

THE INSURANCE AND
REINSURANCE
LAW REVIEW

SIXTH EDITION

Editor
Peter Rogan

THE LAWREVIEWS

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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 play an important role in the world economy. It is an increasingly global industry, with emerging markets in Asia and Latin America developing apace.

Given the expanding reach of the industry, there is a need for a source of reference that analyses recent developments in the key jurisdictions on a comparative 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.

Looking back on the past year, 2017 is likely to be one of the costliest years in the history of the global insurance industry. Market estimates suggest that the final bill for the hurricane trio of Harvey, Irma and Maria, together with other natural catastrophes including a severe earthquake in Mexico, will come to US\$135 billion. Overall losses (including uninsured losses) are likely to amount to US\$330 billion, which would be the second highest ever recorded for natural disasters (topped only by 2011, which saw the Tohoku earthquake in Japan). It is estimated that the US share of losses in 2017 will be larger than usual: 50 per cent compared with the long-term average of 32 per cent. In Europe, a late frost after a long warm period in spring caused billions of dollars' worth of damage to crops while, tragically, some 2,700 people lost their lives following an extremely severe monsoon in South Asia.

Events such as these test not only insurers and reinsurers but also the rigour of the law. Insurance and reinsurance disputes provide a never-ending array of complex legal issues and new points for the courts and arbitral tribunals to consider. I hope that you find this sixth edition of *The Insurance and Reinsurance Law Review* of use in seeking to understand them and I would like once again to thank all the contributors.

Peter Rogan

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April 2018

MEXICO

*Yves Hayaux-du-Tilly*¹

I INTRODUCTION

The new Insurance and Surety Companies Law (LISF) became effective in 2015, and the quantitative elements of Solvency II on calculation of solvency capital and provisions on balancing the economy were implemented in 2016. Notwithstanding the foregoing, the regulatory framework of the new LISF continues to be adjusted and in certain cases continues to lag behind in terms of regulations required to implement some of the reforms introduced with such new LISF, such as the surety insurance line of business.

The market currently operates under this new framework set forth by the new LISF and its regulations. Solvency II standards are being implemented in accordance with the LISF and applicable regulation, causing uncertainty and requiring insurance companies to adjust and bear the cost and effects of such standards in their operations. The foregoing has required continuous adjustments, negotiations with regulators and revisions to business plans, since the effects of the new framework continue to test the market, adding costs to the operation of insurance companies, reducing margins and creating regulatory and consolidation pressure. Unfortunately, the new LISF has not been proven to improve insurance penetration in Mexico, nor financial inclusion.

The effects of Solvency II standards have required that companies redefine certain strategies to mitigate the rise in regulatory and operational costs, requiring complex regulatory and strategic advice.

The challenges of the regulator continue to be important as the National Insurance and Bonding Commission (CNSF) continues to be overwhelmed by its multiple obligations as the main regulatory authority under the LISF. The lack of additional resources to cope with the added regulatory burden, combined with a complex regulatory regime, has resulted in delays in the proceedings and applications filed with the CNSF, seriously affecting the market and creating inefficiencies. The effect of the new legal framework that requires approval by the governing board of the CNSF on certain matters implies that such matters may only be approved in meetings of the board that convenes every quarter or every other month and, therefore, if an item is not included in the agenda for the following governing board meeting, the matter risks being delayed by a quarter with the consequences this entails for the business. It is now critical that additional budget is allocated to the CNSF to build its capacity to respond in a timely fashion to the needs of the industry.

¹ Yves Hayaux-du-Tilly is a partner at Nader, Hayaux & Goebel. The author is grateful to Juan Pablo Sainz of Nader, Hayaux & Goebel for his assistance in preparing this chapter.

Despite Mexico being the second-largest Latin American market with an advanced regulatory regime, the lack of penetration continues to be a cause of concern, as well as a magnet for potential opportunities, notwithstanding the fact that such 'potential' has been mentioned as a factor to target the Mexican market for the past 25 years and has yet to deliver.

The complexity of new risks and the increase in additional lines of business that are capital intensive or require added capacity have increased the use of reinsurance to cope with the ongoing concerns in underwriting and capacity, and a system that permits 'fronting' activities has mainly been relying on reinsurance to grow and face these new risks and challenges, rather than developing its local capacity. The legal framework and the new LISF just maintain the regime in place, and there are no indications of changes to the regime going forward.

