Research Office
Legislative Council Secretariat

Information Note

Policyholders' protection schemes in selected places

IN08/17-18

1. Introduction

1.1 In Hong Kong, authorized insurers are subject to the prudential regulation under the Insurance Ordinance (Cap. 41) to ensure their financial soundness. Nevertheless, the possibility of insurer insolvency cannot be totally avoided. At present, if an insurer becomes insolvent, compensation schemes are only in place for non-life insurance policies covering employees' work-related injury compensation and motor vehicle third party claims.[1] There are no compensation funds for life insurance and other types of general (i.e. non-life) insurance if the insurer becomes insolvent.[2] This contrasts with many developed economies which have supplemented their prudential regulatory regimes with a policyholders' compensation fund to provide a safety net for policyholders in the event of an insurer's insolvency.

1.2 Against the above, there have been discussions about setting up a policyholders' compensation fund in Hong Kong to better protect policyholders' interest, maintain market stability in case of insurer insolvency, and enhance public confidence and competitiveness of the insurance industry. Indeed, as early as in 2011, the Government proposed a framework on Policy Holders' Protection Scheme ("PPS") for public consultation on details such as scope of coverage, level of compensation and funding approach.[3] The

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1 The Employees Compensation Insurer Insolvency Bureau administers an insolvency fund which assumes responsibility for the liabilities of insurers engaging in employees' compensation business that become insolvent on or after 1 April 2004. Likewise, the Motor Insurers' Bureau of Hong Kong sets up an insolvency fund which provides compensation to injured victims of traffic accidents where the drivers concerned are uninsured or untraceable, or the insurers concerned are insolvent.

2 Nevertheless, the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) ("CO") and the Insurance Ordinance (Cap. 41) contain specific provisions for dealing with insolvency of insurers. For insolvent non-life insurers, policyholders have a preferential claim against the remaining assets of the insurer under CO. For insolvent life insurers, the Insurance Ordinance has stipulated how the assets under their long term business fund are to be dealt with, and has also provided for the continuation of the life business in liquidation by the liquidator. See Financial Services and the Treasury Bureau (2011).

3 In the consultation document, the scheme was named Policyholders' Protection Fund. According to the latest government information, the scheme is now named Policy Holders' Protection Scheme. See Financial Services and the Treasury Bureau (2011) and (2018).

conclusions and proposals for PPS were announced by the Financial Services and the Treasury Bureau in January 2012. The Government has then proceeded with the preparation of the enabling legislation for establishing PPS.

1.3 At the meeting of the Panel on Financial Affairs to be held on 5 March 2018, the Government will brief Panel members on the legislative proposals of setting up PPS in Hong Kong. To facilitate members' deliberations, this information note aims to (a) provide information on the development of PPS in Hong Kong; and (b) study the major features of overseas policyholders' compensation funds by making reference to Singapore, a regional financial centre, and the United Kingdom ("UK"), the global centre for insurance.

2. Proposed Policy Holders' Protection Scheme in Hong Kong

2.1 The idea of establishing PPS in Hong Kong was first conceived in the early 2000s. Back in 2002, the Government commissioned a consultancy study on the feasibility of setting up PPS and subsequently conducted a public consultation exercise during 2003-2004. However, the public feedback was mixed. Some expressed support while some others, particularly members of the insurance industry, were concerned about possible moral hazard[4] and impact on premiums. According to the Government, it had at that time continued to engage in a dialogue with industry stakeholders to address the industry concerns. After much discussion and deliberation, the Hong Kong Federation of Insurers agreed in principle to explore a contingency plan to protect policyholders in case of insurer insolvency.

2.2 A conceptual framework on PPS was later developed by the Government in collaboration with the Hong Kong Federation of Insurers. On 6 July 2009, the Panel on Financial Affairs was briefed on the framework and members were in general supportive of establishing PPS. Subsequently, the Government commissioned an actuarial consultancy study to examine the details of implementing the proposed PPS, such as optimal levy rate and target fund size, and a public consultation ensued in 2011.

[4] After the introduction of PPS, insurers might become more aggressive in their pricing and investment strategies, thus increasing the potential for insurers becoming insolvent.

