MAYER BROWN

Global Corporate Insurance and Regulatory Bulletin

INSURANCE & REINSURANCE INDUSTRY GROUP

Second Quarter 2014

Global Corporate Insurance & Regulatory Bulletin

INSURANCE & REINSURANCE INDUSTRY GROUP

Second Quarter 2014

Contents

AMERICAS/US

US – ONGOING CONSIDERATION BY NAIC OF RESERVE FINANCING, USE OF CAPTIVES, AND PRINCIPLE-BASED RESERVING

During the first half of 2014, the NAIC, through its various task forces and working groups, has continued its work on reserve financing issues, including the use of captive reinsurers for so-called AXXX and XXX reserve financing transactions and the potential use of principle-based reserving. As summarized in a February 17, 2014 report from Rector & Associates, Inc. ("Rector") to the NAIC's Principle-Based Reserving Implementation (EX) Task Force (the "PBRI Task Force"), the use of AXXX and XXX financing transactions "arises from the belief of some insurers that current reserving and statutory accounting requirements force them to carry traditional insurance admitted assets in larger amounts than is necessary, thereby increasing costs to insurers and policyholders. Those insurers want to fund reserve liabilities using assets, including traditionally non-admitted assets, which in their view better correlate to the probability the assets will be needed to pay claims." Further background on this topic is available in our First Quarter 2014 Bulletin.

Rector Reports and the XXX/AXXX Framework

On June 30, 2014, the PBRI Task Force voted to adopt a framework for financing transactions relating to (1) reserves required for level premium term life insurance policies under Regulation XXX and (2) reserves required for universal life insurance policies with secondary guarantees under Regulation AXXX (the "Framework"). The Framework is based on the modified recommendations presented by Rector to the PBRI Task Force on June 4, 2014 (the "Modified Rector Recommendations"). The Modified Rector Recommendations reflect revisions to the recommendations in Rector's February 17, 2014 report, which had itself followed upon Rector's initial report of September 13, 2013.

The primary goals of the Framework are to require ceding insurers to provide disclosure of all XXX and AXXX reserve financing transactions, establish uniform set of collateral requirements across the US for such transactions, and apply risk-based capital requirements to such reserve financing transactions. As described further below, a significant amount of work still needs to be done with respect to these proposals, including the need for adoption of the Framework by the NAIC's Executive Committee. Although Rector has recommended an aggressive implementation schedule, it remains to be seen to what extent and in what form the recommendations in the Framework will eventually be adopted.

Summary of the Framework

The Framework and its security requirements for reinsurance would apply only to reinsurance involving certain types of XXX and AXXX policies (i.e., those required to be valued under Sections 6 or 7 of the NAIC Valuation of Life Insurance Policies Model Regulation). The Framework would not materially change the ability of insurers to obtain credit for reinsurance ceded to certified reinsurers, licensed reinsurers or accredited reinsurers that follow statutory accounting and/or RBC rules, or unauthorized reinsurers that provide collateral security in one of the standard forms (i.e., funds withheld, unconditional letters of credit or collateral trusts). Rather, the Framework security requirements would apply to XXX and AXXX cessions to reinsurers that do not fall into the foregoing categories. Under the Framework's security requirements, a ceding insurer would receive credit for reinsurance if, and only if:

- The ceding insurer establishes gross reserves, in full, based on applicable reserving guidance (i.e., the so-called "formulaic" approach).
- The ceding insurer satisfies the Primary Security Requirement (i.e., the ceding insurer receives as collateral in the form of "Primary Security," as described under "Implementation of the Framework" below, in at least the amount determined pursuant to the Actuarial Method, as described below).
- However, portions of the statutory reserve which exceeds the Primary Security Requirement may be collateralized by Other Security. In other words, so long as the Primary Security Requirement is satisfied, the ceding insurer may receive as collateral for the remainder of the statutory reserve any other security as to which the NAIC has developed an RBC "asset charge," to be developed by the NAIC Capital Adequacy (E) Task Force ("CATF").
- At least one party to the financing transaction holds an appropriate RBC "cushion," the parameters of which would be developed by CATF.
- The reinsurance arrangement is approved by the ceding insurer's domiciliary regulator.

Implementation of the Framework

The Modified Rector Recommendations called for the PBRI Task Force to take the steps listed below to implement the proposed Framework. After exposing the Modified Rector Recommendations for public comment, the PBRI Task Force voted at its June 30, 2014 meeting to proceed with the first four of the following steps:

