Overview

The ICO and its subsidiary regulations provide the regulatory framework for insurers, reinsurers and insurance intermediaries in Hong Kong and establish basic guidelines governing various aspects, including but not limited to authorization, ongoing compliance and reporting obligations of an insurer or reinsurer's business. The OCI is the regulatory body set up for the administration of the ICO. The OCI is headed by the Commissioner of Insurance, who is the public officer appointed as the IA for regulating and supervising the insurance industry in Hong Kong. In short, the Commissioner of Insurance is the IA who is empowered under the ICO to regulate and supervise Hong Kong's insurance industry and the OCI is the government department to support the Commissioner of Insurance/the IA in exercising his/her functions.

The principal functions of the IA are to ensure that the interests of policy holders or potential policy holders are protected and to promote the general stability of the insurance industry in Hong Kong. The major duties and powers of the IA are set out as follows:

- authorising insurers to carry on insurance business in or from Hong Kong;
- ensuring the financial soundness and integrity of the insurance market, primarily through the examination of the annual audited financial statements and business returns submitted by the insurers;
- working closely with the representative bodies of the insurance industry in promoting self-regulation by the industry with the aim of enhancing the protection of policy holders; and

In addition, the IA promotes and encourages proper standards of conduct and sound and prudent business practices among insurers. In this regard, the IA may from time to time issue new guidelines, regulations and requirements in relation to risk management, business conduct, customer protection, etc. The IA ensures that it is observing the insurance core principles stipulated by the International Association of Insurance Supervisors, and keeping with market developments and provides adequate protection to the insuring public.

Regulation of Insurance Companies

Authorisation

Companies carrying on insurance business in or from Hong Kong must obtain authorisation from the IA. Authorisation will only be granted to insurers meeting certain requirements under the ICO, which focus on, among other things, the following aspects:

- paid up capital;
- solvency margin;
- fitness and properness of directors and controllers; and
- adequacy of reinsurance arrangements.

In addition, an insurer must meet certain other conditions under the Authorisation Guidelines issued by the IA, which seek to ensure that the insurer is financially sound and competent to provide an adequate level of services to the insuring public.

Types of Insurance Business

The ICO requirements vary depending on the type of insurance business being undertaken by an insurer. The ICO defines two main types of business as follows:

- General business covers all business other than long-term business, including but not limited to accident and sickness, fire, property, motor vehicle, general liability, financial loss and legal expenses insurance; and

- Long-term business covers those types of insurance business in which policies are typically in place for long periods and includes but not limited to life and annuity, linked long-term, permanent health and retirement scheme management policies.

An insurer that undertakes both long-term and general business is referred to by the IA as a composite insurer.

In addition to these main types of business, the IA imposes further requirements on insurers conducting insurance business (not being reinsurance business) relating to liabilities or risks in respect of which persons are required by any Ordinance to be insured ("**Statutory Business**"), including employees' compensation insurance, third-party insurance in respect of motor vehicles and local vessels, and building owners' corporation third party risks insurance.

Capital Requirement

According to the ICO, the minimum paid-up capital for an insurer carrying on solely general business is HK$10 million. For a composite insurer (carrying on both general and long-term business) or for an insurer carrying on Statutory Business, the minimum paid-up capital is HK$20 million. However, for the purpose of applying for authorization in Hong Kong, applicant should demonstrate to the IA that it has sufficient financial resources to pre-finance its proposed operation and has long-term commitment to Hong Kong.

Solvency Margin

Pursuant to section 8(3) and 35AA of the ICO, an insurer is required to maintain at all times an excess of assets over liabilities of not less than a specified amount. For a company carrying on general business only, the specified amount applicable to the company is determined as follows:

- Where the relevant premium income of the company in its last preceding financial year, or the relevant claims outstanding of the company as at the end of its last preceding financial year, whichever is the greater, did not exceed HK$50 million or its equivalent, the specified amount is HK$10 million or its equivalent.

- Where the said income in that year, or the said claims outstanding as at the end of that year, whichever is the greater, exceeded HK$50 million but did not exceed HK$200 million or its equivalent, the specified amount is one-fifth of the said income in that year, or one-fifth of the said claims outstanding at the end of that year, as the case may be.

