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Insurance & Reinsurance 2025

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Japan: Trends and Developments
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Trends and Developments

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Increase in Reinsurance Transactions in the Japanese Market

Background – introduction of economic value-based solvency regulations in Japan

Japan will introduce economic value-based solvency regulations in 2025. Under the new regulations, the economic value-based solvency ratio (ESR), as an indicator of the financial soundness of insurers, will be calculated by assessing the assets and liabilities of insurers on an economic value basis. The Japan Financial Services Agency (JFSA) has been preparing to align the implementation of the regulations in 2025 with the scheduled introduction of the Insurance Capital Standard (ICS) agreed by the International Association of Insurance Supervisors (IAIS). In October 2024, the JFSA announced proposed amendments to related laws and regulations. According to the JFSA, the amendments will be later amended along with the finalisation of the ICS, and the JFSA will officially announce those additional amendments in the summer of 2025.

Due to the introduction of economic value-based solvency regulations, many Japanese insurance companies, especially life insurance companies, are considering entering into new reinsurance agreements, which are sometimes called "block reinsurance" or "funded reinsurance", with reinsurers. ESR can be profoundly affected by fluctuations in interest rates especially when an insurer has existing blocks of insurance contracts with high long-term interest rates. One solution which insurance companies are considering to address the new regime is entering into such a reinsurance agreement.

Issues on offshore reinsurers in the Japanese market

Licensing requirements and considerations for offshore reinsurers

Under the Insurance Business Act of Japan (IBA), "insurance business" includes any business that receives insurance premiums in exchange for the agreement to compensate someone for damages caused by uncertain events. This definition is broad enough to capture reinsurance businesses. Generally, an insurance business must be licensed. The exception to this licensing requirement is a reinsurance transaction carried out "offshore" (ie, outside Japan) as it is exempted from regulations on overseas direct insurance. If a reinsurer operates a "(re)insurance business" on an "offshore" basis (ie, it carries out all underwriting, claims handling, contract negotiations and other activities from outside Japan and does not utilise its own employees or agents to conduct any such activities in Japan), then it is not required to obtain an insurance business licence under the IBA and, thus, is not subject to the supervision of the JFSA, any regulatory (including reporting) obligations or any capital requirements regardless of the amount of business it conducts with Japanese cedants.

However, cedants must pay attention to regulatory requirements for them to obtain credit for reinsurance on their financial statements. Licensed cedants (insurers) in Japan must hold policy reserves for the policies they have insured. However, there is an exemption for policies that have been reinsured, which exemption is available without limitation for reinsurance transactions concluded by licensed reinsurers in Japan. Foreign reinsurers without a licence in Japan may also invoke this exemption but only to the extent that the reinsurance would not impair the financial soundness of the cedants considering the foreign reinsurer's businesses and financial conditions. There is no bright-line test based on specific monetary thresholds or limits under the IBA; however, if, for example, the maximum reinsurance payment is less than 1% of the total assets of the cedant and there is no concern that the foreign reinsurer would fail to make the reinsurance payments due to insolvency or other reasons, then this exemption may be invoked according to the Supervisory Guidelines for Insurers published by the JFSA. Japanese insurance companies (cedants) may ask a foreign reinsurer for information, materials and other evidence regarding the foreign reinsurer's businesses and financial conditions from this perspective.

Insurance broker

Along with the increase in reinsurance transactions, an increasing number of companies have registered or are preparing to register as insurance brokers under the IBA. The IBA provides for two types of insurance intermediary (insurance solicitation) licences: (i) insurance broker (*hoken nakadachi-nin*) registration and (ii) insurance agent (*hoken dairi-ten*) registration. While insurance brokers act as intermediaries for the conclusion of insurance contracts on behalf of insurance policyholders (cedants in reinsurance transactions), insurance agents act on behalf of insurers (reinsurers in reinsurance transactions). Regarding these two intermediary licences, there are no overseas or reinsurance exemptions under the IBA, unlike the licensing requirement discussed above. In other words, those who act as intermediaries for the conclusion of (re) insurance contracts must obtain either licence, even if they act as intermediaries from abroad or for reinsurance. In addition, the insurance agent registration is in place only for insurance agents who act as intermediaries on behalf of Japanese licensed insurers and is not available to those who act on behalf of unlicensed reinsurers. Therefore, the only option for those who act as intermediaries for the conclusion of insurance contracts with unlicensed reinsurers is to obtain the insurance broker registration and to act on behalf of insurance policyholders (cedants in reinsurance transactions).

