

立法會

Legislative Council

LC Paper No. CB(1)625/17-18(05)

Ref: CB1/PL/FA

Panel on Financial Affairs

Meeting on 5 March 2018

Updated background brief on the Establishment of and financial arrangements for the Insurance Authority

Purpose

This paper provides background information on the establishment and financial arrangements of the Insurance Authority ("IA"). It also gives a brief account of the major views and concerns raised by Members since the Fifth Legislative Council ("LegCo") on IA's financial arrangements and related issues.

Background

2. The Insurance Companies (Amendment) Ordinance 2015 ("the Amendment Ordinance")¹ was enacted on 10 July 2015 to amend the Insurance Companies Ordinance (Cap. 41) to provide for, among others, the establishment of IA to take over the statutory functions of the Office of the Commissioner of Insurance ("OCI") (a government department) for regulating insurance companies and the supervisory functions of the existing three Self-Regulatory Organizations ("SROs").² The Amendment Ordinance also renamed the Insurance Companies Ordinance as the Insurance Ordinance ("IO").

¹ The Insurance Companies (Amendment) Ordinance 2015 provides for, inter alia, the establishment of the Insurance Authority ("IA"), the enforcement powers of IA, the establishment of the Insurance Appeals Tribunal and a statutory licensing regime for insurance intermediaries.

² The three Self-Regulatory Organizations 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.

3. To allow for a smooth transition from the existing regulatory regime from OCI to IA, the Amendment Ordinance is being implemented in three stages as follows:

Stage 1: To establish the Provisional Insurance Authority ("PIA") ³ (without regulatory functions and co-exists with OCI)	December 2015
Stage 2: PIA to be renamed as IA and replaces OCI by taking over its regulatory functions (the self-regulatory regime for insurance intermediaries remains unchanged)	26 June 2017
Stage 3: IA to implement the statutory licensing regime and take over the regulation of insurance intermediaries from the three SROs	Within two years from the establishment of PIA

4. PIA was established on 7 December 2015.⁴ PIA is not vested with any regulatory powers before it becomes the IA to take over the duties of OCI. On 28 December 2015, the Chief Executive ("CE") announced the appointment of the Chairperson and seven Non-executive Directors of IA for a term of three years from 28 December 2015 to 27 December 2018.

5. In order to commence the new regulatory regime to be administered by IA on 26 June 2017 (i.e. Stage 2 of the table in paragraph 3), the Government tabled nine pieces of subsidiary legislation before LegCo at the meeting of 26 April 2017.⁵ To enable IA to collect levy on insurance premiums from

³ Section 4AAA(2) of the Insurance Ordinance (Cap. 41) provides that when IA is established, it is automatically renamed as "Provisional Insurance Authority" in English and "臨時保險業監管局" in Chinese for the period from its inception to the disbandment of Office of the Commissioner of Insurance ("OCI").

⁴ The Insurance Companies (Amendment) Ordinance 2015 (Commencement) Notice 2015 ("Commencement Notice") was tabled at the Legislative Council meeting of 14 October 2015. No subcommittee was formed for scrutiny of the Commencement Notice.

⁵ The nine pieces of subsidiary legislation were Insurance Companies (Actuaries' Qualifications) (Amendment) Regulation 2017, Insurance Companies (Register of Insurers) (Prescribed Fee) (Amendment) Regulation 2017, Insurance Companies (Authorization and Annual Fees) (Amendment) Regulation 2017, Insurance Companies (Determination of Long Term Liabilities) Regulation (Amendment) Rules 2017, Insurance Companies (Margin of Solvency) Regulation (Amendment) Rules 2017, Insurance Companies (General Business) (Valuation) Regulation (Amendment) Rules 2017, Insurance Companies (Amendment) Ordinance 2015 (Commencement) Notice 2017, Insurance Ordinance (Amendment of Schedules) Notice 2017 and Insurance Companies (Actuaries' Standards) Regulation (Amendment) Rules 2017.

policy holders starting from 1 January 2018, the Government further tabled the Insurance (Levy) Order and the Insurance (Levy) Regulation before LegCo at the meeting on 14 June 2017.⁶

