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China Confirms Motor Insurance Premium Reform

The Announcement

On 8 March 2012, the China Insurance Regulatory Commission (CIRC) issued an announcement on the strengthening of the premium rating management for voluntary motor insurance covers. In essence, the majority of companies will be required to follow a standard tariff for pure premiums, and use standard product designs and policy wordings. However, companies will be allowed to vary their premium loadings for expenses and commission up to an overall maximum of 35% of premiums, subject to prior approval by CIRC.

Companies able to manage their combined ratios below 100% for two consecutive years will be allowed to expand the benefits offered beyond that of the standard product, subject to approval from CIRC. In addition, companies meeting the following criteria would be allowed to use their own data to determine their pure premium rates:

- Combined ratios are below 100% for the past two consecutive years
- Comprehensive corporate governance with effective internal controls
- Has been writing motor insurance business for at least the past three years
- Statutory solvency ratio above 150% for the past two consecutive years
- Has accumulated motor data for at least 300,000 vehicles
- Has a commercial motor business development team that is familiar with the associated laws and regulations, and has pricing capabilities and a complete business workflow and information systems
- Other requirements set by the CIRC

However, these premium rates would be subject to formal approval by CIRC and would need to be reviewed annually, giving due consideration to the historical data, business development and claims reserve requirements.

The announcement also touched upon a few long-standing issues the industry has been grappling with, although the details have not yet been worked out:

- An insurer and a policyholder will need to agree on the market value of the insured vehicle.
- In the case of damage to the insured vehicle caused by a third party vehicle, the insurer cannot refuse to reimburse the damage; instead, the insurer will have to pay the claim regardless of fault and pursue subrogation from the third party.

These will be more clearly defined and addressed in the impending standard industry policy wording.

Implications

In principle, the guidelines are effective immediately. However, in practice, there are still a lot of important and sensitive issues that need to be ironed out. We would not expect the guidelines to be implemented within the next six months.

In principle, these guidelines should result in free market pricing. There is enough leeway for well-managed small to medium-sized insurers to differentiate themselves through premium rates and product design, targeting specific segments.

However, all premium rates and products are subject to CIRC's prior approval, and the memory of the industry's losses during the years when the motor premium rates were de-tariffed, leading to large capital injections by numerous companies, is still fresh in the minds of CIRC and insurers. We expect CIRC will continue to keep tight control of insurers, at least in the near future.

Still, this does present opportunities for the more sophisticated insurers. In particular, this may play into the hands of the foreign insurers, who in the future will be allowed to sell compulsory third-party motor insurance, which has long been a stumbling block to foreign companies writing motor insurance in general. There could be significant opportunities for foreign insurers who are able to adapt their technology and knowledge from more developed markets to suit the local business practices in China.

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