BERMUDA MONETARY AUTHORITY

CONSULTATION PAPER

REPEAL OF SECTION 57(1)(A) OF THE INSURANCE ACT 1978

JUNE 2014

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The views of the insurance industry and of other interested persons on the proposals set out in this paper are invited. Comments should be sent to the Authority, addressed to policy@bma.bm no later than 30th July, 2014.

I. INTRODUCTION

1. The Bermuda Monetary Authority ("the Authority") is proposing to amend the Insurance Act 1978 ("the Act") by repealing Section 57(1)(a). The repeal seeks to bring insurance business conducted by a registered friendly society or trade union for their members within the insurance legislative framework.

2. Presently Section 57(1)(a) states that "insurance business carried on by a friendly society registered under the Friendly Societies Act 1868 or by a trade union registered under the Trade Union Act 1965, being business in which risks of members of the friendly society or trade union, as the case may be, are insured "*shall be deemed* ***not*** *to be* ***insurance business*** *within the meaning of this Act.*" Consequently, insurance business conducted by these entities falls outside the Authority's regulatory and supervisory remit and is therefore not subject to the same prudential requirements as other providers of the same services.

3. The proposed amendment would entail the removal of this subsection which would result in insurance business carried on by a registered friendly society or a registered trade union would be under the Authority's regulatory and supervisory oversight.

4. Although in some jurisdictions friendly societies have evolved and have become incorporated into the financial or health system, in other countries friendly societies have taken on a more charitable or social role which has largely been the case in Bermuda. While early trade unions offered a similar range of benefits to insure employees against unemployment, ill health, old age and funeral expenses, in most countries they did not continue in insurance business. The primary role of trade unions today, both in Bermuda and around the world, is to work towards and achieve goals such as better working conditions, pay, and employment benefits.

5. While the Authority is mindful of the historical value of the insurance services that these kinds of mutual organisations provided in the past to their respective communities, the Authority is of the view that appropriate supervisory oversight would be in the best interests of policyholders, beneficiaries and claimants. This position is consistent with the goals of the International Association of Insurance Supervisors (IAIS), the international standard setting body responsible for developing principles and standards for the supervision of the insurance sector.

6. The IAIS principles and standards for the supervision of the insurance sector are articulated in the "Insurance Core Principles, Standards, Guidance and Assessment Methodology" of October 2011 (ICPs). ICPs are applicable to supervisors/regulators of insurance companies and are considered fundamental for the effective supervision of insurers. ICPs seek to foster convergence towards a globally consistent supervisory framework. Most importantly, ICPs set principles and standards for the supervision of all key aspects of insurance, regardless of the type of provider, product, or services provided. The ICPs cover all key areas of insurance supervision, including solvency, risk management, governance and transparency of insurers.

II. BACKGROUND

7. Both friendly societies and trade unions have their origins in the UK and Europe during the industrial revolution of the 18th and 19th centuries as mutual or self-help organisations. The general concept is that the memberships banded together to work towards and achieve common goals such as better working conditions, pay, employment benefits and insurance. Every member contributed to a fund to be used for the welfare of the members or their families for assistance in times of need or distress. While there were many different types of mutual aid organisations, friendly societies were among the most popular due in part to the efficient manner in which they were run. Friendly societies and early trade unions offered a range of benefits to insure members against unemployment, ill health, old age and funeral expenses.

8. Initially the British government supported the friendly society movement as evidenced by the 1793 Friendly Society Act[1].

9. From their British origins friendly societies spread to other countries in the Commonwealth including Bermuda, Isle of Man, Scotland, Australia and New Zealand where they are said to have reached their peak in the 1930s. Following this period, greater government and commercial sector involvement in the provision of insurance prompted the review of the roles of friendly societies in this sector. (See for example, the changes introduced in the UK to the Friendly Society Act in 1974 and 1992).

10. At present, in the UK some friendly societies now specialise in savings and investments, and tax-exempt savings plans that provide tax-free savings. Some focus on insurance products such as income protection while others cover savings and investments protection. Additionally, an information bulletin from the UK HM Revenue and Customs[2] identifies three categories of friendly society: unregistered, registered, and incorporated friendly societies.

