

Response to public comments received on Insurance Bill, 2016

Presentation to the Standing Committee on Finance

National Treasury | 10 May 2017



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Department:
National Treasury
REPUBLIC OF SOUTH AFRICA

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Structure of presentation

1. Introduction
2. Background on consultation process
3. Overview of Insurance Bill, 2016 in context of Twin Peaks
4. Overview of key issues addressed in proposed revisions
5. Significant revisions per chapter (refer to comment matrix and revised Bill)



Introduction

- Insurance requires strong regulation:
 - It is a business in which the insurer promises to protect the consumer against the small probability of a large loss in exchange for a regular ongoing payment
 - Insurance is characterised by a high level of asymmetry of information between providers and consumers and requires payment for the service long before the customer has an opportunity to experience its value
 - As a result, this “business of promises” requires a high level of consumer confidence and trust in the industry if markets are to develop and grow
 - Effective regulation and supervision are essential to build consumer confidence and trust and help ensure financial stability
- **Licensing:** ensure that only fit and proper persons are allowed to engage in insurance business – while also addressing transformation [**covered in Bill**]
- **Solvency supervision** helps identify the risk that insurers will be unable to meet their promises to policyholders [**covered in Bill**]
- **Conduct of Business** supervision helps monitor the risk that insurers (and their intermediaries) will not treat their customers fairly [**covered in PPRs to come**]

Introduction contd...

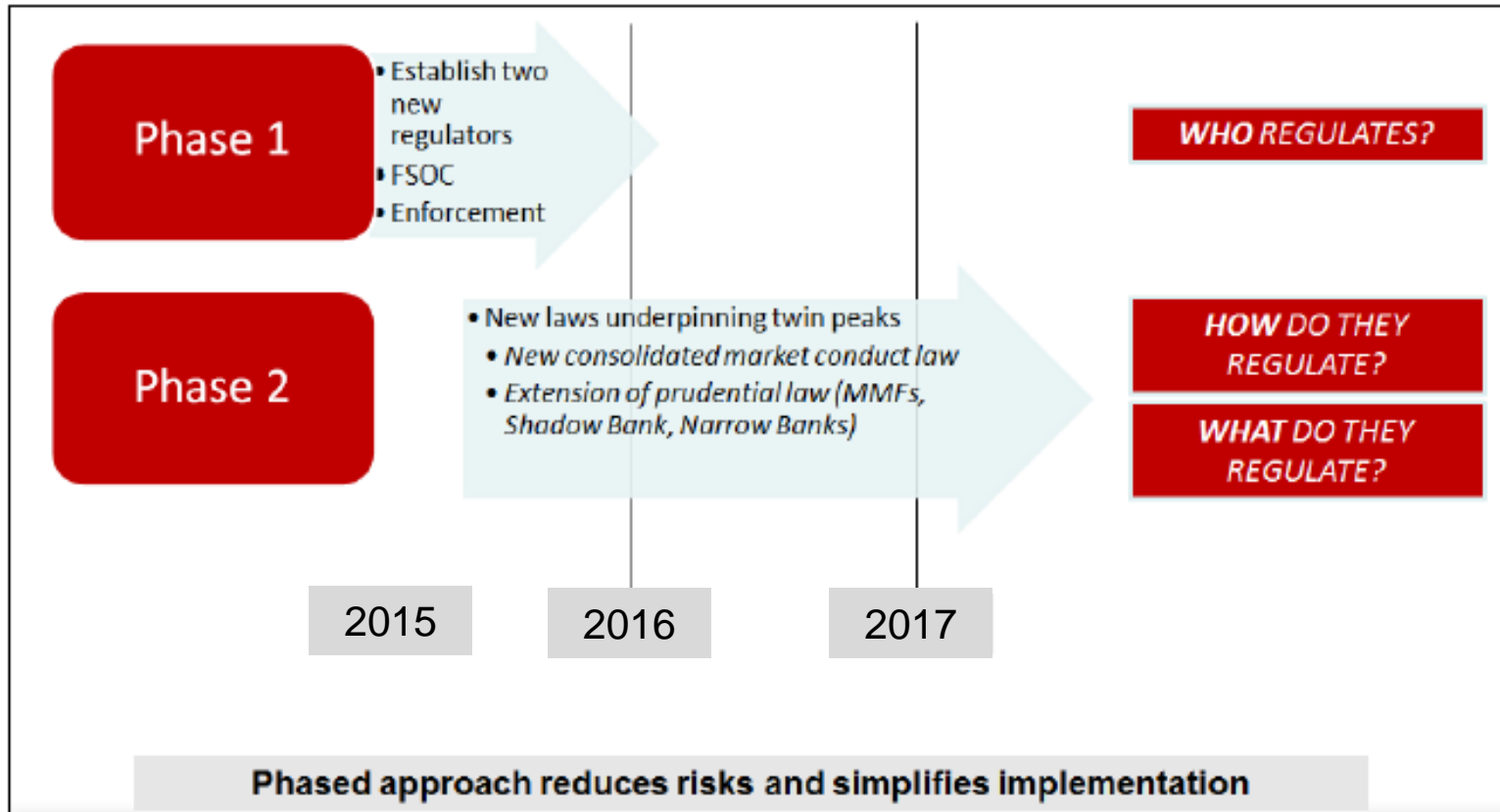
- NT welcomes the opportunity to respond to submissions made during public hearings on the Insurance Bill, 2016 (“Bill”)
 - Detailed responses to public comments set out in supporting matrix and revised Bill
 - Comments focused broadly on transformation of insurance sector, financial inclusion, cost of regulation, certain powers of the regulator, technical amendments & alignment with the Financial Sector Regulation Bill
- NT cognisant of broader transformation issues raised:
 - Focus on implementation of transformation initiatives (Financial Sector Summit, NT ownership monitor, support for SMEs – e.g. emerging panel beaters, auditing/actuarial firms, better data collection and monitoring)
 - Bill explicitly refers to broader transformation policy objectives:
 - Included in objective of Bill
 - Allows for proportionality in applying regulatory standards (proportionate to risk of insurance business and provides for progressive implementation), and balancing for prudential/stability