The high reliance on reinsurance with a system based on fronting arrangements creates enormous challenges when adjusting and settling certain claims. Recent trends in the Mexican market have translated into a malaise within the Mexican insurance market with foreign reinsurers, regarding the manner in which claims are being handled and resolved. There is growing concern from certain reinsurers and markets and their respective advisers regarding measures that are considered to be abusive in their use of the claims control clause. Such problems are typical of fronting arrangements. There are ongoing conversations with reinsurance markets to explore the manner in which the reinsurance market may change its current practices affecting the long-standing working relationship between cedants and reinsurers.

We have seen a steady increase in M&A activity, driven mostly by international transactions with effects on the Mexican market. There has been a reduction in the companies currently operating in Mexico, arising from the dissolution of certain companies and the revocation of licences. The impact of the intervention and eventual revocation of the licence of Istmo Re in Panama had repercussions in Mexico, exposing failures in the regulation and, mostly, the negative effects of relying on fronting arrangements as well as on ratings to determine whether or not foreign reinsurance companies may take risk from Mexican cedants. The Mexican market was one that was more heavily affected by the Istmo Re scandal, with little or almost no expectations of recoveries from the Mexican subsidiary, now also in liquidation.

II REGULATION

i The insurance regulator

Insurance and reinsurance operations in Mexico are regulated by both the Ministry of the Treasury and Public Credit (SHCP) and the CNSF. The SHCP has authority to interpret, implement and execute the LISF for administrative purposes. The CNSF has authority to grant and revoke authorisations to incorporate and operate insurance companies in Mexico, and to register reinsurance companies with the General Registry of Foreign Reinsurance Companies to take Reinsurance and Rebonding from Mexico (the Reinsurance Registry), to take reinsurance from Mexican insurance companies. The CNSF is also responsible for supervising the operation of insurance and reinsurance companies and has authority to supervise, inspect and issue regulations applicable to the operations of Mexican insurance and reinsurance companies. All the applicable regulations issued by the CNSF are compiled in a single regulatory circular (the Circular).

ii Position of non-admitted insurers

Article 20 of the LISF provides that only those entities duly licensed by the Mexican federal government through the CNSF to operate as insurance companies may undertake active insurance operations within Mexican territory.²

If a non-licensed insurance company operates in Mexico on a non-admitted basis and carries out active insurance operations in Mexico, it shall be deemed to be breaching Mexican law and the transaction shall be null and void. Furthermore, such conduct would constitute criminal liability on the part of: (1) the non-admitted foreign insurer; (2) the insurance intermediaries (broker or agent); and (3) the officers, managers, directors, representatives and agents of the entities referred to in (1) and (2).

iii Position of brokers

As a general rule, insurance companies may only pay brokerage fees to insurance brokers duly authorised as such by the CNSF. There is a licence to act as an individual agent and another for entities to act as insurance brokers. To obtain the licence to act as an agent or broker, the individual or entity concerned must submit an application to the CNSF, which must comply with the requirements set out in the Regulation of Insurance and Surety Brokers (the Brokers Regulation). The legal provisions applicable to insurance brokers are contained in Chapter 32 of the Circular.

Reinsurance intermediaries are entities licensed to provide reinsurance intermediation services (Article 106, LISF). To incorporate and operate a reinsurance intermediary, the prior authorisation of the CNSF is required, and to obtain the authorisation an application must be filed with the CNSF. The application must comply with the requirements set out in the Rules on the Authorisation and Operation of Reinsurance Intermediaries (the Intermediaries Rules). Reinsurance intermediaries must be incorporated as limited liability stock companies and have their corporate domicile in Mexican territory. The legal provisions applicable to reinsurance intermediaries are contained in Chapters 9, 32 and 35 of the Circular.

iv Requirements for authorisation

Pursuant to the LISF, to incorporate and operate an insurance company in Mexico, an application shall be filed with the CNSF. The application must comply with the requirements set out in Article 41 of the LISF. The CNSF has discretionary authority to grant or deny the authorisation. These authorisations are regulated in Chapter 2 of the Circular.

An insurance company must start operations within three months of receiving the relevant authorisation from the CNSF. Before starting its operations, the CNSF must carry out an inspection visit and confirm that the insurance company has the infrastructure, procedures and systems required to operate according to Article 47 of the LISF.