Proposed PPS for public consultation

2.3 As stated in the consultation document[5], the proposed PPS comprises two separate and independent funds, namely (a) **Life Fund** and (b) **Non-Life Fund**.[6] Life Fund covers all direct life policies written in Hong Kong, including term life policies, whole life policies, annuities, investment-linked policies and permanent disability policies. Non-Life Fund covers all direct non-life insurance policies written in Hong Kong, such as accident and health policies, home insurance policies and travel insurance policies. Employees' compensation and motor vehicle third party claims are excluded as they are already covered under other existing schemes.[7]

2.4 Major features of the proposed PPS are as follows:

(a) **coverage on policyholders:** PPS will cover natural persons, small and medium enterprises ("SMEs")[8], and building owners' corporations. SMEs are covered because they are considered less able than large corporates to protect their interests when buying policies and manage their risks.[9] Building owners' corporations are also included in the light of their statutory requirement to procure third party risk insurance since 2011;

(b) **participation of insurers:** all authorized direct life and non-life insurers are mandated to participate in PPS. Insurers domiciled in other jurisdictions with similar protection schemes may be exempted. However, exemption should be considered and approved by the PPS governing body on a case-by-case basis. Reinsurers and captive insurers[10] are not required to participate;

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5 See Financial Services and the Treasury Bureau (2011).

6 In the consultation document, the two funds were named Life Scheme and Non-life Scheme respectively. According to the latest government information, they are now known as Life Fund and Non-life Fund. See Financial Services and the Treasury Bureau (2011) and (2018).

7 See footnote 1.

8 In the consultation document, an SME is defined in the context of PPS as a manufacturing business which employs fewer than 100 persons in Hong Kong, or a non-manufacturing business which employs fewer than 50 persons in Hong Kong.

9 It is proposed that SMEs be required to self-declare at the time of policy procurement or renewal in order to spare the need for insurers to verify the SME status of policyholders, thereby minimizing the administrative cost impact on insurers.

10 A reinsurer is an insurance company that insures the risks of other insurance companies, whereas a captive insurer carries on insurance business to insure the risks of its parent and related companies.

(c) **compensation limit:** a compensation limit is proposed in order to strike a balance between the cost and benefit of PPS, and to minimize the risk of moral hazard that insurers might become more aggressive in pricing and investment strategies after the launch of PPS. **The proposed compensation limit is 100% for the first HK$100,000 of any claim**, **plus 80% of the balance up to a total of HK$1 million**. According to the consultation document, a claim for HK$1.225 million would hit the compensation limit of HK$1 million.[11] For **life insurance**, the compensation limit would be applied on a **per-policy basis** (for group life policies, compensation is on a per-life basis); for **non-life insurance**, the compensation limit would be applied on a **per-claim basis**.

Proposed funding arrangement

2.5 The Government has proposed in the consultation document a progressive funding model under which an initial target fund will be built up through a moderate levy on insurance premiums, with the option to impose a higher levy as necessary upon occurrence of insurer insolvency. Based on the actuarial consultancy study, the initial target fund size should be HK$1.2 billion for the Life Fund and HK$75 million for the Non-Life Fund, expectedly to be built up in 15 years. On this basis, the initial levy rates for both Schemes should be set at 0.07% of the applicable premiums, to be contributed by the insurers. It is proposed that the levy rates together with the target fund size would be reviewed after implementation of PPS.

2.6 In the event of insurer insolvency, funds in PPS would be deployed to meet the liability of the insurer. If the funds are not sufficient to meet all the liabilities especially during the fund accumulation stage, PPS would be able to borrow from a third party (such as commercial lenders with guarantee from the Government) to bridge the liquidity gap. Thereafter, a "stepped-up" levy may be collected. In addition, an asset recovery mechanism should be put in place until which any claims that have been compensated by PPS should be subrogated to PPS for recovery from the assets of the insolvent insurer.

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11 It is computed as: (HK$100,000 × 100%) + ((HK$1,225,000–HK$100,000) × 80%) = HK$1 million.

