

# **立法會**

## ***Legislative Council***

LC Paper No. CB(1)1494/13-14(02)

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### **Bills Committee on Insurance Companies (Amendment) Bill 2014**

#### **Background brief**

#### **Purpose**

This paper provides background information on the Insurance Companies (Amendment) Bill 2014 ("the Bill") and a summary of the major views and concerns expressed by Members on related issues.

#### **Background**

##### Existing regulatory framework of the insurance industry

2. At present, the Commissioner of Insurance is appointed by the Chief Executive ("CE") under section 4(1) of the Insurance Companies Ordinance (Cap. 41) ("ICO") as the Insurance Authority ("IA") to carry out the principal function of regulating and supervising the insurance industry for the promotion of the general stability of the insurance industry and for the protection of existing and potential policyholders as set out in section 4A(1) of ICO. The Commissioner of Insurance is supported by the Office of the Commissioner of Insurance ("OCI"), which is a government department.

3. According to OCI, there are 154 authorized insurers<sup>1</sup> in Hong Kong as at 31 March 2013. IA regulates them through examination of their financial statements and business returns, and also by on-site inspections. While IA can impose under ICO intervention measures on insurers, it does not have explicit powers to enter into the premises of insurers to conduct inspections and investigations, issue reprimands, impose fines or prosecute offences summarily.

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<sup>1</sup> Under ICO, an insurer is a person carrying on insurance business. An insurer has to apply to IA for authorization to carry on insurance business in or from Hong Kong.

4. As at 31 March 2013, there are some 76 800 insurance intermediaries<sup>2</sup> in Hong Kong regulated by three self-regulatory organizations ("SROs")<sup>3</sup>. While IA has certain powers over these SROs, such as instructing them to issue and amend codes of practices and requiring them to produce information, she does not regulate the intermediaries direct. The SROs handle complaints against individual intermediaries, and conduct investigations and impose disciplinary sanctions as appropriate. In addition, insurance intermediaries who are bank employees are registered with the Insurance Agents Registration Board ("IARB") for engaging in the sale of insurance products in banks. IARB monitors their compliance with conduct requirements and handles complaints referred by the Hong Kong Monetary Authority ("HKMA") via OCI. HKMA does not have direct power to discipline those bank employees.

The Administration's initiative to establish an independent insurance authority and a statutory licensing regime for insurance intermediaries

5. The proposal of establishing an independent IA ("IIA") was first announced by the former Financial Secretary in the 2003-2004 Budget Speech. The Administration subsequently 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 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 the establishment of an IIA from October 2012 to January 2013 and announced the consultation conclusions in June 2013.

6. 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 an independent regulatory regime for insurance intermediaries to replace the existing self-regulatory system administered by the three SROs. The major features of the proposed regulatory regime under the Bill are as follows:

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<sup>2</sup> Under ICO, an insurance intermediary means an insurance agent or an insurance broker. The former is a person who holds himself out to advise on or arrange contracts of insurance in or from Hong Kong as an agent or subagent of one or more insurers while the latter is a person who carries on the business of negotiating or arranging contracts of insurance in or from Hong Kong as the agent of the policy holder or potential policy holder or advising on matters related to insurance. It is an offence under the ICO for an insurer to effect a contract of insurance through, or accept insurance business referred to it by, an insurance intermediary who has not been properly appointed (for insurance agent) or authorized (for insurance broker).

<sup>3</sup> 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.

### Establishment of IIA with new regulatory powers

- (a) An IIA will be established to replace OCI and take up its regulatory responsibilities.
- (b) IIA will be vested with powers to conduct investigations in respect of authorized insurers' contraventions (e.g. the power to conduct inspection and to enter premises and search for, seize and remove records and documents under a magistrate's warrant), and to impose disciplinary sanctions including reprimand, fines, suspension or revocation of licence of insurance intermediaries or authorization of insurers.
- (c) Subject to the approval of CE in Council, IIA may delegate its powers of inspection and investigation to HKMA for the frontline regulation of banks' insurance intermediary activities. IIA will remain the single authority to set regulatory requirements, to grant licences and to impose disciplinary sanctions.
- (d) As checks and balances, an Insurance Appeals Tribunal ("IAT") will be established to review certain decisions made by IIA.
- (e) IIA will be financed by fees payable by insurers and insurance intermediaries, user fees for providing specific services by IIA, and a levy of 0.1%<sup>4</sup> on insurance premiums for all insurance policies.

