

## Financial Sector Regulation Act, 2017

### Joint Guidance Notice 1 of 2021

### Insurance Act, 2017

## GUIDANCE NOTICE ON THE APPLICATION OF SECTION 5 OF THE INSURANCE ACT, 2017 (ACT NO. 18 OF 2017) IN RESPECT OF FOREIGN ENTITIES INSURING FIRST PARTY RISKS.

### 1. Application

This joint guidance notice has general application and is issued under section 141 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (FSRA) and must be read with Joint Guidance Notice 1 of 2019 - Guidance on the application of section 5 of the Insurance Act, 2017 (Joint Guidance Notice 1 of 2019).

### 2. Purpose of the Guidance Notice

The purpose of this joint guidance notice is to –

- 2.1 provide guidance on the application of section 5(1) read with section 5(2) of the Insurance Act, 2017 (the Act), read together further with Joint Guidance Notice 1 of 2019, in the context of foreign entities<sup>1</sup> insuring “first party risks” in the Republic; and
- 2.2 confirm the view of the Prudential Authority (PA) and Financial Sector Conduct Authority (FSCA), that unless a person is licensed as a captive insurer under the Act that person may not conclude insurance business in relation to “first party risks” in South Africa.

### 3. Joint Guidance Notice 1 of 2019

- 3.1 On 17 April 2019, the PA and the FSCA issued Joint Guidance Notice 1 of 2019. Joint Guidance Notice 1 of 2019 provided clarity on the application of section 5 of the Act and set broad parameters in the determination of whether a foreign re/insurer was conducting “insurance business” as defined in the Act, in the Republic. These parameters included:
  - 3.1.1 A foreign re/insurer soliciting insurance business from a South African based customer is acting directly in the Republic and is to be regarded as conducting insurance business in terms of section 5(2)(b) of the Act. A South African based customer that seeks and secures re/insurance with a foreign re/insurer

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<sup>1</sup> For purposes of this Joint Guidance Notice “foreign entities” means a person established or domiciled outside of the Republic.

of its own accord directly will not result in the re/insurer “being regarded as conducting insurance business” as defined in the Republic.

- 3.1.2 A foreign re/insurer acting through (by means of appointment, instruction, or influence) an intermediary, where such intermediary places the insurance business of a South African based customer with the foreign re/insurer, is “regarded as conducting insurance business” in terms of section 5(2)(b) of the Act. The foreign re/insurer is regarded to have acted indirectly through the intermediary if the foreign re/insurer appointed, instructed, or influenced the intermediary to place the insurance business of a South African customer with the foreign re/insurer.
- 3.2 Joint Guidance Notice 1 of 2019 did not explicitly mention captive insurers domiciled and licensed in a foreign jurisdiction. However, it is critical to note that section 5 of the Act applies to a “person” as defined in the Act and the meaning of “person” cross-references to the FSRA definition of “person,” which includes both natural persons and “juristic persons” as defined. Juristic persons, as per the FSRA, includes a company, close corporation or co-operative incorporated or registered in terms of legislation whether in the Republic or elsewhere.<sup>2</sup> It, therefore, follows that the prohibition in section 5(1) of the Act applies to juristic persons registered in the Republic or outside of the Republic of South Africa.

#### 4. Relevant definitions in the Act

- 4.1 The Act provides the following relevant definitions:

**“captive insurer”** means an insurer that only insures first party risks;

**“first party risks”** means—

(a) in respect of a captive insurer, the operational risks of—

- (i) the group of companies of which the insurer is a part;
- (ii) any associate of a company that is part of the group of companies referred to in subparagraph (i); or
- (ii) any joint arrangement that a company that is part of the group of companies referred to in subparagraph (i) participates in;

(b) in respect of a cell captive insurer, the operational risks of the cell owner and

the operational risks of—

- (i) the group of companies of which the cell owner is a part;
- (ii) any associate of a company that is part of the group of companies referred to in subparagraph (i); or
- (iii) any joint arrangement that a company that is part of the group of companies referred to in subparagraph (i) participates in;

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<sup>2</sup> As per the definitions in section 1 of the FSRA as follows:

“person” means a natural person or a juristic person, and includes an organ of state; and

“juristic person” includes (a) a company, close corporation or co-operative incorporated or registered in terms of legislation whether in the Republic or elsewhere;

and

**“operational risk”**, for the purposes of the definition of first party risks, means the risk of incurring losses as a result of inadequate or failed internal processes, people and systems, or from external events and excludes any risks associated with the insurance obligations of an insurer;

4.2 In terms of the Act, a “captive insurer” is essentially a type of “insurer” as defined, but is one that may underwrite only “first party risks”. Consequently, a captive insurer may not conduct any “insurance business” other than “insurance business” related to “first party risks,” as defined.