Financial arrangements for the Insurance Authority

6. Sections 5A to 5G of IO set out the accounting and financial arrangements of IA. The main provisions include requirements for IA to prepare and submit its corporate plan (including the estimates of income and expenditure) for the next financial year to the Financial Secretary ("FS") for approval and submit annual reports to FS; FS to table IA's estimates, annual reports and audited financial statements before LegCo; and the Government to pay IA out of the general revenue the monies appropriated by LegCo. As a check and balance, the Director of Audit may conduct value-for-money audit on IA.

7. To enhance transparency in the preparation of IA's annual estimates, during the scrutiny of the Insurance Companies (Amendment) Bill 2014, the Government has taken on board the suggestion of the relevant Bills Committee for IA to brief the Panel on Financial Affairs ("FA Panel") on the main features of its proposed budget prior to seeking approval by FS.

Income of the Insurance Authority

8. The Government's policy objective is for IA to fully recover its costs via income from the market and become financially independent of the Government. It is the long-term target that about 70% of the expenditure of IA be met by levy and the remaining 30% by various authorization, licence and user fees.⁷ In respect of the levy, IA will impose 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), which will be implemented through an incremental approach,⁸ and

⁶ No subcommittee had been formed to scrutinize the subsidiary legislation concerned.

⁷ Authorization fees are payable by insurance companies, licence fees are payable by insurance intermediaries and user fees are charged for provision of specific services. Levies are collected from insurance premiums.

⁸ According to the Schedule to the Insurance (Levy) Order, IA's level of levy will be in accordance with the following schedule –

	From 1 January 2018 to 31 March 2019	From 1 April 2019 to 31 March 2020	From 1 April 2020 to 31 March 2021	From 1 April 2021 onwards
Market levy as a % on insurance premiums	0.04%	0.06%	0.085%	0.1%

exempt premiums of reinsurance contracts from the levy. As regards authorization, licence and user fees, they will be payable by all insurers and licensed intermediaries.

9. Under sections 128 to 134 of IO, all fees and levies of IA are to be stipulated in regulations and orders to be made by CE which are subsidiary legislation subject to negative vetting of LegCo. Section 135 of IO provides for the mechanism for reduction of IA's levies. The policy intent is that when the reserves of IA are more than twice its estimated operating expenses for the financial year (after deducting depreciations and all provisions) and that IA has no outstanding borrowing, IA has to consult FS with a view to recommending to CE in Council that the rate or amount of a levy be reduced.

Funding for the establishment of the Insurance Authority

10. To help meet part of IA's expenses in the initial five years before it achieves the target levels of fees and levy, the Government's proposal is to provide a lump sum provision to IA on its inception. On 7 December 2015, the Government briefed FA Panel on its funding proposal for the establishment of IA and the exit arrangement for the existing Insurance Officers in OCI. A lump sum provision of \$650 million⁹ was proposed for meeting the first four years of operation of IA. During the examination of the Estimates of Expenditure 2016-2017 in April 2016, the Government explained that \$450 million of the lump sum provision for meeting the shortfall of IA's budget for the first two years had been included in the Estimates of Expenditure 2016-2017. The Government plans to provide the remaining \$200 million to IA tentatively in 2018-2019, subject to the progress of the transitional work from the existing regulatory regime to the new one.

Concerns and views expressed by Members

11. FA Panel was briefed on IA's proposed budgets for 2016-2017 and 2017-2018 at the meetings on 6 June 2016 and 16 March 2017 respectively.

⁹ Based on a consultancy study conducted by the Administration in 2010, a lump sum of \$500 million was required as seed money and contingency reserve to support IA's initial years of operation. The Administration updated the estimates in November 2015 and revised the lump sum to \$650 million having regard to the additional regulatory functions of OCI (including enforcement of the anti-money laundering regulatory regime) since the study in 2010 to be taken over by IA. The Administration also advised that based on 2010 consultancy study, IA would have an establishment of about 250 staff members at its inception. As for OCI, the number of staff members was 150 as in mid-2014. As indicated in the updated consultancy study in November 2015, IA will have an initial establishment of 299 staff members.

