The Problematic Regime of "Fronting" in Angolan Insurance and Reinsurance Law – Assessment in Comparison with Africa Re, and the Approaches in Macau and Brazil

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Abstract: A new Angolan legal framework for insurance and reinsurance activity recently entered into force to improve the previous regime through the introduction of innovative insurance solutions, improve insurance regulation and supervision, harmonise legal concepts, and integrate into its scope the substantive sanctioning regime for the insurance business. Among various new regulated matters, it approves a fronting regime, which allows insurance companies to underwrite insurance policies and place 100% of the assumed risk in the international reinsurance market.

This article will evaluate the fronting regime and its likely effects on the Angolan insurance industry in light of the regulatory purposes, while making comparisons to other African and international perspectives on this subject matter. This paper will argue that the current fronting regime does not accomplish some of its main goals: fostering national financial growth and building technical capacity. The paper will conclude with some suggestions for improving the fronting regime.

I. INTRODUCTION

The Angolan Insurance and Reinsurance Activity Law ("LASR")[1] recently entered into force providing the Angolan insurance industry with an innovative regulatory framework, which aims to be aligned with international standards and principles. The main objectives of LASR are to promote policyholder protection, healthy competition, financial growth and stability, and to build technical capacity. Among new regulated matters, it aproves a fronting regime in the reinsurance section.[2] The fronting regime allows insurance companies to act as front companies for reinsurers, except in health or motor insurance transactions. While the modernisation of the legislation may be virtuous, the way fronting is regulated may at the same time represent a threat to its effectiveness.

This paper first discusses the definition of reinsurance and fronting and its nature in Part I. Part II then explores the main provisions of LASR and its objectives, considering the best international principles and standards, given the recommendations from the Committee of Insurance, Securities, and Non-Banking Financial Authorities

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I dedicate this piece of research to my beloved father in memory, Victor Manuel, and to my beloved mother, Felícia Cafundi Manuel, who dedicated their whole lives to ensuring that I could strive and succeed in this challenging world.

[1] See Law nº 18/22, 7th of July, the Insurance and Reinsurance Activity Law at https://www.arseg.ao/legislacao/legislacao-do-mercado/leis-e-decretos/ (last accessed 06 September 2022).

[2] Ibid. See article 137.

(CISNA), the International Association of Insurance Supervisors (IAIS), and the International Organization of Pension Supervisors (IOPS), while also considering to what extent the new Angolan law has adopted concepts from the EU Solvency II Directive[3], and from the UK approach to prudential regulation. Part III provides an evaluation on whether the fronting regime is aligned with the objectives of the reform and the implementation in the insurance industry of an effective risk-based management system. Part IV gives a comparative perspective by reference to case studies of Africa Re, and the fronting regimes in Macau and Brazil. Part V makes some suggestions as to how the new LASR fronting regime could be adjusted to guarantee more effectively the necessary alignment to its objectives.

1. Definition of Reinsurance and Fronting

According to LASR, "Reinsurance" means the contract whereby an insurance undertaking insures, in turn, part of the risks which it underwrites, and the activity consisting in accepting risks ceded by an insurance or reinsurance undertaking, or by an insurance or reinsurance undertaking of a foreign country.[4] Reinsurance is the insurance of insurance companies.[5] Under a contract of reinsurance, the reinsured, which is the direct insurer of the original subject-matter under the underlying insurance contract, transfers, part or all of its risk to the reinsurer. In return for premium payment, the reinsurer undertakes to indemnify the reinsured for losses that fall within the scope of the reinsurance contract. Although the underlying insurance contract is usually in force before the reinsurance is placed in facultative placements, because in this arrangement the policy is usually concerned with the placement of a single risk, in treaty reinsurance, which aims to put in place a prospective reinsurance program for specified risks, the treaty may be in place even before the underlying insurance contracts are formed.[6]

Where the whole risk accepted under the underlying contract is transferred under a contract of reinsurance, the arrangement is known as fronting, as the insurer acts in this situation as a mere pass-through vehicle as a 'front' – to the reinsurer.[7] In essence, an insurance carrier issues an insurance contract and afterwards transfers 100% of the risk to a reinsurance carrier. This reinsurance carrier is usually not licensed in the jurisdiction where the front carrier operates. In a perfect fronting arrangement, policies are issued by a home jurisdiction-licensed insurance company and then completely reinsured to a reinsunrer who is not licensed in that jurisdiction. Typically, the fronting insurer issues policies on behalf of the reinsurer, and the reinsurer administers all claims under the reinsurance agreement.[8] Frequently, the reinsurer controls the claims handling process, including the settlement of the underlying claims, behind the scene.

Thus, fronting is a mechanism through which a carrier can effectively operate in an insurance market in which it is not licensed to write business directly.

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[3] Directive 138/2009/EC.
[4] See n 1, Article 3 and paragraph 41 of the annex.
[5] *Travellers Casualty & Surety Co of Europe Ltd v Commissioners of Customs and Excise* [2006] Lloyd's Rep IR 63, [43] and [57]. See also Merkin, R. Colinvaux's Law of Insurance (11th edn, Sweet & Maxwell 2016). Chapter 17, para 17–001.
[6] See *Crane v Hannover Rückversicherungs AG* [2008] EWHC 3165 (Comm).
[7] Ozlem Gurses, Marine Insurance Law (2016), Reinsurance, Chapter 15, 326.
[8] Reliance Ins. Co. v. Shriver, Inc., 224 F.3d 641, 643 (7th Cir. 2000).

The LASR defines a fronting transaction as the business accepted by an entity qualified to carry on insurance business (cedant), with the prior intention of passing it totally or substantially to another insurance or reinsurance company (cessionary).[9]

Holzheu perceives fronting as an alternative risk transfer, i.e. a specialised form of reinsurance often used in the captive insurance market.[10] He considers that, generally, a fronting insurance company, licensed in the country of location of the insured risk, issues the insurance policy, and cedes the entire premium obtained to the captive,[11] via a reinsurance policy, known as a fronting agreement.[12]

To this extent, a fronting reinsurance contract is reinsurance on its own terms, as there is a transfer of the whole or a substantial amount of the risk accepted under the underlying insurance policy to a reinsurance carrier or a captive insurer, so it operates in the same fashion as traditional reinsurance. What makes fronting a special reinsurance arrangement is that the underlying insurance carrier act as a mere pass-through vehicle to the reinsurance company.

2. Nature of Reinsurance and Application to Fronting

Courts and commentators have been debating whether the nature of reinsurance is the indemnification of the reinsured's liability under the underlying insurance contract (the indemnity view)[13], or the reinsurance of the underlying subject-matter in accordance with the terms of the reinsurance contract (the further insurance view).[14]

In *Vesta v Butcher*[15], the House of Lords, adopting the indemnity view, held that in proportional reinsurance[16] on the same terms as the underlying insurance contracts, there is a presumption that the parties intended the reinsurance to be back-to-back (indemnity view). In contrast, in *AXA Reinsurance (UK) Ltd v Field*[17], Lord Mustill rejected such a presumption in relation to non-proportional reinsurance,[18] it being clear that "the elements of the