Background on consultation process

- Cabinet first approved the release of the Bill for comment 15 April 2015
- NT releases Bill for comment 17 April 2015
- Public comment allowed until 29 May 2015 with 34 comments received
 - Comments received from insurers, reinsurers, industry bodies, law firms, NGOs
- Cabinet approved the Bill at its meeting of 4 November 2015
- Minister of Finance tabled the Bill in Parliament 28 January 2016
- SCOF invitation for public comments 15 December 2016
- SCOF briefing on the Bill 24 January 2017
- SCOF public hearings on the Bill 7 February 2017
 - 19 public comments received
- Today NT responds to public comment and proposes changes to the Bill

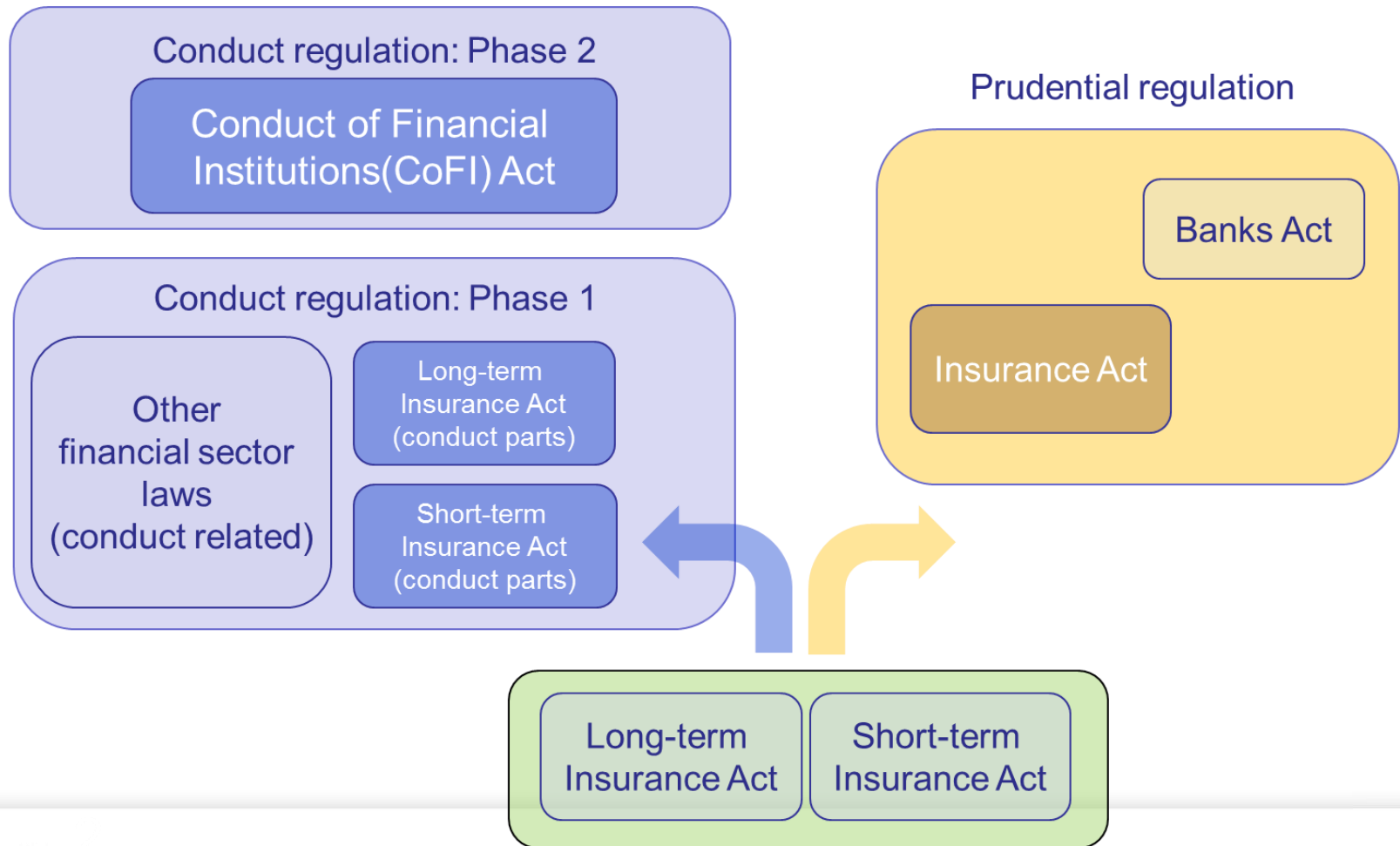
Overview of Insurance Bill, 2016 in context of Twin Peaks

Bill is part of Phase 2 of Twin Peaks reforms



Overview of Insurance Bill, 2016 in context of Twin Peaks contd...

Twin Peaks Reforms – how Insurance Act fits in



Background to the Bill

- Builds on the Twin Peaks model of financial regulation envisaged in the FSRB in respect of prudential supervision
- Provides a consolidated legal framework for the prudential supervision of insurers as envisaged in the FSRB
- Insurance Bill will:
 - Promote financial inclusion & insurance sector transformation
 - Enhance safety and soundness of insurers through introducing a new Solvency Assessment and Management (SAM) regime
 - Help maintain financial stability through introducing a framework for insurance group supervision
 - Facilitate alignment with international standards (adapted to South African circumstances) in accordance with South Africa's G20 commitments

Background to the Bill contd...

- Proportionality:
 - Bill entrenches the principle of proportionality - regulatory requirements to be applied in a manner which is proportionate to the nature, scale and complexity of the risks inherent in the business of an insurer, so that requirements imposed on emerging insurers (which do not have complex business models) are not onerous
 - Proportionality applies across all aspects of the Bill
 - Requirements & exemptions may be granted to provide for progressive or incremental compliance with requirements
- Framework legislation:
 - Bill is enabling/empowering
 - Contains the framework for prudential regulation, with the detailed governance, financial soundness and reporting requirements contained in Prudential Standards
 - Prudential Standards to be consulted on and tabled in Parliament following enactment of Bill, in terms of requirements for regulatory instruments contained in FSRB

KEY ISSUES ADDRESSED IN PROPOSED REVISIONS



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Transformation of insurance sector

