

Public Consultation on

**Proposed Establishment of an
Independent Insurance Authority**

Response to

Financial Services and the Treasury Bureau

by

The Hong Kong Confederation of Insurance Brokers

CIB

October 2010

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INTRODUCTION

The Hong Kong Confederation of Insurance Brokers (CIB) was established in 1993 by the amalgamation of the former Hong Kong Insurance Brokers Association (HKIBA), a voluntary professional body formed in 1979 and the Society of Insurance Brokers (SIB) established in the mid-1980s.

- The HKIBA responded to the Law Reform Commission's 20 July 1982 consultation on Topic 9, Insurance Item B as to "Whether there should be any regulation of the activities of intermediaries such as brokers and agents and if so what form should it take". The HKIBA response of 23 September 1982 proposed self regulation of brokers as quite separate from agents and the subsequent regulation as exists today was largely modelled on that HKIBA proposal.
- In 1990 the first Commissioner of Insurance (Col) decreed that Government could only deal with one professional body of brokers and to that end the HKIBA and the SIB amalgamated to form the CIB as a regulatory body and negotiated the terms of the current regulations with the Col.
- The second Col subsequently decreed that Government could not condone monopolies and therefore the then small Professional Insurance Brokers Association Ltd (PIBA) was elevated to the second broker Self Regulatory Organisation (SRO) role thus creating the duplication and differential standards which are criticised today.

The CIB today is a body of professional insurance brokers authorized by the Col as an SRO with some 246 corporate members registering some 4,236 Chief Executives and Technical Representatives.

- CIB is run by a General Committee (GC) comprising 12 members representing the executive level of its member brokers.
- The administrative and registration functions of the CIB are undertaken by a Secretariat headed by a professional "Secretary General and Registrar" assisted by five full time staff from premises situated in AIA Tower, Electric Road, Fortress Hill.
- Complaints are investigated by the Investigation Board (IB) with an independent chairman and advised by two GC members supported by an alternate GC member. The function of the IB is to decide whether a prima facie case has been established which should be further pursued.

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INTRODUCTION (continued)

- When a prima facie case has been identified, it is referred to the Disciplinary Committee (DC). The DC is chaired by an independent chairman. The current chairman is a solicitor. His predecessors were a solicitor and a retired High Court Judge.
- When sitting the DC draws two supporting independent members from Panel A comprising an actuary and four solicitors and two GC members from Panel B comprising four GC members.
- In case of an appeal of a DC judgement, the matter is referred to the Disciplinary Appeals Committee (DAC). The DAC has an independent chairman, currently a senior barrister with extensive Government and professional disciplinary board experience, supported by an independent member, currently a retired former senior official of the Insurance Authority and the Chairman of CIB in an ex officio capacity.
- The IB, DC and DAC are all established in accordance with the Articles of Association of the CIB and operate in accordance with guidelines formulated in consultation between the GC, the Secretariat and the respective independent chairmen.
- CIB retains a firm of solicitors to act as law clerk to the DC and a separate firm of solicitors to act as prosecution advisors where necessary. Persons appearing before the IB, DC or DAC are entitled to be legally represented.
- It is notable that independent chairmen and independent members past and present of the IB, DC and DAC have commented on the value of the contribution made by the nominated GC members to these committees in guiding the independent members through interpretation of insurance broking terminology, methodology and practice.

The CIB holds an Annual General Meeting each year at which the officers and committee members are elected. The Chairman holds office for two years and GC members are due for re-election after three years.

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INTRODUCTION (continued)

- In order to fully understand the issues and implications of this consultation, the CIB Task Force and Secretariat have undertaken extensive preparatory work including having :
 - met with the other two SROs to examine the issues involved in the proposal;
 - attended all four public consultation sessions to listen to views from all sections of the community;
 - met with the Government officials to explore and clarify their thinking behind the proposal;
 - met with a LegCo Member to learn the general opinion of the social and political leaders;
 - conducted an open Members' Forum to exchange views with fellow Members of CIB and to give them the opportunity to express their opinions;
 - the Secretary General of CIB has raised this for discussion with Members during the course of annual inspections;
 - discussed with fellow practitioners through personal contacts to tap market intelligence; and
 - debated within the General Committee to develop a constructive response.

