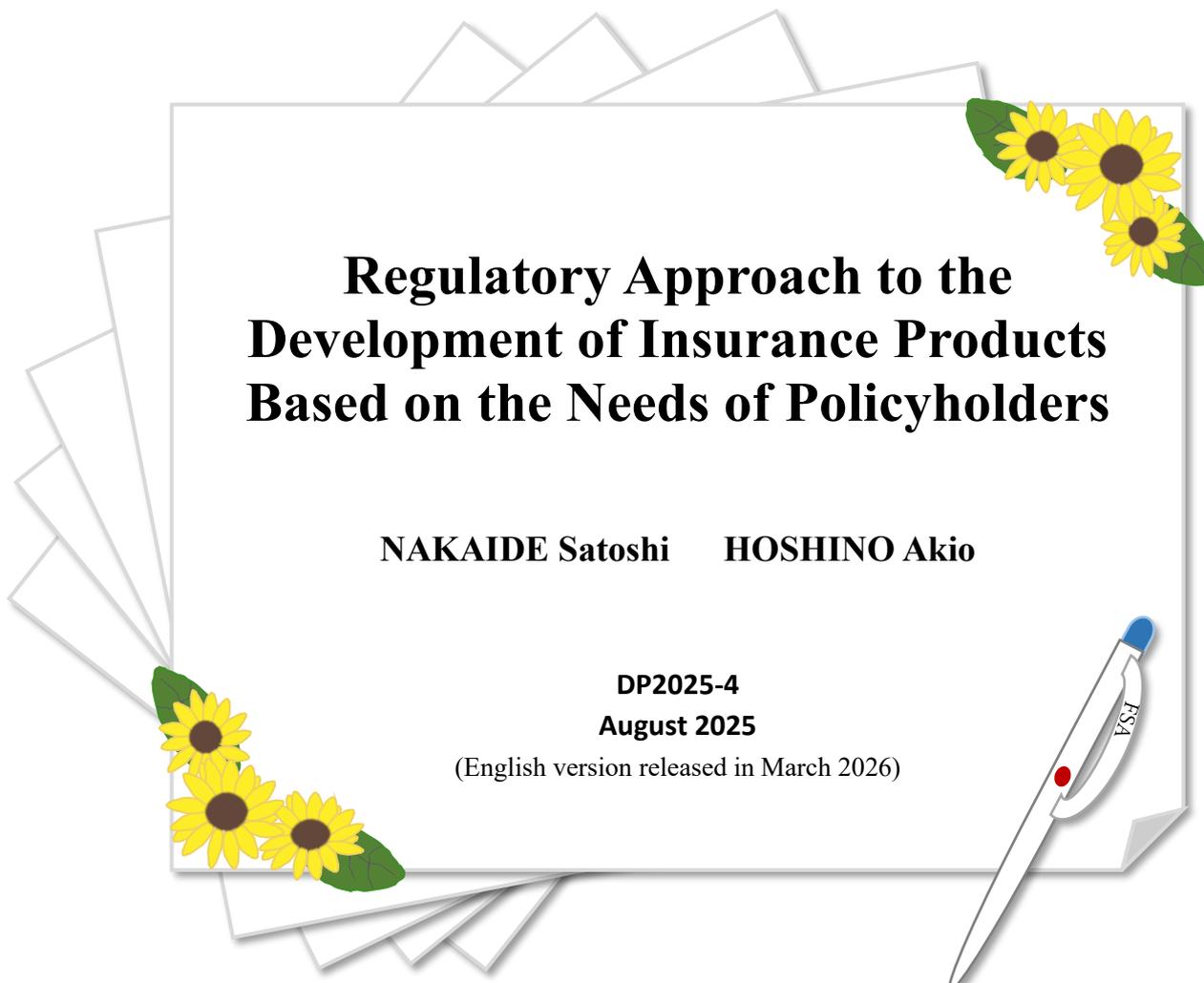




Financial Services Agency

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Regulatory Approach to the Development of Insurance Products Based on the Needs of Policyholders

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Regulatory Approach to the Development of Insurance Products Based on the Needs of Policyholders

NAKAIDE Satoshi* HOSHINO Akio**

Abstract

In Japan, insurance regulation faces the need to promote product development in response to changes in the social environment, such as the declining birthrate and aging population, the increased frequency of large-scale natural disasters, and the rapid advancement of new technologies. To contribute to discussions on a desirable regulatory approach to insurance product development that reflects contemporary needs, this paper examines the insurance product review systems and practices of insurance companies in the United Kingdom, Germany, and the United States (the State of New York). These three jurisdictions were selected to compare distinct insurance market environments. The three countries have the following distinct characteristics: the United Kingdom traditionally allows insurers to develop insurance products and set insurance rates with relative freedom; Germany formerly had a strict review system, but deregulation has progressed due to EU integration; and the United States maintains strict review systems regulated at the state level.

In the United Kingdom and Germany, prior approval is not required for insurance policy terms or premium rates. In the United States, while regulatory systems differ by state, prior notification is generally required for introducing insurance products and determining premium rates. This paper focuses on the regulatory framework of the State of New York, which is known for its rigorous product review system.

In New York, insurance products and insurance rates are reviewed under a licensing system based on state law. However, certain exemptions from prior approval exist, particularly for contracts

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involving corporate policyholders with well-established risk management systems. The scope of these exemptions appears to be expanding, particularly in the corporate sector.

In Germany and the United States, non-binding, standard policy provisions are offered by industry associations or specialized insurance service providers and are commonly used. In addition, loss cost data used as the basis for premium calculations are also provided.

In Germany, the prior approval system for insurance contracts and premium rates has been gradually deregulated through EU directives, and the approval system was abolished by the Third Non-life Insurance Directive in the EU. According to interviews, no significant issues have arisen from the abolition of approval.

In Japan, insurance products and insurance rates are subject to prior review. However, in the corporate insurance sector, a certain degree of flexibility is allowed under the “flexible system for rider clauses.” Insurance regulation in Japan may move toward a more segmented review system based on the nature of risks (mass vs. non-mass risk) and the type of policyholders (individuals vs. corporations).

Keywords: insurance; product approval; premium rate approval; model clauses.

1. Introduction

1.1 Japan's Product Review System for Insurance

In Japan, the development of insurance products is regulated through the approval of insurance policies and rates under the insurance business license system. Article 3 of the Insurance Business Act stipulates no entity shall conduct insurance business if the entity has not obtained a license from the Prime Minister, and Article 4, paragraph 2 of the Act provides that filing of application for a license must be accompanied by: (i) the articles of incorporation; (ii) a statement of business procedures; (iii) general policy conditions; and (iv) a statement of calculation procedures for insurance premiums and policy reserves. Insurance providers refer to documents (i) through (iv) above as Basic Documents.¹

Details of insurance contracts, including the payment of insurance claims, are reviewed at the time of application for business license, where policy conditions which are the core insurance clauses are provided in (iii) “general policy conditions” of the above documents, and rider clauses in (ii) “a statement of business procedures,” as an attachment comprising the statement.

With respect to insurance premiums, the calculation method is reviewed by (iv) “a statement of calculation procedures for insurance premiums and policy reserves.” Insurance premiums can be divided into net premiums² which are equivalent to the cost for the payment of insurance claims, and loadings which are used to cover costs such as business expenses. Specific calculation methods are provided only for net premiums in the “statement of calculation procedures for insurance premiums and policy reserves,” except for automobile liability insurance and household earthquake insurance. For loadings, the reasoning behind calculation is provided as a qualitative statement. Therefore, there is room for insurance businesses to decide loadings taking into account the business environment, including competition with other companies.