In light of the purpose of requiring insurance brokers to be independent from insurers and insurance agents, the Comprehensive Guidelines for the Supervision of Insurance Companies (the "Guidelines") provides the following focus points to ensure appropriate business operations by insurance brokers.

- Shared shops: generally, the office for insurance solicitation should not be in the same building as the office of an insurance company. However, if sufficient measures are taken to prevent confusion among customers, such as using separate exclusive areas from the building entrance to each office, this is not considered to be a problem.

- Investments: insurance brokers should not, in principle, receive capital investments from insurance companies.
- Benefits provision: insurance brokers should not accept loans from insurance companies on terms that are significantly favourable compared to normal terms, or request or accept favours such as the provision of money, goods or services, regardless of the name under which such favours are made.
- Personnel exchanges: insurance brokers should not accept the secondment of officers or employees of insurance companies as their officers or employees engaged in solicitation, and insurance companies should not second officers and employees to insurance brokers as their officers or employees engaged in the solicitation of insurance.

Moreover, insurance brokers must act in good faith as intermediaries to conclude insurance contracts on behalf of their insurance policyholder customers (cedants in reinsurance transactions). One of the most notable obligations under the Guidelines is that: “in the performance of its duties and in the selection of an insurance company, an insurance broker should take into consideration the customer’s purpose and assets, and should advise the customer of the insurance products that the insurance broker knows are most appropriate for the customer, clearly indicating the reasons for such recommendations.”

Expected Amendments to the Insurance Business Act

Background – fraudulent insurance claims by large insurance agents and price cartel by major non-life insurers

In 2023, two major incidents shook the non-life insurance industry in Japan.

One incident involved an insurance fraud committed by a large insurance agent which was also a major used car sales dealer. According to news reports, the agent deliberately damaged vehicles that customers had brought in for repair and charged non-life insurance companies an inflated amount for the repair. Analysts contend that insurance companies did not provide appropriate education, monitoring or guidance to some large insurance agents because the agents brought huge profits to the insurance companies and the insurance companies were concerned about the negative impact on their business that may result from a deterioration in relations with those insurance agents.

The other incident involved a price cartel of major non-life insurers. In the process of arranging coinsurance, major non-life insurance companies were widely engaged in activities that may have violated antitrust regulations, such as making preliminary adjustments to insurance premiums before bidding. Cartel behaviour arose because of insufficient knowledge of antitrust regulations among non-life insurance companies and insurance agencies, and the strong pressure on non-life insurance company sales representatives due to rising fire insurance premium. Another contributing cause was the fact that the lead insurer and the allotment of coinsurance shares were decided by factors other than insurance, such as cross-shareholdings and favours to insurance agents.

In reaction to the foregoing scandals, from May to June 2024, the JFSA set up an expert panel that analysed the causes of the incidents and considered preventive regulatory and supervisory measures. Following the report of the expert panel and voluntary efforts of the non-life insurance industry, the JFSA set up a working group in September 2024 to discuss possible amendments to the IBA.

Overview of the report provided by the working group

In December 2024, the aforementioned working group released its report which includes proposals to amend the IBA and reform vicious practices in the Japanese insurance market. Provided below is an overview of the report. The IBA is expected to be revised next year in line with the contents of the report.

Enhancement of "Principles for Customer-Oriented Business Conduct"

- Strengthening regulation of large insurance agents: the report proposes to strengthen the regulation of large insurance agents, especially those who concurrently operate businesses that profit from receiving payments for repairs and other expenses from insurance claims, such as the automobile repair business. Such insurance agents which are also involved in the insurance claims business have an incentive to make fraudulent claims, for example for repair costs, in order to benefit themselves. This became apparent in the major used car sales dealer case. Specifically, the report intends to require the establishment of a system to manage conflicts of interest for insurance agents.
- Tightening regulation of insurance sales practices: under the current IBA, when insurance companies, insurance agents and insurance brokers recommend an insurance product in comparison to other insurance products, they are required to explain the reasons for their recommendation. The report suggests tightening this regulation by imposing an obligation to consider customers' intention and interest in the recommendation.
- Ensuring the effectiveness of monitoring systems of insurance companies: one factor thought to have given rise to the fraudulent insurance claim case is the insufficient provision of education, monitoring or guidance by insurance companies to large insurance agents, for the reasons discussed in the section entitled "Background – fraudulent insurance claims by large insurance agents and price cartel by major non-life insurers". In view of this, the report suggests that insurance companies should ensure the implementation of an effective system to monitor insurance agents.