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[9] See n 1, Article 3, and paragraph 26 of the annex.
[10] Thomas Holzheu, 'Alternative Risk Transfer Products (ART)', in *Reinsurance: Fundamentals and New Challenges* 113, 117 (Ruth Gastel ed., 4th ed. 2004).
[11] Ibid. A captive insurance or reinsurance company has been "more usefully described as an insurer writing risks of limited origin or where access to cover is restricted."
[12] Ibid.
[13] *Vesta v Butcher* [1989] AC 852. See also Terry O'Neill, Jan Woloniecki, Franziska Arnold-Dwyer, *The Law of Reinsurance* (5th edn, Sweet & Maxwell, 2019), para 5-002.
[14] *Wasa International Insurance Co Ltd v Lexington Insurance Co and AGF Insurance Ltd* [2009] UKHL 40. See also O'Neill et al. (n 13), para 5-002.
[15] See n 13.
[16] In proportional reinsurance, the reinsured and the reinsurer share premiums and losses by a ratio or percentage set in the reinsurance contract, however, the reinsurer receives a smaller premium compared to the risk it assumes, taking into account that the premium received by the reinsurer, is net of the brokerage commission, paid to the intermediary, and a ceding commission paid to the reinsured. See O'Neill et al. (n 13), para 1-015. For instance, assuming the reinsured underwrote 30% of the original premium, the insurer can then claim 30% of the losses from the reinsurer in the event of a claim.
[17] *AXA Reinsurance (UK) Ltd v Field* [1996] 2 Lloyd's Rep. 233.
[18] In non-proportional reinsurance, the reinsured cedes a layer or horizontal slice of the risk, "which will be calculated not (only) as a proportion of the reinsured's premium equivalent to the proportion of the risk the reinsurer assumes, but (also) by reference to what part of the risk he assumes." Insurers may namely reinsure the "first loss", or "excess of loss". For example, assuming that an insurance company insures a policyholder against loss up to a limit of £200, that company may reinsure out any loss it has to pay from zero to £100, which would be a "first loss" reinsurance. See n 16, para 1-065. If the company reinsures out any loss it has to pay

prudent underwriter's judgment when writing policies of this kind" do not have to be equal to the "underlying" policy wording. In *Wasa International Insurance*,[19] concerning a proportional reinsurance contract, the House of Lords held that a reinsurance contract is an independent and separate contract which must be construed on its own terms and conditions (the further insurance view) and which only indemnifies the reinsured for its own liability under the underlying insurance contract to the extent that it falls within the terms of the reinsurance contract adequately construed.

Applying the *Wasa* analysis to fronting arrangements, it can be argued that the underlying insurance and the fronting reinsurance contracts are two distinct and independent contracts. Legally, they must be construed on their respective terms and conditions. Commercially, they are symbiotic and designed to transfer the whole risk.

However, it is worth mentioning that in fronting arrangements in the captive insurance market, despite the existence of the original insurance policy, "the risk of that coverage remains with the captive insurance company" in economic terms.[20] Additionally, the difference between the fronting arrangements in the traditional reinsurance industry and in the captive reinsurance marketplace is that in the latter a corporation or a group business owns a reinsurance carrier, a captive, which then insures its owner's risks, that is, the captive reinsurance carrier underwrites "risks that are of limited origin or where access to coverage is restricted".[21] Eventually, it may be considered that, commercially, a cut-through clause is not needed to allow direct claims by the corporation or a company of the group business against its captive reinsurance company, given the referred ownership.

Thus, it may be said that this position seems to technically collide with the thesis that the insurance contract and the fronting reinsurance contract constitute independent and separate contracts. Nevertheless, although the main commercial rationale for the existence of the captive reinsurer is to re/insure its parents,[22] legally, there is no privity of contract with regard to the pure reinsurance transaction between the captive reinsurer and its parents, i.e. the underlying insured, since there is still an insurance policy issued to the latter by the front insurance company, on the one hand, and a reinsurance contract between the front insurer and the captive reinsurer, on the other hand. In this sense, even in the captive reinsurance marketplace the insurance contract and the fronting reinsurance contract are two separate and independent contracts.

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from £100 to £200 which would be excess of loss, losses to the extent they exceed £100 but only up to £200 are paid by the reinsurer.

[19] See n 14.

[20] See n 10.

[21] See n 11.

[22] See n 10.

II. THE ANGOLAN INSURANCE INDUSTRY NEW LEGAL FRAMEWORK

1 The Rationale for the New Legal Regime

The LASR was enacted on 7 July 2022.[23] The Rationale Report for the Law Proposal on Insurance and Reinsurance Activity considered that the previous Law[24] was vital for the Angolan financial sector's development, in particular for the insurance industry, as it would be a channel to introduce private entities to the insurance activity.[25] Consequently, having already fulfilled its mission and two decades after its publication, it would be essential to change and reformulate the regime, giving a new impetus to the insurance activity.[26]

Nonetheless, it could be argued that the previous model was not globally tested, it was not put under enough stress to safely conclude that its regulatory measures were right or wrong. Taking into account the incipient level of market development, it could have been wise to opt for amending the General Law of Insurance Activity.[27]

The introduction of a new insurance legal framework was motivated by the need to align the Angolan insurance market to international practices and standards, while also ensuring adequate legal alignment of the insurance market with the banking and securities, and derivatives markets.[28]

In addition to CISNA,[29] Angola has recently acceded to IAIS[30] and IOPS,[31] showing that the Angolan Government, through the Angolan Agency for Insurance Regulation and Supervision (ARSEG), is interested in positioning itself in the context of nations and, therefore, in the context of best international practices regarding insurance regulation and supervision.

2 Some Main Changes and Innovations

Undoubtedly, the LASR has strengthened supervisory powers, and introduced greater regulatory independence, in the sense that ARSEG no longer depends on governmental superintendence to comply with its mandate.[32] For example, under the previous (revoked) law, the power to authorise entities to conduct insurance activities lay with the Ministry of Finance, under the prior opinion of ARSEG.[33] Under, the previous regime the Ministry of Fincance was responsible for the coordination and supervision of the insurance market, while ARSEG was responsible for

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[23] See n 1.
[24] See Law nº 1/00, 3rd February, General Law of Insurance and Reinsurance Activity at https://www.minfin.gov.ao/PortalMinfin/#!/legislacao/legislacao-sobre-o-sector-de-seguros (last accessed 07 September 2022).
[25] See The Rationale Report of the Bill of Insurance and Reinsurance Activity, 6 at https://owa.arseg.ao/api/v1/public/download?f=QsGRL8hOi%2BmrHWkNXbMq8AA2FyOPPw6mbnncd1%2BJXohhmu273%2F8HMjRmcAbEK5aXpQU9hIxAtV9GkmFPydKFe1WkHiZaNNnDKYzkNOwCg08%3D (last accessed 28 August 2022).
[26] Ibid.
[27] See n 24.
[28] See n 25.
[29] See http://cisna.net/ (last accessed 29 August 2022).
[30] See https://www.iaisweb.org/about-the-iais/iais-members/ (last accessed 29 August 2022).
[31] See http://www.iopsweb.org/membership/iopsmembers-observers.htm (last accessed 29 August 2022).
[32] See n 1, articles 9, 10, e) and 23, paragraphs 2 and 3.
[33] See n 24, article 3, paragraph 2.

implementation.[34] In essence, the ARSEG was dependent upon the governmental intervention to make relevant decisions relating to its mandate. Arguably, that arrangement was unfavorable to the development of the insurance sector and did not reflect the best practices of regulation and supervision, not only because the Ministery of Finance is not a specialized supervisory body, but also because ARSEG did not have the necessary autonomy and independence to fulfil its objectives without policy-driven interference.

The LASR also gives foreign companies access to the Angolan insurance market by way of setting up branches. One might ask whether it would be opportune to open the market, however, the entry of new insurers into the Angolan insurance market can be very valuable, as in addition to increasing its underwriting capacity, it can bring know-how, as long as the market attracts insurers with the relevant experience.[35]

The governance model and risk management systems introduce greater rigour. Therefore, rules of fitness and propriety or other qualifications tests have been established.[36] This means that companies will have to put in place a "fit and proper" guide for assessing the adequacy of members of management and supervisory bodies of supervised institutions. Insurance companies cannot operate without complying with these rules.[37]

The regime also introduces dedicated key functions, such as Risk Management, Internal Audit and Compliance, Internal Control, and Actuarial.[38] These are in line with the IAIS Core Principles. In effect, the supervisor requires an insurer to have, under the corporate governance framework, effective systems of risk management and internal controls, including effective functions for risk management, compliance, actuarial matters, and internal audit.[39] These functions to an extent correspond to Pillar II of EU's Solvency II Directive (SIIDir), treated as qualitative requirements to deal with risks not considered in Pillar I, which is related to minimum capital and solvency requirements. Pillar II includes the Own Risk and Solvency Assessment (ORSA) as part of the risk management system for insurers, which must be an integral part of the insurer's business strategy and it must take the ORSA into account on an ongoing basis in its strategic decisions, and insurers must inform the regulators of the results of each ORSA as part of their reporting obligations in Europe.[40] It is worth mentioning that Solvency II was put in place to address the issue of the capital requirements of Solvency I which was "purely quantitative", essentially not risk-based, and not sophisticated enough.[41]

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[34] Ibid, articles 10, 11, paragraph 1. See also article 4, paragraph 1 of the Organic Statute of ARSEG, approved by the Presidential Decree 141/13, 27th September at https://www.minfin.gov.ao/PortalMinfin/#!/legislacao/legislacao-sobre-o-sector-de-seguros (last accessed 07 September 2022).

