

## NEWSSTAND

An Introduction to the 2009 Insurance Law Reform in China

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The amended Insurance Law of the People's Republic of China (PRC) came into force on 1 October 2009 (the Amended Insurance Law). This is the second revision and the most comprehensive reform of the China Insurance Law since its enactment on 1 October 1995.

The amendments cover five major areas of insurance law including insurance contracts, insurance companies, insurance intermediaries, the management of insurance companies and the supervision of the insurance industry. This article focuses on the amendments which relate to the operation of insurance companies in the PRC. The Amended Insurance Law does not apply to the Special Administrative Regions of Hong Kong and Macau.

### **Shareholders of a PRC Insurance Company**

The Amended Insurance Law has introduced new qualification requirements for the major shareholders of an insurance company when it is established in the PRC. Under article 68(1) of the Amended Insurance Law, major shareholders of an insurance company are required to have (i) sustainable profitability; (ii) good reputation; (iii) net assets of not less than 200 million yuan; and (iv) no record of significant breach of any laws and regulations in the three years immediately preceding becoming a shareholder of the insurance company.

“*Major shareholder*” is not defined in the Amended Insurance Law, and having “*sustainable profitability*” is not explained. It is also unclear what would constitute a “*significant breach*” of the laws and regulations. Effectively, these uncertainties will give the China Insurance Regulatory Commission (CIRC), the regulatory authority for the insurance industry in the PRC, greater discretion in determining whether to approve the establishment of an insurance company in the PRC, though it is to be hoped that an understanding will in due course develop as to the meaning of these terms.

The Amended Insurance Law also grants CIRC power to restrict the rights of the shareholders of an insurance company where the insurance company engages in transactions with its related companies which may seriously jeopardise its interests or solvency. In addition, if the shareholders refuse to procure the reversal of the transactions, CIRC may compel the shareholders to dispose of their shares in the insurance company.<sup>1</sup> This is a significant new power for CIRC, though the Amended Insurance Law does not state how or to whom the shares should be transferred and it will be interesting to see how CIRC and the PRC courts implement this provision.

## **Forms of Insurance Company**

Under the former China Insurance Law, an insurance company could only be formed as a joint stock company or a wholly state-owned enterprise.<sup>2</sup> This restriction has now been removed by the Amended Insurance Law, but in practice it had been rendered largely redundant prior to its removal as CIRC had previously approved the establishment of foreign-invested PRC insurance companies in the form of limited liability companies. Though the removal of this restriction will have limited impact on the future establishment of foreign-invested insurance companies in the PRC, it will permit limited liability insurance companies to be established by PRC investors.

## **Solvency Requirements**

Where an insurance company fails to meet the solvency requirements promulgated by CIRC, CIRC is empowered to take measures against the company, including (i) ordering the company to increase its capital and obtain additional reinsurance cover; (ii) restricting the business scope of the company; (iii) restricting distribution of dividends to the shareholders; (iv) limiting the remuneration paid to its directors and senior management; and (v) ordering the company to stop writing new policies.<sup>3</sup> If an insurance company is, or is at substantial risk of, being restructured, taken-over or placed in liquidation, CIRC may take further measures to restrict its directors and senior management from travelling out of the PRC and disposing of their assets.<sup>4</sup>

## **Investments**

Under the former China Insurance Law, insurance companies could only invest in bank deposits, government bonds, financial bonds and other assets approved by the State Council of the PRC.<sup>5</sup> These were regarded as low risk and low return investments. To enable insurance companies to increase their profitability and financial strength, the Amended Insurance Law now allows insurance companies to invest in stocks, securities investment funds and real estate.<sup>6</sup> The prohibition against insurance companies investing in securities companies and non-insurance related companies has also been removed.

Although this expanded range of investment assets is now set out in the Amended Insurance Law, in practice some of these investments (eg investments in banks and infrastructure projects) had previously been permitted by the State Council. It is expected that CIRC will soon announce detailed rules regarding investment in private equity and real estate by insurance companies.

## **Reinsurance Requirement**

Prior to the reform, the China Insurance Law required that when seeking to reinsure their direct PRC insurance business, insurers had to give priority to reinsurance companies located in the PRC.<sup>7</sup> The former China Insurance Law further gave CIRC a right to restrict or prohibit insurance companies in China from reinsuring with or accepting reinsurance business from overseas insurers. These restrictions have now been removed by the Amended Insurance Law.

However, the Provisions on the Administration of Reinsurance Business promulgated by CIRC in 2005 have not been revised and are still in effect. The 2005 Provisions require that direct insurers must offer to at least two China-based professional reinsurance companies no less than an aggregate of 50% of the China-based risks to be reinsured before they may offer such business to reinsurers located outside the PRC.

CIRC has recently published draft 2009 Provisions on the Administration of Reinsurance Business which will remove these requirements. A final version of the 2009 Provisions is anticipated to come into force at the end of 2009.

### **Foreign-Invested Insurance Companies**

A number of new administrative regulations came into force at the same time as the Amended Insurance Law and, though these apply to all PRC insurance companies including foreign-invested insurance companies in the PRC, foreign-invested insurance companies remain principally regulated by the Administrative Provisions on Foreign-Invested Insurance Companies and the Detailed Rules on the Implementation of the Provisions on Foreign-Invested Insurance Companies which remain in effect and are unchanged. The Amended Insurance Law will therefore have limited impact on the establishment and operation of foreign-invested insurance companies in the PRC.

### **Conclusion**

The Amended Insurance Law provides insurance companies with more flexibility in offering new products and making investments; it also gives CIRC greater enforcement powers against an insurance company which fails to comply with the solvency requirements or other CIRC regulations. It is hoped that by elevating the requirements on the establishment and operation of insurance companies in the PRC and strengthening CIRC's ability to regulate the insurance industry, it will offer more protection to the consumer. However, many of the amendments are not in practice new to the insurance industry in the PRC but are intended to reflect and accommodate the rapid development of the PRC's insurance industry following its accession to the World Trade Organisation in 2002.

We will continue to monitor insurance developments in the PRC, particularly the regulations issued by CIRC to implement the Amended Insurance Law.

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<sup>1</sup> Article 152 Amended Insurance Law.

<sup>2</sup> Article 70 former China Insurance Law.

<sup>3</sup> Article 139 Amended Insurance Law.

<sup>4</sup> Article 154 Amended Insurance Law.

<sup>5</sup> Article 105 former China Insurance Law.

<sup>6</sup> Article 106 Amended Insurance Law.

<sup>7</sup> Article 103 former China Insurance Law.