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Panel on Financial Affairs

Meeting on 5 January 2015

Background brief on proposal for staffing support to implement regulatory reforms for the insurance industry

Purpose

This paper provides background information on the staffing support to implement regulatory reforms for the insurance industry, including creation and retention of two supernumerary posts: an Administrative Officer Staff Grade C ("AOSGC") post in the Financial Services Branch ("FSB") under the Financial Services and the Treasury Bureau ("FSTB"), and an Assistant Commissioner of Insurance ("ACI") post in the Office of the Commissioner of Insurance ("OCI") of FSB. The paper also summarizes the concerns and views expressed by Members during discussions from 2011 to 2014 on the creation and retention of the above posts.

Background

Proposals to establish an independent Insurance Authority and a Policyholders' Protection Fund

2. The proposal of establishing an independent Insurance Authority ("IIA") was first announced by the former Financial Secretary in the 2003-2004 Budget Speech. The Administration conducted a stakeholder consultation on the proposal in mid-2003 and commissioned consultancy studies in 2007 and 2009 respectively. Following a public consultation on the framework of establishing an IIA in 2010, the Administration published the consultation conclusions and detailed proposals in 2011 for further industry engagement. The Administration consulted the public on key legislative proposals for establishing

an IIA from October 2012 to January 2013 and briefed the Panel on Financial Affairs ("FA Panel") on 5 July 2013.

3. According to the Administration, the policy objectives of setting up IIA are to modernize the insurance industry regulatory infrastructure to facilitate the stable development of the industry, provide better protection for policyholders, and comply with the requirement of the International Association of Insurance Supervisors that insurance regulators should be financially and operationally independent of the government and industry. The Administration also plans to set up a statutory regime for licensing insurance intermediaries to replace the existing self-regulatory system administered by three self-regulatory organizations ("SROs")¹.

4. The Insurance Companies (Amendment) Bill 2014 ("the Bill") was gazetted and received its First Reading in the Legislative Council ("LegCo") on 25 and 30 April 2014 respectively. The Bill seeks to amend the Insurance Companies Ordinance (Cap. 41) ("ICO") to: (a) establish IIA (as a body corporate) and the Insurance Appeals Tribunal; (b) provide for the enforcement powers of, and fees and levies payable to, IIA; (c) provide for better corporate governance of authorized insurers and a licensing system and conduct requirements for insurance intermediaries; and (d) provide for transitional and other related matters. At the House Committee meeting held on 2 May 2014, members agreed to form a Bills Committee to scrutinize the Bill.

5. The Administration has proposed to establish a Policyholders' Protection Fund ("PPF") for enhancing protection of insurance policyholders' interests and maintaining market stability in the event of insurer insolvency. In this regard, the Administration commissioned an actuarial consultancy study to assess the optimal levy rate, target fund size and other detailed arrangements for the proposed PPF in 2010, and conducted a public consultation on a detailed proposal in April 2011. The Administration announced the consultation conclusions and finalized proposals in January 2012 and reported the same to FA Panel on 6 February 2012. The Administration is preparing the relevant enabling legislation.

Creation and retention of a supernumerary post of AOSGC

6. In view of the scale, complexity and sensitivity of the IIA and PPF proposals, the Administration submitted a staffing proposal in early 2011 to create a supernumerary AOSGC post (D2) in FSB of FSTB for a period of three years to work on the implementation of both initiatives. FA Panel was briefed

¹ The three SROs are the Insurance Agents Registration Board under the Hong Kong Federation of Insurers, the Confederation of Insurance Brokers and the Professional Insurance Brokers Association.

on the staffing proposal on 3 January 2011. When the Establishment Subcommittee ("ESC") considered the proposal on 12 January 2011, some Members expressed concerns about the setting up of an IIA and considered that the Administration should focus its efforts on taking forward the initiative on PPF. The staffing proposal was voted on and rejected by ESC. The Administration subsequently revised the proposal by shortening the proposed duration of the post to 30 months and revised the duty list. The revised staffing proposal was endorsed by ESC on 16 February 2011 and approved by the Finance Committee ("FC") on 15 April 2011. The post was created for 30 months from 15 April 2011 to 14 October 2013.