### Licensing and regulation of insurance intermediaries

- (f) Under the new regime, a person requires a licence granted by IIA to carry on "regulated activities", including inviting or inducing, or attempting to invite or induce, a person to enter into a contract of insurance or to make a material decision (e.g. the making of an application or proposal for a contract of insurance).
- (g) Regarding conduct requirements for insurance intermediaries, broad and commonly-adopted principles will be stipulated in the primary legislation with details to be set out in subsidiary legislation and non-statutory codes and guidelines. A licensed insurance agency or a licensed broker company would be required to appoint at least one responsible officer ("RO") who should ensure that internal control systems and procedures are in place to

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<sup>4</sup> The levy, which will be subject to a cap of \$100 per life insurance policy and \$5,000 per non-life insurance policy in a year, would reach the target level of 0.1% in the sixth year of IIA's establishment through an incremental approach.

promote compliance with conduct requirements within a body corporate.

## **The Bill**

7. The date of First Reading of the Bill is 30 April 2014. The Bill seeks to amend ICO to: (a) establish IIA (as a body corporate) and IAT; (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.

8. The main provisions of the Bill are explained in paragraph 20 of the Legislative Council ("LegCo") Brief (File Ref: C2/2/50C issued on 16 April 2014), and paragraphs 5 to 11 of the Legal Service Division Report on the Bill (LC Paper No. LS50/13-14).

## **Major views and concerns expressed by Members**

9. On 19 July 2010, the Administration discussed with the Panel on Financial Affairs ("FA Panel") on the proposals for establishing IIA. FA Panel subsequently held a special meeting on 12 October 2010 to receive public views on the subject. FA Panel was briefed on the conclusions of the 2010 consultation and the Administration's detailed proposals at the meeting on 4 July 2011. The Administration further briefed FA Panel on the key legislative proposals of the Bill at its meeting on 5 July 2013. The major concerns and views expressed by members during FA Panel meetings and the Administration's responses are summarized below.

### The Governing Board of the independent Insurance Authority

10. Members welcomed the proposals to increase more representatives from the insurance industry in the Governing Board of IIA ("the GB"), and incorporate members from the insurance industry to the two Industry Advisory Committees of IIA and the Expert Panel. Noting that the legislative proposals only specified that the GB would comprise "at least two directors with knowledge of and experience in the insurance industry", some members relayed the industry's concern that such an arrangement could not ensure sufficient representation of the insurance industry on the GB and suggested that the Bill should specify that one-third of the directors in the GB must be representatives from the insurance industry and include representatives from the insurance intermediaries.

11. The Administration responded that IIA was an independent financial regulator with law enforcement power, and was not an industry organization. It was important that the GB should be broadly based and representative of stakeholders as well as have the necessary expertise in carrying out its regulatory functions. On the other hand, issues relating to the composition of the GB of a financial regulator had to be considered carefully given the need to ensure independence in exercising the regulatory powers by IIA. The current proposal was formulated having regard to the diverse views among respondents to the public consultation on the participation of the insurance industry in the GB of IIA. The Administration was also mindful of the need for IIA to maintain close dialogue and liaison with the insurance industry on matters relating to its regulation and development.

#### Power and functions of the independent Insurance Authority

12. In response to members' enquiry about the major difference between the regulatory regime of IIA and that under the Securities and Futures Ordinance (Cap. 571) ("SFO"), the Administration pointed out that in formulating the regulatory regime of the insurance intermediaries, the Administration had made reference to similar regulatory regimes, including that for the Mandatory Provident Fund ("MPF") intermediaries which was endorsed by LegCo in 2012. The regulatory regime for the MPF intermediaries itself had also drawn reference from the regime under SFO. Therefore, there were common features among the three regimes.