Proposed administration and governance arrangement

2.7 PPS will be established by legislation and operate under the oversight of an independent governing body, Policy Holders' Protection Board[12] ("PPS Board"), with its functions and powers stipulated in the statute. The PPS Board will be required to prepare and publish an annual report for both the Life Fund and Non-Life Fund, and its annual budget should be subject to the approval by the Financial Secretary. It will also have to exercise prudence in investing the money of PPS. On audit review of PPS, it is proposed that the Financial Secretary will have the power to appoint the Director of Audit or an external auditor to do so.

Discussions at the Panel on Financial Affairs in 2011 and 2012

2.8 The proposed PPS was discussed by the Panel on Financial Affairs at its meetings held on 4 April 2011 and 6 February 2012 respectively. At the meetings, members raised questions about the **methodology and assumptions adopted in determining the initial target fund size**. There were also members who were concerned that based on the **fixed levy rate**, PPS might amass a reserve fund much higher than the target level. The Government responded that there would be flexibility to review the levy after the target fund size had been achieved, taking into consideration the market situation at the time.

2.9 In addition, there were members who enquired about whether there would be a **mechanism to revise the levy rate** in case there was a large payout resulting from the insolvency of an insurance company. The Government responded that it would be difficult to predict the arrangement for revision of the levy in case of a large payout from PPS consequential to the insolvency of an insurance company. There were a number of unpredictable factors involved, such as the size of the PPS at the time, the amount of payout and the value of the remaining assets of the insolvent company. The Government said that in case of a funding gap, the PPS Board might take out loans from the Government or commercial lenders to meet the compensation payments. If such action was needed, the Legislative Council would be consulted.

[12] In the consultation document, the board was named Policyholders' Protection Fund Board. According to the latest government information, the board is now known as Policy Holders' Protection Board. See Financial Services and the Treasury Bureau (2011) and (2018).

2.10 In addition, some members also expressed concern that the **additional cost borne by the insurance companies arising from PPS would ultimately be transferred to policyholders**, and that the **cost of administering PPS** might be high. The Government responded that only a small team of professionals would be employed to administer PPS. In the event of insurer insolvency, the PPS Board might hire consultants or temporary professional staff to handle the compensation.

2.11 Some members also enquired about the **arrangement for premature termination of insurance policies in the event of insolvency**. The Government briefed that for a life policy or an accident and health policy with a guaranteed renewability clause, arrangement would be made to transfer the insurance policy to another insurance company. If the insurance policy could not be transferred and had to be terminated, the affected policyholder would be paid the cash/account value of the policy plus declared dividends/bonuses, and might also be paid an "ex-gratia payment" out of PPS to enable him or her to procure a similar policy in the market, with the total compensation up to a cap of HK$1 million. Additionally, there was a member giving views on the governance arrangements for PPS, opining that the Director of Audit should be empowered to carry out audit reviews on PPS at any time without requiring the appointment of the Financial Secretary.[13]

Latest developments

2.12 According to the Government's latest information, there are various new updates on PPS. For example, additional levy that needs to be collected in case of insurer insolvency is proposed to be capped in order to provide more certainty to insurers; for non-life policies, a time limit of 60 days after triggering PPS will be imposed for making compensation claims; and the governing body, PPS Board, may set up a Special Purpose Insurer to take over the policies of the failed insurer in case a commercial buyer cannot be secured.[14]

[13] See Legislative Council Secretariat (2011b) and Legislative Council Secretariat (2012).
[14] For further details, please see Financial Services and the Treasury Bureau (2018).

3. Singapore

3.1 The policyholders' compensation fund in Singapore is known as the Policy Owners' Protection Scheme ("the Singapore PPF Scheme"). It was first introduced in 1986 under the Insurance Act, and has undergone reviews and updates over the years. In 2011, the provisions under the Insurance Act were repealed and new provisions were introduced into the newly-enacted Deposit Insurance and Policy Owners' Protection Schemes Act.

3.2 The Singapore PPF Scheme is administered by the Singapore Deposit Insurance Corporation ("SDIC"). The Scheme comprises two funds, namely the **Policy Owners' Protection Life Fund** ("**PPF Life Fund**") **and the Policy Owners' Protection General Fund** ("**PPF General Fund**"). PPF Life Fund covers all life insurance policies, such as individual/group term life policies, whole life policies, and annuities.[15] Meanwhile, PPF General Fund covers (i) personal travel insurance policies; (ii) personal motor insurance policies; (iii) foreign domestic maid insurance policies; (iv) personal property (structure and contents) insurance policies; and (v) individual and group accident and health insurance policies. Notably, these general insurance policies must be Singapore policies, i.e. policies insure risks arising in Singapore or where the insured is a resident in Singapore or has a permanent establishment in Singapore.[16] In addition, PPF General Fund also covers compulsory insurance policies in relation to motor vehicles and work injury compensation.

