

AIDA Questionnaire on the Corporate Governance of Insurers

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I. General

1. In your jurisdiction, what corporate governance models are available to insurance companies? In case multiple models are available, describe the main differences and the allocation of management and monitoring powers among the relevant bodies/committees and which model is generally or ideally adopted by insurance companies.

In Austria, only certain legal forms are eligible for insurance companies. According to § 8 para 1 Insurance Supervision Act (VAG), insurance companies can only be established as stock company (Aktiengesellschaft), *societas europaea* or mutual insurance (Versicherungsverein auf Gegenseitigkeit). In the stock company and *societas europaea*, the management board is basically independent from the shareholders, but constantly monitored by the supervisory board (§ 70 para 1 Stock Company Act, AktG). The same rules apply for mutual insurances (§ 49 para 1 VAG). Furthermore, insurance companies can be established as public-law institutions through corresponding legal acts. Public-law institutions are typically governed by an executive board that is independent from the members of the corporation but under state supervision. In our view, the stock company should ideally be adopted by private insurance companies that are profit-oriented.

2. What are the main sources of regulation addressing corporate governance of companies (and in particular of insurance companies)? e.g., statutes, regulations, other rules/recommendations issued by national and supranational supervisors/regulators, self-regulation, codes of best practice, codes of ethics.

The sources of regulation addressing corporate governance are generally the applicable corporate (i.e. Austrian Corporations Act - AktG) and, more specific, insurance laws (i.e. Austrian insurance supervision act – VAG) as well as regulation acts such as ordinances and codes by the supervisory authority. Further sources of regulation can be found in the Austrian Corporate Governance Code as well as in regulations and directives of the EU, such as Regulation (EU) 1286/2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs), Regulation (EU) 537/2014 on specific requirements regarding statutory audit of public-interest entities, Commission Implementing Regulation (EU) 2017/1469 – laying down a standardized

presentation format for the insurance product information document, Commission Implementing Regulation (EU) 2017/1421 – laying down technical information for the calculation of technical provisions and basic own funds for reporting, Commission Implementing Regulation (EU) 2016/1800 – allocation of credit assessments of external credit assessment institutions to an objective scale of credit quality steps, Commission Implementing Regulation (EU) 2016/467 amending Commission Delegated Regulation (EU) 2015/35 concerning the calculation of regulatory capital requirements for several categories of assets held by insurance and reinsurance undertakings, Directive (EU) 2016/97 on insurance distribution, Directive 2014/56/EU amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts, Directive 2009/138/EC on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) or Directive 2009/103/EC relating to insurance against civil liability in respect of the use of motor vehicles, and the enforcement of the obligation to insure against such liability.

3. In your jurisdiction, are you aware of any insolvency or distress of an insurer directly attributable to poor corporate governance standards or practices or failure to adequately implement and apply such principles? If so, please identify the main triggers of the insolvency.

No.

4. In your jurisdiction, is corporate governance regulation applied according to the nature, scale and complexity of an insurer's business? If yes, please describe any significant differences and rationale for the differences.

There are differences depending on the nature (private insurance company vs. public-law institution, see above as to the applicable regulations) as well as the complexity and size of insurance companies, e.g. derogations for smaller mutual insurance/insurance companies regarding risk management and compliance. For instance, small insurance companies must provide for a "proper administration and accounting", as well as "appropriate internal control procedures" to ensure that developments which can jeopardize the permanent fulfillment of obligations under the insurance contracts are recognized as early as possible, whereas bigger insurance companies must establish an "effective internal control system", which at least must include management and accounting procedures, an internal control framework, an appropriate reporting system at all levels of the company, and a compliance function (in detail, see §§ 68 ff, 82 ff VAG).

5. Please provide specific examples of corporate governance structures and practices that are better implemented through self-regulation rather than through legal or supervisory

requirements.

Apart from the Corporate Governance Code which is voluntary as far as it does not recite statutory law there are none in Austria as far as we know.

6. In case your jurisdiction was recently requested to implement domestically certain corporate governance principles set forth by supranational regulations, describe the main obstacles and problems (if any) that resulted from such process.

