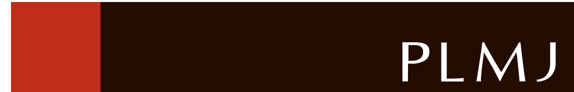
NEWSLEXTTER

RECENT DEVELOPMENTS IN THE INSURANCE LAW

May, 2008



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"Best Portuguese Law Firm of the Year" - IFLR Awards 2006 & Who's Who Legal Awards 2006

"Best Portuguese Tax Firm"- International Tax Review - Tax Awards 2006-2008

New Law On Insurance Contracts

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1. The main objective of Decree-Law 72/2008, of 16 April, which enacted the legal regime for insurance contracts, was to consolidate in one single legislative document the (special-general) law governing contracts of insurance, which had hitherto been spread out, with some overlap, among several legislative documents - a situation which made it difficult to interpret the legislation applicable to this type of contract. The new insurance contract regime also sought to settle any doubts about the application of the existing regime as well as to regulate certain matters where loopholes had been perceived to exist (e.g. the so-called group insurance).

2. The legislative effort in incorporating and consolidating the special substantive provisions that apply generally to contracts of insurance in one single piece of legislation will certainly contribute to greater security and ease in determining the respective regime and to minimising conflict in respect of some controversial issues which the existing law deals with in an insufficient or even obscure manner.

Nevertheless, from 1 January 2009 – when the new regime comes into force – we can anticipate some practical difficulties regarding the application of the transitory material law set out in the new legislation. For instance, the new law imposes on parties to non-renewable contracts of life insurance a duty to have contracts entered into under the existing law amended so that the new law will apply to them as from 1 January 2011 – different provisions apply to non-renewable contracts of non-file insurance. Since the fulfilment of the duty is conditional on agreement between the parties (it seems to disregard the interests of any beneficiaries), the question turns on which legal situation will apply to (non-renewable) contracts of life insurance if such an agreement is not reached by 1 January 2011. Will the old law remain in force or will the new law apply automatically? In the event that the answer is the latter – which may not necessarily be a straightforward conclusion – will only the mandatory provisions of the new law apply or will the subsidiary provisions be applicable too?

Given the financial features of certain contracts of "insurance", the Government has also though that it would be more adequate not to provide a definition of contract of insurance, opting instead to set out the typical duties inherent to such a contract. It is an understandable solution and allows, as the Government also states, for jurisprudential and doctrinal development of the concept through the approximation of the "atypical" figures to the duties typically associated with a contract of insurance. It remains to be seen whether it might not have been convenient expressly to provide in the new law for some cases of negative definition such as, for example, credit derivatives - an instrument with an obvious structural and functional resemblance to credit insurance, which is listed in the *Código dos Valores Mobiliários* (Securities Code) as one of the financial instruments that falls under CMVM supervision.

3. The publication of the new insurance contract regime has provided the PLMJ Multidisciplinary Insurance Team with the perfect opportunity to provide clients and colleague alike with some preliminary thoughts on some of the developments introduced by the new law as well as on other themes related to recent domestic and community law developments applicable to the insurance industry.

The first theme in this Newsletter will look at the issue of unauthorised companies entering into insurance contracts in respect of which the Government, in order to protect the insured person, seeks to restrict

the general consequences of a lack of legal capacity by limiting the possibility of the unauthorised "insurance company" pleading that the contract was void. Protection of insurance consumers is effectively one of the concerns underlying the new insurance contract law and we will discuss some of the fundamental issues where parliament has sought to bridge the gap between the general insurance contract regime and consumers' law. We will also examine the amendments to the regime on initial representations/statements for the purpose of determining/accepting the risk as well as the implications of supervening alterations to the risk covered.

It is also an opportune moment to discuss the new issues generated by the CMVM being allocated supervision of the conduct of business rules applicable to unit linked policies and pension funds and to air some of the doubts regarding the scope of this supervision and its concurrent functioning with Portuguese Insurance Institute supervision of the same products. In addition, the economic and monetary integration in the Eurozone and the progressive harmonisation undertaken via Community law allows insurance companies authorised in other Member States to engage in insurance activities in Portugal under the "passport", but also imposes a special regard for Community law. In this respect, we would like to highlight the public consultation process launched by the European Commission concerning the Insurance Block Exemption Regulation applicable to the insurance sector, and examine the tax regime for community insurance companies that carry on business in Portugal under the freedom to provide services.

