

Proposed Establishment of an Independent Insurance Authority

Frequently Asked Questions

Q1 Why do we need to establish an independent Insurance Authority (“IA”)?

A1 At present, the Office of the Commissioner of Insurance stands out as the only financial services regulator still operating within the Government machinery. This is not in keeping with international insurance supervisory principles that require regulators to be given financial, operational and political autonomy.

Establishment of an independent IA would bring the following benefits to the industry and the public –

- (i) enhanced regulation of insurance companies and insurance intermediaries which can provide for better protection of insurance policyholders and facilitate the stable development of the insurance industry;
- (ii) greater nimbleness in responding to new regulatory challenges and more effective implementation of international regulatory standards;
- (iii) facilitating market innovation and maintaining competitiveness of the industry without undermining regulation; and
- (iv) raising consumer confidence in the insurance industry.

The above will help reinforce Hong Kong’s position as an international financial centre.

Q2 What are the proposed functions of the independent IA?

A2 The independent IA will be responsible for regulating insurance companies and insurance intermediaries, including their financial stability and sales conduct, in order to maintain the general stability of the insurance industry and protect policyholders’ interests.

Besides, we propose that the independent IA should take on an active role in educating public on the features and risks of insurance products, and in conducting thematic studies into the latest market development trends, regulatory issues of the insurance industry, and issues of policyholders' interests, etc.

Q3 How can the independent IA discharge its regulatory functions more effectively in comparison with the existing IA?

A3 The independent IA will not be subject to the intricate Government rules and procedures and should have greater nimbleness and agility in coping with market dynamics and in attracting professionals to join as regulators, thereby enabling Hong Kong to better meet new challenges of the ever-changing financial market.

In order to facilitate more effective regulation of insurance companies and insurance intermediaries, we propose to provide the independent IA with the necessary supervisory powers, including the power to supervise the conduct of insurance intermediaries directly through administering a licensing system.

Q4 What are the additional supervisory powers proposed to be given to the independent IA?

A4 We propose that to provide the independent IA with additional supervisory powers which are modeled on the Securities and Futures Ordinance, including powers to –

- (i) enter into premises of the regulated entities to conduct inspections;
- (ii) initiate and pursue investigations ;
- (iii) make enquiries;
- (iv) have access to records and documents;
- (v) apply to the Court of First Instance for court orders to compel compliance with the reasonable requirements imposed by the independent IA in the course of inspection and investigation;
- (vi) impose supervisory sanctions such as public reprimands and fines; and

(vii) prosecute offences summarily.

Q5 **At present, the three trade associations for insurance intermediaries perform the role of self-regulators. What will be the changes to their role in future?**

A5 The objective of our proposal is to address the key concerns inherent in the existing self-regulatory system, including –

- (i) the perceived and real conflict of interests as the self-regulatory organizations (“SROs”) are the trade bodies financed by their members;
- (ii) inconsistency in the standards and mechanisms adopted for complaints handling, investigation and disciplinary actions by the three SROs, namely the Insurance Agents Registration Board, the Hong Kong Confederation of Insurance Brokers and the Professional Insurance Brokers Association;
- (iii) limited investigatory and sanctioning powers of these SROs; and
- (iv) deviation from practices in other international financial centres whereby insurance intermediaries are directly regulated by an independent regulator.

Our proposal has taken into account the fact that irrespective of the extent of improvement measures to strengthen the existing self-regulatory system, it would not be possible to develop a sustainable solution to address the key concerns inherent in such self-regulatory system. Moreover, there would be duplication of regulatory efforts by the independent IA and the SROs, as well as regulatory gaps between them if we maintain the self-regulatory system with enhanced supervision by the independent IA.

Under our proposal, the three SROs will continue to perform the functions of a trade body including, for example, industry promotion, organization of training courses, and setting best practices, etc. We will work out the detailed transitional arrangements for the smooth migration of existing insurance intermediaries to the new licensing regime.

