

**Information Note for the
Legislative Council Panel on Financial Affairs**

**Measures to Strengthen the Supervision
on Assets of Long Term Insurers in Hong Kong**

Purpose

This paper sets out a package of enhancement measures implemented or being planned for in order to strengthen the supervision on assets of long term insurers in Hong Kong.

Background

2. Historically, supervision of assets held by long term insurers in Hong Kong is predicated on a system whereby the Appointed Actuary performs a “gate-keeper” role in investigating and commenting on the financial status of each insurance company. Despite the robustness of this system, there is a perceived concern on whether the assets in question are valued on a prudent and uniform basis as well as on the need for greater vigilance in asset-liability matching under evolving market conditions.

Enhancement Measures

3. With a view to strengthening its present supervisory framework and to addressing these perceived concerns, the Office of the Commissioner of Insurance (“OCI”) has promulgated two sets of guidance notes setting out respectively, specific duties borne by the board of directors of insurance companies in ensuring that independent risk management functions, effective internal control, written investment mandates and asset valuation/safeguarding procedures are in place, as well as requirements on asset management, risk control systems and reporting framework. As a result, the general awareness and internal capability of long term insurers for sustainable operation have increased.

4. On the other hand, OCI has introduced a new requirement for insurers to segregate for reporting purpose the share of assets held by them which are attributable to local policyholders and deployed Dynamic Solvency Testing as a tool to assess the impact of different economic scenarios. These initiatives are intended to facilitate accurate identification and continuous monitoring of assets on which local policyholders have a legitimate claim as well as to improve the sophistication of stress testing and sensitivity analysis.

5. Going forward, OCI will incorporate checking for compliance with various enhancement measures into its regular on-site inspections. OCI will liaise with professional bodies, notably the Actuarial Society of Hong Kong, to review prevailing professional standards as necessary. In respect of off-site monitoring, long term insurers have been subjected for some time on a trial basis to submission of supplementary returns covering asset/liability valuation, investment yield, valuation interest rate, guarantees and options reserve, currency mismatching reserve and risk assessment models. This practice will be formalised to build up a database for effective oversight.

Looking Ahead

6. Most enhancement measures described in this paper are in line with the findings of the Consultancy Study on Supervisory Framework of the Assets of Long Term Insurers in Hong Kong (“the Study”) which was completed in 2007. The Study noted that whilst local policyholders could not be shielded completely from potential difficulties faced by a long term insurer incorporated overseas and that there was no universally accepted approach for investment restrictions or admissibility, internal management control and stress testing, there is a growing popularity of risk based capital (“RBC”) supervisory regimes that determine solvency requirements by reference to the unique risk profile of each individual insurer. International deliberations are converging towards Solvency II pioneered by the European Union with a three-pillar structure similar to the Basel II Accord focusing on capital adequacy, supervisory review and disclosure. This model could

herald a common solvency standard spearheaded by the International Association of Insurance Supervisors¹ (“IAIS”) which is intended for global implementation in 2012.

7. In this light, OCI has taken steps to keep track of progress achieved at relevant IAIS fora and evaluate carefully proposed changes that may affect Hong Kong. Meanwhile, OCI will explore other measures to strengthen the present supervisory framework.

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¹ The IAIS was established in 1994 to promote cooperation amongst insurance supervisors and other financial sector supervisors with a view to contributing to improved supervision of the insurance industry and thus global financial stability. According to its Annual Report 2006-07, its members include insurance regulators and supervisors from over 190 jurisdictions including Hong Kong.