

BRIEFING

LIBERALISATION OF THE INSURANCE  
SECTOR IN THAILAND –  
TWO STEPS FORWARD?  
NOVEMBER 2016

SINCE FEBRUARY 2016, RESTRICTIONS HAVE BEEN LIFTED ON FOREIGN INVESTMENT IN THE THAI INSURANCE SECTOR. HAS TRUE LIBERALISATION ON FOREIGN INVESTMENT BEEN ACHIEVED?



Until earlier this year, foreign investment in the Thai insurance sector faced very high barriers to entry and restrictions on real and effective control. Changes which came into effect on 19 February 2016 have removed restrictions on foreign investment. After nine months in effect, do these changes represent real liberalisation of foreign investment in the Thai insurance sector or do they represent only progress towards real liberalisation?

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“THIS CHANGE IS ALSO KEY TO AN OVERALL STRATEGY TO REDUCE EXCESSIVE LEGISLATION AND REGULATION IN THE INSURANCE SECTOR...”

#### What has changed?

The changes remove the requirement for foreign investors, seeking 50% or more of an insurer's shares, to obtain a foreign business licence (“FBL”) from the Thai Ministry of Commerce (“MOC”) as a first step to investment by removing life and non-life insurance (“Insurance Businesses”) from the list of restricted businesses which require an FBL. These restrictions were to protect businesses considered unable to compete with foreign counterparts and with Thai competitors with majority foreign ownership.

#### Why has this been done?

These changes appear to have been prompted, at least in part, by liberalisation of market access for financial services, including insurance, as part of the ASEAN Economic Community (“AEC”) objectives.

This change is also key to an overall strategy to reduce excessive legislation and regulation in the insurance sector and to promote foreign investment in the Thai insurance sector.

Critically, this also reflects recognition that the Thai insurance sector can be adequately regulated by the Office of the Insurance Commission (“OIC”).

#### The OIC – gatekeeper or welcoming committee?

The changes have been made to the Foreign Business Act 1999 but not to the Life Insurance Act 1992 and the Non-life Insurance Act 1992 (“the Insurance Acts”) and their operation and requirements. The Insurance Acts contain a number of restrictions governing foreign investment and the control which foreigners can exercise over a Thai insurer, whether as shareholders or directors.

These restrictions remain in force and, in the absence of changes to the Insurance Acts, the OIC will continue to apply these requirements to foreign investment.

#### Foreign shareholding limits

Foreign investors can acquire less than 25% of the total voting shares without regulatory approval by the OIC.

#### Foreign shareholding up to 49%

The OIC has authority to approve foreign investment of between 25% and 49% of total voting shares and where the target Thai insurer has:

- a capital adequacy ratio which meets the OIC’s specifications; or
- a business plan which demonstrates to the OIC how the management of the business will be improved to increase efficiency and the competitiveness of the Thai insurer.

It is not unreasonable or uncommon for investors in Thai insurers, particularly where they seek more than 25% of the total voting shares, to seek a corresponding share of the seats on the Board of Directors. Where more than 25% of the Board comprises foreigners, OIC approval must be obtained. The maximum permitted foreign representation on a board is less than 50%.

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**“THE REQUIREMENT FOR OIC APPROVAL AND THE LIMITS ON BOARD REPRESENTATION REMAIN IN FORCE.”**

The requirement for OIC approval and the limits on Board representation remain in force.

While feasible, obtaining approval from the OIC is not straightforward and represents another barrier to foreign investment in the Thai insurance sector. Given the value of such investments, this restriction on Board representation raises the risk profile of investments in the Thai insurance sector and serves as a distinct disincentive to foreign investment.

OIC regulations to ensure that Board representation is commensurate with levels of investment may serve to protect the interests of minority shareholders. This should be balanced with a more liberalised approach to Board representation, particularly where the investor is a foreign insurer or reinsurer, already subject to prudential supervision in their home jurisdiction.

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“THE BENEFITS OF FOREIGN INVESTMENT TO THAILAND AND THE THAI INSURANCE SECTOR ARE LIKELY TO CONTINUE TO PLAY A CRITICAL ROLE IN OIC ASSESSMENTS OF FOREIGN INVESTMENT APPLICATIONS.”

#### Case study: German investment

An acquisition earlier this year provides a helpful example of a company that successfully obtained OIC approval to exceed the 25% threshold.

ERGO Group, entered the Thai insurance market by acquiring a 40.26% stake in Thaisri Insurance Public Company Ltd (“Thaisri”).

The OIC approved this investment and for ERGO to be able to appoint more than 25% of the directors on the Board.

Although details of the transaction remain confidential, it appears that the OIC accepted that the investment would allow Thaisri access to a greater range of insurance lines and products and the technical expertise of ERGO. The OIC is likely to have viewed this as a benefit for the Thai insurance sector as it would improve the products and lines available to businesses and consumers and the level of technical expertise in Thailand. The benefits of foreign investment to Thailand and the Thai insurance sector are likely to continue to play a critical role in OIC assessments of foreign investment applications.

#### Foreign shareholding exceeding 49% for non-life insurance companies

The Ministry of Finance (“MOF”), rather than the OIC, has authority to approve investments above 49% and can, in certain circumstances, allow foreign investors to acquire more than 49% of the total voting shares and/or have foreigners appointed to more than half of the total number of director positions.

