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## **Proposed Establishment of an Independent Insurance Authority**

### **Frequently Asked Questions**

**Q1      What is the outcome of the public consultation on the proposed establishment of an independent Insurance Authority (“IIA”)?**

**A1**      There is general public support for the proposal to establish an IIA. The establishment of an IIA will enable Hong Kong to comply with the international regulatory principle that all financial regulators should be operationally and financially independent from the government, and improve our flexibility and agility in coping with future regulatory challenges, particularly in light of the fast-changing financial market landscape. It will bring the following benefits to the industry and the public –

- (a) 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;
- (b) greater nimbleness in responding to new regulatory challenges and more effective implementation of international regulatory standards;
- (c) facilitating market innovation and maintaining competitiveness of the industry without undermining regulation; and
- (d) raising consumer confidence in the insurance industry.

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

We have received useful comments from respondents on various details of the proposals. We have taken into account the comments in developing the detailed proposals and will continue to engage the general public and relevant stakeholders during the next phase of work in drafting the legislation.

**Q2 Has the Government made any major changes to the consultation proposals taking into account the comments received from the public consultation exercise?**

**A2** There was positive public response to the consultation proposals for the IIA to assume additional functions in addition to the primary role as a prudential regulator of the insurance industry, viz. direct supervision on the conduct of insurance intermediaries, organize public education programme and conduct thematic researches and studies concerning the industry. With reference to the functions of other local financial regulators, we further propose that the legislation should provide expressly that the IIA should assist the Financial Secretary in maintaining the financial stability of Hong Kong by taking appropriate steps in relation to the insurance industry.

As proposed in the consultation document, for more effective regulation of insurers and insurance intermediaries and to put the IIA on a par with other financial regulators in Hong Kong, the IIA will be provided with express powers to initiate investigations, search and seize materials upon warrant, prosecute offences summarily and impose a range of regulatory sanctions on cases of misconduct. Further details are set out in our detailed proposals.

Taking account of the comments received from the public and stakeholders in the public consultation exercise, we have come up with enhanced proposals in the following areas –

- (a) Licensing and direct regulation of insurance intermediaries by the IIA – to facilitate smooth transition, we propose that pre-existing insurance intermediaries who are validly registered with the self-regulated organizations (“SROs”) should be deemed to be licensed with the IIA for three years upon establishment of the IIA, so that they can carry on their business while applying for licences from the IIA. (Please also see Q3 and Q4.)
- (b) Regulation of insurance intermediary activities of banks – the fundamental principle is that the IIA will be the primary and

lead regulator for all insurance intermediaries and be the sole regulator to set conduct standards and requirements. On the other hand, we note the substantial difference of the client base of bancassurance activities from that of insurance business, the operation of retail banks on an integrated business basis, as well as HKMA's role as the primary and lead regulator of banks. Therefore, it would be necessary for the IIA to work closely with the Hong Kong Monetary Authority ("HKMA") and delegate to it specified powers in respect of the regulation of insurance intermediary activities of banks. The delegation process will be subject to checks and balances. (Please also see Q6.) Disciplinary powers will be vested with the IIA, with HKMA's active participation in the disciplinary process. This arrangement should enhance regulatory effectiveness and consistency. (Please also see Q5 and Q7.)

- (c) Funding mechanism – We propose to introduce a cap on the levy and exempt reinsurance contracts from the levy to minimize impact on policyholders and maintain Hong Kong's competitiveness. (Please also see Q8.)
- (d) Future involvement of the industry – We propose to set up at least two Industry Advisory Committees under the IIA, e.g. one for Life Insurance and the other for Non-life Insurance, to tap the expertise of insurance practitioners who may provide expert advice to the IIA's Governing Board. The IIA should also be empowered to appoint an expert panel with members having industry knowledge for the IIA to seek advice in the disciplinary process as necessary.
- (e) Checks and balances – We propose to modernize the existing appeal mechanism by establishing an Insurance Appeals Tribunal to be chaired by a person who is eligible for appointment as a judge of the High Court. (Please also see Q10.)

**Q3            Why should the IIA take over the role of direct regulation of insurance intermediaries from the SROs?**

**A3**           Many respondents in the public consultation exercise expressed support of direct regulation of insurance intermediaries by the IIA, which would enhance public confidence in their professionalism and align Hong Kong's industry developments with international practices.

