

**For discussion
on 3 June 2019**

Legislative Council Panel on Financial Affairs

**Legislative Framework for
Group-wide Supervision of Insurance Groups**

PURPOSE

This paper briefs Members on the legislative proposals to improve the regulatory framework for the supervision of insurance groups where the holding company of an insurance group is incorporated in Hong Kong.

JUSTIFICATIONS

2. The Insurance Authority (“IA”) is a body corporate established under the Insurance Ordinance (Cap. 41) (“IO”) as the regulator for the insurance sector in Hong Kong. The existing functions and powers of the IA under the IO focus on “solo” regulation, i.e. the IA is assigned powers which focus only on regulating the companies, as single entities, which carry on insurance business (underwriting risk, issuing insurance policies and paying claims) in and from Hong Kong (referred to hereafter as “authorized insurers”). Many authorized insurers, however, are subsidiary companies within wider groups of companies which also have subsidiaries in numerous other jurisdictions carrying on insurance business in those jurisdictions. In these groups (referred to hereafter as “insurance groups”), the risk management and control functions are often carried out at the group level, i.e. by personnel in the holding company who have been assigned responsibility for overseeing the entire insurance group. Significant management and policy decisions in relation to the entire insurance group are therefore, generally, taken at the holding company level. Accordingly, the International Association of Insurance Supervisors (“IAIS”)¹ requires insurance regulators to regulate

¹ The IAIS, the international standard setting body for insurance regulators across the world, has promulgated principles, standards and guidance for group-wide supervision. These are mainly set out in the IAIS’ Insurance Core Principles (“ICPs”) and in the Common Framework (“ComFrame”) for the Supervision of Internationally Active Insurance Groups (“IAIGs”) which the IAIS is developing.

insurers on a “solo” basis and to co-operate and co-ordinate with each other to ensure insurance groups are regulated on a “group-wide” basis by agreeing, where appropriate, on one of their members to serve as group-wide supervisor in relation to an insurance group.

3. At present, the IA is the group-wide supervisor of certain international insurance groups as agreed by insurance regulators of the relevant supervisory colleges². The IA performs this function by using an indirect approach based on its “solo” regulatory powers, i.e. using its regulatory powers in relation to the insurance subsidiaries which it directly regulates (i.e. authorized insurers) to influence the holding company of the insurance group. Currently, the IA does not have direct regulatory powers over the holding companies of the authorized insurers it regulates, even for holding companies incorporated in Hong Kong.

4. The indirect approach described in paragraph 3 above has certain limitations when it comes to conducting effective group-wide supervision. Other jurisdictions including European countries, Bermuda and Singapore have already addressed this, by putting in place group-wide supervisory regimes where the insurance regulators have direct regulatory powers over the holding companies of the insurers they regulate. Further, in the 2013-2014 Financial Sector Assessment Program (“FSAP”), the International Monetary Fund (“IMF”) recommended that Hong Kong should formulate and implement a clear and comprehensive regulatory regime for insurance groups under the IO³.

5. For the reasons stated in paragraphs 1 to 4 above, we consider it necessary to amend the IO to enable the IA to exercise direct regulatory powers over Hong Kong-incorporated holding companies of insurance groups, so as to uphold the international standards and reinforce Hong Kong’s status as an international financial centre. This would build on Hong Kong’s existing experience of exercising group-wide supervision of insurance groups (using the indirect approach) and align Hong Kong’s

² A supervisory college refers to a forum for cooperation and coordination among the regulators of the subsidiary insurance companies, which are located in different jurisdictions, in an insurance group.

³ IMF recommended the IA to (a) ensure adequate supervisory resources to effectively supervise insurance groups and (b) consider legal authority to take measures at the level of the holding company, in line with emerging international practices. According to ICP23, the group-wide supervisor should, in cooperation and coordination with other supervisors, identify the insurance group and determine the scope of group-wide supervision.

regulatory regime with the international standards and practices of insurance regulation.

THE PROPOSALS

6. To enable the IA to carry out effective and direct group-wide supervision, we propose to amend the IO to extend certain powers which the IA currently has over an authorized insurer to a Hong Kong-incorporated holding company of an insurance group. The major legislative proposals are set out in the ensuing paragraphs.

(A) Designation of Insurance Holding Company and Determination of Designated Insurance Group

Designation of Insurance Holding Company

7. We propose that the IA be empowered to designate, by notice published in the Gazette, a Hong Kong-incorporated insurance holding company to be subject to group-wide supervision by the IA. Once designated, the IA will have direct regulatory power over the designated insurance holding company, and via the control and influence that the designated insurance holding company may exercise over the designated insurance group, the IA can carry out effective group-wide supervision over the designated insurance group.

8. In making a decision to designate an insurance holding company, the IA may take into account the following matters –

- (a) whether the supervisory college of the insurance group has agreed to appoint the IA as the group-wide supervisor for the insurance group;
- (b) the number of jurisdictions outside of Hong Kong in which the subsidiaries within the insurance group carry on insurance business;
- (c) the size of the business of the insurance group; and
- (d) any relevant criteria promulgated by international insurance standard setting bodies.

