中国保险行业协会

To: Governor Dirk Kempthorne
Chairman, Global Federation of Insurance Associations

Date: 11 March 2015

Subject: Reply to your letter dated 29 September 2014

Dear Mr. Kempthorne,

Thank you for GFIA's letters with regard to the credit risk regulation in C-RORSS. And thank you for your kind attention to the development of China's new solvency regulation system. I understand you have concerns in terms of the credit risk charge to foreign reinsurers under the new regime. I forwarded your letter to C-ROSS team at CIRC and discussed this issue with them. Now I am glad to present their view on this matter.

CIRC thinks there is a misunderstanding that there is an intention to discriminate international reinsurers under the new regime. On the contrary, CIRC, as regulator, encourages the establishment and development of international reinsurers in China. CIRC values the new technology and service provided by the international reinsurers and believes it would encourage positive competition and benefit China's insurance market in the long term.

The principle of the new regime is to charge capital on risk basis. There are new versions after DingNan Meeting. In the final version, the credit risk charge is only high when the reinsurer is not registered with CIRC and has no collateral. For the international reinsurers who follow China's regulation prudently, for example Swiss Re and Munich re, they are treated exactly the same as the domestic reinsurers.

Three reasons of such regulation were explained by CIRC:

Firstly, international reinsurance market is complicated. Some are not very well known by China's insurers and regulators. Whilst the international direct insurers need to follow tight approval process to be able to operate in China, the reinsurers are subject to minimum regulation. They can write business as long as they can provide a solvency report from the regulators where they are registered. Different regulators require different level of solvency. And the solvency position can change over time. Even CIRC is willing to give benefit of the doubt to those reinsurers who had no credential with CIRC at all, sometimes it presented a problem to the China's cedents and it was too late to find that some of these reinsurers cannot meet their liabilities. A recent example is Best Re, who suffered huge loss in Thailand flood and was unable to meet its claim with HanWha. Best Re was still able to write business even in the midst of the claim according to current regulation. Some China's insurers suffered bad debt. Some off-shore reinsurers took advantage of the regulation by writing business in China with no or minimum capital charge. The aim of new regime is to close the current unregulated gap of reinsurers' credit risk. For that reason CIRC believes reinsurers need to have some credential with CIRC, which is denoted as the solvency level under C-ROSS regime. Companies which don't follow the C-ROSSS regulation can still write business in China. However, CIRC believes those who follow the current C-ROSS rules, which are quite tight regulation requirement, have lower credit risks than those who don't. The difference is reflected in the risk factors. The calculation of risk factors is based on the historic events and the data from rating agencies. CIRC believes it reflects our view on the difference of credit risks.

Secondly, CIRC believes the new regime does not discriminate foreign reinsurers but put the international insurers on the same playground as domestic reinsurers. It is the actual national treatment. If you read the rules carefully you will find that to be a domestic reinsurer you need a) register with CIRC; b) follow the C-ROSS solvency requirement. All these are required to all reinsurers who operate in China no matter which country they domicile. This of course will reduce the unfair advantage for those who did not need capitals to operate in China before. In the long term we believe this will reduce the negative pricing competition and allow reinsurers put margin into the premium. This will encourage property reinsurance premium, especially catastrophe premium return to its normal level. We believe it will promote healthy reinsurance market for all participants.

Thirdly, these types of regulation are not unusual in other market. US NAIC required foreign reinsurers either to get approval status or to provide collaterals to write business in US. This is exactly the same principle as C-ROSS. Singapore required 50% discount for those non-registered reinsurers and there are also discounts by rating levels. Taiwan regulator adopts similar method. I believe all these regulators shares the views that there are higher risks for those reinsurers that are not registered or regulated by local authority thus not known well by the local industry.

The new regime aims to distinguishing the high risks from low risks in insurance industry. The aim is to provide a better understanding of risks managed among China's market and not discriminate any certain group. Like all the regulation changes, there will be winners and losers after the change and shifting the competition ground. CIRC believes the new regime will encourage better understanding of risks and better risk management in China's market. For international reinsurers who want to operate in China, if they read the rules carefully, they will find it is still easy to follow. If they can demonstrate that they can manage risk appropriately, they still stand on good if not better ground. They are in the exactly same position as all other Chinese domestic reinsurers.

I hope I have explained the rational of the regulation by CIRC. CIRC and IAC welcomes your view on this issue and look forward to discuss further with you.

Kind regards,

Yours sincerely,

ZHU Jinyuan
President, Insurance Association of China