

## RVP Bulletin

### Regulated Contracts in the Swiss Insurance Business



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#### Contents

|   |   |
|---|---|
| Form of contract in regulated area.....                     | 1 |
| Insurance contract.....                                     | 2 |
| Collective insurance contract.....                          | 2 |
| Reinsurance contract.....                                   | 3 |
| Outsourcing agreement.....                                  | 3 |
| Deposit agreement for tied assets .....                     | 4 |
| Master agreement for derivative financial instruments ..... | 4 |
| Portfolio transfer agreement .....                          | 4 |
| Agent agreement.....  | 4 |
| Broker agreement.....                                       | 5 |
| Cooperation agreement between insurance com. and broker ... | 5 |
| Cooperation agreement between two insurance companies.....  | 6 |
| Cooperation agreement between insurance com. and bank ..... | 6 |
| Abbreviations .....   | 6 |

#### Form of contract in regulated area

In the Swiss insurance and insurance intermediation business there is freedom of contract to a limited extent only. Various mandatory and semi-mandatory provisions need to be respected when drafting a contract. Most of the provisions concern the content of contract, some of them also the conclusion of contract. In addition, there are provisions that require the prior approval of contract by FINMA (contracts subject to approval).

The contract related provisions in the insurance business are substantially based on the Insurance Contract Act and Insurance Supervision Act, the Supervision Ordinance and Supervision Ordinance-FINMA as well as various circulars and other orders issued by FINMA. Only in those cases where there are no specific provisions in insurance law are the provisions of general private law applicable. Finally, case law of Swiss courts must be taken into consideration.

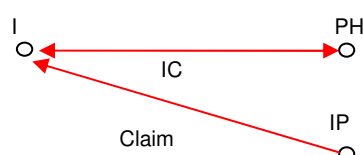
An insurance company or insurance intermediary may face criminal, supervision law or private law sanctions if it does not respect insurance law and does not conclude a contract where a contract is required or concludes a contract in which the content is against the law or does not obtain approval for a contract that is subject to approval. For example, a person who does not obtain approval for a contract subject to approval may incur a penalty. As regards supervision law, FINMA intervenes to protect the insured from any abuse and in the event of any mismanagement that endangers the interest of the insured. Where there is a serious violation of supervision law, FINMA may prohibit the person responsible from acting in a management capacity. There is abuse namely if contract provisions are used in the insurance business that violate mandatory provisions of the Insurance Contract Act or other acts that apply

to the contract, or that provide for an allocation of rights and duties that considerably contradicts the nature of the contract. Finally, as regards private law, a contract with illegal content may be completely or partly void or effective with deviating content.

### Insurance contract

The contract that is regulated the most in the insurance business is certainly the insurance contract. The insurance contract is a contract between the insurer and the policyholder whereby the insurer promises the policyholder against the payment of premium economic benefits in the situation where a person, an object or assets are completely or partly concerned by a future and uncertain event.

The insurance claim generally exists in favour of the policyholder. In such a case the policyholder is at the same time the insured. However, the insurance claim may also exist in favour of a third person as beneficiary (insurance for the account of a third party, insurance for the benefit of a third party) so that policyholder and insured person are not identical. The insured person has generally an independent legal claim against the insurer. The contractual insurance relationship may be shown as follows:



Based on the insurance supervision law, insurance contracts may be entered into by the insurance company only if the relevant insurance class has previously been approved by FINMA. If the approval is waived or withdrawn the insurance company may not conclude further insurance contracts in the relevant insurance classes. Also existing insurance contracts may not be renewed and the extent of coverage may not be extended.

The Insurance Contract Act generally includes provisions regarding conclusion and content of insurance contracts as well as specific provisions for indemnity and personal insurance. Furthermore, the Insurance Supervision Act and the Supervision Ordinance in-

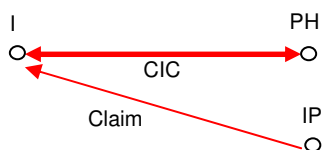
clude provisions regarding contracts subject to approval as well as provisions regarding specific contracts in the following insurance classes: legal protection, natural hazard, life insurance, pension fund insurance as well as health and accident insurance.

The insurers are themselves responsible that the General Insurance Conditions (GICs) of their products comply with the provisions of insurance law. Generally, there is no preliminary review by FINMA. However, FINMA may require at any time within the scope of its supervisory activities that used GICs are presented to it for review. Exceptionally, GICs are preliminarily reviewed by FINMA in social sensible areas. This concerns additional health insurance and collective life insurance. It goes without saying that later changes of GICs in these insurance areas are also subject to review by FINMA.