[35] See n 1, article 41, paragraph 1. It determines a minimum of 5 years of incorporation and beginning of the exercise of activity for access to the market, which, in our view, seems to be a too light a requirement, which to a certain extent, goes against the aforementioned advantages.

[36] See n 1, articles 57 – 61.

[37] Ibid, article 54, paragraph 2.

[38] For the purpose of this article, details will only be provided with regards to Risk Management, Internal Control, and Actuarial.

[39] See Insurance Core Principles and Common Framework for the Supervision of Internationally Active Insurance Groups, ICP 8, 74.

[40] See SIIDir, article 45, paragraph 1; PRA Rulebook 'Conditions governing business' r.3.8-3.11; See also EIOPA, 'Guidelines on ORSA' at https://www.eiopa.europa.eu/browse/solvency-2_en?source=search (last accessed 30 August 2022).

[41] Peter Kochenburger; Patrick Salve, 'An Introduction to Insurance Regulation' (University of Connecticut) USA, 8.

The risk management key function means that the insurers and reinsurers must have an effective risk management system that includes strategies, processes and procedures for providing information that allow, at all times, the identification, measurement, monitoring, management and communication of risks to which they are or may be exposed, in an individual and aggregated manner, and the respective interconnectedness.[42] The risk management system is so paramount that must be integrated into the organizational structure and decision-making process of the insurance and reinsurance companies, considering the board of directors or the people responsible for key functions within the companies.[43] The risk management system covers at least the following areas: underwriting and reserving; asset-liability management; investments; liquidity risk and concentration risk, operational risk; reinsurance and other risk-mitigation techniques.[44] These companies must establish in their organizational structure, a risk management function that is appropriate to the size, nature, and complexity of their businesses.[45] The personnel who executes the risk management function must implement the internal policies defined by top directors and approved by the management, through planning, analysis, monitoring, and reporting of the impact of risks to which the insurance company is exposed, and must propose mitigation plans or risk transfer to deal with different situations.[46]

In relation to the actuarial function, to be performed by a 'Responsible Actuary', the regulatory approach is to maintain the independence of actuaries, rather than requiring an in-house actuarial function, mainly because there is a shortage of actuaries in Angola. ARSEG considered that although it recognised the limitations in terms of the academic training of these professionals, the outsourcing regime provides for the acquisition of external services for this function, to mitigate the effects of this shortage.[47] Insurance and reinsurance underwriters must have an effective actuarial function to coordinate the calculation of technical provisions, ensure the appropriateness of the methodologies and underlying models used, as well as the assumptions made in the calculation of technical provisions, assess the sufficiency and quality of the data used in the calculation of technical provisions, compare the best estimate against experience, inform the insurer's board of directors of the reliability and adequacy of the calculation of technical provisions, express an opinion on the overall underwriting policy, and express an opinion on the adequacy of reinsurance arrangements.[48]

It is established that companies must have an internal control system, which must include administrative and accounting procedures, an internal control framework, appropriate reporting arrangements at all insurer's levels, and a compliance function responsible, inter alea, for advising the governing body on compliance with the applicable legal, regulatory, and administrative provisions, and the identification and evaluation of the risk of non-compliance.[49]

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[42] See n 1, articles 62, paragraph 1.
[43] Ibid, article 62, paragraph 2.
[44] Ibid, article 62, paragraph 3.
[45] Ibid, article 63, paragraph 1.
[46] Ibid, article 63, paragraph 5.
[47] See Final Report of the Consultation Process_Revised Version 24072020.pdf, 25 at https://www.arseg.ao/legislacao/consultas-publicas/relatorios-de-consulta-publica/ (last accessed 16 August 2022).
[48] See n 1, article 67, paragraph 2.
[49] Ibid, articles 64 – 65.

In relation to reinsurance, the obligation to assign locally 30% of unretained liabilities was eliminated, giving insurers greater freedom to manage risks, in accordance with their internal risk control policy, while fronting is now allowed, with an exception for motor and health insurance.[50] The new fronting regime is discussed in Part III.

3 Evaluating the Goals of the New Legal Regime

The Preamble of the LASR states that it takes into account the recommendations of IAIS and CISNA, namely that the market regulation should concentrate on the promotion of healthy competition, the protection of policyholders, the promotion of stability and regular functioning of the market, as well as the systemic risk prevention.[51] The LASR also determines that the ARSEG, in the scope of the supervision of the insurance and reinsurance activity, complies with the principle of the protection of policyholders, insured, and beneficiaries, as the main objective of the supervision, to which all the other objectives converge.[52]

With regard to the promotion of healthy competition, LASR conditions the granting of authorisation to carry on insurance activity on the verification of the compatibility between the development prospects of the insurance company and the maintenance of healthy competition in the market.[53] Once they are operating, insurance undertakings are prohibited from adopting concerted practices of any kind aimed at securing a dominant position on the market or causing alterations in the normal conditions of its operation.[54]

The growth of the financial services market, which is, at least in theory, connected to the financial stability objective, is also seen as a regulatory objective, although it may be considered an implicit one, as discussed in Part III.

III. THE FRONTING ISSUES OF THE NEW LEGAL FRAMEWORK IN ANGOLA

1. Purpose of Reinsurance

To understand the issues relating to fronting in the LASR, it is crucial to consider the purpose of reinsurance. As indicated in the introduction above, fronting is essentially a reinsurance technique, although there are some differences, namely with regards to controlling the underwriting process and claims handling. The dissimilarities impose the need of analysing carefully eventual diversions from the typical reinsurance and possible challenges.

O'Neill, Woloniecki, and Arnold-Dwyer argue that there are three main purposes to transfer risks through reinsurance.[55] First, by means of reinsurance, an insurance company can leverage its capacity to underwrite

[50] See article 3, Paragraph 1 of Decree nº 6/01, 2nd of March, about Co-insurance and Reinsurance.
[51] See n 1, Preamble. See also Insurance Core Principles and Common Framework for the Supervision of Internationally Active Insurance Groups, ICP 1.2, 17 – 19.
[52] See n 1, articles 10 – 11.
[53] Ibid, article 28 paragraph 2 e).
[54] Ibid, article 4, paragraph 1.
[55] O'Neill et al. (n 13), para 1-005.

insurance risks. Under these circumstances, the insurer may be capable of taking enormous singular risks or a panoply of smaller risks, or even both. Otherwise, it could not accept said risks. Secondly, "reinsurance can promote financial stability by ameliorating the adverse consequences of an accumulation of losses or of single catastrophic losses, because these will, at least in part, be absorbed by reinsurers".[56] Thirdly, reinsurance can allow insurance companies to manage their regulatory capital requirements since 'reinsurance' is a recognised risk mitigant in relation to underwriting risk.[57]

If the reinsurer is not financially robust enough to meet the liabilities assumed from the reinsured, then the latter will have to pay out, but if it cannot pay the claim on the underlying insurance policy because this unsound capital base was the reason to look for reinsurance, then one of two things may happen: a new capital injection or the insolvency of the insurer.[58] This is precisely why insurers must pay close attention to the stability and financial health of the reinsurer before the risk placement.[59] Therefore, clear regulatory requirements should be in place, thereby avoiding adverse consequences to the policyholders and the market itself, which would be facing a systemic risk.