There are a number of ways for calculating net premiums in Basic Documents, with different application of regulation depending on the type of insurance products. A regulatory method requiring application of a designated rate for net premiums is called “point system for insurance rate.” The other method is “range system for insurance rate,” which is used for many accident insurance policies, allowing a range of 12.5% above and below the designated rate for net insurance premiums. In addition, some insurance policies define the prescribed rates as “standard rates” and allow changes to the standard rates without setting a range for the change to be within that margin. Therefore, in non-life insurance, insurers have the freedom to change their net premiums within the scope of authorization.

¹ “Basic Documents” is not a legal term from the Insurance Business Act, but is widely used in the insurance industry.

² In this paper, the term “net premium” is used to refer to the portion of the premium allocated for claim payments. This choice maintains consistency with the official English translations used by Japanese institutions, such as the General Insurance Rating Organization of Japan (GIROJ), which uses the term “reference net rates.” However, readers should note that in the context of U.S. property and casualty (P&C) insurance practice, this concept corresponds to the “pure premium.”

Net premiums for life insurance products do not usually have such degrees of freedom. However, the Basic Documents may provide that there is room to change the basic rates, such as “expected interest rates,” which are the elements of calculation, by notification. This notification has a different meaning from the following notification under Article 123, paragraph 2 of the Insurance Business Act, and the direct basis for making a change by notification shall be the Basic Documents, not the Insurance Business Act.

When an insurer makes changes to its Basic Documents after obtaining a license, it must obtain authorization from the Prime Minister as prescribed in Article 123, paragraph 1 of the Insurance Business Act.³ The authorization of the Prime Minister (in practice, the Commissioner of the FSA) is necessary when new insurance products are developed because changes are made to the Basic Documents corresponding to the products. The same applies when premiums are revised.

However, not all insurance products require authorization for changes to Basic Documents. Pursuant to Article 123, paragraph 2 of the Insurance Business Act, Basic Documents for insurance specified by Cabinet Office Order (Article 83 of the Ordinance for Enforcement of the Insurance Business Act) do not require authorization, and can be changed by prior notification.⁴ Changes in Basic Documents by notification are subject to review under the same standards as changes for which approval is needed. Changes in Basic Documents by notification are not effective immediately, and take effect after 90 days have elapsed from the day following the notification is accepted. The Prime Minister may, during that period, order changes to the matters pertaining to the notification or order revocation of the notification, and may, when there are reasonable grounds, extend the period. In practice, if changes to Basic Documents meet the review criteria, the notice is sent to the applicant before 90 days elapse to shorten the period. Insurance companies regard the notice to shorten the 90-day period something equivalent to a license. In other words, the difference between the authorization of changes to Basic Documents prescribed in Article 123, paragraph 1 of the Insurance Business Act and the notification of changes to Basic Documents pursuant to paragraph 2 of the same article is not considered to be substantial. While there are some exceptional cases, which we explain later, insurance business in Japan is reviewed thoroughly and in substance, as the policy conditions and prices of insurance products need to be determined upon authorization or review of

³ The authority of the Prime Minister for authorization of insurers is delegated to the Commissioner of the Financial Services Agency(FSA) pursuant to Article 313 of the Insurance Business Act, and the Commissioner of the FSA actually carries out authorization. Other powers related to insurance supervision under the Act have also been delegated to the Commissioner of the FSA.

⁴ Insurance products subject to this article include, group annuity insurance products such as defined contribution pension insurance and defined benefit pension insurance for life insurance. For general insurance, many products are for businesses such as marine insurance, aviation insurance, machinery insurance, and fleet insurance for over ten insured vehicles. There also products common to businesses and individuals such as fire insurance, liability insurance, and comprehensive insurance for movable property.

notification, through scrutiny at the level of the wording of standard insurance policy provisions and “rider clauses” for policy conditions and at the level of calculation method of premiums for pricing.⁵

The Insurance Business Act allows insurance business that does not require a license, which is a special case regarding “a small amount and short-term insurer.” Article 272 of the Insurance Business Act provides that an entity registered with the Prime Minister may, notwithstanding the provisions of Article 3, paragraph 1, conduct small amount and short-term insurance business. Therefore, a “small amount and short-term insurer” can conduct insurance business upon registration. The authority related to registration is delegated by the Prime Minister to the FSA Commissioner, and further to the Director-Generals of Local Finance Bureaus. As the name suggests, small amount and short-term insurers only handle policies for coverage of small amount and for short insurance terms. Due to their nature, regulation on company establishment and product development are being eased compared to normal insurance companies. In addition, small amount and short-term insurers are allowed to deal in both non-life and life insurance. For the registration of a small amount and short-term insurer, Basic Documents must be attached in the same way as an insurance company, and a notification is required to change the Basic Documents. The authority to review the changes is delegated by the Prime Minister to the FSA Commissioner, and further to the Director-Generals of Local Finance Bureaus, as in the case of registration. Notifications of changes in Basic Documents are subject to a review similar to that of an insurance company, and if they are not met, the change or withdrawal of the notification is ordered. Essentially, review is also conducted for policy conditions and pricing of small amount and short-term insurance products.

1.2 Exception to the Review for the Corporate Sector

In the review system of insurance products in Japan, there is an important exception called the “flexible system for special provisions (rider clauses).” This is possible for insurance products for the corporate sector, by providing in the “statement of business procedures” that insurance rider attached to insurance policies are to be created or changed without filing a notification. The arrangement is referred to as the “flexible system for rider clauses” because, by providing that notification is not required for certain rider in the “statement of business procedures” of the Business Documents, insurance companies can establish or change insurance riders at their own discretion without going through the FSA’s review.

For the “flexible system for rider clauses” to be applied, the “statement of business procedures” that allows flexibility for rider clauses need to be approved upon review. The standards

⁵ There are a number of ways for determining insurance premiums depending on the type of insurance. Examples include: (i) products for which specific rates are identified (so-called “point system for insurance rate”); (ii) products for which the floor and ceiling are specified and the rates can be decided within that range (so-called “range system”); (iii) products for which standard rates are identified but different rates are acceptable (so-called “standard rate system”); and (iv) products for which rates can be decided freely in general. It is specified in the Basic Documents which system is used for calculating the product’s insurance premiums. For products that are calculated by ways other than the point system insurance providers can take the liberty of changing insurance premiums without authorization.

for approval are disclosed in section IV-3-3 of the “Comprehensive Guidelines for Supervision for Insurance Companies” describing the treatment of flexible system concerning insurance rider. The requirements are as follows: (1) the rider to be created or changed is subject to notification; (2) in principle, the policyholder and the insured are business operators; and (3) the “statement of business procedures” provides that rider clauses can be created or changed within the objective and scope of the review criteria.

In cases where it is possible to create or change rider clauses without filing notification as described above, it is also possible to provide in the “statement of calculation procedures” that the calculation method of insurance premiums may be created and changed without notification for insurance premiums of the rider. The review criteria for such statement of calculation procedures are also set forth in IV-3-3 of the “Comprehensive Guidelines for Supervision of Insurance Companies.” The requirements are that the calculation method corresponds to the content of the rider clause, and is reasonable and appropriate from an actuarial perspective, and is not unduly discriminatory.

