

A New Era of Insurance Regulation in Hong Kong

On 10 July 2015, the *Insurance Companies (Amendment) Ordinance 2015* was enacted bringing Hong Kong into a new era of insurance regulation. The Amendment Ordinance establishes a new independent insurance authority and makes some radical changes to insurance regulation in Hong Kong.

The *Insurance Companies (Amendment) Ordinance 2015* (“**Amendment Ordinance**”) makes some radical changes to the *Insurance Companies Ordinance Cap. 41* (“**ICO**”). Most fundamentally, the Amendment Ordinance establishes a new insurance authority which is independent functionally and financially from the Government. This article summarises the key changes brought by the Amendment Ordinance to the ICO.

Independent Insurance Authority (“**IIA**”) – The New Kid on the Block

Currently, the insurance regulator in Hong Kong is the Commissioner of Insurance, supported by the Office of the Commissioner of Insurance (“**OCI**”), which is a government department.

The IIA will replace the OCI. The IIA is independent from the Government and will have a corporate structure with a Chief Executive Officer and not less than six other directors. At least two non-executive directors must have knowledge and experience in the insurance industry and the other directors must have knowledge and experience in other areas such as actuarial science, accounting, law and consumer affairs.

The IIA is financially independent from the Government. Initially, the Government will provide a lump sum of HK\$500 million. Going forward, the IIA will be funded by levies of 1 percent on insurance premiums, but capped at HK\$100 for life insurance

policies and HK\$500 for non-life insurance policies (to be implemented in an incremental approach). The IIA will also be funded by various licence and user fees.

The introduction of the IIA is long overdue as it brings Hong Kong in line with other jurisdictions that have had independent insurance regulators. The financial services sector in Hong Kong has been subject of regulation by the Hong Kong Monetary Authority (“**HKMA**”) and Securities and Futures Commission (“**SFC**”) for some time now and it is only appropriate for the insurance industry to be regulated by an independent statutory body as well. The IIA will join the ranks of the HKMA and SFC as the new regulator for the insurance industry.

Enforcement Powers – A Regulator with Teeth

One of the key changes with the new IIA is enhanced investigatory powers.

The IIA is vested with similar investigatory powers as the SFC and the Mandatory Provident Fund Scheme Authority. Under the new Part VA and amended Part X of the ICO, the IIA has powers to:

- a. Enter into the premises of an insurer or insurance intermediary and inspect and take copies of records and documents without warrant;
- b. Require a person to produce a record or document; and
- c. Require a person to verify his explanation or answer by statutory declaration.

The new Section 41K of the ICO also empowers a Magistrate to issue a warrant authorising a person (such as an investigator appointed by the IIA) to enter premises and to search for, seize and remove documents or records.

If a person fails to comply with the requirements of the IIA, he commits an offence and is liable to penalties upon conviction (the new Sections 41G and 64ZZL of ICO). However, a person's responses or statements made during an investigation are not admissible as evidence in criminal proceedings (other than criminal proceedings under the new Sections 41G and 64ZZL).

Regulation of Insurance Intermediaries – A Whole New Ball Game

Another fundamental change relates to the way in which insurance intermediaries are regulated.

Currently, insurance agents in Hong Kong are regulated by the Insurance Agents Registration Board, set up by the Hong Kong Federation of Insurers. Generally, insurance brokers in Hong Kong belong to two self-regulatory bodies, being the Hong Kong Confederation of Insurance Brokers or the Professional Insurance Brokers Association. The IIA will replace the three self-regulatory bodies and directly supervise all insurance intermediaries in Hong Kong.

Under the new regime, regulation of insurance intermediaries is “activity focused”. The new Section 3A of the ICO defines “*regulated activities*” to include negotiation or arranging contract of insurance, inviting or inducing a person to enter into a contract of insurance, giving advice on insurance and sale and after-sale service in relation to insurance. It is an offence for a person to carry out, or hold out as carrying out, a “*regulated activity*” without licence.

The definition of “*regulated activity*” is very broad. The new Section 123 clarifies that “*regulated activities*” does not apply to legal advisers, accountants, actuaries, loss adjusters etc. Further, the new Section 123(4) clarifies that an employee of an authorised insurer does not need to be licensed if he carried on a “*regulated activity*” that only involves the discharge of underwriting or claims handling duties for an insurer.

Under the new regime, there will be five different types of licences for insurance intermediaries. For insurance agents, they may be licensed as an insurance agency (business entity), insurance agent (individual), or technical representative (“TR”). An insurance broker may be licensed as a broker company (business entity) or a licensed TR (individual).

“Best Interest” Requirement on Licensed Insurance Intermediaries

The new Division four of the ICO sets out conduct requirements for insurance intermediaries. For instance, an insurance intermediary is required to “*act honestly, fairly, in the best interests of the policy holder*”. This is not a problem with insurance brokers, who are the agents of the customer/policy holder. However, an insurance agent is the agent of the insurer and may create a conflict of interest between the customer and the insurer. The role of an insurance agent is therefore fundamentally different from that of an insurance broker. The IIA will issue a code of conduct to further elaborate the conduct requirements of insurance intermediaries and this will hopefully clarify the different roles of insurance agent and insurance brokers with respect to the “*best interest*” requirement.

In the event an insurance intermediary breaches a conduct requirement, this will result in disciplinary action but does not *by itself* render any person liable to any judicial proceedings (the new Section 93 of ICO). The new Section 93 however does not affect a person's liability in common law or whether a person is liable for breach of other provisions of the ICO.

The IIA may also make rules requiring insurance intermediaries to comply with practice and standards such as requiring insurance intermediaries to disclose commission or advantage received (the new Section 94(2)(f) of ICO).

Concluding Remarks

The amendments to the ICO have not come into effect and are expected to take effect in three stages. The goal is to set up a Provisional IIA by end of 2015. The IIA will take over regulation of insurers first and then regulation of insurance intermediaries. The whole process is anticipated to take about two to three years.

Some of the provisions of the amended ICO are not without controversy. The definition of “*regulated activity*” is very broad and has already been the subject of much comment during the consultation process. This is not surprising as law drafters typically define regulated activities in broad terms to cast a wide regulatory net. As the IIA implements the statutory requirements and provides guidance, the scope of “*regulated activities*” will hopefully become clearer.

The new regulatory regime for insurance intermediaries has also attracted much attention, particularly the requirement for insurance agents to act in the best interests of the customer. There are concerns that the insurance agent could face conflicts of interest between the customer and the insurer, who is its principal. These issues will hopefully be clarified in the code of conduct for insurance intermediaries to be issued by the IIA.

The amendments to the ICO will bring about a new era of insurance regulation in Hong Kong. The new IIA's aim and focus is to promote confidence in the insurance industry and enhance customer protection. The new IIA will have stronger and wider investigatory powers, as well as direct regulation of the conduct of insurance intermediaries. All insurance industry stakeholders should carefully review the amended ICO and ensure that they have taken all necessary steps to comply with the requirements under the new regime.

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