File Ref.: INS/2/3C(2017)

LEGISLATIVE COUNCIL BRIEF

Insurance Ordinance[1]
(Chapter 41)

INSURANCE (LEVY) ORDER

INSURANCE (LEVY) REGULATION

INTRODUCTION

At the meeting of the Executive Council on 6 June 2017, the Council ADVISED and the Chief Executive ORDERED that the Insurance (Levy) Order ("the Order") (at **Annex A**) and the Insurance (Levy) Regulation ("the Regulation") (at **Annex B**) should be made. This paper briefs Members on the two pieces of subsidiary legislation which enable the Insurance Authority ("IA") to collect levy on insurance premiums from policy holders.

JUSTIFICATIONS

2. Enacted in July 2015, the Insurance Companies (Amendment) Ordinance 2015 ("Amendment Ordinance") provides for, among other things, the establishment of IA which will take over the statutory functions of the Office of the Commissioner of Insurance ("OCI"), a government department, to regulate insurance companies and the supervisory functions of the existing three Self-regulatory Organizations ("SROs")[2] to regulate insurance intermediaries.

3. To ensure a smooth transition from OCI to IA, the Amendment Ordinance is being commenced in three stages as follows –

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1 The Insurance Companies Ordinance (Cap. 41) will be renamed as "Insurance Ordinance" when section 4 of the Insurance Companies (Amendment) Ordinance 2015 comes into operation on 26 June 2017.

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.

Stage 1: IA was established on 7 December 2015 and immediately renamed as the Provisional Insurance Authority ("PIA") to undertake essential preparatory work;

Stage 2: PIA will be renamed as IA to take over the functions of the existing OCI to regulate insurance companies on 26 June 2017; and

Stage 3: IA is expected to implement the new statutory licensing regime and take over the regulation of insurance intermediaries from the three SROs within two years from the commencement of Stage 2.

4. It is the requirement of the International Association of Insurance Supervisors ("IAIS") that insurance regulators should be financially and operationally independent of the Government and the industry. Specifically, one of the Insurance Core Principles of the IAIS requires that an insurance regulator should be "free from undue political, governmental and industry interference in the performance of supervisory responsibilities". To achieve this objective, while Government funding of $650 million has been set aside for supporting the establishment and initial years of operation of IA, the long-term target is that about 70% of IA's expenditure will be met by income from a levy on insurance premiums from policy holders and the remaining 30% by income from various fees payable by the industry[3]. Accordingly, IA is empowered under the Amendment Ordinance to collect levy from policy holders and various fees from insurance companies and insurance intermediaries, etc.

5. With the approval of the Legislative Council ("LegCo"), the relevant subsidiary legislation on the collection of the authorization fees and user fees will take effect from 26 June 2017 when IA takes over the statutory functions of OCI. The collection of levy should also commence as soon as possible so that IA may recover its operating cost via income from the market early. To allow some lead time for preparation including the launching of publicity measures as well as the modifications of accounting and billing systems by insurance companies, it is proposed that the collection of levy will start on 1 January 2018. Our proposals are set out in the ensuing paragraphs.

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[3] These various fees include authorization fees payable by insurance companies, licence fees payable by insurance intermediaries and user fees on specific services mostly applicable to the industry. Licence fees will be dealt with when the statutory licensing regime for insurance intermediaries enters into force in Stage 3.

Proposals

6. As provided under the Amendment Ordinance, the levy on premiums of insurance policies will be payable by policy holders. Reinsurance policies and policies underwritten by captive insurance companies[4] will be exempt from the levy, and so are marine, aviation and goods-in-transit policies, having taken into account similar practice in overseas regimes. Policies which are already paid up before the implementation of levy are not subject to the levy.

Payment and Remittance

7. IA will collect the levy from policy holders through insurance companies. The insurance companies must remit to IA the sums of levy payable during a specified remittance period, together with a remittance return.

Incremental Approach

8. To reduce the impact on policy holders, an incremental approach[5] will be adopted for introducing the levy. Specifically, the levy rate will start at 0.04% and increase gradually on a yearly basis until it reaches the target level of 0.1%. It should be noted that under the Amendment Ordinance, if, during a financial year of IA, the reserves of IA, after deducting depreciations and all provisions, are more than twice its estimated operating expenses and there is no outstanding debt, IA is required to consult the Financial Secretary with a view to recommending to this Council a reduction of the levy[6].