Finally, the question of applicable law and jurisdiction may be asked in international circumstances. As regards the applicable law, the following applies: If the insurance contract qualifies as a consumer contract the choice of law is excluded under the International Private Law Act (IPLA) and the law of the state where the policyholder or the insured has his or her ordinary residence generally applies. As regards the place of jurisdiction, the policyholder qualifying as consumer may in particular file a claim against the insurer at his or her domicile or ordinary residence in Switzerland. Particular provisions for insurance matters need to be observed within the scope of the Lugano Treaty. According to the Lugano Treaty the policyholder may in particular file a claim against the insurer in his or her state of residence. Such jurisdiction also applies if the policyholder does not qualify as a consumer but is for example an industrial enterprise.

### Collective insurance contract

The collective insurance contract is a specific kind of insurance contract that is entered into by the policyholder in favour of a specified group of persons (e.g. the employer for his employees). Often the insured person has an independent legal claim against the insurer by act of law (e.g. in the case of collective health insurance) or based on contract. The contractual relationship of collective insurance may be shown as follows:



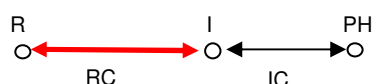
Insurance law includes particular provisions applicable to collective contracts. They are included in insurance contract law (e.g. information and disclosure duty) as well as in insurance supervision law (e.g. collective health daily allowance insurance). Apart from these particular provisions, general insurance contract law applies.

Collective insurance is widespread in the areas of pension funds (collective life insurance) and health and accident insurance. It may also be applied in other insurance classes. Collective insurance contracts may only be entered into if the relevant insurance class has previously been approved by FINMA.

It may be stated in this context that conversely it is also possible that several insurers participate in the insurance of the same risks (co-insurance). This applies for example to the coverage of large industry risks. However, the insurance is not based on one and the same insurance contract. Rather, several legally independent contracts are combined in the insurance policy whereupon each insurer is only responsible for its own share of the total sum insured.

### Reinsurance contract

The reinsurer is the insurer of the direct insurer. The reinsurer helps the direct insurer (ceding company) to fulfil existing insurance contract obligations in form of claim payments. The transfer of risk may continue on another level. The reinsurers may also arrange for a balance of risks among themselves. The balance of risks thereby takes place by means of retrocession between two reinsurers. The reinsurance contractual relationship may be shown as follows:

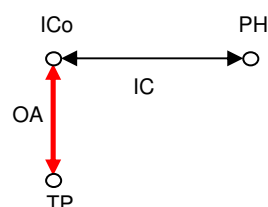


The Insurance Contract Act does not apply to reinsurance contracts. They are subject to the Code of Obligations. The application by analogy of appropriate provisions of the Insurance Contract Act is reserved. Furthermore, various provisions of the Insur-

ance Supervision Act are not applicable to insurance companies which exclusively perform the reinsurance business. Finally, there are specific rules for reinsurance captives. Reinsurance contracts may only be entered into if the relevant insurance class has previously been approved by FINMA.

### Outsourcing agreement

The insurance company may outsource various activities to third parties if the interests of the insured are not jeopardised and the supervision by FINMA not hindered. The outsourcing relationship of the insurance company may be shown as follows:



If important functions of the insurance company are outsourced a written outsourcing agreement is required that generally needs to previously be approved by FINMA. There is no need for approval if the outsourcing relationship is not arranged on a continuing basis or if the outsourcing relationship does not give the service provider any entrepreneurial freedom for the performance of its task. In case of doubt prior approval should be obtained. Important functions that imperatively belong to an insurance company are according to FINMA the production (product development, distribution, underwriting), portfolio administration (administration of policies), claims management, accounting, investment of assets/asset management as well as IT/Electronic Data Management. An insurance company must observe various restrictions issued by FINMA if it outsources important functions.

Outsourcing agreements must provide a minimal content in order to ensure that the interests of the insured are not jeopardized and FINMA is still capable of performing its supervisory tasks. The rules applicable to outsourcing relationships in the banking sector (FINMA-Circular) may partly be applied by analogy. FINMA currently does not apply high standards to the content of outsourcing agreements. It is, howev-

er, also in the insurance company's own interest to agree on contractual clauses that are sufficient for the protection of the insured. Agreements with claims managing companies in legal protection insurance are specific types of outsourcing agreements that are subject to additional provisions in the Supervision Ordinance.

A service provider of the insurance company may enter into sub-contracts. If applicable, the outsourcing agreement must however include a clause according to which a written contract is required to be entered into with the sub-agent that, in principle, includes the same clauses as the outsourcing agreement if important functions are concerned. In addition, such a sub-contract must in my opinion be approved as well by FINMA.

