Upcoming Regulations for Investors in Insurance Companies

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In China, amidst fierce competition amongst insurance companies, more and more investors, both domestic and foreign, are striving to enter this market. Relevant regulations concerning investment limits and the qualifications for shareholders to invest in Chinese insurance companies are a continuing focal point for potential investors.

On December 29, 2016, the Administrative Measures for Equities of Insurance Companies (Draft for Comments) (the "Draft") was publicly released by the China Insurance Regulatory Commission (CIRC). Once the final content of the Draft is passed and officially enforced in the near future, two existing relevant regulations in this area will be affected.One is the Notice of the China Insurance Regulatory Commission on Issues Relating to Article Four of the Administrative Measures for Equities of Insurance Companies (the "Notice") announced by CIRC on April 9, 2013, and the other is the Administrative Measures for Equities of Insurance Companies (2014 Revised) (hereinafter the "Measures") enacted by CIRC on June 1, 2014.

Under these circumstances, it is pertinent to analyze the new draft provisions as they currently stand. This article will primarily focus on some of the major changes brought about by the Draft, as follows:

I. The Draft adds a new criterion dividing the shareholders of insurance companies into threenew different categoriesaccording to their shareholding percentages, qualifying conditions and their impact on the business operationsand management of insurance companies; those categories being Financial Shareholders, Strategic Shareholders and Controlling Shareholders.

Financial Shareholders are those shareholders holding less than 10% of the equity of an insurance company, and do not have any significant impact on the business operations and managementof the insurance company; Strategic Shareholders are those shareholders holding at least 10%, but less than 20%of the equity of an insurance company, or those who hold less than 10% but whose holding is sufficient to exert amaterial impact on the business operations and management of the insurance company; and Controlling Shareholders are those who hold at least 20% of the equity of an insurance company and alsohave a controlling influence on the business operations and management of the insurance company, or those who hold less than 20% but could still have a controlling influence on the business operations and management of the insurance company.

II. With regard to the qualification of shareholders, the Draft specifies that those investors who satisfy the relevant provisions prescribed therein, which could include corporations, limited partnership enterprises, public institutions, social groups and overseas financial institutions,may become shareholders of an insurance company. However, limited partnership enterprises, public institutions and social groups are limited to becoming Financial Shareholders of an insurance company only. Referring to natural persons, the Draft also holds that by purchasing shares in a publicly listed insurance company on the stock market in China, a natural person can (to the extent that they can access the relevant Chinese stock market) become a Financial Shareholder of that listed insurance company.

III. For investors applying to become one of the aforementioned three different types of shareholder in Chinese insurance companies, the Draft sets specific requirements for qualification. Accordingly, investor applicants must meet a set of specific requirements that differ according to their classification.

a) To apply as a Financial Shareholder, a good financial status and be profitable for the past fiscal year are requisite. It is also necessary to provide records of regular tax payments with no tax violations for the last three years. Besides this, further standards for qualification include records showing a favorable recent credit history, no record of dishonest behavior or grave violations of laws and regulations over the past three years, and a good compliance standing ,together with any other requirements that may apply under the laws, administrative regulations and provisions of CIRC.

b) In the event that an investor is preparing to apply as a Strategic Shareholder, in addition to the requirements listed under a) above, the applicant should have an outstanding core business, and sound record of investment activity; occupy a leading position in the industry with a good reputation; have a strong ability to make capital contributions on an ongoing basis, and have been profitable for the past three fiscal years consecutively; have a strong balance sheet with net assets of no less than RMB200 million together with positive retained earnings; and have a balance of long-term equity investments (including current investment projects) that do not exceed net assets (according to consolidated financial statements),together with any other requirements that may apply under the laws, administrative regulations and provisions of CIRC.

c) To apply as a Controlling Shareholder, in addition to the requirements listed under a) and b) above, the applicant should have total assets of not less than RMB10 billion by the end of preceding year; net assets forming 30% or more of its total assets; and an asset-liability ratio or financial leverage ratio that is not significantly higher than the average level in the industry, together with any other requirements that may apply under the laws, administrative regulations and the provisions of CIRC.

Furthermore, the Draft also specifies some particular requirements for the different types of investors on the basis of their own conditions.

IV. The Draft notes the following different means for investors to acquire equity: by initiating the establishment of an insurance company as a promoter; by entering into an agreement to subscribe for shares issued by an insurance company; by reaching an equity transfer agreement to be assigned equity from existing shareholders as a transferee;by public tender if the existing shareholders hold an open auction for shares; by purchasing the shares of listed insurance companies on Chinese stock market; by purchasingconvertible bondsthat can be converted into equity once the conditions as agreed in the relevant contracts are satisfied; through realization of a right to pledged shares by complying with relevant provisions as the pledgee; by participating in a risk-based disposal plan arranged by CIRC, and any other methods approved and admitted by CIRC.

V. The Draftemphasizes that the shareholding ratio of any single shareholder is to be limited to 1/3 of the generalcapital of an insurance company; and that the shareholding ratio of any single limited partnership enterprise is to be limited to 5% of the general capital,(with the total shareholding ratios of all limited partnership enterprises simultaneously holding shares in an insurance company being restricted to 15%). However, restrictions on shareholding ratios should not apply under two circumstances; a) where an insurance company invests in the establishment of another insurance company due to a need for business innovation, specialization or group-style business operations, provided that the equities held by the former in the latter shall exceed 50% within five years; and b) where following CIRC's approval, an investor obtains equity through participation in risk-based disposal measures taken against an insurance company.

When calculating shareholding ratios for this purpose, the shareholding ratios of shareholders affiliated with one another shall be combined.

VI. The same investor may only be the Controlling Shareholder of ONE insurance company amongst insurance companies that engage in the same type of business, except under special circumstances such as participating in a risk-based disposal plan, and so forth, following CIRC's special approval. Similarly, the same investor is prohibited from becoming a Strategic Shareholder in more than two (two is allowed) insurance companies at the same time. An investor applying as a Financial Shareholderis however unrestricted in the number of insurance companies it may invest in.

VII. The Draft expressly prohibits the acquisition of equity in an insurance company through the use of funds obtained, either directly or indirectly, as follows:

a) Borrowingsrelated toan insurance company;

b) Funds obtained againstthe pledges of the deposits or other assets of aninsurance company;

c) Relevant funds obtained through the investment trust schemes, private equity funds, equity investment etc. of an insurance company;

d) Funds obtained owing to the improper use of financial influence by an insurance company, or by virtue of an illegitimate affiliation with an insurance company.

VIII. Trust companies, fund companies, financial companies and other institutions may invest in insurance companies with trust funds or funds under entrusted management, but may only become Financial Shareholders, and shall be requested to progressively disclose, level by level, the following information: the holders of the relevant trust schemes or funds under entrusted management; and any affiliations with the insurance company and other investors of the insurance company.

IX. A Controlling Shareholder shall not transfer any equity held within three years from the date of establishment of the insurance company, but for Strategic Shareholders and Financial Shareholders, the restriction period is limited to two years and one year respectively.

The Draft makes fundamental changes to the existing regulatory framework, and observers may look forward to seeing its positive influence on the Chinese insurance market.