The Government also briefed FA Panel at the meeting on 15 November 2016 regarding the proposed subsidiary legislation for IA to collect levy on insurance premiums from policy holders, authorization fees from insurance companies, and other fees on specific services provided by IA. The major views and concerns expressed by the Bills Committee on the Insurance Companies (Amendment) Bill 2014 ("the Bills Committee") and FA Panel relating to the financial arrangements for IA, the funding proposal for the establishment of IA, the collection of levy and fees by IA, and the regulatory work of IA are summarized in the ensuing paragraphs.

Financing mechanism and estimates of the Insurance Authority

12. Members of the Bills Committee noted that IA was empowered to appoint its staff and consultants, and determine their remuneration and terms and conditions. They stressed the need to put in place a mechanism for regulating the size of IA to prevent over-expansion, and considered that part of the proposed start-up funds provided by the Government to IA should be in the form of a loan so as to enhance the financial prudence and discipline of IA.

13. The Government explained that IA would have a larger establishment than OCI mainly because IA would take up the additional responsibility of administering the licensing system for insurance intermediaries. The Amendment Ordinance required that IA's annual estimates, which included estimated staff costs and professional service fees, to be approved by FS and the approved estimates must be tabled before LegCo. These measures would provide an effective check and balance. The Government stressed the need to provide IA with operational flexibility in employing and engaging suitable talents and determining the appropriate level of remuneration having regard to the actual circumstances and prevailing market situations so that IA could cope with the regulatory challenges effectively and respond swiftly to market changes. This was in line with the practice of other financial regulators, such as the Securities and Futures Commission ("SFC") and the Mandatory Provident Fund Schemes Authority ("MPFA"). The Government also took note of the Bills Committee's suggestion that part of the proposed start-up funds for IA should be provided in the form of a loan, and undertook to consult FA Panel before seeking the relevant funding approval from the Finance Committee.

14. During the discussion at the FA Panel meeting on 7 December 2015, members enquired whether the Administration would top up the shortfall should the proposed lump sum provision of \$650 million for IA was insufficient. The Government advised that if the proposed lump sum provision turned out to be inadequate, it might consider different options including the provision of additional funding to IA in the form of a loan. There were provisions in the Amendment Ordinance enabling IA to borrow money with the approval of FS. Given the healthy and stable development of the insurance industry in the

previous years on which basis the income projection of IA had been worked out, it was envisaged that the proposed \$650 million would be sufficient to support the operation of IA in the initial five to six years.

Levy on insurance premiums

15. Some members of the Bills Committee opined that the levy to be collected by IA should not be borne by policyholders on concern that this might increase the price of insurance products. Some FA Panel members were of the view that insurers and insurance intermediaries should bear IA's expenditure because they would benefit from the new regulatory regime. They reiterated the need for IA to exercise vigilance in controlling its expenditure so as to contain the levels of levy and fees to be collected from policyholders and the industry.

16. The Government advised that one of the main objectives of IA was to protect policy holders, and based on the "user-pay" principle it would be justified to collect levies from policyholders. It was also important for IA to be financially independent to perform its statutory regulatory functions in an equitable and impartial manner. The Government further pointed out that insurance companies were required to pay variable authorization fee in addition to fixed authorization fee under the new regulatory regime.

17. At the FA Panel meeting on 15 November 2016, some members considered that while the proposed levy on insurance premiums would have little impact on policyholders as the amount involved was relatively small and should be affordable to policyholders, they urged the Administration to step up efforts in arranging publicity and public education on the proposed levy to enhance policyholders' understanding of the details, and developing guidelines on levy collection.

