LLOYD'S

MARKET BULLETIN

From	Director, Worldwide Markets (extn 6677)
Date	15 January 2007
Reference	Y3947
Subject	**Japanese Kyosai business**
Subject areas	Latest details on classification of Kyosai and summary of rules applying to their reinsurance arrangements.
Attachments	Appendix 1: Rules applying to Kyosai on purchasing and disclosing reinsurance – summary chart Appendix 2: Maximum level of risk to be carried by a SASTI (Limits A) Appendix 3: (Interim) limits per insured up to which a SIP-SASTI may reinsure above Limits A (Limits B)
Action points	**Brokers and underwriters to note and comply when placing or writing Japanese Kyosai business.**
Deadlines	

1. Purpose of Bulletin

There have been two previous market bulletins on Japanese 'Kyosai' business. The first - ***Y3059 dated 19 May 2003*** – introduced the concept of Kyosai (Japanese mutual aid societies) and explained the regulatory and reputational implications for Lloyd's of managing agents establishing a commercial (reinsurance) relationship with these entities. The second, and more recent, bulletin – ***Y3787 dated 11 April 2006*** – expanded on the original bulletin following changes in Japanese law and the extension of the insurance regulatory regime to certain categories of Kyosai.

The regulatory framework around Kyosai and the rules applying to their reinsurance arrangements in particular are complicated and have given rise to a number of queries. Lloyd's has accordingly sought legal advice to clarify various issues and this market bulletin summarises that advice. As such it effectively replaces – but should still be read in conjunction with – bulletins Y3059 and Y3787.

2. Background

On 1 April 2006, Japanese laws governing Kyosai changed. In simple terms, some Kyosai that were previously unregulated became subject to the Insurance Business Law (IBL) while others remained unregulated.

This has implications for the way Kyosai – both regulated and unregulated – are permitted to obtain reinsurance and is therefore of direct relevance to Lloyd's underwriters.

Specifically, under Japanese law, Kyosai now break down into the following 5 categories:-

1. Kyosai exempt from the IBL (Unregulated Kyosai), defined to include those established:-
    a. by a local authority for residents;
    b. by an employer for its employees;
    c. by a labour union for its members;
    d. by a company for other companies in the same corporate group;
    e. by a school for its pupils;
    f. by certain eligible local area groups for their members.

2. Specific Insurance Providers ***(SIPs)*** – these are transitional Kyosai that will cease to exist once they become registered as SASTIs (below), which they are required to do by 31 March 2008.

3. Small Amount and Short-Term Insurers ***(SASTIs)*** – a new category of regulated Kyosai to which very specific rules apply.

4. ***SIP-SASTIs*** – a sub-category of SASTIs to which specific transitional rules apply (until 31 March 2013, whereupon SIP-SASTIs will be subject to the same rules as SASTIs).

5. Kyosai exempt from the IBL but regulated by laws other than the IBL

The freedom that Kyosai enjoy in obtaining reinsurance coverage depends on the category to which they belong. Sections 3-7 below describe these rules in detail and Appendix 1 summarises them in a quick reference chart.

3. Kyosai exempt from the IBL (Unregulated Kyosai)

Since these Kyosai do not fall within the scope of the IBL, they should in theory be free to reinsure either locally or overseas and with no need to disclose their reinsurer. However, managing agents should be mindful of the following:-

- There is some legal uncertainty on the ability of these Kyosai to reinsure overseas since an entity that is not regulated under the IBL could be regarded as not being an insurer and therefore not qualified to purchase reinsurance. Under this interpretation, such Kyosai would therefore effectively be purchasing ***in***surance rather than reinsurance, for which the provider would need to be licensed in Japan. In this scenario a Lloyd's managing agent would need to write this business through Lloyd's Japan (LJI). Managing agents should seek their own legal advice on this point before entering into an arrangement with an IBL-exempt Kyosai.

- As these Kyosai fall outside any form of independent regulation, they are not subject to any controls other than those they may choose to impose on themselves. They may therefore present reputational or other risk and managing agents should satisfy themselves on these points before entering into an arrangement with an IBL-exempt Kyosai.

4. Specific Insurance Providers (SIPs)

SIPs are Kyosai that were previously not regulated under the IBL, but that are now ***not*** exempt from its provisions and are therefore required to register as SASTI (otherwise they must cease business). However, they have a transitional period of 2 years (until 31 March 2008) in which to do so. In the meantime, they are free to reinsure overseas with no requirement to disclose their reinsurer. Managing agents should note the following:-

- Although SIPs were previously classed as unregulated Kyosai, because they are now covered by the IBL as an entity engaged in insurance business, their legal ability to reinsure (as discussed in 3. above) does not appear to be in question.