2. The Approved Fronting Regime

Under the LASR, insurance, and reinsurance companies shall not assign, respectively, in reinsurance and retrocession, more than 50% of the premiums written for the risks they have underwritten in motor and/or health insurance, taking into account the totality of its operations in each calendar year.[60] The Insurance Activity Regulator justified this regulatory approach with the fact that it understood that motor insurance and health insurance are "massive insurance" with local technical and financial capacity, taking into account the market's historic retention levels in these branches.[61] Conversely, there is no restriction in the LASR fronting for the remaining types of insurances: accordingly, Angolan insurance companies are allowed to reinsure 100% of a (non-motor / non-health) risk in the global reinsurance market.

In light of the above justification, it could be queried why lines of insurance, such as travel insurance, insurance for accidents at work, and occupational diseases, which – according to the statistics – also benefit from significant local and technical capacity, have not been included in the list. The cession rate in these lines of insurance reached 6.68%, with a downward trend.[62]

The LASR stipulates that ARSEG may authorize ceding reinsurance premiums in a percentage higher than the one prescribed for motor and health insurance, as long as it is technically justifiable.[63] However, it does not define what "technically justifiable" means, neither does it provide guidance on who can request authorization and at what cost. However, it has been considered an ineffective strategy. In this context, it is important to mention that

[56] Ibid.
[57] Ibid.
[58] Ibid, para 1-006.
[59] Ibid.
[60] See n 1, article 137.
[61] See the early version of the Rationale Report of the Bill on Insurance and Reinsurance Activity, provided by ARSEG during the consultation process.
[62] See Insurance Market, Pension Funds, and Insurance Mediation 2021 Report, 38.
[63] See n 1, article 137, paragraph 3.

The Brazilian Regulator, the Superintendence of Private Insurance (SUSEP), in its recent public consultation on the reforms regarding insurance and reinsurance, recognized the complexity, as well as the regulatory costs of analysing requests of this kind, with impairment to other work fronts considered more important from the regulatory standpoint, without underestimating the costs that they could imply for the supervised companies, thus recognizing the need to improve the model that was in force by the time of the above-mentioned public consultation.[64]

Additionally, ARSEG may, through its legal instruments, make provision for other lines or types of insurance to which the limit set in paragraph 1 will apply.[65] Bearing in mind the foregoing, ARSEG can now, at the convenience of the insurance industry, determine additional lines of insurance products to which the 50% limit shall apply.

In light of the above, it is clear that the LASR does not provide for any minimum retention rate for the majority of the lines of insurance and does not empower ARSEG to take quick and decisive action on this specific subject matter. So, a regulatory amendment may be required.

3. Fronting, Policyholders Protection and Solvency Requirements

Policyholder protection is one of the main rationales for insurance regulation, due to certain inherent features of the insurance contract, notably, the fact that the claims payments may become due at a future point in time, and the mismatch in the bargaining powers of the parties at the insurance level. Indeed, one of the main concerns regarding fronting is that the front company not only transfers the total amount of the risk, but also the claims handling to the reinsurer, which means that there may be many more delays on pay-outs.

Applying the general principle discussed in Part I to fronting, the underlying insurance contract and the fronting reinsurance are treated as separate and independent contracts. Therefore, the front company remains liable to the policyholders, which means that fronting arrangement does not automatically create a direct claim by the underlying policyholder against the reinsurer since there is no privity of contract between them. The underlying insured has no contractual rights against the reinsurer under the reinsurance contract as it is not a party thereto[66] unless there is a cut-through condition, or the terms of the reinsurance policy may be construed in the sense that the parties (reinsured and reinsurer) intended the terms to be enforceable by the insured (third party).[67]

Some authors believe that fronting arrangements create a "consumer right" for the underlying policyholder, and should be regulated accordingly.[68] Curiale argues that policyholders should be allowed to choose the carriers they find suitable for their needs. In a fronting arrangement, where a reinsurer effectively takes control, this is not necessarily the case as the policyholder has no choice in the insurer's choice of the fronting reinsurer. There is frequently no transparency to the underlying policyholder that the risk is fully passed on to the fronting reinsurer. Curiale therefore suggests that "for policyholder safety and the overall good of the insurance mechanism, sound

[64] See SUSEP Consulta Pública, para 10.3.7 da Exposição de Motivos at http://www.susep.gov.br/setores-susep/seger/exposicao-de-motivos-cp-no-9-compressed.pdf (last accessed 01 September 2022)).
[65] See n 1, article 137, paragraph 4.
[66] See Third Parties (Rights against Insurers) Act 2010, s.15. It does not apply to reinsurance contracts.
[67] Third Parties (Rights against Insurers) Act 1999, s. 1.
[68] Howard W. Greene & Jon Harkavy, 'Fronting is a Consumer Right' (1991), 38, Risk Management, 24.

regulatory policy encourages participation within" the supervised insurance market.[69] Curiale adds as an example, that "[i]f a policyholder's decision to use a fronting carrier meant the insured could be held responsible for lapsed workers' compensation payments or unpaid automobile claims, I suspect fronting would rapidly lose its allure."[70] Thus, one could argue that the problem is not fronting in its nature, but permitting it without any regulatory limitations. Moreover, scholars suggest that "improper fronting arrangement" is found in the amount of the agreement and its purpose.[71] Thus, fronting may be a suitable arrangement, when there is a quantitative limitation and its ultimate goal is to improve the reassured's claims payments capacity. Without regulation, this significant gap between the payment of the premiums and the payment of claims could put insurance companies in a comfortable position to charge, perhaps, low premiums, in order to capture market shares, at the detriment of healthy competition, or to charge high premiums, thereby making excessive profits.

There is also an inconsistency in LASR, as with the strengthening of the solvency regulatory requirements, insurance companies should also be required to manage at least a small part of the risks they accept instead of being allowed to transfer 100% of it to a reinsurer. As discussed in Part II above, the LASR introduces principles of prudential governance and risk management for each regulated insurance company, such as, for example, an internal control system, which must include administrative and accounting procedures, an internal control framework, and appropriate reporting arrangements at all insurer's levels, to ensure that companies are sound for their activities. If companies are allowed to transfer their risks without limitation, this may have a negative impact on capacity and expertise building in those areas. The new measures impose from the industry serious investments in building technical capacity, through human capital training, which should also increase the insurance companies' responsibility in terms of retention levels. On one hand, it is recognised that insurance companies, should be able to meet consumers' needs, through an adequate capital basis. On the other hand, fronting is allowed without relevant restrictions, as mentioned above.

4. Moral Hazard and Risk-based Management

Moral hazard could be defined as a conduct of a person not acting in good faith because said person is aware or led to believe that the economic consequences of its actions or omissions will not fall upon said person. For instance, an insured could be less cautious in terms of risk prevention knowing that insurers will protect him against losses and damages of his property.

An insurer who has fronting reinsurance cover could be tempted to acquire market share by underwriting risks indiscriminately, knowing that the whole risk is reinsured under the fronting arrangement. Fronting can frequently lead the front insurers "to abdicate their underwriting responsibilities, accepting risks and rates they normally would never consider".[72] This in effect means that there is the risk that front insurers would agree on small ceding commissions with reinsurers in respect of the low premiums that they could eventually charge. This is so because

[69] Salvatore R. Curiale, 'The Dark Side of Fronting' (1991), 38, Risk Management, 26.
[70] Ibid.
[71] Thomas F.X. Hodson & Cathleen T. Heath, 'The Outlook for Fronting' (Special Report: Captives & ART), Risk & Insurance (2002).
[72] See Curiale (n 69).

there are no specific regulation limitations, provided that insurers comply with the 50% minimum retention requirements for health and motor insurance.[73]

Alternatively, the insurer may rely on the fronting reinsurer to carry out the risk due diligence and assessment, and claims handling. In the latter scenario, the insurer would not be incentivised to build on their technical and financial capacity to serve their customers in a fair fashion, meeting their necessities and pay out when claims arise.