Other issues could also be broached, such as the (new) acceptance of the validity of the so-called claims-made provisions (as opposed to occurrence provisions) in civil liability insurance: in other words, the cover period in civil liability insurance could also be defined by taking into account the date of submission of the claim and not only the date of the occurrence giving rise to liability. The coordination of this type of clause with the rule for deeming void contracts that cover claims losses occurring prior to entry into force of the contract of insurance as well as with the regime applicable to insurance for legal expenses, which should be associated with this type of insurance cover, is unclear and may give rise to doubts as to its interpretation and application. From the point of view of insurance companies, a civil liability insurance on a claim-made basis will require an especially careful risk assessment, given the difficulty in identifying and quantifying occurrences giving rise to a loss which took place in the past (a question that the insurance companies can only deal with by inserting retroactivity clauses, in other words, establishing that the insurance will only cover civil liability claims arising after a certain date in the past).

Although it is impossible to discuss all the legislative news, with the publication of this Newsletter, the PLMJ Multidisciplinary Insurance Team hopes to contribute to the discussion and dissemination of the new insurance contract regime to all interested parties.

The Pursuit Of Insurance Activities By Unauthorised Entities

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One of the guiding principles of the new insurance contract regime is to reinforce protection for the policyholder and the insured party, as the weaker contractual party, without neglecting to provide due consideration for the interests of the insurance companies.

This is the perspective from which to view the provisions of article 16 of Decree-Law 72/2008 of 16 April, which takes on greater importance since it is included in the general part of the legislation and is thus applicable to insurance contracts in general. The article in question provides that the (intended) insurance contracts made by non-insurers or in general by entities that are not legally authorised to do so will be void.

Parliament also took care to complement this provision with an additional provision aimed at safeguarding the interests and the expectations of the insuring party who took out the insurance policy with the unauthorised entity. In fact, parliament has also established that the void contract does not excuse the person who agreed to cover the other's risk from compliance with the obligations arising to it out of the contract or the law if the transaction was valid, unless the counterpart (the policyholder or the insured party) acted in bad faith. In essence, parliament states that the fact of the contract being void should not operate to the disadvantage of the policyholder, and the alleged insurer will remain bound by all the duties and obligations arising to it under the contract or the law as if the contract were valid.

We can also list briefly some of the main consequences and/or objectives associated with the entry into force of this provision:

- Ease some of the rigidness of the civil invalidity law, seeking to safeguard the interests of the theoretically weaker party, i.e. the policyholder.

- Adapt the legal regime on insurance contract to the reality of the insurance industry, which is increasingly less restricted to the boundaries of the Portuguese State and has an ever larger number of agents (national and foreign) and, consequently, a greater likelihood that unauthorised agents could operate in the market and avoid the scrutiny of the ISP.

- Govern situations where insurance contracts are entered into by: (i) companies whose objects have no relation to the insurance industry; (ii) insurance companies which operate in the Portuguese market but whose business activity is not duly registered with the ISP and; (iii) companies that are authorised to carry out acts which are, from an operational point of view, similar or even identical in nature to those of the insurance sector, but which in certain situations may exceed the limits of their licences.

It must be borne in mind that the interpretation of this provision (and of the generality of Decree-Law 72/2008) will always entail a simultaneous analysis of Decree-Law 94-B/98 of 17 April, in that the latter governs the conditions of access to and pursuit of the insurance and reinsurance industry in European Union territory, notably article 7 which stipulates the entities authorised to carry on insurance activities in Portugal.

In this respect, Article 16 of Decree-Law 72/2008 of 16 April complements Article 202 of Decree-Law 94-B/98, in that the latter provides for a term of imprisonment of up to three years for those who engage in insurance, reinsurance, or pension fund management acts or operations, on their own account or on behalf of another, without the necessary licence, while the treatment that will apply to the (void) contracts entered into by these offenders has now been established.

Another interesting parallel is that established between the regime enacted by Decree-Law 72/2008 for the pursuit of the insurance industry by an unauthorised entity and that stipulated by Decree-Law 94-B/98 for the marketing of insurance policies not registered with the ISP (applicable to compulsory branches or types of insurance), or where amendments to general and/or special conditions clauses have not been approved by the ISP. In this situation, if the insurance companies fail to issue or amend their policies as requested by the ISP, their records will be cancelled although the policies will remain in force until the term of the corresponding contract, so as to safeguard the interests of the policyholder and insured party under these policies.

Consumer Protection Under The New Legal Regime On Insurance Contracts: General Duties Of Information

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The Preamble to Decree-Law 72/2008, of 16 April states that the reform of the legal regime on insurance contracts enacted by said decree-law was guided by *"(…) the safeguard of the insuring and the insured parties – as the contractually weaker party -, without neglecting due consideration for the insurance companies."*

In this discussion, we must naturally have regard to the provisions which, enshrined in the new regime, aim to implement the principle underlying the first half of this equation, although in a more restricted perspective: that of the insuring party/consumer, as the (even) weaker party in the insurance contract relationship.