- However, given that during the 2-year transitional period SIPs effectively remain unregulated (albeit subject to some transitional controls), the same caveat in respect of reputational and/or other risk discussed under 3. above does still apply.

5. Small Amount and Short-Term Insurers ***(SASTI)***

The IBL imposes fixed limits on the maximum level of risk a SASTI is allowed to carry per insured. These limits (for these purposes called Limits A) vary according to the type of risk and are set out in Appendix 2. The limits are rigid and may not be exceeded, even via reinsurance. Up to these limits, however, a SASTI is permitted to reinsure overseas and without the need to disclose its reinsurer.

6. SIP-SASTIs

As soon as SIPs register as SASTIs, (see section 4), they become SIP-SASTIs, once again a transitional arrangement subject to complicated rules:-

- SIP-SASTIs are subject to the same limits as SASTIs on maximum level of risk per insured (Limits A - see Appendix 2). As with SASTIs, SIP-SASTIs are free to reinsure overseas and without the need to disclose their reinsurer below Limits A.

- Unlike SASTIs, however, SIP-SASTIs are permitted to underwrite a risk exceeding Limits A, up to a maximum of Limits B (see Appendix 3), provided the net (of reinsurance) level of risk remains below Limits A[1].

- ***SIP-SASTIs carrying a risk above Limits A are required to seek reinsurance cover from a reinsurance provider located and licensed in Japan.*** If such cover is not available locally, permission must be sought from the Japanese FSA (JFSA) to reinsure overseas[2]. (To this end, managing agents looking to provide reinsurance cover for SIP-SASTIs may wish to consider using the Lloyd's Japan platform. For details, contact Cameron Murray, ext 6854).

- Where reinsurance is purchased above Limits A, the reinsurance provider must be disclosed to both the JFSA and the client[3]. ***NB Such disclosure is a legal requirement; Kyosai (of any type described in this bulletin) should not use any reinsurance arrangements at Lloyd's in a promotional context.***

- These arrangements for SIP-SASTIs are transitional and apply until 31 March 2013. Thereafter, SIP-SASTIs will be subject to the same reinsurance requirements as SASTIs.

7. Kyosai exempt from the IBL but regulated by laws other than the IBL

Kyosai regulated by laws other than the IBL are generally free to reinsure overseas and without the need to disclose their reinsurer.

If you have any queries about the above please contact:

Lloyd's Worldwide Markets:

Market Services Desk: Box 190b
Tel: 020 7327 6677
Email: market.services@lloyds.com

This bulletin has been sent to active underwriters and the compliance officers of Lloyd's brokers and managing agents and for information to market associations.

The information contained in this market bulletin is provided in order to support managing agents in meeting their commitment ***'to protect Lloyd's licences and authorisations to conduct insurance business in the UK and overseas***'. The information will also help underwriters decide, prior to binding, how a risk can be underwritten in compliance with Lloyd's trading rights in the country concerned.

[1] Limits B may themselves be exceeded where risks have been underwritten prior to a SIP's registration as a SIP-SASTI, provided the requirement to reinsure above Limits A is adhered to.

[2] Contracts concluded prior to a SIP's registration as a SIP-SASTI may be freely reinsured overseas without JFSA permission.

[3] Where contracts have been concluded prior to a SIP's registration as a SIP-SASTI, the reinsurer need be disclosed to the JFSA only.

More detailed information on Lloyd’s trading rights may be found on www.lloyds.com/Lloyds_Worldwide. Select the appropriate country from the Lloyd’s country guide box and then the Quick Reference Guide. More detailed information may then be obtained for certain countries by selecting ‘Manual’ from the menu on the left hand side of the screen. You will be asked to input a password. Please contact the Worldwide Market Services (contact details as above) in order to obtain this information.

Julian James
Director Worldwide Markets
Worldwide Markets

Appendix 1

Rules applying to Kyosai on purchasing and disclosing reinsurance
(To be read in conjunction with Appendices 2 & 3 on maximum levels of risk)