The foregoing can raise an issue on how to foster technical and financial capacity with regard to other lines of insurance in Angola, for instance, coverage for the oil and gas sector, which is still Angola's most important industry, after many years. By way of illustration, the ceding rate for this line of insurance, in 2021, was almost 58%, a huge amount, mainly if we consider the mandatory special co-insurance regime in place in the industry.[74] This special co-insurance regime determines that the oil and gas and diamond sectors must be insured by a set of local insurers. This measure was envisioned to assure the balanced and harmonious development of the insurance sector.[75] For said purpose, one of the co-insurers is appointed as the leader, which exercises its mandate on a rotating basis, and is responsible for guaranteeing the transfer of unretained liabilities into reinsurance, after the market capacity is exhausted, within certain criteria.[76] It is evident that, by allowing fronting in such terms, the carriers, mainly the small ones, would not need to be concerned about the acknowledged shortage of specialists in the Angolan insurance industry, avoiding the significant expenditure needed to address it.

To this extent, the CEO of ARSEG mentioned in 2019 that in ten days of its mandate, by analysing the files, they had already identified some challenges in the industry, inter alea, the fostering of training in insurance and pension funds, and presented them as part of its mandate.[77] Concerning the same issue, E&Y considered, following the drafting process of the insurance and reinsurance activity bill, that with the adjustment of the insurance industry to the best international practices, the expectation would be that the governance models of the insurers would also adapt, which would bring greater demand and would put enormous pressure on human resources, in areas such as internal audit, compliance, risk, actuarial, as well as a necessary updating in the areas of subscription and claims management, would be decisive.[78] E&Y also later considered that the training needs in those areas were no longer

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[73] See n 1, article 137, paragraphs 1 and 2.
[74] Insurance Market, Pension Funds, and Insurance Mediation 2021 Report, 38.
[75] Article 16, paragraph 1 of the Angolan Decree nº 6/2001, 2nd of March, About Reinsurance and Co-Insurance (Decreto Sobre o Resseguro e Co-Seguro). According to this provision "…*com o fim de garantir o desenvolvimento equilibrado e harmonioso do sector segurador, os seguros das actividades petrolíferas e diamantíferas são, nos termos do artigo 15.º do presente decreto, obrigatoriamente contratados em regime especial de co-seguro.*" This provision means that, in order to ensure the balanced and harmonious development of the insurance sector, the insurance of the oil & gas and diamonds activities is, pursuant to the Article 15 of the above-mentioned Decree, compulsorily underwritten under a special co-insurance regime.
[76] Ibid, article 15.
[77] Elmer Serrão, *Discurso IV FÓRUM SEGUROS - Expansão* at https://owa.arseg.ao/api/v1/public/download?f=QsGRL8hOi%2bmrHWkNXbMq8N3Y4udSWmD%2fSdpbfdoKtjGE6mpMxfUdI8inGaTtKoUdDIuFGSvEt7ioQjnpW6GrOIqqkaeFn3LSDD5lpqQM%2fy%2flFMOq%2bq%2fS1EE6kqa2af9IA4VTU786hn5MeXYApLZE1R%2fTMmYKDne2G6U2NogAD5gnhzfglJ4FWZXrcB3HleBU (Last accessed 19 August 2022).
[78] Ricardo Vinagre (Senior Manager EY, Assurance Services), *Formação no Sector Segurador – Uma prioridade* (Valor Economico, Edição nº 323 | 23/08/2022) at https://valoreconomico.co.ao/artigo/formacao-no-sector-segurador-uma-prioridade (Last accessed 15 August 2022). See also EY, Formação no Sector Segurador – Uma prioridade II on 06 July 2020 at https://www.ey.com/pt_ao/assurance/formacao-no-sector-segurador-uma-prioridade-ii (Last accessed 15 August 2022).

just a competitive advantage for entities that had staff with certain characteristics, but a requirement for the whole market.[79]

Thus, no technical capacity would be built in theory, and, as a consequence, the Angolan insurance industry would not be aligned with the good international practices relating to the insurance industry. ARSEG, in its introductory remarks on the Rationale Report of the Bill of the insurance and reinsurance activity law, recognised that:

> "[t]he insurance industry has been suffering, over time and worldwide, profound technological and structural changes that are not compatible, neither with the current legislative situation nor with the technical conditions of its operation in Angola, imposing an urgent adaptation and modernization of the sector."[80]

In this sense, with all these aspects in mind, the way fronting is designed could be inappropriate for the regular and stable functioning of the Angolan insurance sector, as the premiums would not remain in the market, thereby promoting the collapse of the companies if things go wrong with the reinsurer. Thus, this could also be inconsistent with some of the central goals of regulation, such as the policyholders' protection, promotion of stability and regular functioning of the market, as well as the prevention of systemic risk.[81]

Notwithstanding the abovementioned, opening up the insurance market to branches of companies headquartered abroad is a new relevant feature that should have been considered alongside the new fronting legal scheme and the potential moral hazard. While the recently approved regulatory strategy seems to be virtuous, as it can attract significant foreign investment and know-how to the Angolan insurance industry, undoubtedly, it could be quite challenging for the existing carriers in the market to compete, depending on the level of regulatory market entry requirements. In this sense, the LASR does not impose any specific restrictive requirements to protect the Angolan insurance companies, such as mandatory association with local companies, or limitations in terms of lines of insurance these branches can underwrite.[82] Kochenburger and Salve support the idea that, in certain cases, the referred requisites "are reasonable restraints" to guarantee that the foreign insurance company seeking to be licensed brings real added value to the local industry, whereas in other situations these can be financially overdemanding and curb the "business growth" for a long period of time until the company is completely settled in and becomes profitable.[83]

Having said that, the new legal framework in Angola is open and innovative. Albeit there should be some limitations to fronting, in order to establish a balanced market and take advantage of the background of some globally relevant companies. With this window of opportunity, fronting would probably be seen by these companies as a good way to circumvent the law and underwrite massive premiums without any oversight by the Angolan authorities as the risks would not be managed locally.

In this context, if things go awry, the front carriers may collapse, with grave consequences for policyholders, precisely because the international reinsurance companies are not under ARSEG's solvency and prudential oversight or may not be subjected to proper supervision in the state they are headquartered. This could not

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[79] Ibid.
[80] See n 25.
[81] See n 1, Preamble.
[82] See Kochenburger (n 41), 12.
[83] Ibid.

guarantee legal certainty and predictability for market actors, from the point of view of the industry, so a middle-ground approach would be wise. Obviously, this may and should raise serious concern to ARSEG.[84] However, this is a problem if the reinsurer is regulated in a dodgy jurisdiction. If the reinsurers are, for instance, Swiss Re, Munich Re or Lloyd's, that are subject to gold-plated regulation, the scenario is totally diferrent.

In this sense, to prevent such situations of credit risk posed by the reinsurer, when developing the reinsurance programme the ceding insurer should consider its appetite for reinsurer credit risk.[85] Reinsurers may face solvency issues, leading to delayed payment or default, and this can have significant consequences for the solvency and liquidity of the ceding insurer.[86] In order to mitigate reinsurer credit risk, various options are available, for example, setting limits on risks ceded to a single reinsurer, ensuring a spread of risk amongst a number of reinsurers, incorporating rating downgrade or other special termination clauses into the reinsurance contract, requiring the reinsurer to post collateral, withholding reinsurer's funds, etc.