1.3 The Need for Product Assessment and the Needs of the Time

It is undisputed that regulatory oversight is necessary for insurance business, and hence, licensing systems are taken for the industry in many advanced countries.⁶ However, there are differences in views between the United States and the European Union on the necessity of regulatory review of insurance policy conditions and insurance premiums, which are equivalent of products and prices in non-financial business. It is a matter of balancing different interests, namely the interests of maintaining appropriate policies and prices of insurance products through review under the approval system and the interests of promoting product development by giving freedom to insurers. There is no lasting optimum solution to the appropriateness of the approval system or the degree of freedom that should be given to insurers, and so we need to strike an appropriate balance suited at the time. From a long-term perspective since the time of the former Insurance Business Act before the revision in 1995, Japan’s financial administration of the insurance industry has evolved to gradually easing the approval system and allowing greater freedom of insurance businesses through the revision of the Insurance Business Act and the use of insurance rider.⁷

Observing developments over time, problems related to insurance sales have surfaced constantly in recent years in the Japanese insurance industry. From 2022 to 2024, a number of incidents arose in the non-life insurance industry, suggesting structural problems in the solicitation of insurance products. The incidents included the following: (i) insurance companies suspected of

⁶ For example, see “Research on the outline of financial systems in selected countries” prepared by NTT Data Institute of Management Consulting, Inc. in March 2023.

⁷ The system has been introduced in which changes to “Basic Documents” are permitted by prior notification instead of approval, and cases where certain matters of “Basic Documents” can be changed without prior notification or notification have been increasing.

violating the Antimonopoly Act shared information and fixed their insurance premiums;⁸ (ii) insurance companies overlooked fraudulent insurance claims by insurance agencies that operate car repair shops despite clear suspicions about fraudulent acts;⁹ and (iii) persons seconded to insurance agents obtained customer information inappropriately and provided it to insurance companies they are from.¹⁰ Although the occurrence of similar incidents in the life insurance industry has not been observed so much as cases in the non-life insurance industry, problems related to insurance sales have occurred at a certain frequency. For example, in 2020, insurance companies were found to have fraudulently obtained large value of funds through fictitious transactions, and there were complaints from customers about insufficient explanations about risky asset management products (pensions denominated in foreign currencies).¹¹

The relationship between regulation of insurance product development and problems related to solicitation is not a straightforward matter. When revising the insurance regulatory system to promote diversification of insurance products, it would be appropriate to promote diversification by ensuring that problems do not exist in the ways insurance solicitation is conducted. If public trust in solicitation is not sufficient, careful consideration is needed for expanding the freedom of product development in order to prevent adverse effects.

1.4 Purpose of this Study

With the above perspectives in mind, we surveyed the insurance product review systems in the United Kingdom, Germany, and the United States (New York State), as well as practices among insurance companies, with the aim of contributing to discussions on the regulation of insurance product development. With regard to the survey of actual business practices, we focused on a standardization mechanism in place for process other than the review of insurance products and premiums, as we considered the standardization useful from the viewpoint of avoiding inefficiencies such as making insurance products complicated and setting unreasonable premiums. Specifically, we examined industry-standard policy terms (model clauses) and the use of cross-industry claims data (loss costs).

We confirmed that insurance products and insurance rates are not reviewed in the United Kingdom and Germany. On the other hand, in the United States (New York State), we found that

⁸ See “Results of survey on the act of coordinating insurance premiums by major non-life insurance companies” by FSA (available in Japanese). <https://www.fsa.go.jp/news/r5/hoken/20231226/01.pdf> (viewed on March 1, 2025)

⁹ See “Administrative actions against Sampo Japan Insurance Inc. and Sampo Holdings, Inc.” by FSA. <https://www.fsa.go.jp/news/r5/hoken/20240125/20240125.html> (viewed on March 1, 2025) (short summary available in English)

¹⁰ See “administrative actions against Aioi Nissay Dowa Insurance Co., Ltd.” by FSA (available in Japanese). <https://www.fsa.go.jp/news/r6/hoken/20250324/20250324-2.pdf> (viewed on March 1, 2025) (short summary available in English) <https://www.fsa.go.jp/en/newsletter/weekly2025/630.html#e09>

¹¹ See “the monitoring results pertaining to the implementation status of customer-oriented business conduct by distributors of financial instruments, such as investment trusts (interim report for program year 2023)” by FSA (available in Japanese). <https://www.fsa.go.jp/news/r5/kokyakuhoni/202403/01.pdf> (viewed on March 1, 2025)

there is a rigorous product review system, and also certain exemptions from it, so we conducted our study focusing on these points.

2. Research on Systems related to Insurance Product Review in the Three Major Countries

We surveyed the product review systems for insurance products, focusing on insurance policy terms, in the United Kingdom, Germany, and the United States (New York State). In Germany (and other EU Member States), since the Third EU Non-Life Insurance Directive in 1992 (later integrated into the Solvency II Framework), the approval system for insurance policy terms has been abolished and there is no review system for insurance products. We would like to note that the UK has not had a system for reviewing insurance products and premium rates even before the Third EU Non-Life Insurance Directive, and thus it has not been affected by the Directive nor Brexit in 2020.

On the other hand, in the United States, generally each state government has in place the approval system. There are two arrangements exempted from the approval system, which are the free trade zone and the non-admitted insurance products.

2.1 United Kingdom

Historically, the UK has had no regulatory arrangements like an approval system for insurance products.

In the UK, insurance regulation is conducted by two institutions, namely, the Prudential Regulation Authority (PRA) under the central bank (The Bank of England), and an independent supervisor Financial Conduct Authority (FCA). Both institutions are supervisory authorities overseeing financial institutions, including banks, across the financial industry.

The PRA's primary role in insurance supervision is to ensure the soundness of insurers' management. The PRA checks the adequacy of capital requirements, including the UK version of Solvency II. It does not have responsibilities to oversee the development of insurance products.

The FCA, on the other hand, is responsible primarily for protecting consumers and enhancing market integrity. The FCA has published a range of guidelines in its FCA Handbook, including those relating to insurance product design.¹² Guidelines on the product design do not specifically regulate the details of products such as insurance policy terms, but show principles regarding product approval procedures to be taken within insurance firms and regarding fair value where products provided to customers are of fair value relative to price (value is worth the price).

In the UK, there are no regulations comparable to the product approval system in Japan, and each insurance company can develop new products at its own discretion, paying attention to the FCA's regulations and guidelines.

¹² The FCA Handbook offers FCA's rules and guidance at a glance. <http://www.handbook.fca.org.uk/> (viewed on March 1, 2025)

Laws and regulations governing the appropriateness of the insurance policy terms and conditions include the Unfair Contract Terms Act 1977 and the Unfair Terms in Consumer Contract Regulation 1999. These acts have clauses that nullify unfair contracts, and unlike the approval system which is an *ex ante* regulation, they basically act as an *ex post* regulation after insurance policy terms have been used.

However, the FCA may require, under the Unfair Terms in Consumer Contract Regulation 1999, insurers to amend or delete unfair clauses, and if this is not done, it may request an injunction to the court.

2.2 Germany

In Germany, with the exception of limited cases, government's control over products, such as approval system, have been abolished under the EU Directive. No approval system for insurance products exists today. Aiming for a free and integrated financial market, the EU has advanced with financial market liberalization removing various regulations, and as part of this effort, it liberalized regulations on insurance products. At the same time, it has strengthened its supervision of the soundness of insurers through Solvency II and other regulations.

