and papers related to the requirements arising under Pillar II of the Directive, including papers

73 2001, Chapter 471 of the Laws of Malta.

74 Directive 2009/138/EC of the European Parliament and of the Council of 25 November 2009 on the taking up and pursuit of the business of Insurance and Reinsurance ('Solvency II').

relating to corporate governance and the risk-management function.[75] Furthermore, the MFSA has been asking insurance undertakings to carry out a calculation and examination of their minimum capital requirement and solvency capital requirement under Pillar I of the directive. The MFSA is setting out the groundwork and foundations in order to best prepare insurance undertakings and captives for the full implementation of the Solvency II Directive in due course.

ii PCCs under Solvency II

The 'three-pillar' system under the Solvency II Directive seeks to implement a risk-based approach with greater emphasis on risk management, transparency and a system where insurance undertakings are sufficiently capitalised for the risks they underwrite. While many of the 'larger' players in the market should have the necessary financial and structural resources to comply with Solvency II, some of the smaller captives may find the costs of Solvency II more demanding.

As a result, some captives or small monoline insurers may be searching for alternative structures that better satisfy their needs. The PCC could emerge as the ideal structure, which offers captives the opportunity to continue to write business through the establishment of a cell at decreased set-up and ongoing costs, and which allows them to share in the capital base of the PCC.

As the PCC is a single legal entity it is the PCC as a whole and not each individual cell that would need to satisfy the statutory minimum capital requirement under the Solvency II Directive. It is anticipated that under the Solvency II Directive each cell will be considered to be a ring-fenced fund. On this basis, while each cell would need to satisfy the solvency capital requirement, it is hoped that, provided that each cell has secondary recourse to the core, then each cell would be able to benefit from the diversification arising when calculating the solvency capital requirement for each cell under Pillar I.

Certain benefits of utilising the PCC structure also arise in terms of Pillar II. The PCC structure offers economies of scale and significant cost burden sharing, as each cell is granted access to a common pool of knowledge and expertise that arises from the common management system at the core. The enhanced corporate governance and the functions of risk management, internal auditor, actuary and compliance can be centralised and satisfied by appointments at the core of the PCC.

Since all transparency and reporting requirements arising under Pillar III can be carried out by the board of the PCC, this will result in a cost-effective structure.

Malta is the only state with full EU membership that has in place PCC legislation that allows affiliated insurance undertakings and smaller insurers to continue to write business through a cell while benefiting from the benefits of the PCC structure. This allows them to write business directly throughout the EU by means of the single passport with lower capital requirements under Pillar I, and less start-up and ongoing costs under Pillars II and III, while taking advantage of the benefits that arise under the Solvency II Directive. These captives may easily utilise a cell structure, as Maltese legislation provides

75 MFSA the System of Governance under Solvency II April 2010; MFSA System of Governance January 2012; and MFSA Risk Management Guidance Paper August 2012.

a certain amount of flexibility and allows promoters to establish a PCC either through incorporation, conversion or re-domiciliation, and allows a person to create cells within these PCCs as well as to transfer cellular assets from and to other PCCs.

VI OUTLOOK AND CONCLUSIONS

The global insurance market, and in particular the EU insurance market, are waiting in suspense for the implementation of the Solvency II Directive.

Notwithstanding the uncertainty created by the delayed implementation of the directive, there is no doubt that it will provide several benefits to the supervision of insurance and reinsurance undertakings, through a more risk-based approach for calculating capital under Pillar I, an enhanced corporate governance system under Pillar II and a greater level of transparency under Pillar III. However, the Solvency II Directive may result in higher costs for insurers, and as a result is pushing insurers to find alternative structures that provide effective solutions such as the PCC.

Reinsurance special purpose vehicles ('RSPVs') are also seen as a possible alternative structure or vehicle for insurers and affiliated insurance undertakings following the implementation of the Solvency II Directive, as the utilisation of this vehicle should result in a certain level of capital relief for such undertakings. While Malta has in place the necessary legislation in the form of the Securitisation Act,[76] which caters for traditional insurance SPVs used in transactions where a credit derivative or an equivalent contract is used to transfer risk, it is hoped that the MFSA will shortly issue the necessary regulations to cater for the RSPVs, as permitted under both the Reinsurance Directive[77] and the Solvency II Directive.

Either way, Malta has an important role to play in offering insurers, reinsurers and affiliated insurance undertakings the possibility of utilising different vehicles such as PCCs, insurance SPVs and others, which should further strengthen Malta's reputation as a flexible, innovative, yet well-regulated, domicile that offers market players various alternatives that best suit their needs.

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76 2006, Chapter 484 of the Laws of Malta.

77 Directive 2005/68/EC of the European Parliament and of the Council of 16 November 2005 on reinsurance and amending Council Directives 73/239/EEC, 92/49/EEC as well as Directives 98/78/EC and 2002/83/EC.

Appendix 1

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