

Japan

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MARKET TRENDS AND REGULATORY FRAMEWORK

1. What were the main trends in the insurance and reinsurance markets over the last 12 months?

Life insurance

As of 4 February 2013, there are 43 private life insurance companies in Japan, which comprise:

- 40 domestic insurance companies. (These include American Life Insurance Company, which changed the form of its insurance business in Japan from a licensed Japanese branch to a licensed Japanese subsidiary on 2 April 2012, and Japan Post Insurance (JPIC), which is held by the Japanese government through a holding company. Although its privatisation was frozen for a period, the law that froze the planned sale of shares in Japan Post Holdings, Japan Post Bank and JPIC was abolished in May 2012. The target period of the sale of the shares (that is, 1 October 2007 to 30 September 2017) originally contemplated and stated in the previous law were deleted by the new act.)
- Three branches of foreign insurers.

The Japanese life insurance market is very competitive with a large number of companies.

Various types of life insurance contracts are offered in Japan. Recently, due to the falling birth rate and the ageing population, the demand for life insurance coverage has declined and the demand for individual annuities has increased.

The sales channels for insurance contracts have diversified. Traditionally, sales were made face-to-face by employees of life insurance companies. However, the use of agents and direct marketing is becoming more common. In addition, bancassurance (that is, the selling of insurance products by a bank) was liberalised in December 2007, and many life insurance companies are now focusing on this channel in anticipation of an increase in sales.

Non-life insurance

As of 4 February 2013, there are 53 private non-life insurance companies in Japan, which comprise:

- 29 domestic insurance companies.
- 23 branches of foreign insurers, and the Society of Lloyd's.

Due to the falling birth rate and the ageing population, the non-life insurance market is shrinking and becoming more competitive. In addition, recently non-life insurance companies have been forced to pay insurance claims for damage caused by huge catastrophes such as those occasioned by the Great East Japan Earthquake of 2011 and the Thailand flood of 2012.

As with the life insurance market, the non-life insurance sale channels are diverse and many insurance companies focus on the bancassurance channel.

Third-sector insurance

Third-sector insurance includes:

- Medical insurance.
- Long-term care insurance.
- Personal injury insurance.

As both life insurance companies and non-life insurance companies are permitted to sell third-sector insurance products, these companies compete in this market.

Small-amount and short-term insurance (SASTI) providers

Small-amount and short-term insurance refers to the business of underwriting insurance limited to insurance periods of two years or less, and insurance amounts not exceeding JPY10 million. Before April 2006 the Insurance Business Act (IBA) did not apply to entities that engaged in quasi-insurance business. However, since this business is similar to the insurance business, the definition of insurance business was reviewed and the IBA introduced provisions concerning SASTI providers. As of 15 January 2013, there are 71 SASTI providers in Japan.

Reinsurance

Due to the expansion, diversification and complication of risks, reinsurance is essential for the insurance market in Japan. In particular, Japan experiences many earthquakes and typhoons. Therefore, insurance companies in Japan are required to reinsure these risks with foreign reinsurers.

There are two domestic reinsurance companies and a number of branches of foreign reinsurers in Japan. Non-life insurance companies also underwrite reinsurance. Japanese non-life insurance companies play an important role in the world's reinsurance market.



2. What is the regulatory framework for insurance/reinsurance activities?

Regulatory framework

IBA. The IBA and related regulations provide for the supervision and regulation of the insurance and reinsurance business. The definition of an insurance business under the IBA includes insurance and reinsurance activities. Therefore, the IBA regulates insurers and reinsurers in the same way.

The IBA consists of three parts:

- Provisions relating to the supervision and regulation of persons/entities which are engaged in insurance business.
- Provisions relating to the incorporation and organisation of mutual insurance companies.
- Provisions relating to the protection of policyholders (including insured(s) or insurance beneficiary(ies) in relation to life insurance or fixed benefit accident and health insurance).

Japanese insurance companies and SASTI providers (excluding non-profit juridical persons approved as SASTI providers) must be stock companies or mutual companies with the following bodies:

- A board of directors.
- A board of company auditors or committee.
- An accounting auditor (with some exceptions).

Non-profit juridical persons (defined under the Act to Promote Specified Non-profit Activities) are also allowed to apply for the registration as SASTI providers if both:

- They have the requisite executive officers.
- Were engaged in quasi-insurance business at the time of the amendment of the IBA in 2006.

In addition, Japanese insurance companies must hold more than JPY1 billion in either:

- Stated capital (in the case of a stock company).
- Total amount of *Kikin* (the funds held by a mutual insurance company, equivalent to the capital held by stock companies) including a reserve for redemption of *Kikin* in the case of a mutual company.

In the case of SASTI providers, the required amount of *Kikin* is JPY10 million. In general, a branch of a foreign insurer (Licensed Branch) must deposit JPY200 million of the statutory deposit amount with the deposit office. In addition, the IBA requires a Licensed Branch to hold and keep assets located in Japan with a value that is equivalent to the total sum of the statutory deposit amount, carried-in capital and certain reserves.

For the restrictions on business, see *Question 7*. In relation to other ongoing requirements, see *Question 13*.

The IBA also sets out special provisions concerning mergers, transfers of business, and company splits concerning insurance companies. These transactions require authorisation from the Financial Services Agency (FSA).

The IBA also regulates shareholders, insurance holding companies, and insurance solicitation.

In addition, the IBA stipulates the establishment of a policyholders' protection corporation system to protect policyholders if the insurance company collapses. Under these provisions, the Non-life Insurance Policyholders Protection Corporation and the Life Insurance Policyholders Protection Corporation were established in Japan.

Insurance Act. The Insurance Act (which replaced certain provisions of the Commercial Code on 1 April 2010) regulates insurance contracts (see *Question 4*).

Other laws. The Financial Instruments Sales Act, the Consumer Contract Act, and the Financial Instruments and Exchange Act (FIEA) also provide rules relating to the solicitation and sale of insurance contracts.

The Act on Prohibition of Private Monopolisation and Maintenance of Fair Trade (Anti-Monopoly Law) and the Act Against Unjustifiable Premiums and Misleading Representations also apply to the insurance business and insurance contracts.