7. Having regard to the progress of work on the two initiatives, the Administration considered it necessary to extend the post. FA Panel was consulted on 8 April 2013 on the retention of the post for a period of 24 months from 15 October 2013 to 31 October 2015. The proposal was discussed and endorsed by ESC on 15 and 29 May 2013 and approved by FC on 21 June 2013.

Creation and retention of a supernumerary post of Assistant Commissioner of Insurance

8. On 6 February 2012, the Administration briefed FA Panel on the proposal to create a supernumerary post of Assistant Commissioner of Insurance ("ACI") (D2) in the Office of the Commissioner of Insurance ("OCI") for a period of 24 months. According to the Administration, the proposed ACI post was required for strengthening the directorate support for enforcing the anti-money laundering ("AML") regime under the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance ("AMLO") in respect of insurers and insurance intermediaries, and performing the new regulatory functions over Mandatory Provident Fund ("MPF") intermediaries, whose main line of business is in the insurance sector, arising from the implementation of the Mandatory Provident Fund Schemes (Amendment) Ordinance 2012 ("MPFS(A)O"). The staffing proposal was endorsed by ESC on 2 May 2012 and subsequently approved by FC on 25 May 2012. The ACI post was created for 24 months from 25 May 2012 to 24 May 2014.

9. Apart from the duties related to implementation of the AML and MPF regulatory regimes, ACI also oversees the Insurance Intermediaries Team of OCI to monitor the operation of the current self-regulatory regime for insurance intermediaries and leads the Team to support FSTB in preparing for the transition from the self-regulatory regime to the new statutory licensing regime. The scope of work covers the preparatory work for the future transfer of relevant regulatory data of insurance intermediaries from the three SROs to IIA,

as well as consolidating existing codes of conduct and supervising guidelines published by the three SROs to facilitate the work of IIA in future.

10. In order to provide continued directorate support for FSTB on the establishment of IIA, the Administration consulted FA Panel on 6 January 2014 on the retention of the ACI post for 17 months from 25 May 2014 to 31 October 2015. The proposal was endorsed by ESC on 5 March 2014 and approved by FC on 6 June 2014.

Deliberations at meetings of the Panel on Financial Affairs and the Establishment Subcommittee

11. The major views and concerns expressed by Members on the creation and retention of the above AOSGC and ACI posts at meetings of FA Panel and ESC held from 2011 to 2014 are summarized in the ensuing paragraphs.

Supernumerary post of AOSGC

Scope of responsibilities and priority of work

12. At the FA Panel and ESC meetings on 3 January and 12 January 2011 respectively, members expressed concerns about the scale and complexity of the work in taking forward the IIA and PPF proposals. Noting that the Administration had agreed to conduct another round of public consultation on the IIA proposal, and in view of resource constraints, some Members considered that the setting up of PPF should have priority over the establishment of IIA for affording protection to insurance policyholders. The Administration advised that both initiatives were important and it was working on them concurrently. On the proposal for setting up a PPF, it involved very complicated technical issues, including the levy to be imposed, the types of insurance policies to be covered, whether corporate policyholders should be covered, the investment and compensation arrangements of the fund, etc.. These matters would have significant impacts on the insurance industry and policyholders. As for the proposal to establish an IIA, the Administration was analyzing the public views received during the three-month consultation exercise which was completed in October 2010. There was general support for the establishment of an IIA, whilst there were different views expressed on the details of the proposed IIA.

13. In view of Members' concerns expressed at the FA Panel and ESC meetings in January 2011, the Administration subsequently revised the staffing proposal to shorten the duration of the AOSGC post to 30 months and modified the duty list concerned. In respect of the work on IIA initiative, holder of the

AOSGC post would focus on developing proposals in addressing the comments received and meet public aspiration and market development needs, and continue to gauge views from the industry and other stakeholders in developing further detailed proposals to facilitate public discussion.