This notwithstanding, we also note that a number of respondents questioned the need of the proposal given that the existing regime has been operating smoothly. While we fully acknowledge the good efforts and valuable contribution of the SROs to the stable development of the insurance industry, there is an inherent problem with the existing self-regulatory framework as it gives rise to issues with perceived or real conflict of interest, and it does not align with local or international practices for financial market regulation. Furthermore, there are concerns on the consistency in the standards and mechanisms adopted for complaints handling, investigation and disciplinary actions by the three SROs. As such, we cannot be complacent, and maintaining the status quo will not be conducive to the long-term, sustainable development of the insurance industry nor to the upholding of Hong Kong's position as a global financial centre.

**Q4            How would the existing SRO regulation regime undergo the transition to the new licensing regime by the IIA? What would be the role of the SROs in future?**

**A4**           To facilitate smooth transition and minimize the impact on pre-existing insurance intermediaries, we propose to provide in the legislation that those who are validly registered with the SROs would be deemed to be licensed with the IIA for three years upon its establishment before they obtain the new licences, so that they can carry on their business while applying for licences from the IIA.

The legislation will specify the eligibility criteria for licensing with reference to pre-existing registration conditions determined

by the Insurance Authority under the Insurance Companies Ordinance and by the SROs before commencement of the new legislation, hence there should not be any material impact on the eligibility of insurance intermediaries who are validly registered with the SROs for obtaining a licence under the new regime. Whilst the professional standards for insurance intermediaries are subject to regular reviews in light of local and international insurance market developments and consumer expectation, there is no intention to introduce any changes to the eligibility requirements through the legislative exercise to establish the IIA.

At present, there are over 70,000 insurance intermediaries. For better management of applications for new licences, pre-existing intermediaries will need to submit their applications to the IIA within a specified period (say, within the first year upon the IIA's establishment) if they wish to carry on their business under the new regime. On the other hand, new insurance intermediaries would be required to submit applications to obtain a licence from the IIA before they are permitted to engage in the sale and marketing of insurance products.

In formulating the new regulatory regime, we shall continue to actively engage the SROs and leverage their experience to ensure a smooth migration to the new regime. We will seek views from the SROs on the detailed transitional arrangements and licensing requirements. To provide a basis for the IIA to establish and maintain a list of licensed insurance intermediaries, the IA will assist in the preparatory work and obtain relevant information of pre-existing insurance intermediaries from the SROs. We envisage that under the new regime, the existing SROs can continue to contribute to the industry as trade associations, representing the interest of their members, and organizing continuous professional development programmes, training courses, roadshows and other trade promotion activities, etc. The experience of local and overseas trade bodies in the financial market is relevant.

**Q5      How would insurance intermediary activities of banks be regulated in future?**

**A5**      Having regard to the views and comments from the insurance and banking industries and the public, we have enhanced the proposal for the regulation of insurance intermediary activities of banks.

The fundamental principle is that the IIA would be the primary and lead regulator for all insurance intermediaries, irrespective of whether or not they are bank employees, and the sole authority to set conduct standards and requirements. The scope of insurance intermediary activities which are subject to conduct regulation (“regulated activities”) will be defined in the legislation. Any person who wishes to undertake regulated activities would have to be licensed by the IIA.

On the other hand, we note the substantial difference of the client base of bancassurance activities from that of insurance business, the operation of retail banks on an integrated business basis, as well as HKMA’s role as the primary and lead regulator of banks. Therefore, it would be logical and necessary for the IIA to work closely with HKMA in the regulation of insurance intermediary activities in banks. To achieve this, it will be necessary for the IIA to delegate specified powers to the HKMA. The delegation of powers is subject to checks and balances set out in A6.

Inspection of banks’ insurance intermediary activities will be carried out jointly by the IIA and HKMA. On top of that, HKMA will also carry out its own inspections (regular or thematic) in relation to general banking activities. As for investigation, the IIA will have the primary power to investigate into complaints and suspected non-compliance of relevant legislation / codes. The IIA will delegate investigatory power in respect of insurance intermediary activities of banks to HKMA. Where the IIA considers necessary, e.g. in cases where the principal insurer is involved, it may carry out investigation, take over investigation from HKMA, or send staff to participate in HKMA’s investigation team. Disciplinary powers would be vested with the IIA, with HKMA’s active participation in the disciplinary process.

