

For discussion
on 8 April 2013

**Legislative Council
Panel on Financial Affairs**

**Extension of a Supernumerary Directorate Post
in the Financial Services and the Treasury Bureau
(Financial Services Branch)
to establish an independent Insurance Authority
and a Policyholders' Protection Fund**

PURPOSE

This paper seeks Members' views on the proposed extension of a supernumerary Administrative Officer Staff Grade C (AOSGC) (D2) post in the Financial Services Branch (FSB) under the Financial Services and the Treasury Bureau (FSTB) for about 24 months from 15 October 2013 to 31 October 2015 for, among other things, the purpose of establishing an independent Insurance Authority (IIA) and a Policyholders' Protection Fund (PPF).

BACKGROUND

2. The proposed establishment of a PPF and an IIA were highlighted as the Government's policy initiatives in the Chief Executive's 2008-09 Policy Address and the Financial Secretary's 2010-11 Budget Speech. They have been among FSTB's priority initiatives. The Financial Secretary has further announced in the 2013-14 Budget Speech that the government aims to introduce an amendment bill to establish the IIA within this year.

Establishment of IIA

3. We aim to set up the IIA in order to align with international practice that financial regulators should be financially and operationally independent of the Government, modernise the insurance industry regulatory infrastructure to facilitate the stable development of the industry, and provide better protection for policyholders. Our first public consultation on the proposal was completed in the fourth quarter of 2010.

We announced the consultation conclusions and detailed proposals on 24 June 2011, and consulted the Legislative Council Panel on Financial Affairs on 4 July 2011. There is general public support for the establishment of an IIA.

4. In October 2012, we embarked on further consultation to gauge views of the public on our key legislative proposals. We are now analysing the views collected from the insurance industry and the general public, and finalising the amendment bill for introduction into the Legislative Council in 2013 with a view to setting up the IIA in 2015.

Establishment of PPF

5. We completed a three-month public consultation in June 2011 on the proposal for the establishment of a PPF to maintain market stability and better protect the interest of policyholders by providing them with a safety net in the event of insurer insolvency. We announced the consultation conclusions and final proposals on 30 January 2012 and reported the same to the Panel on Financial Affairs on 6 February 2012. Since then, we have been preparing the enabling legislation in consultation with the industry.

JUSTIFICATION

6. The proposed establishment of an IIA and PPF are the most significant reform proposals for the insurance industry in the past ten years. Having regard to the scale and complexity of the exercise, the Finance Committee (FC) approved on 15 April 2011 the creation of one supernumerary AOSGC post in FSB (designated as Principal Assistant Secretary (Financial Services) Special Duties (PAS(FS)SD)) for 30 months from 15 April 2011 to 14 October 2013. The Administration has reviewed the operational needs of the post and considered it necessary to extend the post to provide policy inputs to the work as elaborated in the ensuing paragraphs.

Legislative work and establishment of IIA

7. For establishing an IIA by 2015, the Administration will need to assess and work out a wide range of detailed arrangements pertaining to the organisation structure, governance framework, licensing arrangements

for insurance intermediaries, regulatory duties and transitional issues in respect of the IIA for inclusion in the amendment bill against a very tight timeline.

8. In addition to taking forward the primary legislation, we also need to prepare a set of subsidiary legislation and practice guidelines before the IIA is formally set up. For example, the bill itself will only lay down the broad principles of conduct requirements (i.e. acting honestly, fairly and competently in the best interest of existing or potential policyholders) to be observed by licensed insurance intermediaries, and the details will be promulgated in subsidiary legislation. In preparing the subsidiary legislation and guidelines, we need to look into relevant overseas and local experiences in order to ascertain whether certain overseas practices may be applicable to Hong Kong and ensure that the proposed requirements are largely consistent with those set up by other local financial regulators.

9. Apart from legislation, we also need to prepare the groundwork for establishing the IIA. As far as organisational setup is concerned, we will have to recruit the senior executives of the IIA, prepare appointment of members to the governing board of IIA, other committees and the Insurance Appeals Tribunal, etc.

Transitional matters of IIA

10. One of the key objectives of the legislative exercise is to set up a statutory regime for licensing insurance intermediaries to replace the current self-regulatory regime. Currently, insurance intermediaries are subject to a self-regulatory regime stipulated under Part X of the Insurance Companies Ordinance (ICO) (Cap. 41), and appointed or authorised in accordance with the relevant statutory provisions. Under the self-regulatory regime, the three self-regulatory organisations (SROs), namely the Insurance Agents Registration Board (IARB) established under the Hong Kong Federation of Insurers, Hong Kong Confederation of Insurance Brokers (CIB) and Professional Insurance Brokers Association

(PIBA)¹ authorised under the ICO, perform the supervisory role in accordance with requirements stipulated in non-statutory codes approved by the Commissioner of Insurance. The registration, supervisory, investigative and disciplinary functions of the SROs will be transferred to the IIA on its establishment.