- Charge the NAIC's Blanks (E) Working Group with adopting a XXX/AXXX Reinsurance Supplement to be filed by insurers ceding XXX/AXXX business beginning with the 2014 data year. The goal of the supplemental filing is for the ceding insurer to provide transparency regarding the assets and reserves pertaining to reinsurance of XXX/AXXX policies, especially when the assuming reinsurer is not subject to public disclosure requirements for these data points.
- Charge the NAIC's Financial Analysis Handbook (E) Working Group with developing, for year-end 2014, a new section for the *Financial Analysis Handbook* that specifies procedures for domestic/lead/captive states' review of XXX/AXXX reinsurance transactions with captives/special purpose vehicles to be performed initially and on an ongoing basis, consistent with recommendations from the NAIC's Financial Analysis (E) Working Group.
- Charge the NAIC's Life Actuarial (A) Task Force ("LATF") with developing the Actuarial Method for the PBRI Task Force's review and consideration in adopting items such as the XXX/AXXX Reinsurance Model Regulation (the "Model Regulation") and possible changes to the Actuarial Opinion Memorandum Regulation ("AOMR"). The Actuarial Method is to consist of the NAIC Valuation Manual, VM-20, Requirements for Principle-Based Reserves

for Life Products, modified to incorporate changes to mortality tables as developed by the American Academy of Actuaries and any other appropriate modifications determined by LATF, and is to maintain (in current or modified form) or eliminate the "net premium reserve" component of the current VM-20. In the event the Model Regulation is not completed as planned in 2014, this Actuarial Method may be used by states on a voluntary basis in the interim period. Moreover, even before the Model Regulation is implemented, this Actuarial Method proposal may be considered for inclusion in the Financial Analysis procedures referenced above as an appropriate and consistent method for determining whether the ceding insurer has received sufficient collateral to support its policy obligations.

- Adopt the Framework and proposed implementation steps and submit them to the NAIC's Executive Committee for adoption.
- Develop an Actuarial Guideline ("AG") to provide interim guidance for the AOMR as it relates to XXX/AXXX reinsurance transactions, where the AG should specify that, in order to comply with AOMR, the opining actuary must issue a qualified opinion as to the ceding insurer's reserves if the ceding insurer or any insurer in its holding company system has engaged in a XXX/AXXX reserve financing transaction that does not adhere to the Actuarial Method and Primary Security forms adopted by the NAIC. Actuarial Method would consist of VM-20, modified to incorporate changes to mortality tables as developed by the American Academy of Actuaries and any other modifications suggested by the Life Actuarial (A) Task Force. Whether to alter or eliminate the net premium reserve component is still being determined.
- Primary Security would consist of types of assets listed in the Credit for Reinsurance Model Law Section 3.A (cash) and 3.B (SVO-listed securities meeting certain characteristics). To what extent, if any, clean, irrevocable, unconditional "evergreen" letters of credit should be allowed as Primary Security is still being determined. Request permission from the NAIC's Executive Committee to amend the AOMR and draft those amendments to specify that, in order to comply with the AOMR, the opining actuary must issue a qualified opinion as to the ceding insurer's reserves if the ceding insurer or any insurer in its holding company system has engaged in a reserve financing transaction that does not adhere to the Model Regulation and other aspects of the XXX/AXXX Framework, as adopted by the PBRI Task Force.
- Develop the proposed definition for "Primary Security" for use in the PBRI Task Force's future consideration of a proposed Model Regulation.
- Develop a Note to the Audited Financial Statements regarding compliance with the Model Regulation.
- Develop an appropriate "RBC Cushion" for an insurer ceding XXX/AXXX policies when the assuming reinsurer does not file an RBC report using the NAIC RBC formula and instructions.
- Develop appropriate asset charges for the forms of "Other Security" used by insurers under the Model Regulation.

- Evaluate the risk-transfer rules applicable to XXX/AXXX reserve financing transactions to make sure they appropriately apply to situations such as those where parental/affiliate guarantees are used, resulting in the risk effectively being kept within the holding company system even though the reinsurance arrangement involves an unrelated third party.
- As the various work products are adopted by the PBRI Task Force, Executive Committee, and Plenary, consider them for inclusion in the Part A and Part B Accreditation Standards.

Implementation of the Modified Rector Recommendations, as adopted by the PBRI Task Force on June 30, 2014, will require a large amount of work by multiple groups within the NAIC to develop and codify the various elements of the Framework. Accordingly, it is unclear whether the aggressive timetable for implementation with respect to year-end 2014 can be met. In the meantime, it should also be mentioned that the PBRI Task Force's adoption of the Framework was not unanimous, and that dissenting votes were cast by the representatives of California and New York.

US – REGULATORY INITIATIVES RELATING TO ACQUISITIONS OF INSURERS BY PRIVATE EQUITY FIRMS

As reported in our prior bulletins, a number of US insurance regulators have expressed concerns about the growth in acquisitions of insurance companies by private equity firms. There have been two recent initiatives on this topic.

NY DFS Proposes Amendments to Regulation 52

On May 14, 2014, NY DFS released for public comment proposed amendments to certain provisions of its Regulation 52 (11 NYCRR 80-1) relating to information that must be provided by applicants seeking approval of an acquisition of control of a New York-domiciled insurer under Section 1506 of the New York Insurance Law. According to the regulatory impact statement that accompanied the proposed amendments, NY DFS "is concerned that private equity firms, and other investors with a similar investment horizon, focus on maximizing their short-term financial returns rather than ensuring that long-term policyholders receive the insurance benefits for which they have paid." The proposed amendments and regulatory impact statement are available here.