- Where the said income in that year, or the said claims outstanding as at the end of that year, whichever is the greater, exceeded HK$200 million or its equivalent, the specified amount is the aggregate of HK$40 million and (a) one-tenth of the amount by which the said income in that year exceeding HK$200 million; or (b) one-tenth of the amount by which the said claims outstanding as at the end of that year exceeded HK$200 million, as the case may be, or its equivalent.

In the case of an insurer carrying on the Statutory Business, the specified amount shall not be less than HK$20 million or its equivalent.

For this purpose:

- the relevant premium income of a company in any financial year shall be whichever is the greater of the following amounts:

    (i) an amount equal to 50% of the gross premium income of the company in that financial year;

    (ii) the amount obtained by deducting from its gross premium income the amount of any premiums payable by the company in respect of reinsurance; and

- the relevant claims outstanding of a company as at the end of a financial year shall be:

    (a) where no class of the general business of the company is accounted for on a fund accounting basis, the aggregate of:

        (i) an amount equal to 50% of the claims outstanding before deducting any amount recoverable from reinsurers thereon, or the amount of claims outstanding after deducting any amount recoverable from reinsurers thereon, whichever is the greater; and

        (ii) the amount set aside by an insurer at the end of its financial year, in addition to any unearned premiums, which is considered necessary to meet the cost of claims and expenses of settlement arising from risks to be borne by the insurer after the end of the financial year under contracts of insurance entered into before the end of that year (the "**additional amount for unexpired risks**").

    (b) where all classes of the general business of the company are accounted for on a fund accounting basis, the fund.

To determine a general business insurer's solvency margin, assets are valued in accordance with the Insurance Companies (General Business) (Valuation) Regulation (the "**Valuation Regulation**").

Fitness and Properness of Directors and Controllers

The directors or the controllers of all authorised insurers must be "fit and proper" to hold such positions. A controller includes, among others, a managing director of the insurer or its corporate parent, a chief executive of the insurer or its corporate parent (only if the parent is also an insurer), or a person in accordance with whose directions or instructions the directors of the insurer or its corporate parent are accustomed to act or who, alone or with any associate or through a nominee, is entitled to exercise, or control the exercise of, 15% or more of the voting power at any general meeting of an insurer or its corporate parent. The ICO also requires notification to the IA of any change in the directors or controllers of an authorised issuer and prior approval of the IA is required for the appointment of certain controllers, including the chief executive of an insurer. In applying the fit and proper test, the IA will take into account, among other things, the character, reputation, qualifications, experience, integrity, reliability, financial status and ability of the directors or controllers of the applicant company and the ability to perform the relevant functions efficiently, honestly and fairly. The IA has issued a Guidance Note on "Fit and Proper" criteria under the ICO which sets out those factors that the IA will take into account in administering the said requirement.

In addition, under the Guidance Note on "Fit and Proper" criteria under the ICO, the IA is not likely to be satisfied that the director or controller is a fit and proper person, if the person, among others, (i) has been found by a court or other competent authority to have acted fraudulently or dishonestly and (ii) was or has been a director or controller (within the meaning of section 9 of the ICO) of a body corporate or insurer, in Hong Kong or elsewhere, which, with the consent or connivance of, or because of the neglect by, the person failed to comply with any legislative or other regulatory requirements or any guidelines made thereunder.

Adequate Reinsurance Arrangements

An insurer is required under the ICO to have adequate reinsurance arrangements in force in respect of the reinsurance of risks of those classes of insurance which are to be carried on by the insurer. In considering the adequacy of reinsurance arrangements of an insurer, the IA will take into account the following factors:

- reinsurance management framework of the insurer;
- type of reinsurance arrangements;
- maximum retention of the insurer;
- spread of risks among reinsurers; and
- security of the reinsurers.

Reporting Requirements

The ICO requires a submission to be filed by an insurer annually with the IA of its accounts, statements and other information as required by the ICO. An insurer carrying on general business is additionally required to submit annually to the IA an audited general business return and audited statement of assets and liabilities pertaining to its Hong Kong general business.