From the outset, article 3 of the above-mentioned decree-law provides that the respective legal regime will not affect the application, to the insurance contract, of the legislative provisions on (i) general contract clauses, (ii) consumer protection and (iii) distance contracts, reaffirming the special – and prevailing – nature of this legislation over the rules applicable to insurance contracts.

In combining the legal regime on insurance contracts with consumer protection laws, special attention is merited by the general duties of information incumbent on the insurer, which have for the first time been systemised and standardised by means of specific provisions that apply across the gamut of insurance contracts, until now only applying in a less regulated manner to Life assurance products (and to personal accident and long-term illness contracts in the Non-Life branch).

Thus, the general duties of information of the insurer vis-à-vis the insuring party are now provided for in articles 18 to 23 of the legal regime on insurance contracts, and include duties (i) of clarification and information prior to the execution of the insurance contract, and (ii) of communication of the general, special and particular conditions of the insurance policy, being an expression, in the field of insurance contracts, of the duty of utmost good faith in entering into the contracts, provided for in article 227 of the Civil Code.

Such duties take on a still more important role in the field of consumer law, in homage to the principle that the consumer's decision to contract for goods and services must necessarily be informed and duly considered. It is the Consumer Protection Law (CPL) itself that enshrines the right to information as a fundamental right of the consumer.

The general contractual clauses regime enacted by Decree-Law 446/85, of 25 October, as amended (*GCCR*), applies to insurance contracts which, as a rule, have non-negotiated contract clauses, and imposes duties of communication on the proposing insurer – they must be adequate and provided in sufficient time to make full and effective knowledge possible – and duties of information – which in turn include duties of explanation and clarification.

Still in this field, we must consider Decree-Law 57/2008, of 26 March, which sets out the legal regime applicable to unfair competition practices by companies in the course of their business with consumers, deeming as such misleading acts and omissions and aggressive commercial practices. As regards misleading practices, there is obvious parliamentary concern since it deems unlawful the conduct of companies who convey inaccurate information or which omit, conceal or present in an unclear, unintelligible or untimely manner information deemed capable of influencing the decision to carry out the transaction.

Another legislative instrument of relevance in this matter is Decree-Law 95/2006, of 29 May which governs pre-contractual information and contracts for financial services (insurance services) provided to consumers by distance marketing, and under the terms of which consumers are entitled to have certain information, described in detail in articles 13 to 16 thereof, provided in good time and prior to being bound by an offer or contract regarding (i) the service provider/insurer, (ii) the financial/insurance service, (iii) the contract and (iv) the protection mechanisms.

In fact, it is the legal regime on insurance contracts itself that states that when the insurance contract is a distance marketing contract, the compulsory information associated with this type of contract must be reinforced by the information imposed by the above legislation.

The legal provision on matters of general duties of information in consumer relations and in the insurance contract having been summarised, and in view of the large number of applicable regimes, we will seek to anticipate how the legal effects of any breach will be dealt with, since:

(i) The legal regime on insurance contracts establishes the civil liability of the insurer and confers upon the insuring party the right to freely terminate the contract (which must not be confused with the right to withdraw) which must be exercised within 30 days of receipt of the policy, has retrospective effect and confers on the insuring party the right to demand the refund of the total amount of premiums paid;

(ii) The CPL confers a right to withdraw – it would be more accurate to call it termination – on the consumer whenever there has been a lack of information or insufficient, illegible or ambiguous information, which compromises the appropriate use of the goods or services, simultaneously reaffirming civil liability and broadening it in such a way as to institute a principle of solidarity between all the actors in the "production to distribution chain";

(iii) The GCCR considers general contract clauses that were not duly communicated and in good time to the adhering party to be void, and therefore excluded from the affected

individual contracts, and provides for the clauses to be severed, or where this is not possible, deems the contract itself to be void;

(iv) The legislation on unfair commercial practices provides that contracts entered into as a result of misleading practices are invalid and annullable at the request of the consumer (atypical invalidity) who can choose to have such a contract modified in accordance with equitable principles or sever the offending clauses, stipulating in any event the right of any consumer harmed by this type of practice to claim damages;

(v) The legislation on the distance marketing of financial services provides that the breach of such duties constitutes an administrative offence punishable by a fine of between €2,500 and €1,500,000 when committed by companies), while additional penalties may also be imposed, such as the prohibition on engaging in the profession or activity for a period of up to 3 years, the prohibition on holding public positions and administrative functions, engaging in the management or supervision companies for a period of up to 3 years or publication of the definitive penalty in a top-selling newspaper.