The proposed amendments, which are apparently modeled on agreements reached by NY DFS with two private equity firms that recently acquired New York annuity companies, appear to focus on acquisitions by private equity firms of life insurers (e.g., a trust account may be required in connection with life insurer acquisitions). However, the scope of the proposed amendments is broad, and many of the amended provisions would apply to all potential acquirers of New York-domiciled insurers, not just to acquisitions by private equity firms.

Specifically, the proposed amendments require the potential acquirer and other controlling persons to submit their financial statements, investor solicitation materials and any management or operating agreements or any other agreements pursuant to which control is exercised over the applicant. The applicant and its controlling persons must also submit any plans or proposals to change the target insurer's business operations in the five-year period following the acquisition. Such plans or proposals may not be modified or amended after the acquisition without the prior written approval from the NY DFS. In addition, the proposed amendments formalizes the longstanding “desk drawer” rule that the applicant must provide five years of financial projections as part of its proposed business plan for the target insurer. Furthermore, new five-year projections will need to be submitted if the insurer enters into any of the following transactions with the applicant or any person controlling, controlled by or under common control with the applicant within five years of the date of the acquisition: (1) any reinsurance treaty or agreements, (2) any investment, loan, or asset purchase transactions or (3) any transactions encumbering the insurer’s assets to, or for the benefit of, the applicant or any person controlling, controlled by or under common control with the applicant. NY DFS may require the insurer to obtain additional capital if NY DFS determines that the insurer will not have adequate capital under the new projections.

Under the proposed amendments, in the case of life insurer acquisitions, the applicant may be required to establish a trust account if NY DFS determines that the acquisition is likely to be hazardous or prejudicial to the insurer’s policyholders or shareholders. In making such a determination, NY DFS may consider, among other factors, whether the applicant or any person controlling, controlled by or under common control with the applicant is:

- Registered or required to register with the SEC pursuant to the Investment Advisors Act of 1940, or otherwise would be required to register if it had $150 million or more assets under management;
- An investment company, as defined in the Investment Advisors Act of 1940;
- An entity that was formed within 36 months prior to the date of the Form A filing;
- A company primarily engaging in investing or investment management activities; or
- An entity that holds for investment purposes a portfolio where non-publicly registered securities or holdings represent 50% or more of the assets of that entity.

The 45-day comment period for the proposed amendments ended on June 28, 2014. In a June 25, 2014 comment letter, the Insurance Committee of the New York City Bar expressed concern that the proposed amendments would change the scope of the Section 1506 *preacquisition* approval process to a provision for the *post-acquisition* oversight of insurers and their controlling persons. In the commenters’ view, this raises the possibility that a Section 1506 approval, upon which parties rely in order to complete a transaction, would be, in effect, subject to conditions subsequent and would not provide the contract certainty that both buyers and sellers need in order to close a transaction.

Initiatives from the NAIC Private Equity Issues (E) Working Group

On June 11, 2014, the NAIC’s Private Equity Issues (E) Working Group (the “PEI Working Group”) held a conference call in which representatives from NY DFS summarized the proposed amendments to Regulation 52 described above. The chair of the PEI Working Group, Deputy Commissioner Doug Stolte of Virginia, then asked members of the PEI Working Group to individually consider, prior to their next meeting on August 17, 2014, whether the NAIC should pursue similar changes to the NAIC's Model Insurance Holding Company System Regulatory Act.

In addition, the PEI Working Group voted to expose certain proposed changes to the NAIC's *Financial Analysis Handbook* for a 45-day comment period ending July 28, 2014. The proposed changes to the *Financial Analysis Handbook* were developed by the NAIC staff (in response to a request made by the PEI Working Group on March 30, 2014) to provide additional guidance for state insurance examiners who review "Form A" applications for acquisitions of control of insurers.

The proposed changes would focus the examiner's attention on the following considerations:

- Consideration of all aspects of the financial condition of the acquiring entity, including its group business model, its strategy in general and its specific strategy in purchasing the insurer, including the expected benefits to the acquirer of the proposed acquisition.
- Consideration of the risks of the acquiring entity and the entire group of insurers *and non-insurers* under its control – including credit, market, pricing, underwriting, reserving, liquidity, operational, legal, strategic and reputational risks – with a particular focus on the risks associated with the acquirer's proposed investment strategies.
- Consideration of possible stipulations that a state may wish to consider requiring as a condition of its approval of a proposed transaction, such as:
  - maintenance of RBC at a specified amount (e.g., 450% of Company Action Level),
  - submission of RBC reports on a quarterly rather than annual basis,
  - requirement of regulatory approval for the insurer to pay dividends during a specified period,
  - requirement of a capital maintenance agreement or establishment of a prefunded trust account,
  - disclosure of equity holders in the acquirer "up the chain" to the ultimate controlling person, and
  - requiring personal financial statements of directors of the insurer and the acquiring entities "up the chain" to the ultimate controlling persons.
- Consideration of certain post-acquisition measures, such as annual stress testing of the insurer and its affiliated group, or targeted examinations to ensure that the investment strategy continues to be prudent.