11. Under our legislative proposal, the pre-existing insurance intermediaries validly registered with the SROs would be deemed to be licensed with the IIA for three years upon its establishment before the IIA grants new licences. The IIA will establish and maintain a register of licensed insurance intermediaries (viz. insurance agents, insurance brokers and technical representatives), containing relevant information in relation to each licence of an intermediary, including its particulars, any licence conditions imposed by the SROs before the establishment of the IIA and a record of any insurance-related disciplinary actions taken against it by the IIA/SROs within a period of five years. Before commencement of the new licensing regime, we would therefore need to work closely with the SROs to ensure proper transfer of data from the SROs to the IIA for establishing a complete register of insurance intermediaries who are pre-existing members of the SROs.

12. In addition, we have proposed that pre-IIA complaints and disciplinary cases which remain unresolved upon the inception of the IIA should be followed up by the IIA, with reference to the pre-IIA standards and circumstances at the time of the occurrence of the event as far as practicable. The IIA would maintain a central register of all complaints against insurers and insurance intermediaries. As there are more than 70,000 intermediaries currently registered with the SROs, intensive discussion and coordination with the SROs will be required to ensure a smooth transition so that (a) the insurance intermediaries can continue to conduct their business activities without interruption after the establishment of the IIA, and (b) the IIA can promptly follow up all unresolved complaints and disciplinary cases.

¹ The IARB is responsible for the registration of qualified insurance agents and their administration through a non-statutory Code of Practice approved by the Commissioner of Insurance. The CIB and PIBA are responsible for ensuring that their members are fit and proper persons to be brokers and that they comply with the minimum requirements specified by the Commissioner. They are responsible for incorporating such requirements in their respective non-statutory Regulations/Codes issued to members. The SROs are also responsible for handling all complaints against their registrants/members, i.e. insurance intermediaries, carrying out investigations and taking disciplinary actions on substantiated cases.

PPF

13. There is currently no general compensation scheme for insurance policies in Hong Kong.² The international financial crisis in 2008-2009 has highlighted the need for a compensation fund for policyholders in the event of insurer insolvency. The establishment of a PPF will strengthen policyholders' confidence in the local insurance industry.

14. We are preparing the enabling legislation for establishing the PPF and have continued to engage stakeholders in the process. We aim to introduce a bill into the Legislative Council in the 2013-14 legislative session. The bill will set out details related to the development of a cost effective and publicly acceptable funding model for the PPF and an efficient mechanism for distributing compensation to policyholders.

Other duties

15. PAS(FS)SD's duties also include engaging the insurance industry on the introduction of a risk-based capital framework for the prudential regulation of insurers.

Extension of the post of PAS(FS)SD

16. Having regard to the scale, complexity and sensitivity of the IIA and PPF proposals, there is a need for a full-time dedicated AOSGC officer to oversee the related legislative work and coordinate with stakeholders and government departments to prepare for the establishment of the IIA and PPF.

17. As we are engaging the industry and fine-tuning our proposals in response to industry feedback, the need for a longer duration of the post could not have been anticipated at the time the post was created two years ago. In light of the stakeholders' views on the IIA and PPF proposals and the latest progress of our work, we have reviewed the continued need for the PAS(FS)SD post and concluded that the post should be extended in

² There are sector-specific compensation schemes in place for non-life insurance policies covering motor vehicle third party claims and employees' work-related injuries. These types of insurance policies are mandated by statute. If an insurer of these compulsory policies becomes insolvent, compensation is paid to policyholders or third party claimants in respect of claims under the policies.

order to take forward the work related to the establishment of the IIA and PPF. Given the timeframe of these exercises, we propose to extend the post of PAS(FS)SD for about 24 months from 15 October 2013 to 31 October 2015.

18. The proposed job description of PAS(FS)SD is at Annex A.

Non-directorate support

19. PAS(FS)SD will be supported by a team of four time-limited non-directorate officers, comprising one Senior Administrative Officer, one Administrative Officer, one Personal Secretary I and one Assistant Clerical Officer.

ALTERNATIVES CONSIDERED

20. We have considered whether the duties of PAS(FS)SD can be absorbed by other colleagues in FSB upon lapsing of the post on 15 October 2013.

