MAYER | BROWN

GLOBAL INSURANCE INDUSTRY

YEAR IN REVIEW 2019

EXCERPT

Asia

Hong Kong

2019 was a landmark year for the Insurance Authority ("**IA**") as it took from the three Self-Regulatory Organisations ("**SROs**") the responsibility for direct regulation of some 110,000 insurance intermediaries in Hong Kong. Although the IA took over the statutory functions of the Office of the Commissioner of Insurance to regulate insurers in June 2017, it did not regulate insurance intermediaries in Hong Kong until the handover on September 23, 2019.

The IA is now responsible for all aspects of regulation of intermediaries, including determining the minimum capital and net asset requirements of insurance brokers, academic requirements, CPD training, issuing codes of conduct, monitoring compliance, conducting investigations and taking enforcement action where breaches have occurred. Insurance intermediaries are now subject to a higher standards of compliance. Individuals in senior management and responsible officer roles of insurance intermediaries are subject to extensive requirements set out in the codes of conduct, and they will be held accountable for any breaches. After taking over regulation of insurance intermediaries, the IA has issued codes of conduct for insurance agents and brokers, which set out expected standards of conduct as well as new guidelines on insurance sales related activities and CPDs.

It is relevant to note that under the Insurance Ordinance Cap. 41, the IA (like other financial regulators, such as the Securities and Futures Commission) has broad powers of investigation and inspection available at its disposal, and it is expected the IA will be active in its scrutiny of insurance intermediaries. With a tougher stance taken by the Government on anti-money laundering ("**AML**"), it is expected AML may well be an area the IA will further focus on. In 2018, the IA conducted on-site inspections of insurers of their AML controls and some deficiencies were noted

Insurance intermediaries are expected to put in place sufficient controls and policies to ensure compliance with all relevant requirements, as the IA is likely to adopt a proactive role in its investigation. There will be increased compliance and administrative costs for insurance intermediaries, coupled with greater accountability upon key persons, may result in consolidation of insurance brokers.

Completing the IA's taking over of regulation of insurance intermediaries is the coming into effect of the new insurance licensing regime, which is activity-based. "Regulated activities" has been broadly defined under the Insurance Ordinance. Any person who invites or induces a person to enter into a contract of insurance or makes a material decision or gives regulated advice will be caught by the definition of "regulated activity" and must be licensed. The use of the word "attempt" potentially has far-reaching implications, given any effort to induce a person—whether successful or not—is also caught. This also has implications for referrals of business by unlicensed individuals to insurance intermediaries for a fee.

Insurers will also face more onerous requirements in the coming years. The IA is developing its capital framework towards a risk-based capital regime consistent with the insurance core principles issued by the International Association of Insurance Supervisors ("**IAIS**"). The introduction of the risk-based capital ("**RBC**") in 2021 will overhaul the current capital framework set out under the Insurance Ordinance. Similar to the insurance industry RBC requirements in other jurisdictions, RBC in Hong Kong is taking the three-pillar approach in its solvency assessment for insurers. The assessment covers quantitative aspects, qualitative aspects on enterprise risk management ("**ERM**"), own-risk and solvency assessment ("**ORSA**"), and disclosure. Under the Hong Kong RBC, insurers' assets and liabilities are valued on a consistent and economic basis. Insurers have to work ahead in preparing for and implementing the ERM framework under the RBC regime to ensure continued effectiveness.

Aside from RBC, the International Financial Reporting Standard 17 Insurance Contracts ("**IFRS 17**") published by the International Accounting Standards Board ("**IASB**") will come into effect in 2021. This is a major milestone, as the change has been the most significant since the implementation of the Insurance Contracts Project in 1997. The implementation of the IFRS 17 is to achieve consistency and comparability around the world, which poses some difficulties for insurers in Hong Kong. The implementation of IFRS 17 will change the current system, processes, calculations and data stored in Hong Kong. The first key change is the reporting of profit: IFRS 17 will categorize companies by a measurement of profit in line in terms of services provided, rather than in terms of revenue or cash-flow. The rationale is that profit represents what has been earned as a result of services provided in the contract. The second key change is insurance companies will draw up their contracts on a current measurement basis, meaning that companies can no longer use historic assumptions. The last key change is the measurement of risks. The risk of any shortfall of investment returns against pricing assumptions needs to be reflected in the valuation of the insurance contract. The IASB's intent is to ensure companies quantify risks in the insurance contract to protect policy-holders.