Insurance supervision in Germany is undertaken by the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin; Federal Financial Supervisory Authority). State governments are responsible for supervision of public insurance in their states and for some small-scale private insurance. As mentioned above, there is no approval system, but notification to BaFin is required for medical insurance and compulsory long-term care insurance when introducing new products or revising existing products.¹³

Prior to the enforcement of the amended insurance act based on the EU's Third Non-Life Insurance Directive, Germany had the approval system for insurance products. Therefore, unlike the United Kingdom, which has never had an approval system, Germany has experienced transition following the abolition of the approval system. We interviewed two researchers in Germany to find out whether there has been market turmoil or troubles with policyholders as the changes in the system took place.¹⁴ The researchers recalled that there had been no particular problems in the market or with individuals.

In short, there are no regulations in Germany comparable to the product approval system in Japan, and each insurance company can develop new products at its own discretion, bearing in mind the regulations and guidelines of BaFin.

In order to contribute to the standardization of insurance policy terms, the Gesamtverband der Deutschen Versicherungswirtschaft (GDV; German Association of Insurers) has provided model

¹³ https://www.bafin.de/EN/Verbraucher/Versicherung/Produkte/Kranken/krankenversicherung_node_en.html (viewed on March 1, 2025)

¹⁴ Interview with Dr. Christian Armbrüster, Professor at Freie Universität Berlin on October 3, 2024, and with Dr. Mirko Kraft, Professor at Coburg University on July 30, 2024.

clauses (Musterbedingungen) for many insurance products such as life and annuity insurances, liability insurances, home insurances, and automobile insurances. The outline of model clauses is discussed in section 4.1.2.

2.3 United States (New York State)

In the United States, each state government is responsible for insurance supervision, and governing laws vary from state to state. In contrast to the UK and EU countries, insurance products are basically subject to an approval system in each state.

Regarding the consistency of supervision at the federal level, the National Association of Insurance Commissioners (NAIC) publishes model laws and regulations.¹⁵ However, these are not binding and there are likely to be differences in supervision among states.

This paper focuses on supervisory legislation of the New York State and provides an overview of its product approval system. The statutes of the State of New York are organized as the Consolidated Laws of New York, which comprises 94 chapters from Abandoned Property (ABP) to Workers' Compensation (WKC) at the time of writing (March 2025).¹⁶ Among them, Chapter 28 Insurance (ISC) is referred to as the insurance law and governs insurance business. ISC covers a supervisory framework, including a licensing system, as well as specific regulatory matters such as a policy form for each type of insurance.

The New York State Department of Financial Services (NYDFS), or DFS for short, is responsible for insurance supervision in the State of New York.

2.3.1 Overview of product approval system under the insurance law (ISC)

Article 1102 (a) of the ISC reads “No person, firm, association, corporation or joint-stock company shall do an insurance business in this state unless authorized by a license in force pursuant to the provisions of this chapter, or exempted by the provisions of this chapter from such requirement.” Compared to Japan’s Insurance Business Act which restricts entities conducting insurance business to stock companies and mutual companies,¹⁷ the insurance law of New York assumes a wide range of institutions to do an insurance business, but a license is required for any type of institutions.

There are two types of licenses: life insurance business licenses and non-life insurance business licenses. In non-life insurance, the business license is basically given for each type of product. The structure of non-life insurance licenses is not simple. There are primary insurance lines, for which insurers can conduct insurance business independently and non-primary insurance lines,

¹⁵ Model laws may require specific terms to be included in insurance contracts, for example, grace period for payment of premiums and incontestability provision that limits the insurer for two years from the date the policy is issued to rescind it.

¹⁶ The total number of chapters and the number of the last chapter do not correspond because there are sub sections to articles, such as 3-A and 3-B, and missing articles due to deletion.

¹⁷ Beside these, “underwriting member conducting insurance business” and “licensed specified corporation” also conduct insurance business in Japan, though institutions applicable to these type of business is very limited.

for which insurers with licenses for other types of insurance can conduct insurance business as ancillary services. Ocean marine insurance is subject to federal law and is not regulated by state law.

In order to develop or amend an insurance product, the insurer is required to file (equivalent to notification) and obtain approval from the DFS. This system may be viewed as a prior notification system in terms of the way procedures look, but in effect, insurers can implement products only after obtaining approval, so it is considered to be close to authorization. Hereafter, the term “filing” is used in principle in this paper. For filing purposes, DFS uses two checklists, the “Review Standards Checklists” and the “Compliance Questionnaire,” to provide guidelines on review standards. Applicants are to check by themselves whether application is appropriate or not based on the checklist before filing.

2.3.2 Operation of Product Approval System in New York

In 2020, the DFS issued Insurance Regulation 195 (2020), which requires that any submission of a rate, rating plan, rating rule, rating manual, rating classification, territory, or insurance contract or policy form be made through the NAIC’s System for Electronic Rates and Forms Filing (“SERFF”).¹⁸

This system for electronic filing has led to the efficiency of the review process in a number of ways. First is the standardization of procedures.

Detailed instructions for submitting SERFF filings are provided in the New York SERFF General Instructions and State Filing requirements. When submitting a filing through SERFF, applicants should complete all fields by inputting information in the Filing Wizard and on the General Information tab. Applicants shall provide information, such as policy forms and rates, in the appropriate fields of the Filing Wizard, and explain the intent of the filing and highlight any substantive changes (such as changes in ratemaking methodology or major coverages provided) in the Filing Description field under the General Information tab.

Formats for submission are also clearly indicated; all attachments must be provided in Adobe Acrobat (PDF) format and individual attachments should not be larger than 8 megabytes (MB).

To check the content of the filings, the attachment of the appropriate Review Standards Checklist is mandatory for all filings submitted through SERFF. According to the instructions of the checklists, applicants must explain how they comply with the requirements set out in the checklists and provide references to the relevant section of the submission form. This system of submission requires applicants themselves to check that they meet the requirements, and this contributes to the efficiency of supervisors that review the filings.

Where similar products already exist or if the filing is currently in use in another state, these points can be used to conduct the review of filings efficiently. When modifying products, if compliance with applicable Submission Requirements has been evidenced in a SERFF filing previously approved by the Department and there have been no changes to such portion of the filing,

¹⁸ https://www.dfs.ny.gov/apps_and_licensing/property_insurers/rate_form_filings (viewed on March 31, 2025)

such Submission Requirement may be by-passed by referencing the relevant file number with the explanation “previously submitted and approved.” If the filing is currently in use in another state, this should be indicated in the Filing Description. While the fact that the same filing is being made in other states does not directly relate to the content of the review, this point is used as useful information for conducting efficient review, as it would be rationale to adjust the strength of review for products that are completely new and for products with similar features existing in the market.

In addition, DFS has a system called the “Speed to Market” Program for non-life insurance. Insurance providers can use this procedure to further expedite their reviews. DFS will process with priority those filings that are accompanied by the appropriately completed review standards checklists and the appropriate compliance certification forms. To use the program, the applicants attach the “Master List of Review Standards Checklists,” “Policy Form Compliance Certification,” and “Rate and/or Rating plan Compliance Certification.”

The insurer pronounces that all applicable laws and regulations have been properly considered and all necessary evidence is provided. The DFS conducts a swift review with its trust in this pronouncement. If filings are found not compliant subsequently, appropriate action may be taken against the insurer.

