

## Response of the Administration

### I. Employees' Compensation Insurance Market-related Matters

#### (a) "Soaring premium"

As explained in the Information Paper entitled "Insurance coverage for various business sectors" prepared by the Financial Services and the Treasury Bureau / Office of the Commissioner of Insurance (OCI) (copy at — Annex), the recent increase in employees' compensation (EC) insurance premium is the result of a combination of factors. We believe that the main reason is the significant losses suffered by EC insurers in the past few years. From 1997 to 2001, the underwriting loss suffered by EC insurers amounted to \$4,514 million in aggregate. The loss trend continued into 2002 with a provisional underwriting loss of \$323 million reported. These have led to insurers reviewing their underwriting and premium setting policies.

2. Other factors include the contraction of worldwide reinsurance capacity following the unprecedented losses arising from the "911" events in the United States (which raises substantially the reinsurance costs of direct insurers) and the weak investment returns in recent years (which reduces the ability of insurers to offset their underwriting losses).

3. Insurance is a risk assessing and pricing business. Hong Kong has an open insurance market. We believe that the level of premium rates should best be set by market forces, and as a matter of policy and law, it would not be appropriate for the Commissioner of Insurance (CI), the regulator, to intervene. Moreover, the recent increase in premium should be read in the context of the keen competition in the market in the past few years. According

to a survey of the OCI, average premium rate for EC insurance dropped by 22% (non-construction EC business) and 28% (construction EC business) between 1996 and 1999, despite that in the same period the claims payout had increased significantly. Internationally, many other advanced economies also face the issue of increasing EC (or employers' liability) insurance premium. For example, it was reported earlier this year that the increase in premium for employers' liability insurance in the UK over the past 12 months was between 30%-50%.

4. Locally, the Administration has been promoting occupational safety and other measures, such as facilitating the early rehabilitation of injured employees, which would ultimately help to lower the premium rates for EC insurance policies. More details are provided in paragraphs 36 to 41 below.

**(b) “Refusal of underwriting EC insurance for some sectors”**

5. Hong Kong has an open insurance market. At present, there are about 70 insurers authorized to write EC insurance business. Having said so, we are mindful of the need to provide assistance to employers who face genuine difficulties in obtaining EC insurance.

6. In 2002, the Labour Department (LD) received requests for assistance from 12 employers who encountered difficulty in obtaining EC insurance coverage. In the first three months of 2003, LD received 19 such requests. These employers are mostly small and medium-sized establishments with employment size of not more than 20. Most of them are from industries with relatively higher risk exposure, such as engineering (involving work at construction sites), transportation and marine-related operations (such as diving, ship repairing, re-fueling, etc.).

7. LD has approached the Accident Insurance Association (AIA) and the General Insurance Council of the Hong Kong Federation of Insurers (HKFI) as well as the two insurance brokers associations<sup>1</sup> to explore ways of helping employers who have difficulty in obtaining EC insurance. According to these bodies, the situation is mainly attributable to:

- (i) heavy losses suffered by insurers in underwriting EC insurance in recent years; and
- (ii) limited capacity for insuring certain risks such as marine operations resulting from restrictions imposed by reinsurers.

8. Having obtained the assistance of OCI and the insurance brokers associations, LD has compiled a list of insurance brokers who specialise in EC insurance. These insurance brokers, who represent the interests of the policyholders (i.e. employers in the case of EC insurance), should be in the position to help employers search for appropriate EC insurers. LD has passed the list of insurance brokers to employers who request assistance so that they could seek professional assistance. We understand that most of these employers have been able to take out an EC insurance policy eventually.

9. LD is currently exploring with construction contractors the possibility of grouping a number of small contractors to negotiate collectively with insurers through the brokers for EC insurance coverage.

10. Furthermore, CI has written to all EC insurers recently appealing them to offer coverage when they are in a position to do so.

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<sup>1</sup> The two insurance brokers associations are:

- (i) Professional Insurance Brokers Association Limited; and
- (ii) The Hong Kong Confederation of Insurance Brokers

**(c) “Delaying tactic in renewal of policy”**

11. As OCI understands it, the general practice of EC insurers is to give about one-month's notice to policyholders regarding renewal of policies. Sometimes, a shorter notice is given because of the time taken for seeking the necessary reinsurance coverage or in re-assessing the risks, which can be affected by changes in the market. In his letter to EC insurers (see paragraph 10 above), CI has also appealed to EC insurers to give sufficient advance notice to policyholders if they do not intend to renew the policy, to terminate or cancel the policy, or to renew the policy with significant change in premium level or terms and conditions.

12. On the part of employers, LD has been reminding them of the need to act well in advance in preparing for renewals instead of waiting for the insurer or the insurance intermediary to start the process of renewing an insurance policy. Since November 2002, LD has included messages in its departmental newsletter and seminars for employers on the importance of taking early action to contact insurance brokers or insurers for renewal of EC insurance policy. The web sites and addresses of HKFI and the two insurance brokers associations are also provided to facilitate liaison for assistance.

