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The Austrian Insurance Market – a legal perspective

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There are 50 insurance carriers and 56 mutual benefit societies registered in Austria with an Austrian licence on the market. In addition, 26 carriers of the EEA and one Swiss carrier do have branch offices in Austria. Furthermore, 824 carriers carry out business in Austria under the EEA freedom of services. The major Austrian licensed players are Vienna Insurance Group, Uniqa, Allianz and Generali. The Austrian Financial Market Authority (FMA), which supervises the sector, provides a list of insurance undertakings containing all insurance companies authorised to conduct insurance business in Austria plus all insurance classes that the respective companies hold a licence for.

Almost all insurance carriers with registered offices in Austria are members of the Austrian Insurance Association (VVO), which represents the interest of all private insurance companies operating in Austria and supports its members in legal, physical, economical and international matters. VVO claims to have 126 of such companies as members. In stark contrast only 15 EEA insurers are members of the VVO.

In 2009 according to VVO the insurance carriers licensed in Austria earned a premium volume of €16,420bn in total from direct domestic business – this is 1.5% increase compared to 2008. 45.2% of the premiums come from life insurance, 23.1% from loss and damage, 17.1% car insurance, 9.7% health and 4.9% accident. Indemnification payments amounted to €12,214bn in 2009 again according to the VVO.

Update: changes to the law

Transition of EC Directive

The Austrian Insurance Supervision Act (VAG) was amended in order to transform directive 2007/44/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector into the Austrian legal framework. In this regard persons who, alone or together with other persons, (a) wish to acquire direct or indirect participating interests in a domestic insurance undertaking, which would result in them holding at least 10% of the share capital or of the voting rights or exerting a decisive influence on the management in any other way; or (b) already have such a participating interest and increase their interest directly or indirectly in such a way that they reach or exceed the limit of 20%, 30% (instead of one-third) or 50% of the share capital or of the voting rights, or in such a way that the insurance undertaking becomes its subsidiary, shall undertake to notify the FMA thereof in writing under specification of the amount of the said participating interest and the information as per European practice in that area. The same notification obligation applies in case of disinvestments. Further domestic insurance undertakings do have to notify the FMA as soon as they are aware of such acquisition. In case of non-compliance, the FMA may request at the respective District Commercial Court to order the suspension of voting rights for those shares and transfer the voting rights to a trustee who fulfils the requirements that are in the interest of a sound and prudent management of the insurance undertaking.

The FMA has to confirm receipt of notification within two working days and render its administrative decision (*Bescheid*) to prohibit or to not prohibit the acquisition within a maximum period of 60 working days (Monday to Friday). In assessing the notification the FMA shall in order to ensure the sound and prudent management of the insurance undertaking in which an acquisition is proposed, and having regard to the likely influence of the proposed acquirer on the insurance undertaking, appraise the suitability of the proposed acquirer on the financial soundness of the proposed acquisitions on the criteria listed in Article 15b of the directive, i.e., reputation of the acquirer and any person directing the business, financial soundness, future compliance and whether there are any money laundering issues.

Further regulatory issues

Several sections of the Austrian Insurance Supervision Act (VAG) were recently amended. One may highlight that a definition of insurance undertaking was finally incorporated in the VAG. Further, a new form of life insurance, the capital-based life insurance was incorporated, whereby *inter alia* additional information duties were enacted. A 'cool-off' period for executive board members was adopted as well. In addition the money laundering provisions were amended in order to comply with the Financial Acton Task Force (FATF)

Mutual Evaluation Report. The regulation which allows splitting insurance carriers was altered obviously in order to allow the recent restructuring of the Vienna Insurance Group.

Further, the international private law regulations for insurance contracts are now incorporated in several existing acts, especially in the International Private Law Act, instead of the former Austrian Act on Insurance International Law.

Update: recent cases

The Austrian courts had a busy period over the last two years while dealing with insurance related cases. Although Austria is a rather small country there have been several major cases pending. The financial crises hit certain areas of the Austrian economy hard, especially CEE property development companies. Therefore (former) investors initiated thousands of cases against banks and other promoters of shares in Meinl European Land, Immofinanz and other companies which allegedly were sold to individual customers as 'risk free' investments while their share price slumped in the financial crises. Several banks and most of the other intermediaries hold liability insurances, which leads to a stark increase in liability insurance cases.

