Topix
MELVILLE JESSUP WEAVER
CONSULTING ACTUARIES TOWERS PERRIN ALLIANCE PARTNER

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Insurance (Prudential Supervision) Bill

Background

Work began several years ago to bring NZ's insurance regulation into line with international norms and in April 2009 a "consultation draft" of legislation for a new regime was released for stakeholder consultation.

The real thing was released on 29 October, in the form of the Insurance (Prudential Supervision) Bill, which was given its first reading on 8 December and immediately referred to the Finance and Expenditure Committee. The purposes of the Bill are:

- to promote the maintenance of a sound and efficient insurance sector and
- to promote public confidence in the insurance sector.

Change is very much the order of the day for the finance sector at the present time. A number of other changes in regulation for the sector are also at various stages of development.

Submissions and deadlines

The deadline for written submissions on the Insurance (Prudential Supervision) Bill is 10 February 2010 and the FEC is expected to report back to Parliament by 30 June.

The proposed prudential supervision regime is a major change. Insurers should be seeking legal, accounting and actuarial advice as to how the regime will affect their business and whether there are any issues they wish to raise in submissions to the FEC as a result.

Insurance (Prudential Supervision) Bill

The Bill runs to 191 pages and sets out a comprehensive new regulatory structure for entities that issue "contracts of insurance".

Insurance is not defined, because of the difficultly of doing so with precision. Rather, a general definition of contract of insurance is used, with various types of contract being specifically excluded. Contracts declared by regulations to be not insurance are also excluded.

The RBNZ will be the regulator of all general, health and life insurers, which the Bill specifies to include Friendly Societies and Credit Unions. Its powers include licensing, specifying regular reporting requirements, investigations and dealing with "distressed" insurers.

The explanatory note and general policy statement which accompany the Bill provide a useful overview of the legislation.

Key provisions include:

- Insurers that "carry on business in NZ" (as defined in the Bill) must be licensed.
- The directors and certain staff of insurers must be fit and proper.
- Approval for transfers and amalgamations.
- Solvency standards.
- Disclosure of financial strength ratings, which are mandatory for most insurers.
- Risk management programme.
- Appointed actuary.
- Statutory fund for life insurance ("life policy" is also defined in the Bill).
- Whistle blowing responsibilities.
- Statutory management provisions.

RBNZ will have the power to impose conditions for the granting of a licence. Clearly such conditions will be important but the approach that will be taken by RBNZ in practice is not yet known.

Many other issues are set out in detail in the Bill and we refer the reader to the summaries and commentaries already issued by various other advisory and professional groups.

Implementation timetable

The Bill includes information on how transition to the new regime will be managed. Enactment is currently expected to be in September 2010.

All insurers will need to obtain a licence (provisional or full) within 18 months of the date the Bill is enacted, and a full licence within 3 years of that same date. There is a special form of provisional licence for insurers who intend to exit the market.

As an illustration, we set out below the licensing timetable based on an assumed enactment date:

01 Oct 10	Act passed (assumed)
31 Dec 10	Final date to register intention to apply for full licence
31 Mar 12	Final date to apply for a full licence
30 Sep 13	Provisional licences expire

We understand that RBNZ will be meeting with each insurer to discuss a "path to compliance" in accordance with the required timeframes.

AMP Chambers Level 5 187 Featherston Street
PO Box 3109 Wellington 6140 NZ
Tel: +64 (4) 499 0277 Fax: +64 (4) 499 0488
wgtn@mjwactuary.co.nz

www.mjwactuary.co.nz

South Canterbury Finance Building 6 57 Fort Street
PO Box 4014 Auckland 1140 NZ
Tel: +64 (9) 300 7155 Fax: +64 (9) 300 7199
akld@mjwactuary.co.nz

Solvency standards

One of the most important outcomes of the new supervision environment will be solvency standards. The standards will be specified in regulation, which allows greater flexibility. As well as the rules for calculating solvency, other important areas of detail will be the way the rules apply for overseas insurers and the requirements for financial condition report.

RBNZ must consult with parties that will be substantially affected before issuing solvency standards and must also consult regarding changes of other than a minor nature. Matters that *may* be contained in a solvency standard are listed. No minimum dollar amount of capital is specified, although that is expected to be prescribed within the standards.

In July 2009, RBNZ released a draft "Solvency Standard for Non-Life Insurance Business" developed by RBNZ in conjunction with the NZ Society of Actuaries. A description of this draft standard was set out in our Topix dated September 2009 – please let us know if you would like a copy of that earlier Topix.

A calculation template (spreadsheet) to determine a general insurer's solvency position according to the draft standard was circulated by RBNZ in November. Insurers were asked to complete and return it, to enable RBNZ to better analyse the proposed approach by assessing its effect at an individual insurer level. Completion was by no means a simple matter, and the process and results no doubt threw up interesting issues for some entities.

Development of a solvency standard for life insurers has now begun, also in conjunction with the NZSA. The new standard is expected to be based on the existing actuarial professional standard "Solvency Reserving for Life Insurance Business."

Actuarial reports

NZ actuaries have been preparing Financial Condition Reports for life insurers for many years. Some general insurers also have FCRs, generally because of the regulatory requirements of their parent companies.

The FCR is a confidential document that provides the Board of an insurer with an overall view of its situation. This would typically include a prospective view of the company's solvency as well as comment on the insurer's risk management programme including reinsurance arrangements, assessments of its assets, insurance liabilities and premium adequacy, and an overview of its operations.

It is not clear at this stage whether the actuarial report envisaged under the Bill will be a "full" FCR as described above, or a report that is limited only to matters relating to the application of the solvency standard. However, we are firmly of the view that the additional material described in the previous paragraph would be invaluable to each entity's Board.

Final word

Any readers interested in more details are invited to contact MJW. We'd welcome the opportunity to assist in preparing submissions.

We understand that RBNZ intends to consult (as far as is practical) regarding the detail of the various regulations. While regulations cannot be made until after the legislation is enacted, it may be that consultation drafts will be issued earlier. We also understand that guidelines will be available in due course on matters such as fit and proper policies and risk management programmes. We will keep you informed as and when we become aware of any progress in these important areas.

For further information please contact:
Neil Christie
Auckland *Phone (09) 300 7571*
Janet Lockett
Linda Caradus
Wellington *Phone (04) 499 0277*

ABOUT MELVILLE JESSUP WEAVER

Melville Jessup Weaver is a New Zealand firm of consulting actuaries. The areas in which we provide advice include superannuation, employee benefits, life insurance, general insurance, health insurance, asset consulting, accident insurance and information technology. The firm, established in 1992, has offices in Auckland and Wellington.

Melville Jessup Weaver is affiliated to Towers Perrin, a global professional services firm that helps organisations around the world optimise performance through effective people, risk and financial management. Towers Perrin has offices in 25 countries and the business covers human resources services, reinsurance and Tillinghast.

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