Recruitment and pay policies of the Insurance Authority

18. At the FA Panel meetings on 7 December 2015, 6 June 2016 and 16 March 2017, some members enquired about the recruitment policies of IA and how it would benchmark the remuneration of its staff. There were views that the provision of "bonus" should not be linked with staff members' work in combating misconduct of insurance intermediaries lest they might be motivated to take enforcement actions in a less prudent manner. The Government advised that IA would formulate its own recruitment policies including staff salaries and employment terms. IA had engaged a human resources consultant for advice, and considered adopting arrangements similar to those of other statutory regulatory bodies like SFC and MPFA. IA had also made reference to the salary levels of comparable positions in the market and those of other financial regulators in determining the remuneration of its own staff.

IA would recruit its staff in phases and explore arrangements for experienced staff members in the industry and other financial regulators to be seconded to IA. The variable pay for staff of IA would be linked to their performance. Fines imposed by IA on disciplinary cases would be paid into the general revenue of the Government.

Regulatory work of the Insurance Authority

19. At the FA Panel meeting on 6 June 2016, some members called on IA to enhance the regulation of Investment-Linked Assurance Schemes ("ILAS") products, and enquired about the division of responsibilities between SFC, OCI (and the future IA) in regulating the design, risk disclosure and sale process of such products. They stressed the importance for the regulators concerned to adopt consistent regulatory standards.

20. IA advised that the relevant regulatory standards of SFC and IA should be consistent. IA would liaise with SFC to enhance cross-regulator co-ordination whenever necessary, and would step up effort in promoting public education, and enhancing the professional knowledge and conduct of insurance intermediaries. The Government pointed out that ILAS products, like other investment products, had to comply with the disclosure requirements set by SFC in order to be authorized for sale in the market. OCI had issued Guidance Note on Underwriting Class C Business (GN15) and Guidance Note on Underwriting Long Term Insurance Business (other than Class C Business) (GN16) to provide guidance to the industry on treating customers fairly in designing long-term and ILAS products. It was observed that these guidelines were effective in addressing a range of regulatory issues from product design to the sales process.

21. At the FA Panel meeting on 6 June 2016, some members suggested that IA should look into the complaint cases being handled by the three SROs and take appropriate follow-up actions. IA responded that it had noted that there were inconsistencies in the existing complaint handling mechanism administered by the SROs. IA would review the mechanism to ensure its efficiency and effectiveness.

22. At the FA Panel meeting on 16 March 2017, some members suggested that IA should consider issuing guidelines to insurance companies with a view to standardizing certain key terms used in insurance policies, such as the definition of "terminal diseases". IA advised that it could not directly regulate individual insurance products but would take relevant measures (like rolling out public education programmes) to enhance consumers' awareness to protect their rights and interests in purchasing insurance products. Moreover, the industry had established an independent mechanism to handle claim disputes, and IA

would soon commence preparatory work on the establishment of the Policy Holders' Protection Scheme.

Preparatory work of the Insurance Authority

23. At the FA Panel meetings on 15 November 2016 and 16 March 2017, members enquired about the progress of the preparatory work of IA including the formulation of relevant guidelines and development of the code of conduct for insurance intermediaries.

24. The Government advised that it would liaise with IA and the insurance industry in formulating guidelines on various matters for implementing the new regulatory regime, and arranging publicity campaigns including the provision of hotline services. The Working Group of Transition (which included representatives of the existing three SROs) had been established to work out the detailed arrangements on transitional issues including developing the code of conduct for insurance intermediaries. The target was for IA to promulgate the code of conduct before commencement of the statutory licensing regime.

Work in promoting the sustainable development of the insurance industry

25. At the FA Panel meeting on 16 March 2017, members enquired about IA's work in promoting the sustainable development of the insurance industry. IA advised that it had been liaising with stakeholders in promoting the sustainable development of the insurance industry, and would implement measures focusing on areas including enhancing the image of the insurance industry, promoting continuous professional development of industry practitioners, attracting new talents to the industry, and enhancing consumer protection. A Future Task Force had also been established to explore the future of the insurance industry in Hong Kong.

Council question

26. Hon CHAN Kin-por raised a written question on "Measures to facilitate the development of the insurance industry" at the Council meeting of 5 July 2017. The question sought details of how IA would promote the use of financial technologies by the insurance industry and facilitate the development of the insurance industry. The question and the Government's written response are hyperlinked in the **Appendix**.

