

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

New Part IA and New Schedules 1B, 1C & 1D

INTRODUCTION

This paper briefs Members on the policy objectives and major provisions in the new Part IA of as well as new Schedules 1B, 1C and 1D to the Insurance Companies Ordinance (Cap. 41) (“ICO”), added by the Insurance Companies (Amendment) Bill 2014 (“the Bill”) concerning the constitution, functions and powers of the independent Insurance Authority (“IA”).

BACKGROUND

2. At present, the Insurance Authority (“IA”) is a public officer (viz. the Commissioner of Insurance) who is supported by a government department, i.e. the Office of the Commissioner of Insurance (“OCI”) established under the Financial Services and the Treasury Bureau. Both the IA and staff at the OCI are government employees. The principal functions of the IA are to ensure that the interests of policy holders or potential policy holders are protected and to promote the general stability of the insurance industry.

3. The IA discharges his/her functions in accordance with the ICO. The ICO has provisions governing the regulation of insurers in Hong Kong.¹ The ICO also provides for the operation of a self-regulatory regime under which insurance agents and brokers are registered with and supervised by three Self-regulatory Organizations (“SROs”)².

¹ An insurer must be authorized by the IA before carrying on insurance business in or from Hong Kong. The IA has set out the criteria for authorization which include, among other things, strong financial position, proper management, viable business plan and physical presence in Hong Kong.

² The three SROs are the Insurance Agents Registration Board established under the Hong Kong Federation of Insurers, the Hong Kong Confederation of Insurance Brokers, and the Professional Insurance Brokers Association.

POLICY OBJECTIVES AND MAJOR PROVISIONS

(a) Establishment and Constitution of the IIA

4. Clause 9 of the Bill adds a new section 4AAA to the ICO to provide for the establishment of the IIA. In particular, the new section 4AAA(1) establishes the IIA as a body corporate, i.e. it is an insurance regulator independent of the Government and will replace the existing IA. Hence, the appointment of a public officer as the IA under the existing section 4(1) of the ICO will be repealed by Clause 10 of the Bill.

5. We need to ensure that the transition to the IIA is seamless so that performance of important existing functions (e.g. prudential regulation of insurers) will not be interrupted. Therefore, section 4AAA(2) introduces a mechanism through which the IIA is to be renamed as “Provisional Insurance Authority” (“PIA”) immediately after its establishment. The PIA will be given certain administrative powers to undertake essential preparatory work, such as recruiting key personnel, leasing office premises and procuring office and IT equipment, etc., before the full-fledged IIA may replace the existing IA.

6. Clause 11 adds a new section 4AA to the ICO to set out the detailed provisions concerning the composition of the IIA which comprises a chairperson who is a non-executive director, a Chief Executive Officer (“CEO”) who is an executive director, and not less than six directors. All directors are appointed by the Chief Executive (“CE”) (see new section 4AA(1)). There will also be a majority of non-executive directors in order to ensure effective oversight of executive decisions (see new section 4AA(2)). Members of the IIA should have expertise relevant to the regulatory functions of the IIA. As specified in new section 4AA(3), apart from at least two non-executive directors with knowledge of and experience in the insurance industry, the IIA should comprise persons with knowledge in actuarial science, accountancy, law, consumer affairs, or other suitable professional experience.

7. New Schedule 1B provides detailed arrangements concerning the constitution and proceedings of the IIA, including functions and office as well as removal of members of the IIA (sections 3 and 4 of that Schedule), administration of meetings and resolutions (sections 6 to 8 of that Schedule), disclosure of pecuniary interests by members of the IIA and handling conflicts of interests (section 5 of that Schedule), as well as

relevant arrangements in case the position of the chairperson or CEO is vacant (sections 1 and 2 of that Schedule).