- A number of amendments have been made to explicitly provide for the realisation of this public policy objective:
 - *Definitions (section 1)*: The term “transformation of the insurance sector” has been defined with reference to the B-BBEE Act
 - *Objective of the Act (section 3)*: The section has been amended to include a specific reference to transformation of the insurance sector
 - *Requirements for licence (section 22)*: The section has been amended to require an applicant to have a clear plan to meet transformation objectives. The PA must take in account the public interest, including transformation when considering a licence
 - *Variation of licencing conditions (section 26)*: Section amended to require PA to take account of transformation when deciding to vary a licence
 - *Exemptions (section 66)*: The section has been amended to empower the PA to exempt any insurer or a controlling company from, or in respect of, a provision of the Bill to achieve developmental, financial inclusion and transformation objectives



Promoting financial inclusion through microinsurance

- Concern that the Bill seeks to distinguish between micro-insurance and macro-insurance business and this will exacerbate lack of transformation in the industry
 - The Bill gives effect to the NT's Microinsurance Policy Document released in July 2011. It balances lowering regulatory barriers to entry, so as to facilitate access and support affordability, while at the same time ensuring that there is appropriate and sufficient consumer protection in place
 - A microinsurance licence provides for other types of non-traditional industry participants – such as financial services cooperatives or funeral parlours – to also be able to conduct insurance business
 - Commercial insurers may also conduct microinsurance business, but this will be optional
 - A microinsurance licence facilitates financial inclusion through having more proportionate regulations (including capital requirements) based on the low risk of microinsurance products from a prudential perspective

Cost of regulation as a barrier to entry

- Section 37: Concern that Prudential Authority may direct a capital add-on if the risk profile of insurer or governance framework deviates from underlying Solvency Capital Requirement calculation. This may result in small black-owned businesses being taken over by big insurers
- To ensure the financial soundness of the insurer so that promises to and claims of policyholders can be met, capital add-ons may be imposed, but this power is limited in the Bill to where the PA reasonably believes that—
 - the risk profile of the insurer or the insurance group deviates significantly from the assumptions underlying the solvency capital requirement calculation or the group solvency capital requirement calculation
 - the governance framework of an insurer or a controlling company deviates significantly from the requirements of this Act
 - PA must review any capital add-on imposed at least once a year and remove the capital add-on when the PA is satisfied that an insurer or controlling company has remedied the deficiencies that led to its imposition



Levies Bill –levy proportional to size of insurer

Alignment with the Financial Sector Regulation Bill

- The Bill was tabled on 28 January 2016, while the FSRB was being processed by the SCOF. The Bill needs to be revised to be properly aligned with the FSRB

Section 1	“Financial Sector Regulation Act”, “fit and proper requirements”, “governing body”, “group of companies”, “head of a control function”, “juristic person”, “outsourcing”, “Prudential Standard”, “Regulation”, “senior manager”, “this Act”, “transformation of the insurance sector”, “winding-up” “General interpretation of Act” and “Objective of Act”
Section 5	Insurance business and limitations on other business
Section 7	Claims against branches of foreign reinsurers or Lloyd’s underwriters
Section 10	Designation of insurance group and licensing of controlling company
Section 12	Transparent insurance group structure
Section 16	Termination of appointment of key persons
Section 17	Changes in control of insurer or controlling company
Section 23	Licensing
Section 44	Claims against branches of foreign reinsurers or Lloyd’s underwriters
Section 62	Designation of insurance group and licensing of controlling company
Section 63	Transparent insurance group structure
Schedule 1	Termination of appointment of key persons

SIGNIFICANT REVISIONS PER CHAPTER



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Long Title & Chapter 1: Interpretation and Objective of Act

- The Long Title of the Bill and the objectives clause has been amended to explicitly refer to Constitution
- “*microinsurance*” The definition has been amended to include agriculture in the classes of business that may be underwritten by microinsurers
- “*reinsurer*” The definition has been amended to allow reinsurers to conduct insurance business directly with a medical scheme registered under the Medical Schemes Act, 1998
- “*state-owned insurer*” to remove the criterion that such an insurer must be established under or establishment must be authorised under an Act of Parliament. This criterion has been provided for in section 22
- *Section 3: Objective of Act* - The section has been amended to explicitly recognise that the objective of the Bill is to be achieved in a manner that is consistent also with the Constitution and the addition of an explicit reference to transformation of the insurance sector