**(d) “Collusion/sharing of customer information by the insurance companies”**

13. Insurers are bound by the Personal Data (Privacy) Ordinance (Cap. 486) and the HKFI had issued guidelines to facilitate its members to comply with the relevant statutory requirements. OCI is not aware of any sharing of policyholders' information among insurers, except for risk assessment purposes and, where necessary, after obtaining the consent of the concerned

policyholders.

**(e) “Lack of transparent mechanism for determining risk level and premiums”**

14. In general, an EC insurer determines the risk level and premiums based on various factors such as the characteristics of the risks concerned, its past claims experience, its reinsurance protection and financial capability, as well as the prevailing market situation.

15. OCI attaches great importance to further enhancing the transparency of the EC insurance market which, we believe, would facilitate premium setting by EC insurers and help policyholders to better understand the state of the industry. The Office will be publishing the underwriting statistics of EC insurers to be broken down into ten occupational types commencing with the statistics relating to the financial year ended 31 December 2002.

## **II. Employees’ Compensation**

**(a) Employees’ Compensation Ordinance**

16. The Employees’ Compensation Ordinance (ECO) provides for payment of compensation to employees who are injured in the course of their employment, regardless of whether the injury is caused by the negligence, breach of statutory duty or other wrongful act or omission of the employer, or of any person for whose act of default the employer is responsible.

17. To ensure that employees will be able to receive compensation and to protect employers when they are liable for the payment of compensation or damages, the ECO requires employers to purchase EC insurance with an insurer

authorized under the Insurance Companies Ordinance<sup>2</sup> to underwrite such line of business. There are about 70 authorized insurers who carry on EC insurance business.

**(b) Employer's liability for statutory claims and common law damages**

18. There are comments that the EC underwriting losses are partly attributable to the current system of allowing an injured employee to claim both statutory compensation and common law damages against the employer. It is a fact that the ECO does not limit or in any way affect any civil liability of the employer independent of the Ordinance. However, section 26(1) of the Ordinance sets out that any damages awarded against an employer in an action at common law shall be reduced by the value, as decided by the Court, of any compensation which has been paid or is payable under the ECO in respect of the injury sustained by the employee.

19. Given the above offsetting provisions in the ECO, injured employees do not receive double benefits. It should also be noted that an injured employee is awarded damages only when he has proved negligence or fault on the part of the employer. An employer who does not breach his duty of care will not be liable to pay common law damages to the employee.

20. Furthermore, the right of a party to claim common law damages against another party for wrongful action has been a well-established part of Hong Kong's legal system. An injured employee's right to claim damages under the common law should not be restricted without good cause and full justification. Moreover, the common law right is applicable to all personal

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<sup>2</sup> Under the ECO, the following two types of bodies may also underwrite EC insurance:

- (i) an association of underwriters approved by the Insurance Authority under the Insurance Companies Ordinance; and
- (ii) the society of underwriters known in the United Kingdom as Lloyd's.

injury claims, of which work injury cases are only a sub-group. Any move to limit such right, which would have far-reaching and wide implications, should be handled with great care.

**(c) Suggestion of setting up a central EC system**

21. There have been suggestions for the establishment of a central EC system to resolve the high EC premium charged on employers of some sectors. It is understood that insurers generally take into account a number of factors, including the risks of accident, past claims experience, prevailing market situation etc., in deciding the level of insurance premium. The same factors would still have to be applied in assessing the insurance premium, albeit under a central EC system. Therefore, the suggestion could not be the solution to high insurance premium.

22. Furthermore, a system of decentralised private insurers is more flexible than a centralised insurance scheme in sharing risks and attracting investments in the global capital market. A decentralised system is also more efficient and cost effective than a central system which would operate under a monopolistic environment.

23. As mentioned in the meetings of the LegCo Panel on Financial Affairs in January and March 2003, the general insurance market in Hong Kong and in the world is currently beset by unfavourable factors such as the sluggish economy and weak investment returns. A centralised insurance arrangement cannot resolve these problems and the resultant increases in insurance premium.

24. Indeed, there is no justification for making fundamental changes to the current system of private insurers and replacing it by a centralised EC system.

**(d) Protection to ‘self-employed persons’ and requiring employees to take out insurance**

25. Genuine self-employed persons are not covered by the ECO. However, employers could not evade their liabilities under the ECO by simply labelling employees as “self-employed persons”. Reference has to be made to the substantive facts of the case to determine the existence of employment relationship. This is borne out by court judgements.

26. Nevertheless, LD is aware of the concerns of employees in respect of their protection under the ECO and has discussed the issue with the insurance industry. After a series of discussion, it has reached an understanding with the insurance industry that insurers would take account of all circumstances of the case, rather than just the status of a worker under the Mandatory Provident Fund Scheme, when determining whether an injured worker is an employee or a self-employed person for the purposes of the ECO.