3.3 Under the Singapore PPF Scheme, all insurers registered with the Monetary Authority of Singapore ("MAS") to carry on direct life business or direct general business are required to participate, except captive insurers, specialist insurers and professional reinsurers. The Scheme covers both individual and non-individual policyholders (including corporations), but there are different compensation limits for different types of life policies. No caps are applicable for general insurance policies. Major features of the Singapore PPF Scheme, in terms of compensation limits, funding arrangement, levies charged, target fund size, and governance arrangements are detailed in the paragraphs below.

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15 It also includes policies issued to non-Singapore residents but does not cover those issued by overseas branches of a registered direct insurer incorporated in Singapore.

16 The definition of a Singapore policy is given in Schedule 1 to the Insurance Act. See Singapore Statutes Online (2011).

Compensation limit

3.4 Under the Singapore PPF Scheme, different types of life policies are subject to different caps. For instance, for individual life and voluntary group life policies, compensation is 100% up to the cap of S$500,000 (HK$2.96 million) for aggregated guaranteed sum assured and S$100,000 (HK$592,000) for aggregated guaranteed surrender value (i.e. the amount entitled for early termination) on a **per life insured per insurer basis.**[17] For non-voluntary group life policies[18], the cap is S$100,000 (HK$592,000) for sum assured **per policy**. Where the sum assured or surrender value guaranteed payable exceeds the cap, a protection ratio will be applied in determining the compensation entitlement[19].

3.5 As to **compensation for general insurance policies**, there is **no cap**, as these polices typically indemnify losses and payouts are made based on actual claims incurred.[20] However, policyholders will only be compensated for claims incurred, up to 30 days after the winding up order is made against the failed insurer.

Funding arrangement

3.6 Funds in the Singapore PPF Scheme are contributed by the registered insurers in the form of levy. Initially, a post-funding approach was used where levies were imposed on insurers only when there was a need to make compensation payment. In order to make the system more equitable (i.e. requiring the failed insurer to contribute prior to default) and expedite payout,

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17 For example, if a policyholder owns three life insurance policies in an insurance company, and he or she is also the life insured under these policies, the total compensation for the guaranteed sum assured is capped at S$500,000 (HK$2.96 million) under the three policies.

18 Under the Insurance Act, non-voluntary group insurance policy means a group policy to insure the lives of certain individuals which is not taken out at the request or discretion of any of the life assureds.

19 For example, for an insured person holding two life policies (policy A and policy B) in an insurance company, if the guaranteed sum assured for policy A is S$400,000 (HK$2.37 million) and policy B is S$200,000 (HK$1.18 million), the combined guaranteed sum assured is S$600,000 (HK$3.55 million). Since it exceeds the cap of S$500,000 (HK$2.96 million), a protection ratio will be applied which is calculated as S$500,000/S$600,000 = 83.3%. Based on this protection ratio, the resultant compensation entitlement for policy A is S$400,000 x 83.3% = S$333,320 (HK$1.97 million), and that for policy B is S$200,000 x 83.3% = S$166,600 (HK$986,300). See Singapore Deposit Insurance Corporation (undated).

20 According to Monetary Authority of Singapore (2017), MAS is planning to introduce a cap to certain types of general insurance policies to prevent PPF General Fund from being potentially exposed to very high property claims which could otherwise translate into higher levies for insurers and in turn higher premium rates for consumers. The cap proposed for introduction is applicable to own property damage motor claims for personal motor insurance policies, and property damage claims for personal property (structure and contents) insurance, which is S$50,000 (HK$296,000) and S$300,000 (HK$1.78 million) respectively.

the Scheme has since 2011 adopted the **pre-funding approach**,[21] which may be complemented by **post-funding** arrangement in the event that the funds are insufficient for compensation, and money borrowing may also be an option to fund any costs of payout.[22]

