



**Financial Services and the Treasury Bureau  
The Government of the Hong Kong Special Administrative Region**

**CB(1)1870/10-11(01)**

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# *Proposed Establishment of a Policyholders' Protection Fund ("PPF")*

**4 April 2011**

## PPF Guiding Principles

- Strike a reasonable balance in enhancing protection for policyholders and minimizing additional burden to the insurance industry
- Enhance market stability while minimizing the risk of moral hazard
- Provide certainty on the level of compensation payment to policyholders when an insurer becomes insolvent, and a reliable system should be put in place to facilitate the collection, custody, investment and administration of levy contributions to the PPF
- Should not in any way compromise the regulatory standards and requirements laid down by the Insurance Authority under the ICO



# Coverage

## Two separate schemes for Life & Non-Life business covering :

- Individual policyholders
- SME policyholders and building owners' corporation third party liability insurance policyholders
- All authorized direct life and non-life insurers should be mandated by statute to participate except
  - Reinsurers
  - Wholesale retirement schemes
  - Captive insurers
  - Motor vehicle and employees compensation policies
- All in-force policies as at the date of the introduction of the PPF & new policies issued thereafter will be covered



## Level of Compensation

	Life Scheme	Non-Life Scheme	
		Policies except Accident and Health (“A&H”) policies with guaranteed renewability	A&H policies with guaranteed renewability
<b>Claims</b>	100% for the first HKD100,000, plus 80% of the balance of the claim, up to a total of HKD1 million per-policy for life insurance policies and per-claim for non-life insurance policies		
<b>In-force policies (First priority)</b>	<ul style="list-style-type: none"> <li>• Transfer the policies to another insurer</li> <li>• PPF should be allowed to pay up to HKD1 million per policy to facilitate the transfer</li> </ul>	<ul style="list-style-type: none"> <li>• Provide for continuity of coverage until expiry of policies</li> <li>• Meet claims up to the compensation limit of HKD1 million per policy</li> </ul>	<ul style="list-style-type: none"> <li>• PPF should be allowed to pay up to HKD1 million per policy to facilitate transfer of the policies to another insurer</li> </ul>
<b>In-force policies (When policies cannot be transferred)</b>	<p><b>Two choices :</b></p> <p>(a) To continue the policy until expiry</p> <ul style="list-style-type: none"> <li>• PPF should settle any claims arising subject to a compensation limit</li> </ul> <p>(b) To terminate the policy</p> <ul style="list-style-type: none"> <li>• PPF should pay the policyholder the cash / account value of the policy and declared dividends / bonuses</li> <li>• PPF may also pay an ex-gratia payment to compensate the losses due to premature termination. The total payment should be capped at HKD1 million per policy</li> </ul>	N/A [ <i>Transfer is not arranged given that it is not cost-effective</i> ]	<ul style="list-style-type: none"> <li>• PPF may pay the affected policyholders an ex-gratia payment</li> </ul>



# Funding Mechanism

## Progressive funding approach

	Life Scheme	Non-Life Scheme
<b>Initial target fund size</b>	HKD 1.2 billion	HKD 75 million
<b>Initial levy rate</b>	0.07%	0.07%

- Levy collection : Charged on insurers
- Given the affordable proposed levy rates and the keen competition among insurers in Hong Kong, the impact on the premium levels would be minimal



## Funding Mechanism (Cont'd)

### **Asset recovery mechanism**

- PPF will take over the protected element of policyholders' claims and seek recovery from the estate of the insolvent insurer
- PPF should have equal ranking with the two classes of creditors specified in section 265 of the CO, i.e. the Employee Compensation Assistance Fund and all other direct insurance claims not met by the PPF

### **Financing arrangement to bridge liquidity gap**

- Borrow from a third party to bridge any liquidity gap, e.g. from commercial lenders for which the Government may act as the guarantor, or from the Government direct
- Approval of the Legislative Council will be required



# Governance and Related Matters

## Legal and organizational structure

- Established by legislation and be administered by a statutory body (the PPF Board), appointed by the Financial Secretary ( “FS” )
- Establish two industry committees for Life Scheme and Non-Life Scheme

## Governance arrangements

- Annual budget of the PPF should be subject to approval by the FS
- Prepare and publish an annual report (including the audited statement of accounts) for both Schemes and laid before the Legislative Council
- FS should have the power to appoint the Director of Audit or an external auditor to perform audit reviews on the PPF



# Governance and Related Matters (Cont'd)

## **Guidance on Investment**

- Invest in low-risk vehicles, e.g. deposits with banks, Exchange Fund Bills and sovereign bonds with good credit rating

## **Daily operations**

- Maintain a small team of staff for daily operations and be empowered to engage additional staff or advisers in the event of insurer insolvency

## **Appeal mechanism**

- Set up an Appeal Board to deal with appeals against the decisions of the PPF Board





# Next Steps

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- **Public consultation exercise : 25 March – 24 June 2011**
- **We aim to announce the finalized proposals within 2011**

