

Consumer Council
Submission to the LegCo Panel on Financial Affairs on
Proposed Establishment of an Independent Insurance Authority
(12 October 2010)

Introduction

1. The Consumer Council (“CC”) welcomes the opportunity to provide its views on the proposed establishment of an Independent Insurance Authority (IIA) for consideration of the LegCo Panel Members.

2. In discussions of the appropriate regulatory models for the professional sectors, the focus tends to be placed on professional operation, resulting in concerns of having “non-professionals regulating the professionals” and its appropriateness. The issue is rarely approached from a consumer perspective to explore whether industry self-regulation can effectively protect the interests of consumers.

Increased consumer complaints

3. Since January 2000, CC has received insurance-related complaints at the average rate of about 400 cases a year. There were 230 cases between January and August 2010. The number has risen over the past 10 years (see attached table).

4. In addition to regular problems such as consumers being refused coverage, excessive increase in insurance premiums, refusal or delay in compensation, as well as sales agents’ provision of false or misleading information on ‘guaranteed’ dividend/bonus, contribution period, early surrender of policy, there has been increase in recent years in the number of complaints concerning newly emerged investment-linked insurance products (31 cases in 2007, 51 cases in 2008 and 42 cases in 2009) and the issue involved are becoming more and more complex.

5. CC is of the view that if industry self-regulation cannot provide adequate protection to consumers, there is a need to consider alternative regulatory models, such as the establishment of an independent regulator.

Lack of confidence in industry self-regulation

6. The advantage of industry self-regulation is that regulators are familiar with industry operation and would be in a better position to grasp the crux of problems, so that the problems could be handled and resolved swiftly. On the other hand, some may perceive that with self-regulatory bodies dealing with complaints about their industry members, the mode of “putting your own house in order” lacks impartiality. It is questionable to the public whether self-regulatory bodies sponsored or supported by industry members would play an effective role in monitoring members’ compliance.

7. At present, three trade bodies perform the role of self-regulators (the self-regulatory organizations, SROs) in respect of insurance intermediaries.

There are role conflicts and potential conflict of interests. As these SROs are trade bodies financed by their members, they may be hesitant with taking strict disciplinary action lest there are members' complaints. Even with the involvement of some non-industry members in the handling of complaints, it is still difficult to dispel public perception that the SROs will be biased towards the industry.

8. In addition, the SROs have limited investigatory and sanctioning powers which constrain them from making full and effective regulation of the insurance industry. For instance, they cannot inspect a company's documents and accounts (these are industry trade secrets) for carrying out detailed investigations. As sanctions that can be applied are primarily suspension or revocation of membership which are very severe, the SROs may take a lenient approach in dealing with non-complying members.

9. Furthermore, consumers may have difficulty looking for the appropriate regulatory bodies to handle their complaints in view of the present fragmented regulation. CC believes that having an independent statutory body to assume direct supervisory and disciplinary roles over the insurance industry can be more objective and impartial. Its credibility and public acceptance can also enhance consumer confidence in the insurance industry

The proposed IIA

10. CC supports the establishment of the IIA to improve the existing insurance regulatory regime and enhance the protection of the interest of existing and potential policyholders. With respect to some of the proposals in the consultation paper, CC has the following views:

Regulatory functions

11. In relation to the proposal of vesting the Hong Kong Monetary Authority (HKMA) with powers similar to the IIA for HKMA to regulate bank staff selling insurance products, CC considers that caution should be taken to avoid any overlap in regulatory efforts resulting in increased supervision costs which may ultimately be passed onto consumers. Or there could be regulatory gaps as a result of ambiguity in their respective role and responsibility, likewise, inconsistency in regulation (in terms of rules and execution) can lead to regulatory arbitrage to the detriment of consumer interests.

12. As a new dedicated Investor Education Council is to be set up, CC considers that necessary arrangements should be made by the IIA with organizations currently engaged in promoting consumer understanding of insurance products to ensure there is close collaboration with these organizations to avoid wasting resources.

13. Many of the insurance complaints received by CC concern excessive increases in insurance premiums and consumers being misled into buying inappropriate insurance products. CC is therefore of the view that the public would have expectation of the IIA, as an independent entity, to play an active

role to address their concerns, thereby ensuring the interests of policyholders are effectively protected.

Levy

14. It is proposed in the consultation paper that part of the funding of the IIA is to be raised from a levy of 0.1% on insurance premiums for all insurance policies, and that about 70% of the expenditure of the IIA is to be met by this levy ultimately. Nevertheless, the Government has not stated in the consultation paper who will pay the levy.

15. As seen from many regulators in Hong Kong (e.g. HKMA, the Mandatory Provident Fund Authority, and the Hong Kong Deposit Protection Board) and financial regulators in other jurisdictions (e.g. the Financial Services Authority of the UK, the Office of the Superintendent for Financial Institutions of Canada, the Federal Deposit Insurance Corporation of the US), the funding sources of these regulatory agencies are largely derived from industries, instead of having consumers pay for the cost of industry regulation.

16. CC is of the view that the Government should make clear to the public who will pay for the levy on the policies.

- CC will not support having policyholders directly pay the levy. It also opposes shifting the regulatory cost to consumers.
- If the levy is to be paid by the insurance industry, CC recommends that the Government put in place safeguards to ensure premiums would not be unreasonably increased in consequence.

17. If the Government eventually chooses not to align with international practices and settles on raising funding for the IIA directly from policyholders, CC considers that the use of the levy must be made accountable to the public, i.e. to spell out clearly the scope of work in respect of protecting the policyholders' interests and its effectiveness, as well as the percentage of the expenditure of the IIA to be spent on this aspect.

18. As to the fee structure, CC recommends that consideration be given to introduction of other fees for demand-driven services e.g. charging regulated entities for complaints handling to reflect the costs involved in the investigation.

Conclusion

19. With Hong Kong as an international financial centre, the Council considers that strengthening the protection of policyholders is a task to be given priority.

20. The Government released a similar consultation as far back as 2003 but not much progress has been made. Now that establishment of the IIA is again raised, CC urges the Government to speed up the related legislative work to render better protection to the public.

Table: Consumer Council's insurance complaint statistics

Year	No. of insurance complaints
2000	246
2001	338
2002	380
2003	472
2004	401
2005	404
2006	414
2007	398
2008	425
2009	447
2010 (1-8)	230
Total:	4155