**Q6        Are there any safeguards against any abuse of the proposed delegation arrangements?**

**A6**        To enhance transparency and certainty, the delegable powers would be stipulated in the statute. Certain powers that would be made non-delegable (i.e. must be executed by the IIA Governing Board or IIA executive) would also be stipulated in the statute. Delegation of any powers and withdrawal of such delegation to HKMA would be subject to the approval of the Chief Executive (“CE”) in Council on the recommendation of the IIA.

In exercising such delegated powers, HKMA would be accountable to the IIA, which may withdraw or modify the delegation subject to the approval of CE in Council.

**Q7        How to ensure regulatory consistency between the IIA and HKMA?**

**A7**        There will be only one authority, viz. the IIA, which will be vested with the power to issue licence and set conduct standards and requirements for all insurance intermediaries.

To ensure consistency in disciplinary decisions, the disciplinary power on all insurance intermediaries is vested with the IIA. The IIA will exercise its disciplinary power with the support of a Disciplinary Committee (“DC”) chaired by a senior IIA executive with members from both IIA and HKMA. The IIA will consider all investigation reports on alleged misconduct of insurance intermediaries and take a view on whether and if so, what disciplinary sanctions are warranted.

The IIA and HKMA will sign a Memorandum of Understanding setting out the detailed arrangements for the two authorities to cooperate to facilitate consistency in regulation, minimize regulatory gap or overlap in powers, as well as facilitate exchange of information. In exercising its delegated powers, HKMA will involve the IIA in the process and there will be close communication between the two regulators. For example –

(a) Inspection of banks’ insurance intermediary activities will be carried out jointly by IIA and HKMA.

- (b) For inspections to be carried out by HKMA, HKMA and IIA will agree on the annual supervisory focus in respect of insurance intermediary activities of banks and any subsequent material changes;
- (c) HKMA will share with the IIA inspection findings in relation to the banks' insurance intermediary business;
- (d) IIA and HKMA will jointly design and implement composite mystery shopper programmes in relation to insurance intermediary activities of banks; and
- (e) IIA and HKMA will exchange information at their regular liaison meetings, share information relating to their investigation, and keep each other posted of their investigations and follow-up actions for cases with mutual regulatory concerns.

**Q8            How would the IIA be funded?**

**A8**            To ensure financial independence of the IIA, we propose that it should have stable sources of revenue to fully recover its cost from the market under the following structure –

- (a) a fixed licence fee payable by all insurers and insurance intermediaries;
- (b) a variable licence fee payable by insurers only and calculated on the basis of their individual liabilities;
- (c) user fees for specific services; and
- (d) a levy of 0.1% on insurance premiums for all insurance policies.

To alleviate the impact on the industry and policyholders, we further proposed in the consultation document that the IIA should

recover its cost in the sixth year of its operation, i.e. during the first five years of the IIA's establishment –

- (a) the licence fee for insurance intermediaries would be waived;
- (b) an incremental approach would be adopted in achieving the target levels of variable licence fee on insurers and levy on insurance policies; and
- (c) a lump sum subsidy of \$500 million would be provided by the Government to the IIA.

Public response to the above was generally positive. We note the views from some respondents that the levy may drive high premium policies offshore, and that reinsurance contracts should be exempted from the levy to avoid double-charging. Taking into account the views from respondents in the public consultation exercise, we further propose that –

- (a) a cap be imposed on the levy on non-life insurance policies with annual premiums at or above \$5 million and life insurance policies with single or annualized premiums at or above \$100,000; and
- (b) reinsurance contracts be exempted from the levy.

According to industry statistics, high premium policies account for only a very small part of the total pool of policies. We believe these further proposals will help minimize the impact on policyholders and maintain Hong Kong's competitiveness in the international insurance market.

We also propose that the IIA should review the levy/fee levels once its reserve has reached a level equivalent to 24 months of its operating expense, after deducting depreciation and all provisions. Any revision to the levy/fee levels should be subject to negative vetting by the Legislative Council ("LegCo").