OUR MAIN CONCLUSIONS

CIB will support the proposal by the Financial Services and Treasury Bureau (FSTB) for the formation of an Independent Insurance Authority (IIA) as set out in the Consultation Paper dated July 2010 on the understanding that implementation is inevitable given the political pressure from the International Monetary Fund (IMF) and the pronouncements of the International Association of Insurance Supervisors (IAIS). This is however subject to further detailed and meaningful consultation by FSTB with the insurance industry in general and the CIB in particular on the future regulatory standards and administrative processes to be proposed in the legislation. Such consultation is hinted at but not adequately guaranteed by the Consultation Paper Clause 1.6.

- The GC of the CIB and its Members' majority view is that the SRO framework has worked well.
- We believe that the majority of our Members would support the continuation of the current SRO framework.
- **The reality is that in order to meet with the demands of the IMF and also to align Hong Kong with current international practice, the Government has made clear its determination to establish the IIA including direct supervision of insurance intermediaries.**
- **The GC of the CIB believes that rather than challenge the formation of the IIA, a more constructive approach is to assist the Government in shaping the framework of the IIA in order that it operates effectively and enables Hong Kong to maintain its competitiveness as a leading insurance centre in Asia.**
- In line with Hong Kong SAR's reputation as one of the most business-friendly economies in the world, the IIA must avoid falling into the trap of over-regulating the insurance industry.
- The growth and long term development of the insurance industry in Hong Kong is dependent on a viable and uninhibited market and regulatory environment and should inappropriate constraints be introduced there is little doubt that large sectors of specialist lines and reinsurance would move offshore to the detriment of the Hong Kong insurance industry and the Hong Kong economy in general.

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OUR MAIN CONCLUSIONS

(continued)

- The Consultation Paper is a high level document which states Government's intentions in very broad terms but does not indicate how these will be achieved. CIB would like to meaningfully participate in a second formal consultation process to ensure that the framework and operational regulatory processes will not be disruptive to established trade practices and international reporting systems and that the future cost of compliance will not be excessively increased.
- CIB Members in Forum have expressed their serious concern at the potential fee costs and increased costs of compliance that will be imposed on brokers as the Consultation Paper is silent on this critical issue. CIB urges FSTB to be more transparent on this matter and to give clarity to the expected level of licence fees for brokers and agents. In particular CIB is concerned with the accuracy of the projected costs of the IIA which would appear to be understated.
- CIB has grave concerns that the proposed policy levy will drive certain policyholders to arrange their insurances overseas, to the detriment of the Hong Kong market and local economy.
- The IIA should draw on the industry to provide input on strategic and operational issues, and there should be statutory standing committees within the IIA with industry representation.
- CIB expressly disagrees with the proposal that the HKMA should regulate the selling of insurance by banks. This would effectively repeat Government's previous mistake in 1990 of requiring two Broker SROs. The aim of the new regulatory framework should be to avoid any of the perceived weaknesses or pitfalls of the existing regime and in particular to ensure that there is no repetition of the differing approaches and arbitrage as exists between the OCI and the SFC and between CIB and PIBA.
- CIB proposes that a Provisional IIA should be established at least one year before the IIA formally takes over the regulatory role. During this period the OCI working with industry representatives could ensure that the operational structure and guidelines are formed in such a way as to provide a seamless transition with all uncertainties having been resolved in advance.

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OUR MAIN CONCLUSIONS

(continued)

- It has been well recognised that other jurisdictions have rushed into changes in their insurance and financial regulatory processes with less than satisfactory results, indeed having created serious problems detrimental to their local insurance establishments. CIB trusts that FSTB will carefully review the circumstances in the United Kingdom and Australia respectively where the first regulatory changes have needed to be revisited and completely restated after a relatively short period.
- The new IIA should be charged with a clear responsibility to promote Hong Kong as the pre-eminent insurance centre in Asia, a position that Hong Kong has arguably already lost to Singapore. In addition the IIA must ensure that Hong Kong is given preferential treatment in allowing it's insurers and intermediaries access to the mainland market.