In fiscal year 2023, the insurance unit of NYDFS supervised approximately 128 life insurers and 800 non-life insurers.¹⁹ The total number of filings by these companies is around 4, 500 annually.²⁰ We were unable to determine the number of staff in charge of reviewing the filings, as no disclosed information was available and specific figures to our enquiry have not been provided. However, since the total number of full-time employees at DFS is 1,391,²¹ we assume that employees engaged in insurance review are several dozen at maximum. The efficiency of review operations is essential for the institution.

We consider that the New York State has established a system that achieves efficiency of review by creating standard formats for filing, introducing electronic filing and using review results of similar cases as secondary information.

2.3.3 Exemptions - A. Non-admitted insurer (also known as surplus lines insurer)

2.3.3.1 Overview

Insurance business is regulated by state governments, and insurers seeking to do business must obtain a business license from the relevant state government. The major exception to this is non-admitted insurers. In recent years, the terms “surplus line insurance company” or “excess and surplus line insurance company” have often been used instead of non-admitted insurer due to the impression the

¹⁹ Searching the website of DFS, the number of non-life insurers is 802. However, the actual number is likely to be less because insurers with the same addresses and company names are found.

²⁰ According to interview with DFS on August 6, 2024.

²¹ The official website of New York State.

https://www.budget.ny.gov/pubs/archive/fy25/ex/agencies/appropdata/FinancialServicesDepartmentof.html?utm_source=chatgpt.com (viewed on March 23, 2025)

term gives, but there is no difference in the substance of insurance. The term “non-admitted” is used in the model law of NAIC, the Non-admitted and Reinsurance Reform Act 2010 (NRRA) as well as in many states. In New York, however, the formal term used is “unauthorized.” This paper uses the term “non-admitted insurers” or “surplus line insurers.”

Non-admitted insurers mean insurers licensed in another state or a foreign country, but not in the state where the policyholder is located. Insurers that are licensed in other states within the United States and not licensed in the state where the policyholder is located are referred to as “Foreign Insurers.” Here, “foreign” is understood as meaning “outside the state.” There are cases where insurers licensed outside the United States become non-admitted insurers, and such insurers are referred to as “Alien Insurers.” Obviously, an insurer that has not been licensed anywhere cannot operate as a non-admitted insurer.

To do business as a non-admitted insurer, other conditions such as capital adequacy need to be met. Specifically, the minimum requirement for the sum of capital and surplus is \$15 million.

The history of non-admitted insurers is long in New York, where the surplus lines law was enacted in 1890. This is because, when insurers with weak solvency positions became insolvent due to the Great Chicago Fire of 1871 and the Great Boston Fire of 1872, policyholders purchased insurance policies from insurers established in other states.

Non-admitted insurers provide coverage against catastrophic events such as earthquakes and hurricanes, as well as extraordinary risks such as those related to satellites. In recent years, insurance for ride hailing services operated by transportation network companies like Uber has been provided by insurers specializing in surplus lines.²²

Regulation of non-admitted insurers is stipulated in NRRA.

Some of the differences between non-admitted insurers and admitted insurers regarding regulation of business management and financial requirements are that non-admitted insurers are not subject to rating methodology regulation, they do not have to participate in mandatory insurance pools, and they have different annual reporting requirements. Since no state approval is necessary, insurers operating in multiple states in the United States, such as AIG, have set up non-admitted insurers as subsidiaries that address needs across the country for insurance products covering extraordinary risks. This is considered as benefits of non-admitted insurers because obtaining licenses to conduct admitted insurance in different states requires a significant amount of processing.

²² There are three types of insurance for ride-hailing automobile insurance: (i) personal auto policy (PAP) ;(ii) insurance policies and rider clauses for drivers of transportation network companies; and (iii) automobile policies for transportation network companies. Two major companies operating transportation network companies in California, namely Uber and Lyft, offer insurance to drivers from non-admitted insurers to cover compensation (Furuhashi, K, 2016, “development of ride hailing and non-life insurance in the United States: based on the expansion of the sharing economy” Sampo-hoken report, Vol. 117, October 2016).

2.3.3.2 Conditions for non-admitted insurers

Important conditions are imposed on the underwriting of insurance contracts by non-admitted insurers that are different from those of admitted insurers.

2.3.3.2.1 Type of transaction

In the United States, contracts with insurers licensed outside the state where the policyholder is located are prohibited in general. Non-admitted insurer is an exemption from this. With regard to non-admitted insurers, direct transactions with policyholders or underwriting through general insurance agencies are not permitted and contracts are concluded through surplus lines brokers who are licensed in the relevant state. Non-admitted insurers are not permitted to engage in insurance sales activities, and they can only underwrite policies upon request from policyholders. Therefore, a specialized broker called the “surplus lines broker” (also referred to as “excess line broker”) is needed to intermediate the underwriting of this insurance.

Surplus lines brokers undertake the underwriting business for insurance companies and play a role similar to that of product providers or wholesalers. They usually do not sell insurance directly to policyholders; they use retail agents or brokers.

2.3.3.2.2 Types of risk

Non-admitted insurers can only take on risks that licensed insurers do not. To buy insurance from a non-admitted insurer, in general, proof of decline from three admitted insurers is necessary. To comply with this rule, the policyholder must submit to the State Insurance Authority documents proving that admitted insurers declined to underwrite insurance. These procedures are performed by surplus lines brokers in practice. In this regard, the presence of brokers is essential for the business of non-admitted insurers.

Typically, surplus lines insurance are insurance policies providing coverage for risks that are significant and cannot be handled under normal circumstances. Examples include nuclear insurance and insurance for summer camps. Non-admitted insurers are not permitted to underwrite products such as personal automobile insurance, home insurance, and life insurance, which are key fields of insurance for normal insurance businesses.

2.3.3.2.3 Exempt Commercial Purchasers

As stated in paragraph 2.3.3.2.2 above, policyholders who wish to use a non-admitted insurer must demonstrate that they have been denied coverage by a licensed insurer, but this requirement is waived for Exempt Commercial Purchasers, which include large enterprises that meet certain requirements. An exempt commercial purchaser must, besides meeting asset and profit requirements, appoint a risk manager.

This scheme is, therefore, essentially one for large corporate contractors.

2.3.3.3 Premium income of non-admitted insurers

According to statistics of the Excess Lines Association of New York (eLANY), an industry association of surplus lines brokers in New York, premium income over recent years has been as follows.

(U.S. dollars)

2021	2022	2023	2024
\$6,205,508,069	\$7,496,382,177	\$7,884,734,251	\$8,985,706,524

(Source: Prepared by the authors based on data from reports and eLany Annual Report of relevant years.)

As evident from the table, the market is expanding at an average annual growth rate of over 13%.

2.3.4 Exemptions - B. Free Trade Zone

2.3.4.1 Overview

Besides non-admitted insurers, there is a system called Free Trade Zone (FTZ) that enable underwriting of non-admitted insurance. This is sometimes called the “third avenue” as it is the third form of underwriting after admitted insurance and non-admitted insurance.

This scheme can be used by admitted insurers, but to use it, an insurer needs to have an insurance business license as well as a Special Risk License for the FTZ. The use of this system will also enable admitted insurers to promptly respond to the individual needs of policyholders.

When insurance policy terms are customized using FTZ, normally review by DFS is not required nor submission is necessary, but compliance with acts and regulation applied to general insurance contracts is necessary. As for risks related to Class 3 described below (see 2.3.4.2 (iii)), insurance contracts are submitted to the superintendent for the purpose of information provision.