Levies charged

3.7 The Singapore PPF Scheme has adopted a risk-based levy system, under which levy charged to individual insurers varies with the insurer's supervisory risk rating. The supervisory ratings are categorized into low, medium low, medium high, to high.[23] At present, the levy rates for PPF Life Fund and PPF General Fund are set out in **Table 1** below:

Table 1 – Levy rates under the Singapore PPF Scheme

Supervisory Ratings	PPF Life Fund (as a % of relevant protected liabilities of insurer)	PPF General Fund (as a % of relevant protected liabilities/gross premium income of insurer)
Low	0.028%	0.106%
Medium Low	0.033%	0.121%
Medium High	0.049%	0.181%
High	0.142%	0.529%

Source: Monetary Authority of Singapore (2011).

Target fund size

3.8 A target fund size has been set for PPF Life Fund and PPF General Fund respectively. It is set at 0.61% of the relevant aggregate protected liabilities for PPF Life Fund and 1.51% of the relevant gross premium income

21 See Monetary Authority of Singapore (2005) and (2010).

22 The relevant provisions are contained in section 40 of the Deposit Insurance and Policy Owners' Protection Schemes Act. The funding arrangement is confirmed by the Singapore Deposit Insurance Corporation in its email reply to the Research Office dated 7 February 2018.

23 Assessment of risks is based on the supervisory rating system developed by MAS, known as the Common Risk Assessment Framework and Techniques.

for PPF General Fund. The regulation provides that when the funds achieve or exceed the target size, a review of the levy rates may be conducted.[24]

Arrangements in the event of insurer insolvency

3.9 In the event of insurer insolvency, how the funds in the Singapore PPF Scheme will be used depend on the arrangement of the failed business. According to SDIC, the preferred course of action is to transfer the failed business to another insurer, especially if it is concerned with a life insurer as there is less disruption for policyholders. If the business is transferred to another insurer, the funds will be used to support the transfer. In this case, the insurer taking over must provide coverage to policyholders up to an amount no less than what they are covered under the Singapore PPF Scheme.

3.10 However, if a buyer cannot be found or if costs are excessive to facilitate a transfer, MAS may decide on termination if the impact on policyholders is not significant (e.g. policyholders can easily find alternative coverage). If so, the funds in the Singapore PPF Scheme will be used to compensate policyholders. On the other hand, if the impact on policyholders is significant, MAS may decide on a run-off. SDIC will take over the failed business and protection will continue to be provided until the policies have matured or expired. Similarly, the coverage is up to the amount no less than the protection under the Singapore PPF Scheme. Based on SDIC's financial statements in the past few years, there was no compensation paying out of the PPF Life Fund and PPF General Fund.

Governance arrangements

3.11 SDIC, designated as the deposit insurance and policy owners' protection fund agency, is a company limited by guarantee under the Companies Act. Defined under the Deposit Insurance and Policy Owners' Protection Schemes Act, its functions include collecting levies from insurers, managing the funds, making compensation payments and educating the public.[25] The board of SDIC is appointed by and accountable to the Minister in charge of MAS. The accounts of SDIC including PPF Life Fund and the PPF General Fund are subject to independent audit annually.

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[24] See Monetary Authority of Singapore (2011).

[25] SDIC is also responsible for managing the Deposit Insurance Scheme.

4. The United Kingdom

4.1 The UK has put in place a protection scheme to compensate policyholders in the event of insurer default. The scheme was formerly known as the Policyholders Protection Scheme which was replaced by the Financial Services Compensation Scheme ("FSCS") in 2001. FSCS is the compensation scheme set up under the Financial Services and Markets Act 2000 which acts as a statutory fund of last resort for customers of financial services firms authorized by Financial Conduct Authority ("FCA") and/or Prudential Regulation Authority ("PRA").[26]

4.2 In addition to insurance policies, FSCS also covers claims related to deposits, investment business, insurance broking and home finance.[27] On insurance policy protection, FSCS is applicable to life and general insurances, and excludes re-insurance and marine, aviation and credit insurance as they are related to commercial risk. FSCS covers mainly policyholders who are individuals and small businesses.[28] Large businesses are generally excluded unless under certain exceptions, e.g. for claims related to compulsory insurances.[29]

<u>Compensation limit</u>

4.3 Where compensation is payable, the current level of compensation is set as follows:[30]

(a) for **long-term insurance contracts** such as life and annuity, claims for benefits are provided 100% without upper limit; and

(b) for **general insurance contracts**, claims are provided 100% for (i) compulsory insurance; (ii) professional indemnity insurance;

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26 FCA regulates the conduct of authorized financial services firms and authorized individuals, while PRA at the Bank of England is responsible for prudential matters in banks, building societies, credit unions, insurers and major investment firms.