Power of Intervention

The IA is empowered under the ICO to take appropriate actions against an insurer where there are causes for concern over that insurer. The purpose is to protect the interests of policy holders and potential policy holders of the insurer against the risk that the insurer may be unable to meet its liabilities or to fulfill the reasonable expectations of policy holders or potential policy holders. These actions include:

- restrictions on effecting new business;
- limitation of premium income;
- restrictions on investments;
- custody of assets by an approved trustee;
- requirement for a special actuarial investigation; and
- assumption of control of an insurer.

Maintenance of Assets

Generally, the ICO requires an insurer carrying on general business, other than a professional reinsurer and a captive insurer, to maintain assets in Hong Kong of an amount which is not less than:

(a) the aggregate of (i) 80% of its liabilities after deducting the amount in respect of which contracts of reinsurance have been entered into and (ii) the Relevant Amount, i.e. the specified amount determined in accordance with "Solvency Margin" above (except that the gross premium income shall be deemed to be the gross premium income arising from the insurer's Hong Kong insurance business only, and claims outstanding, additional amount for unexpired risks and fund shall be deemed to be the claims outstanding, additional amount for unexpired risks and fund respectively arising from the insurer's Hong Kong insurance business only); or

(b) where, in respect of such liabilities, it has entered into contracts of reinsurance for which the premiums payable exceeded one half of the gross premiums received, the aggregate of (i) 40% of its liabilities before deducting the amount in respect of which contracts of reinsurance have been entered into and (ii) the Relevant Amount,

and where paragraph (b) applies, the insurer shall maintain assets in accordance with paragraph (a) or (b), whichever is greater.

The objective is to ensure that, in the event of insolvency of an insurer, assets will be available in Hong Kong to meet the claims of Hong Kong policy holders. These claims are accorded a preferential status under Hong Kong's insolvency laws to those of ordinary creditors.

Actuarial Review of Insurance Liabilities

Adequacy of the reserves set aside by an insurer is an important factor affecting the insurer's ability to meet its obligations for the payment of claims and to fulfil the reasonable expectations of policy holders. To ensure reserve adequacy, the IA has issued a Guidance Note on "Actuarial Review of Insurance Liabilities in respect of Employees' Compensation and Motor Insurance Businesses" which requires insurers and reinsurers carrying on employees' compensation and/or motor insurance businesses in or from Hong Kong to conduct an actuarial review of reserves relating to the said two important statutory classes of insurance business, in accordance with the criteria set out in the said Guidance Note on an annual basis. An actuarial report is required to be prepared and certified by the actuary, and to be submitted to the IA annually for review.

Statutory Valuation Basis for Assets and Liabilities

The Valuation Regulation provides a basis for the valuation of the assets and liabilities of an insurer carrying on general business. The Valuation Regulation prescribes the valuation methods for different types of assets commonly found in an insurer's balance sheet. To ensure a prudent spread of investments, the Valuation Regulation also stipulates admissibility limits for different categories of assets. The admissibility limits, however, do not apply to assets maintained in Hong Kong pursuant to the local asset requirement.

Corporate Governance of Authorised Insurers

The IA has issued a Guidance Note on "The Corporate Governance of Authorized Insurers", which aims to enhance the integrity and general well-being of the insurance industry through providing guidance to authorised insurers for the evaluation and formulation of their internal control and procedures. The Guidance Note sets out the minimum standard of corporate governance that is expected of authorized insurers and applies to an authorised insurer incorporated in Hong Kong and an authorised insurer incorporated outside Hong Kong where 75% or more of the annual gross premium income pertains to its Hong Kong insurance business, unless written consent for exemption has been obtained from the IA.

Asset Management

In order to ensure that an insurer will meet its contractual liabilities to policy holders, its assets must be managed in a sound and prudent manner, taking into account the profile of liabilities and risks of the insurer. The IA has issued a Guidance Note on "Asset Management by Authorized Insurers", which is adopted from the paper "Supervisory Standard on Asset Management By Insurance Companies", as approved by the International Association of Insurance Supervisors in 1999. The Guidance Note applies to an insurer incorporated in Hong Kong and the Hong Kong branch of an insurer incorporated outside Hong Kong whose investment in financial assets exceeds HK$100 million. The Guidance Note provides a checklist for assessing how insurers should control the risks associated with their investment activities.

