



3 November 2017

TO: ALL LIFE INSURERS

REVIEW OF PRUDENTIAL STANDARD LPS 230 REINSURANCE

Purpose of Letter

This letter outlines APRA's proposal to amend the requirements of *Prudential Standard LPS 230 Reinsurance* (LPS 230), specifically as they relate to financial reinsurance. APRA welcomes feedback from life insurers and other interested parties on the proposals discussed in this letter.

Background

The current LPS 230 requires reinsurance contracts that are potentially financial reinsurance arrangements, or that include non-standard features or clauses that may impact on the extent of risk transfer, to be submitted to APRA for approval. Financial reinsurance arrangements are reinsurance arrangements that may not genuinely transfer, for the life of the book of business being reinsured, significant insurance risk from the life company to another life company or a reinsurer. Given the potential adverse prudential consequences of such arrangements, and the difficulty of precisely defining when a reinsurance arrangement would require APRA approval, the current LPS 230 requires a wide range of contracts to receive APRA approval, and is very narrow in defining which contracts are exempt.

As outlined in APRA's 30 June 2017 letter to industry, the current LPS 230 will sunset in April 2018 and needs to be re-made.¹

Proposed approach

APRA proposes to amend LPS 230 to align the approach to financial reinsurance with the approach taken in the general insurance industry, under *Prudential Standard GPS 230 Reinsurance Management*. Specifically, the proposed draft standard takes a principles-based approach to determining when approval is required, rather than the current prescriptive criteria.

APRA expects that this approach will:

- allow for clearer focus on the economic substance of reinsurance arrangements;
- support better quality discussions between life insurers and APRA supervisors regarding the key issues in reinsurance arrangements; and
- be more responsive to developments in the reinsurance market.

¹ http://www.apra.gov.au/lifs/PrudentialFramework/Documents/LPS-230-Reinsurance_Nov2007.pdf

The new approach is also intended to reduce the burden on both APRA and life insurers, by minimising instances in which contracts which are not of prudential concern are required to be submitted to APRA for approval. It will create greater consistency between the general insurance and life insurance prudential frameworks.

This is achieved through paragraphs 8 - 14 of the draft LPS 230, which outline APRA's general approach to Limited Risk Transfer Arrangements, and Attachment B of the draft, which outlines the circumstances in which approval is required. Contracts would require APRA approval where the arrangement meets the definition of a Limited Risk Transfer Arrangement contained in LPS 230. APRA expects that life insurers will consider the economic substance of proposed reinsurance arrangements when assessing whether they meet the definition of Limited Risk Transfer Arrangement.

Further, in view of APRA's review of the role of the Appointed Actuary, APRA proposes to remove the current requirement in Attachment A of LPS 230 for the Appointed Actuary to express an opinion on reinsurance arrangements in the reinsurance report.² The role of the Appointed Actuary in assessing reinsurance is being addressed in APRA's broader review of the role.

Next steps

The draft LPS 230 is attached to this letter. APRA seeks feedback from insurers about the proposed changes. Insurers are also welcome to raise any other issues within LPS 230 that they consider worthy of review.

Written submissions should be sent to insurance.policy@apra.gov.au by 22 December 2017 and addressed to:

Senior Manager
Policy Development
Australian Prudential Regulation Authority

APRA expects to finalise the revised standard next year, for implementation from 1 April 2018.

We look forward to your contribution to this consultation process.

Yours sincerely,



Pat Brennan
Executive General Manager
Policy and Advice Division

² Note that the Appointed Actuary has a role in relation to applications for approval of Limited Risk Transfer Arrangements under subparagraph 6(d) of Attachment B of draft LPS 230.