(b) Functions and Powers of the IIA

8. Clause 12 of the Bill amends the existing section 4A of the ICO which specifies the functions of the IIA. While the principal functions of the regulator will remain unchanged (see paragraph 3 above),³ some new functions are added by the Bill such as the regulation of the conduct of insurance intermediaries through a licensing regime (under the new section 4A(2)(ea)).

9. During the public consultation on the key legislative proposals on the IIA, the insurance industry advocated that the IIA should promote the development of the industry and expressed concerns about over-regulation. We agree that in discharging its regulatory functions, the IIA should also give due regard to market innovation and the competitiveness of the insurance industry of Hong Kong. We have therefore included facilitating “the sustainable market development of the insurance industry” and promoting “the competitiveness of the insurance industry in the global insurance market” as statutory functions of the IIA (new section 4A(2)(ec)).

10. Insurance has the social value of cushioning the public financially against unfortunate events. In addition to promoting best practices among insurance practitioners, it is equally significant to educate the public on the nature of insurance, features of particular insurance products and assessment of insurance needs against various risks. Based on these considerations and industry feedback, the IIA will also be tasked to promote understanding by policy holders and potential policy holders of insurance products and insurance industry (new section 4A(2)(eb)) and conduct studies into matters affecting the insurance industry (new section 4A(2)(ed)). The IIA will assist the Financial Secretary (“FS”) in maintaining the financial stability of Hong Kong as well (new section 4A(2)(ee)).

11. The new section 4B of the ICO (as added by Clause 13 of the Bill) confers upon the IIA general powers to do such things that are necessary for, or incidental to, the performance of its functions, and

³ The statutory functions of the IIA are set out at **Annex**.

specific powers that are essential to the operation of the IIA, e.g. entering into contracts. The new section 4E (as added by Clause 13 of the Bill) further specifies that the IIA may employ its own staff and engage consultants, agents or advisors to assist its work.

(c) Industry Advisory Committees (“IACs”) and Consultative Committees

12. The new sections 4C and 4D of the ICO (as added by Clause 13 of the Bill) provide the IIA with power to set up committees to further its work. The new section 4C provides that the IIA should establish at least two IACs, one for long term business and the other for general business, to advise it on industry-related issues and policies, and the new Schedule 1C (as added by Clause 86 of the Bill) specifies the constitution and proceedings of the IACs. Section 1 of the new Schedule 1C prescribes that members of an IAC include the chairperson and CEO of the IIA, not more than two executive directors of the IIA, and 8 to 12 other members appointed by the FS after consultation with the IIA who are persons with knowledge of or experience in the insurance industry, the conduct of insurance intermediary activities and consumer affairs. Section 3 of the new Schedule 1C further provides that an IAC would meet at least once every three months. The composition of the IACs makes them effective regular communication platforms between the highest echelon of the IIA and stakeholders, including the insurance industry.

13. The IIA may establish additional IACs after consulting the FS on any matters regarding the performance of its functions. Under the new section 4D, the IIA can also establish consultative committees on topical issues to engage the industry.

(d) Delegation of Functions

14. For practical and operational reasons, it is necessary for the IIA to have the power to delegate some of its functions to members of the IIA, committees and its employees. This is provided for in the new section 4F. The new section 4F(4) gives the IIA power to revoke a delegation and attach restrictions or conditions to a delegation.

15. As safeguards, some key functions of the IIA are made non-delegable. As listed in the new Schedule 1D to the ICO (as added by Clause 86 of the Bill), these include the power to make subsidiary

legislation and issue codes and guidelines (section 1(a) and 1(o) of that Schedule respectively), the power to authorize an insurer to carry on insurance business (section 1(m) of that Schedule), and the delegation of power to appoint inspectors and investigators to the Monetary Authority (“MA”) under the new section 4G (section 1(i) of that Schedule). According to the new section 4G, the IIA may, subject to the approval of the CE in Council, delegate its powers to appoint inspectors and investigators to the MA for the frontline regulation of banks’ insurance intermediary activities. The policy objectives and details of the delegation will be discussed under the provisions related to the establishment of the statutory licensing regime for insurance intermediaries. By virtue of the new section 4F(5), after delegation, the IIA may exercise such powers concurrently.