US – EFFORTS TO EXTEND TRIA ADVANCE IN US CONGRESS

In recent weeks, there has been significant progress in the efforts to obtain Congressional reauthorization of the US federal terrorism risk insurance program that was established under the Terrorism Risk Insurance Act of 2002 ("TRIA"). Enacted in 2002 after the September 11, 2001 terrorist attacks, TRIA created a US government facility to provide coverage to insurance companies following an act of terrorism. The Terrorism Risk Insurance Extension Act of 2005 extended the program until December 31, 2007, and the Terrorism Risk Insurance Program

Reauthorization Act of 2007 extended the program until December 31, 2014, when it is currently due to expire.

On July 16, 2014, the Committee on Financial Services of the House of Representatives approved H.R. 4871, the "TRIA Reform Act of 2014," and forwarded it to the full House of Representatives for consideration. H.R. 4871 would extend TRIA for five years, until December 31, 2019, but it would also make changes in program parameters that would reduce the share of insured losses paid by the federal government and increase the share paid by private insurers.

- H.R. 4871 would bifurcate the definition of "act of terrorism" and require the Secretary of the Treasury, when certifying an event as an act of terrorism to include a determination as to whether the event involves nuclear, biological, chemical or radiological ("NBCR") terrorism.
- The bill would change the program trigger, which is the level of aggregate insured losses from a certified act of terrorism that must be incurred before insurers would become eligible for federal assistance. For non-NBCR acts of terrorism, the trigger would increase incrementally from $100 million in 2015 to $500 million in 2019. The trigger for NBCR acts of terrorism would remain at $100 million.
- Under TRIA, an insurer suffering losses as a result of a certified act of terrorism would pay claims up to a specified deductible. H.R. 4871 would maintain the current deductible level – 20% of property and casualty insurance premiums collected in the year preceding the act of terrorism.
- After the deductible is met, TRIA requires a cost-sharing component. The federal share of insured losses is currently 85%, and insurers must absorb the remaining 20%. Under H.R. 4871, the federal share of insured losses would be reduced incrementally from 85% in 2014 to 80% in 2019. The federal share for NBCR acts of terrorism would remain at 85%.
- H.R. 4871 would increase the industry retention amount – the amount of federal payouts that the federal government would recover via a surcharge on policyholders – from a fixed amount ($27.5 billion) to a floating amount. The floating amount would be equal to the sum of the deductibles for all insurers participating in the program during the year the act of terrorism occurs. The Congressional Budget Office estimates that this amount would be about $44 billion in 2016.
- Recognizing that the increased program trigger would significantly increase the potential exposure for smaller insurers, H.R. 4871 would require the Secretary of the Treasury to promulgate regulations to allow a smaller insurer to voluntarily opt-out of TRIA's mandate to make terrorism coverage available in all its property and casualty insurance policies – if its state insurance regulator determines that continued participation would create a financial hardship for such insurer or that it would be financially infeasible for the insurer to provide coverage for insured losses.

Members of the Democratic minority of the House Financial Services Committee issued a minority report criticizing the increase in the program trigger and expressing concern that it would force smaller insurers from the market. They also pointed out that because state workers' compensation statutes prohibit insurers from excluding coverage for acts of terrorism, workers' compensation carriers will be unable to take advantage of the small insurer opt-out included in the bill and will be forced to accept the increased potential exposure.

Meanwhile, on July 17, 2014, the US Senate passed its own bill by a vote of 93 to 4. Senate Bill No. 2244, the "Terrorism Risk Insurance Program Reauthorization Act of 2014,"would extend TRIA for seven years, until December 21, 2021, and would make fewer changes to the program parameters than would H.R. 4871.

- Under S. 2244, the federal share of insured losses would be reduced incrementally from 85% in 2014 to 80% in 2019.
- S. 2244 would incrementally increase the industry retention amount from $27.5 billion in 2014 to $37.5 billion in 2019, but would not tie this amount to a formula as would H.R. 4871.
- S. 2244 would not change the program trigger or create a bifurcated regime for NBCR acts of terrorism.

It is, of course, hard to predict the precise nature of the TRIA legislation that will eventually be enacted into law, although proponents of extension have been heartened by the fact that an extension bill has made it out of House committee. There is a certain perception that the momentum is with the House bill because the House has been harder to "sell" on the concept of a TRIA extension (due to a strong sentiment in the House against government programs generally), but it is still too early to make any predictions.