In 2020, the Hong Kong Government plans to introduce an insurance-linked securities ("**ILS**") regime. Hong Kong is a prime location for an ILS market due to its developed capital markets and its proximity to mainland China. According to the 2019-2020 budget speech the Government is prioritizing the ILS regime so that such securities can be issued in Hong Kong. It is hoped this regime will give reinsurance companies in mainland China an alternative option to manage and share their risks. Institutional investors will also gain an alternative investment method that is not correlated to economic cycles. As real estate and urban development in mainland China continues to grow, especially in the Great Bay Area, there is significant opportunities for the ILS market in Hong Kong. [*See* "ILS and Convergence Markets" chapter beginning on page 35].

Alongside ILS, the Hong Kong Government also wants to promote the use of captives. The Government has mentioned the development of captive insurance in Hong Kong is one of its priorities for the insurance industry, aiming to license five to ten captives per year. Hong Kong is attractive in its proximity to mainland China which has the size, scale, risk profile and growth plan to utilize captives. Along with China's initiative to internationalize Chinese Renminbi, this combination of currency liberalization and development of captive insurance provides an opportunity for Hong Kong to increase its financial product offerings. Further, with the relaxing of financial restrictions in mainland China to foreign companies, Hong Kong has an unprecedented opportunity to host captives. The potential of insurance service expansion in Hong Kong also creates an opportunity for the development of insurtech within the sector. A local captive market potentially leads to an increase in tailored or bespoke risk management and captive management systems in aid of the operation of captives.

China

In recent years, the China Banking and Insurance Regulatory Commission ("**CBIRC**") has made remarkable progress in opening up to foreign investors in the banking and insurance sectors, with 34 measures released to encourage liberalization in the past two years. Since the beginning of the year, the regulator has issued administrative approvals for several foreign-funded institutions to set up insurance agencies, including AXA and Allianz.

We highlight some of the significant regulatory developments throughout the course of 2019 which contributed to liberalization below:

- In July 2019, the CBIRC announced that the 51% foreign shareholding restriction in joint venture life insurance companies will be lifted in 2020, one year earlier than originally planned.
- On October 15, 2019, the amended "Regulations on Administration of Foreign-Funded Insurance Companies" came into force. The revised regulations removed existing requirements for foreign insurance companies to have at least 30 years of relevant experience and to have operated a representative office in China for at least two years before setting up business. In addition, overseas insurance groups are now permitted to establish foreign-funded insurers in China, and overseas financial institutions may hold stakes in foreign-funded insurers.
- In December 2019, the CBIRC announced that it will further reduce the number of items on its "negative list" in order to ease market access and ensure that liberalization policies are effectively implemented.

On October 1, 2019, new bancassurance regulations issued by the CBIRC came into force. The comprehensive set of regulations cover access to bancassurance channels, operating rules, exit from bancassurance operations, management and supervision of bancassurance. For the first time, the CBIRC set out quantitative requirements for protection products sold through bancassurance, such as the premium income generated from various types of life and health insurance, and annuities with a term of no less than ten years. Other provisions include:

- Banks are required to obtain an insurance agency licence in order to offer bancassurance services;
- Insurance sales personnel in banks should have at least one year of insurance sales experience and must have received a required amount of training and a favourable track record; and
- Restrictions on the type of products to be sold to low-income individuals and senior citizens.

Indonesia

In February 2019, the Directorate General of International Trade at the Indonesian Ministry of Trade ("**DGIT**") finally issued the long-awaited implementing regulation for the mandatory procurement of insurance Regulation No. 02/DAGLU/PER/1/2019 ("**DGIT 2/2019**") following the issuance of the Minister of Trade Regulation No. 82 of 2017 regarding Provision on Utilization of Sea Transportation and National Insurance for Export and Import of Certain Goods ("**MR 82/2017**"), which was first issued in October 2017, and subsequently amended. Under Article 4 of the DGIT 2/2019, from February 1, 2019 onwards, exporter/importers of coal, crude palm oil, rice and goods for government procurement are required to procure insurance from an Indonesian insurance company and/or Indonesian insurance consortium.

Myanmar

Foreign insurance companies had been largely barred from operating in Myanmar (except the three foreign insurers that have already been licensed to operate in the Thilawa Special Economic Zone).