Chapter 2: Conducting insurance business & insurance group business

- *Section 5: Insurance business and limitations on other business* – The section has been amended to –
 - remove the requirement that reinsurers must secure the approval of the PA to conduct any business outside the Republic.
 - in light of the amended definition of “state-owned insurer”, remove the requirement that a state-owned insurer may not conduct insurance business that is not explicitly authorised under the Act of Parliament that established it or authorised its establishment. This requirement has been provided for in section 22
 - exemption provision relating to state-owned entities as all insurers must be subject to similar minimum requirements removed
 - *Section 10: Designation of insurance group and licensing of controlling company* –has been amended to oblige the PA to, as part of designating an insurance group, also designate the holding company or juristic person that must apply for a licence as a controlling company of that insurance group

Chapter 4: Licensing, suspension and withdrawal of licence

- *Section 22: Requirements for licence:* The section has been amended to allow reinsurers and all insurers to also be co-operatives registered under the Co-operatives Act. This will allow for the establishment of mutual insurers
- *Section 25: Licence conditions* – The section has been amended to allow the PA to impose conditions in a manner that seeks to facilitate the progressive or incremental compliance with the Bill by a specific insurer to promote developmental, financial inclusion and transformation objectives

Chapter 6: Financial soundness

- *Section 40: Security to be held in trust* – The section has been amended to clarify that security must be provided by Lloyd’s underwriters and to facilitate the definition of “business conducted in the Republic” in order to clarify what is regarded as insurance business conducted in the Republic by branches of foreign insurers and Lloyd’s underwriters
- *Section 41: Trust and trustees* - The section has been amended to clarify that the security held in the trust may not, without the approval of the PA, be withdrawn or accessed by a foreign reinsurer, a Lloyd’s underwriter or Lloyd’s even in circumstances where the funds in the trust exceeds the required technical provisions

Chapter 7: Reporting and public disclosures

- *Section 47: Auditing requirements* - The section has been amended to clarify that the audited annual financial statements of the controlling company need not be made available to the public

Chapter 10: Administration of Act

- *Section 62: General powers, and functions and duties of PA:* This section has been amended to explicitly provide –
 - that the Promotion of Administrative Justice Act applies to any approval, determination, designation, decision, exemption or other administrative action taken by the PA
 - for specific matters that must be considered (such as the nature, scale and complexity of the business of an insurer or an insurance group, submissions made and the like)
- *Section 63: Prudential standards:* This section has been amended to explicitly provide for specific matters that must be considered (i.e. the objective of the Bill, international regulatory and supervisory standards, to the extent practicable and with due consideration to the South African context and the nature, scale and complexity of different kinds or types of insurers and controlling companies)
- *Section 66: Exemptions:* This is a new section that includes specific matters that must be considered when granting exemptions (such as practicalities, proportionality and developmental, financial inclusion and transformation objectives). The section on delays and exemptions in the tabled Bill has been moved to Schedule 3

Schedule 1: Laws amended

- An updated schedule is proposed which provides for
 - alignment with the Bill, the FSRB and additional amendments necessitated by market conduct reforms such as imposing requirements relating to the collection of premiums by intermediaries in the Long-term Insurance Act
 - extending the matters in respect of which Policyholder Protection Rules may be made and to limit offences to non-compliance in respect of which no administrative remedies are available to the PA

Schedule 3: Transitional arrangements

- *Repeal of matters prescribed under previous Act:* This item has been amended to ensure the continuation of the demarcation regulations made in December 2017
- *Maintenance of financial soundness:* This item has been amended to facilitate an appropriate transitional period for existing reinsurance arrangements.
- *Lloyd's:* This item has been amended to facilitate an appropriate transitional period
- *Delays and exemptions:* A new item was added to facilitate the incremental implementation of the Bill

Documents available to the Committee

- Detailed matrix responding to public comments
- Proposed revised Bill, taking into account public comments

QUESTIONS