Under the LISF, Mexican insurance and reinsurance companies and foreign reinsurance companies registered with the Reinsurance Registry may cede or take risks in reinsurance to and from Mexican insurance companies. Pursuant to the Circular, foreign reinsurance companies may not take reinsurance in Mexico when they intend, or when they effectively carry out, on a majority or exclusive basis, reinsurance operations with Mexican insurance

2 Article 20, Paragraph 2 of the LISF defines 'active insurance operations' as those in which, upon the occurrence of a future and uncertain event agreed upon by the parties, one party agrees to directly or indirectly indemnify or pay an amount of money to the other party, in exchange for a premium.

companies with whom they have financial or business ties. Although it is not clearly explained in the LISF, the 'majority or exclusive' operations referred to in this provision relate to the global reinsurance activities undertaken by foreign reinsurance companies, and not only their reinsurance activities in Mexico. The reason for this provision is to prevent the proliferation of captive reinsurance companies.

Insurance companies authorised in Mexico are allowed to carry out reinsurance operations in the same lines of business in which they have a licence to take insurance. However, a licence to exclusively operate reinsurance business can also be obtained. There are currently only two Mexican insurance companies authorised to exclusively operate reinsurance: Reaseguradora Patria and Der Neue Horizont Re.

The registration of foreign reinsurance companies with the Reinsurance Registry is governed by the LISF and the Circular. To register with the Reinsurance Registry, foreign reinsurance companies must file an application with the CNSF in the terms set forth in Article 107 of the LISF and Chapter 34.1 of the Circular. The CNSF may grant or deny this registration on a discretionary basis. The registration of foreign reinsurance companies is valid until 31 December of the year on which the registration is given and must be renewed every year.

v Regulation of individuals employed by insurers

Title 3, Chapter 1, Section II of the LISF and Chapter 3.7 of the Circular provide basic requirements of experience, expertise and knowledge in finance, law, administration or insurance for the eligibility of directors, officers and statutory examiners within an insurance company and also prescribe which individuals may not be appointed as such. Insurance companies must give notice to the CNSF on any such appointment and provide sufficient evidence to the CNSF that the individual complies with the requirements under the LISF to serve in the relevant capacity. The insurance company must maintain a file for each individual with supporting documentation and evidence of their qualifications and representations and annually confirm to the CNSF that its directors and officers comply with the requirements set forth in the LISF and the Circular to serve in their respective positions.

vi The distribution of products

Pursuant to the LISF and Chapter 4 of the Circular, standard-form contracts, collective and group contracts and surety insurance must be registered with the CNSF.

Insurance products registration must comply with the following documentation (contractual documentation): (1) general conditions and model contracts, containing the general and particular conditions under which the insurance product will be commercialised; (2) a technical note, containing the technical and financial hypothesis for the calculation of the premium and the ongoing risk reserve; (3) a legal opinion, certifying that the insurance product complies with all applicable legal provisions; and (4) a 'congruency opinion' that certifies that both the technical note and the legal opinion are consistent.

Insurance companies may use, sell and distribute insurance products immediately upon their registration. The CNSF may at any time suspend the registration of an insurance product if, in its opinion, the insurance product does not comply with applicable laws and regulations.

The LISF requires that standard-form insurance contracts are filed with the National Commission for the Defence and Protection of Financial Services Consumers (Condusef), for their registration with the Standard-Form Contracts Registry.

vii Compulsory insurance

Under Mexican law the main difference between compulsory insurance and other insurance products, other than the fact of the insurance coverage being required by law, is that compulsory insurance contracts shall continue in full force and effect until their termination, and may not be terminated, even when the corresponding premium is not paid when due or within the cure period set forth under the LISF. Compulsory insurance premiums may not be paid in instalments.

Compulsory insurance in Mexico includes, among others, social security (e.g., life, health and disability), which is mandatory for employers with respect to their employees; professional liability insurance to practise certain professions; and automobile insurance to circulate on roads and highways under federal jurisdiction.

viii Taxation of premiums

Insurance companies are subject to income tax and value added tax. Income tax is levied at 30 per cent on insurance companies' accrued income less authorised deductions. The Income Tax Law provides special rules for deductions applicable to insurance companies.

Value added tax is levied at 16 per cent on all insurance services paid for by customers, except for agricultural insurance, mortgage and financial guaranty insurance, and life insurance.