Transitional arrangements for the existing OCI and establishment size of the future IIA

14. Members noted that the existing OCI would be abolished upon establishment of IIA, and enquired about the arrangements for staff working in OCI upon abolition of the Office, as well as for setting up the provisional office to prepare for the establishment of IIA. The Administration advised that upon establishment of IIA, the general grades staff would be re-deployed to other bureaux/departments of the Government. All posts of IIA would be filled by open recruitments, and there would not be any direct transfer of existing staff from OCI to IIA. However, the existing insurance officers and contract staff in OCI might have a competitive edge owing to their relevant work experience.²

15. At the meetings of ESC on 15 and 29 May 2013, Members enquired about the number of staff members of the future IIA and whether a mechanism would be put in place for determining the remuneration packages of its senior management. The Administration advised that the proposed headcount of IIA would be 237 according to the consultation document released in 2010. It was likely that IIA would commission a consultant to, with reference to pay packages of the relevant industry, recommend on the appropriate remuneration packages for its executives.

Extension period for the AOSGC post

16. When FA Panel discussed the Administration's proposal to retain the AOSGC post at the meeting on 8 April 2013, members expressed concern whether the proposed two-year extension would be adequate to deal with the various tasks ahead and whether the Administration would seek further extension if the work for establishing IIA had not been completed nearer the expiry of the post. The Administration advised that its plan was to introduce the Bill into LegCo before the end of 2013, with a view to setting up IIA by

² According to supplementary information provided by the Administration in July 2013, as at 1 July 2013, there were 140 staff members in OCI, including 70 civil servants and 70 Non-Civil Service Contract ("NCSC") staff members. For the civil servants, the 22 general grades staff members would be re-deployed to other Government offices in accordance with established procedures. As for the other 48 staff members who were of the Insurance Officer grade, the Administration would consult them on the arrangements after OCI's transfer of functions to IIA and the abolition of OCI. As for the NCSC staff members, OCI would, having regard to the timetable of transition to IIA and operational needs, enter into contracts and maintain close liaison with them, in order to ensure that they would have ample time to plan ahead.

2015. The Administration projected that, in the absence of unexpected events, the relevant tasks could be completed by 2015.

Supernumerary post of ACI

Manpower of OCI during the transition period

17. When FA Panel discussed the proposal to create the post of ACI at the meeting on 6 February 2012, members enquired about the arrangement for the existing staff members of OCI upon the establishment of IIA, and stressed the importance for the Administration to ensure adequate provision of manpower resources to undertake the work of OCI during the transition period before the formal establishment of IIA. During the discussion of the proposal at the ESC meeting on 2 May 2012, Members agreed that there was a pressing need to create the supernumerary post of ACI having regard to OCI's new duties of supervising registered MPF intermediaries and strengthening the AML regulatory regime of the insurance sector.

Retention of the post in 2014 and responsibilities of the post

18. When FA Panel discussed the proposal to retain the ACI post for 17 months on 6 January 2014, members were concerned whether the proposed retention period would tie in with the establishment of IIA. At the ESC meeting on 5 March 2014, Members sought justifications for retaining the ACI post for 17 months and asked if the Administration would consider extending the post further when it lapsed in October 2015.

19. The Administration responded that the proposed retention period of 17 months had taken into account the expected timetable for the establishment of IIA. Given that the target date for the establishment of IIA had been deferred, it was necessary to retain the ACI post to perform the regulatory functions arising from implementation of AMLO and MPFS(A)O. On the reasons for the delay in the establishment of IIA, the Administration explained that as the two relevant consultation exercises had taken longer than originally expected, the introduction of the relevant bill into LegCo had been deferred accordingly. The Administration stressed that the continued need for the ACI post would be reviewed in light of the progress of scrutiny of the bill for the establishment of IIA.

20. In response to Members' enquiry about the tasks that the holder of the ACI post would be responsible for in discharging the regulatory functions arising from AMLO and MPFS(A)O, the Administration advised that the two ordinances stipulated various supervisory functions for the Insurance Authority

("IA"). AMLO stipulated the customer due diligence measures and record-keeping requirements to be undertaken by financial institutions in line with the relevant standards promulgated by the Financial Action Task Force. To implement the AML regulatory regime, IA had to carry out inspections on insurers and insurance intermediaries, i.e. insurance brokers and insurance agents. Under MPFS(A)O, IA assumed the statutory role as the frontline regulator responsible for the supervision of registered MPF intermediaries whose main line of business was in the insurance sector. IA would help ensure compliance by MPF intermediaries from the insurance sector with the conduct requirements on regulated activities specified in MPFS(A)O. Apart from the power to investigate into cases of suspected non-compliance under both regulatory regimes, IA was also empowered to impose disciplinary sanctions against insurance institutions and make prosecutions under AMLO. For MPF intermediaries from the insurance sector, the investigation findings would be forwarded to the Mandatory Provident Fund Schemes Authority for consideration of disciplinary sanctions or prosecutions according to provisions in Mandatory Provident Fund Schemes Ordinance.