27 FSCS was set up in 2001 to replace five previous compensation schemes, including the Policyholders Protection Scheme (which protected insurance policyholders); the Deposit Guarantee Scheme (which covered bank deposits); a similar scheme for building societies; and the Investors Compensation Scheme (which protected customers of investment businesses).

28 Small businesses are those with an annual turnover of less than £1 million (HK$10.8 million).

29 See Financial Services Compensation Scheme (undated).

30 See Prudential Regulation Authority (2018).

and (iii) claims arising from death or incapacity of the policyholder due to injury, sickness or infirmity. For other types of general insurance contracts, protection is provided at 90% of claims with no upper limit.

Funding arrangement and levies charged

4.4 FSCS is funded on a **pay-as-you-go basis (i.e. raising levies as failures arise)**[31] and raises annual levies from authorized firms based on the costs expected to be incurred in the year ahead. Levy is made up of two cost elements: management expenses and compensation payments. The former are the costs of running FSCS, whereas the latter are for claims payment. FSCS comprises different funding classes according to the nature of business[32]. The funding classes relevant to insurance policies are "general insurance provision" and "life and pensions provision", which are contributed by the respective insurance businesses.

4.5 For the cost element of **management expenses**, it is subject to an annual limit, fixed by FCA and PRA following consultation with the industry.[33] For the cost element of **compensation payments**, the aggregate amount to be raised each year is determined based on the compensation payments expected to be made, subject to a limit. Details of the arrangements are as follows:

(a) **amount of levy to be raised for compensation payments:** the aggregate amount of levy to be raised each year is determined by the greater of the expected compensation payment in the 12 months following the levy date, or one-third of expected compensation in the 36 months following the levy date. FSCS will also take into account the claims already incurred and expected asset recoveries from the failed insurers. For individual firms, their levy contribution is calculated by reference to the share of its income (or similar parameters) as a proportion of the industry total in the respective funding class;[34] and

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31 See Financial Services Compensation Scheme (2016b).

32 The FSCS levy is split into eight broad classes: (a) deposits; (b) life and pensions; (c) general insurance; (d) general insurance intermediation; (e) life and pensions intermediation; (f) investment intermediation; (g) investments; and (h) home finance.

33 The element of management expenses is made up of base costs and specific costs. Base costs are the cost of running FSCS, while specific costs are the costs of assessing claims and making payments.

34 See Prudential Regulation Authority (2018) and Financial Services Compensation Scheme (2016a).

(b) **levy limits for compensation payments:** PRA has set out an annual limit on the aggregate amount FSCS can levy. The limit is determined with reference to the expected affordability of the firms as well as past funding needs. For the funding class of "life and pensions provision" and "general insurance provision", the annual limit is £690 million (HK$7.5 billion) and £600 million (HK$6.5 billion) respectively.[35] In the event that the cost incurred for compensation is not sufficiently covered by the levy, FSCS may impose an interim levy to meet the cost, or utilize other sources of funding such as commercial borrowing.[36]

4.6 While the pay-as-you-go funding mechanism is in use, it is subject to criticism that future claims are hard to predict accurately and the level of levies charged each year is volatile. While FCA agrees that a pre-funding arrangement might be able to reduce the levy volatility, it does not intend to pursue this option in view of a higher level of levies required to build a reserve for future claims and the high industry resistance ensues. Recently, FCA has indicated that it would consider introducing a risk-based levy system in the future that charges higher levies on financial services firms selling high-risk products. Whether the idea will come with further details and has an impact on the insurance industry remains to be seen.[37]