It should be noted that under the general terms governing the access to and pursuit of the insurance and reinsurance activity, breach of the duties of information to the insuring parties constitutes a minor administrative offence, punishable by a fine of between €748.20 and €74,819.68 in the case of companies, and additional penalties may also be imposed on the offender, such as the total or partial prohibition on entering into new contracts with insuring or insured parties, of the type, product or operation that the administrative offence concerns for a period of up to three years, or full or total prohibition on entering into new contracts of the type, product or operation that the administrative offence concerned for a period of between six months and three years.

As a result, a breach of the general duties of information by the insurer could give rise to:

A. the insurer's liability for an administrative offence (liable to a fine and additional penalties);

B. the insurer's civil liability vis-à-vis the insuring party, which includes:

(i) the insuring party's right to claim compensation for damages arising from the breach, and

(ii) the insuring party's right to exercise one of the following rights:

I – terminate the insurance contract;

II – demand that the void clauses be eliminated from the contract or demand that the contract itself be declared void.

As regards the annulment of the contract, which is allowed under the unfair competition practices regime, this seems to be subsidiary in nature as it states that the respective regime *"shall not adversely affect the application of more demanding regimes related (…) to the financial services"* and that *"it shall not affect the [legal?] provisions governing the formation, validity and effects of the contracts".*

It is not, however, clarified whether any type of hierarchy applies to these remedies or whether the insuring party/consumer is free to choose the regime they consider most appropriate, bearing in mind the provisions that best safeguard their interests in each case, but at the same time within the limits imposed by good faith in the exercise of their rights.

In conclusion, while recognising the merit of broadening the scope of application of the general duties of information to all insurance contracts, in cases where the insuring party is a consumer, the legislative technique used could be improved, at least in respect of the penalty regime applicable to the breach: instead of resorting to open-ended referral clauses, it would have been better for all – particularly the insurers and the insuring party/consumer – if parliament had clearly listed and linked all the potential penalties associated with such a breach.

INITIAL DECLARATION OF RISK

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The new legal regime for insurance contracts dedicates one sub-section, more precisely articles 24 to 26, to the *duties of information of the insuring and the insured party.* This is due to the importance attached to this matter, which has been the focus of intense judicial discussion, since breach of the above-mentioned duties of information in respect of the risk to be insured against can bring about the cancellation of the insurance contract and the subsequent non-liability of the insurer for any damage that may have occurred.

It is worth taking another look at the previous regime governing this matter. Under Article 429 of the Commercial Code, any inaccurate declaration, as well as the withholding of any facts or circumstances known to the insured or the insuring party, will render the insurance contract void. Doctrine and jurisprudence have repeatedly held the vitiating factor in question to be not that the contract is void but that it is voidable, grounding this view on: (i) the imprecise terminology of the Commercial Code which failed to distinguish between the vitiating factors, (ii) the particular nature of the interests at stake and (iii) the non-existence of breach of any compulsory provision. Along with this general provision, jurisprudence has also tempered this regime by requiring the insurer to demonstrate that had it known of the actual or omitted fact, it would not have entered into the insurance contract or would have done so under different conditions .

The new regime will give voice to this jurisprudential trend and introduce some new provisions. Firstly, the regime imposes an obligation on the insuring or insured party to disclose all the circumstances of which they are aware and which are significant for the insurer to assess the risk, even if the fact to be disclosed is not covered on a questionnaire provided to the latter for the purposes of the insurance. Conversely, the insurer has a duty to inform its future customer about the duties of disclosure to which we have referred and the consequences of a failure to comply therewith, or run the risk of incurring civil liability under the general law.

Another new addition is the differentiation of the consequences of breach of the obligation to disclose, by the insuring or insured party, according to the degree of fault. If the breach is wilful, the insurer

1
e.g. Moitinho de Almeida, O Contrato de Seguro *(The Insurance Contract)*, p. 61, footnote 29; José Vasques, Contrato de Seguro *(Insurance Contracts)*, p. 379; Supreme Court Ruling 3-3-98, Supreme Court Ruling Collection VI, 1º, 103; Supreme Court Ruling 10-5-01, Supreme Court Ruling Collection IX, 2º, 60; Supreme Court Ruling 4-3-04, Supreme Court Ruling Collection XII, 1º, 102.

2
Supreme Court Ruling 4-10-1990, BMJ 400, 672, Lisbon Appeal Court Ruling 28-2-91, Judicial Collection 1991, I, 172, among others. See also Calvão da Silva in RLJ 133, 221.

may annul the contract by means of a declaration sent to the insuring party within three months of the date on which it became aware of the breach of the duty, and is not obliged to cover any claims lodged prior to it acquiring this knowledge and during the three-month period . In the event of negligent breach, the insurer may terminate the contract if it demonstrates, within the same three-month period, that under no circumstances does it enter into insurance contracts where the initially omitted or inaccurate fact has been declared. If this is not the case, it should propose to amend the contract and set a reply/acceptance period of not less than 14 days.