The Code of Conduct for Insurers

As part of the self-regulatory initiatives taken by the industry, the Hong Kong Federation of Insurers ("**HKFI**") has published The Code of Conduct for Insurers. This Code seeks to describe the expected standard of good insurance practice in the establishment of insurance contracts and claims settling; promote the disclosure of relevant and useful information to customers; facilitate the education of customers about their rights and obligations under insurance contracts; foster a high professional standard in the transaction of insurance business; and encourage insurers to promote and enhance the industry's public image and standing. This Code applies to all general insurance members and life insurance members of the HKFI and applies to insurance effected in Hong Kong by individual policy holders. As a condition of membership of the HKFI, all general insurance members and life insurance members shall undertake to abide by this Code and use their best endeavours to ensure that their staff and insurance agents observe its provisions.

The Insurance Claims Complaints Panel

The Insurance Claims Complaints Bureau was set up by the insurance industry in February 1990 to implement self-regulation in the interpretation and handling of insurance claims complaints arising from all types of personal insurance policies. The Insurance Claims Complaints Panel ("**Complaints Panel**") was established by the Insurance Claims Complaints Bureau with the objective of providing independent and impartial adjudication of complaints between insurers and their policy holders. The Complaints Panel is in charge of handling claims complaints either from policy holders themselves or their beneficiaries and rightful claimants. The Complaints Panel, in making its rulings, shall act in conformity with the terms of the relevant policy, general principles of good insurance practice, any applicable rule of law or judicial authority, and any codes and guidelines issued from time to time by the HKFI. It is also given the power by its members to look beyond the strict interpretation of policy terms.

The Complaints Panel's decisions are binding on members of the Insurance Claims Complaints Bureau, without any right of appeal. However, if complainants find the Complaints Panel's decision unacceptable, they are free to seek legal redress, because their legal rights are not affected by reference to the Complaints Panel.

Motor Insurers' Bureau of Hong Kong

The Motor Insurers' Bureau of Hong Kong (the "**MIB**") was incorporated to secure the satisfaction of claims in respect of liability for death or bodily injury which arises from the use of motor vehicles on the road, when the use of the vehicle is required to be covered by the Motor Vehicles Insurance (Third Party Risks) Ordinance. Under the Motor Vehicles Insurance (Third Party Risks) Ordinance, all vehicles must be insured against claims for third party bodily injuries arising out of an accident involving the use of the vehicle on a road. The MIB has been providing compensation to victims of traffic accidents where the drivers concerned are uninsured or untraceable, or the insurers concerned are insolvent.

The MIB administers two funds, namely the First Fund and the Insolvency Fund. The First Fund provides relief to a third party traffic accident victim (or his/her dependants) who suffers bodily injury or death but is unable to obtain compensation because the driver is uninsured or untraceable. As a result of the legislative changes in 1995 whereby insurance policies are allowed to set a limit on third party liabilities, the coverage of the First Fund is extended to include that part of the awards to traffic accident victims which exceeds the policy limit. The Insolvency Fund compensates a third party claimant whose claims for bodily injury, death or property damage resulting from a traffic accident remains unsettled due to the insolvency of the insurer concerned.

All insurance companies in Hong Kong who are authorized by the IA to write motor insurance are required to be members of the MIB. Each member has entered into an agreement with the MIB to contribute such funds as may be required by the MIB to meet its objectives.

Regulation of Insurance Intermediaries

General Provision

Insurance intermediaries, i.e., insurance agents and insurance brokers, are subject to a self-regulatory system supported by legislation which is contained in Part X of the ICO.

An insurance agent means a person who holds himself out to advise on or arrange contracts of insurance in or from Hong Kong as an agent or subagent of one or more insurers. An insurance broker means a person who carries on the business of negotiating or arranging contracts of insurance in or from Hong Kong as the agent of the policy holder or potential policy holder or advising on matters relating to insurance.