Cap

9. A cap would be imposed on the levy on general insurance policies with annual premiums at or above $5 million and long term insurance policies with single or annualized premiums at or above

[4] A captive insurance company, a risk financing tool of conglomerates, is set up by the mother company to insure the risk of companies of the same group only. All policy holders of a captive insurance company are companies of the group.

[5] The incremental pattern is as follows –

	1.1.2018 – 31.3.2019	**1.4.2019 – 31.3.2020**	**1.4.2020 – 31.3.2021**	**from 1.4.2021 onwards**
Levy Rate	0.04%	0.06%	0.085%	0.1%

[6] Section 135 of the amended Cap. 41.

$100,000. In other words, on full implementation (i.e. when the levy rate hits 0.1%), the cap for long term policy will be $100 and that for general policy will be $5,000. To maintain a level-playing field, group life insurance policies with medical protection offered by employers will be subject to the levy cap for general business. Otherwise, insurance companies carrying on long term business will, arguably, have an advantage over those carrying on general business in selling such policies due to the difference in the cap level.

Refund

10. If an insurance company refunds its policy holders the premiums paid wholly or partially, the corresponding levy paid[7] must be refunded accordingly. If the amount concerned has already been remitted to IA, insurance companies may adjust and reflect the refund in a subsequent remittance.

Consequences of Non-payment, Excessive Collection and Non-remittance of Levy

11. Under the Amendment Ordinance, IA may recover outstanding levy as a civil debt due to it. If a policy holder has not paid the levy as required, IA may impose on the policy holder concerned a pecuniary penalty not exceeding $5,000. If an insurance company has collected excessive levy from a policy holder, IA may impose on the company concerned a pecuniary penalty not exceeding $10,000. If an insurance company has not remitted the levy to IA as required, IA may impose on the company concerned a pecuniary penalty not exceeding $10,000 or 20 times the amount of the levies that were not remitted, whichever is the greater.

THE ORDER AND REGULATION

12. The Order at Annex A and the Regulation at Annex B seek to implement the proposals. The main provisions are explained below –

[7] IA plans to prescribe in the guideline for industry that the amount of levy to be refunded must be proportional to the amount of premium refunded except for policies which are cancelled within the cooling-off period where full refund of levy is to be made irrespective of whether the premium is fully refunded.

(a) Section 1 of Annexes A and B provides for the commencement date.

(b) Sections 4 to 6 of Annex A prescribe the amount of levy payable and maximum levy payable.

(c) Schedule to Annex A provides for the rates of levy.

(d) Section 3 of Annex B provides for the payment of levy.

(e) Sections 4 to 7 of Annex B provide for the requirements on remittance of levy.

LEGISLATIVE TIMETABLE

13. The legislative timetable is as follows –

Publication in the Gazette	9 June 2017
Tabling before LegCo	14 June 2017

IMPLICATIONS OF THE PROPOSALS

14. The proposals are in conformity with the Basic Law, including the provisions concerning human rights. The proposals will not affect the current binding effect of the Insurance Ordinance (Cap. 41). The proposals do not have civil service, environmental, productivity, gender, sustainability or significant family implications. The financial and economic implications are set out in **Annex C**.

MAINLAND RELATIONS AND RELATED PUBLIC RELATIONS MEASURES

15. The proposals have no implication for Mainland relations. No related public relations measure is considered necessary.

PUBLIC CONSULTATION

16. The Government launched a three-month public consultation from October 2012 to January 2013 on the key legislative proposals for the establishment of IA, including the proposals on the funding mechanism. General support was received. In order to iron out the

collection mechanism and other implementation details in respect of the levy, we have been engaging the insurance industry through the Hong Kong Federation of Insurers since February 2016. The Panel on Financial Affairs of LegCo was consulted on 15 November 2016. Panel Members did not raise any objections.

PUBLICITY

17. A press release will be issued and a government spokesperson will be available to answer enquiries. Subject to the approval of the Order and the Regulation by LegCo, publicity measures will be launched before the collection of levy commences on 1 January 2018.

ENQUIRIES

18. Enquiries relating to this brief can be addressed to Ms Joan Hung, Principal Assistant Secretary for Financial Services and the Treasury (Financial Services), at 2810 2201.

Financial Services and the Treasury Bureau
7 June 2017

Insurance (Levy) Order

(Made by the Chief Executive in Council under section 134 of the Insurance Ordinance (Cap. 41))

1. Commencement

This Order comes into operation on 1 January 2018.

