insurance europe

Market access and trade barriers faced by European insurers and reinsurers in foreign jurisdictions (June 2022)

CANADA

The review of the Canadian regulatory framework includes several threats to foreign/European reinsurers that conduct business on a cross-border basis. Insurance Europe is also concerned that the review will increase Canada's protection gap, as reinsurance capacity will significantly reduce and insurance prices will need to rise.

Existing legislation and recent developments

Reform of the Canadian reinsurance framework

Currently, reinsurance is permitted on a cross-border basis. There is, however, a collateral requirement of 120% of ceded policy liabilities, plus receivables from the assuming insurer minus the amount of payables to the assuming reinsurer.

Canada recently concluded its review of the reinsurance framework. It began in June 2018, when the Canadian regulator — the Office of the Superintendent of Financial Institutions (OSFI) — published a discussion paper which included proposals that could threaten the operations of foreign reinsurers. In February 2022, OSFI published two revised guidelines, which are due to come into effect in January 2025. The transition period will allow federally regulated insurers (FRIs) to adjust their business practices.

The guidelines, "B-2, Property and Casualty Large Insurance Exposures and Investment Concentration" (here) and "B-3, Sound Reinsurance Practices and Procedures" (here) introduce a number of measures that will have a negative impact on the industry. Effectively, these guidelines will create an **unlevel playing field between non-registered reinsurance (business written on a cross-border basis) and registered reinsurance (business written by a branch), in favour of registered reinsurance**.

Guideline B-3 introduces several restrictions for reinsurance, such as counterparty concentration limits and ceding limits, with insurers not allowed to cede 100% (or substantially all) of its insurance risks to another reinsurer. They also tighten requirements for reinsurance security arrangements, notably by requiring FRIs to regularly assess these arrangements. This may involve stress testing to determine if the reinsurance arrangements mitigate exposures to acceptable levels adequately in accordance with the FRI's appetite. In addition, the Guideline B-3 effectively denies recognition of foreign reinsurance arrangements when risks insured in Canada are ceded back to the foreign insurer's home office through affiliated reinsurers. These reforms focus mainly on property and casualty (P&C) business — some additional life and health capital requirements are, however, already in place.

Guideline B-2 sets out OSFI's expectations in relation to large insurance exposures, namely losses a P&C FRI could suffer from a single large insurance exposure and the sudden failure of an individual, unregistered insurance counterparty. The guideline will require registered P&C insurers to establish a Gross Underwriting Limit Policy (GWUP), setting limits by class of insurance regarding the level of gross insurance risk that the P&C insurer accepts in respect of a maximum loss related to a Single Insurance Exposure (SIE). Further, the Guideline defines an Insurance Exposure Limit based on the net retention of a P&C insurer plus its largest net counterparty unregistered reinsurance exposure due to the occurrence of the maximum loss related to a SIE. It also requires limits for investment concentration within an entity or group.

Impact of the reform on foreign reinsurers and the Canadian (re)insurance market

The reform creates barriers to foreign/European reinsurers doing business on a cross-border basis and impacts the business models of major international insurance and reinsurance players. Registered (re)insurers need to obtain additional capital or secure collateral in Canada from unregistered reinsurance counterparties. It is also likely that limits on certain business lines would need to be reduced.

Insurance Europe considers that the proposals constitute market access barriers, including the introduction of a reinsurance concentration limit for retrocession contracts, as well as limitations on high-risk exposure policies to be ceded to a reinsurer. The target of overseeing the default counterparty risk should not result in regulations that eliminate vital reinsurance diversification and free access to cross-border reinsurance.

The impact of the proposed B-2 Guideline will be to concentrate reinsurance purchasing in the hands of a relatively small number of registered reinsurers in Canada (effectively eliminating access to unregistered reinsurance capacity) thereby driving the cost of reinsurance significantly higher.

Cedants will have no option but to pass on the burden of higher reinsurance costs to Canadian policyholders. Some Canadian businesses will not be able to purchase the coverage they need, and this will increase the insurance gap. If the Canadian (re)insurance market shrinks, this would have negative implications for premium taxes and HST (a local form of value-added tax).

When implemented, these proposals are likely to create unintended consequences that may adversely impact the Canadian insurance market and effectively reduce its reinsurance capacity. The functioning of insurance markets relies on the global nature of reinsurance and the ability of writers of large coverages to pool these risks effectively with other risks diversified by geography, line of business, etc. While OSFI may view the acquisition by Canadian cedants of registered reinsurance to be preferable, it ignores the benefits of reinsurer counterparty diversification. The impact of Guideline B-2 will be the concentration of reinsurance counterparty credit risk.

Restrictions on ease of doing business in Quebec

In 2021, the Quebec government introduced Quebec Bill 96, "An Act respecting French, the official and common language of Quebec and professional bodies ("Bill 96"), which would significantly heighten requirements for business conducting operations in Quebec with regards to their communications in French.

In its current form, the proposed Bill sets out that **contracts and other documents must be drafted in French**. Bill 96 elaborates on the existing requirement that contracts pre-determined by one party, contracts containing standard clauses, and the related documents, must be drawn up in French. Businesses will have to provide a French version of these documents before a counterparty expresses a wish to be bound by a version written in another language.

In addition, the proposed Bill introduces explicit requirements for **businesses to offer goods and services to consumers, as well as non-consumers, in French**. It would extend the current consumers' right to be informed and served in French, to non-consumers and explicitly imposes obligation on businesses to respect such right.

These proposed requirements would therefore create significant barriers to doing business in the Province of Quebec and is likely to impact (re)insurers' business model in Canada.

Recommendations and preferred outcomes

Insurance Europe takes the view that the proposed reform does not adequately take into account how the global reinsurance market operates.

The reform is clearly not in line with the spirit of the Canada-EU free trade agreement, even though the agreement stipulates that a local regulator can apply separate rules, which is what OSFI is doing. It is unclear whether the reform is in line with the WTO's General Agreement on Trade in Services (GATS).