Under the ICO, a person is prohibited from holding himself out as an insurance agent or insurance broker unless he is properly appointed or authorised. A person is also prohibited from holding himself out as an appointed insurance agent and an authorised insurance broker at the same time. It is an offence under the ICO for an insurer to effect a contract of insurance through, or accept insurance business referred to it by, an insurance intermediary who has not been properly appointed or authorised.

The OCI introduced an Insurance Intermediaries Quality Assurance Scheme for insurance intermediaries. Under the scheme, all insurance intermediaries, their chief executives or responsible officers and technical representatives are required to pass the Insurance Intermediaries Qualifying Examination conducted by the PEAK Examination Centre of the Vocational Training Council as one of the requirements for entry to the profession (unless they are exempted) and to comply with the requirements of the continuing professional development programmes thereafter.

Registration of Appointed Insurance Agents

To act as an insurance agent, a person is required to be appointed by an insurer and registered with the Insurance Agents Registration Board ("**IARB**") set up by the HKFI. An appointed insurance agent shall not represent more than four insurers, of whom no more than two shall be long-term business insurers.

Under the ICO, an insurer is required to keep a register of appointed insurance agents and to make it available for public inspection at its registered office or at a place approved by the IA. For this purpose, the IA has approved the registered office of the HKFI as the place where the register should be maintained and made available for public inspection.

An insurer is required to give the IA details of the registration and removal of its appointed insurance agents within seven days of such registration or removal. Alternatively, the insurer may provide such details to the IARB, and in so doing the insurer concerned is considered as having complied with this requirement. Upon receipt of such notification by the insurer, the IARB shall update the register and notify the IA accordingly.

Administration of Insurance Agents

An insurer is required to comply with the Code of Practice for the Administration of Insurance Agents ("**the Code of Practice**") issued by the HKFI and endorsed by the IA. An insurer is responsible for the actions of its appointed insurance agents in their dealings with clients in respect of the issue of insurance contracts and related insurance business.

The Code of Practice specifies, among others, the rules and procedures governing the registration and de-registration of insurance agents, the power of the IARB to handle complaints and require the insurers to take disciplinary actions against their insurance agents, the fit and proper criteria of insurance agents and the minimum requirements of the agency agreement. In particular, the Code of Practice provides for the following:—

- A register of appointed insurance agents and a sub-register of insurance agents' responsible officers and technical representatives shall be kept and maintained for public inspection;

- An insurer must ensure that its agents are registered with the IARB whereas an insurance agent must ensure that its responsible officer and technical representatives are registered with the IARB;

- An insurance agent is prohibited from representing more than four insurers, of which no more than two shall be long term insurers;

- A responsible officer or technical representative of an insurance agent is prohibited from being a responsible officer or technical representative of another insurance agent; and

- The IARB has disciplinary powers against insurance agents, their responsible officers or technical representatives registered with it. Disciplinary actions may include:

  (i) issuing a reprimand to an insurance agent, its responsible officer or technical representatives;

  (ii) suspending or terminating the appointment of an insurance agent, its responsible officer or technical representatives; or

  (iii) such other actions as the IARB thinks fit.

The IARB issues guidelines from time to time indicating how it intends to exercise its powers and fulfil its responsibilities under the Code of Practice. The guidelines issued by the IARB include the following:

- guidelines on misconduct;
- guidelines on handling of premiums; and
- guidelines on the effective date of registration of insurance agents, responsible officers and technical representatives.

Authorisation of Insurance Brokers

An insurance broker shall either obtain an authorisation from the IA or be a member of a body of one of the two insurance broker bodies approved by the IA, namely The Hong Kong Confederation of Insurance Brokers and Professional Insurance Brokers Association.

An insurance broker who is a member of an approved body of insurance brokers is also subject to the membership regulation of his own professional body that is approved by the IA.

In order to be authorised as an insurance broker or be admitted as a member of an approved body of insurance brokers, a person, apart from being fit and proper to be an insurance broker, must satisfy the minimum requirements specified by the IA with regard to:

- qualifications and experience;
- capital and net assets;
- professional indemnity insurance;
- keeping separate client accounts; and
- keeping proper books and accounts.