27. The HKFI has already incorporated this understanding into their Code of Best Practice for Employees’ Compensation Insurers in March 2003. LD has also issued a letter to EC insurers promulgating the factors which have been commonly adopted by the Court in determining the employment status of workers. This should help to clarify the status of injured workers who are labelled as self-employed persons but are bona fide employees according to the facts of the relationship, thereby reducing unnecessary disputes. Those factors include:

- (a) financial risk to be borne;
- (b) responsibility for investment and management;
- (c) possibility of profit via effective management;
- (d) overall control of the work to be performed;



- (e) ownership of tools and equipment for carrying out the work;
- (f) agreement for a complete work to be paid by a fixed sum (although this also sometimes happen in employer/employee relationship); and
- (g) responsibility and power to hire and fire workers.

28. As regards the suggestion of requiring employees to take out insurance cover against work injury for themselves, it is not compatible with government policy that the employer should be liable to compensate the employee for injuries or death sustained in an accident that arises out of and in the course of employment.

### **(e) Statutory Compensation**

#### **(i) Prolonged sick leave**

29. There are comments that some injured employees abuse the EC system by taking prolonged sick leave. We do not agree that there are serious abuses in this respect. The granting of sick leave, which is a period of absence from duty, is determined and certified to be necessary by medical practitioners in accordance with their professional judgement. For EC cases settled in 2002, about 74% were granted certified sick leave of less than 30 days. The number of those cases with certified sick leave of a period between 30 days to less than six months accounted for only 20% of the total number of these settled cases.

30. LD has also adopted an administrative procedure whereby its staff would, amongst other purposes, go through the sick leave certificates produced by injured employees. In the event that doubts are raised on any sick leave period, accident information would be sought from the employee and employer.

Checks against medical reports from treating doctors would also be made.

**(ii) Determination of earnings in calculating amount of compensation**

31. A written submission to the Panel has queried the wage statistics used in determining the employee's earnings for the purpose of calculating compensation. In fact, ECO has clear provisions for such purpose. Under section 3 of the ECO, "earnings" is defined as any wages paid in cash to the employee by the employer and any privilege or benefit which is capable of being estimated in money, including any overtime payments or other special remuneration for work done. The ECO also provides that for the purposes of calculating compensation, the monthly earnings of an employee at the time of the accident shall be the earnings:

- (a) for the month immediately preceding the date of the accident; or
  - (b) computed in such manner as is best calculated to give the rates per month at which the employee was being remunerated during the previous 12 months if he has been so long employed by the same employer, but, if not, then for any lesser period during which he has been employed by the same employer,
- whichever calculation is more favourable to the employee.

32. For the construction industry, the majority of disputes over the earnings of injured employees arise because employers concerned have not kept proper wage and attendance records. Through written publications, seminars and meetings with contractors and trade unions, LD has repeatedly urged employers and construction workers to keep proper wage and attendance records and to submit such information to LD and their insurers for the

processing of an EC case. With such records, there should be less difficulty in applying the relevant provisions of the law to determine the earnings of an injured employee for calculating the amount of compensation.

### **(iii) Legislative amendments**

33. There are comments that the legislative amendment on the settlement of fatal accidents at work has led to higher compensation. In August 2000, the ECO was amended to improve the settlement of compensation claims in fatal cases. One of the amendments was to make compensation for death payable to family members, rather than dependants, of the deceased employees. The objectives were to streamline the settlement of fatal cases and to improve the compensation for death.

34. In 2002, a total of 228 fatal cases were reported to LD. It only accounted for a small percentage of the total number of 59 448 reported EC cases in the year. In terms of compensation, the payout for fatal cases settled in 2002 accounted for only 7.11% of the total amount of compensation for all EC cases settled in 2002. For 2000, before the provisions were amended, the corresponding figure was 6.54%. Therefore, the increase in compensation payout due to the amendment is insignificant.

35. The legislative amendments introduced in August 2000 also provided an additional avenue where compensation claims in fatal accidents can be determined by the Commissioner for Labour if there is no dispute by employer and employee. Prior to the amendment, all claims in fatal accidents were determined by the Court. This amendment helps to save legal costs which in turn could have beneficial effect on the overall payouts made by insurers in statutory EC claims.

### **III. Work Place Safety and Rehabilitation of Injured Workers**

#### **(a) Work Place Safety**

36. Better risk management and reduction in work accidents should be helpful to individual employers in negotiating EC insurance premium with insurers. In this respect, LD has been promoting risk assessment and good occupational safety and health practices to help employers reduce or prevent occupational accidents. Employers who have invested in safety management should inform their insurers of the measures adopted when they take out or renew the EC insurance policy so that insurers could take this factor into account when determining the premium level.

37. Through a wide spectrum of activities such as seminars, safety training, publications and advertisements, LD disseminates information on occupational safety and health to employers and employees. In 2002, two territory-wide safety award schemes were organised for the construction and catering industries respectively. These two award schemes featured a series of activities and an open competition to give recognition to those employers and employees with good safety performance in the industries concerned. With a view to sustaining the efforts to build up a strong safety culture in these two high-risk and accident-prone industries, LD will continue to organise the award schemes in 2003.