Regulatory bodies

The FSA is the governing authority that regulates the insurance industry and supervises the entities which conduct insurance business and related business. The Prime Minister of Japan (PM) delegates authority (excluding certain important powers such as granting or cancelling insurance business licences) to the commissioner of the FSA. The commissioner of the FSA further delegates a part of his authority to the directors of the Local Finance Bureau of the Ministry of Finance (LFB).

The FSA and the LFB have the authority to (*IBA*):

- Demand reports from and inspect insurance companies, licensed branches, SASTI providers, subsidiaries thereof, service providers subcontracted by any insurance company, certain major shareholders, insurance holding companies, and insurance agents and brokers.
- Take administrative action against insurance companies, licensed branches, SASTI providers, certain major shareholders of insurance companies, insurance holding companies, and insurance agents and brokers.

The FSA stipulates detailed regulations under the IBA. Additionally, the Comprehensive Guidelines for the Supervision of Insurance Companies and SASTI Providers (Guidelines), set by the FSA, contain basic concepts, evaluation criteria and other guidelines relating to the supervision of insurance companies and SASTI providers, which should be observed when doing insurance business in Japan.

REGULATION OF INSURANCE AND REINSURANCE CONTRACTS

3. What is a contract of insurance for the purposes of the law and regulation? How does it differ from a contract of reinsurance?

IBA. A contract of insurance is not defined in the IBA.

Insurance Act. An insurance contract under the Insurance Act is defined as an insurance contract, a mutual aid contract or any other contract in whatever name, under which both:

- One party undertakes to pay financial benefits (limited to the payment of money in life insurance contracts and fixed benefit accident and health insurance contracts) to the other party, subject to a certain event occurring.
- The other party undertakes to pay insurance premiums (including mutual aid premiums), the calculation of which are based on the possibility of a certain event occurring.

There is no definition of a contract of reinsurance in the Insurance Act or the IBA. A contract of reinsurance is a type of non-life insurance.

Life insurance is defined as an insurance contract in which insurers pay financial benefits with respect to the survival or death of individuals. Medical insurance, long-term care insurance and personal injury insurance are included in third-sector insurance, where an interest is clearly eligible to be insured. Non-life insurance is defined as an insurance contract under which the insurer agrees to indemnify the loss that may arise from specific accidents. The subject matter of a non-life insurance contract must be an interest that may be measured by an amount of money (that is, an insurable interest). The insurable interest must be held by the insured. In this way, non-life insurance is distinguished from gambling. In practice, whether the insured holds insurable interests is decided on a case by case basis, so that those in need of cover are not unduly restricted from accessing sufficient cover.

4. Are all contracts of insurance/reinsurance regulated?

IBA. The IBA does not regulate the underwriting of the following contracts of insurance:

- Contracts of insurance/reinsurance regulated by other laws of Japan.
- Contracts of insurance/reinsurance provided by certain groups (such as local governments, companies, and labour unions) with their members as the other party.
- Contracts of insurance/reinsurance transacted within a limited group of 1,000 persons or fewer.

Insurance Act. Apart from marine insurance, which is still governed by the Commercial Code, the Insurance Act generally regulates insurance contracts entered into after 1 April 2010. Insurance contracts are classified into three categories (*Insurance Act*):

- Non-life insurance.
- Life insurance.
- Fixed benefit accident and health insurance.
- A contract of reinsurance is a type of non-life insurance and is regulated by the Insurance Act.

The Japanese government, local government and other public entities provide public insurance contracts, such as health insurance, care insurance, annuity insurance, worker's compensation insurance, and trade insurance. Special laws regulate each type of insurance contract.

CORPORATE STRUCTURE

5. What form of corporate organisation can insurers take?

Japanese insurance companies and SASTI providers, apart from non-profit juridical persons approved as SASTI providers, must be stock companies or mutual companies with certain bodies (see *Question 2, Regulatory framework*). Foreign insurers with licences under the IBA are allowed to engage in insurance business through their Japanese branches (see *Question 9, Insurance/reinsurance providers*).

REGULATION OF INSURERS AND REINSURERS

6. Are all insurers and reinsurers regulated? Are they all regulated in the same way?

In general, insurers and reinsurers are regulated in the same way (see *Question 2*).

7. Can insurers and reinsurers carry on non-insurance business? Are there any restrictions on their business activities?

One person cannot obtain both a life insurance business licence and a non-life insurance business licence. Accordingly, insurance companies and licensed branches are allowed to conduct either life insurance or non-life insurance business subject to the licence obtained. However, life insurance companies are entitled to hold subsidiaries that could be licensed as non-life insurance providers and vice versa. Through these subsidiaries, life insurance companies can carry on non-insurance business, and non-life insurance companies can carry on life insurance business, which allows insurance companies undertake cross selling (that is, life insurance companies are able to sell life insurance to non-life insurance customers of their non-life insurance subsidiaries, and non-life insurance companies are able to sell non-life insurance to life insurance customers of their life insurance subsidiaries).

Insurance companies and licensed branches can carry out only the following three types of business under the IBA:

- Underwriting insurance and management of assets (Typical Business).
- Business related to Typical Business, for example:
 - representing the business or performing services on behalf of other insurance companies and other entities carrying out financial business;
 - guarantees of obligations;
 - handling private placements of securities; and
 - derivative transactions.
- Business permissible under the IBA and other laws (for example, certain securities trading business and trust business concerning secured bonds).



Insurance companies cannot hold subsidiaries other than those set out in the IBA, including, among others:

- Insurance companies.
- Banks.
- Securities companies.
- Companies that engage in business that is dependent on the business of their parent insurance companies and the above-listed financial subsidiaries of the parent insurance companies.
- Companies that engage in business incidental or related to financial business.

Insurance companies or their subsidiaries cannot acquire or hold, on an aggregated basis, more than 10% of the total voting rights of all shareholders of any other company in Japan, except certain companies listed in the IBA. The Anti-Monopoly Law imposes similar restrictions.

The limitation under the IBA and its regulation on the types of investments which insurance companies and licensed branches could make and the percentage of their total assets which could be invested in certain types of investment was removed in April 2012. However, the IBA still limits the insurance company's (and, on an aggregated basis, an insurance company's group's) exposure to any one person/entity (including its affiliates).