2.3.4.2 Terms and conditions

The requirements for using FTZs are set out in Article 63 of the State Insurance Law and Regulation No. 86. The risks covered are one of the three types below. The underwriting of insurance is possible for these risks without filing.

(i) Class 1 Risk

A minimum annual premium in excess of \$100,000 or higher for any one policy, or a minimum combined annual premium in excess of \$150,000 or higher for multiple policies.

(ii) Class 2 Risk

The coverage is for a risk or class of risks which is of an unusual nature, a high loss hazard, or difficult to place. The list of coverages that can be contracted as Class 2 risks is maintained and regularly updated by DFS. Risks that do not fall under Class 1 or Class 3 may only be contracted in the FTZ if they are on the Class 2 list.

(iii) Class 3 Risk

Risks in this category were included by Act 490 of 2011, this category involves insurance for a large commercial insured that employs or retains a special risk manager to assist in the negotiation and purchase of a policy. It should be noted that a medical malpractice insurance policy cannot be contracted as a Class 3 risk.

According to an article by the New York Times, the history of the FTZ dates back to September 1978.²³ The article writes that the use of the term “free trade zone,” which is commonly used to describe tax-free trade within a region, implies that there was a motivation to make New York the center of free trade on insurance comparative to the Lloyd’s through this system. Statistics on the size of FTZ market reveal that the market is approximately \$1.8 billion, according to DFS’s 2010 Annual Report of the Insurance Department. More recent figures are not available.

2.3.5 Comparison between non-admitted insurance and FTZ

The main features of the two schemes are as below.

Table 1: Comparison of Non-admitted Insurance and FTZ in New York State

	Non-admitted insurance (surplus lines)	FTZ
Underwriters	surplus line insurers (licensed outside NY)	Insurers licensed in NY
Authorization of products	Not subject to state regulation	Not subject to authorization, but products must comply with the state review standards
Underwriting method	Must go through a surplus lines broker	No restrictions (e.g., agents, general brokers, direct underwriting)
Key requirements for covered insurance	Normal underwriting declined and/or the insured is a “commercial insured”	Contracts with value in excess of \$100,000, or insurance for risks that are listed in advance as having special nature

(Source: prepared by the authors using data on the DFS website.)

²³ December 10, 1978. “The New Insurance Free-Trade Zone,” New York Times, Section F, page 15.

3. Study on Systems for Reviewing Premiums in the Three Major Countries

3.1 United Kingdom

The UK has historically had no such regulatory arrangement as an approval system for insurance premiums. In the UK, there are no regulations comparable to Japan's rate approval system, and so each insurance company can set insurance premiums at its own discretion.

In addition, there are no standard rates equivalent to the standard rates for Japan's earthquake insurance or automobile liability insurance, or the reference net rates for fire insurance, automobile insurance, or accident insurance.

3.2 Germany

In Germany, regulatory arrangements such as the rate approval system have been abolished based on the EU Directive. There are no regulations equivalent to Japan's rate approval system, and each insurance company can set its premiums at its discretion.

The German insurance association (GDV) collects data from member insurance companies and feeds back information such as loss costs.

3.3 United States (New York State)

3.3.1 Overview of rate approval system in New York State Insurance Law (ISC)

In the state of New York, Article 2305 of the ISC lists 13 types of insurance that require prior approval of rates by filing with the superintendent. Such insurances include workers' compensation insurance, motor vehicle insurance, and medical malpractice liability insurance. For other types of insurance, such as homeowners' insurance, the filing of rates after they are set is permitted. For life insurance, there are no legal provisions requiring rate approval.

In addition, pursuant to Article 2308 of the ISC, the superintendent may order that premiums for insurance types not covered in Article 2305 of the ISC referred to above be subject to prior approval if the superintendent determines, after a hearing, that competition is insufficient, or that insurance business is conducted as to be detrimental to the solvency of insurers.

The rules for approval of insurance premiums vary depending on the type of insurance, applying specific rates for some, while for some other types allowing a certain range to the rates that have been filed in advance. For example, Article 2350 of the ISC allows for increases or decreases in rate level of premiums for insurance of a motor vehicle predominantly used for nonbusiness purposes. The level change permitted is five percent above or below the approved rates, which is smaller than 12.5 percent applied to net premiums for non-life insurance in Japan.

3.3.2 Administration of the New York State Rate Approval System

The approval of premium rates of non-life insurance constitutes the system for the filing of insurance products, and the filings are made through the NAIC SERFF mentioned earlier in 2.3.2. Insurers

submit the rates and rating plans, etc., on the DFS filing site prepared according to formats specific to each class of insurance. The relevant chapter of the ISC applies to rating standards for each type of insurance.

The “Speed to Market” Program, which speeds up the review process by requiring insurers to complete checklists and certifications, also applies to rate filing, but this program does not apply to motor vehicle insurance for nonbusiness purposes, public motor vehicle insurance, workers’ compensation insurance, or medical professional liability insurance. Premiums for these types of insurance must be filed in the usual way.

3.3.3 Exemptions

The approval of rates is not required for non-admitted insurance (surplus lines) and for insurance written in FTZ.

4. Research on Scheme to Standardize Matters Other Than Review of Insurance Products and Premiums

4.1 Model Clauses and Their Use

4.1.1 United Kingdom

In the United Kingdom, no model clauses have been prepared, so each insurance company prepares and applies its own policy terms. The Association of British Insurers (ABI) has not developed model clauses like the German GDV described below. The ABI has presented industry guidelines and so they are involved in standardization in that regard, but the structure and wording of insurance policy terms vary from company to company.

UK policy terms have become the global standard for products such as marine insurance and aviation insurance, which are concluded globally. Although such policy terms cannot be considered as policy terms prepared by the UK’s insurance industry since the products are not necessarily targeted for the UK market, it is worth noting that UK has policy terms that are global standard. This is likely to be due to the fact that the products are often traded in the London market like the Lloyd’s, and the need for de facto standard is strong because the use of reinsurance is common. The International Underwriting Association of London composed of international insurers has published a total of 1,063 model clauses and guidelines (as of April 2, 2025) for marine insurance, aviation insurance, and other commercial insurance for businesses. The Lloyd’s provides its members with a database of policy wordings and clauses (Lloyd’s Wordings Repository). The fact that the London market provides global-standard policy terms for international corporate insurance not only expands the underwriting possibility of insurance but also increases the likelihood of entry by new companies into the market, leading to the promotion of competition. These points may have implications to the direction of future development for Japanese insurance market.

With regard to premiums, there is no industry-based standard rate in the UK. In addition, data such as loss cost calculation data is not shared.

4.1.2 Germany

In Germany, the German Insurance Association (GDV) has prepared a number of non-binding model clauses, and this has in fact had a standardization effect. The model clauses are available from GDV's website free of charge for its members as well as the public. The broad classification of model clauses is as follows. In the life insurance field, there are life insurance, business disability insurance, asset formation life insurance, pension insurance, other primary insurance, secondary insurance, and other insurance. In the non-life insurance field, there are cyber insurance, liability insurance, automobile insurance, clinical trial insurance, legal protection expense insurance, travel insurance, corporate property insurance, personal property insurance, emergency service insurance, marine aviation insurance, and accident insurance.

Approximately five samples of model clauses are provided for individual products in each major classification, offering nearly 100 types of model clauses. According to a survey conducted by the General Insurance Institute of Japan in 2012 on automobile insurance policy terms in Germany, the structure and content of major insurance companies' policy terms were found almost the same as those of model clauses except for minor details.²⁴ It is considered that model clauses of the GDV have contributed to the standardization of insurance products in Germany.