Further certain Austrian banks were quite active in selling Madoff funds, hundreds of customers are now claiming that the banks should have checked Madoff's behaviour in detail before recommending his funds and should not have recommended such risky products at all, at least not to non high net-worth individuals. As several of those banks entered into Bankers Blanket Bonds this is a quite insurance related issue as well.

In addition, the public prosecutor is quite active during the last years, which led to dozens of D&O cases, although most of them are not publicly known. All members of Austria's fourth largest bank and their president were convicted for betrayal of confidence and misstatements in their balance sheet by the Criminal Court Vienna. Although this decision has been appealed and the proceeding is still pending at the Supreme Court, the first instance judge, Ms Bandion-Ortner, was recently appointed Austrian Minister of Justice. Further, the public prosecutor is currently examining certain actions of the (former) management boards of Immofinanz, Meinl European Land and Hypo-Alpe-Adria. The public and especially Investors seem to await the outcome anxiously; the same applies to insurance active in that area. In this regard one may highlight that it is publicly known that the former chairmen and new president of Meinl Bank AG had to put €100m in custody in order to avoid being imprisoned during investigation proceedings.

One may also mention that there is a (former) notary public who went bankrupt with unsatisfied claims of €117m. Allegedly the notary committed betrayal of confidence when disbursing funds he held in trust for certain banks which financed a real estate developer. As notary publics are obliged to hold PI insurance and there is in addition a fidelity insurance this case is consequently now an insurance dispute as all insurers refused to provide coverage.

Finally, the Austrian Supreme Court held that insurance broker's PI does not cover selling of US second hand policies as this is not an insurance business, but mere investment (which is excluded by the policy); the contrary legal opinion of one of the highest rated Austrian professors did not convince the Supreme Court.

Regulatory background

From a regulatory perspective the Austrian Insurance Supervision Act is the source of the most important regulations.

Licence

Generally speaking, the conduct of contractual insurance business in Austria requires an appropriate licence. Insurance companies may be divided into the following three categories:

1. Domestic insurance carriers: domestic companies, i.e., companies based in Austria, need a licence which is granted by the Financial Market Authority (FMA) in order to be able to conduct contractual insurance business: generally speaking the licence is valid in the whole European Economic Area.
2. Third country insurance: third country insurers should acquire a licence by the FMA in order to be able to conduct insurance business in Austria. After having been granted a licence, third country insurers are only allowed to the business in Austria by establishing a branch office. The business activities of the domestic branch office are supervised by the FMA.
3. EEA insurance carriers: insurance carriers based in other EEA countries do not require an additional licence in order to conduct insurance business in Austria. Nevertheless, they have to notify the intention of doing business in advance to their home country's supervisory authority. The home supervisory authority will then liaise with the FMA. EEA insurers generally speaking are placed under the supervision of the competent supervisory authority in their home country (principle supervision by the home country).

Licences are granted by the FMA separately for each insurance class. In each case, the licence refers to the entire insurance class unless the insurance undertaking has applied for a licence covering only parts of the risks belonging to the respective insurance class. The classification is given in Annex A to the Austrian Insurance Supervision Act.

Once granted, licences for insurance classes expire if operation has not been commenced within one year after the issue or renewal of the licence, or the operation has not been performed continuously for the duration of six months. Furthermore, the licence expires for insurance classes whose operation the insurance undertaking has waived or whose entire insurance portfolio has been transferred to other insurance undertakings.

Licences are revoked by the FMA if the conditions for the issue of the licence are no longer fulfilled.

Business requirements for Austrian insurance companies

As pointed out, the operation of the contractual insurance business requires a licence from the FMA. The licence for the operation of life assurance business and the licence for the operation of other insurance classes, with the exception of accident insurance and health insurance, are mutually exclusive. Affiliates are not subject to this exclusion.