The arm's-length rule applies to transactions between insurance companies (including Licensed Branches and SASTI providers) and a specific party (such as a subsidiary or affiliated company of each relevant insurance company) or its customers. The arm's length rule prohibits transactions that would be unduly favourable or detrimental to the insurance company in light of the insurance company's normal terms of trade (*IBA*).

SASTI providers can conduct small-amount and small-term insurance business (*IBA*). They can conduct certain other types of business with the LFB's approval. There are stricter restrictions regarding subsidiaries and limitation on the types of investments.

8. Are there any statutory limits or other restrictions on, or requirements relating to, the transfer of risk by insurance or reinsurance companies?

When an insurance company reinsures its insurance policies under financial reinsurance contracts, it must reserve a certain amount as a policy reserve (*IBA*). In addition, the insurance company must submit a notification to the FSA in advance of the execution or termination of financial reinsurance contracts.

The Guidelines require insurance companies to:

- Stipulate the policies and rules relating to ceding risks to reinsurers and underwriting reinsurance from other insurance companies.
- Disclose their basic policy relating to ceding risks to reinsurers and underwriting reinsurance from other insurance companies in the disclosure document.
- Manage these risks properly.

OPERATING RESTRICTIONS

Authorisation or licensing

9. Does the entity or person have to be authorised or licensed?

Insurance/reinsurance providers

Japanese insurance companies. Insurance companies must obtain from the PM either a:

- Life insurance business licence.
- Non-life insurance business licence.

The applicant must submit a licence application with required attachments to the PM through the FSA. The required attachments include, among others:

- The following four documents (Basic Documents), the applicant's:
 - articles of incorporation;
 - statement of business procedures;
 - general policy conditions;
 - statement of calculation procedures for insurance premiums and policy reserves.
- A business plan.
- Documents explaining the status of recent assets, profits and losses.
- Documents relating to the applicant's subsidiaries.

To protect the public interest, the PM can impose conditions on licences or revise their conditions.

SASTI providers. SASTI providers must register with the PM through the LFB. The registration application and its required attachments are similar to those for a licence application (*see above, Japanese insurance companies*).

Japanese branches of foreign insurers. For a foreign insurer to conduct insurance business in Japan, its Japanese branch must obtain from the PM either a:

- Life insurance business licence.
- Non-life insurance business licence.

The procedures for foreign insurers to obtain a licence are similar to those for Japanese insurance companies (*see above, Japanese insurance companies*).

Syndicates of Lloyd's. Syndicates of Lloyd's can engage in insurance business in Japan through a general agent in Japan, if the Lloyd's representative in Japan and its underwriting members file a notification relating to the members of the syndicates who engage in insurance business in Japan with the PM through the FSA.

Insurance/reinsurance intermediaries

The persons/entities permitted to act as agents or intermediaries for the conclusion of an insurance contract are limited to the following (*IBA*):

- Life insurance agents.

- Officers and employees of non-life insurance companies.
- Non-life insurance agents, their officers and employees.
- Small-amount and short-term insurance agents.
- Brokers.

Life insurance agents, non-life insurance agents, and small-amount and short-term insurance agents must register with the PM through the LFB. The applicant submits an application for registration with the LFB.

Other providers of insurance/reinsurance-related activities

Brokers must register with the PM through the LFB. The applicant must submit a registration application with the LFB.

Other entities that market insurance and reinsurance-related services, or conduct insurance and reinsurance-related activities, are not required to be licensed or registered (*IBA*).

10. What are the main exemptions or exclusions from authorisation or licensing?

Insurance/reinsurance providers

The IBA does not apply to the following types of business:

- Business regulated by other laws.
- Business transacted by certain groups (such as local governments, companies and labour unions) with their members as the other party.
- Business transacted within a limited group of 1,000 persons or fewer.

Insurance/reinsurance intermediaries

The IBA does not require the officers and employees of non-life insurance companies to register when they act as agents or intermediaries for the conclusion of an insurance contract. However, it requires those of life insurance companies to register as life insurance agents.

Other providers of insurance/reinsurance-related activities

There are no available exemptions or exclusions for brokers.

Restrictions on ownership or control

11. Are there any restrictions on the ownership or control of insurance-related entities?

Insurance/reinsurance providers

For the restrictions on the ownership or control of insurance/reinsurance providers, see *Question 12, Insurance/reinsurance providers*.

Insurance/reinsurance intermediaries

There are no restrictions on ownership or control.

Other providers of insurance/reinsurance-related activities

There are no restrictions on ownership or control.

12. Must owners or controllers be approved by or notified to the relevant authorities before taking, increasing or reducing their control or ownership of the entity?

Insurance/reinsurance providers

IBA. A shareholder of a Japanese insurance company or insurance holding company that holds more than 5% of the total voting rights must file a notification with the LFB or (in certain cases) the FSA, and file a report each time there is a change to the notification.

If the person/entity is to acquire directly or indirectly (through other entities) at least 20% of the total voting rights of a Japanese insurance company (or 15% in certain cases) (Major Shareholder Threshold), they must obtain prior authorisation from the FSA.

The IBA provides a certain review standard for the authorisation to ensure sound and appropriate management of the insurance company's business.

Acquisitions of SASTIs must be pre-approved by the LFB when the Major Shareholder Threshold is surpassed.

The acquirer or holder must file an ex-post notification with either the FSA or LFB respectively, if either:

- The person/entity acquires more than 50% of the total voting rights of a Japanese insurance company or SASTI provider.
- The number of voting rights held becomes either:
 - equal to or less than 50%;
 - less than the Major Shareholder Threshold.

Holding companies. The following must obtain prior authorisation from the PM:

- A company which intends to become a holding company with an insurance company as its subsidiary.
- A person who intends to establish such a holding company.

In the case of SASTI providers, pre-approval is required from the PM through the LFB.

After becoming an insurance holding company, notification is necessary when the company makes an insurance company its subsidiary.

The holding company must file a notification if an insurance company or a SASTI provider ceases to be its subsidiary.

Other laws. In some cases, a person/entity that acquires the shares of a Japanese insurance company must file a report in advance or an ex-post report (*FIEA* and *Foreign Exchange and Foreign Trade Act of Japan*).

Insurance/reinsurance intermediaries

The IBA does not require authorisation, approval, or notification when owners or controllers take, increase, or reduce their control or ownership of these entities.