Austria was most recently requested to apply/implement EU regulations/directives, such as Commission Implementing Regulation (EU) 2017/1469 – laying down a standardized presentation format for the insurance product information document, Commission Delegated Regulation (EU) 2017/653 supplementing Regulation (EU) No 1286/2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs) or Directive 2009/138/EC on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II). The main obstacles for insurance companies were related to increased regulatory requirements, legal restrictions, further requirements for insurance products and stricter capital requirements as well as the costs resulting from implementation. Due to tighter regulations, many insurers had to increase their financial reserves while investing more in risk management expertise, encompassing counter-terrorism, climate change and cyber-attacks.

7. Are there any significant differences between general corporate governance rules and the specific rules governing insurance companies?

Rules governing insurance companies contain specific provisions with regard to the business model and the activities of insurance companies, e.g. provisions for general governance, risk management, compliance, solvability monitoring and actuary operations. For example, insurance and reinsurance companies have to issue and implement written guidelines at least in the areas of risk management, internal controlling, internal revision, remunerations and, if applicable, outsourcing operations (§ 107 para 3 VAG). In addition, insurance companies must take appropriate precautions and develop emergency plans to ensure the continuity and regularity of their activities. For this purpose, appropriate and proportionate systems, procedures and resources shall be used (§ 107 para 4 VAG). Insurance companies must establish specific functions/divisions for risk management, compliance, internal revision and actuary operations (§ 108 para 1 VAG). They must set up an effective risk management system that includes all strategies, processes and reporting procedures necessary to measure, monitor, manage and report incoming and potential risks on a single and aggregated basis of the business as

well as the dependencies between these risks (§ 110 para 1 VAG). The risk management system/division shall be effective and has to be integrated in the organizational structure and decision-making processes of the insurance company while consulting the persons who effectively lead the company or hold key positions. It has to cover the risks that must be included in the calculation of the solvency capital requirement as well as the risks that are not fully covered by this calculation, but at least the areas of risk modeling and provisioning, asset-liability management, investments, in particular derivatives and similar obligations, liquidity and concentration management, management of operational risks and reinsurance and other risk mitigation techniques (§ 110 para 2 VAG). Insurance companies also have to carry out company-specific risk and solvency assessments within their risk management framework. This has to be an integral part of the business strategy and incorporated in strategic decisions (§ 111 para 1 VAG). The insurance companies' compliance division has to advise the management board regarding compliance with the rules governing the operation of the company, assess the possible effects of changes in the legal framework on the activities of the insurance company as well as identify and assess the risk associated with non-compliance with the legal requirements (§ 118 VAG). In addition, insurance and reinsurance companies must implement an effective division in the field of insurance mathematics encompassing specific actuary operations referred to in the VAG (§ 113 para 1 VAG).

II. Fitness and Propriety of Board Directors

1. Are there any laws or regulations already adopted or any proposals in your jurisdiction, relating to the qualification and composition of board directors in an insurance company? If so, please explain.

Members of the executive board have to meet certain functional and personal qualifications. In particular, at least two members of the management board must have sufficient knowledge and experience in the insurance business as well as management skills, which can be assumed if the board member proves to have at least three years of senior management experience with an insurance or reinsurance company of comparable size and type. Where managing directors are not members of the management board (this only applies to the *societas europeae*), this requirement must be met by at least one member of the board and at least one managing director; for other board members or directors, knowledge and experience in other fields that are essential for the operation of the insurance business as well as a senior position in corresponding enterprises are sufficient. Furthermore, at least one member of the management board has to speak German; if managing directors are not members of the board (*societas europeae*), at least one of them has to speak German as well.

Board members must also be personally reliable and trustworthy. They are not allowed to engage in any activity which is likely to affect the proper management of the insurance or reinsurance company. They may not exercise any main profession outside insurance, banking, pension funds businesses, payment institutions, e-money institutions, securities companies or securities service companies (§ 120 VAG).