3
Retaining its right to the premium due until the end of the three-month period, unless it contributed knowingly or in a grossly negligent manner to the breach of the duties of declaration of the insuring or insured party (Cf. Article 25 of the Insurance Contract Legal Regime).
4
Cf. Article 26 of the Insurance Contract Legal Regime

Any claim during this period whose occurrence or consequences have been influenced by the omitted or inaccurately declared fact will signify (i) non-liability of the insurer when it is able to demonstrate that it would not otherwise have entered into the insurance contract or (ii) coverage of the claim in proportion to the difference between the premium paid and that which would have been paid had the disclosure duties of the insuring or insured party been fulfilled. In conclusion, in comparison to the former law and consolidated jurisprudence, it is clear that the new regime will aggravate the consequences of breach in cases where the insuring or insured parties act wilfully and mitigate them when it occurs through negligence, by allowing the insurer to provide proportional cover.

CMVM With Jurisdiction To Supervise Unit-linked Insurance And Pension Funds

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The insurance and pension funds linked to investment schemes, also known as structured savings instruments (*Instrumentos de Captação de Aforro Estruturados (ICAE)*, are products that can be included in the insurance sector yet have particular features which are typical of investment products. In effect, ICAEs are primarily insurance or pension funds covering typical life risks, which can only be provided by insurance companies. Yet ICAEs are also based on investment goals, in that insurance companies make a separate investment of the assets that are given to them by the customers in subscribing to financial instruments, such as shares, bonds, investment fund participation units, etc, the value of the ICAEs varying according to the development of the assets that comprise the associated investment portfolio.

Until recently, the Portuguese Insurance Regulator (the ISP) was the only supervisory body with jurisdiction to regulate and supervise insurance companies that market this type of product in Portugal.

Although the allocation of powers to this regulatory body was justified for a prudential supervision of the insurance companies involved (the need for the creation of technical provisions, maintenance of the solvency ratio, participation in guarantee funds, etc), the regulation of the ICAEs' financial component was more connected with the supervision of investment products (imposition of duties of information regarding the performance and volatility of the investment portfolio, respective certification by auditors, etc) for which the Portuguese Securities Market Authority (the CMVM) – as the competent authority for supervising these products – might be better prepared than the ISP.

In consideration of the mixed nature of the ICAEs - insurance with characteristics of investment products - amendments were introduced at a legislative and regulatory level so that jurisdiction for supervising the ICAEs would be divided between the ISP and the CMVM by means of the publication of Decree-Law 357-A/2007, followed by Regulation 8/2007 of the CMVM (and the consequent revocation of the corresponding Regulatory Rule 5-2004-R of the ISP). Thus, while the ISP retains its powers to carry on prudential supervision and, in relation to certain issues pertaining to the supervision of the conduct of insurance companies, the CMVM has been allocated powers to establish pre- and post-contractual duties of information in respect of ICAEs.

A comparison of Regulation 8/2007 with Regulatory Rule 5-2004-R of the ISP shows that the requirement to provide an information prospectus to customers subscribing to ICAEs, prepared on the basis of a draft attached to the Regulation, has been retained, as has the provision on the duty to provide, in advertising materials, information such as on the risk of losing the investment as well as various details about the performance of the ICAEs, which should be calculated according to the formulae set out therein.

However, the new Regulation has brought some new developments. Operators are now required to provide advance communication of the information prospectuses and advertising material to the CMVM, which will maintain a public record of these prospectuses on its official site so that they can be examined by the customers. The information prospectus will also contain the figures for the overall costs and average rotation of the portfolio, calculated according to new formulae. It also sets out a duty for the operators to ensure that each ICAE is suitable for the personal circumstances of the customer, which has possibly been inspired by the appropriateness test foreseen in Article 19(5) of the Markets in Financial Instruments Directive (MiFID). Finally, it is also worth mentioning the referral from this Regulation to the exhaustive rule on Internet marketing set out in CMVM Regulation 2/2007 on financial intermediation.

Although the new Regulation is generally more demanding than the previous one, the CMVM has provided a more flexible regime for operators in certain matters: it will for example no longer be compulsory to send monthly and yearly detailed reports to the customers, just a quarterly report with brief information on the nature and value of the investment associated with the ICAE. Furthermore, while the ISP Regulation required the use of Portuguese in the prospectus, operators may now use English instead, subject to the approval of the CMVM, when it considers the interests of the investors to be safeguarded.