Register of Insurance Brokers

The IA is required to maintain a register of authorised insurance brokers as well as a register of approved bodies of insurance brokers. The registers are open for public inspection.

An approved body of insurance brokers is required to maintain a register of its members which contains information required by the IA in respect of each member for public inspection.

Audit Requirement of Insurance Brokers

An insurance broker, authorised by the IA or who is a member of an approved body of insurance brokers, is required to submit an annual audited financial statements together with an auditor's report as to whether the auditor is of the opinion that the insurance broker has continued to comply with the minimum requirements of the IA or the approved body, as the case may be. The approved body of insurance brokers is required to submit to the IA an annual auditor's report on its members' continued compliance with the minimum requirements.

Power of Intervention regarding Insurance Agents and Insurance Brokers

The IA is empowered to direct the insurer to deregister an appointed insurance agent if that agent has breached the Code of Practice. The IA is also empowered to withdraw the authorisation of an insurance broker authorized under the ICO or approval of a body of insurance brokers if the broker or the approved body has failed to comply with the relevant authorisation or approval requirements under the ICO as appropriate or the withdrawal is justified in the interests of policy holders or potential policy holders or the public. The IA also has the power to require an insurer, insurance agent, insurance broker or approved bodies of insurance brokers to produce books and papers for its examination of the affairs of insurance intermediaries. The IA also has the power to present a petition for an insurance intermediary to be wound up or declared bankrupt if he considers it to be in the public interest.

Authorization from the IA in respect of our Group's Reorganization and use of company names

Pursuant to section 13B of the ICO, in general, no person shall become a controller of an authorised insurer incorporated in Hong Kong unless (1) he has served on the IA a notice in writing stating that he proposes to become a controller of that insurer and containing the information required under the ICO; and (2) the IA has either notified him in writing that there is no objection to his becoming a controller of the insurer or no notice of objection is served on him from the IA after expiration of the period prescribed under the ICO. Under section 13B of the ICO, a controller means a person who, alone or with others as stated in the ICO, is entitled to exercise, or control the exercise of, 15% or more of the voting power at any general meeting of the insurer.

Before the Reorganisation, Target was owned by Tracing Paper, Mr. Chiu and Mr. Lai as to 70%, 15% and 15% respectively. Tracing Paper is in turn owned by Dr. Cheung and Dr. Choi as to 70% and 30% respectively. Upon completion of the Reorganisation but before completion of the Share Offer, Target has become a wholly-owned subsidiary of our Company. Dr. Cheung, Dr. Choi, Mr. Chiu and Mr. Lai, through their respective wholly-owned nominee companies, namely, Independent Assets, Allied Connect, Generous Rich and Champion City, owned 49%, 21%, 15% and 15% of the entire issued share capital of our Company respectively immediately after completion of the Reorganisation but before completion of the Share Offer.

As each of our Company, Independent Assets, Allied Connect, Generous Rich and Champion City was entitled to exercise, or control the exercise of, 15% or more of the voting power at any general meeting of Target following completion of the Reorganisation, all of them had become the new controllers of Target under section 13B of the ICO. Hence, the Reorganisation is subject to the approval of the IA under section 13B of the ICO. The IA had granted its approval to each of our Company, Independent Assets, Allied Connect, Generous Rich and Champion City to be the controllers of Target in November 2014.

For details of the Reorganisation, please refer to the paragraph headed "Our Group's Reorganisation" under the section headed "History, Reorganisation and Corporate Structure" in this prospectus.

Further, pursuant to section 56A of the ICO, written consent from the IA is required for a company using the words "insurance" and "保險" in the description of the name of the company under which it is carrying business in or from Hong Kong. As the official English and Chinese company names of our Company contain the words "insurance" and "保險" respectively, an application was made to the IA for its consent regarding the use of the words "insurance" and "保險" in the name of our Company pursuant to the ICO. The IA has given its consent to our Company to use the words "insurance" and "保險" in its official English and Chinese names in November 2014.