Mexican reinsurance companies receive the same tax treatment as insurance companies. Income tax is applicable to foreign reinsurance companies when they receive premiums from a Mexican resident or from a foreign resident with a permanent establishment in Mexico. The income tax is calculated by applying a 2 per cent withholding rate on the gross amount paid to reinsurers with no deductions.

The person paying the premium to the reinsurers must withhold and pay the income tax at the applicable rate. Depending on the jurisdiction in which the reinsurance company is incorporated, there might be a double taxation treaty that applies to the payment of premiums to foreign reinsurance companies and that supersedes the general provisions referred to herein.

Insurance and reinsurance brokers are subject to the same taxes and to the same rates as insurance companies but are not subject to special deductions applicable to insurance companies.

ix Other notable regulated aspects of the industry

Pursuant to Mexican law, insurance companies must maintain a minimum paid-in capital stock. That minimum paid-in capital stock is regulated in Chapter 6 of the Circular.

The following are the minimum paid-in capital requirements applicable for 2018, expressed in Mexican pesos, for each line of business (approximate numbers):

- a* life: 37.90 million pesos;
- b* pensions: 155.6803 million pesos;
- c* accidents and health:
 - personal accident or medical expenses: 9.47 million pesos; and
 - health, including personal accident or medical expenses: 9.47 million pesos;
- d* property and casualty:
 - one line: 28.43 million pesos;
 - two lines: 37.9 million pesos;
 - three or more lines: 47.38 million pesos;

- mortgage insurance: 67.83 million pesos; and
- financial guarantee insurance: 184.59 million pesos.

Insurance companies authorised exclusively for reinsurance operations are required to maintain 50 per cent of the applicable minimum paid-in amount, as listed above.

III INSURANCE AND REINSURANCE LAW

i Sources of law

Mexican insurance and reinsurance companies are governed by the LISF. The LISF was published in the Official Gazette of the Federation (DOF) on 4 April 2013 and entered into effect on 5 April 2015, repealing the General Insurance and Mutual Companies Law that was in effect since 1935.

The Insurance Contract Law (LCS), enacted by Decrees dated 29 December 1934 and 1 January 1935, also published in the DOF on 31 August 1935, is applicable to all insurance contracts subject to Mexican law, except for maritime insurance, which is governed by the Navigation and Maritime Commerce Law published in the DOF on 1 June 2006.

Reinsurance contracts are governed by the applicable law expressly agreed by the parties in the contract. Generally, the parties agree to subject reinsurance contracts to Mexican law.

ii Making the contract

Article 1 of the LCS defines insurance contracts as agreements in which an insurance company agrees to indemnify or pay for damages, or to pay an amount of money on the occurrence of a risk covered under the terms of the contract, in exchange for the payment of a premium.

The reinsurance contract is not a regulated contract. This generates many disputes in practice. The reinsurance contract is defined in Article 2, Section XXV of the LISF, as the contract in which an insurance company assumes totally or partially a risk that is covered by another insurance company, or the liability exceeding the amount insured by the direct insurer.

Article 25 of the LISF provides a general classification of insurance contracts as follows:

- a* Life.
- b* Accidents and health including:
 - personal accidents;
 - medical expenses; and
 - health.
- c* Property and casualty including:
 - civil liability and professional;
 - maritime and transportation;
 - fire;
 - agriculture and livestock;
 - automobiles (motor insurance);
 - credit insurance;
 - surety insurance;
 - mortgage insurance;
 - financial guarantee insurance;
 - earthquake and other catastrophic risk;
 - miscellaneous; and
 - risks declared by the SHCP as specialty risks.

Essential elements of an insurance contract

Under the LCS, insurance policies must contain:

- a* the name and address of the contracting parties and the signature of the insurance company;
- b* a description of the insured asset or person;
- c* a description of the risks insured;
- d* the effective date of coverage and its duration;
- e* the amount insured;
- f* the insurance fees or premium; and
- g* any other clauses required by law or agreed by the parties.

It is common to find the following clauses in insurance policies:

- a* coverage limits and exclusions;
- b* form and terms under which the premium must be paid;
- c* insured's right to be informed about commissions paid to intermediaries;
- d* insured's right to revise the policy if its terms differ from the agreed terms;
- e* competence of Condusef and choice of jurisdiction clause; and
- f* special clauses required for specific lines of business.

