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Reserve Bank of New Zealand  
Financial System Policy and Analysis – Financial Policy  
**Wellington**

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**Re: Review of the Insurance (Prudential Supervision) Act 2010 Options Paper 1: Scope of the Act and Overseas Insurers**

The New Zealand Law Society | Te Kāhui Ture o Aotearoa (**Law Society**) welcomes the opportunity to comment on the Reserve Bank of New Zealand (**RBNZ**) options paper: *Review of the Insurance (Prudential Supervision) Act 2010, Options Paper 1: Scope of the Act and Overseas Insurers (options paper)*.

The options paper covers the scope of the Insurance (Prudential Supervision) Act 2010 (**Act**) and raises issues relating to the definitions of “contracts of insurance” and of “carrying on business”, as well as discussing the regulatory regime for overseas insurers and reinsurers, and group supervision and outsourcing. The Law Society’s Commercial and Business Law Committee have reviewed the options paper and provide the following comments.

### **1. Scope of the Act**

- 1.1 The section of the options paper dealing with the scope of the Act focuses on the definitions of “contract of insurance” and what it means to “carry on business in New Zealand”. These key terms in the legislation determine the scope of coverage of the IPISA regime.
- 1.2 However, the options paper also acknowledges that the underpinning policy question is whether some kinds of business might have insurance-like characteristics and whether those businesses also require the prudential regulation that IPISA provides, with its emphasis on risk management in the face of future uncertainty and the maintenance of appropriate capital solvency to reflect such risks.<sup>1</sup>
- 1.3 This fundamental policy question is not currently reflected in the statement of the purposes of the Act (in section 3) or its principles (in section 4). In particular, section 3 provides for regulation of the “insurance sector” and does not engage the substantive policy issue identified in paragraph [39] of the options paper. It provides:

#### **3 Purposes**

- (1) The purposes of this Act are to—
  - (a) promote the maintenance of a sound and efficient insurance sector; and
  - (b) promote public confidence in the insurance sector.
- (2) Those purposes are achieved by—
  - (a) establishing a system for licensing insurers; and

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<sup>1</sup> See [39] of the options paper.

- (b) imposing prudential requirements on insurers; and
- (c) providing for the supervision by the Reserve Bank of New Zealand (the **Bank**) of compliance with those requirements; and
- (d) conferring certain powers on the Bank to act in respect of insurers in financial distress or other difficulties.

1.4 Because the ambit of the review includes revisiting sections 3 and 4, options for modifying those sections should be included in this consultation process.

## **2. Definition of “contracts of insurance”**

2.1 The current definition of “contracts of insurance” does not provide an exhaustive definition of a contract of insurance but describes insurance in terms familiar from the common law checklist set out by Channell J in *Prudential insurance Co v Commissioners of Inland Revenue*.<sup>2</sup>

2.2 Insurance business is dynamic and constantly evolving. For that reason, other common law jurisdictions also rely on the common law description of insurance in their prudential supervision legislation. The Law Society is not aware that the current definition of “contract of insurance” has caused problems for New Zealand lawyers or their clients. On that basis, the Law Society is broadly supportive of the status quo (option 1.1), subject to the following comment. The inclusion of the words “unless the context otherwise requires” in the definition introduces further uncertainty and their inclusion should be reconsidered. The phrase “contract of insurance” appears in the Act 273 times in 34 sections, and it is not easy to see where the context might require a different definition than the one given in section 7(1).

2.3 With regard to option 1.4 (that the RBNZ maintain guidelines), we note that maintaining up to date guidelines is a resource-intensive commitment. Provision for guidelines can potentially transgress into effectively giving the RBNZ law-making powers. We agree with the points made in the paper that this can create uncertainty and is inappropriate, given the importance of the definition.

2.4 There is a case for the regulations to include a new power for the RBNZ to designate arrangements to be treated as contracts of insurance, noting that the Financial Markets Authority has a very similar power in the Financial Markets Conduct Act 2013 (section 562) which is constrained by certain procedural requirements (section 563). However, this should be subject to further consultation.

2.5 We note that although deeming provisions are generally helpful in ensuring the effective functioning of regulatory legislation, these powers should only be provided to an appropriately resourced supervisor.

2.6 If provisions are developed providing the RBNZ power to “deem in”, such powers should be accompanied by the development of a clearly articulated, effective and efficient review process.

## **3 Definition of “carrying on business in New Zealand”**

3.1 The question whether a person is “carrying on business in New Zealand” under the Companies Act 1993 is a factual question that must be determined in the particular circumstances. Paragraph [54] of the options paper sets out the RBNZ’s approach, which considers the degree of connection to New Zealand. Regardless of any changes made as a result of the options

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<sup>2</sup> [1904] 2 KB 658 at 63.

paper, it is appropriate that the RBNZ publish guidelines as soon as possible, so that all entities are aware of the approach the RBNZ will exercise when considering whether an entity is “carrying on business in New Zealand”.