2. In your opinion, what factors, conditions, or incentives might weaken the independence of the board of directors or individual members of the board?

Short sighted remuneration plans that only focus on share-price might weaken the independence of the board as well as certain privileges for intra-group investments.

3. How does an insurance company ensure that individual board members and the board collectively have enough knowledge to monitor and oversee the activities of the insurer appropriately, particularly where specific expertise is needed?

Insurance companies must meet the requirements laid down by the applicable law and seek approval by the supervisory authority that monitors board members: According to § 120 para 1 VAG, insurance and reinsurance companies must ensure that all persons who manage the company or have governance or other key functions have sufficient professional qualifications, knowledge and experience to ensure sound and cautious management, and are personally reliable and trustworthy, at all times. Additionally, insurance companies must notify the supervisory authority when they intend to appoint members of the managing board no later than one month prior to the appointment. The insurance company must provide all the documents necessary to assess professional and personal qualifications of the board members. If the authority has reasonable doubts concerning the fulfillment of professional qualification or personal reliability, the authority shall object the appointment and require other suitable persons to be appointed. The same rules apply if reasonable doubts arise after board members have been appointed, or in case the requirements are no longer met or the persons are no longer able to perform their tasks properly. The insurance company is obliged to notify the supervisory authority in case requirements are no longer met (§ 122 VAG). Pursuant to § 123 VAG, members of the supervisory board must also prove to have professional and personal qualifications and the supervisory authority must be notified when members of the supervisory board are appointed or retiring.

4. Are there significant differences in terms of requirements and duties between executive and non-executive members of the board of directors of an insurer?

The requirements and duties are typically stricter for executive members

of the board. While executive members of the board/managing directors must meet the requirements pointed out in section II.1. of this questionnaire (§ 120 VAG), non-executive members/members of the supervisory board are only required to have professional and personal qualifications pursuant to § 123 VAG, that is sufficient professional qualification, knowledge and experience as well as personal reliability and integrity in order to be able to supervise the managing board.

5. In your jurisdiction are there any black letter rules or general principles that enable directors to rely upon external opinions when addressing issues or aspects where specific expertise is needed?

In general, the managing board of the insurance or reinsurance company is responsible for complying with the rules applicable to the operation of the insurance business as well as with the recognized principles of a proper business operation (§ 106 VAG). Furthermore, insurance companies must establish an effective governance system that ensures sound and prudent corporate management and is appropriate to the nature, scale and complexity of the business. An internal review of the governance system is to be carried out on a regular basis (§ 107 VAG). In case the insurance undertaking is based on a stock company, the corresponding rules of the stock company act (AktG) impose that members of the managing board must apply the diligence of a duly and conscientious manager in their management (§ 84 para 1 AktG). This standard of diligence for the members of the managing board is accompanied by the business judgement rule as set out in § 84 para 1a AktG: In any event, a member of the managing board is complying with the diligence of a duly and conscientious manager if he is not guided by misleading interests and his decision is based on appropriate information so that he can assume to act in the company's best interest.

The Supreme Court of Austria (OGH) has addressed black letter rules and principles that enable directors to rely upon external opinions on several occasions. According to the OGH, members of the managing board can only rely on expert opinions if this opinion is obtained from a reliable, objectively competent source that has been informed comprehensively about all the facts necessary (legal proposition RS0089613). In the decision 6 Ob 198/15h, the OGH additionally pointed out that an expert opinion can only be reliable if the request of the managing board was formulated openly; mere subjective opinions in favor of the client are not sufficient, whereas an extremely low or high level of the opinion's fee may indicate a lack of seriousness. The OGH summarized that a strict criterion is to be applied in order to assess a potential legal error of managers, since everyone is obliged to obtain knowledge of the laws which govern him according to his life. Finally, members of the managing board relying on expert opinions that are not meeting the

requirements mentioned above and causing damage to the company by this may potentially be culpable for committing a breach of trust or embezzlement.

6. Describe the extent and scope of supervisors'/regulators' intervention with reference to the qualifications and to the activities of the board of an insurer.