GUIDING PRINCIPLES FOR THE ESTABLISHMENT OF AN INDEPENDENT INSURANCE AUTHORITY (CHAPTER 2 OF THE CONSULTATION PAPER)

Question 1

Do you agree that an independent IA should be established along the principles set out in paragraph 2.6?

Our Answer

CIB agrees in general with the principles stated in 2.6.

- Para 2(d) refers only to prudential regulation of insurers and conduct regulation of intermediaries. It should be made clear that the conduct regulation applies equally to insurers and intermediaries.
- While not stated in the Paper, it has been commented by officials in presentations that there is currently no intention to change the Minimum Requirements or Codes of Conduct. CIB would be concerned if, after dissolution of the SRO consultative process and the Provisional IIA, the new IIA were to decide to unilaterally make significant changes to these regulatory documents and CIB would like to see the intentions and consultancy framework clarified before establishment of the IIA.
- The current financial regulatory regime in Hong Kong is frustrated by demarcation disputes or grey areas as between the HKMA, SFC and OCI. Further discrepancies of interpretation are held by consumers, the OCI and LegCo to exist as between the CIB and PIBA. In establishing an IIA which should remove any anomalies as between the existing SROs, it is important that no new anomalies and potential arbitrage are allowed under the new regime. In fact if the new insurance regulatory regime is to succeed it is imperative that the new IIA, the HKMA and the SFC are completely aligned so as to ensure seamless coordination between their respective jurisdictions.

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**GUIDING PRINCIPLES FOR THE ESTABLISHMENT
OF AN INDEPENDENT INSURANCE AUTHORITY
(CHAPTER 2 OF THE CONSULTATION PAPER)
(continued)**

Question 2

Do you think that there are other important principles in addition to those set out in paragraph 2.6 that the Administration should adopt in working out the detailed legislative proposals for the establishment of the independent IA? If so, what are they?

Our Answer

The stated principles are very high level as would be expected in a consultation document. In establishing the IIA, it should be noted that:

- Clear differentiation should be made between Agents and Brokers to recognise their different legal status and fiduciary duties.
- In defining the functions and structure of the new IIA, it is imperative that Government recognizes that the Hong Kong insurance industry is part of a global insurance and reinsurance market, not restricted to the sale of retail personal lines products in the local market. The provision of insurance products to commercial and corporate enterprises forms a major segment which not only generates significant income to the local market, but which also facilitates secure investment by local enterprises within Hong Kong and internationally eg, shipping, telecommunications, construction, financial services, manufacturing etc etc. The formation of the IIA must not overlook this or be distracted by the higher profile consumer issues relating to the regulation of personal lines products.
- In addition to the stated principles of the IIA, CIB would like to see a clear statement of intent that the IIA will draw on the industry to provide input on strategic and operational issues.
- **In particular the new arrangements should recognise that Hong Kong's local insurance industry is only a small part of the global insurance and reinsurance industry and care needs to be taken not to impose restrictions or requirements which are out of line with global transactional standards and practices.**

FUNCTIONS OF THE INDEPENDENT INSURANCE AUTHORITY (CHAPTER 3 OF THE CONSULTATION PAPER)

Question 3

Do you agree that the independent IA should have an expanded role beyond the existing functions of the IA as set out in paragraph 3.1? If so, do you agree that the independent IA should assume the additional functions as proposed in paragraph 3.3 and 3.4?

Our Answer

CIB agrees that the IIA should be given an expanded role beyond the functions currently performed by the IA.