Austrian insurance companies have to set up an internal auditing unit for the entire business (comprising at least two persons) that reports directly to the management and whose sole purpose is to continuously and comprehensively verify that the business and the operation of the insurance undertaking are lawfully, properly and expediently conducted. Furthermore, insurance companies have to maintain risk management as well as proper administration and accounting.

Financial status and investment restrictions

Insurers in Austria have to undertake to hold at any time own funds to the extent as specified in the VAG (at the very least, amounts that guarantee continued compliance with the obligations arising from the insurance contracts for the entire business). At the time of their computation, the own funds must be clear of any foreseeable tax liability. The Austrian provisions for the solvency margin also apply to branches of foreign undertakings (except for EEA or Swiss insurers).

Insurance undertakings have to establish a risk reserve which has to be shown separately on the balance sheet.

Austrian insurance companies must always place their funds in accordance with several technical provisions. Only assets that belong to certain categories within the limits stipulated under Art 22 Sec 1 and Sec 4 of Council Directive 92/49/EEC as well as Art 24 Sec 1 and Sec 4 of Council Directive 2002/83/EC are deemed as appropriate investment assets. If particularly significant reasons exit, the FMA can permit individual insurance undertakings to use assets which are not listed above.

Supervision

Domestic insurance undertakings: the FMA supervises all business practices of insurance undertakings to the extent of the granted licence.

EU/EEA insurers: insurance companies that conduct insurance business on a cross-border basis into Austria on the basis of a European Passport are subject to home supervision.

Non-EU/EEA insurers: insurers that solicit insurance business in Austria and have been granted a licence by the FMA, including insurers controlled by parent companies domiciled outside the EU/EEA, are subject to the supervision of the FMA.

Taxation

With regard to corporation tax, insurance companies compute their income according to the same principles as other corporations. The corporation tax rate is 25%. The premiums paid by the insured persons to the insurance companies are taxable, and the insurance capital paid out to insured persons is deductible from the tax base, unless a provision has been made beforehand. However, according to a special provision in section 17 of the Corporation Tax Act, insurance companies have to pay tax on at least 20% of their earnings before deduction of payments to insured persons.

The Austrian Corporation Tax Act states in sections 15-17 special rules for insurance companies. Provisions made for the fulfilment of obligations are deductible to the extent that these provisions are necessary according to actuarial principles. Provisions for long-term obligations are deductible only to a certain extent. The disbursement of earnings to insured persons in the context of premium-payback programmes is deductible under certain conditions, as are provisions for these purposes.

In Austria certain insurance premiums paid by private individuals are tax deductible as special expenses at the level of the insured person (*Sonderausgaben*).

Payments from insurance companies to private individuals may be taxable income at the level of the private individual, on the other hand, if the payments fall under the scope of section 27 of the Income Tax Act (capital income). This applies mainly to life insurance and pension payments from insurance companies to private individuals.

Insurance companies are exempt from Value Added Tax, which means that premiums paid to insurance companies are not subject to VAT. However, the insurance company is not allowed to deduct input tax on services rendered to them.

Foreign insurance companies that have neither their seat nor their office in Austria are only subject to limited corporation tax liability in Austria. With regard to limited tax liability, income is only taxed if the income of the corporation has a genuine link to Austria. Income derived from insurance business is taxable if it is part of Austrian business income. Income from a business activity is regarded as Austrian business income (and therefore taxable) if the entity has a permanent establishment or a permanent representative in Austria.

A permanent establishment means fixed assets located in Austria by means of which the business activity is carried out. A permanent representative means a person or entity that serves as an intermediary for the foreign entity to carry out business activity in Austria. The income of a foreign insurance company is computed according to the same rules that apply to domestic insurance companies.

Foreign insurance companies that have no permanent establishment and no permanent representative in Austria are not taxable on their insurance business income, but may be liable for tax following the disposal of real estate located in Austria, or on the disposal of shares of Austrian companies or from any other income which has a genuine link to Austria according to section 98 of the Income Tax Act. However, Austria has concluded tax treaties with (currently) about 70 countries, which may apply to the individual case and may reduce the Austrian tax liabilities of foreign companies.

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