13. Some members considered that the function of IIA should include promotion of the development of the insurance industry apart from regulation of the insurance market. On the other hand, some members were of the view that there should be a clear demarcation of responsibilities between IIA and the Financial Services and the Treasury Bureau ("FSTB"). Moreover, IIA's main responsibilities should focus on the regulation of the industry instead of promoting the development of the insurance market.

14. The Administration said that the legislative proposals had included a new function for IIA to promote the competitiveness of the insurance industry in the global insurance market. In formulating new regulatory requirements for insurance intermediaries, IIA would also seek to adopt a pro-compliance attitude in order to facilitate the intermediaries to comply with the requirements, e.g. by issuing guidelines. The Administration added that while FSTB was responsible for policy initiatives to enhance market development, the relevant regulatory bodies had to draw up the relevant regulatory guidelines/rules correspondingly. Hence there was a division of labour between the Government policy bureau and the relevant regulatory bodies.

15. Members noted the Administration's decision of not pursuing the introduction of the specified suspension power ("SSP") in the legislative proposals. While some members welcomed the decision, other members enquired about measures IIA would take to enhance protection for policyholders against repeated misconduct committed by insurers or insurance intermediaries and breaches of requirements by them, and whether the Securities and Futures Commission ("SFC") was currently vested with power similar to SSP.

16. The Administration responded that there were concerns from the insurance industry to the introduction of SSP on grounds of procedural justice. Having regard to the relevant views, the Administration decided not to pursue the introduction of SSP but to ensure effective implementation of the other regulatory arrangements to protect the policyholders. For instance, the appointment of an RO by an insurer or a corporate insurance intermediary to enhance conduct regulation and imposition of disciplinary sanctions by IIA against misconduct committed by regulated persons. The Administration also advised that SFC was not vested with any power similar to SSP under SFO.

17. Some members expressed concern that since investigations by IIA would be kept confidential as in the case of those carried out by the Securities and Futures Commission and HKMA, it would be difficult for the public to monitor IIA's investigations. The Administration responded that a balance had to be struck between transparency and fairness as it would be unfair to the subject of investigation if a regulatory body disclosed the identity of the subject before completion of its investigation. It was also the international practice that a financial regulatory organization would abide by the confidentiality principle when it conducted investigation.

18. In response to members' enquiry about whether IIA would develop guidelines to elaborate the standards expected by the regulator to facilitate compliance by the insurers and insurance intermediaries, the Administration remarked that IIA would issue relevant guidelines to facilitate compliance with conduct requirements by insurers and insurance intermediaries, and the guidelines might cover areas such as providing suitable training for employees to promote conduct compliance, conducting regular assessment of conduct compliance by insurance intermediaries, etc.

19. With the increase in the number of complex insurance products in the market, some members enquired whether IIA would be empowered to authorize new insurance products. The Administration responded that insurance was a private contract between a policyholder and an insurer. The insurer would need to design different insurance products to meet the needs of their clients. Having regard to overseas experience, the Administration considered that IIA would not possess the necessary commercial knowledge to approve new insurance products to meet evolving market needs. However, it was envisaged

that IIA would closely monitor the changing market landscape and issue guidelines for strengthening product disclosure, in order to enable potential policyholders to make an informed decision.

20. Pointing out that some investment-linked insurance products consisted mainly of investment elements and were financial products in essence, members were concerned about whether such insurance products were subject to the regulation of SFC and were concerned about consumer protection. A member also had reservation about providing IIA with the power to regulate investment-linked insurance products. Some members further pointed out that the Lehman Brothers incident had exposed problems of subjecting one industry to the regulation by multiple regulatory authorities, including inconsistent regulatory standards adopted by different regulators and practitioners unfamiliar with certain financial products could be allowed to sell such products. They opined that the amendment bill should plug these loopholes.

21. The Administration responded that a stringent regulatory approach was adopted in approving the offering documents of investment-linked insurance products, and confirmed that such products would fall under the definition of "collective investment scheme" of SFO and were subject to approval by SFC. This arrangement would remain unchanged upon the establishment of IIA. Moreover, the conduct requirements of insurance intermediaries would be strengthened upon the establishment of IIA. The current self-regulatory regime for insurance intermediaries would be replaced by a statutory licensing regime, under which IIA could impose licensing conditions on insurance intermediaries in view of new market developments.