2. Interpretation

In this Order—

inception anniversary date (開立周年日), in relation to a contract of insurance, means the day and month of each year that correspond to the inception date of the contract;

inception date (開立日), in relation to a contract of insurance, means the date on which the first premium under the contract becomes payable;

policy year (保單年度)—

(a) in relation to a contract of insurance that lasts for more than 12 months, means—

(i) the 12-month period beginning on the inception date;

(ii) each subsequent 12-month period beginning on an inception anniversary date; or

(iii) the period beginning on the last inception anniversary date and ending on the date on which the contract expires; or

(b) in relation to a contract of insurance that lasts for 12 months or less, means the period beginning on the inception date and ending on the date on which the contract expires;

premium (保費)—see section 3;

specified general business (指明一般業務) means insurance business of the nature specified in—

(a) class 1, 3, 4, 8, 9, 10, 13, 14, 15, 16 or 17 in Part 3 of Schedule 1 to the Ordinance; or

(b) class 2 in Part 3 of that Schedule, regardless of whether the business is also of the nature specified in class I in Part 2 of that Schedule;

specified long term business (指明長期業務)—

(a) means insurance business of the nature specified in any of the classes in Part 2 of Schedule 1 to the Ordinance; but

(b) excludes insurance business of the nature specified in both class I in Part 2, and class 2 in Part 3, of that Schedule.

3. Meaning of *premium*

(1) For the purposes of this Order, premium, in relation to a contract of insurance, is the amount of the premium receivable—

(a) after deducting—

(i) any discounts specified in the contract; and

(ii) any refunds of premiums made in respect of any avoidance or reduction of risks; and

(b) before deducting—

(i) any premiums for reinsurance ceded; and

(ii) any commission payable by the authorized insurer for the contract in relation to a Hong Kong insurance business, or a Hong Kong long term insurance business, as defined by paragraph 1(1) of Schedule 3 to the Ordinance.

(2) To avoid doubt, premium—

(a) includes any premium paid otherwise than in cash; and

(b) excludes any premium settled by way of a waiver of premium by an authorized insurer.

4. Levy payable for premium

For the purposes of section 134(1) of the Ordinance, a levy is payable for each premium payment made under a contract of insurance if—

(a) the contract relates to—

(i) specified general business; or

(ii) specified long term business;

(b) the contract is not—

(i) a contract of reinsurance; or

(ii) a contract of insurance underwritten by a captive insurer; and

(c) the policy year for which the premium payment is made begins in a period set out in column 1 of the Schedule.

5. Amount of levy

Subject to section 6, the amount of levy payable for each premium payment is the amount of the premium multiplied by the levy rate set out in column 2 of the Schedule opposite to the period set out in column 1 of the Schedule in which the policy year for which the premium payment is made begins.

6. Maximum levy

(1) If—

(a) there is a premium payment schedule in a contract of insurance; and

(b) the schedule stipulates that premiums are payable more than once a year,

then—

(c) the maximum aggregate amount of levies payable for scheduled premium payments for a policy year is the relevant maximum amount; and

(d) if there is one or more extra premium payments for the policy year, the maximum aggregate amount of levies payable for the scheduled premium payments and extra premium payments for the policy year is the relevant maximum amount.

(2) If—

(a) there is a premium payment schedule in a contract of insurance; and

(b) the schedule stipulates that a premium is payable once a year,

then—

(c) the maximum amount of levy payable for each scheduled premium payment is the relevant maximum amount; and

(d) if there is one or more extra premium payments for a policy year, the maximum aggregate amount of levies payable for the scheduled premium payment and extra premium payments for the policy year is the relevant maximum amount.

(3) If—

(a) there is a premium payment schedule in a contract of insurance; and

(b) the schedule stipulates that a premium is payable once in more than a year (***insurance period***),

then—

(c) the maximum amount of levy payable for each scheduled premium payment is the relevant maximum amount multiplied by the specified ratio for the contract; and

(d) if there is one or more extra premium payments for the insurance period, the maximum aggregate amount of levies payable for the scheduled premium payment and extra premium payments for the insurance period is the relevant maximum amount multiplied by the specified ratio for the contract.

(4) If there is no premium payment schedule in a contract of insurance, the maximum amount of levy payable for each premium payment is the relevant maximum amount.

(5) For the purposes of subsections (1), (2), (3) and (4), the relevant maximum amount is the amount set out in column 3 or 4 of the Schedule (as may be appropriate) specified opposite to the period set out in column 1 of the Schedule in which the policy year for which the relevant premium payment is made begins.