- Given the very different roles, duties and responsibilities of agents and brokers, there must be clear differentiation within the IIA on the licencing, inspection, handling of complaints, investigation into misconduct and imposing of disciplinary sanctions for agents and brokers.
- In particular CIB has concerns that a single disciplinary panel could not adjudicate both agents and brokers due to their differing responsibilities and practices and supports the precedent of the judiciary where different courts with specialist judges establish guilt but then all follow the same sentencing guidelines as laid down by the Chief Justice.
- We believe it will be beneficial to both the IIA and the industry for the involvement of experienced industry professionals within these functions.
- In this regard, we have concern as to the proposed organizational structure of IIA whereby the “Advisory Committee” is linked at the top level to the Governing Board, remote from the administrative and operational activities where understanding of professional practices is most needed.
- CIB believes that there should be at least one senior broker representative appointed to the “Advisory Committee”.
- Additionally, CIB and other SROs have appointed independent members to many of their committees and panels thus creating an invaluable and irreplaceable pool of relevant expertise and experience. CIB trusts that these people will continue to be appointed by the IIA to retain the benefit of this senior resource.

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**FUNCTIONS OF THE INDEPENDENT
INSURANCE AUTHORITY
(CHAPTER 3 OF THE CONSULTATION PAPER)
Question 3 (continued)**

- We would see additionally a Technical Advisory Committee most appropriately being placed along side the Chief Executive Officer and with technical sub-committees delegated to the four supervisory and development divisions, such sub-committees to have representation from relevant segments of the insurance industry.
- The SFO (s.8) provides that the SFC may establish standing and special committees to consider, inquire or manage matters referred by the Commission, meanwhile the proposal (7.2) recommends “that the Governing Board be assisted by Committees designated to oversee specific areas of the independent IA’s work”. This is in line with our proposed “technical sub-committee” structure, and we would like to see such standing committees as statutory, not optional, with different panels for agents and brokers, at the least for the aforesaid functions. A clear brief of the sub-committees’ role and responsibilities needs to be agreed with the industry in advance of the establishment of the IIA.
- There is concern that once the SROs are devolved of their registration and regulatory functions many members will resign once re-registered directly with the IIA. Members who remain with the SROs will need to pay fees to both the IIA and their SRO. The pressure will be to reduce the SROs’ subscriptions meaning that SROs are unlikely to be able to maintain secretariat premises and staff. As the staff of the CIB Secretariat are the most experienced and competent insurance regulatory registrars and administrators in Hong Kong, CIB believes it would be of great benefit to the IIA and the industry if the IIA were to offer them employment if and when their roles within the CIB become redundant.
- With the possible demise of the SROs as administrative bodies, although they can continue to have an advisory role, the administration and monitoring of CPD and educational activities related thereto would presumably devolve into the IIA. CIB believes strongly in the need for quality professional education and would recommend that the IIA should align with an experienced and capable educational provider such as the Insurance Institute of Hong Kong which is aligned with the Chartered Insurance Institute in order to maintain an appropriate and suitable standard.

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**FUNCTIONS OF THE INDEPENDENT
INSURANCE AUTHORITY
(CHAPTER 3 OF THE CONSULTATION PAPER)
(continued)**

Question 4

Do you agree the independent IA should also have a duty to enhance the competitiveness of the insurance industry, which will help to reinforce Hong Kong's status as an international financial centre?

Our Answer

We believe IIA should be responsible for enhancing the competitiveness and reinforcing HK's status as Asia's pre-eminent insurance and financial centre and to foster closer relationships with CIRC in particular with a view to securing preferential status for Hong Kong firms seeking access to the mainland market. The IIA should also proactively promote Hong Kong as a captive domicile. In order to avoid Singapore claiming the title of the pre-eminent insurance and reinsurance market in Asia, the IIA must recognise and observe the following :

- In order to enhance the competitiveness of the market, IIA must avoid over-regulation.
- It is absolutely imperative that the cost structure imposed under the new IIA should not force business offshore.
- In line with current practice IIA should be precluded from restricting/dictating policy terms or influencing the premium levels charged by insurers.
- Any tolerance of un-authorized insurance intermediaries practicing in or from Hong Kong will compromise the competitiveness of the insurance industry. The IIA should be duly empowered to stamp out such un-authorized practice.
- CIB Members have strongly expressed the view that the new IIA should have the resources to invest in the promotion of the Hong Kong insurance industry in the region and particularly in China. Little has been done in this direction whereas other jurisdictions, particularly Singapore, have been positive in their promotional efforts. For example many commercial organisations have benefitted from the provisions of the Closer Economic Partnership Arrangement (CEPA) with mainland China but insurance has not been raised in any significant way.