Creating a sound competitive environment in the Japanese insurance market

- Promoting the use of insurance brokers: see details in the section headed "Expected revisions relating to insurance brokers".
- Prohibition of giving excessive benefits to policyholders by insurance companies: when the working group scrutinised insurance industry practices, it quickly saw the practice of insurance companies providing "benefits" to policyholders, typically by purchasing goods and services from, or providing services (such as secondment of personnel) to, the policyholders and their group companies, and noted that this practice has a significant impact on the decision-making of policyholders. The report therefore suggests prohibiting insurance companies from providing excessive benefits to policyholders.
- Restructuring of regulations for in-house insurance agents: in the Japanese insurance

market, there are so-called in-house insurance agents who mainly handle insurance policies for their group companies and the latter's employees. The report points out that the number of policies handled by in-house insurance agents is huge, resulting in a less competitive environment in the commercial lines insurance market; thus, the regulations on in-house insurance agents should be restructured.

- Improving the deficit structure of fire insurance in the Japanese insurance market: in recent years, large-scale natural disasters such as typhoons and floods are becoming more frequent, leading to the insurance companies' deficit in fire insurance that covers corporate damages caused by such disasters. The report points out that this situation may be a cause of the recent major non-life insurers price cartel, and suggests that the JFSA enhance the monitoring of commercial lines and facilitate the entry of small- and medium-size insurance companies into this market.

Expected revisions relating to insurance brokers

From the perspective of creating a sound competitive environment in the Japanese insurance market, the report stresses the importance of promoting the use of insurance brokers. The insurance broker system was introduced in Japan in 1995, but the share of insurance premiums handled by insurance brokers in Japan had been sluggish (0.9% of the total share in 2023). The report suggests revising the current regulation as follows.

Revision of the method for receiving brokerage fees

Under the current Supervisory Guidelines for Insurers published by the JFSA, insurance brokers are not allowed to charge brokerage fees to customers but must instead charge brokerage fees to insurance companies. The report proposes allowing insurance brokers to charge customers for a portion or all of the brokerage fees in the commercial lines insurance market, and to require insurance brokers to explain to customers in advance whether (i) they will receive the full commission from the insurance company, (ii) the full commission from the customer, or (iii) a portion of the commission from both the customer and the insurance company.

Revision of security deposit

Insurance brokers must make a minimum deposit of JPY20 million at the "deposit office" nearest to their principal office. Although the purpose of the security deposit is to ensure that insurance brokers have the financial resources to compensate for damages, it may be an obstacle to registration as an insurance broker. In view of this, the report suggests that the minimum deposit be reduced to JPY10 million.

Joint insurance solicitation with insurance agents

Under the current Supervisory Guidelines for Insurers published by the JFSA, insurance brokers are not allowed to engage in joint insurance solicitation with insurance agents for the same insurance policy. When insurance is jointly arranged for projects funded by multiple companies, insurance agents related to the companies that have invested in the project often participate. However, insurance brokers are not allowed to participate as it would be considered a joint insurance solicitation with the insurance agents, which is prohibited under the above Guidelines. The report proposes to eliminate this regulation and for the insurance parties to give prior explanation to customers and to implement measures to prevent misidentification.

Utilising insurance brokers for overseas direct insurance

Under the IBA, if a person seeks to apply, with a foreign insurer without a branch in Japan, for an insurance contract relating to persons with an address or residence in Japan, or to property located in Japan, or to vessels or aircraft with Japanese nationality, the person must obtain approval from the JFSA prior to the application. The report proposes to allow insurance brokers to conduct research on matters that would be required for approval and to engage in insurance solicitation for such insurance contract for the purpose of enhancing the use of insurance brokers.

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