Utmost good faith, disclosure and representations

In Mexico the duty of utmost good faith is an implied principle applicable to all insurance contracts. This duty demands diligent and honest conduct from both parties, including the duty of the insured to disclose to the insurer any fact that may help the underwriter to evaluate the risks and determine the premium.

iii Interpreting the contract

General rules of interpretation

To the extent the terms and conditions of the agreement are clear and there is no question as to what the intent of the parties was, the insurance policy must be interpreted in accordance with its terms:

- a* if the terms of the insurance policy seem contrary to the evident intent of the parties, the intent of the parties shall prevail over the terms of the insurance policy;
- b* if the insurance policy is generic in its terms, its interpretation must be limited to the purposes of the insurance policy;
- c* if the insurance policy permits various interpretations, it must be interpreted in the most convenient manner for the insurance policy to be effective;
- d* the terms and conditions of an insurance policy, including those terms that are not clear, must be interpreted in a manner that is consistent with the interpretation of the insurance policy as a whole;
- e* the terms of an insurance policy that may have different meanings must be interpreted in a manner consistent with the nature and purposes of the insurance policy;
- f* ambiguities of the insurance policy may be interpreted taking into consideration the customs of the country; and
- g* if it is impossible to construe the insurance policy using the rules set out above, the insurance policy must be construed in favour of the interpretation that provides reciprocity of interests between the parties.

Incorporation of terms

The LCS is mandatory, therefore any agreement contrary to the LCS is null and void, unless otherwise permitted under the LCS. Taking this into account, it is implied that insurance contracts are subject to the provisions of the LCS.

iv Intermediaries and the role of the broker

Conduct rules

Pursuant to Article 106 of the LISE, only reinsurance intermediaries are authorised to provide reinsurance intermediation services. Authorisation from the CNSF is required to incorporate and operate a reinsurance intermediary. In order to obtain such authorisation, an application must be filed with the CNSF. The Intermediaries Rules set forth the requirements and information that the application for authorisation must contain. A reinsurance intermediary must be incorporated as a limited liability company with a residence in Mexico.

Agencies and contracting

As a general rule, intermediation of insurance products may only be carried out by insurance brokers certified and licensed by the CNSF. Insurance companies may only pay commission arising from the sale of insurance policies to insurance brokers.

How brokers operate in practice

To carry out brokerage services in Mexico, insurance brokers must be authorised by the CNSF. To this end, an application must be filed with the CNSF. The requirements and information that the application must contain is set forth in the Brokers Regulation. The authorisation may be granted to:

- a* individuals acting as employees of an insurance company or independent individuals operating with a service agreement with an insurance company; and
- b* limited liability companies incorporated under Mexican law.

The authorisation to act as an insurance broker is granted for a period of three years for individuals (renewable at the request of the insurance broker) and, in the case of legal entities, the CNSF can grant the authorisation for an indefinite period.

Article 12 of the Brokers Regulation lists entities and individuals that cannot participate, directly or indirectly, in the capital stock of an insurance broker legal entity; these include Mexican insurance companies and financial entities subject to approval by the corresponding Mexican authority; foreign governments or authorities; and foreign financial entities.

v Claims

A claim is triggered on the occurrence of a peril covered by the policy. An insurable interest is required to make a valid claim and demand payment under a policy.

The statute of limitation of claims is of two years after the date of the occurrence of the loss, except for life insurance, where the statute of limitations is five years (Article 81, LCS). The statute of limitations can be interrupted:

- a* on appointment of experts as a result of a loss;
- b* if a claim is filed with the specialised unit of the corresponding insurance company or Condusef;

- c* by initiating an action or proceeding before competent courts, on service of process to the insurance company; or
- d* by the express acknowledgment of the rights of the insured or its beneficiaries by the insurance company.

Good faith and claims

The LCS establishes the obligation of the insured (1) to give timely notice of the occurrence of the casualty; (2) regarding property and casualty insurance, to prevent or reduce the damage; and (3) not to modify the status of the assets. If, when acting in good faith, the insured omits to give timely notice of the occurrence of the casualty or to carry out reasonable actions to prevent or reduce the damage, or modifies the status of the insured asset, the insurance company may reduce the indemnity in proportion to the damage that could have been mitigated or avoided by the insured. If the insured were to act fraudulently, the insurance company would be released from its obligations under the policy.