9. The IA may, at any time, by notice published in the Gazette, withdraw the designation of a designated insurance holding company. The withdrawal may be triggered where the circumstances on which the original designation was based have fundamentally changed, taking account of the criteria set out in paragraph 8 above. For example, if there is a restructuring of the designated insurance group or the relevant supervisory college agrees that the IA should no longer serve as the group-wide supervisor.

Determination of the Scope of the Designated Insurance Group

10. We propose that the IA be empowered to determine the scope of the designated insurance group that is subject to group-wide supervision. In making such determination, the IA will take into account the accounting standards used by the group in preparing its consolidated financial statements. Moreover, the IA will have the discretion to include or exclude a legal entity as necessary, by reason of the proximity of the connections or links such entity has with the designated insurance group. A company which falls within the designated insurance group is a “within-scope group company”, and it may or may not be an insurance company.

Fees payable

11. We propose to require a designated insurance holding company to pay the IA annual fee and user fee for recovering the cost of the IA in acting as the group-wide supervisor of the designated insurance group. The fees will be prescribed in a regulation to be made by the Chief Executive in Council in accordance with section 128 of the IO.

(B) Governance on Chief Executive, Director, and Key Person in Control Functions and Shareholder Controller

12. The chief executive, director, key person in control functions of and a person who has a significant shareholding control of a designated insurance holding company can impact the strategic direction, quality of the governance, controls and risk management, financial position and funding support available to the entire designated insurance group. Similar to the IA’s existing powers over an authorized insurer under sections 13A, 13AC, 13AE and 13B of the IO, we propose that the designated insurance holding company or the proposed shareholder controller, as the case may be, must apply for the

IA's prior consent for the appointment of such persons. The IA may refuse the application or revoke an approval granted if it appears to the IA that a person is not or is no longer fit and proper. Factors to be taken into consideration in ascertaining the fitness and propriety of a person are largely similar to the ones applicable to an authorized insurer as set out in section 14A of the IO and Guideline on "Fit and Proper" Criteria under the IO published in November 2017.

(C) Regulatory and Intervention Powers

Regulatory Powers

13. To exercise effective group-wide supervision, the IA would need to apply regulatory measures, similar to those currently under the IO for an authorized insurer, directly to a designated insurance holding company. These measures include requiring a designated insurance holding company to appoint an auditor, to submit financial information and returns (e.g. account, balance sheet, auditor's report etc.) and to comply with capital, investment, reporting and public disclosure requirements⁴.

Intervention Powers

14. In addition to the regulatory powers set out in paragraph 13 above, if the situation so warrants, the IA may deploy intervention measures, i.e. power to obtain information and require production of documents, power to obtain a skilled person report and power to restrict the transfer of assets among the within-scope group companies. The IA may also give a direction that, during the period for which the direction is in force, the affairs, business and property of the designated insurance holding company including the exercise of the designated insurance holding company's control and influence over within-scope group companies shall be managed by a Manager as appointed by the IA. This will be similar to the arrangements for the IA to appoint a Manager to manage the affairs of an authorized insurer under section 35(2)(b) of the IO.

⁴ The requirements will be further provided in rules to be made by the IA and supplemented by guidelines where appropriate.

Inspection and Investigation Powers

15. The IA may exercise the powers to conduct inspection and investigation for ascertaining whether a designated insurance holding company, or any of its within-scope group companies, is complying with, has complied with, or is likely to be able to comply with the provisions of, or a condition imposed under the IO. Where the within-scope group company is carrying on business outside Hong Kong or is subject to regulation by another regulator, the IA may exercise such powers in relation to the within-scope group company by –

- (a) requiring the designated insurance holding company to procure the within-scope group company to comply with the requirements of the IA’s inspector or investigator;
- (b) participating in the inspection or investigation coordinated by the regulator of the within-scope group company; or
- (c) acting pursuant to any agreement or arrangement the IA has with the regulator of the within-scope group company.

Disciplinary actions against the designated insurance holding company

16. It is proposed that the existing disciplinary actions against authorized insurers under the IO under section 41P of the IO be applied to the designated insurance holding company where appropriate. These would include reprimanding the designated insurance holding company publicly or privately and imposing a pecuniary penalty.

(D) Capital Requirements

17. A designated insurance group will be required to comply with the capital requirements in line with the risk-based capital standards and guidance issued by the IAIS for Internationally Active Insurance Groups. As the IAIS capital requirements have not yet been finalized and could be subject to frequent amendments, we propose that the detailed capital requirements be specified in subsidiary legislation subject to negative vetting by the Legislative Council (“LegCo”). We also intend to provide a transition lead-in period to alleviate the financial impact of complying with the capital requirements to be imposed on designated insurance groups.

WAY FORWARD

18. The IA consulted the industry on the legislative proposals to establish a regulatory framework for the supervision of insurance groups during Q1 2019. The IA has taken into account the feedback received during the industry consultation in formulating the major legislative proposals. Our current target is to introduce the relevant amendment bill into LegCo within the 2019-20 legislative session.

19. Meanwhile, the IA will continue to work closely with the industry in ironing out the details, including the fees payable (paragraph 11 above) and the capital requirements (paragraph 17 above) both of which are to be prescribed in subsidiary legislation to be made after the passage of the relevant amendment bill.

ADVICE SOUGHT

20. Members are invited to comment on the legislative proposals set out in paragraphs 6 to 17 above.

**Financial Services and the Treasury Bureau
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