### Deposit agreement for tied assets

Insurance claims must be secured by tied assets at all times. That is why values allocated to tied assets must be kept separately from other assets of the insurance company and identified as such. Both internal and external storage are possible. Currently, external storage is, in principle, only admissible in Switzerland, Belgium, Liechtenstein and Luxembourg.

If allocated values are kept with a bank, the insurance company must enter into a deposit agreement with the respective bank. The deposit agreement must include the clauses of the model agreement of the Swiss Banking Association. This model agreement, however, needs in my opinion to be updated. It should include the supervisory authority as additional party. Also its content should be completed. Reference is made to the model agreement of the Luxembourgian supervisory authority that has recently been updated.

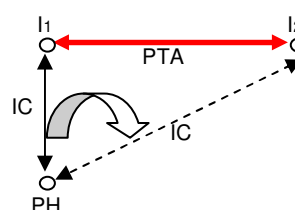
### Master agreement for derivative financial instruments

Offsetting (netting) of all derivative businesses covered under a master agreement is only permitted pursuant to the Supervision Ordinance if the master agreement is entered into separately for each type of tied assets.

Permitted are only such master agreements of which the enforceability of the close-out-nettings can be established. The standardized master agreements that are most common in Switzerland are the Swiss master agreement for over-the-counter (OTC)-derivatives and the ISDA master agreements. The FINMA investment guidelines include provisions concerning the form of master agreements for derivative financial instruments.

### Portfolio transfer agreement

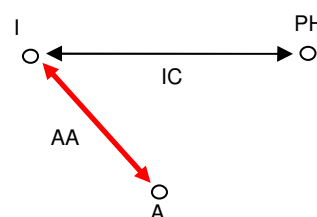
An insurance company may transfer its Swiss insurance portfolio completely or partly to another insurance company without need to obtain approval from the policyholders. The transfer takes place by means of a portfolio transfer agreement and must be approved by FINMA. The portfolio transfer agreement may be shown as follows:



The policyholders will be informed of the portfolio transfer by the insurance company which assumes the portfolio. They are, in principle, given the option to terminate the insurance contract. An approved portfolio transfer will be published by FINMA.

### Agent agreement

A tied agent is a person who offers or concludes insurance contracts and is thereby tied to an insurance company, either legally, commercially or in any other way. The tied agent is subject to insurance supervision law. There is generally an employment or agency agreement between the agent and the insurer. The contractual relationship between agent and insurer may be shown as follows:

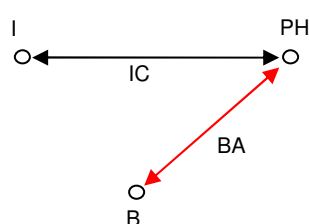


With regards to the form of the contract between agent and insurer, it should be taken into consideration that the insurer is subject to statutory liability. Pursuant to the Insurance Contract Act the insurer is responsible to the policyholder for the agent's performance just as for its own performance. For this reason, it might be sensible to state in the agreement with the (non employed) agent that minutes must be produced at the end of the counselling interview. Insurance law does not include specific requirements for the form of the agent agreement regarding the content.

### Broker agreement

A free intermediary (broker) is a person who offers or concludes insurance contracts and thereby is not tied to an insurance company, neither legally, commercially nor in any other way. The broker is subject to insurance supervision law. He acts on behalf of the client/policyholder. He generally examines and decides with which insurance company he will enter into the insurance contract on behalf of the client.

There is a (written or oral) agreement between broker and client pursuant to the Code of Obligation. Insurance law does not include specific requirements for the form of the broker agreement regarding the content. The contract between broker and policyholder may be shown as follows:

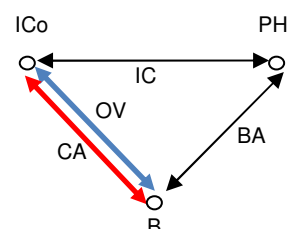


It is current practice that the commission for the broker's services is paid by the insurance company, although the broker acts in the interest of the client/policyholder. Unlike the current practice, the government report of 2009 regarding the revised Insurance Contract Act states that the broker is compensated by the policyholder for his intermediary services.

### Cooperation agreement between insurance company and broker

A cooperation agreement is generally entered into between broker and insurance company. Such agreement concerns the commission of the broker and includes various other provisions.