38. The LD also places great emphasis on the establishment of safety management systems by individual employers. The Factories and Industrial Undertakings (Safety Management) Regulation, which came into operation on 1 April 2003, requires proprietors in certain high-risk industries and certain contractors in the construction industry to adopt a safety management system and to conduct regular safety audits to ensure that their safety management

system is implemented effectively and efficiently. The Department also adopts focused enforcement strategy to tackle companies/contractors with poor safety performance. Special operations and campaigns are organised in response to accident trends and special problems.

39. Case management by the employer and the insurer after an accident has occurred is also important in preventing future accidents and in ensuring that proper attention is given to the injured employees. To facilitate early injury management, LD launched a scheme in June 2002 to provide timely information on work-related accidents which involve back injuries and multiple injuries to participating insurers on a weekly basis. More than 50 insurers have subscribed to take part in the Scheme. With such information, insurers should be able to contact the employers concerned to work out appropriate follow-up measures with regard to the management of the claims.

#### **(b) Rehabilitation for injured employees**

40. In March 2002, LD also initiated the Voluntary Rehabilitation Programme for Work Injuries in the Construction Industry with a view to providing timely rehabilitation services to injured workers in the construction industry for better and speedier recovery, and to facilitate their safe and early return to work. It is expected that the Programme, which is run on a pilot basis, shall have positive effect on the recovery and rehabilitation of injured employees, and would help to reduce the claim costs borne by insurers in the long run.

41. Since rehabilitation would involve close co-operation of doctors, rehabilitation professionals, injured employees, employers and insurers, and Hong Kong does not have much experience in this area, the pilot programme is a good opportunity for us to consider the practical experience and its

effectiveness. We do not consider it appropriate to make the rehabilitation programme for injured employees a mandatory requirement at this stage.

## **IV. Others**

### **(a) Terrorism Facility**

42. A body from the construction sector suggested that the “Government Terrorism Facility Charge” should be abolished. For this, Members may wish to note that since the “911” events, reinsurers worldwide have ceased to provide reinsurance cover for terrorist activities on a treaty basis<sup>3</sup>. To ensure that employers and employees will continue to be able to enjoy EC insurance protection, and with the approval of the Finance Committee of LegCo, the Government established on 11 January 2002 a \$10 billion facility covering terrorism risks in respect of EC insurance business. Participation in the scheme is voluntary for EC insurers. In return for the protection provided by the facility, EC insurers participating in the scheme are required to pay to the Government a charge of 3% of the gross premium of the EC policies they underwrite. It is a commercial decision of individual insurers as to whether, and if so to what extent, this charge would be passed on to other parties. The current arrangement is considered reasonable. We have made it clear that we will withdraw the facility once the relevant reinsurance cover has returned to the market<sup>4</sup>. Towards this end, OCI will continue to closely monitor the reinsurance market.

### **(b) Compensation awarded by the courts**

43. In its written submission to the FA Panel, a professional body,

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<sup>3</sup> Refers to standing facilities for reinsurance coverage on all businesses accepted by direct insurers during the year of the treaty without individual assessment of the risks

<sup>4</sup> So far, there is still no sign for such return.

among other things, expressed concerns on the escalating trend of damages for compensation awarded by the Court both for employee claims and for other personal injury litigations. It also believes that there was evidence of inconsistency of awards by the Courts, inflation of claims of loss of earnings and the use of statistics produced by the Census and Statistics Department which were allegedly out of date.

44. According to the Judiciary Administrator, the award of damages depends on the particular circumstances and the facts of individual cases. Damages are not awarded without a proper assessment, which in turn depends on proper evidence by the parties. The claims for loss of earnings are found in pleadings drafted by the lawyers. In assessing damages, evidence of loss of earnings will be examined by the Court. Statistics produced by the Census and Statistics Department are some of the evidence used by the Court. It will be for the parties to address the Court on the issue if the statistics are considered out of date and unreliable. And the Court will decide on the use of them. The final award is determined upon the case's own merits. The decision in each case is a judicial decision. There is always the avenue of appeal open to the aggrieved party if he considers the assessment improper.

### **(c) Granting of legal aid**

45. Some parties suggested that the right of workers from other places to obtain legal aid to make EC claims should be restricted.

46. The Administration's policy as regards legal aid for civil cases is to ensure that those people who have reasonable grounds for pursuing or defending a civil legal case is not prevented from doing so by a lack of means. Applicants for civil legal aid are therefore subject to means and merit tests. Article 14(1) (read with Article 2(1)) of the International Covenant on Civil and

Political Rights (ICCPR) guarantees that all persons within the territory and jurisdiction of Hong Kong are equal before the Courts and tribunals. Article 26 of the ICCPR further provides that all persons are equal before the law and are entitled to the equal protection of the law without any discrimination on any ground such as race, national or social origin, birth or other status. The Administration considers that it is in the interests of justice and in line with the ICCPR as applied to Hong Kong not to impose any residency restrictions on applicants for civil legal aid.