It is still too early to draw any definitive conclusions as to the merits of this reform in the legislative and regulatory provisions applicable to ICAEs. Nevertheless, it could be argued that the allocation of certain powers to the CMVM to supervise compliance with duties of information in respect of these products would appear to be opportune, since this particular regulatory body is better prepared to monitor the financial component of the ICAEs. It is not, however, clear whether the ISP has retained the jurisdiction to supervise certain matters concerning the

conduct of operators not provided for in the CMVM Regulation, in particular compliance with duties of information unrelated to the financial component of the product, set out in the general legislation that applies to insurance, such as for example the duties of information set forth in article 18 and thereafter of the new insurance contract regime envisaged in Decree-Law 72/2008, of 26 April.

It is also possible to confirm that the exhaustive regulation of these products has been maintained and, as has been demonstrated, actually increased by the new CMVM Regulation. While this path ensures greater protection for the interests of the customers, it may have the negative effect of limiting the freedom of operators to develop innovative products, and throw up obstacles to the marketing of ICAEs in Portugal by foreign operators, which will have difficulty in adapting their products to the demands of Portuguese legislation in matters that have still not been harmonised at community level.

European Commission Launches Consultation On The Functioning Of The Insurance Block Exemption Regulation

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The European Commission launched a public consultation process on 17 April regarding the functioning of Regulation No. 358/2003 – the Insurance Block Exemption Regulation (hereinafter "BER") applicable to the insurance sector.

THE BER provides for the automatic exemption of the prohibition of the commercial practices set out in Article 81(1) of the EC Treaty, particularly cooperation agreements between insurance companies. The consultation process may result in the renewal, amendment or repeal of the BER in March 2010, when its term ends.

The BER establishes a "safe haven" regime for insurance companies and an automatic exemption for certain types of cooperation agreements (subject to the fulfilment of certain conditions), particularly:

- Joint calculations and studies aimed at determining, among other things, the cost of covering a given risk, the frequency of illness, accidents and disability and the frequency or size of future indemnity claims for certain risks;
- The joint establishment and distribution of non-binding direct insurance policies;
- The joint establishment and management of insurance pools;
- Tests and joint acceptance of security devices.

In June 2005, the European Commission launched a Sector Inquiry into the insurance sector under Article 17 of Regulation No. 1/2003. At the time, the majority of the participants in the inquiry decided in favour of renewing the BER, fearing that its repeal would increase the costs of compliance with legal rules and deprive companies from legal security. Nevertheless, the European Commission noted that the majority of the participants' replies failed to distinguish between the need for the types of cooperation provided for in the BER and the need for the BER itself.

In this respect, and still without having reached a final conclusion, the European Commission noted in the conclusions of the above-mentioned inquiry that it could see no overwhelming reasons to renew the BER.

Under the terms of the BER itself, the European Commission should now, at the end of the public consultation process, prepare and deliver its report on the functioning of the BER to the European Parliament and the Council by March 2009.

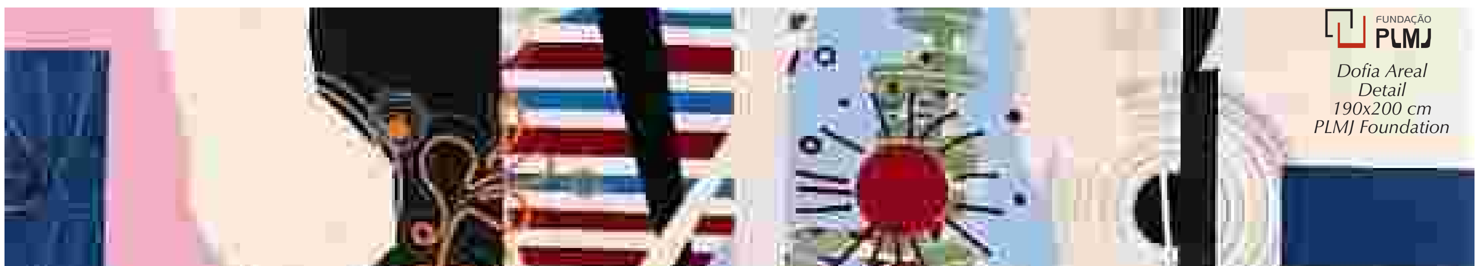
With a view to the preparation of the above-mentioned report, the European Commission intends, through the current consultation, to obtain contributions from economic operators on questions such as:

- If the BER is being used, where and why;
- If business risks and other factors make the insurance sector different from other sectors that operate without a BER;
- If the BER creates anti-competitive effects capable of affecting consumers (such as higher prices or reduced offer of certain types of insurance); and
- If the repeal of the BER would result in a greater administrative burden for the competent competition authorities and greater difficulty in applying competition law.