- 3.2 The Law Society does not support the objective test in option 2.3 of a level of written premium that automatically implies a company is not “carrying on business in New Zealand”, because such a dollar amount would be arbitrary. This approach would not support the purposes of the Act. Instead, the Law Society considers that the RBNZ should hold information about all insurers operating in New Zealand, regardless of whether they are required to hold a licence. As set out in the Law Society response to the 2017 Issues Paper, *“The insurance prudential regulator needs to have sufficient detail of the insurance business written in New Zealand in order to be able to appropriately supervise insurers.”*<sup>3</sup>
- 3.3 The Law Society does not consider it is appropriate to apply all aspects of the Act to all insurers providing insurance coverage in New Zealand. Generally, captive insurers should remain within the scope of the Act, because the failure of a captive insurer could adversely impact New Zealanders and so damage public confidence in the insurance sector. However, the requirement of section 9 that “entering into the contract or contracts ... is incidental or ancillary to the business of the person” should be reconsidered, to enable the RBNZ to provide relief to captives where requiring the captive to obtain a licence is unduly onerous or burdensome. We note that the powers of the RBNZ to declare that a person is not carrying on insurance business in New Zealand under section 9 of the Act have only been used in one instance.<sup>4</sup> It would be helpful if the section 9 declaration provisions were amended to provide additional clarity on the scope of the regime. We would favour a regime that requires an entity that provides insurance business to either hold a licence or hold a section 9 declaration stating that no licence is necessary. This would provide lawyers and their clients with the certainty they need and would enable the RBNZ to have oversight of all insurance business written in New Zealand.

#### **4 Requirement for contracts with New Zealand policyholders**

- 4.1 The Law Society does not express a view on these issue as it is one of policy but agrees with the comments of Mary Scholtens QC and John Trowbridge<sup>5</sup> that there is a reputational risk from unregulated insurers based in New Zealand offering contracts overseas. Amending the section 9 declaration process could provide a means of limited oversight without the supervisory burden of licensing. One way this could be achieved would be to remove the requirement for one New Zealand policyholder (section 8(1)(c)), then amend section 9 so that another ground on which a declaration could be made was if the insurer had no policyholders

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<sup>3</sup> New Zealand Law Society submission on a review of the Insurance (Prudential Supervision) Act 2010, 30 June 2017, <https://www.lawsociety.org.nz/assets/Law-Reform-Submissions/0014-113108-I-RBNZ-IPSA-Review-30-6-17.pdf>

<sup>4</sup> <https://www.rbnz.govt.nz/-/media/ReserveBank/Files/regulation-and-supervision/insurers/licensing/declarations-and-exemptions/Ganson-Management-Ltd-Section-9-declaration.pdf?la=en&revision=3e552fb0-d020-4f34-8a6e-25ec19d37929>

<sup>5</sup> Mary Scholtens, John Trowbridge *An Independent Review for the RBMZ of the Supervision of CBL Insurance Ltd.* (2019) <https://www.rbnz.govt.nz/-/media/ReserveBank/Files/regulation-and-supervision/insurers/CBL-RBNZ-Final-Report.pdf?revision=e7308ab8-6b67-402b-9fd3-11427df713e7&la=en>

in New Zealand and there was no risk of reputational damage to the New Zealand regulatory system by the insurer continuing to operate from New Zealand.

## **5 Overseas branches**

5.1 It would be prudent to take an approach that follows international best practice, as demonstrated by the regimes in Australia, Canada and the UK. This would require branches to hold assets in New Zealand plus additional sums analogous to the capital requirements under the solvency standard. We suggest that more consideration should be given to this approach and details could be based on comparable rules in Australia.

## **6 Treatment of overseas reinsurers**

- 6.1 We do not support the greater licensing and supervision of inwards reinsurers. However, there should be stronger incentives for insurers to manage their own reinsurance risk prudently. Requirements should be developed for insurers' reinsurance management by placing more explicit requirements on insurers to manage and document the management of their reinsurance risk. This could be in addition to altering the solvency standard to make it more sensitive to reinsurance risk. Accordingly, the Law Society supports options 5.3 and 5.4.
- 6.2 Reflecting the increasing importance of risk management, it would be timely for the RBNZ to review the Guidelines for Risk Management issued in 2012,<sup>6</sup> particularly in light of the IMF FSAP observations on ICP 8 Risk Management and Internal Controls and ICP 13 Reinsurance and other forms of Risk Transfer.<sup>7</sup>

## **7 Group Supervision**

7.1 The Law Society supports option 6.2, the introduction of comprehensive group supervision for the reasons set out in the options paper, namely as a means of gauging group-level risk in accordance with international practice.

## **8 Outsourcing and business continuity**

8.1 The Law Society supports risk-based outsourcing rules and business-continuity focused rules. It is important that all outsourcing arrangements are appropriately documented. We support an approach that is in line with international best practice and suggest the Australian rules mentioned in paragraph [172] could provide a suitable model.

### **Next steps**

We hope these comments are helpful. If you have any questions or further discussion would assist, please contact the Commercial and Business Law Committee convenor, Charlotte McLoughlin, through the Law Society's Law Reform and Advocacy Adviser, Emily Sutton ([emily.sutton@lawsociety.org.nz](mailto:emily.sutton@lawsociety.org.nz)).

Nāku noa nā,



Arti Chand  
**NZLS Vice-President**

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<sup>6</sup> <https://www.rbnz.govt.nz/-/media/ReserveBank/Files/regulation-and-supervision/insurers/licensing/4266093.pdf?la=en>

<sup>7</sup> <https://www.imf.org/en/Publications/CR/Issues/2017/05/10/New-Zealand-Financial-Sector-Assessment-Program-Detailed-Assessment-of-Observance-Insurance-44904>