**Financial Services and the Treasury Bureau**

**Economic Development and Labour Bureau**

**Labour Department**

**Office of the Commissioner of Insurance**

**19 May 2003**



For information  
on 15 March 2003

**Legislative Council Panel on Financial Affairs**  
**Meeting on 15 March 2003**

**Insurance Coverage for Various Business Sectors**

**Introduction**

At the meeting of the LegCo Panel on Financial Affairs held on 16 January 2003, Members considered the Information Paper entitled “Business environment of the Hong Kong insurance industry and the difficulties encountered by some professional and business sectors in obtaining insurance coverage”. This paper updates the position in respect of matters mentioned in that Information Paper.

**Background**

2. There are two major types of mandatory insurance in Hong Kong: insurance in respect of employees’ compensation (EC) and motor vehicle third party risk in relation to death or bodily injury. The requirements in respect of these two types of compulsory insurance are set out in the relevant Ordinances. All employers, except for the Government, are required to obtain EC insurance cover for their employees. Depending on the nature of business activities, employers may need to obtain additional types of insurance cover. For example, employers in the transport business using motor vehicles would need to obtain cover for their motor vehicle third party risk. EC and motor insurance together takes up a significant portion of the general insurance market in Hong Kong for

they amount to some 22% and 16% of the market in 2002.

3. Hong Kong has one of the most open insurance markets in the world. As at the end of January 2003, there were 194 insurers authorized to carry on insurance business in Hong Kong. Among these, 148 were authorized to carry on general insurance business.

4. The Hong Kong general insurance industry, similar to that in many other places, has been hit by the sluggish economy, shrinkage of investment returns and keen competition. The hardening of the market has led to increase in premium level, around 20% in 2002 in terms of total gross premium. Hong Kong's situation is not unique. Premium for general insurance in most other advanced economies (e.g. Australia, US, UK and Singapore) has also increased substantially and the trend is likely to continue. General insurers have also adopted a more conservative approach in underwriting policies, for example, stepping up risk assessment. Details of the business environment of the Hong Kong insurance industry is set out in the Information Paper discussed at the \_\_\_\_\_ Panel meeting on 16 January 2003, copy at Attachment A.

5. In 2002<sup>1</sup>, the Hong Kong general insurance industry recorded an underwriting profit of HK\$1,125 million, turning around losses for five consecutive years, which totaled HK\$3,487 million.

### **EC and Motor Insurance**

6. The latest statistics on the gross premium and underwriting performance of EC and motor insurance direct business<sup>2</sup> are set out in \_\_\_\_\_ Attachment B. In 2002, EC and motor insurance recorded a 50.7% and 7.2%

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<sup>1</sup> All figures of the premium levels and underwriting results in 2002 are provisional figures.

<sup>2</sup> This means that reinsurance inward business accepted by direct insurers and reinsurers is not included

increase in gross premium. While the increase has helped improve the underwriting performance of motor insurance direct business, which showed an underwriting profit of HK\$24.7 million for the first time since 1996 (yet an underwriting loss of HK\$79.6 million recorded for overall motor insurance), EC insurance direct business still incurred underwriting losses of HK\$323.3 million.

### **Difficulties in Obtaining Insurance Coverage**

7. Against the background of the hardening of the general insurance market, some transport trades (e.g. public light bus and taxi) and employers of specific sectors (e.g. diving industry) have complained that they have difficulties in obtaining the required EC and/or motor insurance cover. In some cases, the complaints relate more to the level of premium, rather than a supply problem.

8. As mentioned in the paper at Attachment A, the situation of the insurance market in Hong Kong is not unique. Insurance business is a risk-assessing and pricing business. Hong Kong has an open insurance market and there is no barrier for new qualified companies to enter the market. We believe that the level of premium rates should best be left to market forces.

9. The recent increase in premium should also be read in the context of the keen competition in the market in the past few years. Between 1996 and 1999, average premium rate for EC insurance dropped by 22% (non-construction EC business) and 28% (construction EC business), despite that in the same period claims had increased significantly. As for motor insurance, information provided by several major insurers<sup>3</sup> regarding their underwriting

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<sup>3</sup> These insurers together have around 90% share in the motor insurance market.

performance in the past three years in respect of taxi and public light bus is set out in Attachment C. It illustrates the level of losses incurred by insurers in covering these types of vehicles. According to the statistics of the Police, the accident rates in respect of taxi and public light bus for the years 2000 to 2002 are 20% and 25% respectively, which are much higher than the 2% accident rate of private cars during the same period. Obviously, the higher the risk accepted by insurers, the higher the premium policyholders would have to pay.