**Q9           What is the governance structure of the proposed IIA?**

**A9**       We propose to provide in the legislation for the following governance structure for the IIA :

- (a) Governing Board (“the Board”): The Board should be appointed by the CE to provide leadership and direction and to guide the IIA in the development of a corporate strategy to achieve its objectives and perform its functions effectively. It should comprise predominately non-executive directors from a cross-section of the community.
- (b) Supporting Committees: The Board should be empowered to form supporting committees designated to oversee specific areas of the IIA’s work and make recommendations to the Board. The supporting committees should include (but not be limited to) an Audit Committee, a Finance Committee, a Remuneration Committee and a Management Committee.
- (c) Industry Advisory Committees: There should be at least two Industry Advisory Committees, e.g. one for Life insurance and the other for Non-life insurance, to advise and make recommendations to the Board on industry-related issues and policies. We propose that the Industry Advisory Committees be appointed by the Financial Secretary. They may comprise insurance practitioners, industry body representatives and user/consumer groups.
- (d) Disciplinary Committee (“DC”): The IIA should form a DC, as an internal administrative arrangement, to assist the IIA in hearing and advising on investigation reports compiled by IIA / HKMA executive. The DC will be chaired by a senior IIA executive with members from both the IIA and HKMA.
- (e) Expert Panel: The Board should be empowered to appoint an expert panel. Individual members of the panel may be invited by the IIA to assist in the disciplinary process by way of providing expert advice on the nature of a specific product or related industry practices, or experiences in previous cases of similar nature, if the IIA considers that such advice would be

desirable for its deliberations in the process. The expert panel may include lay members of existing SROs, senior executives from authorized insurers, agents in life or non-life business, senior executives of insurance brokers, senior executives of banks and travel agencies with insurance intermediary business, and representatives from consumer interest bodies (e.g. the Consumer Council and the proposed Investor Education Council).

**Q10**      **What measures would be taken to provide adequate checks and balance for the IIA's exercise of powers?**

**A10**      To enhance accountability of the IIA in the exercise of its statutory powers, we propose to put in place the following checks and balances :

- (a) the IIA should table its annual reports before the LegCo;
- (b) the annual budget and corporate plan of the IIA should be subject to the approval of the Financial Secretary;
- (c) certain powers should be made non-delegable (i.e. must be executed by the Board, or IIA executive);
- (d) where the IIA has exercised its disciplinary power against an insurer / insurance intermediary, it should disclose to the public details of the decision including the reasons and any material facts relating to the case;
- (e) an independent Insurance Appeals Tribunal should be established to handle appeals from insurers and insurance intermediaries against relevant decisions made by the regulator under the legislation. The tribunal should operate on a full-time basis and be chaired by a person who is eligible for appointment as a judge of the High Court and include a number of market practitioners and others with appropriate knowledge and experience of the insurance industry, all to be appointed by the CE. The tribunal may confirm, vary or set aside the decisions made by the regulator, as well as direct the

regulator to make a decision afresh in respect of any specified matter. A party who is dissatisfied with a decision of the tribunal may appeal to the Court of Appeal against the decision on a point of law;

- (f) an independent Process Review Panel should be established by the CE to review internal operating procedures of the IIA and HKMA in respect of the regulation of insurers and insurance intermediary activities; and
- (g) Complaints against the IIA may be lodged with the Office of the Ombudsman. The Director of Audit and the Independent Commission Against Corruption should also be empowered to oversee the practices and procedures of the IIA. The use of personal data by the IIA should be in compliance with the Personal Data (Privacy) Ordinance.

**Q11      What are the next steps and the timetable for the establishment of the IIA?**

**A11**      We will continue to engage with the insurance and banking industries and relevant stakeholders with a view to refining the detailed proposals for the drafting of legislation. We aim to make available draft key legislative provisions for engaging the general public and stakeholders in early 2012.

**Q12      How to access the consultation conclusions and the detailed proposals?**

**A12**      The consultation conclusions, written submissions received and the detailed proposals for the proposed establishment of an IIA have been uploaded to the website of the Financial Services and the Treasury Bureau  
([http://www.fstb.gov.hk/fsb/ppr/consult/iaa\\_conclusion.htm](http://www.fstb.gov.hk/fsb/ppr/consult/iaa_conclusion.htm)).

**Financial Services and the Treasury Bureau  
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