Q6 **What are the reasons for proposing that the sale of insurance products by bank staff should be regulated by the Hong Kong Monetary Authority (“HKMA”)?**

A6 At present, over 30% of insurance products sold in Hong Kong are distributed through banks. Noting that the client profile and sale environment in a bank are different from those of an insurance intermediary outside a bank, we consider that there are merits for HKMA to regulate bank employees selling insurance products by giving HKMA similar powers as the independent IA. Under this proposal, the relevant bank employees should first be licensed by the independent IA before they could engage in banks’ insurance business. HKMA would be responsible for conduct regulation on the basis of the standards and procedures set by the independent IA for routine supervision, investigation and disciplinary process. HKMA may impose additional conduct requirements on bank employees, on top of what the independent IA may stipulate, having regard to the special circumstances associated with the sale of insurance products in banks for the purpose of effective protection of policyholders’ interests.

Q7 **What measures would the Government take to provide adequate checks and balances for the exercise of powers by the independent IA?**

A7 We propose to put in place the following arrangements to provide adequate checks and balances for proper exercise of powers by the independent IA –

- (i) a Governing Board comprising predominantly independent non-executive directors be appointed by the Government to provide leadership and direction, and to guide the independent IA in the development of a corporate strategy to achieve its objectives and perform its functions effectively;
- (ii) its annual report be tabled before the Legislative Council (“LegCo”);
- (iii) its annual budget and corporate plan be subject to the approval of the Financial Secretary;
- (iv) a statutory appeals tribunal be established to handle appeals from insurers and insurance intermediaries against relevant decisions made by the independent IA;

and

- (v) an independent Process Review Panel be established by the Chief Executive to review its internal operating procedures, including those for ensuring consistency and fairness.

Items (iv) and (v) above should also apply to the HKMA in respect of its performance of supervisory functions over bank employees selling insurance products.

Q8 What are the communication and collaboration arrangements between the independent IA and the other financial regulators?

A8 The independent IA and the other financial regulators should maintain efficient liaison and establish robust communication and collaboration arrangements to ensure consistency in regulation and minimize duplication of efforts. For instance, a formal inter-regulator communication platform could be established to promote regular exchanges on product trends and associated risks for insurance policyholders. This would facilitate the timely development of appropriate conduct requirements for different sectors taking into account their specific circumstances.

Q9 What is the proposed source of funding for the independent IA and what measures will be taken by the Government to mitigate the impact on the industry and policyholders?

A9 The Consultant estimates that the independent IA would require an establishment of about 237 staff and the annual operating cost would be around \$240 million. In line with the insurance supervisory principle that the regulator should be financially independent of the Government, the independent IA should have stable sources of revenue and recover its cost from the market. We propose a new fee structure comprising –

- (i) a fixed licence fee payable by all insurers and insurance intermediaries;

- (ii) a variable licence fee payable by insurers only and calculated on the basis of their individual liabilities;
- (iii) user fees for specific services such as application for transfer of business, change of shareholding structure or change in key personnel; and
- (iv) a levy of 0.1% on insurance premiums for all insurance policies.

To reduce the impact on the industry and policyholders, we propose that the independent IA should recover its cost in six years and to pursue the following mitigating measures during the first five years of its establishment –

- (i) the licence fee for insurance intermediaries be waived if they are to be licensed directly by the independent IA as proposed;
- (ii) an incremental approach be adopted in achieving the target levels of variable licence fee on insurers and levy on insurance policies; and
- (iii) the Government should provide a lump sum of \$500 million to the independent IA on its inception to help meet its expenses in the initial five years and to serve as contingency reserve in the event of poor market conditions which would lead to low levy income.

Q10 When is the independent IA expected to be established?

A10 We will listen to the views of the industry and the public on the proposals during the 3-month consultation period, and thereafter prepare detailed legislative proposals. We aim to introduce a bill on the establishment of an independent IA to LegCo in 2011.