(6) In this section—

extra premium payment (額外保費付款), in relation to a contract of insurance, means a premium payment that is not stipulated in the contract's premium payment schedule;

scheduled premium payment (議定保費付款), in relation to a contract of insurance, means a premium payment stipulated in the contract's premium payment schedule;

specified ratio (指明比率), for a contract of insurance, means the number of months between the dates on which 2 successive premium payments are required to be made in accordance with the premium payment schedule in the contract (rounded up to the next whole number if the number of months is not a whole number) divided by 12.

7. Rounding of levy amounts

If the amount of a levy payable would, but for this section, include a fraction of a cent, the amount is to be rounded to the nearest cent.

Schedule

[ss. 4, 5 & 6]

Rates of Levy

Column 1	Column 2	Column 3	Column 4
Period	Levy rate	Maximum levy for specified general business	Maximum levy for specified long term business
From 1 January 2018 to 31 March 2019 (both dates inclusive)	0.04%	$2,000	$40
From 1 April 2019 to 31 March 2020 (both dates inclusive)	0.06%	$3,000	$60
From 1 April 2020 to 31 March 2021 (both dates inclusive)	0.085%	$4,250	$85
From 1 April 2021 onwards (inclusive of that date)	0.1%	$5,000	$100

Clerk to the Executive Council

COUNCIL CHAMBER

2017

Explanatory Note

1. Under section 134(1) of the Insurance Ordinance (Cap. 41), a prescribed levy is payable to the Insurance Authority for a contract of insurance by its policy holder if the contract relates to a prescribed class of insurance business or a prescribed type of contract of insurance.

2. This Order specifies—

   (a) the classes of insurance business;

   (b) the types of contract of insurance; and

   (c) the rates of the levies.

Insurance (Levy) Regulation

(Made by the Chief Executive in Council under section 134 of the Insurance Ordinance (Cap. 41))

1. Commencement

(1) Subject to subsection (2), this Regulation comes into operation on 1 January 2018.

(2) Section 3(7) (in so far as it relates to paragraph (c) of the definition of ***intermediary***) comes into operation on the day on which section 5(15) (in so far as it relates to the new definition of ***licensed insurance intermediary***) of the Insurance Companies (Amendment) Ordinance 2015 (12 of 2015) comes into operation.

2. Interpretation

In this Regulation—

prescribed levy (訂明徵費) means a levy prescribed in the Insurance (Levy) Order;

remittance period (轉付期) means a period specified under section 4(2);

specified form (指明格式) means a form specified by the Authority;

specified period (指明期間) means a period specified by the Authority;

specified way (指明方式) means a way specified by the Authority.

3. Payment of prescribed levies

(1) Subject to subsection (2), the policy holder under a contract of insurance issued by an authorized insurer must, each time a

premium is paid, also pay to the insurer a prescribed levy for the premium.

(2) If an intermediary collects for the authorized insurer an amount of money purportedly paid by a policy holder as a prescribed levy, the intermediary must, as soon as practicable after the collection, forward the amount of money to the insurer.

(3) An authorized insurer must not retain any part of an amount of money purportedly paid by a policy holder as a prescribed levy that is in excess of the levy.

(4) If a policy holder contravenes subsection (1), the Authority may impose on the policy holder a pecuniary penalty not exceeding $5,000.

(5) If an authorized insurer contravenes subsection (3), the Authority may impose on the insurer a pecuniary penalty not exceeding $10,000.

(6) A pecuniary penalty imposed under subsection (4) or (5) is recoverable as a civil debt due to the Authority.

(7) In subsection (2)—

intermediary (中介人) means—

(a) an appointed insurance agent;

(b) an authorized insurance broker; or

(c) a licensed insurance intermediary.

4. Remittance of prescribed levies and remittance return

(1) Subject to subsections (6) and (7), an authorized insurer must—

(a) remit to the Authority, in accordance with section 5 and in the specified way, the amount of prescribed levies payable under section 3(1) in respect of a remittance period; and

(b) lodge, at the same time, a remittance return in the specified form.

(2) For the purposes of subsection (1), the Authority may from time to time by notice specify a period as a remittance period, whether generally or in a particular case.

(3) A notice issued under subsection (2) is not subsidiary legislation.

(4) If an authorized insurer contravenes subsection (1), the Authority may impose on the insurer a pecuniary penalty not exceeding the amount which is the greater of—

(a) $10,000; or

(b) 20 times the amount of the prescribed levies that were not remitted.