(to be continued)

**FUNCTIONS OF THE INDEPENDENT
INSURANCE AUTHORITY
(CHAPTER 3 OF THE CONSULTATION PAPER)
Question 4 (continued)**

- The insurance industry together with an initiative from the Business and Professionals Federation of Hong Kong (BPF) have been pushing to establish Hong Kong as a centre for captive insurance companies particularly to attract mainland China based corporations. However this has made little progress due to the refusal of the Inland Revenue Department to grant the necessary tax concessions to make captives viable. Captives could be a lucrative form of business income to Hong Kong and the IIA should be charged with ensuring the necessary Government cooperation to achieve this.

REGULATION OF INSURERS (CHAPTER 4 OF THE CONSULTATION PAPER)

Question 5

Do you agree the independent IA should be vested with additional powers as proposed in paragraph 4.7 to enable it to regulate insurers more effectively?

Our Answer

CIB agrees with the proposed additional powers to be vested in the IIA as proposed under para 4.7 and in particular their ability to intervene in situations which may compromise policyholders' interests.

- Such additional powers should be vested also for the purpose of regulating un-authorized insurance intermediaries acting in or from Hong Kong.
- The power of the IIA to impose supervisory sanctions such as public reprimands and fines needs to be matched with a transparent appeals process to apply before any public pronouncement of guilt is issued.
- The level of sanctions needs to be tempered by realistic comparison to the regulatory sanctions handed out by other professional regulatory bodies.
- The use of "suspensions" needs to recognise the necessity for the clients of a broker or agent to be able to receive adequate servicing of their insurance programmes by people knowledgeable and familiar with them during any period of suspension. The sudden withdrawal of on-going service due to a suspension is not in the best interests of, and indeed is detrimental to, the consumers whom the new regulatory framework is intended to protect.
- The IIA should have greater powers of intervention to enable it to take positive action, including closure, against defaulting or endangered insurance companies at an early stage to protect consumers and the market.

REGULATION OF INSURANCE INTERMEDIARIES (CHAPTER 5 OF THE CONSULTATION PAPER)

Question 6

Do you consider that the existing self-regulatory arrangements for insurance intermediaries should be changed, and if so, do you support that Option 2 (i.e. direct supervision of insurance intermediaries by the independent IA) should be pursued? If not, why?

Our Answer

The GC of the CIB and its Members' majority view is that the SRO framework has worked well, with CIB in particular experiencing comparatively low levels of complaints and ensuring disciplinary matters are appropriately and promptly resolved.

- We believe that the majority of our Members would support the continuation of the current SRO framework.
- CIB considers that if the SRO framework was to continue it would be necessary to combine CIB and PIBA in to one Broker SRO. However the reality is that in order to meet with the demands of the IMF and also to align HK with current international practice, the Government has made clear its intention to establish the IIA with direct responsibility for licencing insurers and intermediaries.
- The GC of the CIB believes that an SRO framework operating under an IIA with expanded powers could operate effectively however we do not believe that this would be sufficiently independent to meet the IMF's and Government's requirements.
- **Consequently, the CIB supports Government's preference for direct licensing and supervision under Option 2. The GC of the CIB believes that the most constructive approach is to assist the OCI in shaping the framework of the IIA in order that it operates effectively and enables the industry to maintain its competitiveness and to contain the cost of compliance.**

(to be continued)

REGULATION OF INSURANCE INTERMEDIARIES
(CHAPTER 5 OF THE CONSULTATION PAPER)
(continued)

Question 7

Do you consider that in relation to the sale of insurance products in banks, the HKMA should be vested with powers similar to those for the independent IA to allow HKMA to regulate bank employees selling insurance products given the different client profile and sale environment in banks?