Latest development

27. The Government will brief FA Panel on IA's proposed budget for 2018-2019 at the meeting to be held on 5 March 2018.

Relevant papers

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

Council Business Division 1
Legislative Council Secretariat
28 February 2018

List of relevant papers

Date/Period	Event	Paper/Minutes of meeting
May 2014 to July 2015	The Bills Committee on Insurance Companies (Amendment) Bill 2014 was in action	Report of the Bills Committee (LC Paper No. CB(1)1055/14-15) Legislative Council Brief (File Ref: C2/2/50C) Legal Service Division report (LC Paper No. LS50/13-14)
10 July 2015	The Legislative Council ("LegCo") passed the Insurance Companies (Amendment) Bill 2014	Hansard
14 October 2015	The Insurance Companies (Amendment) Ordinance 2015 (Commencement) Notice 2015 gazetted on 9 October 2015 was introduced into LegCo	Legislative Council Brief (File Ref.: INS/2/3C(2015)) Legal Service Division Report (LC Paper No. LS2/15-16)
7 December 2015	The Panel on Financial Affairs ("FA Panel") was briefed by the Administration on its funding proposal relating to the establishment of the Insurance Authority ("IA")	Administration's paper (LC Paper No. CB(1)209/15-16(04)) Minutes (LC Paper No. CB(1)540/15-16) Background brief (LC Paper No. CB(1)209/15-16(05))
28 December 2015	The Chief Executive announced the appointment of the Chairperson and seven Non-executive Directors of the Provisional Insurance Authority	Press release

Date/Period	Event	Paper/Minutes of meeting
5 April 2016	Special meeting of the Finance Committee for examination of Estimates of Expenditure 2016-2017	Written questions raised by Members and Administration's replies for the session on "Financial Services" (Reply serial numbers: FSTB(FS)001, 009, 010, 011, 012, 013, 014, 024, 033, 035, 037, 038, 039, 044, 060, 092, 098, 099 and 103)
6 June 2016	FA Panel was briefed by the Administration and IA on IA's proposed budget for the financial year of 2016-2017	Administration's paper (LC Paper No. CB(1)987/15-16(04)) Minutes (LC Paper No. CB(1)1162/15-16) Background brief (LC Paper No. CB(1)994/15-16(01))
15 November 2016	FA Panel was briefed by the Administration and IA on the subsidiary legislation for IA to collect levy on insurance premiums from policy holders, authorization fees from insurance companies, and other fees on specific services provided by IA	Administration's paper (LC Paper No. CB(1)78/16-17(08)) Minutes (LC Paper No. CB(1)364/16-17) Background brief (LC Paper No. CB(1)78/16-17(09))
6 February 2017	FA Panel was briefed by the Secretary for Financial Services and the Treasury on the Chief Executive's 2017 Policy Address	Administration's paper (LC Paper No. CB(1)459/16-17(04))
16 March 2017	FA Panel was briefed by the Administration and IA on IA's proposed budget for the financial year of 2017-2018	Administration's paper (LC Paper No. CB(1)660/16-17(06)) Minutes (LC Paper No. CB(1)1178/16-17) Background brief (LC Paper No. CB(1)660/16-17(07))

Date/Period	Event	Paper/Minutes of meeting
26 April 2017	Nine pieces of subsidiary legislation for IA to take over the regulatory functions of the former Office of the Commissioner of Insurance gazetted on 21 April 2017 were introduced into LegCo	Legislative Council Brief (File Ref.: INS/2/3C(2017)) Legal Service Division Report (LC Paper No. LS58/16-17)
14 June 2017	The Insurance (Levy) Regulation and the Insurance (Levy) Order gazetted on 9 June 2017 were introduced into LegCo	Legislative Council Brief (File Ref.: INS/2/3C(2017)) Legal Service Division Report (LC Paper No. LS78/16-17)
5 July 2017	Hon CHAN Kin-por raised a written question on measures to facilitate the development of the insurance industry	Hansard (pages 11120 – 11123)