


Policy Holders' Protection Scheme Bill

Legislative Council Panel on Financial Affairs

5 March 2018



Financial Services and the Treasury Bureau

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1. Purpose of Establishing the PPS

- To enhance protection for policy holders in case of insolvency of insurance company, so as to provide a safety net for policy holders
- To maintain stability of the insurance market
- To strengthen public confidence in the insurance industry

2. Background

- Hong Kong insurance companies are financially healthy
 - 1) The Insurance Ordinance imposes prudential and comprehensive regulatory requirements on insurance companies
 - 2) The Insurance Authority (“IA”) closely monitors the financial positions of insurance companies and will exercise intervention powers when necessary

- Existing compensation schemes :
 - Insolvency Fund Scheme administered by the Motor Insurers’ Bureau of Hong Kong
 - Employees Compensation Insurer Insolvency Scheme

3. Considerations

- To strike a reasonable balance between enhancing protection for policy holders and minimising additional burden to the industry
- For life policies, the priority is to secure continuity of contracts, as premature encashment or surrender could lead to substantial losses to policy holders
- For non-life policies, we need to provide continuity of cover and allow sufficient time for policy holders to seek replacement policies
- To enhance market stability while minimising the risk of moral hazard

4. Proposal - Overview

Governance	<ul style="list-style-type: none">➤ The Policy Holders' Protection Board ("the Board") as the governing body, with IA as the administrative arm
Scheme Members	<ul style="list-style-type: none">➤ All authorized insurance companies, except :<ul style="list-style-type: none">◆ reinsurers◆ captive insurers◆ insurance companies which are only authorized to sell unprotected policies (e.g. motor insurance) <p>A foreign incorporated insurance company may apply for exemption if similar protection scheme of its home jurisdiction already covered protected policies under the PPS with similar scope and level of protection</p>
Coverage	<ul style="list-style-type: none">➤ Eligible policy holders: individuals, SMEs and Owners' Corporations➤ Protected policies: all direct life and non-life policies underwritten in Hong Kong (except retirement schemes, motor vehicle policies, employees' compensation policies, aviation and marine insurance policies and certain offshore risks)

4. Proposal – Overview (cont')

Target Fund Size	<ul style="list-style-type: none">➤ Life Fund (\$1.2 billion)➤ Non-life Fund (\$75 million)
Levy	<ul style="list-style-type: none">➤ Payable by insurance companies➤ Initial levy rate at 0.07% of premium➤ In case of insolvency of an insurance company, an additional levy (cap at 1%) may be collected if the Funds are not sufficient. The level of any additional levy would require LegCo's approval

4. Proposal – Overview (cont')

Compensation Limit	<p>➤ \$1 million cap for the aggregate of below:</p> <ul style="list-style-type: none">• Claims for insured events, surrender value and annuity, etc. (100% for the first \$100,000, plus 80% of the balance)• Ex-gratia payment in case of involuntary termination of policies <p>(life policy: calculated on a per-policy basis non-life policy: calculated on a per-claim basis)</p>
Usage of Funds	<p>➤ Compensation for insurance claims *</p> <p>➤ Pending the transfer of policies, to provide undertaking to the liquidator *</p> <p>➤ In case the Court orders a reduction of contract amount, to provide guarantee top up payment to eligible policy holders i.e. excess of amount calculated based on the original contract over the reduced contract amount *</p> <p>➤ To provide payment to facilitate the transfer of polices</p> <p>* Note: Items subject to a cap of \$1 million on the aggregate amount</p>

4. Proposal – Operation

Specified event which will trigger the use of the Funds –

- ◆ Winding up petition of a Scheme member has commenced

AND

- ◆ IA may, after consultation with the Financial Secretary, serve on the Board a written notice of its decision that the PPS Fund(s) should be triggered

4. Proposal – Operation (cont')

➤ **Life Policies**

- ◆ Transfer of policies to secure continuity of contracts
- ◆ To provide undertaking to the liquidator
- ◆ To provide guarantee top up payment
- ◆ To provide payment to facilitate the transfer of policies
- ◆ To set up a Special Purpose Insurer to receive the contracts
- ◆ May consider ex-gratia payment in case the life policies cannot be transferred and have to be terminated

➤ **Non-Life Policies**

- ◆ To provide continuity of cover for up to 60 days
- ◆ Refund of unexpired premiums

4. Proposal – Asset Recovery Mechanism

- The PPS will be subrogated to the rights of the policy holders and recover the claims from the insurance company
- PPS will have the same priority as Employees Compensation Assistance Fund under s.265 of the Companies (Winding Up and Miscellaneous Provisions) Ordinance
- Under the preferential payment of the relevant provision, the liquidator is required to handle wages and salary of employees first. As such, the proposed asset recovery mechanism will not affect the existing rights of employees in case of a company insolvency

4. Proposal – Example 1: Endowment Policy

- Mr C has procured an endowment policy for himself. The sum insured is HKD900,000. The beneficiary is Mrs C. The insurance company will pay the sum insured if he dies. The insurance company becomes insolvent on 28 February 201X
- Suppose Mr C dies on 20 March 201X, and HKD200,000 has been paid from the assets of the insurance company
- In this scenario, Mrs C will be entitled to compensation of HKD540,000 [$\text{HKD}100,000 + 80\% \times \text{HKD}800,000 - \text{HKD}200,000$ compensation received] from the PPS, and can file a claim of HKD160,000 from the assets of the failed insurance company

4. Proposal – Example 2: Home Insurance Plan

- Mr A has a home property insurance plan. It is a 1-year policy that will expire on 31 December 201X. The relevant insurance company becomes insolvent on 15 September 201X
- Suppose Mr A submits a claim to the liquidator on 30 October 201X. The claim adjustor confirms that the claim amount payable is HKD150,000. The insurance company has no remaining assets
- In this scenario, Mr A will be entitled to compensation of HKD140,000 [$\text{HKD}100,000 + 80\% \times \text{HKD}50,000$] and refund of unexpired premium from the PPS, and to claim HKD10,000 from the assets of the insolvent insurance company in accordance with the existing mechanism

5. Issues to Discuss with the Industry

- 1) To set a levy cap in response to the industry's operational need (international norm : the US 2%, Canada 1.5%, Singapore 1%)
- 2) Continuity of cover for non-life policies up to 60 days (international norm : Canada 45 days, the US and Singapore 30 days), so as to give policy holders sufficient time to procure replacement policies
- 3) Refund of the unexpired portion of premium after termination of non-life policies

6. Timetable

Target Dates		Key Milestones
March 2018		Legislative Council Panel on Financial Affairs
2018-19 year	legislative	Introduction of the Policy Holders' Protection Scheme Bill into the Legislative Council



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