New regulatory regime

Introduction

The Insurance Companies (Amendment) Bill 2014 (the "**Bill**") was introduced by the HK Government to provide for, among other things, the establishment of an independent Insurance Authority (the "**IIA**") and a statutory licensing regime for insurance intermediaries to replace the existing self-regulatory system. The Bill was gazetted on 25 April 2014 and was presented to the Legislative Council for a first reading on 30 April 2014.

Key milestones for the proposed establishment of the IIA include:

- launched public consultation on the proposed establishment of the IIA in July 2010;
- announced the consultation conclusions and detailed proposals in June 2011;
- consulted the Legislative Council Panel on Financial Affairs on consultation conclusions and detailed proposals in July 2011;
- issued the key legislative proposals on establishing the IIA for a 3-month consultation from October 2012 to January 2013;
- reported the consultation conclusions and the revised proposals to the Legislative Council Panel on Financial Affairs in July 2013;
- established a working group to ensure a smooth transition to the statutory licensing regime under the IIA in October 2013;
- issued a Legislative Council brief to the Legislative Council on 16 April 2014; and
- presented the Bill to the Legislative Council for the first reading on 30 April 2014.

Establishment of the IIA

In line with international supervisory principles and to keep pace with the rapid developments of the insurance industry, the HK Government proposed to establish the IIA, which would be both financially and operationally independent of the HK Government, to replace the OCI which is a government department. The policy objectives of setting up the IIA are to modernize the regulatory infrastructure to facilitate the stable development of the insurance industry, provide better protection for policy holders and align with international practice that insurance regulators should be financially and operationally independent of the government and the industry. The HK Government believes that compared to the existing self-regulatory system, the proposed arrangements should be more effective and better meet the needs of market development.

Governance and funding of the IIA

The IIA will be a body corporate with perpetual succession comprising a chairperson, a chief executive officer and not less than six directors with at least two directors being persons with knowledge of or experience in the insurance industry. To attach importance to the accountability of the IIA, the IIA will comprise majority of non-executive directors in order to ensure effective oversight of executive decisions.

To ensure that the IIA is financially independent of the HK Government, it is proposed that the IIA should be financed by fees payable by insurers and insurance intermediaries, user fees for providing specific services by the IIA and a levy of 0.1% on insurance premiums for all insurance policies.

Functions and powers of the IIA

The IIA is expected to work with the insurance industry to promote healthy and sustainable development of the insurance industry and to educate the public on the nature of insurance, features of particular insurance products and assessment of insurance needs against various risks.

The IIA will also be vested with appropriate powers of inspection, investigation, imposition of disciplinary sanctions and prohibition of licence application of insurance intermediaries in relation to a regulated activity or authorization application of insurers for any class of insurance business in a specified period. The IIA will be empowered to make rules and publish codes and guidelines. Prior to the introduction of new regulatory requirements via rules which are subsidiary legislation, the IIA is required to consult the industry. As safeguards, it is proposed that its regulatory decisions including licensing, authorization and disciplinary decisions are subject to review by the Insurance Appeals Tribunal, an independent quasi-judicial body. The Insurance Appeals Tribunal may confirm, vary or set aside any such decisions of IIA.

Licensing of insurance intermediaries and conduct regulation

Pursuant to the Bill, a person requires a licence granted by the IIA to carry on regulated activities, which cover activities in relation to giving advice on insurance and sale and after-sale administration of insurance policies (such as policy renewal or insurance claims), in the course of their business or employment or for reward. The Bill contains an express provision that it is an offence for a person who is not a licensed insurance intermediary to carry on any regulated activity or to hold out as a licensed insurance intermediary.

The categorization of licences will mirror the existing five categories of registration under the current self-regulatory system to ensure a smooth transition and all pre-existing insurance intermediaries validly registered with the current self-regulatory organizations before the commencement of the statutory licensing regime would be deemed as licensees under the new regime for three years. The proposed categorization of licences under the Bill is as follows:—

	Insurance agent	**Insurance broker**
Licence to business entities	(1) Licensed insurance agencies	(2) Licensed insurance broker companies
Licence to individuals	(3) Licensed individual insurance agents (4) Licensed technical representatives (agent)	(5) Licensed technical representatives (broker)

The Bill also provides that a licensed insurance agency or licensed broker company would be required to appoint at least one responsible officer who should ensure that internal control systems and procedures are in place to promote compliance with conduct requirements within a body corporate. The existing provisions of the ICO subjecting the appointed actuary, directors and controllers of an insurer to regulatory scrutiny will be updated to vest in the IIA the power to approve the appointment of senior executives who carry out "control functions", including risk management, compliance, actuarial matters and internal audit, based on fit and proper criteria such as professional competence, financial soundness and record of legal and regulatory compliance.