Other providers of insurance/reinsurance-related activities

No authorisation, approval, or notification is required for other providers of insurance/reinsurance-related activities. This is the same as for marketing insurance/reinsurance services (see above, *Marketing insurance/reinsurance services*).

Ongoing requirements for the authorised or licensed entity

13. What are the key ongoing requirements with which the authorised or licensed entity must comply?

Insurance/reinsurance providers

Disclosure requirements. For each business year, insurance companies must both:

- Submit an interim business report and business report to the FSA.
- Prepare explanatory documents relating to the status of their business and property and keep them for public inspection at their head office and branch offices.

Basic Documents. If an insurance company wishes to amend its Basic Documents other than its articles of incorporation, it must obtain prior authorisation from the FSA. However, certain amendments to these documents, such as matters relating to corporate insurance, require only filing.

Amendments to certain material matters of the articles of incorporation of insurance companies, such as the company's name and (in the case of a mutual company) matters relating to redemption of *Kikin* (see *Question 2*) and termination of membership, require authorisation from the FSA.

Notification requirements. The IBA requires insurance companies to file a notification relating to certain matters, such as:

- Amendments to the articles of incorporation (other than for matters which require authorisation).
- An increase in capital amount or the total amount of *Kikin*.
- If one shareholder acquires or holds at least 5% of the voting rights of a concerned insurance company.
- A change of directors or auditors.
- Matters relating to its subsidiaries.

Solvency margin requirement. The IBA provides for a solvency margin ratio as a standard to assess the soundness of an insurance company's business. The solvency margin ratio is calculated by dividing the total amount of stated capital/*Kikin*, reserves and other amounts by the amount available to cope with possible risks, exceeding the standard predictions that may occur due to insurance accidents. Insurance companies must maintain a solvency margin ratio of at least 200%. However, in practice, all insurance companies maintain a higher ratio.

A new method of calculating the solvency margin ratio has applied from the fiscal year ended 31 March 2012.

In addition, the group solvency margin requirement has applied since the fiscal year ended 31 March 2012, which means the

solvency margin ratio should be calculated on a group basis (that is, the insurance holding company and its subsidiary or the insurance company and its subsidiary).

Similar ongoing requirements apply to Licensed Branches and SASTI providers.

Approval requirements. Insurance companies must obtain approval for the following (*IBA*):

- Transactions that are not generally conducted in the ordinary course of business (such as a comprehensive transfer of insurance contracts, transfer of insurance business or entrustment of insurance business).
- Corporate actions which involve:
 - a reduction of the capital of stock insurance companies;
 - entity conversion of a stock insurance company into a mutual insurance company (and vice versa);
 - a merger, company split or liquidation.

Issuance of any equity triggers an *ex ante* notification obligation only when the insurance company increases its stated capital with such issuance of equity. Debt security also requires an *ex ante* notification, but only if it is in the form of bonds with share warrants.

The arm's-length rule. See *Question 7*.

Insurance/reinsurance intermediaries

Registered agents must file a notification when either:

- There is a change to the basic information provided in the application.
- They cease to act as an agent or intermediary for the conclusion of an insurance contract.

Other providers of insurance/reinsurance-related activities

The registered brokers have the same filing obligations as those of registered agents (see above, *Insurance/reinsurance intermediaries*).

Penalties for non-compliance with legal and regulatory requirements

14. What are the possible consequences of an entity failing to comply with applicable legal and regulatory requirements? What recourse do policyholders have if they have done business with a non-approved entity?

The IBA provides for imprisonment or fines for persons who violate certain provisions of the IBA.

Insurance/reinsurance providers

When the FSA finds it necessary to protect policyholders by ensuring the sound management of an insurance company, in view of the situation of the business or property of the insurance company (or situation of the assets of its subsidiaries), it can:

- Issue a business improvement order.
- Issue a full or partial suspension order of the insurance company's business.

- Order the deposit of property of the insurance company.
- Take other necessary measures for supervision.

The FSA can also combine some of the above measures.

The FSA (in the case of rescission, the PM) can order the full or partial suspension of the insurance company's business or the dismissal of any of the directors, executive officers, accounting advisers, or auditors, or rescind the licence, if an insurance company:

- Is in violation of laws and regulations, measures of the PM under laws and regulations, or particularly vital matters among those prescribed in its Basic Documents.
- Is in violation of the conditions attached to its licence.
- Commits acts prejudicial to the public interest.

In addition, the PM can rescind the insurance company's licence if he finds that the financial situation of an insurance company is significantly worsening and that it is not appropriate to continue the insurance business from the viewpoint of protecting policyholders.

Insurance/reinsurance intermediaries

The LFB can cancel the registration of an agent or take other administrative action.

If a customer incurs loss due to improper actions of an agent, the agent must indemnify the customer against such loss. If the loss is associated with the solicitation of insurance contracts, the insurance company must also indemnify the customer.

Other providers of insurance/reinsurance-related activities

The LFB can cancel the registration of a broker or take other administrative action.

If a customer incurs loss due to the improper action of a broker, the broker must indemnify the customer for the loss. Brokers are independent from insurance companies. Therefore, to ensure the resources to indemnify customers against loss, the IBA requires brokers to:

- Deposit a security deposit with the deposit office.
- Conclude a contract stipulating that a required amount of security deposit be lodged by the broker, by order of the PM.
- Conclude a broker's liability insurance contract.

If policyholders have done business with a non-approved entity, they may only have recourse to the assets of the non-approved entity.

Restrictions on persons to whom services can be marketed or sold

15. Are there any restrictions on the persons to whom insurance/reinsurance services and contracts can be marketed or sold?

Insurance/reinsurance providers

There are usually no restrictions on the persons to whom insurance/reinsurance services and contracts can be marketed or sold.

However, when soliciting insurance contracts with a market risk (such as individual variable annuity insurance), each policy applicant must be informed of this risk both:

- In a manner and to the extent necessary for the applicant's understanding.
- In a manner that is appropriate in light of the applicant's knowledge, experience, financial condition or purpose for concluding the contract.

Foreign insurers not licensed under the IBA in Japan and without branch offices in Japan cannot conclude domestic risk insurance contracts, except certain insurance contracts, such as:

- Reinsurance.
- Insurance covering international freight.
- Overseas travel insurance.
- Insurance for which prior permission from the FSA has been received by the policy applicant.