Our Answer

CIB strongly disapproves of the proposal to grant HKMA the authority to regulate the sales of insurance products in banks. To do so would repeat the totally unsatisfactory position which has been allowed to exist in the lack of alignment between SFC and IA in their regulation of ILAS, and also flys in the face of the Government's stated perception that conflicts of interest exist within CIB and PIBA with their respective disciplinary committees' allegedly granting leniency in disciplinary matters in order not to upset their respective members. (CIB vociferously rejects such allegations .)

- There is no clear rationale provided in the Consultation Paper for the proposal other than "different client profile" and "different sales environment". Ultimately the risks associated with the mis-selling of insurance products and misconduct are the same, regardless of the environment in which they are sold and the point that the bank knows its clients better than an insurance broker or agent is also highly debatable.
- Unless there are corresponding changes to amend the secrecy provisions in the Banking Ordinance, as revealed by the recent Octopus fiasco, there are issues that the IIA would not be able to overcome when a licensed bank staff member is disciplined by HKMA such as :
 - (a) The licensed bank staff member lodges an appeal against the sanction; or
 - (b) IIA is to review his fitness and propriety to remain being licensed.

In both scenarios, HKMA may have to refuse to disclose details due to the secrecy provisions, hence preventing a fair hearing of the appeal.

(to be continued)

REGULATION OF INSURANCE INTERMEDIARIES

(CHAPTER 5 OF THE CONSULTATION PAPER)

Question 7 (continued)

- Contrary to the scenario where a regulator imposes a sanction based on its own set of rules and regulations and the other regulator reviews the sanctioned person's fitness and propriety to be licensed, HKMA will be implementing the IIA's rules and regulations and exercising power vested by IIA. After the HKMA has imposed the sanction on a bank employee, IIA's review of his fitness and propriety would amount to a "double penalty", which is inequitable and legally unsound.
- In the public forum, OCI has indicated that the IIA would not under current legislation be allowed access to banking records in its investigation of a complaint. CIB believes this concern could be easily overcome by obtaining customer consent to release documents in the event of a complaint to facilitate the investigation. In any event any documents not related to insurance sales to clients would be either irrelevant or of a matter concerning fraud, and in the latter case, a criminal investigation should be instigated by the Police instead.
- In the event that IIA grants HKMA powers to regulate the sale of insurance products and disciplinary functions within banks, there is a real danger that these functions would be performed by banking specialists, not by staff conversant or familiar with the insurance industry. As such regulation of insurance sales within banks by HKMA could only be effective if a specialist insurance team was formed within HKMA, which would appear to be sub-optimal, and inevitably lead to conflicts and inconsistencies in the application of rules, regulations and disciplinary matters, and involve unnecessary duplication of resources.
- If HKMA was to set up a specialist insurance regulatory team, this would compete in the market with the IIA for scarce technical resources, ultimately leading to an overall deterioration in the quality of the regulatory and supervisory regime and consequential adverse effects on both the insurance industry and the consumer.

(to be continued)

REGULATION OF INSURANCE INTERMEDIARIES
(CHAPTER 5 OF THE CONSULTATION PAPER)
Question 7 (continued)

- Banks sell insurance as registered agents of insurance companies, whether the bank's own insurer or an independent commercial insurer. Under current regulation, which we are told is not intended to be changed, insurance companies are responsible for the actions of their agents. Clearly therefore circumstances could arise where a bank agency and an insurer are jointly responsible and the question would then arise as to whether the HKMA would have jurisdiction over the insurer also or whether a confusing situation would pertain with both the IIA and the HKMA involved in the same disciplinary action.
- The argument of "different client profile" in terms of a bank knowing its clients better if true, which we doubt, will no longer be a factor as banks will be restricted as to use of clients' personal data following the Octopus fiasco.
- CIB can see no rationale for this proposal and believes that any sale of insurance products should be regulated by the IIA. To draw parallel examples, if the HKMA is to regulate selling by Banks, why should travel agents selling insurance not have that activity regulated by the Insurance Industry Council or motor car dealers selling motor insurance by the Motor Traders Association. This is clearly not a practical proposition.