US – NAIC GROUP SOLVENCY ISSUES (E) WORKING GROUP EXPOSURE DRAFT

In 2008, the National Association of Insurance Commissioners ("NAIC") launched its Solvency Modernization Initiative ("SMI") as a critical self-examination of the US insurance solvency regulation framework. One of the emphases of SMI has been to develop a US framework for group-wide supervision. The NAIC's Group Solvency Issues (E) Working Group ("GSI Working Group") has been tasked with leading that effort. On June 5, 2014, the GSI Working Group voted to expose three documents relating to group-wide financial reporting issues for a 30-day comment period that will end on July 7, 2014. The three documents, which are found here, are: (1) a form of spreadsheet currently used for group reporting by a number of states; (2) proposed changes to the NAIC Model Holding Company Registration Statement (Form B); and (3) a preliminary listing of the types of group-wide consolidated data that could be collected in a possible supplement to the annual statement filed by US insurance companies. More generally, the GSI Working Group continues its work on developing potential changes to the current US insurance solvency regulatory framework as it relates to group solvency issues.

US – NAIC 2014 INTERNATIONAL INSURANCE FORUM

The NAIC held its 2014 NAIC International Insurance Forum on May 13-14, 2014 in Washington, DC. The forum consisted of panels covering various issues relating primarily to the regulation and supervision of global insurance companies. The topics covered included group supervision, best practices for supervisory colleges, corporate governance issues, resolution of companies, emerging issues for reinsurers, capital standards for systemically important and international active insurers and financial stability considerations, and emerging market issues. The panels were composed of US, non-US and international regulators as well as members of the US insurance industry

Several themes were consistent across the panels. In particular, many US regulators and US industry representatives expressed concerns about the pace and direction of the development by IAIS of the Common Framework for the Supervision of Internationally Active Insurance Groups ("ComFrame") and the related risk-based global insurance capital standards (including the basic capital requirement (BCR) and higher loss absorbency (HLA) requirements for global systemically important insurers).

LEGAL ISSUES IN CONTRACTING FOR SMAC SERVICES

It is important for insurance and reinsurance companies to consider key legal issues for companies sourcing what are popularly called SMAC: an acronym for Social media, Mobile computing, "big data" Analytics and Cloud computing. Please see the article regarding the key legal issues by the Mayer Brown team, which can be found here.

EUROPE/UK

UK – SOLVENCY II IMPLEMENTATION UPDATE

In March this year, the European Parliament passed the Omnibus II Directive that will amend the Solvency II Directive. The Omnibus II Directive defines the areas in which the European Insurance and Occupational Pensions Authority ("EIOPA") will be able to propose technical standards in relation to Solvency II and the European Securities and Market Authority ("ESMA") in relation to the Prospectus Directive, which addresses the requirements for the publication of prospectuses when securities are offered to the public or admitted to trading. It also details the process by which EIOPA and ESMA will settle disagreements between national supervisors. Furthermore, it includes measures to provide clarity on the treatment of insurance products with long term guarantees to mitigate the effects of long term volatility. Passing of the Omnibus II Directive puts the Solvency II regime on track for implementation on January 1, 2016.

Separately, on April 25th of this year, the United Kingdom Prudential Regulatory Authority ("PRA") issued guidance on the calculation of technical provisions and the use of internal models in a supervisory statement (*Solvency II: calculation of technical provisions and the use of internal models for general insurers (SS5/14)* (http://www.bankofengland.co.uk/pra/Documents/publications/policy/2014/ss5-14.pdf)), in order to help insurers plan for Solvency II. The guidance follows a consultation process on PRA's previous draft statement and is issued on the basis of what outcomes the PRA expects to achieve; the guidance may be subject to future amendment based on future guidelines or regulations from the EIOPA.

With respect to risk models, under Solvency II government bonds are modelled as risk-free investments. However, there are concerns about this approach. For instance, it has been criticised by an official of BaFin, the German insurance industry supervisory body, as German bonds would be deemed as carrying the same risk as Greek bonds; some German insurers using internal models are already incorporating different risk levels for government bonds.

UK – BUDGET 2014 BRINGS SWEEPING CHANGES TO ANNUITIES

In the Spring 2014 budget for the United Kingdom, Chancellor of the Exchequer George Osborne announced sweeping changes to pension rules, the most significant of which was the abolishment of the punitive 55% tax charge on drawdowns beyond the tax free lump sum. This is the sum of money that an individual may take from their pension on retirement without paying tax. The 55% tax on any drawings above this threshold effectively forced pensioners into investing their pensions in annuities provided by the insurance sector. Instead, drawdowns above the tax free amount will be taxed at marginal rates, meaning a reduction to 20% for most pensioners. This change will enter into force in April 2015. This change is expected to lead to few sales of annuities, which until now have been a significant source of revenues and profit margins for UK life insurance companies, and potentially the growth of variable annuities in the UK.

The Chancellor also announced the following changes to pension rules, which came into immediate effect:

1. a reduction in the income requirement for flexible drawdown from £20,000 to £12,000;
2. a raising of the capped drawdown limit from 120% to 150%;
3. an increase of the lump-sum small pot from £2,000 to £10,000; and
4. an increase in the overall size of pension savings that can be taken as a lump sum without incurring a tax liability from £18,000 to £30,000.

