LegCo Panel on Financial Affairs
(Meeting on 3 July 2001)

Monitoring of the Financial Position of Insurance Companies and the Compensation Arrangements for Insurance Policy Holders

Market Overview

1. As at 31 May 2001, there were 207 authorized insurers in Hong Kong. Of these insurers, 46 were long term insurers, 142 were general insurers and 19 were composite insurers (carrying on both long term and general insurance business). About half (105) of the authorized insurers were incorporated outside Hong Kong.

2. In 1999, the total gross premiums written by the Hong Kong insurance industry grew by 6.7% to HK$57.8 billion, representing 4.7% of the Hong Kong Gross Domestic Product. General business recorded a continued premium decline of 8% to HK$16.5 billion while the long term business continued to grow by 14% to HK$41.3 billion.

3. The year 2000 provisional statistics showed signs of recovery for general business, with a 0.7% increase in gross premiums while premiums for new long term business, particularly new retirement scheme business due to the implementation of the Mandatory Provident Fund schemes, grew by 34%.

Regulation of Insurance Companies

4. The principal function of the Insurance Authority ("IA") is to regulate and supervise the insurance industry for the promotion of the general stability of the insurance industry and for the protection of the insuring public.

5. All authorized insurers are required to comply with the provisions of the Insurance Companies Ordinance ("the Ordinance"). The major requirements are -
   - minimum paid-up capital
   - minimum solvency margin
   - fit and proper person
   - adequate reinsurance arrangement

6. *Minimum paid-up capital* — the minimum paid-up capital is HK$10 million, or HK$20 million for a composite insurer or for an insurer wishing to carry on statutory classes of insurance business (i.e. motor third party liability, pleasure vessel third party liability and employees' compensation insurance business).

7. *Minimum solvency margin* — the solvency margin is the amount of excess in value of the assets over liabilities required to be maintained by an insurer.

   For general business, the solvency margin is determined according to an insurer's relevant premium income or relevant claims outstanding, whichever is the greater.

   For long term business, the solvency margin is generally linked to the mathematical reserves and the capital at risk as specified under the Insurance Companies (Margin of Solvency) Regulation, subject to a minimum of HK$2 million.

8. *Fit and proper person* — the Ordinance requires that any person who is a director or controller of an insurer must be "fit and proper" to hold such position.

9. *Adequate reinsurance arrangements* — the Ordinance requires that adequate reinsurance arrangements are in force, or will be made, for the reinsurance of risks written by the insurer.

Continuous Monitoring

10. Under the Ordinance, all authorized insurers are subject to the prudential supervision of the IA. On-going monitoring of the authorized insurers is principally carried out through examination of the audited financial statements, actuarial investigation reports and business returns submitted by them on an annual basis. Where necessary, the IA may require such returns to be submitted more frequently (e.g. quarterly) for early review. The IA will also conduct regular on-site inspections to the insurers to ensure that they comply with the statutory requirements.

11. Where the IA has concern over the affairs of an insurer, he may exercise powers of intervention for the purpose of protecting the interests of policy holders. The major powers of intervention are -

    - Restriction on new business

    - Restrictions on investments

- Acceleration of submission of financial information

- Custody of assets by a trustee

- Limitation of premium income

- Special actuarial investigations of long term business

- Making of bank deposits in the name of the IA

- Other residual powers

In extreme circumstances where the exercise of the above powers would not appropriately safeguard the interests of policy holders, the IA will consider the appointment of an advisor or manager and as a last resort, to present a petition for winding up the insurer concerned.

Recent Developments

12. The IA has been proactive in the regulation and supervision of the insurance industry. The insurance regulatory framework is kept under constant review in the light of operational experience, market developments and international trends to ensure its effectiveness. New initiatives are introduced from time to time to enhance policy holders protection. The following are some examples.

13. In order to enhance the transparency of the industry, quarterly statistics of the industry on an aggregate basis has been published by the IA since the first quarter of 1998. Such statistics has also been made available to the public through the IA's website since the first quarter of 1999. Furthermore, the IA has been releasing individual insurers' annual statistics commencing with the Annual Report for 1998.

14. To strengthen reserves for investment guarantees, the IA has issued in January 2001 a Guidance Note on Reserving Standards for Investment Guarantees to ensure that insurers carrying on the relevant class of retirement scheme management business will set aside sufficient funds to meet their obligations in respect of such business. To enhance corporate governance, the IA is at present working on a Guidance Note on the Corporate Governance of Authorized Insurers. The Guidance Note will set out the roles and duties of the directors and controllers and will provide guidance on good practices for insurers to follow.

15. The IA initiated in 2000 an educational drive through the publication of the quarterly newsletter — "I lens" and 2 pamphlets, namely "Know the Insurance

Agents and Brokers at Your Service" and "Insurance Intermediaries in Hong Kong". To continue with the drive, 2 further insurance educational pamphlets will be published within 2001 to provide the general public with some guidance on the matters they need to be aware of when buying new insurance policies or replacing their existing insurance policies.

Compensation Arrangements in winding-up cases for Insurance Policy Holders

16. There are two compensation funds which provide relief to claimants in respect of motor and employees' compensation insurance respectively.

17. For motor insurance, the Motor Insurers' Bureau of Hong Kong ("MIB") provides compensation to injured victims of traffic accidents where the drivers concerned are uninsured or untraceable, or the insurers concerned are insolvent. Established in 1980, the MIB administers two funds, namely the First Fund and the Insolvency Fund. The First Fund provides relief to a traffic accident victim suffering bodily injury who is unable to obtain compensation because the driver is uninsured or untraceable. The Insolvency Fund compensates a claimant whose claims for bodily injury resulting from a traffic accident remain unsettled owing to the insolvency of the insurer concerned. The Insolvency Fund is financed by a levy on the motor insurance premiums payable by the policy holders.

18. For employees' compensation insurance, the Employees Compensation Assistance Fund will render relief. This fund is administered by the Employees Compensation Assistance Fund Board established under the Employees Compensation Assistance Ordinance. One of its functions is to reimburse an employer who has taken out an insurance policy and paid compensation to an employee but is unable to obtain recovery under the insurance policy because of the insolvency of the insurer concerned. It is financed by a levy on premiums payable in respect of employees' compensation insurance policies.

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