Type of Kyosai	Free to reinsure overseas?	Disclosure of reinsurer required?
IBL-exempt Kyosai (Unregulated Kyosai)	• In theory free to reinsure overseas. • However, legal uncertainty over whether this is reinsurance as opposed to insurance (requiring the insurer to be licensed in Japan). Managing agents should seek their own legal advice. • No controls in place therefore managing agents should consider reputational / other risks.	In theory no need to disclose reinsurer.
Specific Insurance Providers (SIPs)	• Free to reinsure overseas until they are registered as SASTIs, which they are required to do by 31 March 2008. Once they are registered as SASTIs, separate rules apply. • Until SIPs are registered as SASTIs, they remain effectively unregulated. Therefore managing agents should consider reputational / other risks.	Until SIPs are registered as SASTIs, which they are required to do by 31 March 2008, no need to disclose reinsurer.
Small Amount and Short-Term Insurers (SASTIs)	• Limits (A) imposed on maximum level of risk per insured. SASTIs are not permitted to carry risks above these limits even if the risk is netted by reinsurance arrangements. • Below these limits SASTIs are free to reinsure overseas.	If reinsuring below limits A, no need to disclose reinsurer.
SIP-SASTIs	• Same limits (A) imposed on maximum level of risk per insured. Below these limits SIP-SASTIs are free to reinsure overseas ("Reinsurance Below Limits A"). • SIP-SASTIs may exceed limits A by reinsuring up to limits B, provided net of R/I level of risk remains below limits A ("Reinsurance Above Limits A"). • Reinsurance above limits A must be sought from a local licensed reinsurance provider. If not available, authorisation must be sought from JFSA to seek reinsurance overseas. • These requirements are transitional and apply until 31 March 2013. Thereafter SIP-SASTIs will be subject to the same rules as SASTIs.	• In respect of Reinsurance Below Limits A, no need to disclose reinsurer. • With respect to Reinsurance Above Limits A, reinsurance provider must be disclosed to the JFSA and the client. ***NB Reinsurance arrangements at Lloyd's made by <u>any</u> class of Kyosai should be disclosed only as far as is required by law, and not for promotional purposes.***
Kyosai exempt from the IBL but regulated by laws other than the IBL	Free to reinsure overseas	No need to disclose reinsurer.

Appendix 2

Maximum level of risk to be carried by a SASTI (Limits A)

Under the Japanese Insurance Business Law (IBL), a SASTI may underwrite up to the following limits per insured. These limits may not be exceeded, even via reinsurance.

1. Death (excluding deaths falling under risk 5 below): **3 million yen**;

2. Medical, Sickness, Injury (excluding those falling under risks 3 or 4 below): **800,000 yen**;

3. Permanent Disability (or other qualifying injuries set out in the IBL Regulations) caused by injury or sickness: **3 million yen**, provided that if the same insurance product covers risks 1, 4 or 5 in respect of the same insured, the payment of insurance money under risk 3 would have to reduce the amount payable under risks 1, 4 or 5;

4. Permanent Disability (or other qualifying injuries set forth in the IBL Regulations) caused by injury: **6 million yen**, provided that if the same insurance product covers risks 1, 3 or 5 in respect of the same insured, the payment of insurance money under risk 4 would have to reduce the amount payable under risks 1, 3 or 5;

5. Death caused by Injury: **3 million yen**. If, however, the same insurance product covers risk 1 in respect of the same insured, and where the payment of insurance money under risk 5 would reduce the amount payable under risk 1, then the amount is 6 million yen;

6. Insurance products covering losses caused by an unexpected accident (which includes non-life insurance products excluding medical or injury in general): **10 million yen**.

Appendix 3

(Interim) limits per insured up to which a SIP-SASTI may reinsure above Limits A (Limits B)

Under the Japanese Insurance Business Law (IBL), a SIP-SASTI may underwrite above Limits A up to the following limits per insured, provided the net (of reinsurance) level of risk remains below Limits A.

1. Death (excluding deaths falling under risk 5 below): **15 million yen**;

2. Medical, Sickness, Injury (excluding those falling under risks 3 or 4 below): **2.4 million yen**;

3. Permanent Disability (or other qualifying injuries set out in the IBL Regulations) caused by injury or sickness: **15 million yen**, provided that if the same insurance product covers risks 1, 4 or 5 in respect of the same insured, the payment of insurance money under risk 3 would have to reduce the amount payable under risks 1, 4 or 5;

4. Permanent Disability (or other qualifying injuries set forth in the IBL Regulations) caused by injury: **30 million yen**, provided that if the same insurance product covers risks 1, 3 or 5 in respect of the same insured, the payment of insurance money under risk 4 would have to reduce the amount payable under risks 1, 3 or 5;

5. Death caused by Injury: **15 million yen**. If, however, the same insurance product covers risk 1 in respect of the same insured, and where the payment of insurance money under risk 5 would reduce the amount payable under risk 1, then the amount is 30 million yen;

6. Insurance products covering losses caused by an unexpected accident (which includes non-life insurance products excluding medical or injury in general): **50 million yen**.