Also announced was a promise of free guidance for pensioners, with a £20 million development fund for the scheme; however it has not yet been announced how the scheme shall operate and how it shall be funded on an annual basis, with estimates of the cost ranging from £1 million to £13 million a year.

UK – EIOPA EUROPE-WIDE STRESS TEST FOR INSURERS

On April 30, 2014, EIOPA announced a new round of stress tests for insurance companies to evaluate how the companies would cope with shocks in relation to sovereign debt, corporate bonds, interest rates, property and equity stresses, mortality, longevity, insufficient reserves and catastrophes, in addition to a test for how they would weather the impact of a low investment yield environment. EIOPA has said that the stress test will cover 50% of life and non-life insurance sectors by market share in each European Union Member State. Data is due to be submitted in July and EIOPA will disclose the results of the testing in November.

ASIA

CHINA – LIBERALIZATION OF MARINE INSURANCE IN THE CHINA (SHANGHAI) PILOT FREE TRADE ZONE

On May 19, 2014, the China Insurance Regulatory Commission ("CIRC") announced the following three measures to liberalize the marine insurance industry in the China (Shanghai) Pilot Free Trade Zone (the "FTZ"):

1. Shanghai Institute of Marine Insurance ("SIMI"), which is China's first professional marine insurance association, will be allowed to formulate standard terms and conditions of marine insurance on a trial basis, which, after being registered with the CIRC, may be freely adopted by the members of SIMI;

2. Marine insurance operation centers and reinsurance companies in Shanghai will be allowed to set up branches in the FTZ through registration with the Shanghai Bureau of the CIRC without having to obtain a prior approval of the CIRC or its Shanghai Bureau; and

3. The qualifications of senior management personnel to be appointed to the branches of insurance companies within the FTZ will no longer need to be verified by the CIRC or its Shanghai Bureau before their appointment, and registration with the Shanghai Bureau will suffice.

The FTZ was launched in September 2013 and is designed as an experimental platform to promote trade and investment in China and to explore new channels for the overall deepening of economic reforms in China.

SIMI was launched in December 2013. It currently has 31 members including the major Chinese insurance companies and a number of foreign invested insurance companies in China.

The new measures are expected to simplify regulation of and provide greater flexibility for the industry. They should also foster the standardization of marine insurance terms and conditions which are intended to make China's marine insurance more competitive.

HONG KONG – INSURANCE COMPANIES (AMENDMENT) BILL 2014 GAZETTED

As noted in our First Quarter 2014 Bulletin, after years of drafts and consultation, the Insurance Companies (Amendment) Bill 2014 (the "Bill") was finally gazetted in April. The Bill includes the establishment of the Independent Insurance Authority ("IIA"), which marks a shift in the insurance sector as the industry will cease to be self-regulated by insurers and oversight will be placed thereafter in the hands of the new independent regulator IIA.

The Bill represents a fundamental overhaul of Hong Kong's insurance regulatory framework and should raise the supervisory standards of the local regulations to comparable global levels. It is expected to provide and ensure greater consumer protection and to ultimately facilitate the industry's sustainable development. According to the Legislative Council Brief, a core function of the IIA will be the prudential regulation of insurers, serving to ensure that insurers will be financially sound to meet their obligations. In short, insurers will now need to follow and observe the requirements of the International Association of Insurance Supervisors (the "IAIS") on macro-prudential surveillance, group-wide supervision and corporate governance of insurers. It is possible that certain insurers may need corporate restructuring in order to comply with such requirements.

Another major function of IIA will be to regulate the conduct of insurers and intermediaries. For instance, there will be more vigorous regulation of insurance intermediaries to ensure that sale and post-sale administration of insurance policies are done honestly, fairly and professionally. In particular, *Article 89* of the Bill states that all insurance intermediaries owe a duty to act in the best interest of policyholders.

Other key aspects of the Bill include the administrative side of IIA, including formation of a statutory Insurance Appeals Tribunal to review its decision, statutory requirements to strengthen corporate governance of insurers, powers of inspection, investigation and disciplinary sanctions on insurers and insurance intermediaries, statutory licensing requirement for insurance intermediaries, and transitional arrangements.

HONG KONG – SFC ENHANCES SUPERVISION OF INVESTMENT-LINKED INSURANCE

The Hong Kong Securities and Futures Commission ("SFC") issued a circular on April 30, 2014, which took effect on May 1 2014, requiring all Hong Kong insurance companies offering investment-linked assurance schemes ("ILAS") policies to sign a compulsory confirmation form with the SFC confirming that internal control checks are in place so as to ensure that their offered products are fair to investors. This is intended to further enhance investor protection and bolster confidence in ILAS. In the past, many policyholders have complained about inappropriate selling of ILAS and there was concern about intermediaries who had failed to act in consumers' best interests and failed to ensure suitability of products for consumers; in response the Hong Kong Monetary Authority had previously tightened banks' sale of investment products.