In addition, Angolan carriers will need to build their technical and financial capacities to compete effectively with proper abilities to manage their businesses, considering the risk to which they are exposed. This should be a natural consequence of the new requirements relating to risk management.[87] Thus, the LASR prescribes that the insurance company must establish in its organizational structure a risk management function appropriate to the size, nature, and complexity of its operations, and this obligation must be fulfilled within a maximum period of two years starting from its entry into force, that is, 1st July 2024.[88] It also states that the risk management function must be carried out by competent and qualified personnel with a clear understanding of their role and responsibilities.[89] So, Angolan companies must start creating new processes and systems of risk management where they are needed now, even with small steps, not only because it is mandatory, but as it is common knowledge that there is a glaring shortage of specialists in the Angolan insurance industry, so serious investments in high-level training is required. With this in mind, one may question whether it is appropriate to impose stricter measures on insurers in terms of risk management, as shown in the previous Part, while simultaneously LASR almost eliminates retention requirements in reinsurance.

5. The Growth of the Financial Services Market as a Regulatory Objective

The LASR does not refer directly to the financial growth of the industry as one of its ultimate goals. However, it could be argued that this idea is implied therein. In this sense, the LASR provides that, according to constitutional imperatives, the financial system must be organised in such a way as to guarantee the mobilisation and application of the financial resources necessary for economic and social development.[90] Additionally, emphasis is given to the promotion of the insurance market, recognised as fundamental for efficient risk mitigation and redistribution, an effective complement to social security, and as effective protection of people, companies, and their respective

[84] See Curiale (n 69) above.
[85] See n 39 ICP 13.2.2.
[86] Ibid.
[87] See n 1, articles 62 - 63 and 235.
[88] Ibid, articles 63, paragraph 1 and 235.
[89] Ibid, article 63, paragraph 2.
[90] Ibid, Preamble.

assets.[91] This perspective may also be inferred from the Organic Statute of the ARSEG, which determines that it is its mandate to monitor and assess the microeconomic impact of the insurance industry.[92] IAIS considers that the supervisory objectives and their respective priority may vary by jurisdiction depending on the level of development of the insurance markets, market conditions, and consumers.[93] So supervisory objectives could also include promoting insurance market development.[94]

ARSEG, in its 2021 annual report, stated that the penetration rate of the insurance industry on the Angolan gross domestic product (GDP) is less than 1% (0.70%)[95] and recognised it is still far from what it envisages. For said reason, ARSEG considers that via its Financial Communication and Education Programme, it has been taking steps to reverse the current paradigm, which involves fostering the financial literacy of consumers of insurance products and pension funds in Angola.[96] Nonetheless, this measure is not enough, it is urgent to leverage the retention levels of the insurance carriers operating in the insurance industry, relating to reinsurance. By doing so, insurers could pay claims when they arise, without relying too much upon the reinsurance industry. In this way, policyholders are protected, while more money is kept in the local economy.

Furthermore, some commentators point out that, among others, the paramount reason that backs "active governmental involvement in the insurance marketplace" relates to the fact that insurance allows individuals and businesses to protect themselves and their assets from catastrophic events.[97] They assert that the said protection is linked to the solidity "of a private sector economy as a whole". In essence, this connection makes it necessary for the government to intervene in the marketplace to ensure that it remains "stable and financially strong", while also promoting policyholders' confidence in the insurance industry's integrity.[98]

In light of this, it could be argued that, although front companies receive ceding commissions, fronting without relevant limitations, is not fit for the purpose of strengthening the insurance industry because what makes an insurance company robust are the significant amounts of premiums it collects and manages, regardless the amounts it retains, not the commissions paid to the front company. The Angolan insurance industry is crucial to back and financing the emerging economy of the country, creating job opportunities, developing human capital, and promoting growth. ARSEG perceives as a consensus that only a strong insurance sector, subject to adequate oversight, is capable of backing the economic recovery in Angola, guaranteeing in this way the needed level of insurance protection to safeguard families and businesses.[99] Arguably, the current fronting framework does not seem to constitute a good tool to leverage the Angolan technical (human) and financial capacity in the pursuit of an alignment with the international standards, which seems to be relevant for the industry.

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[91] Ibid.
[92] Article 9, paragraph 2 c) of the Angolan Insurance Regulator Organic Statute.
[93] See n 39, ICP 1.2.1, 18.
[94] Ibid.
[95] See n 62, 13 and 44.
[96] Ibid, 12 and 44.
[97] See n 41.
[98] Ibid.
[99] See Elmer Serrão *'A Importância do Sector Segurador na Recuperação Económica do País' V Fórum Seguros – Expansão,* para XI at https://owa.arseg.ao/api/v1/public/download?f=QsGRL8hOi%2bmrHWkNXbMq8N3Y4udSWmD%2fSdpbfdoKtjEcbrffDxVKmfT%2bPTOIqx8x%2f7kzeCEMPm1vweF33J4HR%2fa58o3F1aYR8MlKfuqh%2f1%2fDCraA%2bq0gNnruWgxQ4WFd (Last accessed 19 August 2022).

In the UK, in connection with the Financial Services and Markets Bill [100], which has now gone before Parliament, there has been a debate about whether the growth of the financial services industry should be an additional regulatory objective in the FSMA framework. Some commentators are concerned that this could dilute regulatory rigour in relation to protecting consumers and safeguarding financial stability. The FSMA Bill will introduce a new secondary 'competitiveness and growth objective' pursuant to which the PRA and the FCA would be required to advance that objective when discharging their general functions.[101] The rationale for this proposal – which has now found its way into the FSMB[102] – is based on the idea that the UK financial services market should be prepared to compete internationally.[103]

In turn, Angola as a developing country must be prepared to adapt quickly, while also considering its weak economic situation. To this extent, it may be argued that fronting does not seem to contribute to the growth of the insurance market in an effective way. It will in theory grow limitedly, taking into account that relying completely on ceding commissions is usually not worthwhile when compared to the retention of premiums if reinsurance is needed, or the total assumption of the risks by keeping the total amount of insurance premiums, where reinsurance is unnecessary.[104] By ceding 100% of the risk to non-Angolan reinsurers, the growth of the Angolan re/insurance market will be stunted because profits from premiums will leave the country, meaning also significant pressure on the Angolan net reserves in foreign currency. This is also a problem because there is no capacity building. Notwithstanding the foregoing, the insurer's underwriting and retention capacity should always be taken into consideration.

IV. COMPARISON WITH AFRICA RE, AND THE APPROACHES IN MACAU AND BRAZIL

This part the paper brings about a comparative perspective by reference to case studies of Africa Re, and the fronting regimes in Macau and Brazil. The paper uses these case studies to illustrate what lessons can be learnt from these realities, since the respective legal frameworks on reinsurance, especially on fronting, have been fairly tested and shown to be working well. In addition, the choice for these examples was also based on the close connection between Angola and Africa Re as a member state, and the close relationships between the Angolan Regulator and both Brazil and Macau Regulators through cooperation and technical assistance protocols as mentioned in each subsection.

1. Africa Re – A Good Example Coming From the African Continent.

Following a recommendation of the African Development Bank (AfDB), the African Reinsurance Corporation (Africa Re) was established on 24 February, 1976 in Yaounde, Cameroon. An international Agreement was signed by the Plenipotentiaries of 36 member States of OAU and the AfDB with the aim of reducing the outflow of

[100] See FSMB, s 24 at https://publications.parliament.uk/pa/bills/cbill/58-03/0146/220146.pdf (last accessed 07 September 2022).
[101] FSMA Bill, cl. 24.
[102] FSMB, cl. 24.
[103] Ibid.
[104] Robert H. Jerry, II & Douglas R. Richmond, Understanding Insurance Law 1017 (4th ed. 2007).

foreign exchange from the continent by retaining a substantial proportion of the reinsurance premiums generated therein.[105] According to The Agreement, each Member State shall authorise Africa Re to carry out its functions in its territory.[106] This is a natural consequence of acceding the membership. The Agreement stipulates that each Member State shall undertake to guarantee that all insurance and reinsurance companies operating in its territory shall offer to place with the Africa Re a minimum of 5% of each of their reinsurance treaties, both present, and future including life treaties on the terms granted to most favoured reinsurers.[107]

Regarding the accomplishment of its objectives, since its beginning, Africa Re has underwritten and retained a cumulative premium in excess of US$ 7 billion, which might otherwise have left the African Continent.[108]

Africa Re considers that it is fulfilling its purpose for the following reasons:[109]

a) In over 40 years of existence, Africa Re has given valuable technical support to its cedants, thus enabling them confidently to write business at the national or regional levels;

b) As a commercial concern, Africa Re prides itself as the only African financial entity, apart from ATI (African Trade Insurance Agency), to be rated "A" by S&P and A.M. Best;

c) At year-end 2021, Africa Re had a shareholder's fund of US$1.00 billion and posted a gross premium income of US$845.34 million while retaining 83.8% of its premium income. Africa Re has been consistently profitable since its inception, accumulating a total profit of US$1.19 billion since 1978.