(5) A pecuniary penalty imposed under subsection (4) is recoverable as a civil debt due to the Authority.

(6) If a policy holder fails to pay a prescribed levy, the authorized insurer—

(a) is not required to remit the levy to the Authority; but

(b) must, within the specified period and in the specified way, inform the Authority of the failure.

(7) The Authority may, on a written request of an authorized insurer, vary the basis for the calculation of the amount of prescribed levies to be remitted by the insurer for a period agreed between the Authority and the insurer.

5. Timing of remittance

An authorized insurer must, for each remittance period, make the remittance—

(a) within 2 months after the end of that period; and

(b) on a basis of accounting approved by the Authority.

6. Revision of remittance return

An authorized insurer may revise the insurer's remittance return or the amount of prescribed levies to which the return relates to correct any error in a previous remittance return or reflect any refund made to a policy holder in respect of a prescribed levy covered by a previous remittance.

7. Authorized insurer to lodge remittance report

(1) An authorized insurer must lodge with the Authority a remittance report annually to certify that—

(a) the remittance returns lodged under section 4(1)(b) in respect of the remittance periods covered by the report are correct and comply with this Regulation; and

(b) the insurer has remitted the prescribed levies in accordance with section 4.

(2) A remittance report must cover the remittances made in respect of the 2 remittance periods immediately preceding the date of the report unless otherwise approved by the Authority.

(3) A remittance report must be—

(a) in the specified form; and

(b) certified by an auditor appointed by and at the expense of the authorized insurer.

8. Refund of money paid as prescribed levy

(1) This section applies if—

(a) a policy holder paid an amount of money to an authorized insurer or an intermediary for compliance with section 3(1); and

(b) the policy holder was not liable, or becomes not liable, to pay that amount or any part of it.

(2) An authorized insurer must refund, in the specified way, to a policy holder any amount of money that is purportedly paid by the policy holder as a prescribed levy but is not required by this Regulation to be paid as a prescribed levy.

9. Providing particulars of policy holder if prescribed levy is unpaid

If a policy holder contravenes section 3(1), the Authority may require the authorized insurer to provide the particulars of the policy holder reasonably required by the Authority for recovering a prescribed levy under section 134(3) of the Ordinance.

Clerk to the Executive Council

COUNCIL CHAMBER

2017

Explanatory Note

Under section 134(1) of the Insurance Ordinance (Cap. 41), a prescribed levy is payable to the Insurance Authority for a contract of insurance by its policy holder if the contract relates to a prescribed class of insurance business or a prescribed type of contract of insurance.

2. This Regulation prescribes—

(a) the way in which the prescribed levy must be paid; and

(b) the matters relating to the remittance to the Insurance Authority by an authorized insurer of the prescribed levy payable by a policy holder.

Annex C

Financial and Economic Implications

According to the findings of the consultancy study [1] commissioned by the Government, IA will face a shortfall of about $650 million in the first four years of operation. With the approval of LegCo, the Government has provided $450 million to IA in 2016-17. We will seek the approval of LegCo for providing the remaining $200 million to IA in 2018-19, subject to a review of the progress of IA's transitional work.

2. The consultant's projection is that IA would be able to fully recover its operating cost via income from the market and be financially independent of the Government in the fifth year. Major sources of income are levy on premiums paid by policy holders (accounting for 70% of IA's income), authorization fees paid by insurance companies, licence fees paid by insurance intermediaries, and user fees (altogether accounting for 30% of IA's income). Under the proposed incremental approach, the estimated annual income from levy is around $120 million at the initial rate of 0.04% and will gradually increase to around $400 million in the first year when the target rate of 0.1% is reached.

3. Currently, OCI[2] incurs an annual operating cost of around $124 million. It recovers around 30% of the cost from the annual authorization fees paid by insurance companies. Upon transition to IA, OCI will be disbanded and will no longer require funding from the Government.

4. On economic implications, the proposed levy would impose additional costs on policy holders, but the additional costs should be relatively small (0.1% of insurance premium with cap).

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[1] The consultancy study was carried out by the PricewaterhouseCoopers and first concluded in 2010. The projection on the estimated cashflow of IA was updated in November 2015 having regard to the additional regulatory functions undertaken by OCI since 2010 and the latest market conditions. The Government consulted the Legislative Council Panel on Financial Affairs on the funding proposal in December 2015.

[2] There are about 150 staff members in OCI. Based on the recommendations of the consultancy study commissioned by the Government, IA will have an initial establishment of 299 staff members.