Arrangements in the event of insurer insolvency

4.7 According to the rules of PRA, in the event that an insurance firm is unable to meet claims against it, FSCS has a duty to make arrangements to secure the continuity of insurance for all eligible policyholders. This may be arranged, for example, by transferring the ongoing policies of the failed insurer to another insurance firm, or by arranging the issue of new policies from another insurer in substitution for existing policies. The insolvency practitioner of the failed insurer is expected to appoint a run-off agent to calculate the claims, which are then submitted to FSCS for confirmation and payment. During the financial year 2016-2017, there were no claims on FSCS in respect

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35 Under the current rules, however, some funding classes including "general insurance provision" and "life and pensions provision" are required to contribute towards other funding classes (e.g. "investment intermediation" and "home finance intermediation") in the event that funds in the latter classes are insufficient to meet the cost of payout.

36 See Prudential Regulation Authority (2018).

37 See Financial Conduct Authority (2016) and (2017), and FT Adviser (2017a).

of life and pensions insurance. For general insurance, there were claims for compensation due mainly to the failure of two general insurance companies, and the compensation costs incurred exceeded the annual levies collected. As a result, supplementary levy had to be raised to meet the cost of payout during the year.[38]

Governance arrangements

4.8 FSCS is a company limited by guarantee created under the Financial Services and Markets Act 2000 while subject to oversight and rules set by FCA and PRA. It is governed by a board of directors appointed by both FCA and PRA. The FSCS Board is responsible for setting policies, overseeing FSCS' operations, and approving budgets, among others. FSCS is operationally independent but accountable to FCA, PRA and the HM Treasury. The accounts of FSCS are audited annually and the Comptroller and Auditor General of the National Audit Office is the statutory auditor.

5. Conclusion

5.1 Based on the study above, the major features of the proposed PPS in Hong Kong and the policyholders' compensation funds in Singapore and the UK are highlighted in **Table 2** below.

[38] See Financial Services Compensation Schemes (2017a) and (2017b).

Table 2 – Summary of major features of policyholders' compensation funds in selected places

		Hong Kong	Singapore	United Kingdom
1.	Scheme	• Policy Holders' Protection Scheme.	• Policy Owners' Protection Scheme.	• Financial Services Compensation Scheme.
2.	Year of launch	• Under proposal.	• 1986.	• 2001.
3.	Sub-classes	• Life Fund. • Non-Life Fund.	• Policy Owners' Protection Life Fund. • Policy Owners' Protection General Fund.	• Life and pensions provision. • General insurance provision.
4.	Types of policyholders protected	• Individuals, SMEs and building owners' corporations.	• Individuals and non-individuals.	• Individuals and small businesses mainly.
5.	Compensation for life schemes	• 100% for the first HK$100,000 of claims, plus 80% of the balance up to HK$1 million, on a per policy basis. (For group life policies, compensation is on a per-life basis.)	• Different limits apply to different types of policies. For example, for individual life policies, compensation is 100% up to the limit of S$500,000 (HK$2.96 million) for guaranteed sum and S$100,000 (HK$592,000) for guaranteed surrender value, on a per life insured, per insurer basis.	• 100% of claims without limit.
6.	Compensation for non-life schemes (general schemes)	• 100% for the first HK$100,000 of claims, plus 80% of the balance up to HK$1 million, on a per claim basis.	• 100% coverage of claims without limit.	• 100% without limit for (a) compulsory insurance; (b) professional indemnity insurance; and (c) claims arising from death or incapacity due to injury, sickness or infirmity. • For other types of general insurance, 90% of claims without limit.
7.	Funding mechanism	• Progressive funding – initial moderate levy rate, complemented by a "stepped-up" levy rate upon occurrence of insolvency.	• Pre-funding, which may be complemented by post-funding to meet the cost of payout.	• Pay-as-you-go funding, based on compensation payment expected to be made in the year ahead.
8.	Levy collection	• Collection from insurers at a uniform rate.	• Collection from insurers based on the risk-based levy system.	• Collection from insurers based on the share of income relative to the industry.
9.	Administration and governing body	• Policy Holders' Protection Board.	• Singapore Deposit Insurance Corporation.	• Financial Services Compensation Scheme Limited.

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Hong Kong

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