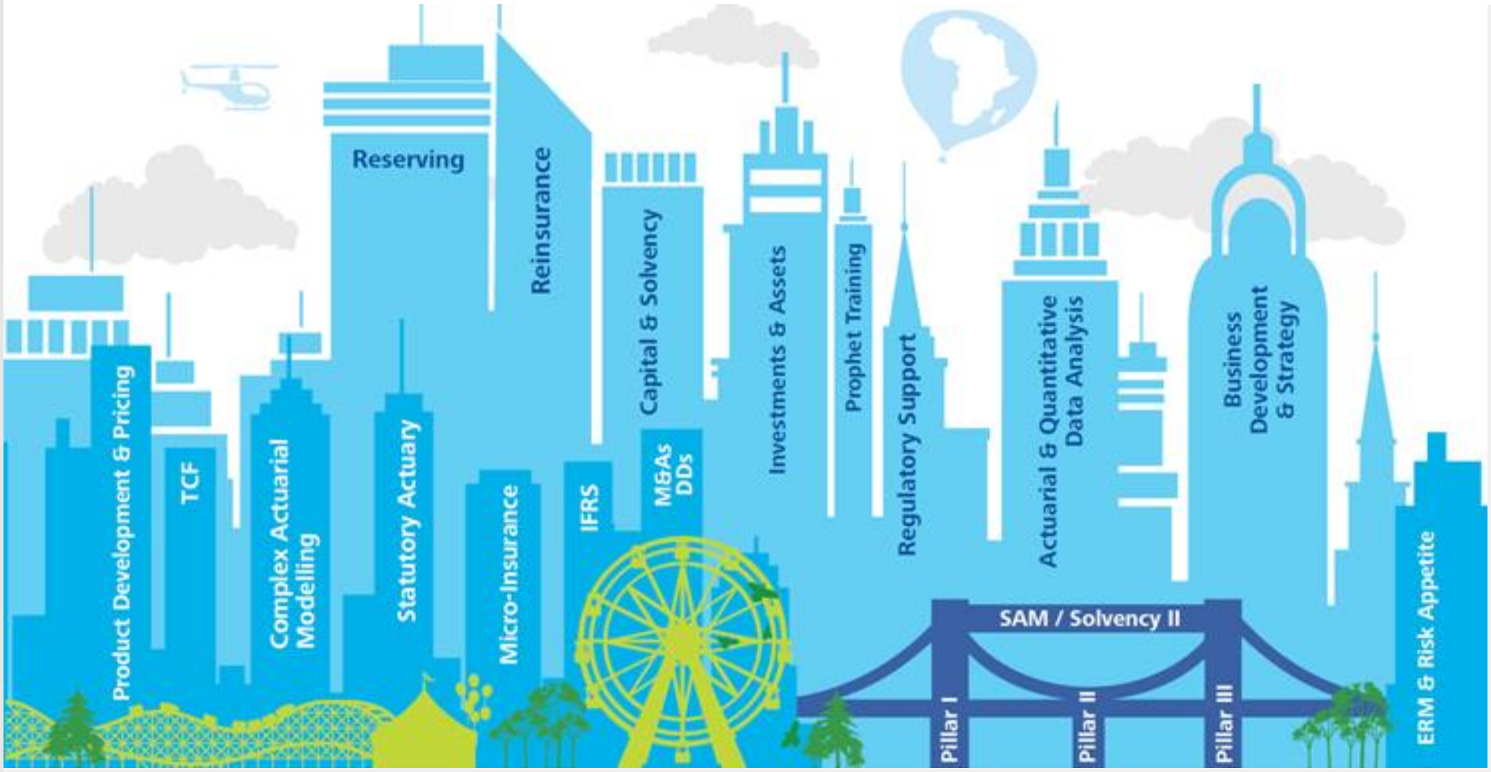
South Africa | Short-term Insurance | 26 May 2015



FSB: Reinsurance Regulatory Review

Summary of Discussion Paper

A message from Jaco van der Merwe | Director **|** AIS – Short-term Insurance

Dear client

The volume and rate of regulatory change in the South African Insurance Industry is reaching a peak with the proposed SAM implementation deadline looming. In addition to SAM, numerous other areas are changing as well, such as the regulation of reinsurance.

We have been requested by a number of clients to provide a quick summary of the reinsurance discussion paper circulated by the FSB (attached). It is important to note that the deadline for submission of comments to the FSB is **1 June**. The FSB has however granted extensions to those requesting them.

Below is a very high level summary touching on the key areas of change. We recommend further reading of the discussion paper on topics of interest highlighted below.

This summary represents only the most significant changes in our view. Should you have any questions or require an assessment of the impact on your business, please contact me or my team. Deloitte Actuarial and Insurance Solutions has one of the largest and most experienced Short Term insurance consulting teams in the country and we would be happy to assist with your queries.

Kind regards

Jaco van der Merwe
Director | Short Term Insurance | Actuarial & Insurance Solutions
Deloitte & Touche
Deloitte Place, Building 33, 20 Woodlands Drive, Woodmead, 2052, South Africa
Tel/Direct: +27 11 209 8163 | Fax: +27 11 252 7257 | Mobile: +27 82 682 3270
javandermerwe@deloitte.co.za | www.deloitte.com

Comments due by 1 June 2015

Companies can respond via SAIA or directly to the FSB.

Companies can apply to the FSB for extension of the submission deadline.

Key Changes

The new framework will replace the prior framework of "approved" and "non-approved" reinsurers.

Credit ratings will be adjusted to remove the effect of the **sovereign cap**.

Local direct insurers will need **authorization** to conduct reinsurance business.

Cell captives and micro-insurers will **not** be allowed to conduct reinsurance.

Reinsurance placed with a **foreign reinsurer** can only be accounted for on a **statutory basis** if the regulatory framework is approved.

More **granular reporting requirements** for both inwards and outwards reinsurance.

"Pay-as-paid" clauses will be removed.

No recognition of **financial reinsurance** for solvency calculations.

No composite reinsurers will be allowed.

Impact on reinsurers

Different requirements will be placed on:

- Local professional reinsurers and insurers conducting inwards reinsurance
- Branches of foreign reinsurers
- Reinsurer's operating on a cross border basis
- Lloyd's

Credit ratings of the foreign reinsurers will be adjusted to reflect the reduced supervisory power that the regulator has over them and cross border resolution risk.

- Cross border reinsurers' credit ratings will be bumped down three notches
- Foreign reinsurers' credit ratings with local branches will be bumped down two notches

Reinsurers are allowed to use the branch basis to conduct business in South Africa.

Credit ratings of local reinsurers will be adjusted to remove the effect of the sovereign cap

- Local credit ratings will be bumped up three notches
- Or the parent company's rating can be adopted if parental guarantees are in place

Impact on cedants

Reinsurance with a **foreign reinsurer** can only be accounted for on a **statutory basis** if the foreign regulatory framework is approved by the regulator. It is anticipated that approval will be limited to countries with risk based solvency capital requirements.

No recognition of **financial reinsurance** for solvency calculations.

Different treatment for solvency purposes of reinsurance placed with:

- Local reinsurers

- Branches of foreign reinsurers
- Lloyd's
- Cross border reinsurance

Fronting will be avoided by placing limits on percentage of business that may be ceded to a single counter party:

- 75% limit on cession to an unrelated counter party
- 85% limit on cession if ceding to a group member

Impact on Lloyd's

Business placed:

- directly with Lloyd's will get a three notch credit downgrade.
- with a Lloyd's representative office will get a one notch credit downgrade.

Lloyd's representative offices and branches have to hold technical provisions within RSA in a trust.