

Insurance Authority
Estimates of Income and Expenditure for 2020-21

		Estimates 2019-20	Revised Estimates 2019-20	Proposed Estimates 2020-21	Variance Proposed Estimates vs. Revised Estimates 2019-20
		(i) Note	(ii) <u>HK\$</u> <u>million</u>	(iii) <u>HK\$</u> <u>million</u>	(vi) = (iii) - (ii) <u>HK\$</u> <u>million</u>
A. Income and Expenditure Statement					
Income	1				
(a) Interest income	2	3.2	4.6	4.5	(0.1)
(b) Levy and fees	3	239.8	234.4	335.2	100.8
Total Income		243.0	239.0	339.7	100.7
Operating Expenditure					
(a) Staff costs	4	331.4	307.0	390.5	83.5
(b) Office rental and related expenses	5	23.1	23.0	31.2	8.2
(c) Engagement of professional services	6	10.4	10.2	24.7	14.5
(d) Information Technology (“IT”) expenses	7	14.3	13.7	21.1	7.4
(e) External relations expenses	8	7.1	6.4	10.5	4.1
(f) Remuneration to Members		2.6	3.2	3.7	0.5
(g) Other operating expenses	9	18.1	16.5	25.5	9.0
(h) Depreciation	10	35.4	31.3	27.7	(3.6)
(i) Non-recurrent projects	11	4.1	4.4	-	(4.4)
Total Operating Expenditure		446.6	415.7	534.8	119.1
Result for the year		(203.6)	(176.7)	(195.1)	(17.6)
B. Capital Expenditure Statement					
(a) Office set-up	12	4.8	3.8	13.7	9.9
(b) IT systems and equipment	13	17.0	16.0	20.0	4.0
Total Capital Expenditure		21.8	19.8	33.7	13.9

Notes to the Proposed Estimates for 2020-21

1. Income

According to the consultancy study¹ commissioned by the Government, income of IA in the first four years of operation is not sufficient to cover its expenditure and will face a deficit of about \$650 million. Two instalments have been received from the Government to help IA meet the shortfall in its initial years of operation. On 13 May 2016, the Legislative Council (“LegCo”)² approved the provision of \$450 million to IA. On 10 May 2018, LegCo approved the remaining provision of \$200 million to IA. The provision of \$450 million and \$200 million received in June 2016 and June 2018 respectively were recognized as capital upon receipt in the statement of financial position and they are provided by the Government without related costs.

The deficit of 2020-21 is estimated to reach the amount of some \$200 million and the IA expects to face a cash shortfall in the year and in the short to medium term. Given the need to tide over its projected cash shortfall in the short to medium term and maintain an appropriate level of reserve, the IA has secured support from the Government for an additional funding injection of \$300 million in 2020-21.

2. Interest income

With the approval of the Financial Secretary (“FS”), IA has adopted an interim investment arrangement where funds not required for immediate use would be invested in the form of placement of Hong Kong Dollars fixed deposits to earn interest income. A long term investment strategy of IA’s reserve funds will be worked out when there is more certainty on IA’s cash flow requirements.

3. Levy and Fees

Starting from 1 January 2018, a levy of 0.04% on premiums of insurance policies will be payable by policyholders. The levy rate will gradually increase until it reaches its target level of 0.1% in 2021-22. A cap will 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 \$100,000. Captive insurance, contracts of reinsurance and marine, aviation and goods in transits are exempt from levy.

¹ The consultancy study was carried out by the PricewaterhouseCoopers.

² Before obtaining LegCo’s funding approval, the Government approved in February 2016 a small sum of \$3 million in 2015-16 for IA to meet mainly the cash flow requirement of the essential consultancy services. The allocation was received by IA in March 2016.

The new annual authorization fees payable by insurance companies effective from 26 June 2017 consist of two elements, namely, (a) a fixed fee of \$300,000 (for captive insurance company, \$30,000; and for composite insurance company, \$600,000); and (b) a variable fee subject to a cap of \$7 million on insurance liabilities (\$14 million for composite insurer). The variable fee rate pitches at 0.0001% and will increase gradually until it reaches its target rate of 0.0039% in 2022-23.

With effect from 26 June 2017, the IA has been charging user fees to recover the cost of providing 11 specified services. The number of user fee items has been increased to 23 starting from 27 May 2019, of which 22 are applicable to insurance companies.

4. Staff costs

The staff costs involve mainly salary, contributions to Mandatory Provident Fund schemes, staff insurance and employees' compensation insurance. The revised estimate for 2019-20 is mainly based on the actual profile of serving staff. We envisage that we would have full strength of about 330 permanent staff members on board in 2020-21. There will be increase in staff costs in 2020-21 arising from additional staff for new initiatives.

5. Office rental and related expenses

This item includes mainly office rental, management fees, utility charges, government rent/rates as well as other related expenses such as general office insurance and telephone rental. The increase in rental expenses is mainly due to projected rise in rental on renewal of lease of existing office premises and the need to rent additional office space to accommodate additional headcounts.

6. Engagement of professional services

This item represents mainly executive search services for staff recruitment, consultancy, legal and audit services. The estimate for 2020-21 is higher than the revised estimate for 2019-20 mainly due to the anticipated increase in fees for legal advice and consultancy resulted from the group-wide supervision.

7. IT expenses

IT expenses cover maintenance fees of server infrastructure, security protection system and various IT application systems. The estimate for 2020-21 is higher than the revised estimate for 2019-20 mainly due to the additional expenses related to the document management system and

maintenance of newly implemented IT systems.

8. External relations expenses

The revised estimate for 2019-20 comprises mainly PR campaigns, the Asian Insurance Forum, online news and social media monitoring. An increase in the estimate for 2020-21 is mainly related to a public education campaign.

9. Other operating expenses

Other operating expenses covers mainly expenses on staff training and development, travelling expenses, events and other incidental expenses. The estimate for 2020-21 is higher mainly because expenses increase in line with more staff members coming on board. There will also be more duty visits arising from the group-wide supervision.

10. Depreciation

Depreciation is calculated to write off the cost of fixed assets (such as furniture and fixtures as well as office and IT systems and equipment) using the straight-line method over their estimated useful lives of either three or five years.

11. Non-recurrent projects

This item is for conducting consultancy studies related to the development of the Risk-Based Capital (“RBC”) regime³ which will complete in 2019-20.

12. Office set-up

The estimate for 2020-21 represents mostly the renovation of additional office space.

13. IT systems and equipment

The estimate for 2020-21 included the phase 2 implementation of the document management system.

December 2019

³ The RBC regime is aimed to enhance the prudential regulatory system for insurance companies with a view to aligning the capital requirements for insurance companies with the risks to which they are exposed and strengthening their enterprise risk management system. The RBC regime is being developed in phases.