#### Pecuniary penalty on insurers and insurance intermediaries

22. Some members relayed the industry's concern about the proposed heavy pecuniary penalty limit of \$10 million for misconduct of regulated persons and enquired whether the Administration would consider the industry's suggestion of imposing different pecuniary penalties for corporate intermediaries and individual intermediaries, and imposing the pecuniary penalty on regulated persons with reference to the profit gained by them as result of the misconduct. Some members also suggested that the bill should specify that the pecuniary penalty imposed by IIA should not put a regulated person into financial jeopardy. On the other hand, some members expressed support for the maximum pecuniary penalty of \$10 million to enhance protection for consumers.

23. The Administration responded that there was a wide spectrum of regulated persons in the insurance industry and it was important that the pecuniary penalties should have adequate deterrence against non-compliance or misconduct of different regulated persons. The Administration also pointed out that it would be difficult to implement the suggestion of imposing different

pecuniary penalty levels for corporate and individual regulated persons. The Administration had made reference to the practices of other financial regulators and noted that these regulators would, in addition to the specification of a statutory pecuniary penalty maximum, publish guidelines on how they might calibrate the level of a pecuniary penalty. It was envisaged that the future IIA would also be mindful that the penalty imposed should not put the regulated persons into financial jeopardy. The Administration further remarked that apart from the absolute amount, insurance intermediaries, especially the large ones, would also be concerned as to how the pecuniary penalty would affect their reputation. Apart from the pecuniary penalty, a range of other disciplinary sanctions, including reprimand, suspension or revocation of licence, and prohibition of licence application within a specified period, would be available to IIA.

#### Issue of "dual regulators for one industry"

24. Members were concerned about inconsistent regulatory standards resulted from the proposed regulatory regime involving IIA and HKMA, and enquired how the Administration would address the insurance industry's concern about "dual regulators for one industry". Some members were concerned how IIA and HKMA would prevent double jeopardy on the same misconduct committed by an intermediary.

25. The Administration responded that under the legislative proposals, IIA would be the lead regulator for all insurance intermediary activities by, say setting the relevant conduct standards and requirements, and acting as the sole licensing authority for intermediaries working for insurance agencies and banks alike. HKMA, which possessed more experience and expertise in the overall regulation of banks, would be delegated with specified functions (viz. day-to-day inspection and investigation) for effective regulation of banks' insurance intermediary activities in the context of the whole operation of banks. However, IIA would be the focal point for administering the disciplinary process; and the independent IAT would hear all appeal cases concerning licensed insurance intermediaries working for insurance agencies and banks. IIA would be the sole regulator responsible for imposing sanctions on misconduct of all insurance intermediaries including those engaged by banks.

26. In response to members' concern about the different disclosure requirements for insurance intermediaries and bank employees selling insurance products, the Administration remarked that as many banks in Hong Kong were offering a mix of financial products to their clients, it was important that IIA would maintain close liaison and coordination with HKMA to ensure effective regulation, minimize regulatory duplication or gaps, and avoid inconsistency in regulatory standards in order to create a business-friendly environment and level playing field for both bank and non-bank insurance intermediary activities. In

discharging their responsibilities in specific cases, they had to act in accordance with the law.

### Disciplinary and appellate mechanism

27. Members enquired about the details of the proposed IAT for review of IIA's disciplinary sanctions, and whether IIA's disciplinary committee would include representatives from the insurance industry or persons with knowledge of and experience in the insurance industry.

28. The Administration responded that in formulating the disciplinary and appellate mechanism under IIA regime, the Administration had made reference to other relevant regulatory regimes, including that for MPF intermediaries and that under SFO. The Administration also pointed out that IAT would be set up as an independent quasi-judiciary body to hear appeals against the decisions of IIA. Under the legislative proposals of the Bill, an IAT hearing would be chaired by a person eligible for appointment as a High Court judge with two market practitioners as members. IAT might confirm, vary or set aside IIA's decisions or remit the matter to IIA with directions as appropriate. IIA would also set up an Expert Panel with a broad range of insurance expertise to provide it with advice on market practices or specific products for making disciplinary decisions.