Model clauses for personal health insurance, which is equivalent to the third-sector insurance in Japan, are provided by PKV-Verband, an industry association of health insurance companies and long-term care insurance companies.

Regarding insurance premiums, the GDV provides statistics on insurance data such as loss cost for various types of insurance based on data from insurance companies. The data serves as basic information for the calculation of premiums by insurance companies. Statistical data is provided for fire insurance, automobile insurance, and accident insurance (for these reference net rates are provided in Japan), as well as liability insurance and legal protection expense insurance.

The GDV also provides actuarial support to insurance providers, including the development of natural catastrophe risk models.

4.1.3 United States

In the United States, many non-binding model clauses are provided by insurance service organizations such as the Insurance Service Office (ISO), and this has resulted in standardizing products. Besides ISO, other insurance service organizations include the American Association of Insurance Services (AAIS), which specializes in corporate insurance, and the National Council on Compensation Insurance (NCCI), which provides loss costs to companies that handle workers' compensation insurance.

²⁴ Research section of the General Insurance Institute of Japan, "Regulations and the situation of insurance solicitation and insurance claims payment in major European countries and the United States," September 2012. (available in Japanese).

ISO is particularly important as it operates in all 50 states. Since its establishment in 1971, ISO has provided rating services to member insurance companies as a non-profit organization. It was reorganized into a stock company in 1993. In 2008, the company launched Verisk Analytics, a data analytics business that also targets companies in industries other than insurance. In 2009, Verisk Analytics became the parent company and ISO became a subsidiary of it. While there have been no significant changes to services provided by ISO, such as the development of model clauses, actuarial services, provision of data, and submission of forms to state regulators on behalf of insurers, services are now conducted for profit and are sold to insurance companies for a fee as a commercial enterprise. For the financial year 2024, Verisk Analytics had revenue of \$2,880 million with net income of \$950 million, and had 7,800 employees.

ISO has an extensive range of model clauses. According to the 2012 survey by the General Insurance Institute of Japan, there are model clauses for as many as 9,000 products.

ISO accumulates a vast amount of data on loss costs and provides them to insurance companies, which serves as important basic data for determining their insurance premiums.

ISO also provides extensive support on filings, helping insurers to submit forms to state regulators. The DFS expects service organizations like ISO to perform filing operations on behalf of insurers; for non-life insurance, Article 2313 of ISC provides for this. As for life insurance, there are no statutory provisions, but in an official opinion for Industry Guidance, DFS states that filings by service companies on behalf of insurers are also possible.²⁵

According to an interview with ISO by the General Insurance Rating Organization of Japan in 2023, filings are almost automatically permitted when ISO standard clauses are used without any specific changes. This is referred to as “Me-too” filing.

Since the risk of litigations challenging the appropriateness of insurance policy terms is considerable for insurers, it would be a great benefit to reduce the risk by using “Me-too” filing.

Insurance for large corporates often needs policy terms specific to the institution, but insurance for individuals and small businesses does not need to be planned exclusively for them.

4.2 Unique Services: Specialty Insurance Companies

In UK, Germany, and the New York State, there are a number of insurers that specialize in offering insurance products on particular risks or sectors, referred to as “specialty insurers.” Each specialty insurer has considerable expertise in the underwriting of specific risks and has unique features in risk assessment and underwriting arrangements.

In Japan, there is a trend toward oligopoly of the market by major insurance companies, and so the presence of specialty insurers in countries abroad can provide useful implications for product diversification.

²⁵ Re: Life Insurance Forms Filing License
https://www.dfs.ny.gov/insurance/ogco2001/rg103052.htm?utm_source=chatgpt.com (viewed in March 2025)

4.2.1 United Kingdom

Leading insurers handling specialty insurance in the UK are syndicates of Lloyd's of London. Syndicates are specialized underwriters different from insurers, accepting specialized insurance such as insurance for artworks, cyber insurance, and political risk insurance, applying high expertise. There were 77 syndicates in 2024.²⁶

4.2.2 Germany

In Germany, ERGO Group AG, the parent company of Munich Re's primary insurance group, has multiple subsidiaries and a number of specialty products, including orthodontic insurance, dog owners' liability insurance, horse owners' liability insurance, and personal articles insurance for items such as musical instruments and sports equipment.²⁷ Talanx group has multiple brands under HDI Deutschland AG, which sells products to banks and other customers.²⁸

4.2.3 United States

The majority of surplus lines insurers in the United States are specialty insurers.

5. Product Development Environment for Japan in Consideration of the Nature of Insurance Products and Policyholders

5.1 Classification of Insurance by the Nature of Risk: Mass Risk and Non-Mass Risk

There is no review system for insurance products and premium rates in the UK and Germany in general, but the New York State (US) has a rigorous review system. The filings in New York State differ depending on the type of insurance, and for non-admitted insurance and FTZ, which are exempted from the review system, conditions for exemptions were set out by the type of risk and the status of the policyholder, respectively.

When studying how review should be conducted in Japan based on the systems in the three countries, one method may be to refer to the US style. That is, to classify insurance by the type of risks, and allow more freedom in product development for insurance that would have relatively large benefits and less adverse effects from greater freedom. In this respect, Japan's insurance system has classified insurance into that for individuals and businesses, and we have promoted to increase freedom in insurance for businesses.

²⁶ Lloyd's of London: History of the Insurance Marketplace, Investopedia.

<https://www.investopedia.com/terms/l/lloyds-london.asp?utm> (viewed in June 2025)

²⁷ <https://www.ergo.de/de/Produkte> (viewed in June 2025)

²⁸ Takeuchi, M. 2020. "Developments in German insurance market: management of insurance group under prohibition of undertaking both life and non-life insurance business." *Hokengaku journal*, Vol. 651. (available in Japanese)

The classification of insurance into personal insurance and commercial insurance is an effective way but not a panacea for categorizing insurance. Even in the corporate sector, insurance for small and medium-sized enterprises has characteristics closer to personal insurance than those of insurance for large corporates, and so classification is not simple.

One idea would be to classify insurance focusing on its essential function, categorizing into mass risk insurance and non-mass risk insurance.²⁹

Insurance against mass risk refers to insurance areas where it is possible to calculate premiums based on the law of large numbers. Specifically, these include life insurance, automobile insurance, fire insurance, and accident insurance.

Insurance against non-mass risk, on the other hand, refers to insurance areas where it is difficult to calculate premiums based on the law of large numbers. Specifically, these include marine insurance, reinsurance, large factory insurance, cyber insurance, and insurance related to COVID-19. Mass risk insurance is mainly for the household sector, and non-mass risk insurance is mainly for the large enterprise sector. Even in the household sector, however, there are risks that are not suited to the law of large numbers, such as war risk, earthquake risk, and pandemic risk. Many of these risks are excluded from coverage by exemption clauses, though some insurance cover them.

Mass risk insurance utilizes the law of large numbers, so it requires the accumulation of many homogeneous policies for its operation. In this regard, it is important to maintain the integrity of insurance. Appropriate governance over products and rates is necessary. On the other hand, in the case of non-mass risk insurance, it is difficult to balance income and expenditure based on the law of large numbers in the first place, and for insurers it has the aspect of a business that earns returns by taking on unknown risks. For some non-mass risk, it may be difficult to accumulate certain amount of policies, and therefore rules applied to insurance managed based on the law of large numbers may not be suited for insurance against such risks.