The main lesson that could be taken from this perspective, taking into account that Angola has not as of today any reinsurance company, is that the Angolan Government could seriously consider the possibility of creating a national reinsurance company, of private capital, with the State as a shareholder with a qualified shareholding, for the period necessary for it to mature, given that a reinsurance company is an investment of enormous financial magnitude. Doing so would promote the participation of a large number of investors, both national and international, and would significantly increase the market's retention levels, a matter that was debated during the public consultation process that preceded the entry into force of the LASR.[110]

2. Macau

In Macau, it has been a common practice to enter into "fronting policy" contracts, whereby the insurance coverage is provided by general insurance companies and the policyholders are guaranteed the application of Macau law

[105] Africa Re, History at https://www.africa-re.com/history (Last Accessed 27 August 2022).
[106] Multilateral Agreement establishing the African Reinsurance Corporation (The Agreement), article 27, paragraph 1 at http://www.worldlii.org/int/other/treaties/UNTSer/1980/809.pdf, (last accessed 04 September 2022).
[107] Ibid, article 27, paragraph 2.
[108] Africa Re FAQ at https://www.africa-re.com/about_us/faq (last accessed 27 August 2022.
[109] Ibid.
[110] Final Report of the Consultation Process_Revised Version 24072020.pdf, 24 at https://www.arseg.ao/legislacao/consultas-publicas/relatorios-de-consulta-publica/ (last accessed 16 August 2022).

and jurisdiction. To ensure the financial capacity of locally authorised insurers to cope with the impact of major risks, the transferee insurers and reinsurers are required to have a solid and stable financial capacity.[111]

In cases where the insurer accepts insurance through a "fronting policy", the pledging, either of the part of the outstanding premium part of the provisions for risks in progress or of the provisions for claims, for the amount corresponding to the full retention of the insurer is accepted, provided the following two conditions are met:[112] (a) the amount of capital insured is at least MOP100,000,000,[113] for each fronting policy transaction,[114] and b) the ceding insurer/reinsurer participating in the fronting policy should fully comply with the credit rating grades given in the annex to the respective notice, namely A- A.M. Best Company, Inc.

In this context,"fronting policy" is understood as the agreement by which the ceding insurer transfers the risk it has accepted to another ceding insurer/reinsurer, retaining only a share not exceeding 5% of the risk in question. In such situations, the applicant insurer should submit the fronting policy, evidence of reinsurance agreement, its proposal to pledge the technical provisions together with other documents and supporting documents required by the Monetary Authority of Macau (AMCM) for approval.[115] A relevant detail is that the Regulator assumes that companies, even in fronting arrangements, will retain at least a portion of the premiums, which may be as high as 5%, considering their retention capacity.

For Angola, although with relevant implications in terms of strengthening supervisory capacity, with investment in specialised training for its technicians, in terms of fronting control, the requirement to set aside provisions in line with the retention capacity of companies, as well as the determination of credit rating grades of reinsurers, would bring clear benefits in terms of promoting financial capacity and risk management, allied to the acquisition of know-how. The Cooperation and Technical Assistance Agreement between ARSEG and AMCM was a good initiative put in place, which opens a window of opportunity to learn and implement the good examples in terms of supervision that can be taken.[116]

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[111] See The Preamble of the Notice 004/2021-AMCM on Supervision of insurance – Requirements of Guaranteeing Technical Reserves due to Abnormally High Loss or "Fronting Policy", Notices and Circulars at https://www.amcm.gov.mo/en/insurance-sector/regulatory-guidelines?type=notices-in-force-from-amcm (last accessed 22 March 2023).
[112] Ibid. See requests for "Fronting Policy" cases, paragraph 1.
[113] Equivalent to £10,114,100, according to OANDA at https://www.oanda.com/currency-converter/en/?from=MOP&to=GBP&amount=100000000 (last accessed 22 March 2023).
[114] See n 112.
[115] Ibid. See, paragraph 3.
[116] See ARSEG Protocolos at https://owa.arseg.ao/api/v1/public/download?f=QsGRL8hOi%2bmrHWkNXbMq8Hj%2ffL2JQSaDIzw3F7be8v34fixGUxWRV7djL%2b7HE9zA8JbmG70KEH3AbWtt%2bjLZ4oLs9iPNRiWKN1ee3vTd%2bcM%3d

3. Brazil

3.1. The Previous Regime

In order to explain the new Brazilian regime, it is necessary to give some background to the reinsurance and retrocession legal framework in force in Brazil until 31 December 2022.

Before the CNSP Resolution N.º 451 of 19 December 2022 entered into force on the 1 January 2023, repealing the CNSP Resolution N.º 168 of 17 December 2007, if there was local acceptance of insurance, fronting was not permitted.[117]

As for the limit of global cession in reinsurance, it had been established that insurers and local reinsurers could not cede, respectively, in reinsurance and retrocession, more than 50% of the premiums issued relative to the risks they had underwritten, considering the globality of their operations, in each calendar year.[118] However, the legislation in force presented some exceptions, namely guarantee insurance, export credit insurance, rural insurance, domestic credit insurance, as well as the nuclear, named and operational, oil, and aeronautical risks.[119] In any case, insurance and reinsurance carriers were allowed to request authorisation to cede more than 50% of the risks they had underwritten, provided that they had technical justification.[120]

Despite the evident degree of flexibility considered by the legislator, the previous regime clearly prioritised the development of a local market and the retention of reinsurance premium within Brazil.

3.2. Brief Reference to the Recently Enacted CNSP Resolution and Rationale

At the beginning of the public consultation that preceded the new insurance and reinsurance legal framework, SUSEP presented the reasons for why CNSP Resolution Nº 168/2007 should be reformed.

In the last few years preceding the new regime, SUSEP had been receiving more and more frequent requests from the market to exceed the cession limit in reinsurance and retrocession, supported by the repealed rule according to which SUSEP could authorise cessions in a percentage higher than 50% if due to a technically justifiable reason.[121] According to the explanatory memorandum, such requests tended to come from companies operating in branches involving high insured amounts and which, naturally, demanedd intensive use of reinsurance.[122] Another category of cases were start-ups in certain lines of business, a situation in which the support of the expertise of a reinsurer is important to enable the operation of the business.[123] As a result, it was understood that these situations constituted examples in which the regulatory limit imposed constituted a certain impediment to

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[117] See heading of artigo 16º da Resolução CNSP nº 168/2007 (Repealed).
[118] Ibid.
[119] Ibid. See article 16, paragraph 1. See also SUSEP Consulta Pública, 10.3.2 da Exposição de Motivos at http://www.susep.gov.br/setores-susep/seger/exposicao-de-motivos-cp-no-9-compressed.pdf (last accessed 01 September 2022)).
[120] See n 117, Article 16, paragraph 2.
[121] See SUSEP Consulta Pública, 10.3.3 da Exposição de Motivos at http://www.susep.gov.br/setores-susep/seger/exposicao-de-motivos-cp-no-9-compressed.pdf (last accessed 01 September 2022)). See also (n 118), article 16, paragraph 2.
[122] Ibid. See para 10.3.4.
[123] Ibid.