21. There are at present seven other PAS(FS)s in FSB overseeing different policy areas including securities and futures, banking, mandatory provident funds (MPF), insolvency and accountancy, rewriting of the Companies Ordinance and trust law reform, and Mainland-related measures on financial services. All of them are fully committed to other policy initiatives and legislative exercises which are significant to the development of financial services sector in Hong Kong. Regarding legislative work, FSB is preparing to introduce legislation for the regulation of over-the-counter derivative financial products, implementation of the scripless securities markets, improvement of the corporate insolvency regime, regulation of stored value facilities and retail payment systems, subsidiary legislation for the new Companies Ordinance, and subsidiary legislation for Basel III regulatory rules. FSB is also seeking to implement measures that aim to enhance the MPF Schemes and consolidate Hong Kong's position as an offshore Renminbi centre. It will not be viable to redeploy other PAS(FS)s to take up the proposed duties of PAS(FS)SD without prejudicing the delivery of policy initiatives and legislative exercises under their respective portfolios. An organisation chart of the FSB is at Annex B and the existing job descriptions of all other PAS(FS)s are at Annex C.

FINANCIAL IMPLICATION

22. The proposed extension of the supernumerary directorate post will bring about an additional notional annual salary cost at mid-point of \$1,696,200. The additional full annual average staff cost, including salaries and staff on-cost is \$2,427,000.

23. As for the four non-directorate civil service posts supporting PAS(FS)SD referred to in paragraph 19 above, the notional annual salary cost at mid-point is \$2,436,060 and the full annual average staff cost, including salaries and staff-on-cost, is \$3,274,404.

24. We have included sufficient provision in the 2013-14 draft Estimates and will include the necessary provision in the 2014-15 and 2015-16 draft Estimates to meet the cost of the proposal.

ADVICE SOUGHT

25. Members are invited to comment on the proposals. Subject to Member's views, we will seek the recommendation of the Establishment Subcommittee in May 2013 and approval from the FC in June 2013.

**Financial Services Branch
Financial Services and the Treasury Bureau
March 2013**

Proposed Job Description
Principal Assistant Secretary for Financial Services and the Treasury
(Financial Services) (Special Duties)

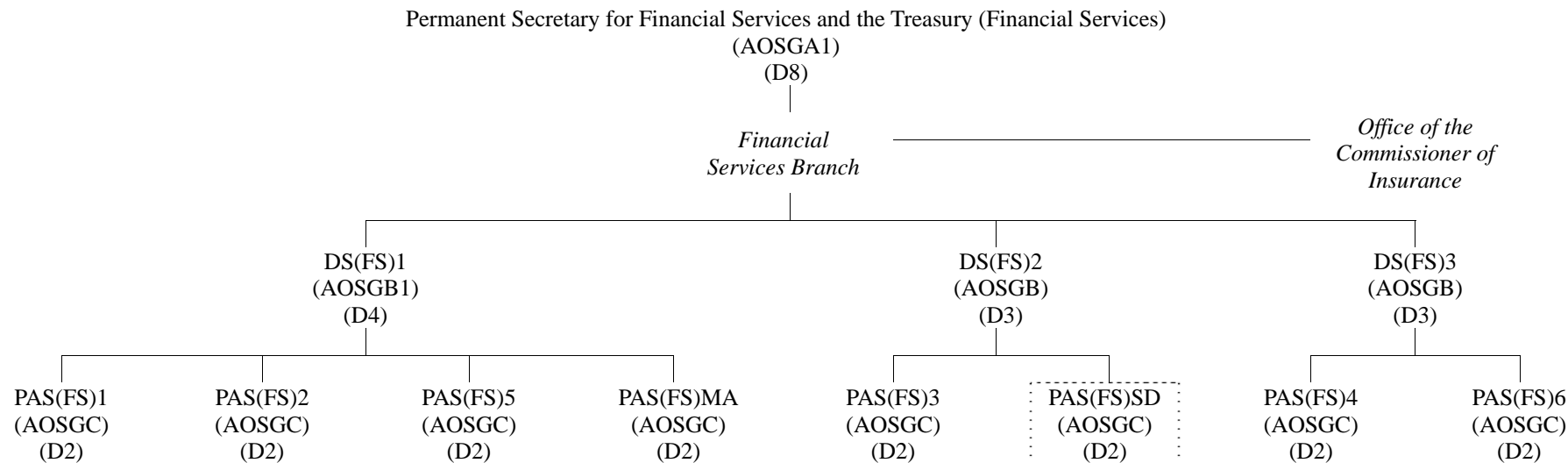
Rank : Administrative Officer Staff Grade C (D2)

Responsible to : Deputy Secretary for Financial Services and the Treasury (Financial Services) 2 (DS(FS)2)