Besides implementing new measures on insurance companies submitting ILAS products to follow, the circular also reminds existing ILAS product providers that these ILAS products are to have a robust internal approval process. The circular provides 14 general principles to which insurance companies should adhere, including with respect to accountability and transparency. Among other things, insurance companies are obliged to have proper risk management systems by way of internal committees and follow applicable disclosure requirements when meeting legal and compliance matters.

All submissions for authorization of SFC-authorized products on or after July 31, 2014 should include a confirmation form along with applications. As for existing ILAS product providers, though they are not required to submit such confirmation forms, there is a continuing obligation to adhere to general product governance principles throughout the life of ILAS products. Failure to comply would lead to a prohibition on offering such products.

Have you seen our Year in Review?

Earlier this year, we published our Global Insurance Industry 2013 Year in Review, which discusses some of the more noteworthy developments and trends in insurance industry transactions in 2013 in the US, Europe, Asia and Latin America, with particular focus on mergers and acquisitions, corporate finance, and the insurance-linked securities and convergence markets. A request for the 2013 Year in Review can be made here.

If you have any query in connection with anything in this Bulletin, please do not hesitate to get in touch with your usual Mayer Brown contact or one of the contacts referred to below.

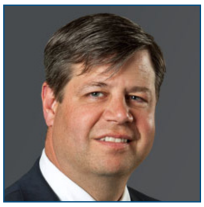
CO-EDITOR
David Alberts
Partner
+1 212 506 2611
dalberts@mayerbrown.com

CO-EDITOR
Lawrence Hamilton
Partner
+1 312 701 7055
lhamilton@mayerbrown.com

CO-EDITOR
Colin Scagell
Partner
+44 20 3130 3315
cscagell@mayerbrown.com

CO-EDITOR
Vikram Sidhu
Counsel
+1 212 506 2105
vsidhu@mayerbrown.com

Global Insurance and Reinsurance Transactions Team

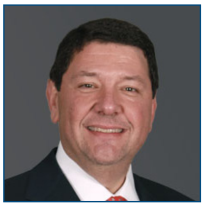


David W. Alberts
Partner, New York
+1 212 506 2611
dalberts@mayerbrown.com

Keith M. Andruschak
Partner, New York
+1 212 506 2658
kandruschak@mayerbrown.com

David S. Bakst
Partner, New York
+1 212 506 2551
dbakst@mayerbrown.com

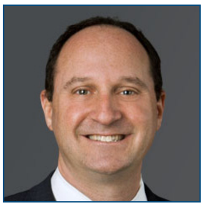
John P. Berkery
Partner, New York
+1 212 506 2552
jberkery@mayerbrown.com



Edward S. Best
Partner, Chicago
+1 312 701 7100
ebest@mayerbrown.com

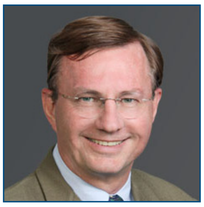
John P. Boelter
Partner, Chicago
+1 312 701 8284
jboelter@mayerbrown.com

Bernd Bohr
Partner, London
+44 20 3130 3640
bbohr@mayerbrown.com

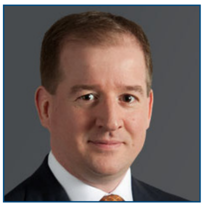


Rory M. Cohen
Partner, New York
+1 212 506 2500
rcohen@mayerbrown.com

Julio Costa
Partner, Rio de Janeiro
Tauil & Chequer Advogados
+55 21 2127 4222
jcosta@mayerbrown.com

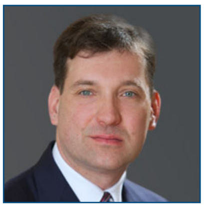


George W. Craven
Partner, Chicago
+1 312 701 7231
gcraven@mayerbrown.com

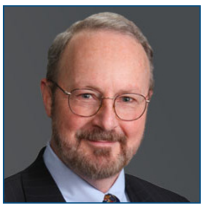


Edward A. Davis
Partner, New York
+1 212 506 2663
edavis@mayerbrown.com

Curtis A. Doty
Partner, New York
+1 212 506 2224
cdoty@mayerbrown.com



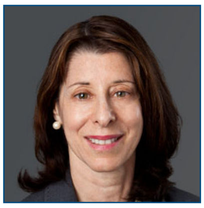
Robert M. Flanigan
Partner, London
+44 20 3130 3488
rflanigan@mayerbrown.com