The government moves to attract foreign investment by introducing new Myanmar Companies Law on August 1, 2018, which permits foreign investors to take up 35% in local companies, including non-life joint ventures. In January 2019, the Ministry of Planning and Finance ("**MOPF**") issued the announcement No. 1/2019 that the government would grant permission to foreign companies wishing to operate businesses offering life and non-life insurance in Myanmar.

As of November 2019, the Financial Regulatory Department, under MOPF, awarded licenses to five fully foreign-owned life insurers and six joint venture companies for insurance services. It was the first time the government granted license to fully foreign-owned life insurers to issue life insurance policies in Myanmar. The Financial Regulatory Department, under the Ministry of Planning and Finance, has authored a proposed Insurance Business Law which is currently under public consultation.

Following the liberalization of the insurance sector, insurance providers are preparing to introduce more options to the market where only 1% of the nation's population currently has exposure to insurance.

Malaysia

Following its order that foreign insurers should reduce their shareholdings to a maximum of 70% to comply with the foreign ownership cap introduced in 2009, the Bank Negara Malaysia ("**BNM**") (the country's central bank and regulator for the insurance sector) confirms that all foreign insurers have submitted their proposals to address the minimum 30% Malaysian ownership requirement for their businesses by the deadline of April 30, 2019. BNM will assess the insurers' proposals on a case-by-case basis and will engage in ongoing discussions with the foreign insurers. If approved, these foreign insurers will be exempted from having to pare down their holding to 70% by divesting the remainder to local institutions or via an initial public offering. The exemption scheme kicked off in 2019, when a Singapore-owned foreign insurer contributed MYR 2 billion (US$479 million) fund to a proposed national "B40 Health Insurance Fund", which has allowed its exemption from the minimum 30% local shareholding threshold set by BNM.

Philippines

The Philippines Insurance Commission ("**IC**") is seeking to amend the insurance law, which was last revamped in 2013, to cater to developments like takaful and catastrophe insurance. The IC will pitch the new amendments to the Philippines's Congress by the middle or latter part of 2020.

The proposed amendments are expected to, amongst other things, include a supervisory framework to enforce and monitor insurance companies' compliance with antifraud regulation, public disclosure requirements for insurers, development of reinsurance regulations, and will introduce new rules on agri-insurance as well Islamic, catastrophe and parametric insurance.

Separately, the IC confirms that a majority of general insurers in the Philippine market could not meet increased capital requirements in the Phillipines Insurance Code by the deadline of December 31, 2019. Several insurance companies are expected to merge in order to meet the new capital requirement, and announcements would be made by the relevant insurers.

Early in the year of 2019, the IC deferred the implementation of new accounting rules (IFRS 17) to give life and non-life insurers more time to comply with the new insurance accounting regulation. This gives insurers an additional year from the initial January 1, 2022 deadline set out by the International Accounting Standards Board.

Thailand

In May 2019, Thailand's Supreme Court overturned two lower court decisions and ordered six insurers (New Hampshire Insurance, Dhipaya Insurance, Fall Call Insurance, Bangkok Insurance, Deves Insurance, and Muang Thai Insurance) to pay THB 89 million to the Stock Exchange of Thailand, THB 57,500 to the Thailand Securities Depository, and THB 9 million to the Family Knowhow Company in compensation for losses incurred due to anti-government protests that led to rioting in 2010. The Supreme Court held that the torching of the building and valuables during a riot was not an act of terrorism (due to the numbers of persons causing the damage were very few), and so the damage caused by the rioters was covered under the insurance policy taken out by the claimants.

Amendments to the Non-life Insurance Act B.E. 2535 (1992) and Life Insurance Act B.E. 2535 (1992) became effective on November 21, 2019, introducing the modernization and improvement of Thailand's insurance laws. These amendments mainly deal with insurance intermediaries, i.e., agents and brokers including (i) adopting electronic transactions; (ii) extension of the validity period of loss adjuster licenses from two years to five years; (iii) new qualifications of loss adjusters, agents, individual brokers, or corporate brokers; (iv) introduction of corporate brokers' obligations and liabilities; (v) conditions to terminate an agent or broker's license and suspension procedure; (vi) use of advertisement materials by agent or broker without prior approval from the insurer; and (vii) penalties where breach of regulations including additional daily penalty rates. Three new offences (including fraudulent claim, offering or accepting bribes for the payment of claims, and encouraging a person to enter into an insurance contract by deceitfulness were also introduced). Penalties for these offences extend to the managing directors or other persons responsible for a corporate broker's business operation.

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