Main Duties –

1. To engage the industry and other stakeholders in the formulation of the detailed proposals on the establishment of an independent Insurance Authority (IIA) and a Policyholders' Protection Fund (PPF) and work with the industry on the detailed transitional arrangements for the establishment of the IIA.
2. To prepare the detailed legislative proposals on the establishment of an IIA and a PPF, and oversee the drafting of the bills and the legislative process.
3. To handle corporate governance and high-level staffing matters in setting up an IIA, including formation of its governing board and advisory committees, and recruitment of its chief executive officer and other senior executives.
4. To provide policy support to the Office of the Commissioner of Insurance (OCI) in handling staff issues arising from the abolition of OCI upon establishment of an IIA.
5. To complete the necessary preparatory work (including the set-up of a provisional office as necessary and seeking funding support from the Finance Committee) for the IIA; and the legislative work on the subsidiary legislation with a view to enabling commencement of operation of an IIA in 2015.
6. To undertake any other duties as assigned by DS(FS)2.

Organisation Chart of the Financial Services and the Treasury Bureau (Financial Services Branch)



Legend

- Supernumerary directorate post to be extended
- AOSGA1 – Administrative Officer Staff Grade A1
- AOSGB1 – Administrative Officer Staff Grade B1
- AOSGB – Administrative Officer Staff Grade B
- AOSGC – Administrative Officer Staff Grade C
- DS(FS) – Deputy Secretary for Financial Services and the Treasury (Financial Services)
- PAS(FS) – Principal Assistant Secretary for Financial Services and the Treasury (Financial Services)

**Duties and Responsibilities of the Existing
Principal Assistant Secretaries (Financial Services) (“PAS(FS)s”)**

PAS(FS)1 is responsible for policy and matters relating to investor protection in the securities and futures markets and the development of the asset management industry. In addition, he/she provides policy input on supervision of intermediaries and of market operation, and deals with the housekeeping matters of the Securities and Futures Commission (SFC). He/She also coordinates the operation of the Securities and Futures Appeals Tribunal and the Market Misconduct Tribunal, provides secretariat support for the Process Review Panel for SFC, and coordinates among the financial regulators on risk management matters.

2. PAS(FS)2 is responsible for listing-related matters and liaison with the Hong Kong Exchanges and Clearing Limited. He/She works on the proposed legislation on the regulation of over-the-counter derivative market to implement the G20’s commitment and a scripless securities market in Hong Kong. He/She also handles matters relating to the development of the commodities market in Hong Kong.

3. PAS(FS)3 oversees policy and legislative matters over the Mandatory Provident Fund (MPF) Schemes and the Occupational Retirement Schemes. His/Her portfolio covers all MPF-related matters, including the housekeeping matters of the Mandatory Provident Fund Schemes Authority. He/She also handles housekeeping matters of the Census and Statistics Department.

4. PAS(FS)4 oversees an exercise to improve Hong Kong’s corporate insolvency law and is responsible for formulating the proposal on the introduction of a new corporate rescue procedure. He/She also oversees public and legislative matters concerning the accountancy profession, and assists in handling insolvency policy and administration and corporate governance of non-listed companies. He/She also deals with housekeeping matters of the Official Receiver’s Office and the Financial Reporting Council (FRC), and provides secretariat support for the Process Review Panel for FRC.

5. PAS(FS)5 is responsible for the review and maintenance of the Banking Ordinance including implementation of Basel III, and liaison with

the Hong Kong Monetary Authority on banking and other related issues. He/She oversees policy matters and legislation concerning the Deposit Protection Scheme, electronic retail payments, anti-money laundering for financial institutions, resolution regime for financial institutions as well as those relating to bond market development and Islamic finance. In addition, he/she coordinates input from financial services perspective in connection with Hong Kong's participation in relevant international and regional fora, including G20, Financial Stability Board, International Monetary Fund, Asia-Pacific Economic Cooperation, Asian Development Bank, Organization for Economic Co-operation and Development and the Financial Action Task Force on Money Laundering.

6. PAS(FS)6 deals with policies and legislation relating to companies and trusts. He/She co-ordinates the work relating to the new Companies Ordinance as well as the review of the Trustee Ordinance. He/She also deals with the housekeeping matters of the Companies Registry.

7. PAS(FS)MA coordinates the implementation of new measures by the Central People's Government (CPG) announced in August 2011 to support the economic and social development in Hong Kong. He/She also oversees the financial co-operation with the Mainland at the CPG and regional levels as a strategic goal under the National 12th Five-Year Plan as well as the development of offshore RMB business in Hong Kong.