ORGANISATION FRAMEWORK OF THE INDEPENDENT INSURANCE AUTHORITY (CHAPTER 6 OF THE CONSULTATION PAPER)

Question 8

Do you agree that the recommendations as set out in paragraphs 6.5 to 6.8 should be pursued for the independent IA to operate as an independent entity? Any other views?

Our Answer

CIB believes it will be beneficial to both the IIA and the industry for the involvement of experienced industry professionals within the IIA on a strategic as well as an operational level.

- In this regard, we have concerns as to the proposed organizational structure of IIA whereby the only “Advisory Committee” is linked at the top level to the Governing Board, remote from the administrative and operational activities where understanding of professional practices is most needed.
- We would propose also a Technical Advisory Committee most appropriately to be placed alongside the Chief Executive Officer and with technical sub-committees appointed to provide guidance to the Long Term Business, General Business, Market Conduct and Policy and Development Divisions, such sub-committees to have representation from relevant segments of the insurance industry to advise and/or to address the specific issues pertaining to insurance companies, agents and brokers and also recognising the different aspects of life and general insurance business within those sectors.
- Under Market Conduct, given the very different roles and responsibilities of agents vs brokers, a clear differentiation should be made between insurers, agents and brokers, with separate teams given responsibility for authorizations, supervision, conduct, complaints, investigations and enforcement relating to brokers or agents.
- We feel that the Consumer Education and Protection function should be moved to the Policy and Development division, given this is closely aligned to External Relations.

(to be continued)

**ORGANISATION FRAMEWORK
OF THE INDEPENDENT INSURANCE AUTHORITY
(CHAPTER 6 OF THE CONSULTATION PAPER)
(continued)**

- CIB would expect to be involved in the drafting of the objectives, roles and responsibilities of the Technical Committee and Technical Sub-committees and to be consulted on the level of industry and non-industry participation in each.
- The CIB's proposed revised Organisation Structure Chart is attached as Appendix A.

GOVERNANCE AND RELATED MATTERS (CHAPTER 7 OF THE CONSULTATION PAPER)

Question 9

Do you agree with the proposed checks and balances and governance arrangements for the independent IA as set out in this Chapter?

Our Answer

Please refer to CIB's answer to Question 8 regarding the role and position of the Advisory Committee within the structure of the IIA.

- We have concerns that the Governing Board members may not have adequate understanding of the global insurance and reinsurance industry and would like to see a more commercially based range of constituencies.
- We have concerns that the issues addressed as potential checks and balances are of a bureaucratic nature rather than ensuring the reasonableness and functionality of the regulation and supervision.
- In respect of 7.3 (d) we should like it clarified that a statutory appeals tribunal would hear appeals both against disciplinary decisions and also against regulations or requirements imposed by the IIA which were held to be unreasonable or excessively costly.
- It is not clear whether the Appeals Tribunal and Review Panel set up by the IIA under 7.3 (d) and (e) will have jurisdiction over the HKMA or whether HKMA sets up its own bodies. If the latter, then we would have real concerns as to standards applied.
- We would question whether the secrecy provision in the Banking Ordinance may have a bearing on the proper discharge of duties by HKMA and the proper conduct of appeals tribunal and process review.
- There should be alignment of different financial regulators so as to address the issues with product and regulatory arbitrage.

FUNDING MECHANISM (CHAPTER 8 OF THE CONSULTATION PAPER)

Question 10

Do you agree that the Government should provide a lump sum to support the independent IA in its initial years of operation and the independent IA should seek to reach full cost recovery in six years?

Our Answer

While CIB supports the proposed lump sum funding in the initial years and full cost recovery in subsequent years, the Consultation paper does not provide sufficient data to allow us to comment on the expected level of cost of the IIA. There is therefore a concern that the proposed fee structure might be inadequate to support the costs of the the IIA in the future.