Domestic risk insurance refers to insurance contracts for persons resident or domiciled in Japan or with property located, or vessels and aircraft registered, in Japan.

However, policy applicants cannot enter into any domestic risk insurance contract with a foreign insurer not licensed in Japan, subject to the same exceptions (*see above*).

Marketing insurance/reinsurance services

The same restriction applies to marketing insurance/reinsurance services (*see above, Insurance/reinsurance providers*).

Other providers of insurance/reinsurance-related activities

The same restriction applies to other providers of insurance/reinsurance-related activities (*see above, Insurance/reinsurance providers*).

REINSURANCE MONITORING AND DISCLOSURE REQUIREMENTS

16. To what extent can/must a reinsurance company monitor the claims, settlements and underwriting of the cedant company?

A reinsurance company has no rights or obligations to monitor the claims, settlements or underwriting of a cedant company under the Insurance Act, IBA or any other laws of Japan.

However, these rights and obligations can be stipulated in the reinsurance contract. Generally, a reinsurance company is granted a right to inspect the related records and documents of a cedant company under a reinsurance contract.

17. What disclosure/notification obligations does the cedant company have to the reinsurance company?

There are no specific regulations providing any obligations on the cedant company to the reinsurance company under the Insurance Act, the IBA, or any other laws of Japan. It is suggested that the



articles of the Insurance Act relating to non-life insurance, such as the duty of disclosure and notification (see *Question 20*), may also apply to reinsurance, since reinsurance is a type of non-life insurance.

However, in practice, obligations of disclosure or notification are stipulated in a reinsurance contract. Generally, a cedant company is required by the terms of the reinsurance contract to notify the reinsurance company if either:

- An original insurance contract is executed.
- The general policy provisions of the ceded insurance are changed by the ceded company.

INSURANCE AND REINSURANCE POLICIES

Content requirements and commonly found clauses

18. What are the main general form and content requirements for insurance policies? What are the most commonly found clauses?

Form and content requirements

Policy conditions. Under the Insurance Act, there are several types of provisions that include discretionary provisions, compulsory provisions and unilateral compulsory provisions in favour of insureds or policyholders. When an insurance policy excludes or sets out a provision that conflicts with discretionary provisions, the insurance policy supersedes the discretionary provisions. With respect to compulsory provisions, parties are not allowed to conclude insurance policies that contradict the compulsory provisions and such contradicting policy provisions are null and unenforceable. In addition, unilateral compulsory provisions make provisions in the policy that are less favourable to insureds or policyholders than such unilateral compulsory provisions invalid and unenforceable (see *Question 20*).

While insurance policies are not required to be in writing, insurance contracts are generally concluded with policy conditions (*hoken yakkan*) predetermined by the insurance company and approved by the FSA, or instead of the approval, certain types of insurance contracts can be sold either (*IBA*):

- By giving prior notification to the FSA.
- By stating that the insurance company can create or change the insurance contracts without any prior notification in the statement of business procedures (see *Question 9, Insurance/reinsurance providers*).

A person who wants insurance coverage submits an insurance application form to an insurance company, and if the insurance company accepts his application, an insurance contract is concluded and the terms of the policy conditions become binding between them.

Policy conditions consist of both:

- General policy conditions in which the basic terms of the insurance policy are stipulated (see *below, Commonly found clauses*).
- Special policy conditions by which the terms of the general policy conditions are amended or supplemented.

Insurance certificate. If an insurance contract is concluded, the insurance company must deliver an insurance certificate (*hoken shoken*) to the policyholder where the policy conditions do not exclude the application of this provision (*Insurance Act*). The insurance certificates set out basic information such as the (*Insurance Act*):

- Insurance premium.
- Insurance period.
- Risks covered.
- Insured amount.
- Policyholder's name.

Commonly found clauses

General policy conditions commonly include clauses relating to the following matters:

- Scope of the insurance.
- Limit of the insurance company's liability.
- Commencement and termination date of the insurance.
- Calculation of the amount of the insurance claim.
- Procedure for payment of the insurance claim.
- Duty of disclosure.
- Duty of notification.
- Insurance subrogation.
- Invalidity, expiration or termination of the insurance contract.
- Resolution of disputes and governing law.

19. Is facultative or treaty reinsurance more common? What are the most commonly found clauses in reinsurance policies?

Facultative/treaty reinsurance

Treaty reinsurance is more common in Japan.

Commonly found clauses

There are generally many common clauses in treaty reinsurance policies, such as:

- Commencement of liability.
- Exclusions.
- Cancellation.
- Claims before cession entry.
- Right of reinsured to alter retentions.
- Follow the fortune.
- Currency.
- Commission.
- Accounts.
- Settlement of losses.
- Premium reserve.
- Inspection.

*Implied terms***20. Are there any terms that are implied by law or regulation (even if not included in the insurance or reinsurance contract)?**

In principle, the Japanese Insurance Act regulates insurance policy conditions. Policy conditions should not contradict the compulsory provisions or unilateral compulsory provisions in favour of insureds or policyholders, and if they do so, they will be unenforceable. Major compulsory provisions and unilateral compulsory provisions, and simple explanations of them, are provided in the following paragraphs. In addition, if any of the terms set out in the Insurance Act are omitted from insurance contracts or reinsurance contracts, they will be implied by the Insurance Act. Unilateral compulsory provisions in favour of insureds or policyholders are not applicable to certain commercial lines of insurance, including:

- Marine insurance.
- Insurance concerning airplanes or air cargo.
- Insurance concerning nuclear facilities.
- Business activities insurance.

Duty of disclosure

An insurance company can cancel an insurance contract if a policyholder has failed to disclose material facts or has misrepresented material matters in relation to the insurance (an insurance company must specify material facts relating to insurance under the Insurance Act), due to malicious intent or gross negligence at the time of concluding an insurance contract (*Articles 4, 28, 37, 55, 66 and 84, Insurance Act*). However, this does not apply if an insurance company knew of this fact, or did not know of the fact due to its own negligence. In addition, the insurance company cannot terminate the insurance contract for breach of the duty of disclosure, if an insurance agent either:

- Prevented the policyholder from disclosing material facts.
- Advised the policyholder not to disclose material facts or to misrepresent material matters.