### **Actions by OCI**

10. The Administration is mindful of the need to provide assistance to those who face genuine difficulties in obtaining compulsory insurance. Towards this end, the Office of the Commissioner of Insurance (OCI) has been liaising with the associations of insurance brokers (who are specialists in finding the appropriate insurance for their clients) and the Hong Kong Federation of Insurers (HKFI). In the past two years, the OCI has received a total of 24 complaints about the difficulties in obtaining insurance coverage. With the assistance of the relevant Government departments, insurers and industry bodies, all complaints had been resolved. Moreover, OCI will continue to ensure that insurers operate in a business-friendly and open environment, so that they can react to market demand more effectively and efficiently.

11. We also attach great importance to market transparency. In this regard, starting with the financial year ended 31 December 2002, OCI will publish underwriting statistics of EC insurers in respect of ten broad occupation types. This should facilitate premium setting by insurers and help policyholders to better understand the state of the industry.

12. The Administration will also continue its efforts on promoting road and occupational safety, as well as other measures, such as facilitating the early rehabilitation of injured employees, which would ultimately help to lower the premium rates for EC and motor insurance policies.

**Financial Services and the Treasury Bureau/OCI**

**March 2003**

For information  
on 16 January 2003

**Legislative Council Panel on Financial Affairs  
Meeting on 16 January 2003**

**Business environment of the Hong Kong  
insurance industry and the difficulties encountered by  
some professional and business sectors in obtaining insurance coverage**

**Introduction**

This paper sets out the present business environment of both the worldwide and Hong Kong general insurance markets as well as the Administration's response to the matters raised by the Honourable Bernard Chan regarding the difficulties encountered by some professional and business sectors in obtaining insurance coverage.

**Business Environment**

*Worldwide General Insurance Market*

2. In the international scene, the last two years have been very stressful for the general insurance industry, particularly the reinsurance industry. Insurance capacity has contracted due to a combination of weak investment returns, keen competition among insurers and unprecedented losses. In 2001, worldwide general capital funds in the insurance industry decreased by about US\$90 billion. The contraction for 2002 was projected to be approximately

the same amount if the current state of stock markets continues. This would mean some US\$180 billion, or 25%, decrease in global capital funds of the general insurance industry since early 2000. The about US\$30 billion new capital infused after the 911 events has not been enough to make up for the decrease. Apart from a shrinking in capital fund, the 911 events in the United States (US) in 2001 had caused an estimated US\$50 – 70 billion loss to general insurers worldwide.

3. As a result, insurers worldwide have raised their premium rates, particularly in commercial lines and reinsurance business. Moreover, they have become more conservative in underwriting risks. The hardening of the international insurance market is projected to continue in 2003, given the global shortage of quality capital for the insurance sector and increased risk exposures after the 911 events.

#### *Hong Kong Insurance Market*

4. Hong Kong has one of the most open insurance markets in the world. As at 30 November 2002, there were 197 insurers authorized to carry on insurance business in Hong Kong. Among these, 150 were authorized to carry on general insurance business. The Hong Kong general insurance industry, similar to that in many other countries, has been hit by the sluggish economy, shrinkage of investment returns and keen competition. The overall underwriting loss of general insurers amounted to HK\$1,379 million, HK\$872 million and HK\$473 million in 1999, 2000 and 2001 respectively. For the first nine months of 2002, the general insurance industry recorded an underwriting profit of HK\$604 million.

## *EC Insurance Business*

5. As at 30 November 2002, there were 73 authorized insurers writing Employees' Compensation (EC) insurance business in Hong Kong. In the past few years, EC insurance business had experienced continuous and significant underwriting losses. The underwriting loss for this statutory line of business was HK\$1,370 million in 1999, HK\$1,091 million in 2000, HK\$1,039 million in 2001 and HK\$315 million for the first nine months in 2002. Such losses are attributable to inadequate premium rate, an intensely competitive and fragmented EC insurance market, and substantial increase in common law damages and statutory benefits.

6. In the light of the significant underwriting losses and in response to the suggestion of the industry, in December 2000 the Office of the Commissioner of Insurance (OCI) conducted an industry-wide survey to gauge the performance of EC insurance business in two areas, i.e. construction and non-construction businesses. The survey revealed that for construction EC business, the underwriting result deteriorated by 487% from a loss of HK\$98 million in 1996 to a loss of HK\$576 million in 1999. Over this 4-year period, the number of claims reported increased by 20%. The average amount paid per claim increased by 91% and the amount of the largest claim settled increased by 90% (up to HK\$14 million in 1999). On the other hand, the average premium rate dropped by 28% in the same period.

7. As for non-construction EC business, the underwriting result deteriorated by 1,673% from a loss of HK\$42 million in 1996 to a loss of HK\$740 million in 1999. Over the period, the number of claims reported increased by 37%, the average amount paid per claim increased by 19% and the amount of the largest claim settled increased by 40% (up to HK\$21 million in



1999). On the other hand, the average premium rate dropped by 22% in the same period.