The consequences of bad faith may:

- a* trigger the right to terminate the insurance contract;
- b* allow the parties to recover premiums paid or request payment of damages and loss of profit; and
- c* release the parties from their obligations under the insurance contract.

Set-off and funding

The parties can set off mutual debts and credit as long as both are due and payable.

Reinstatement

Reinstatement is the act through which an insurance contract regains its validity, once the circumstances that caused the suspension of the contract have ceased.

The LCS does not regulate reinstatement, but it may be included in the insurance contract. Reinstatement generally operates when the insured pays the outstanding premiums, provided the risk has not changed.

If any risk takes place prior to reinstatement of the insurance contract, the insured is not entitled to obtain any compensation, since he or she was not covered by the insurance.

Dispute resolution clauses

Clauses regarding choice of forum, jurisdiction and applicable law are valid and enforceable in Mexico in insurance and reinsurance contracts. Furthermore, the parties in insurance and reinsurance contracts can convene to solve potential disputes through an arbitration. Mexico is a contracting state of the Hague Convention on Choice of Court Agreements (2005) and of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (also known as the New York Convention 1958).

IV DISPUTE RESOLUTION

i Jurisdiction, choice of law and arbitration clauses

The parties in a reinsurance contract are free to agree the terms and conditions of the contract as long as they do not breach any mandatory legal provision or go against public policies.

Arbitration clauses are enforceable in insurance and reinsurance agreements. The terms and conditions of an insurance contract are subject to and shall comply with the LCS, which is mandatory; any agreement contravening the LCS shall be null and void.

ii Litigation

Insurance and reinsurance disputes are regulated by the Code of Commerce. If one of the parties breaches a contract, the non-defaulting party can initiate ordinary commercial proceedings. This judicial process has four basic stages: (1) filing of the claim by the plaintiff and response from the defendant; (2) submission and presentation of evidence of any kind; (3) pleadings; and (4) award.

The parties can appeal any ruling to a higher tribunal, unless the aggregate amount is less than 574,690.47 pesos.

Each party pays its own litigation costs and the losing party might be required to indemnify the winning party, including for attorneys' fees, subject to certain established thresholds and the decision of the court.

iii Arbitration

The insured and the respective beneficiaries can file claims with the insurance company, Condusef and Mexican courts.

Claims filed with Condusef or before a competent court interrupt the statute of limitations.

Condusef can act as a mediator in disputes resulting from an insurance contract if the amount in dispute is less than 6 million Mexican investment units (approximately 34.01 million pesos). Condusef can also act as an arbitrator if the dispute is not solved in a mediation process; however, the parties can choose a third party as an arbitrator.

The foregoing does not affect the right of the parties to bring a legal action before Mexican courts.

Mexico is a contracting state of the New York Convention and agreements to submit disputes arising from reinsurance policies to arbitration are valid, and the respective awards can be enforced by Mexican courts.

The Mexican chapter of the International Insurance Law Association, the Mexican Insurance and Bonding Law Association (AMEDESEF), together with the Arbitration Centre of Mexico (CAM), created the Mexican chapter of the Insurance and Reinsurance Arbitration Society (ARIAS Mexico). ARIAS Mexico, managed by the CAM with the technical assistance of AMEDESEF, promotes arbitration to resolve insurance and reinsurance disputes.

In Mexico, reinsurance claims can be resolved in judicial proceedings through arbitration or through other alternative dispute resolution mechanisms, such as mediation and conciliation.

iv Mediation

There is an important increase in mediation as an alternative mechanism for settling international reinsurance disputes and claims involving Mexican cedants and the London market. Mediation has proven to be an efficient alternative.

v Alternative dispute resolution

Even though Article 17 of the National Constitution refers to means of alternative dispute resolution, Mexico does not have a federal regulation regarding alternative dispute resolution processes. Nevertheless, several states of the Federation have enacted specific laws on this matter.

The most popular alternative dispute resolution procedures are arbitration and mediation, which are discussed in Sections IV.iii and IV.iv, above.

V YEAR IN REVIEW

According to the CNSF, as of September 2017, the Mexican insurance sector is comprised of 98 insurance companies licensed to operate in Mexico and more than 250 foreign reinsurance companies registered with the Reinsurance Registry, including Lloyd's of London. Ten atomic pools (nuclear insurance pools) were also registered with the Reinsurance Registry to take reinsurance in Mexico.

