

Press release

Government launches consultation on Policyholders' Protection Fund

Friday, March 25, 2011

The Government commenced today (March 25) a three-month consultation on the proposed establishment of a Policyholders' Protection Fund (PPF), aimed at providing a safety net for policyholders against insurer insolvency.

Explaining the PPF proposal, the Secretary for Financial Services and the Treasury, Professor K C Chan, said, "It will serve as an added assurance to policyholders on top of the existing prudential regulation of insurers by the Insurance Authority.

"We believe the proposed PPF will better protect policyholders' interest, maintain market stability in the event of insurer insolvency, and enhance public confidence in and the competitiveness of our insurance industry.

"To ensure a high level of certainty and transparency, we propose to establish the PPF by statute."

The consultation document released today covers recommendations on the coverage, level of compensation, funding mechanism and governance arrangements of the proposed PPF. All authorised direct life and non-life insurers will be required to participate in the PPF.

The PPF would comprise two separate and independent schemes, namely the Life Scheme and the Non-Life Scheme. They will respectively cover all direct life and non-life policies, except employees' compensation and motor vehicle third party claims which are covered by other existing compensation schemes.

Based on the results of the actuarial consultancy study, the initial target fund size would be HK\$1.2 billion for the Life Scheme and HK\$75 million for the Non-Life Scheme, with both planned to be built up over a 15 year period. The initial levy rate for both Schemes is proposed to be set at 0.07% of the applicable premiums.

"As the proposed PPF seeks to promote industry competitiveness and address issues arising from insurer insolvency, it is recommended that the proposed PPF should collect the levy from insurers," Professor Chan added.

"Given the moderate levy rates and the keen competition among insurers in Hong Kong, we believe that the impact on the premium levels would be minimal."

Considering concerns about moral hazard, there would be a compensation limit for the PPF, proposed at 100% for the first HK\$100,000 of any claim, plus 80% of the balance, up to a total compensation limit of HK\$1 million. It should be applied on a per-policy basis for life insurance policies and a per-claim basis for non-life insurance policies.

Based on the findings of a consultancy commissioned by the Government and using industry data as at end-2009, the proposed PPF is expected to be able to meet 90%-100% of claims arising from some 90% of life policies, and to fully meet claims of some 96% of non-life policies.

Other aspects of the proposed PPF include-

- a) The proposed PPF would focus on individual policyholders, and may include small and medium enterprise policyholders subject to views of stakeholders and the public.
- b) Third party risks insurance procured by building owners' corporations would be covered.
- c) The proposed PPF should have the option to impose a "stepped-up" levy rate as necessary upon occurrence of insurer insolvency.
- d) The proposed PPF should be allowed to borrow from a third party to bridge any liquidity gap e.g. from commercial lenders with the Government acting as the guarantor, or from the Government direct. Approval of the Legislative Council would be required in either case.

e) Policyholders of life policies and accident and health policies with guaranteed renewability may suffer from a disadvantage in procuring alternative coverage should their insurers become insolvent. The proposed PPF should thus be allowed to make payments to facilitate the transfer of such policies to another insurer in case of insurer insolvency, up to a limit of HK\$1 million per policy.

f) The proposed PPF should be administered by an independent statutory body (i.e. the PPF Board) appointed by the Financial Secretary.

g) The PPF Board should maintain a small team of staff and be empowered to engage additional manpower or advisers in the event of insurer insolvency.

h) An Appeal Board should be set up to deal with appeals against the relevant decisions made under the proposed PPF.

The Government will take into account the views received from stakeholders and the public in the consultation exercise in finalising the proposals, which will then form the basis for preparing legislation for the establishment of the PPF. "We aim to finalise the proposals within this year. Assuming smooth progress of the necessary steps to be taken, we aim to establish the proposed PPF in 2013-14," Professor Chan said.

Full details of the consultation document on the proposed establishment of the PPF are available at the Financial Services and the Treasury Bureau's website (www.fstb.gov.hk/fsb/ppr/consult/ppf.htm). Members of the public are welcome to send their written comments on or before June 24, 2011 by mail to the Special Duties Division, Financial Services Branch, FSTB on 18/F, Tower I, Admiralty Centre, 18 Harcourt Road, Hong Kong; or by email to ppf_consultation@fstb.gov.hk; or by fax to 2527 0292.

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