(e) Accounting and Financial Arrangements

16. Clause 15 of the Bill adds a new Division 2 of Part IA to the ICO (consisting of new sections 5A to 5G) which sets out the accounting and financial arrangements of the IIA. The major sources of IIA’s income are fees payable by insurers and insurance intermediaries, user fees for providing specific services by the IIA, and a levy of 0.1% on insurance premiums for all insurance policies (capped at \$100 for life policies and \$5,000 for non-life policies)⁴. The new section 5B requires the IIA to prepare and submit its corporate plan to the FS for approval. The corporate plan shall comprise the objectives of IIA’s activities, the nature and scope of the activities to be undertaken in order to achieve those objectives, and the estimates of IIA’s income and expenditure.⁵ The new section 5D requires the IIA to keep proper accounts and records of its transactions, and prepare its annual report to the FS. The new section 5E provides that the IIA must, with the approval of the FS, appoint one or more auditors to audit its annual financial statements. The FS should table the estimates, the annual report and the audited

⁴ As we will adopt an incremental approach for the introduction of a levy on insurance premiums, the Administration will, subject to the approval of the Finance Committee, provide a lump sum of \$500 million to the IIA, partly as seed money for the IIA to meet part of its expenses in the initial five years before the target levels of licence fees and levy are set in, and partly as contingency reserve.

⁵ The new section 4H provides that upon the request of the FS, the IIA must provide him with information on its policies and practices as well as the reasons for pursuing those policies and practices.

financial statement with the auditor's report to the Legislative Council ("LegCo"). As a check and balance, the Director of Audit may conduct value for money audit on the IIA (new section 5E(3)). While we envisage that the levy as well as fees and charges of the IIA should generate sufficient income to support its operation, the new section 5C provides a mechanism through which the Government can provide the IIA with funding approved by the LegCo. The IIA is exempt from taxation (new section 5G).

Financial Services and the Treasury Bureau
June 2014

Statutory Functions of the IIA

(re. the revised section 4A in Clause 12 of the Bill)

- (1) The principal function of the IIA shall be to regulate and supervise the insurance industry for the promotion of the general stability of the insurance industry and for the protection of existing and potential policy holders.
- (2) Without limiting the generality of subsection (1), the IIA shall –
 - (a) be responsible for supervising an authorized insurer's and a licensed insurance intermediary's compliance with the provisions of this Ordinance;
 - (b) consider and propose reforms of the law relating to insurance business;
 - (c) promote and encourage the adoption of proper standards of conduct and sound and prudent business practices by authorized insurers;
 - (d) promote and encourage the adoption of proper standards of conduct by licensed insurance intermediaries;
 - (da) review and, if necessary, propose reforms of the systems for regulating authorized insurers and licensed insurance intermediaries;
 - ~~(e) promote and develop self-regulation by market and professional bodies of the insurance industry;~~
 - (ea) regulate the conduct of insurance intermediaries through a licensing regime;
 - (eb) promote the understanding by policy holders and potential policy holders of insurance products and the insurance industry;
 - (ec) formulate effective regulatory strategies and facilitate sustainable market development of the insurance industry, and

promote the competitiveness of the insurance industry in the global insurance market;

- (ed) conduct studies into matters affecting the insurance industry;
- (ee) assist the FS in maintaining the financial stability of Hong Kong by taking appropriate measures in relation to the insurance industry; and
- (f) co-operate with and assist financial services supervisory authorities of Hong Kong or of any place outside Hong Kong, whenever appropriate, to the extent permitted by the Ordinance; and
- (g) perform functions imposed or conferred on the IIA by this or any other Ordinance.

Note: The functions that will be repealed by the Bill are crossed-out, and the revised/new functions underlined.