According to the CNSF, when compared with the same period in 2016, overall annual growth in the Mexican insurance industry from January to September 2017 was 4.8 per cent in real terms; this figure takes into account that direct premiums related to the state-owned oil company Pemex's two-year policy renewal. Out of the 9.3 per cent growth, life insurance was the line of business with the largest annual growth, with 9.9 percentage points, followed by property, which increased by 3.3 per cent; motor insurance grew 15.9 per cent while accident and health grew by 13.1 per cent, and pensions decreased by 6.1 per cent.

The penetration of insurance with respect to Mexico's GDP is 2.3 per cent. The Mexican Association of Insurance Institutions, together with the CNSF, are working on a strategy to increase penetration to 3.4 per cent by 2020.

On 25 September 2017, the CNSF revoked Istmo México, Compañía de Reaseguro's licence to operate as an insurance company, and it is currently the subject of insolvency proceedings. This has caused financial problems for a number of cedants who are now trying to recover from Istmo.

VI OUTLOOK AND CONCLUSIONS

i Regulatory

Regulatory challenges are likely to arise from operating under Solvency II standards as there is ongoing concern with regard to maintaining a competitive sector while at the same time increasing penetration, maintaining operational costs in reasonable levels to permit growth and ensuring that Mexican operations are attractive to investors. Regulators will continue to be concerned and impose strict measures in compliance with anti-money laundering and similar regulations.

Depending on the market rates, certain insurance companies may explore investment alternatives within the flexible regulatory framework under Solvency II for investments.

There is extensive interest in developing insurtech potential, while coping with compliance and regulatory challenges including a strict regime that is not very well adapted from the banking sector on anti-money laundering regulation, and a new and evolving regime on data protection and privacy. New risks require new products as well as new challenges. There continues to be appetite from funds to work alongside insurance companies to exploit the role of insurance companies as institutional investors. The challenges have been clearly

identified, and except for a few examples of insurance companies actively investing in private equity, venture capital and other securities such as development trusts and real estate trusts, the insurance industry has not fully embraced its potential as a key institutional investor; and at the same time, regulators have not amended the regulations to enhance and give incentives for such purpose.

In terms of insurance products, the surety insurance was the most important innovation introduced by the new LISF. Currently, four groups have been licensed by the CNSF to incorporate a surety insurance company. However, owing to lack of implementing regulation, such companies have not been given the final authorisation required to operate surety insurance in Mexico, and it is expected that such approval will not be granted until the third or fourth quarter of 2018 – three years after the law came into effect and five years after the law was published. It is still uncertain what impact surety insurance will have on the market.

ii Case law

There has been important growth in litigation, and precedents continue to be formed by Mexican courts on insurance matters. The most relevant development continues to be the concept of moral damages being regarded in similar terms as those of punitive damages, with important focus on the insurance industry. Other precedents continue to reinforce the *contra proferentem* principle in insurance, impacting the manner in which cases are being argued before Mexican courts. There are also important developments in the interpretation and application of terrorism exclusion in Mexico owing to recent cases of looting and civil commotion in the context of demonstrations and protests against the government that occurred in January 2018, as a consequence of a substantial rise in the price of petrol known as ‘el gasolinazo’. These cases are relevant to the industry as the Mexican precedents do not reflect international market practices.

iii Reinsurance claims

Owing to an increase in disputes arising from the inconsistency of applicable laws and regulations governing reinsurance contracts and, in particular, to abuse in the application of claim control clauses, the Mexican insurance market has expressed its concerns about certain practices of reinsurers. There is an ongoing conversation to resolve these practices that are damaging the credibility of, and confidence in, reinsurers.

One of the main problems is caused by the recurrent use of fronting arrangements in a legal framework where the insurance company maintains its liability before the insured despite the fact that, technically, it is just fronting the risk. Issues such as lack of understanding or even neglect of Mexican law, and the respective failure to review the effect that Mexican law has in relation to the English wording used in some placements through fronting arrangements, raises inconsistencies between the insurance or reinsurance policies and Mexican law, and to growing differences in the manner in which reinsurance companies handle claims in prejudice of the insurance company that placed the business. Despite various efforts, the regulators in Mexico have not approved a mechanism to effectively address the effects of international money laundering regulations in local placements and limitations of liability under reinsurance programmes.