The essential agreement types are the subject of specific questions on the part of the Commission, as follows:

- Joint calculations and studies: are there alternative solutions to overcome the asymmetrical information problems that the insurance sector is faced with?;
- Standard policy conditions and models: does cooperation in standard policy condition matters affect the existence of a variety of policies and favour the use of restrictive terms in policies?
- Common coverage for certain types of risks (pools): do the current provisions of the BER adequately define pro-competitive pools? Would the BER impede the establishment of pools based on innovative policies? Would the BER impede the establishment of cross-border pools?
- Safety mechanism: does the BER create competition problems related to the production, appraisal, installation and maintenance of safety mechanisms?

The Commission has invited interested parties to present their responses to the public consultation no later than 17 July 2008.



*Dofia Areal
Detail
190x200 cm
PLMJ Foundation*

Freedom to provide insurance services (Tax implications for Portugal)

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A) Introduction

In the field of insurance activities, the freedom to provide services (FPS) signifies that an insurance company with a permanent (registered office) or secondary establishment (branch office, subsidiary or permanent office) in a Community Member State (Member State of establishment) can cover, from this establishment, risk situated in the territory of other Member States (Member States where the services are provided). Similarly to the remaining questions related to the choice of law governing the contract, the implementation of the FPS on a community level implies, as a basis for its enforceability, a need to establish a minimum level of harmonisation in respect of the tax burden levied on insurance premiums falling within the scope of this regime.

With the possible options being taxation by the Member State of the establishment or by the Member State where the services are provided, the community lawmakers have opted for the latter, establishing the rule that insurance contracts entered into under the freedom to provide services (similarly to those entered into under the freedom of establishment principle) would be liable to the tax and non-tax charges levied on insurance premiums in the Member State where the risk is situated or the commitment undertaken, according to whether the insurance involves "Life" or "Non-Life" products. With the definition of this principle and the stable community harmonisation on Value-Added Tax (VAT), one of the main tax obstacles to implementing the internal market in the insurance sector has been removed, and now only the broader issue of income taxation harmonisation, which traverses various sectors of economic activity, remains to be settled.

We intend to provide a brief description of the main taxes and non-tax charges to be taken into account by insurance companies established in another Member State when calculating risk cover in Portugal and the additional obligations arising therefrom.

B) Direct taxation

As mentioned above, income taxation has not yet been the subject of community harmonisation and is perhaps the area where the biggest tax obstacles to the implementation of the principle of free movement of persons and capital are located.

With regard to Corporation Tax (IRC), the tax treatment for companies and other entities that do not have a registered office or effective control in Portugal varies according to whether such entities have a permanent establishment (PE) to which the income can be attributed or otherwise. If they have a PE in Portugal, they are taxed at the general 25% rate on the profit attributable to the establishment; if they do not have a PE, they are taxed only on the income deemed to have derived from national territory, generally speaking by means of definitive withholding taxes.

From the outset, bearing in mind the definition provided by both domestic law and by the Conventions for the Avoidance of Double Taxation entered into by Portugal, it could be argued that the mere exercise of an activity under the FPS principle does not establish the existence of a PE in Portugal, insofar as such an activity does not assume the existence of "dependent agents" with powers to contract on behalf of the insurance company. Likewise, the mere appointment of a representative for the purposes of complying with obligations related to the assessment and passing on of taxes and charges levied on insurance related to risks situated in Portugal does not, in itself, establish the existence of a PE.

Although not directly relevant to the taxation levied on insurance companies, we must draw attention to another aspect of income taxation that can have an indirect influence on the insurance activity exercised under the FPS principle. We refer of course to the fact that most tax benefits associated with insurance and financial applications are conditional by law upon the existence of a more or less strict connection with the Portuguese legal order (whether by the requirements for the establishment in Portugal of the entities with which these are held, by compulsory compliance with national legislation, or because of the compulsory composition of the assets of the Funds associated with the financial applications.). Additionally, although the Portuguese government has taken some tentative steps with a view to suppressing some of the discriminatory treatment provisions against non-resident agents (an example of this in the insurance sector is the extension of costs incurred with contributions to pension funds deductible against IRC to contributions made to pension plans run by community insurance companies), this is an area which is still strewn with obstacles to full competition by non-resident insurance companies in the national market.

C) Indirect taxation

Similarly to the case with the remaining member States of the European Community, insurance and reinsurance transactions are exempt from Value-Added Tax (VAT) and there are no other particularities worthy of mention.

Although exempt from VAT, the insurance industry is liable to stamp duty, which is levied on the amount of the insurance premiums, the costs of the policy and on any other amounts that constitute income for the insurance activity; at variable rates according to the branch that the policy in question covers. Premiums received for reinsurance underwritten by companies operating legally in Portugal and the premiums and commission related to the "Life" branch of insurance are exempt from stamp duty.