4.3 The definition of “first party risks” is restrictive by statutory design to only “operational risks,” in order to circumscribe the nature and scope of a captive insurer underwriting “first party risks” within the group of companies of which the captive insurer is a part of.

4.4 The definition of “first party risks” references a captive insurer that is “part of the group of companies”. The group of companies may include subsidiaries in other jurisdictions that place “first party risks” as defined with the captive insurer. Accordingly, the definition of “first party risks” encapsulates the operational risks of such subsidiaries.

4.5 In terms of Section 5(2) of the Insurance Act:

*“A person is regarded as conducting insurance business in the Republic if-*

(a) *the person conducts business similar to insurance business outside the Republic; and*

(b) *that person or another person, in relation to the business referred to under paragraph (a), directly or indirectly acts in the Republic on behalf of the first-mentioned person, including, but not limited to, by rendering a financial service within the meaning of the Financial Advisory and Intermediary Services Act, 2002 (Act No. 37 of 2002), in respect of that business.”*

4.6 As stated in the Joint Guidance 1 of 2019, both the criteria set out in paragraphs (a) and (b) of section 5 (2) of the Act must be met to regard a person as conducting insurance business in South Africa. Foreign entities that are licensed insurers in a foreign jurisdiction (i.e. conducts business similar to insurance business outside the Republic) are captured under section 5(2)(a) of the Act. Accordingly, foreign entities that conduct “insurance business” in relation to “first party risks” in foreign jurisdictions, and that in relation to that insurance business acts in the Republic (in accordance with section 5(2)(b), will be regarded as conducting insurance business in the Republic, and fall within the definitive context of a captive insurer.

4.7 Captive insurers that are domiciled in and operate from a foreign jurisdiction are typically wholly owned subsidiaries of a group of companies (parent company) and insure exclusively the “first party risks” of the group of companies of which the insurer is a part. It is the view of the Authorities that in

these instances, captive insurers either solicit insurance business directly from the South-African based subsidiaries of the parent company or act indirectly through an intermediary by appointing, instructing, or influencing the intermediary to place the insurance business of a South African based subsidiary with the foreign domiciled captive insurer. In both instances, the description of section 5(2)(b) will be met and, accordingly, such a foreign domiciled captive insurer will meet both the criteria set out in paragraphs (a) and (b) of section 5(2) of the Act and is required to be licensed.

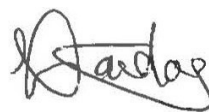
## **5. Licensing approach**

- 5.1 Foreign entities that meet the definition of “captive insurer” read with the definition of “first party risks” are therefore regarded as conducting “insurance business” in the Republic in terms of sections 5(1) and 5(2) of the Act if they act as explained in paragraph 4.7. Accordingly, to legitimately insure “first party risks” in the Republic, foreign entities are required to be licensed within the construct of the Act.
- 5.2 The Prudential Authority shall consider applications for the licencing of any person intending to insure “first party risks” in terms of section 23 of the Act read with item 13(b) of schedule 3 to the Act.
- 5.3 Foreign domiciled captive insurers conducting insurance business in relation to “first party risks” in the Republic may submit an application for exemption, in terms of section 66(1) of the Act, from the provisions of section 23 read with item 13(b) of the Act. Such application should accompany the licensing application referred to in paragraph 5.2 *supra*.
- 5.4 Foreign entities (i.e. entities established or domiciled outside of the Republic) endeavouring to undertake captive or cell captive insurance business within the Republic are referred to in paragraph 5 of Joint Guidance Notice 1 of 2019, in terms of potential supervisory or regulatory action that may be adopted.
- 5.5 As was explained in paragraph 5 of Joint Guidance Notice 1 of 2019, the FSCA holds the delegated authority on behalf of the PA for the regulation and enforcement of sections 5(1) and 5(2) of the Act, in respect of all instances other than where a person may be conducting unlicensed reinsurance business or where an insurer conducts insurance business in terms of a class or sub-class of business not included in its license. By implication, this means that the FSCA is also responsible for regulating and enforcing compliance with sections 5(1) read with section 5(2) of the Act, insofar as it relates to conducting insurance business in relation to “first party risks” without the relevant licence.



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**Date: 30 August 2021**



**Kuben Naidoo**  
**Deputy Governor and CEO:**  
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**Date: 30 August 2021**