There is an opportunity to effectively use and promote alternative dispute resolution mechanisms in Mexico specialised in insurance and reinsurance claims, including mediation and arbitration and the use of ARIAS Mexico, by including arbitration clauses in insurance

and reinsurance agreements to resolve disputes in arbitration, as a consequence of the ongoing conflicts arising in reinsurance contracts, and also to prevent certain situations in global insurance programmes.

While mediation and arbitration are supposed to be attractive alternatives to settle claims and disputes between Mexican cedants and the London Market, they are not effectively addressed in the reinsurance contracts, and therefore, it is difficult to include or agree on mediation or arbitration once there is a dispute.

iv Distribution

Efforts from the CNSF and the Association of Mexican Insurance Companies to expand insurance offers to small and medium-sized companies, which contribute around 52 per cent of the national GDP, and enforcing automobile insurance and other mandatory insurance products have had limited success.

There is interest in developing innovative products for the Mexican market and using technology to promote, develop and expand penetration in Mexico; however, there is indecisiveness in the market combined with a conservative approach from regulators, as well as regulatory challenges.

Bancassurance continues to develop and is one of the most important areas of growth within the industry. With very few exceptions, most banking groups operating in Mexico have transferred their insurance business and operations to insurance groups and entered into exclusive distribution arrangements.

v Further consolidation

The increase in operation costs because of the new legal and regulatory framework implementing Solvency II standards, the competitive market conditions with a lack of penetration, stagnation of the Mexican economy, mediocre growth of the Mexican insurance market, and the de-risking and changes in strategy of international groups regarding Latin America and Mexico in particular, may contribute to certain groups entering the Mexican market and others exiting the market, and some consolidation of the insurance industry in Mexico. Recent growth in niche sectors, and through cross-border alliances and collaborative structures securing and bringing capacity from London and other markets to the Mexican market, may continue.

vi Lloyd's

In January 2018, Probitas Syndicate 1492 opened a representative office in Mexico, becoming the first Lloyd's syndicate with a physical presence in Mexico. Probitas aims to coordinate its strategy in Latin America from its office in Mexico. Taking into account the constant conflicts arising from inadequate placement of reinsurance policies in Mexico, having a local team of underwriters will contribute to a more efficient and transparent operation for the benefit of the Lloyd's market and the local cedants. Two Mexican groups, Grupo Nacional Provincial and Reaseguradora Patria, currently have investments in Lloyd's.

vii Product development

The appetite of the Mexican insurance market for capacity to underwrite the new energy-related risks has been invigorated by the developments in the reform of the energy sector and new players operating in Mexico. Such developments include environmental risks,

exploration and production of hydrocarbons, upstream, midstream and downstream. The complexity and size of the Mexican market demands new and innovative products to cover new risks such as cyber risk, as well as health and medical coverage insurance, professional liability, directors and officers, and errors and omissions policies. There has also been growth in asset management-related products and services.

Surety insurance policies are being developed to be placed by local surety insurance companies as soon as they are authorised to operate, most likely until the end of the year.

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Yves is a partner of the Mexican independent law firm Nader, Hayaux & Goebel, the only Mexican law firm with an office in London.

Yves specialises in insurance and reinsurance, both in contentious and non-contentious matters. Yves currently represents the following Mexican affiliate insurance companies on an ongoing basis in transactional work, mergers and acquisitions, product development and general regulatory, corporate governance and compliance-related matters: AXA Seguros Mexico, Assurant Daños Mexico, Assurant Vida Mexico, BUPA Mexico, Cardif Mexico Seguros de Vida, Cardif Mexico Seguros Generales, Dentegra Seguros Dentales, Der Neue Horizont Re, Genworth, Grupo Nacional Provincial, Grupo Sudamericano de Inversiones (Grupo SURA), LandAmerica Mexico (in liquidation), Mapfre Asistencia, MetLife Mexico, Panamerican Life Mexico, Seguros Azteca, Seguros Principal, Skandia, Principal Pensiones, Prudential Seguros Mexico and Zurich Mexico.

Yves also represents Mexican and foreign insurance and reinsurance companies, and has experience in arbitration and mediation.

Yves is former chairman, vice chairman and board member of the Mexican chapter of AIDA, former vice chairman of CILA, and was responsible for establishing ARIAS Mexico. He is also a member of the presidential council of AIDA, vice president of the transnational legal practice committee of the American Bar Association and honorary member of the Commercial Bar Association.

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