The supervisory authority is entitled to enact ordinances in order to specify functional and/or personal qualifications of board members. The supervisory authority is also entitled to request documents to verify the board member's qualifications (§ 120 para 5 VAG). According to § 122 para 2 VAG, the supervisory authority is entitled to request the appointment of other suitable persons in the event that reasonable doubts arise after board members have been appointed, or in case the requirements are no longer met or the persons are no longer able to perform their tasks properly. The insurance company is obliged to notify the supervisory authority in case requirements are no longer met or managers are resigning.

7. Are there any special rules and regimes applicable to the governance of subsidiaries belonging to an insurance group, also in terms of information flows?

Insurance groups must implement adequate measures to monitor the solvability and risk situation of the subsidiaries and the group as a whole constantly. For this purpose, insurance groups are obliged to adopt efficient reporting systems and board members must meet the same qualifications as the subsidiary's board: Pursuant to § 222 para 1 VAG, the rules concerning governance of single insurance undertakings also apply on a group level. Moreover, the insurance group must establish internal control mechanisms including appropriate mechanisms for the group's solvency situation that enable it to recognize and measure all material risks and to adequately hedge them with equity, as well as proper reporting and accounting procedures to monitor and manage intra-group transactions and risk concentration (§ 223 VAG). The risk and solvency assessments required from insurance undertakings must also be carried out at group level (§ 224 para 1 VAG). Insurance holding companies and mixed financial holding companies domiciled in Austria must ensure that persons who effectively manage the business of an insurance holding company or a mixed financial holding company have the necessary professional qualifications and personal reliability to perform their duties. The rules concerning the skills and qualifications of the subsidiary's board apply analogously (§ 225 para 1 VAG).

III. Risk Management

1. In your opinion, what is the biggest risk challenge (e.g. regulation, capital standard, pricing, interest rate, cyber, terrorism, etc.) facing the insurance industry today in your jurisdiction?

The insurance industry is currently facing several risk challenges, in particular stricter regulation and capital requirements, increasing costs of implementing new regulations, market volatility and increasing risks related to cyber-attacks, climate change and terrorism, low interest rates, increasing competition in the industry as well as increasing digitization of the insurance business.

2. What specific laws or regulations, actual or pending in your jurisdiction, will present significant implementation risk challenge toward the insurance industry?

In our view, implementation of the Insurance Distribution Directive (directive [EU] 2016/97, IDD) and application of new rules concerning insurance distribution as from 23 February 2018 pose significant risk challenges toward the insurance industry. The directive primarily aims at promoting transparency throughout the business in order to satisfy consumers' and retail investors' needs. For example, the IDD imposes stricter regulation on insurance distribution in regard to the price and the costs of insurance products as well as concerning remuneration/incentives of distributors related to their sales, standardized information for non-life insurance products (through a standardized insurance product information document, IPID), new regulation on insurance products that are offered in a package and general rules on transparency and business conduct of distributors to prevent consumers from buying products that do not meet their needs. These rules also apply when a product is bought directly from an insurance company, and not only (as in the past) when products are bought via intermediaries such as agents or brokers. The IDD applies from 22 February 2016. EU countries have to incorporate it into national law by 23 February 2018.

IV. Ethics and Corporate Social Responsibility

1. Please provide any concrete examples where business ethical standards and/or corporate social responsibility standards have been applied and have changed the behaviors of the insurance company.

As far as we know there is only a code of ethics in place for public social security insurance regarding anti-corruption and anti-bribery. This has led to an increase of standards in these areas. However, these rules have been largely implemented in Austrian criminal law by now so that they apply for all companies and cannot be qualified as a (mere) business standard.

2. In your jurisdiction, are there any specific laws or regulations already adopted or any proposals, or any arrangements in place in the governance system, relating to the protection of policyholders' and/or financial consumers' interests?