- The Consultation Paper proposed an increase in the level of staffing from 123 to 237 (+92%) and an increase in costs from HKD110m to HKD240m (+118%). We believe that in order to attract suitably qualified staff from the insurance market, employment costs will be considerably higher per capita in comparison with existing levels. Furthermore, a significant portion of the work to be performed by the IIA is currently undertaken *pro-bono* by industry practitioners and going forward, this will need to be paid for based on the proposed structure of the IIA.
- Furthermore, IIA will assume a broader role necessitating increased expenditure on promoting the Hong Kong insurance industry, actuarial resources, market research, public awareness, legal fees etc.
- We would question whether the projected costs reflect the IIA occupying Grade A office premises in Central or offices in a lower-cost location.
- We would question whether the current OCI costs (HKD110m) include the costs associated with support provided to the OCI by other Government Bureaux, ie Department of Justice, Civil Service Bureau, Government Logistics Department, Office of the Government Chief Information Officer, Information Services Department per Para 6.2 of the Consultation Paper.
- Further information on the assumptions used in projecting costs for the IIA needs to be provided.

(to be continued)

FUNDING MECHANISM
(CHAPTER 8 OF THE CONSULTATION PAPER)
(continued)

Question 11

Do you agree with the proposed fee structure as set out in paragraphs 8.2 and 8.6?

Our Answer

CIB is concerned over the level of license fee to be levied on insurance intermediaries in particular the insurance brokers. An estimated level of fee should be provided and should be included in the legislation, to be reviewed with approval by the LegCo.

- Over 60% of CIB members are small businesses, and if the fee is increased along with the inevitable increase in costs of compliance consequent upon the establishment of the IIA and the introduction of higher standards of compliance, there is little doubt that many of these firms will be forced out of business or be required to consolidate with other firms.
- Non-admitted policies are not prohibited in Hong Kong and CIB would question how IIA will be able to collect the levies from overseas insurers.
- In the absence of a cap on the levy, there will be a significant impact to premium for major multi-national corporate insurance and also on “Jumbo” life insurance policyholders, and as a result these buyers may be very likely to buy their products from overseas carriers to the detriment of the Hong Kong insurance market and the Hong Kong economy in general.
- In particular, specialist lines, such as aviation, marine hull, P&I and marine cargo, are most likely to be driven to overseas markets to the detriment of the Hong Kong insurance market and the Hong Kong economy in general.
- If the levy is to be applied to reinsurance, this would be a double counting, driving insurers to purchase reinsurance overseas and reinsurers to book their business offshore to the detriment of the Hong Kong insurance market and the Hong Kong economy in general.
- To avoid this potential loss of business to offshore markets, any levy should only be applied to direct policies, and not to reinsurance.

(to be continued)

FUNDING MECHANISM
(CHAPTER 8 OF THE CONSULTATION PAPER)
Question 11 (continued)

- CIB proposes that if there is to be any levy then it should be capped at not more than HK\$1,000, that it should apply to direct policies only and not to reinsurance. The threat to the future of the Hong Kong insurance industry from potential IIA driven initiatives and in particular a significant policy fee should not be underestimated and all of the specialist coverages and reinsurance are readily available from the large and growing Singapore market.

- **It is the firm view of CIB that a policy levy is an undesirable funding mechanism for a number of reasons. We have previously stated the need for a cap to defer the flight of insurance business offshore. The drawback of such a cap is that individual consumer interests will claim that large corporate business is being cared for and that a disproportionate amount of levy falls on the small individuals. Conversely the premium pool of insurers is large enough that, while they will object, they will not have difficulty in absorbing the IIA costs. CIB prefers a direct fee levy on insurance companies to cover all costs and allow market forces to take care of insurers' ability to absorb or to charge such increased costs back to policyholders.**

The Hong Kong Confederation of Insurance Brokers
Hong Kong
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Proposed Organisation Structure of the Independent Insurance Authority