Proposed establishment of a policy holders' protection fund

To better protect policy holders' interest, maintain market stability in the event of insurer insolvency and enhance public confidence in and competitiveness of the insurance industry, the HK Government intends to establish a policy holders' protection fund as a safety net for policy holders.

The risk-based capital framework for the insurance industry in Hong Kong

The ICO and its regulations, together with the Guidance Notes issued by the IA, prescribe a capital adequacy framework for insurers operating in Hong Kong. For the existing capital adequacy framework, capital adequacy is assessed based on an insurer's solvency margin, i.e. the level of surplus derived from the value of assets of an insurer vis-a-vis the value of its liabilities. Solvency requirements for general business are calculated with reference to the premium levels and claims outstanding, the risk factors pertinent to an individual insurer are not featured or quantified under the existing framework, but are examined separately by the IA together with the insurer concerned. In the current regime, while the ICO stipulates a minimum solvency requirement of 100%, the IA adopts a solvency ratio benchmark of 200% for general insurers (including Target). In recent years, it has been recognized globally that the capital adequacy framework should take into account different risk factors of different insurers, and be conducive to enhance the corporate governance, enterprise risk management and public disclosure practices of insurers. The International Association of Insurance Supervisors has issued new Insurance Core Principles in relation to risk-based capital ("RBC") requirements in late 2011. The IA has reviewed the existing regulatory capital framework for insurance business in Hong Kong and proposed to revamp it towards an RBC regime.

Accordingly, the IA plans to move towards an RBC regime, establishing a clear and consistent valuation standard (including explicit best estimates of technical provisions and risk margins) and risk-sensitive capital requirements, supported by continued enhancement of corporate governance, enterprise risk management and public disclosure. The IA commissioned a consultancy study in 2012-2013 for developing an RBC framework that is appropriate for Hong Kong's insurance industry.

Under the RBC regime, it is proposed that the protection of policy holders will be strengthened by relating capital adequacy to the risk exposure of the insurer. An insurer exposed to higher risks is required to hold a higher amount of capital. Apart from capital adequacy, a solvency regime also includes other qualitative and technical requirements, in particular on corporate governance and enterprise risk management. Key elements of the regime will cover the nature of groups to be subject to group-wide supervision, as well as prudential, corporate governance, enterprise risk management and disclosure requirements at the group level. These proposed developments will also enable a more structured approach for macro-prudential surveillance, enhancing the supervisory capacity to identify, assess and mitigate vulnerabilities. The move towards developing an RBC framework does not necessarily imply a need to increase or decrease capital for individual insurers. The framework seeks to, consistent with international practice, make capital requirements more sensitive to the level of risk that individual insurers and insurance groups are bearing. The three-month consultation on the proposed RBC framework for the insurance industry of Hong Kong ended on 15 December 2014 and implementation of the RBC regime may not take place by 2018.

It is intended by the IA that the RBC regime will be developed in the following phases:

- Phase I has commenced and it involved development of the framework and key approaches.

- Phase II will involve development of detailed rules. Quantitative impact study should be conducted for different types of insurers to ensure that the new regime is viable and practicable, and that it should not bring about instability to the insurance industry. Phase II will begin in 2015 and it will be followed by another consultation exercise.

- Phase III will involve amendment of legislation. At least 2 to 3 years will be needed to complete all the preparatory tasks including public consultations.

- Phase IV will be the implementation phase. The new RBC regime should be rolled out in phases with a sufficiently long run-in period, so that insurers will have adequate time to understand the requirements thoroughly, and be able to achieve full compliance incrementally.