The Insurance Distribution Directive (directive [EU] 2016/97, IDD) referred to above imposes new standards related to the protection

of policyholders and consumer's interests. EU countries have to transpose it into national law by 23 February 2018. Besides, consumers are entitled to withdraw from the insurance contract without giving reasons within 14 days after being informed about the right to withdraw by the insurance company (§ 5c Insurance Contract Act, VersVG). Furthermore, consumers concluding an insurance contract of more than 3 years are entitled to quit the contract once a year after the first 3 years have passed (§ 8 para 3 VersVG). §§ 252 ff Insurance Supervision Act (VAG) contain specific information duties for insurance companies to policyholders, including the obligation to inform about the name, address of the registered office and legal form of the insurance undertaking, the law applicable to the contract, the name and address of the supervisory authority responsible for the company and, where appropriate, a body to which the complaints relating to the insurance contract may be addressed, the term of the insurance contract, the method and period of payment and the circumstances under which the policyholder may revoke or withdraw the insurance contract if applicable. According to §§ 3 and 3a Consumer Protection Act (KSchG), consumers are entitled to withdraw from the contract within 14 days if the contract was neither concluded in a permanently used office of the insurance company nor at a fair or market stand and within 7 days if certain essential circumstances for the contract which according to the company are likely to occur, do not occur, or only to a much lesser extent. Pursuant to § 8 Remote Financial Services Act (FernFinG), consumers are entitled to withdraw from a remotely concluded contract (via telecommunication) within 14 days (life insurance) or 30 days (retirement insurance) after the contract has been concluded or the consumer has been informed that the contract has been successfully concluded (life insurance).

3. In your jurisdiction, is an insurance company required to produce an annual Corporate Social Responsibility (CSR) report or a Global Sustainability Initiative (GSI) report? If so, what context needed to be disclosed in these reports?

Following the directive 2014/95/EU of the European Parliament and the Council, the Austrian legislator transposed the requirement to produce such reports into national law by December 6, 2016. According to § 243b Austrian Commercial Code (UGB), large capital corporations of public interest with more than 500 employees on an annual average have to include a non-financial statement in their annual reports. This statement shall include the information necessary to understand the course of the business, the business results, the situation of the company and the effects of its activities and shall be based at least on environmental, social and workers' concerns, on respect for human rights as well as on combating corruption and bribery. The analysis shall explain the non-financial performance indicators in relation to the amounts and

information disclosed in the annual reports.

V. Disclosure

1. In your opinion, what mechanisms shall be in place or considered in an insurance company to ensure the transparency of its governance structure? (e.g., the articles of association, the organization chart, any existing committees, the major shareholders, the ethical standard, corporate social responsibility, etc.)

A strong supervisory board, responsibility to the shareholders and a profound reporting system, including ethical and social topics as named above.

For public disclosure the articles of association could be disclosed but it would still be possible to state more sensitive matters in other statutes/contracts between the shareholders.

It would seem sensible to annually disclose any insurance payments to managers of the company as well as the payment policy of the insurance company as a whole. In this respect committees might also have a positive aspect on governance.

Disclosing the organizational chart might be problematic as it often contains business secrets of the company.

2. Are there any governance practices that, in your opinion, can best be achieved through disclosure rather than through specific supervisory requirements? Which governance practices should be mandatory for an insurance company?

We believe the best approach to efficient and reliable governance practices encompasses both, transparency and supervision. Having an Ombudsmann can be positive and the factors that are relevant for the managers' remuneration should also be disclosed.

3. What is the interplay between market abuse regulations and other disclosure/transparency rules applicable to listed insurers and industry specific rules applicable only to insurance companies?

According to the IDD all violations of the relevant laws will be published on the supervisory authority's homepage together with the name of the person. This will automatically lead to the person not being able to continue working in a top-level management position in the industry.

VI. Outlook

In respect of the corporate governance of insurers, please describe your criticisms on the system in your jurisdiction, any recommendations for the future, and/or the main challenges which insurance undertakings encountered.

The interplay of ever stricter capital requirements together with tougher

consumer protection rules and pricing competition makes for a very difficult situation on the insurance market right now. This will lead to the disappearance of smaller more specialized companies and could lead to gaps that will not be filled by bigger players.