8. The results of the OCI's survey show that during the relevant period while the claims had risen substantially, both in terms of number and amount, the premium rate had on the contrary dropped by 28% and 22% in respect of construction and non-construction EC business respectively. This underlines how competitive the market had been.

9. With the amount of losses and against the background of developments in the global market highlighted above, Hong Kong EC insurers raised the premium. For the first nine months of 2002, EC insurance business recorded an increase of 33% in gross premium. Moreover, many insurers had stepped up their risk management in underwriting EC insurance policies, for example, requiring the wage roll of employers to be certified and to have more regard to the safety measures at the work place in setting the premium. These measures have improved the underwriting performance of this line of business with the underwriting loss reduced from HK\$421 million for the first 9 months of 2001 to HK\$315 million for the same period in 2002.

#### *Motor Insurance Business*

10. As at 30 November 2002, there were 68 authorized insurers writing motor insurance business in Hong Kong. Motor insurers in Hong Kong had also suffered heavy underwriting losses in recent years: HK\$166 million in 1999, HK\$407 million in 2000 and HK\$108 million in 2001. The main reasons for such losses are inadequate premium rate and increase in compensation. From 1996 to 2001, the average premium per vehicle had fluctuated between \$5,067 and \$5,797. Relevant statistics are at Annex.

## **Market Outlook**

11. Despite the losses incurred by the general insurers in the statutory lines of business, they are compensated by profits in other profitable business, and other pre-financing arrangements such as new capital injection. Moreover, the Insurance Authority imposes stringent solvency and asset requirements for general insurers. The overall insurance industry is financially sound.

## **Difficulties in obtaining insurance coverage**

12. The Hong Kong insurance industry is not immune to problems faced by the global market, including the tight reinsurance capacity available. In addition, the increasing amount of court award for personal injury has increased the operating costs of insurers. In light of the difficult business environment, particular in the case of general insurance, insurers have increased premium rates and tightened underwriting measures.

13. The hardening of the general insurance market has drawn a number of complaints from the insuring public, mainly motorists and employers of specific sectors. For EC insurance, the complaints are mostly related to smaller companies in the construction, engineering and diving sectors. For motor insurance, they are mostly related to motor cycles, public light buses (PLB) and taxis. In the past two years, the OCI received a total of 24 such complaints. In some cases, the complainants faced genuine difficulties in obtaining insurance coverage. In other cases, the issue was related more to the level of premium rates. With the assistance of the relevant Government department and the insurers, all complaints had been resolved.

14. As mentioned in paragraphs 2 to 4 above, given the global development,

the current business environment and the losses in the past, insurance premium would remain high. This is not inconsistent with the worldwide trend. Insurance business is a risk-assessing and pricing business. Hong Kong has an open insurance market and there is no barrier for new qualified companies to enter the market. We believe that the level of premium rates should be best left to market forces. In line with the practice in other jurisdictions with a well-developed insurance market (UK, Australia and Singapore), OCI does not interfere with premium setting by insurers. OCI is debarred under section 26(3A) of the Insurance Companies Ordinance from intervening into the premium setting by insurers.

15. For persons facing genuine difficulties in obtaining insurance coverage, they may seek the assistance of brokers, who are specialists in finding the appropriate insurance for their clients. In this regard, the OCI has been in close liaison with the two broker associations and has drawn up a list of brokers for public inspection. Moreover, a list of brokers who may help employers in securing EC insurance is now available at the Labour Department. In the longer term, the Administration will explore the feasibility of encouraging employers from a specific sector to purchase EC insurance on a collective basis.

16. The Administration will continue to ensure that insurers operate in a business-friendly environment and on a level-playing field. We will also work closely with relevant stakeholders to promote road and occupational safety, which would ultimately help to lower the premium rates for motor and EC insurance policies.

**Financial Services and the Treasury Bureau/OCI**

**January 2003**

**Motor Insurance Market (Direct Business)**

|                           | Total gross premium<br>(\$ <i>billion</i> ) | Underwriting performance<br>(\$ <i>million</i> ) | No. of vehicle covered | Average premium per vehicle (\$) |
|---------------------------|---|--|------------------------|----------------------------------|
| 1996                      | 2.69  | (82.7)   | 496 266                | 5 426                            |
| 1997                      | 2.81  | (346.3)  | 484 922                | 5 797                            |
| 1998                      | 2.78  | (383.9)  | 489 393                | 5 674                            |
| 1999                      | 2.35  | (176.3)  | 456 006                | 5 144                            |
| 2000                      | 2.47  | (324.9)  | 448 368                | 5 508                            |
| 2001                      | 2.77  | (121.0)  | 546 072                | 5 067                            |
| 2002 ( <i>Jan-Sept</i> )* | 2.23  | (80.4)   | N/A                    | N/A                              |

\*: Provisional figures.