### Conduct requirements and appointment of a responsible officer

29. Noting that an insurer and a corporate insurance intermediary was required to appoint an RO to monitor the internal control system to ensure compliance of conduct requirements by insurance practitioners, a member suggested that the Administration should consider the Hong Kong Federation of Insurers' suggestion to allow the delegation of the responsibility of RO to a designated officer of the insurance company so that the Chief Executive Officer ("CEO") of the company would concentrate on other important tasks.

30. The Administration said that the CEO of an insurance company should be appointed as the RO because the CEO would have the power to deploy adequate resources for putting in place an appropriate internal control system and staff training programmes to ensure conduct compliance by insurance agents appointed by the company. The Administration added that the CEOs of insurance companies were already held responsible for the whole of the company's business under the existing law and the Administration considered that the new regulatory regime should not dilute the pre-existing requirement.

### Funding arrangements

31. Some members considered that the levy, which stood at 0.1% on insurance premiums for all insurance policies, should not be borne by policyholders. The Administration responded that the funding proposal was based on the "user-pay" principle. The feedback from the respondents to the public consultation showed that the public generally accepted the proposed levy in order to finance the operation of IIA for the better protection of policyholders' interests. The Administration also advised that in accordance with regulatory principle, it was important for IIA to be financially independent to perform its statutory regulatory functions in an equitable and impartial manner.

### Liaison with stakeholders and staffing arrangements

32. The Administration took note of members' views about the importance to continue communication with the insurance industry before introducing the amendment bill into LegCo. Noting that there would be no direct transfer of the existing staff working in OCI to the proposed IIA, members requested the Administration to provide information on the arrangements for OCI staff upon abolition of OCI. At members' request, the Administration has provided supplementary information to address their concerns<sup>5</sup>.

### **References**

33. A list of relevant papers is in the **Appendix**.

Council Business Division 1  
Legislative Council Secretariat  
 26 May 2014

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<sup>5</sup> The Administration's written response was circulated to members vide LC Paper No. CB(1)1633/12-13(02) issued on 30 July 2013.

## List of relevant papers

Date/Period	Event	Paper/Minutes of meeting
19 July 2010	FA Panel was consulted on the proposed establishment of an independent Insurance Authority (IIA)	<a href="#">Discussion paper</a> (LC Paper No. CB(1)2525/09-10(01))  <a href="#">Minutes</a> (LC Paper No. CB(1)2933/09-10)
12 October 2010	FA Panel discussed the proposed establishment of IIA with deputations	<a href="#">Discussion paper</a> (LC Paper No. CB(1)2525/09-10(01))  <a href="#">Minutes</a> (LC Paper No. CB(1)827/10-11)
4 July 2011	FA Panel was consulted by the Administration on the detailed proposals for the establishment of an IIA	<a href="#">Discussion paper</a> (LC Paper No. CB(1)2590/10-11(01))  <a href="#">Minutes</a> (LC Paper No. CB(1)324/11-12)
26 October 2012	The Administration launched consultation on the key legislative amendments for establishment of IIA	<a href="#">Consultation Paper</a>  <a href="#">Press Release</a>
26 June 2013	The Administration published the consultation conclusions on the key legislative proposals for the establishment of IIA	<a href="#">Press release</a>  <a href="#">Consultation conclusions</a>
5 July 2013	FA Panel was consulted by the Administration on the consultation conclusions on key legislative proposals regarding the proposed establishment of IIA	<a href="#">Administration's paper</a> (LC Paper No. CB(1)1387/12-13(01))  <a href="#">Minutes</a> (LC Paper No. CB(1)1838/12-13)  Follow up papers <a href="#">1</a> and <a href="#">2</a> (LC Paper No. CB(1)1633/12-13(02) and LC Paper No. CB(1)1685/12-13(01))

<b>Date/Period</b>	<b>Event</b>	<b>Paper/Minutes of meeting</b>
30 April 2014	The Insurance Companies (Amendment) Bill 2014 was introduced into the Legislative Council	<a href="#">The Bill</a> <a href="#">Legislative Council Brief</a> <a href="#">Legal Service Division report</a> (LC Paper No. LS50/13-14)