Retrospective insurance

An insurance contract is null and void if either (*Articles 5, 39 and 68, Insurance Act*):

- A policyholder is aware that any accident to be covered by the insurance has already occurred.
- An insurance company is aware that an accident to be covered by the insurance will never occur.

Over insurance

In relation to non-life insurance, if an insured amount exceeds the value of the object insured, a policyholder can cancel the excess part of the insurance contract, unless either (*Article 9, Insurance Act*):

- The excess is caused by the malicious intent or gross negligence of the policyholder.
- There is an agreement regarding the value of the object insured.

Rights of reducing insurance premiums due to decreasing insurance value

If a non-life insurance value is reduced in a significant way, the policyholder can claim for reducing insurance premiums at the level of reduced insurance value (*Article 10, Insurance Act*).

Rights of reducing insurance premiums due to decreasing insurance risk

If an insurance risk is reduced in a significant way, the policyholder can claim for reducing insurance premiums at the level of reduced insurance risk (*Articles 11, 48 and 77, Insurance Act*).

Extinguishment of the insured objects after the occurrence of covered damage

In relation to non-life insurance, insurers must pay insurance reimbursements if the insured objects are extinguished after the covered damage has occurred (*Article 15, Insurance Act*).

Due date of payment of insurance reimbursements

Payment of insurance reimbursements must be forthcoming after a reasonable period required for investigations (*Articles 21, 52, and 81, Insurance Act*).

Statutory lien for liability insurance

In relation to liability insurance, those damaged by covered accidents are entitled to obtain a lien over claims for insurance reimbursements. Therefore, insured parties are allowed to exercise their claim against the insurer only:

- With the consent of those damaged by covered events.
- To the extent that they have indemnified those damaged by covered events.

In addition, liability insurance claims against insurers cannot be transferred, be subject to a pledge or be sequestered, except in certain cases (*Article 22, Insurance Act*).

Insurance subrogation

In relation to non-life insurance, if an insured can claim against another person with respect to the loss covered by the insurance and an insurance company has paid the insurance claim, the insurance company will be subrogated to the rights held by the insured against the other person to an extent that does not prejudice the rights of the insured, but only to the extent of the amount paid (*Article 25, Insurance Act*).

Rights to cancel by insurer

An insurer can cancel the insurance contract when (*Articles 30, 57, and 86, Insurance Act*):

- A policyholder commits fraud or tries to commit fraud against the insurer.
- Where there is a material issue that adversely affects the insurer's trust in the policyholder, making it difficult for the insurer to maintain the insurance contract with the policyholder.

Legal effect of cancellation

The cancellation of insurance contracts is only effective going forward, and the insurer is not then liable for further cases when the insurance contract is cancelled (*Articles 31, 59, and 88, Insurance Act*).



Rights to cancel by the insured

In certain circumstances, when the insured is not the same person as the policyholder, the insured can cancel the insurance contract (*Articles 34, 58, and 87, Insurance Act*). This applies to non-life accident and health insurance, life insurance and fixed-benefit accident and health insurance.

Customer protections

21. How do customer protections in the general law affect insurance contracts? What customer protections are generally included in insurance policies to supplement this?

General law

Consumers including policyholders can rescind their application or acceptance where a business operator including insurance companies and other insurance providers took certain inappropriate actions, for example, made false representation regarding an important matter at the time of solicitation that the consumer relied on at the time of application or acceptance (*Article 4, Consumer Contract Act*).

In addition, certain clauses that impair the interests of consumers unilaterally by restricting the rights of consumers or extending the duties of consumers against the principle of good faith in the Civil Code are void (*Article 10, Consumer Contract Act*).

Insurance policies

The IBA provides an insurance contract applicant with the right to revoke or cancel the application in certain cases (cooling-off). Generally, this information is delivered to the applicants with the supplemental documents of insurance policies. This right will expire in certain cases, for example:

- Where eight days have passed from the issue date of documents describing the right or the date of application, whichever is later.
- Where an application is made for an insurance contract for business use.
- In other cases set out in the IBA and its regulations.

In addition, unfair contract terms that contradict the compulsory provisions or unilateral compulsory provisions in favour of insureds or policyholders, will be unenforceable (*see Question 20*).

Standard policies or terms

22. What are the main standard policies or terms produced by trade associations or relevant authorities?

Some insurance companies disclose their policy conditions on their webpage.

The Non-Life Insurance Rating Organisation of Japan (*songai hoken ryoritsu santei kikou*) (NLIRO) has prepared samples of policy conditions of some types of non-life insurance, especially policy conditions relating to automobile liability insurance, which have been translated into English (*see page 93, www.nliro.or.jp/disclosure/pdf/eibunjibaihou201105.pdf*).

INSURANCE AND REINSURANCE POLICY CLAIMS

Establishing an insurance claim

23. What must be established to trigger a claim under an insurance policy?

Procedures for the payment of an insurance claim are generally stipulated in the policy conditions. A policyholder must usually notify their insurance company of the occurrence of an insured event without delay, otherwise the insurance company may (*Supreme Court decision, 20 February 1987, Minshu Vol.41, no.1 page 159*):

- Be indemnified for any damage that it incurs due to the delay.
- Deduct an amount equivalent to any loss caused by failure of this notice from insurance monies.

In addition, the policyholder must submit all the following to the insurance company when making an insurance claim:

- A written notice of claim.
- Documents to prove the loss covered by the insurance.
- All other documents the insurance company deems necessary.

According to litigation practice in Japan, if a policyholder files an action for an insurance claim, he must prove all the following facts:

- Existence of a valid insurance contract.
- Occurrence of an insurance event during the insurance period.
- Occurrence and quantum of loss.
- Causal relationship between the insured event occurred and the loss.

Third party insurance claims

24. What are the circumstances in which third parties can claim under an insurance policy?

If a third party is designated as the insured (in relation to non-life insurance) or the insurance beneficiary (with respect to life insurance or fixed benefit accident and health insurance), he can claim under the insurance policy.

In relation to third-party liability insurance, a victim who has a right to claim compensation for damage against an insured cannot exercise the right to make an insurance claim against the insurance company, unless the right of victims is stipulated in the policy conditions. However, a victim has a statutory lien (*sakidori tokken*) on the insured's claim for insurance against an insurance company (*Article 22, Insurance Act*). In addition, the victim may be able to exercise the right to make an insurance claim against the insurance company by subrogation (*Article 423, Civil Code*).