5.2 Desirable Ways for Managing Mass-Risk Insurance and Non-Mass Risk Insurance

5.2.1 The need for the review of insurance products and rates

While there are a number of reasons why product review is needed, the main objectives are the protection of the interests of policyholders and the maintenance of public order. To this end, for many non-insurance contracts, there are *ex post* measures in place, such as the overriding of unjustified clauses. In contrast, prior screening is in place for insurance, despite the incurrance of relatively large administrative burden. This is because insurance regulation presumes mass risk, which are premised on the sound formation of a homogeneous and large insurance group.

²⁹ Nakaide, S. 2022. "Two insurance systems based on risks: taking up issues in consideration of the principles of insurance." *Seimeihoken-ronshu Journal*, Vol. 221, p.1.

For non-mass risk insurance, on the other hand, this characteristic of collectiveness becomes less distinct, and the nature of insurance becomes closer to the usual business of a profit-making company that expects to make profits by taking risks. This characteristic is particularly noticeable in insurance that responds to the individual needs of large corporates.

The need for premium review reflects this trend even more strongly. The three principles of insurance premiums, i.e., reasonable, appropriate, and not unfairly discriminatory, correspond to not being too large or too small regarding the expected value of insurance claims under the law of large numbers for mass risk. On the other hand, for non-mass risk, the expected value cannot be determined by the law of large numbers, so subjectivity arises in the assessment of the appropriateness of the rates. It could be considered that one of the objectives of premium review is to ensure the soundness of insurers, but the idea of ensuring the soundness of the entire institution by regulating the premium rates of individual products is somewhat unreasonable, and the mainstream in international trend is to ensure the soundness of insurers through solvency regulations and capital regulations.

However, there are non-mass risk that have a homogeneous and sizable group; an example is the so-called “aggregate loss risk” relating to natural catastrophes and social risks. Aggregate loss risk insurance for individuals is non-mass risk insurance. The reason for this is not the uniqueness of insurance but its collectiveness and given that the main objective of this kind of insurance is to stabilize the lives of individual policyholders, prior review of products and insurance premiums has great significance.

5.2.2 The significance of model clauses

Based on the idea described above, with respect to mass risk where the law of large numbers holds, the standardization of insurance policy terms would be effective in forming a homogeneous and large insurance group, and its benefits would be significant.

On the other hand, regarding non-mass risk, many of the risks are not suited to the law of large numbers due to their uniqueness. It would be appropriate to develop their clauses individually, as it seems they are difficult to standardize.

Among non-mass risk, compensation for accumulated losses for individuals is often excluded by exemption clauses. In the case of underwriting risk of such losses, the standardization of clauses would have a significant meaning. Preparation of model clauses may become indispensable for, particularly, products such as earthquake insurance, where underwriting of non-mass risk is made through specialized arrangements.

5.2.3 Rationale for standard premiums

A similar thinking as above would apply to premiums. For mass risk, it would be desirable to calculate stable loss costs based on cross-industry data, following the example of the reference net

rates. On the other hand, with regard to non-mass risk, there is little benefit in doing so for specific individual risks, and it can be left to the discretion of each insurer.

Furthermore, for non-mass risk, it would be meaningful to establish an industry-wide calculation method for the aggregated loss risk by, for example, using engineering models.

6. Desirable Regulation of Product Development with Consideration of Policyholders' Needs

As described in section 1.3, it is important to balance the interests of ensuring appropriate insurance policies and prices through review under the approval system with the interests of promoting product development by providing freedom to insurers. In addition, given that the review of insurance products requires expertise and takes time and effort, consideration should be paid to what would be the optimal allocation of administrative resources for product review in the situation where there are wide-ranging operations for insurance supervision.

Our basic thinking is that, if it is possible, it would be desirable to simplify review of insurance products from the viewpoint of promoting free market in market capitalism and allocating administrative resources to other issues such as product solicitation and insurers' soundness.

Turning to the regulation of the United States, while the basic approach is that it applies rigorous notification system, innovative insurance products that meet the needs of policyholders are provided swiftly, particularly for products for the corporate sector. For example, operators of ride-hailing businesses incur specific risks that are not covered by normal automobile insurance, and unless such risks are addressed their business could have been hindered, but through the use of non-admitted insurance effective coverage is being provided. For the review of such innovative insurance products, knowledge based on experience is not so helpful, and so it would be difficult to improve the effectiveness of prior screening. On condition that policyholders have sufficient expertise, allowing transactions to be concluded freely between insurers and policyholders would contribute to the social progress.

On the other hand, it is important to maintain the review operations that serve a great function for the protection of policyholders and social stability.

In other words, it is desirable to apply different regulatory approaches depending on the nature of insurance products and the level of policyholders' insurance knowledge and risk management ability. In order to develop an appropriate regulatory framework by combining various systems, the following directions can be considered.

(i) With regard to mass-risk insurance products, the approval system is maintained for the time being from the viewpoint of ensuring appropriate policy terms and prices of insurance products, but at the same time improve the efficiency of regulatory review process by further realizing standardization through expanding the scope of model clauses and reference net premiums. Based on the New York State's system, it may be one option to introduce an arrangement demanding applicants themselves

to check whether they meet legal requirements for review, and a penalty is imposed in a timely manner when any deficiency is found.

(ii) Regarding non-mass risk insurance products for which large enterprises are policyholders, greater freedom in product development is envisaged from the viewpoint of promoting innovative insurance products. The freedom in product development has already been realized to some extent through the “flexible system for insurance rider,” and greater freedom can be applied to corporates, particularly larger ones, abolishing the requirement for approval and notification. From an academic point of view, “insurance rider” and “general policy conditions” have different meanings. However, in a simple example, if an insurance rider that completely changes the content of the “general policy conditions” by denying every clause of the policy conditions is written and applied, the current regulation on “general policy conditions” can become hollowed, a mere name. While “insurance rider” is created and changed freely now, having “general policy conditions” to remain subject to the approval or prior notification system seems there is no practical benefits, making procedures complicated. It is desirable to promote new ideas by eliminating the process necessary for changing “general policy conditions.” On the other hand, regarding insurance for small and medium-sized companies, it could be considered that some types of insurance are close to mass risk and therefore, regulation should be considered not by the classification that they are in the corporate sector, but should also take into account the size and the insurance knowledge of policyholders, upon referring to exemptions to “commercial insured contractor” for non-admitted insurance and Class 3 risk for Free Trade Zone in the US. These examples consider the expertise and competence of the insured in determining the need for regulation, and this could be regarded as applying the suitability principle in a broader aspect. Japan can draw on this thinking for its regulatory approach.

(iii) Expand, to the extent possible, the scope of model clauses and reference net rates provided by the General Insurance Rating Organization of Japan for insurance addressed to mass risk in general and insurance addressed to accumulation risk within non-mass risk where policies would have homogeneous quality. This approach would simplify insurance products and improve policyholders’ understanding of products for mass risk insurance and increase stability of rates for insurance for natural catastrophes and social risks.

In the three major countries surveyed here, it seems specialty insurers are playing a role in diversifying insurance products. In contrast, Japan’s insurance industry can be characterized as oligopoly market and similarities in major insurers’ business models where they offer full range of products. There is some small amount, short-term insurers that have business models with limited range of products, specializing in niche market, but the impact of their business on the market is not big.

It would be beneficial to promote the emergence of specialty insurers that have extensive expertise in specific areas of insurance products as one approach to diversifying Japan’s insurance market.

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