As stamp duty legally falls on the person taking out the insurance (and is therefore included in the cost of the policy), it is the insurance companies that have the duty to assess and pass on this tax to the state coffers. For this purpose, insurance companies not resident in Portugal who carry on activity under the FPS principle must appoint a representative in Portugal to ensure, on its behalf, compliance with these obligations.

D) Non-tax charges

Apart from the stamp duty on the policy, Portuguese law also provides for a wide range of non-tax charges aimed at financing public services and funds, levied on the income from the insurance business, which also affect the activity carried out under the FPS, as follows:

- The Portuguese Insurance Institute (*Instituto de Seguros de Portugal* (ISP)) charge levied on the annual revenue of insurance companies;

- The contribution to the National Medical Emergency Institute (*Instituto Nacional de Emergência Médica* (INEM)) levied on the premiums of some types of life assurance contracts, in the case of death, as well as on illness, accident and land vehicle contracts;
- The levy in favour of the Automobile Guarantee Fund (*Fundo da Garantia Automóvel*) charged on the commercial premiums of compulsory civil liability automobile insurance cover;
- The levy in favour of the Occupational Accidents' Fund (*Fundo dos Acidentes de Trabalho*) charged on the value of the insured salaries in the occupational accidents branch of insurance, on the principal of pension refunds and on the value of the accounting provision for supplementary payments in respect of third party assistance, payable on 31 December;
- The levy in favour of the National Civil Defence Authority (former National Fire Brigade Service) charged on fire insurance, transport of hazardous goods, including cargo insurance, vehicles destined for this type of transport and agricultural and fishing premiums.

E) Obligation to appoint a representative

As a corollary of the rule subjecting the insurance contract to the tax regime of the Member State where the service is provided, Portuguese law on the access to and pursuit of the insurance and reinsurance activities establishes that insurance companies operating in Portugal under the principle of freedom of provision of services, prior to commencing their activity, should appoint a representative by means of a power of attorney conferring sufficient powers, who is normally resident in Portugal and who is jointly and severally liable for the payment of indirect taxes and charges levied on contract premiums that the company enters into in respect of risks located here. For the purposes of monitoring these obligations, the representative is also obliged to comply with some registration obligations in respect of such contracts.

New Rules On Loan Contract-associated Life Assurance Covering Death, Disability Or Unemployment

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On 24 April last, the Portuguese Insurance Institute approved Regulatory Rule 6/2008-R, which establishes a set of rules applicable to the information given to customers and the calculation of the amount of cover and premiums due under the individual or contributory group life assurance contracts that include the cover against risk of death, disability or unemployment associated with loan contracts. The rule will come into force 90 days after publication in the official journal *Diário da República*.

Under this Rule, the following information must be included in the insurance contracts which fall within its scope, as well as in all information provided to the customers prior to finalising the contracts:

(i If there is a ratio between the principal insured and the principal outstanding on the loan contract with which it is associated and, if so, how this ratio develops throughout the respective period up to the date of maturity stipulated in the contract with the longest term;
(ii) The ratio existing between the premium and the amount of insured principal for each cover throughout the duration of the contract, specifying the applicable premium regime;
(iii) In the case of insurance contracts that include cover where the value of the insured principal is determined on the basis of the outstanding principal in the associated loan contract, the criteria for adjusting the respective premium, namely whether the adjustment operates to change the insured principal automatically and immediately or on the anniversary thereof or on the date of renewal of the insurance contract;
(iv) Criteria for identifying the beneficiaries, as well as the criteria for distributing the insured principal that is payable in the case of a claim, and for participating in the results that may be attributable during the term of the contract.

In relation to the bases for calculating the insurance premiums, the contracts must now explain whether these remain constant throughout the duration of the contract or whether they are subject to periodic review, in which case the criteria for determining the new calculation bases and the corresponding review periods must be explained.

Insurance contracts subject to this regulatory rule which include cover where the insured principal is calculated on the basis of the principal outstanding on the associated loan contract should provide that the adjustment of the outstanding principal results in an adjustment of the premium to the new outstanding principal, which could effect the change to the insured principal automatically and immediately or on the date of the anniversary thereof or renewal of the insurance contract.

In relation to the methods followed for communicating the new figures for the outstanding principal, the regulatory provisions provide two alternatives:

(i) When part of the same business group as the credit-lending institutions, insurance companies must take the appropriate steps to ensure that the former make any information relating to changes in the outstanding principal of the loan contracts in question available to them in good time;
(ii) In the remaining cases, the insuring parties must convey the information to the insurance companies in advance.

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