In relation to compulsory and voluntary automobile liability insurance, a victim can make a direct claim against an insurance company:

- For compulsory insurance under Article 16 of Automobile Liability Security Act.
- For voluntary insurance under the typical voluntary policy conditions.

In relation to nuclear energy liability insurance, a victim has a statutory lien on the insured's claim for insurance against an insurance company (*Article 9, Act on Compensation for Nuclear Damage*).

Time limits

25. Is there a time limit outside of which the insured/reinsured is barred from making a claim?

The statute of limitations for insurance claims expires after three years, and this is commonly stipulated in policy conditions (*Article 95, Insurance Act*). Provisions that aim to reduce these time limits in policy conditions are void.

Enforcement

26. Can the original policyholder or other third party enforce the reinsurance contract against a reinsurer?

In general, policyholders and other third parties have no right to make an insurance claim directly against the reinsurance company. However, it may be possible for a policyholder, or a third party who is a creditor of the insurance company, to exercise the right to make an insurance claim against the reinsurance company by way of subrogation under Article 423 of the Civil Code.

If an insurance company is subject to insolvency proceedings, it will be difficult to exercise a right against the reinsurance company under Article 423 of the Civil Code because the claims of policyholders and/or other third parties are handled collectively in these proceedings.

Remedies

27. What remedies are available for breach of an insurance policy?

Insurer

If insureds or policyholders breach the insurance contract, insurers can file an action for damages, specific performance, or an injunction, depending on the case.

In addition, the insurers can agree to resolve disputes by arbitration (*see Question 33*).

An insurance company is allowed to terminate an insurance contract when any of the following occur (*Articles 30, 57 and 86, Insurance Act*):

- A policyholder causes or will cause a loss with the intention of making the insurance company pay for the loss.

- A policyholder defrauds or will defraud the insurance company in an insurance claim.
- Any other event occurs involving a policyholder that violates the insurance company's trust and makes it difficult to continue the insurance agreement with him.

Insured

If insurers breach the insurance contract, insureds or policyholders can file an action for damages, specific performance, or an injunction, depending on the case. Insureds or policyholders can agree to resolve disputes by arbitration.

Punitive damage claims

28. Are punitive damages insurable? Can punitive damages be reinsured if they are covered by an underlying policy?

Punitive damages are not generally awarded by Japanese courts. The Supreme Court has refused to enforce foreign judgments awarding punitive damages due to their penal character and because they are contrary to public order in Japan (*Minshu Vol. 51, No. 6, page 2563, 11 July 1997*).

While there is no precedent to this effect, the Japanese courts may deny the coverage of punitive damage in both primary insurance and reinsurance agreements.

INSOLVENCY OF INSURANCE AND REINSURANCE PROVIDERS

29. What is the regulatory framework for dealing with distressed or insolvent insurance or reinsurance companies, or other persons or entities providing insurance or reinsurance related services? What regulatory and/or other protections exist for policyholders if the insurance company is insolvent?

Insurance/reinsurance companies

There are various kinds of insolvency proceedings for companies, such as:

- Liquidation procedures:
 - bankruptcy proceedings (*hasan tetsuzuki*);
 - special liquidation proceedings (*tokubetsu seisan tetsuzuki*).
- Restructuring procedures:
 - civil rehabilitation proceedings (*miji saisei tetsuzuki*);
 - company reorganisation proceedings (*kaisha kousei tetsuzuki*).

However, in the case of the failure of an insurance company (which is a Japanese company), special proceedings are provided, since there are many policyholders requiring protection. The administrative procedures for the insolvency of an insurance company are set out under the IBA. In such procedures, the conditions of insurance policies are amended to restructure the failed insurance company, with the approval of a shareholder's meeting and the government authority.



Additional proceedings for bankruptcy (*hasan*) and company reorganisation (*kaisha kousei*) are set out in the Act on Special Treatment of Corporate Reorganisation Proceedings and Other Insolvency Proceedings of Financial Institutions (*Act No. 95 of 1996*).

80% to 100% of the policy reserve of an insolvent insurance company, and any other reserve for the payment of insurance claims, are kept for the payment of insurance claims. Any shortfall below these percentages of the policy reserve is covered by the Insurance Policyholders Protection Corporation (*hoken keiyakusha hogo kikou*) (*IBA*).

No distinction is made between Japanese insurance companies and reinsurance companies that are licensed under the *IBA* or other regulations. However, the Insurance Policyholders Protection Corporation of Japan does not provide financial assistance in relation to reinsurance contracts.

Other persons or entities providing insurance/reinsurance-related services

There are no special proceedings established for providers of insurance or reinsurance-related activities.

30. Can excess insurance policies “drop down” to provide coverage if the primary insurer goes into insolvency?

This issue has not been considered by the Japanese courts and there are no regulations or proceedings relating to “drop down” of excess coverage. Therefore, excess coverage may “drop down” in the event of the insolvency of the underwriter of the underlying policy, depending on the language and interpretation of the particular “drop down” clause.

31. Is a right to set-off mutual debts and credits recognised in an insolvency proceeding involving an insurer or reinsurer?

A right to set-off mutual debts and credits is generally recognised in Japan if certain conditions are met (*Article 505, Civil Code*). These conditions include the satisfaction of both obligations that are due, even in insolvency proceedings involving an insurer or reinsurer.

Creditors can assert set-offs at any time during ongoing liquidation procedures (bankruptcy proceedings and special liquidation), unless a trustee of the bankrupt party makes a demand to the creditors for a definitive answer within a certain period regarding whether they will exercise the right to set-off.

In restructuring procedures (civil rehabilitation proceedings and corporate reorganisation proceedings) a creditor can assert set-offs on the condition that their intention to set-off is conveyed to a debtor (trustee) by the due date for filing a proof of claim.

In both liquidation and restructuring procedures, the exercise of set-off rights is not generally allowed if this would harm the equality of creditors. For example, where a creditor has assumed, or obtained from a third party, a debt to the insurer or reinsurer after the commencement of court procedures for insolvency.

TAXATION OF INSURANCE AND REINSURANCE PROVIDERS

32. What is the tax treatment for insurers, reinsurers, and other persons or entities providing insurance and reinsurance-related services?