Latest development

21. At the meeting to be held on 5 January 2015, the Administration will brief FA Panel on a proposal to retain the supernumerary posts of AOSGC and ACI, as well as the proposed creation of a new Preparatory Team to help set up IIA.

Relevant papers

22. A list of relevant papers is given in the **Appendix**.

List of relevant papers

Date	Event	Paper/Minutes of meeting
3 January 2011	The Panel on Financial Affairs ("FA Panel") was briefed on the creation of a supernumerary post of Administrative Officer Staff Grade C ("AOSGC") (D2) in the Financial Services Branch ("FSB") under the Financial Services and the Treasury Bureau ("FSTB")	<p>Administration's paper (LC Paper No. CB(1)910/10-11(03))</p> <p>Minutes (LC Paper No. CB(1)1336/10-11)</p>
12 January 2011	The Establishment Subcommittee ("ESC") discussed the creation of the supernumerary AOSGC post	<p>Administration's paper (EC(2010-11)17)</p> <p>Minutes (LC Paper No. ESC25/10-11)</p>
16 February 2011	ESC discussed the creation of the supernumerary AOSGC post	<p>Administration's paper (EC(2010-11)18)</p> <p>Minutes (LC Paper No. ESC33/10-11)</p>
15 April 2011	Meeting of the Finance Committee (FC)	<p>Minutes (LC Paper No. FC118/10-11)</p>
6 February 2012	FA Panel was briefed on the creation of a supernumerary post of Assistant Commissioner of Insurance ("ACI") in the Office of the Commissioner of Insurance	<p>Administration's paper (LC Paper No. CB(1)959/11-12(04))</p> <p>Minutes (LC Paper No. CB(1)1417/11-12)</p>

Date	Event	Paper/Minutes of meeting
2 May 2012	ESC discussed the creation of the supernumerary ACI post	Administration's paper (EC(2012-13)3) Minutes (LC Paper No. ESC40/11-12)
25 May 2012	Meeting of FC	Minutes (LC Paper No. FC181/11-12)
8 April 2013	FA Panel was consulted on the proposed retention of the supernumerary AOSGC post	Administration's paper (LC Paper No. CB(1)781/12-13(04)) Minutes (LC Paper No. CB(1)1654/12-13)
15 May 2013	ESC discussed the proposed retention of the supernumerary AOSGC post	Administration's paper (EC(2013-14)3) Minutes (LC Paper No. ESC42/12-13)
29 May 2013	ESC continued to discuss the proposed retention of the supernumerary AOSGC post	Administration's paper (EC(2013-14)3) Minutes (LC Paper No. ESC46/12-13)
21 June 2013	Meeting of FC	Minutes (LC Paper No. FC23/13-14)

Date	Event	Paper/Minutes of meeting
5 July 2013	FA Panel discussed the consultation conclusions of key legislative proposals on the establishment of an independent Insurance Authority	<p><u>Administration's paper</u> (LC Paper No. CB(1)1387/12-13(01))</p> <p><u>Minutes</u> (LC Paper No. CB(1)1838/12-13)</p> <p><u>Follow-up paper</u> (LC Paper No. CB(1)1633/12-13(02))</p>
6 January 2014	FA Panel was consulted on the proposed retention of the supernumerary ACI post	<p><u>Administration's paper</u> (LC Paper No. CB(1)625/13-14(10))</p> <p><u>Minutes</u> (LC Paper No. CB(1)1310/13-14)</p>
5 March 2014	ESC discussed the proposed retention of the supernumerary ACI post	<p><u>Administration's paper</u> (EC(2013-14)24)</p> <p><u>Minutes</u> (LC Paper No. ESC46/13-14)</p>
6 June 2014	Meeting of FC	<p><u>Minutes</u> (LC Paper No. FC55/14-15)</p>