**EC Insurance Direct Business Market**

|      | Total gross premium<br>(\$ <i>billion</i> ) | Underwriting performance<br>(\$ <i>million</i> ) | No. of policies<br>in force | Average premium per<br>policy (\$) |
|------|---|--|-----------------------------|------------------------------------|
| 1996 | 2.31  | (130.7)  | 220 477                     | 10,473                             |
| 1997 | 2.54  | (283.8)  | 246 977                     | 10,276                             |
| 1998 | 2.08  | (730.2)  | 238 148                     | 8,736                              |
| 1999 | 2.13  | (1,370.0)  | 233 947                     | 9,102                              |
| 2000 | 2.46  | (1,091.4)  | 226 141                     | 10,897                             |
| 2001 | 2.70  | (1,039.0)  | 225 048                     | 12,012                             |
| 2002 | 4.07  | (323.3)  | Not available               | Not available                      |

**Motor Insurance Direct Business Market**

|      | Total gross premium<br>(\$ <i>billion</i> ) | Underwriting performance<br>(\$ <i>million</i> ) | No. of vehicles<br>covered | Average premium per<br>vehicle (\$) |
|------|---|--|----------------------------|-------------------------------------|
| 1996 | 2.69  | (82.7)   | 496 266                    | 5,426                               |
| 1997 | 2.81  | (346.3)  | 484 922                    | 5,797                               |
| 1998 | 2.78  | (383.9)  | 489 393                    | 5,674                               |
| 1999 | 2.35  | (176.3)  | 456 006                    | 5,144                               |
| 2000 | 2.47  | (324.9)  | 448 368                    | 5,508                               |
| 2001 | 2.77  | (121.0)  | 546 072                    | 5,067                               |
| 2002 | 2.97  | 24.7   | Not available              | Not available                       |

Note: Figures in the above tables cover direct business only, i.e. reinsurance inward business accepted by direct insurers and reinsurers is not included.





### Underwriting Performance of Taxi Insurance

|   | 2000                        |                               | 2001                        |                               | 2002                        |                               |
|---|-----------------------------|-------------------------------|-----------------------------|-------------------------------|-----------------------------|-------------------------------|
|   | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M |
| Gross premiums  | 35.5                        | 77.7                          | 21.1                        | 152.1                         | 26.4                        | 186.9                         |
| Net earned premiums <sup>4</sup> (a)                  | 26.9                        | 56.7                          | 13.4                        | 90.8                          | 19.5                        | 131.5                         |
| Net commissions payable (b)                           | 4.4                         | 9.4                           | 3.0                         | 21.4                          | 4.1                         | 25.6                          |
| Net claims incurred <sup>5</sup> (incl.IBNR)(c)       | 41.4                        | 55.5                          | 19.7                        | 58.1                          | 37.4                        | 109.0                         |
| Management expenses <sup>6</sup> (d)                  | 2.1                         | 4.3                           | 1.6                         | 11.8                          | 1.8                         | 11.9                          |
| Underwriting Profit/(Loss)<br>[(a) – (b) – (c) – (d)] | (21.0)                      | (12.6)                        | (11.0)                      | (0.5)                         | (23.8)                      | (15.0)                        |

<sup>4</sup> Means the net amount after deducting: (i) premiums for reinsurance ceded from the gross premiums; and (ii) the amount set aside by an insurer at the end of its financial year out of premiums in respect of risks to be borne by the insurer after the end of the financial year under the relevant insurance contracts.

<sup>5</sup> The gross claims incurred after deduction of recoveries from reinsurers and other parties.

<sup>6</sup> Expenses incurred in the administration of an insurer or its business which are not commissions payable and, in the case of general business, are not included in claims paid, claims outstanding, expenses for settling claims and expenses for settling claims outstanding.



### Underwriting Performance of Public Light Bus Insurance

|   | 2000                        |                               | 2001                        |                               | 2002                        |                               |
|---|-----------------------------|-------------------------------|-----------------------------|-------------------------------|-----------------------------|-------------------------------|
|   | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M | Third Party<br>Cover<br>\$M | Comprehensive<br>Cover<br>\$M |
| Gross premiums  | 27.1                        | 23.4                          | 67.5                        | 27.3                          | 78.0                        | 32.3                          |
| Net earned premiums (a)                               | 24.8                        | 20.3                          | 49.5                        | 19.9                          | 50.9                        | 23.1                          |
| Net commissions payable (b)                           | 6.6                         | 5.4                           | 16.9                        | 6.9                           | 9.5                         | 4.5                           |
| Net claims incurred (incl.IBNR)(c)                    | 28.3                        | 51.4                          | 29.4                        | 50.4                          | 53.0                        | 53.7                          |
| Management expenses (d)                               | 1.6                         | 1.5                           | 4.6                         | 1.9                           | 3.6                         | 1.7                           |
| Underwriting Profit/(Loss)<br>[(a) – (b) – (c) – (d)] | (11.7)                      | (38.1)                        | (1.4)                       | (39.3)                        | (15.1)                      | (36.8)                        |