11. The functions that can be undertaken by a registered friendly society are limited to the provision of specified provident benefits for their members and their dependents including most forms of life insurance, annuity, unemployment and health insurance contracts[3]. They are registered as mutual societies and receive oversight from the Financial Conduct Authority. The Financial Conduct Authority (FCA) is one of the UK's two financial regulators, together with the Prudential Regulation Authority (PRA). The FCA aims to make financial markets work well. The FCA does this by protecting

[1] *A History of Friendly Society Law in the British Islands ,* available from: http://www.isle-of-man.com/manxnotebook/fulltext/rh1911/p379.htm

[2] Bank of England, Prudential Regulation Authority, bulletin CTM40310 - Particular bodies: friendly societies: meaning of : http://www.hmrc.gov.uk/manuals/ctmanual/ctm40310.htm

[3] Bank of England, PRA, and FCA. SU(n) Application for Authorisation Supplement, Release 1, April 2013 (Friendly Society)

consumers, promoting effective competition and enhancing the integrity of the UK financial system.

12. An incorporated friendly society can undertake all of the same activities of a registered society and can also set up subsidiary companies, and are subject to prudential oversight by the Prudential Regulatory Authority ("PRA"). They must receive permission to conduct regulated activities from both PRA and the Financial Conduct Authority ("FCA"), and may only be authorised to write Long-Term insurance business or general insurance business classes 'accident', 'sickness' and 'miscellaneous financial loss', with some supplementary general insurance business[4].

13. Similarly, in Australia friendly societies are regulated under the Life Insurance Act 1995 and are permitted to offer annuities and conduct certain types of life insurance business[5]. Additionally, the National Uniform Regulation of Friendly Societies and the Friendly Societies (Queensland) Bill 1997 was an effort to harmonise the regulation of friendly societies throughout Australia and to integrate them into the existing Financial Institution Scheme (FI Scheme) which already regulated other mutual organisations such as building societies and credit unions[6]. This bill prompted additional changes to the Friendly Societies Code for the express purpose to:

- register, supervise and regulate friendly societies: s 22(a)[7]
- supervise and enforce compliance by friendly societies with the Friendly Societies Code and prudential standards: s 22(b)
- ensure that an effective and efficient system of prudential supervision is applied to friendly societies: s 22(c), and
- protect the interests of members of friendly societies: s 22(d).

14. These jurisdictions, among others, have brought insurance business conducted by friendly societies and trade unions under regulatory oversight which is in keeping with the objectives stated in the ICPs. Bermuda also adheres to the tenets of the ICPs with the overall objective of promoting a stable insurance market and protecting policyholders; as such, the development of the insurance industry in Bermuda warrants that insurance business fall under the regulatory scope provided by the Act.

III. PROPOSAL

15. Although the role of friendly societies in Bermuda is as noted above primarily for charitable and social purposes, the Insurance Act 1978 Section 57(1)(a) provides them with an exemption from regulatory oversight by the Authority for insurance services that

[4] FCA website; www.hmrc.gov.uk/manuals/ctmanual/ctm40310.htm
[5] Section 11(3)(a) of the Commonwealth Life Insurance Act 1995.
[6] Friendly Societies (Queensland) Bill 1997, explanatory notes, p1.
[7] Friendly Societies (Victoria) Code and Regulations 1996.

they provide to their members. Similar to the approach taken in other jurisdictions the Authority believes that insurance business conducted by these entities should be, as in other jurisdictions, subject to appropriate prudential regulation and supervision. Therefore, the Authority proposes that Section 57(1)(a) of the Act be repealed.

16. This repeal would not impair the ability of a registered friendly society or trade union to offer insurance services to its members. Rather, the Authority is of the view that all entities that provide domestic insurance business in the jurisdiction should receive an appropriate level of supervision and regulation. Accordingly, this repeal would mean that insurance business conducted by a registered friendly society or trade union would be subject to the same level of prudential supervision as other providers of the same services.

17. The Authority further proposes a transition period of ninety days from the date of the repeal of Section 57(1)(a) for any registered friendly society or trade union that is writing insurance business to become compliant with its obligations under the Insurance Act 1978.

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