J. Paul Forrester
Partner, Chicago
+1 312 701 7366
jpforrester@mayerbrown.com

Christof Gaudig
Partner, Düsseldorf
+49 211 86224 224
cgaudig@mayerbrown.com

Patricia V. Gentry
Counsel, Chicago
+1 312 701 7831
pgentry@mayerbrown.com

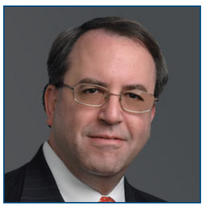


Barbara M. Goodstein
Partner, New York
+1 212 506 2264
bgoodstein@mayerbrown.com

Simon Grieser
Partner, Frankfurt
+1 49 69 79 41 1301
sgrieser@mayerbrown.com

Zhen Han
Partner, Beijing
+86 10 6599 9357
zhen.han@mayerbrownjsm.com

Erwan Heurtel
Partner, Paris
+33 1 53 53 43 43
eheurtel@mayerbrown.com



Lawrence R. Hamilton
Partner, Chicago
+1 312 701 7055
lhamilton@mayerbrown.com

Paul A. Jorissen
Partner, New York
+1 212 506 2555
pjorissen@mayerbrown.com

William Kucera
Partner, Chicago
+1 312 701 7296
wkucera@mayerbrown.com

Jean-Pierre Lee
Partner, Paris
+33 1 53 53 43 43
jplee@mayerbrown.com

Tow Lu Lim
Partner, Hong Kong
+ 852 2843 4490
tl.lim@mayerbrownjsm.com

Russell E. Nance
Partner, New York
+1 212 506 2534
rnance@mayerbrown.com

Andrew J. Noreuil
Partner, Chicago
+1 312 701 8099
anoreuil@mayerbrown.com

Sara S. M. Or
Partner, Hong Kong
+852 2843 2268
sara.or@mayerbrownjsm.com

Edmund "Ed" Parker
Partner, London
+44 20 3130 3922
eparker@mayerbrown.com

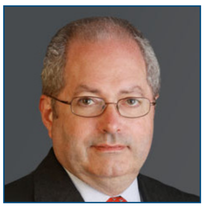
Elizabeth A. Raymond
Partner, Chicago
+1 312 701 7322
eraymond@mayerbrown.com

Martin S. Robertson
Partner, Hong Kong
+852 2843 2248
martin.robertson@mayerbrowjsm.com

Jerome J. Roche
Partner, Washington, DC
+1 202 263 3773
jroche@mayerbrown.com

Stephen G. Rooney
Partner, New York
+1 212 506 2567
srooney@mayerbrown.com

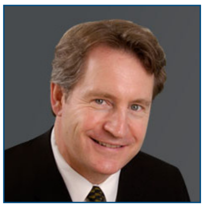
Colin Scagell
Partner, London
+44 20 3130 3315
cscagell@mayerbrown.com



Richard W. Shepro
Partner, Chicago
+1 312 701 7007
rshepro@mayerbrown.com

Vikram Sidhu
Counsel, New York
+1 212 506 2105
vsidhu@mayerbrown.com

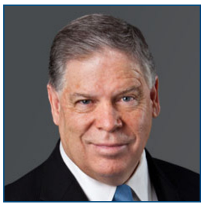
Richard Spitzer
Partner, New York
+ 212 506 2309
rspitzer@mayerbrown.com



Mark Uhrynuk
Partner, Hong Kong
+852 2843 4307
mark.uhrynuk@mayerbrownjsm. com

Guilherme Vieira da Silva
Partner, Rio de Janeiro
(Tauil & Chequer Advogados)
+55 21 2127 4210
gvieira@mayerbrown.com

Reb D. Wheeler
Partner, New York
+1 212 506 2414
rwheeler@mayerbrown.com



James Woods
Partner, New York, Palo Alto
+1 212 506 2390
jrwoods@mayerbrown.com

Jörg Wulfken
Partner, Frankfurt
+49 69 79 41 2951
jwulfken@mayerbrown.com

Nicole Zayac
Counsel, Palo Alto
+1 650 331 2066
nzayac@mayerbrown.com

Dennys Zimmermann
Partner
Tauil & Chequer Advogados
Rio de Janeiro
+55 24 2427 4228
dzimmermann@mayerbrown.com

Mayer Brown is a global legal services organisation advising many of the world's largest companies, including a significant portion of the Fortune 100, FTSE 100, DAX and Hang Seng Index companies and more than half of the world's largest banks. Our legal services include banking and finance; corporate and securities; litigation and dispute resolution; antitrust and competition; US Supreme Court and appellate matters; employment and benefits; environmental; financial services regulatory & enforcement; government and global trade; intellectual property; real estate; tax; restructuring, bankruptcy and insolvency; and wealth management.

OFFICE LOCATIONS AMERICAS: Charlotte, Chicago, Houston, Los Angeles, New York, Palo Alto, Washington DC
ASIA: Bangkok, Beijing, Guangzhou, Hanoi, Ho Chi Minh City, Hong Kong, Shanghai, Singapore
EUROPE: Brussels, Düsseldorf, Frankfurt, London, Paris
TAUIL & CHEQUER ADVOGADOS in association with Mayer Brown LLP: São Paulo, Rio de Janeiro

Please visit our website for comprehensive contact information for all Mayer Brown offices. www.mayerbrown.com

0370ins
August 2014