market development, thus justifying the exemption.[124] It is important to mention that SUSEP also recognises the complexity, as well as the regulatory costs of analysing requests of this kind, with impairment to other work fronts considered more important from the regulatory standpoint, without underestimating the costs that they may imply for the supervised companies, thus recognising the need to improve the previous model.[125] Therefore, the resolution in force eliminated the 50% cession limit in reinsurance, by local insurers, and increased to 70% the cession limits in retrocession, for local reinsurers, of issued premiums relative to the risks they have underwritten, considering the globality of their operations, in each calendar year, except for the groups of branches such as financial, rural, and nuclear risks.[126]

However, minimum criteria and guidelines to be observed by local insurers and reinsurers are established, namely, the proper management of their reinsurance and retrocession operations, which includes the development and implementation of a risk retention and ceding policy, complementing, but not limited to, the specific regulation that provides for the internal control system, the risk management structure and the internal audit activity, and shall be aligned with their underwriting policy.[127]

In this sense, a more principled approach is adopted, that is, more qualitative, less prescriptive and adherent to the business policy and strategy of the companies, with emphasis in the structuring of the reinsurance and retrocession programs by the supervised companies, in line with the best international practices, mainly those issued by the IAIS.[128] This, in effect, shows that it is perfectly possible to conciliate the best international principles and practices, including the IAIS Insurance Core Principles (ICPs) with some degree of market protection.

The 70% limit referred to above was established based on the market's historical behaviour, given that in the general context the reinsurers' portfolios are well suited to the operating limit in force, also considering the nature of these operations.[129] It is fundamental to highlight, at this point, the protectionist approach of SUSEP when placing among the regulatory provisions considered relevant by the IAIS those which guide as to the possible distortion of operations, such as those related to fronting operations in portfolios of an essentially mass nature.[130] To this extent, the relevance given by the Brazilian Regulator to fronting issues is notorious, without however losing sight of the need to foster innovation and stimulate the development of the supervised market.

It is suggested that the Brazilian approach would be an effective model for the Angolan insurance sector, bearing in mind that with the LASR, branches of international insurance and reinsurance companies can be licensed to operate in Angola, establishing limits on retrocession. A regulatory position in these terms would promote local technical and financial capabilities in an effective manner, both through local coverage and the transfer of know-how. However, the effectiveness of such a measure would have to take into consideration a strengthening of

[124] Ibid.
[125] Ibid. See paras 10.3.7 – 10.3.9.
[126] See Article 6, paragraph 3 of CNSP Resolution Nº 451 of 19 December 2022.
[127] Ibid. Article 6, paragraph 2.
[128] See n 121, heading of paragraph 10.3.12 and paragraph 10.3.13. See also n 39, ICP 13.
[129] See Comparative Table, 8 at http://www.susep.gov.br/setores-susep/seger/quadro-comparativo-cp-no-9-compressed.pdf (last accessed 03 September 2022).
[130] See n 121, para 10.3.12 c).

market access requirements. Thus, instead of the five years required,[131] minimum credit rating grades would be established.

In fact, in view of the necessary precautions, insurance companies must submit to SUSEP, by 31 March of the following calendar year, a technical justification for a reinsurance cession percentage higher than 90%, considering the totality of their operations, per calendar year, and failure to do so will result in sanctions.[132] In essence, the need for justification for insurance companies with a retention below 10% is a precautionary measure, also adopted by other reference jurisdictions, aimed at monitoring and curbing possible misuse of reinsurance.[133] This is a more appropriate and more flexible approach, capable of accommodating the regulatory objectives without calling into question the flexibility of the insurance market.

Reference should be made to the careful approach adopted by the Brazilian reinsurance regime, that provides for, from the outset, the question of nuclear risks because, notably, there is no internal capacity, thus authorising the fronting, through cession to eventual foreign reinsurers, of the total value of the premiums ceded in reinsurance in the nuclear risks branch.[134]

For the foregoing reasons, the Angolan insurance market, as an incipient market that needs technical and financial strengthening, can take full advantage of the Brazilian experience. This process may even be made easier by the existing cooperation protocol between ARSEG and SUSEP in the fields of training and information sharing.[135]

V. CONCLUSION AND RECOMMENDATIONS

The LASR is an innovative regulatory framework, aligned with the best international standards and principles with regards to the insurance market, given the policyholder protection, healthy competition, promotion of financial growth and stability, and building technical capacity objectives. Among various new regulated matters, it brings a series of new key functions to be observed by the Angolan insurance and reinsurance industry, and this work mainly focused on Pillar II of Solvency II, which reflects the qualitative requirements, the UK approach on the same, and the fronting regime.

The core of the evaluation considered that the approved fronting regime allows insurance companies to act as front companies for reinsurers unless the transaction is related to health and motor insurance, and while the modernisation of the legislation is virtuous, the way fronting is regulated tends to represent a threat to its effectiveness, since it may create moral hazard to the industry, which would be tempted to rely on small payments in ceding commissions. This could have a negative impact on the process of fostering technical and financial

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[131] See n 35.
[132] See n 126, article 6, paragraphs 4 and 7.
[133] See n 121, para 10.3.18.
[134] See n 126, article 14, paragraph 3.
[135] See ARSEG *Protocolos* at https://owa.arseg.ao/api/v1/public/download?f=QsGRL8hOi%2bmrHWkNXbMq8BWJ6Q4INPELVVZB%2bTpIaTe5qwnt3PCsRcrtPKwiXjP%2b (last accessed 05 September 2022).

capacity in the industry, with negative externalities to the policyholders. Therefore, in our view, the LASR should be amended.

In terms of comparative research, it can be concluded that Macau adopted a model which takes into account the market's retention capacity, which naturally contributes more effectively to its maturation, from a technical and financial point of view, with positive externalities for the financial sector and the economy considered as a whole. Brazil, in turn, has been imposing local retention limits on both insurers and reinsurers, though the relevant changes, recently enacted to improve the insurance and reinsurance legal framework, based on its own and the international experiences. Africa Re is also a worthwhile example, as it clearly shows that it is possible to improve retention levels of the Angolan insurance industry through the state's intervention in the insurance business.

In light of the critical appraisal relating to the subject matter discussed, some recommendations should be made, in order to contribute to the effectiveness of the legal framework.

Bearing in mind that with the enactment of the LARS, branches of insurance and reinsurance companies headquartered abroad can be licensed to operate in Angola, the limits on retrocession should, equally, be established. A regulatory position in these terms guarantees the creation and improvement of the local technical and financial capabilities in an effective manner, both through the transfer of know-how and local coverage, respectively. However, the effectiveness of such a measure would have to take into consideration a strengthening of market access requirements, by requiring minimum credit rating grades, instead of just relying upon a minimum of 5 years of incorporation and beginning of the exercise of activity for access to the market, which, in the author's view, seems to be too light a requirement.

Similarly to the new reinsurance regime entered into force in Brazil, Angolan insurance companies should submit to ARSEG an annual technical justification for a reinsurance cession percentage higher than, for instance, 95%, considering the totality of their operations, per calendar year, and determine legal consequences for failure to comply this requirement. In essence, the need for an insurance company to present technical justification, in cases where its retention is below a certain percentage is a precautionary measure, also adopted by other reference jurisdictions, aimed at monitoring and curbing possible misuse of reinsurance.

Although with relevant implications in terms of strengthening supervisory capacity, with investment in specialised training for the Regulator's technicians, in terms of fronting control, the pledging of provisions in line with the retention capacity of companies, as well as the determination of credit rating grades of reinsurers, would bring clear benefits in terms of promoting financial capacity and sound risk management, allied to the acquisition of know-how.

By considering the recommendations above, the Angolan insurance market, as an incipient market that needs technical and financial strengthening, alongside the commitments with CISNA, IAIS, IOPS, and other international institutions, may comply more effectively with its regulatory goals.

Finally, the Cooperation Agreement between ARSEG and AMCM, as well as, the existing Cooperation Protocol between ARSEG and SUSEP for training and information sharing are initiatives to be welcomed, opening a window of opportunity to learn and implement good examples in terms of regulation and supervision that can be taken.