The cooperation between insurance company and broker occasionally goes beyond mere insurance intermediary services. In addition, the broker may assume functions of the insurance company and, as a consequence, also acts as service provider of the insurance company. The relevant contractual relationships may be shown as follows:



If the cooperation between insurance company and broker includes the outsourcing of important functions of the insurance company, the approval by FINMA is required. It is advisable to document the actual outsourcing relationship and the other aspects of the cooperation separately so that there is no need to file the entire contractual relationship with FINMA. It is only the outsourcing agreement that is subject to approval and needs to be filed with FINMA.

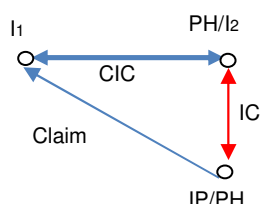
The broker acts in the interest of the policyholder under private law. There is a fiduciary relationship between broker and client. If the broker also acts for the insurance company conflicts of interests may occur. The broker must thereby consider the interests of his clients on the one hand and observe the instructions of the insurance company on the other hand. The conflict of interests may be more or less dominant depending on the type of the outsourced function. If the broker provides services to the insurance company in the area of IT/Electronic Data Processing the activity may still be compatible with the protection of the policyholder's interests. If, however, the broker takes over claims management for the insurance company and own clients are thereby concerned the

activity is not compatible with the broker's fiduciary duty. Conflicts of interests may cause the broker to be liable to the client under private law. They are relevant also under supervision law. Therefore, they should in my opinion also be examined by FINMA if an outsourcing relationship is subject to approval.

### Cooperation agreement between two insurance companies

The Insurance Supervision Act provides that, apart from insurance activities, an insurance company may only operate business directly associated with those activities (no business different from insurance business). FINMA, in principle, has a function related understanding of the provision so that an insurance company may not only perform its own insurance business but generally also act in connection with the insurance business of other insurance companies.

Cooperation between two insurance companies is, in principle, possible in distribution. Therefore, intermediary activities by an insurance company for another insurance company are generally allowed. Furthermore, insurance companies may also cooperate between each other by means of a collective insurance agreement. They may enter into a collective insurance contract where one insurer acts as policyholder of the other. An insurer offers its clients not only its own products but also products of another insurer. The insured are at the same time policyholders of the one insurer and insured persons of the other insurer. It must be apparent for the insured which insurer is liable for which risk and what steps are precisely required in case of a loss event. The collective contractual relationship between two insurers may be shown as follows:

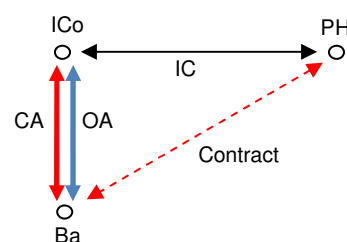


An insurance company in my opinion may, in principle, also take over functions of another insurance company and thereby act as service provider besides its actual insurance activity. However, it is recommended to preliminarily discuss the planned coopera-

tion with FINMA. In the event of outsourcing of important functions, approval by FINMA is generally necessary in any case.

### Cooperation agreement between insurance company and bank

Insurance companies and banks may in particular cooperate in the area of life insurance. If the cooperation includes outsourcing of important functions, it is recommended to document the outsourcing rules separately from the other rules so that only the actual outsourcing agreement needs to be filed with FINMA. Besides the agreements between insurance company and bank, there may also be a direct contractual relationship between policyholder and bank. The relevant contractual relationships may be shown as follows:



Cooperation between an insurance company and a bank or bank group is interesting for example in the area of fund related life insurance (in particular in the insurance classes A.2.4 and A.6). The cooperation may be structured as follows: The insurance company may purchase investment products of the bank; the bank may manage the relevant assets; the policyholder may obtain information about the performance online from the bank; the bank may guarantee the value of assets to the policyholder; etc.

### Abbreviations

|      |   |
|------|---|
| A:   | Agent   |
| AA:  | Agent agreement or agreement between agent and IC             |
| B:   | Broker  |
| Ba:  | Bank  |
| BA:  | Broker agreement or agreement between broker and policyholder |
| CA:  | Cooperation agreement   |
| CIC: | Collective insurance contract                                 |

|        |  |      |                              |
|--------|--|------|------------------------------|
| FINMA: | Swiss Financial Market Supervisory Authority     | OA:  | Outsourcing agreement        |
| GICs:  | General Insurance Conditions                     | PH:  | Policyholder                 |
| I:     | Insurer  | PTA: | Portfolio transfer agreement |
| IC:    | Insurance contract                               | R:   | Reinsurer                    |
| ICo:   | Insurance company                                | RC:  | Reinsurance contract         |
| IP:    | Insured or insured person                        | TP:  | Third party                  |
| IPLA:  | Federal Act on International Private Law of 1987 |      |                              |

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