Insurance/reinsurance companies

Under the Corporation Tax Act and any other related acts, Japanese companies are subject to around 40% corporate income tax (including corporate residence tax and corporate enterprise tax). This applies equally to Japanese insurance companies and reinsurance companies. However:

- In principle, the reserve for policy dividends, policy reserves (generally, except for risk reserves), and reserves for outstanding claims are treated as deductions for corporate income tax purposes, to the extent approved by the Japanese tax authority.
- In relation to corporate enterprise tax, a certain percentage of insurance premium revenue is the base of taxation.

No consumption or excise tax applies to insurance premiums in Japan.

Other persons or entities providing insurance/reinsurance-related services

Providers of insurance or reinsurance-related activities are subject to personal income tax or corporate income tax in the same way as other Japanese persons and companies.

INSURANCE AND REINSURANCE DISPUTE RESOLUTION

33. Are there special procedures or venues for dealing with insurance or reinsurance complaints or disputes?

In October 2010, the Financial Alternative Dispute Resolution (ADR) System under the *IBA* was introduced in Japan. Under the Financial ADR System, insurance companies and reinsurance companies are required to both:

- Conclude a contract with the designated institution for dispute resolution (*shitei hunsou kaiketsu kikan*) designated by the FSA.
- Comply with the procedure of the designated institution for dispute resolution to resolve insurance or reinsurance complaints or disputes arising from insurance business.

However, insurance companies and reinsurance companies are guaranteed the right of access to a court.

The Life Insurance Association of Japan (*seimei hoken kyokai*), the General Insurance Association of Japan (*nihon songai hoken kyokai*), the Insurance Ombudsman (*hoken onbuzuman*) and The Small Amount & Short Term Insurance Association of Japan (*nihon shougaku tanki hoken kyokai*) are the designated institutions for dispute resolution in insurance business.

MAIN INSURANCE/REINSURANCE TRADE ORGANISATIONS

Life Insurance Association (*seimei hoken kyokai*)

Main activities. The Life Insurance Association strives for the sound development and improvement of the life insurance industry.

W www.seiho.or.jp/english/index.html

General Insurance Association (*nihon songai hoken kyokai*)

Main activities. The General Insurance Association promotes the sound development of the non-life insurance industry in Japan.

W www.sonpo.or.jp/en/

Foreign Non-life Insurance Association (*gaikoku songai hoken kyokai*)

Main activities. The Foreign Non-life Insurance Association represents its members in various matters concerning non-life insurance business.

W www.fnlia.gr.jp/english/

Non-Life Insurance Rating Organisation (*songai hoken ryoritsu santei kikou*)

Main activities. Main activities include:

- Calculation and provision of Reference Loss Cost Rates and Standard Full Rates.
- Investigation of CALI claims.
- Maintenance of a data base.

W www.nliro.or.jp/english/index.html

In addition, there are some ADR forums for insurance complaints and disputes, such as the:

- Japan Centre for the Settlement of Traffic Accident Disputes (*koutsuu jiko hunsou shori center*).
- Automobile Liability Insurance and Mutual-aid Dispute-Settlement Mechanism (*jibaisekihoken kyosai hunsou shori kikou*).
- Dispute Resolution Committee (*hunsou kaiketsu iinkai*) established by the National Consumer Affairs Centre of Japan (*kokumin seikatsu center*).

There are no special methods used to resolve disputes regarding reinsurance. If a reinsurance company breaches a reinsurance contract, a cedant company can file an action for damages, specific performance, or an injunction, as the case may be.

34. Are arbitration clauses in insurance and reinsurance agreements enforceable?

Arbitration clauses in insurance and reinsurance agreements are enforceable in Japan. Although arbitration clauses are not commonly provided in insurance policies, reinsurance contracts often stipulate such clauses in relation to disputes between cedant companies and reinsurance companies.

35. Are choice of forum, venue and applicable law clauses in an insurance or reinsurance contract recognised and enforced?

Claims for insurance reimbursements against an insurance company must generally be filed in the jurisdiction of the debtor's residence, unless expressly provided in the insurance policy (*Article 5, Code of Civil Procedures of Japan (Act No. 109 of June*

26, 1996)). Insurance policies sometimes stipulate the choice of forum and venue as the headquarters of the insurance company or, simply, Japan. These arrangements are valid and enforceable in Japan, subject to the FSA approval/notification requirements in the policy conditions (*see Question 18, Form and content requirements*), provided that they are not prejudicial to consumers' interests under the Consumer Contract Act, which does not apply to commercial lines (including reinsurance contracts).

Choice of law is often stipulated in non-life insurance policies, and is also valid and enforceable in Japan, subject to the FSA approval/notification requirements in the policy conditions. If not, it is assumed that Japanese law applies to both life and non-life (except for marine) insurance contracts. A choice of foreign law may be void in insurance policies with consumers (*Consumer Contract Act*).

REFORM

36. What proposals are there for reform of the law, regulation or rules relating to the provision of insurance or reinsurance services?

The Working Group for Providing Insurance Products and Services, which is constituted under the Financial System Council (*kinnyuu shingikai*) of the FSA is now in discussions regarding appropriate regulations and their applicability in relation to (among other things):

- Restrictions on the business engaged in by insurance companies and their subsidiaries.
- Insurance benefits in kind.
- Rules regarding providing information during insurance solicitation.



- Rules regarding informational documents used for insurance solicitation.
- Rules regarding solicitation by intermediaries, and insurance agents who are undertaking solicitation activities on behalf of multiple insurance companies.
- Cases where solicitation regulations are applicable.

Some reforms were made to the IBA in March 2012, in response to the report by the Working Group for the Regulation of the Group Management of Insurance Companies, which include:

- Easing of the restrictions on the business engaged in by foreign subsidiaries of insurance companies that became subsidiaries on acquisition of foreign insurance companies, where approvals are obtained.
- Revision of the rules regarding the types of insurance contracts with regard to comprehensive transfers of insurance contracts and removal of the restrictions on solicitation during comprehensive transfer procedures.
- Loosening of the restrictions on consignment of insurance solicitation business to the extent that the consignments are made between those belonging to the same group of insurance companies.

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Recent transactions

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- Conversion of a Japan branch of a foreign insurer to a Japanese corporation.

Languages. Japanese, English

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