This level of approval is typically granted reluctantly and only in circumstances where no other realistic alternatives appear to be available to the insurer ceasing business or where there are significant risks to its continued operations, including where:

- the insurer has been ordered by the OIC to rectify its status or business operations, increase or decrease its capital or to stop issuing non-life insurance policies; or
- there is an adverse event which requires the company to increase its loss reserves to a level which has a material effect on the company’s capital adequacy ratio.

It is important to bear in mind that approval for this level of foreign investment is often considered the solution of last resort. It is unlikely to be approved where the insurer can be acquired by another Thai insurer or Thai company or where existing shareholders are able to provide further capital.

Foreign investors should anticipate thorough and extensive scrutiny of their plans, structure and source of the funds for this investment.

The OIC is also in the process of finalising similar rules for life insurance companies.

### Case study: French and Japanese investments

Approval to exceed the 49% threshold was given to AXA Insurance PCL ("AXA"), Sampo Insurance (Thailand) PCL ("Sampo") and Tokio Marine Insurance (Thailand) PCL ("Tokio Marine") to acquire almost all the shares in their Thai subsidiaries. The Thai subsidiaries were faced with significant claims arising out of their exposure to 2011 Thai flood claims, raising concerns about their capital adequacy.

The MOF approved an increase in the shareholding of the AXA Group to 86% of AXA and this was eventually increased to 99.31%. The Japanese parent companies of Sampo and Tokio Marine have similarly obtained approval to increase their stakes in their Thai operations to 99.99% and 99.84% respectively.

The inability or reluctance of existing shareholders to invest further, combined with the risk to the continued financial viability of these three Thai insurers prompted the MOF to approve these investments. The approval may have been prompted more by concerns of the impact on personal and corporate insureds and the number of people directly and indirectly employed by these insurers if they were unable to continue to operate.

Approval for these investments should be viewed as exceptional rather than typical. It is also important to note that the majority owners were the parent companies of the Thai insurers and it remains to be seen whether the OIC would have approved such investments if the foreign shareholder was an unrelated entity.

Nevertheless, distressed Thai insurers may present attractive investment opportunities for certain types of foreign investors.

### Other considerations for foreign investors

Some foreign investors take a broader and longer-term view of the opportunities in the Thai insurance market and are prepared to forgo Board and management representation commensurate to their investment.

However, in many cases, this is not possible and foreign investors are deterred by their inability to ensure commensurate Board representation to protect their investment and to make changes in the structure and management of the target Thai insurer to increase competitiveness, efficiency and technical expertise.

Key issues for foreign investors include:

- the level of Board representation;
- the extent to which the foreign investors can influence the decisions of the Board and management of the insurer;
- the likely position of the OIC on approving the investment and level of Board representation;
- the role and influence of other shareholders;
- the extent to which the foreign investor can implement changes to increase competitiveness, efficiency, technical expertise and improve distribution costs and networks;

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“...FURTHER  
LIBERALISATION OF  
FOREIGN INVESTMENT  
APPEARS LIKELY.”

- whether the acquisition will enable the Thai insurer to access more flexible and cost-efficient reinsurance;
- whether the acquisition will enable the Thai insurer to offer a greater range of lines and products at more competitive price levels;
- the level of risk exposure, particularly to large, complex and long-tail claims.

#### What next for the Thai insurance market?

The OIC is continuing to review the Insurance Acts and considering various proposals to amend them. From our understanding of the proposed and long-awaited changes, further liberalisation of foreign investment appears likely.

The amendments to the Insurance Acts have yet to be finalised by the OIC, but the awaited changes are understood to be likely to reduce barriers to foreign participation. It is anticipated that investments up to 49% of total voting shares and up to 49% of Board seats may no longer require OIC approval. A key issue to monitor is the total permitted foreign shareholding by a single shareholder in the total share capital of a target Thai insurer and whether investment beyond a determined percentage may be subject to OIC approval.

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“THAILAND FACES A  
CHOICE BETWEEN  
PROTECTING ITS  
INSURANCE SECTOR  
AND THE NEED FOR ITS  
INSURERS TO REMAIN  
COMPETITIVE WITH RIVAL  
ASEAN INSURERS.”

In view of the steps to liberalise access to the financial sector in ASEAN member states, a significant issue is whether the changes to the Foreign Business Act and the anticipated changes to the Insurance Acts will result in a more competitive and stronger Thai insurance market, able to both expand into other ASEAN markets and to compete with ASEAN rivals eventually entering the Thai market. If ASEAN rivals are able to achieve economies of scale and expand regionally in a market of 600 million consumers before Thai insurers do so, the latter may be at a competitive disadvantage.

Thailand faces a choice between protecting its insurance sector and the need for its insurers to remain competitive with rival ASEAN insurers.

For foreign investors, in the absence of further liberalisation, the issue would then be whether there are sufficient benefits in the domestic Thai insurance market to invest in a Thai insurer. Recent transactions suggest that some foreign investors see such benefits.

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## FOR MORE INFORMATION

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Should you like to discuss any of the matters raised in this Briefing, please speak with a member of our team below or your regular contact at Watson Farley & Williams.



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