

INDEPENDENT INSURANCE AUTHORITY COMMENCES REGULATION OF INSURERS WITH ENHANCED POWERS

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Legal Briefings

With effect from yesterday (26 June 2017), the independent Insurance Authority (**IA**) assumed its regulatory responsibilities and replaced the Office of the Commissioner of Insurance (**OCI**) in regulating insurers. The IA will be a much more powerful regulator than its predecessor, with enhanced authorisation and supervisory powers, as well as inspection, investigation and disciplinary powers over insurers.

The IA was established on 7 December 2015 as part of the enhancement of Hong Kong's insurance regulatory regime, by putting in place a regulator which is financially and operationally independent of the government and the industry in compliance with international standards. The regulation of insurers, which has just commenced, is the first phase in the IA's assumption of regulatory responsibilities. It is anticipated that the second phase will occur in around two years' time, when the IA takes over the regulation of insurance intermediaries (ie, agents and brokers) from the three self-regulatory organisations.¹

The IA's new website has been launched and can be accessed here - www.ia.org.hk.

THE IA

Mr John Leung Chi-yan (the former Commissioner of Insurance) has recently been appointed as the IA's Chief Executive Officer for its first year of operation. His role is to ensure a smooth transition into the new regulatory regime, pending the appointment of a suitable candidate for the position.

A brief overview of the IA's senior management, governance structure and means of funding is set out in the [attached](#).

ENHANCED POWERS OVER INSURERS

The IA's powers over insurers are much broader than that available to its predecessor, the OCI, and are largely modelled on the regime for regulating licensed corporations by the Securities and Futures Commission (**SFC**).

AUTHORISATION AND SUPERVISION

The amended *Insurance Ordinance* provides for increased scrutiny and supervision over key persons appointed by authorised insurers, such as certain controllers and directors, and the newly introduced concept of "key persons in control functions". This concept captures individuals who are responsible for one or more of the "control functions" of authorised insurers (except captive insurers), including intermediary management, risk management, financial control, compliance, internal audit and actuarial matters. This is consistent with the trend in Hong Kong (as well as globally) for financial regulators to put in place clear mechanisms for identifying individuals who play a key role in managing a financial institution and to hold them accountable.

The above key persons must be fit and proper to be appointed and to remain appointed. In this regard, the existing OCI guidance note on fit and proper criteria (GN 4) has recently been updated to incorporate the new provisions under the amended *Insurance Ordinance* on factors which the IA must have regard to when determining whether a person is fit and proper, and to incorporate the revised Insurance Core Principle 5 on Suitability of Persons promulgated by the International Association of Insurance Supervisors (see core principles [here](#)).

INSPECTION, INVESTIGATION, DISCIPLINARY AND DISCIPLINARY POWERS

The IA will now have powers to (among others):

- conduct compliance inspections on authorised insurers;
- conduct investigations where (amongst other things) it has reasonable cause to believe that there may have been a breach of the *Insurance Ordinance*, fraud or misfeasance, or it has reason to enquire if an authorised insurer is guilty of misconduct or is no longer fit and proper – under which it may require an authorised insurer (or any other person who may be of assistance to the investigation) to:

- produce documents or records;
- provide explanations or further particulars in respect of documents or records;
- provide answers to written questions;
- attend interviews; and/or
- provide all other reasonable assistance in connection with the investigation;
- apply to a Magistrate for a search warrant to enter premises and to search for, seize and remove a record or document where specified grounds exist;
- impose disciplinary sanctions on an authorised insurer for misconduct, such as:
 - issuing a reprimand;
 - revoking or suspending an authorisation for a specified period;
 - prohibiting an insurer from applying to be authorised for a specified period;
 - imposing a fine on an authorised insurer up to the greater of HK\$10 million or three times the profit gained or loss avoided as a result of the misconduct (a new guideline on considerations in exercising the power to impose pecuniary penalties on authorised insurers has recently been issued ([GL 18](#)));
- prosecute in its own name offences under the Insurance Ordinance which are triable summarily.

Further details in relation to the IA's powers above and the insurance regulatory reform in general are set out in our *Guide to the Independent Insurance Authority* published in December 2015. If you do not already have a copy, please do not hesitate to reach out to your usual contacts or email asia.publications@hsf.com.

Authorised insurers should take this opportunity (if they have not already done so) to:

- review their existing internal controls and policies and ensure that they are sufficient, properly in place and are being complied with;
- ensure that there are proper record keeping and audit trails;
- ensure that there are in place processes for responding to inspections and investigations by the IA; and
- provide training to staff on internal policies, key regulatory requirements as well as how to respond to inspections and investigations by the IA.

Herbert Smith Freehills would be very happy to assist with the above reviews. If this would be of interest, please do not hesitate to get in touch with one of your usual contacts.

TRANSITION OF CODES AND GUIDELINES

The existing guidance notes and guidelines promulgated by the OCI will continue to have effect as if they were issued by the IA, including the OCI's guidance notes GN 1 to 17. Apart from GN 4 on fit and proper criteria (which has been updated as described above), only technical amendments have been made to the guidance notes, for example, to update references to the law and to change the issuing authority from the OCI to the IA.

To align with the terminology in the new *Insurance Ordinance*, all OCI guidance notes will be renamed as guidelines, and the abbreviation will be amended from "GN" to "GL".

As mentioned above, the IA has issued a new guideline (GL 18) setting out its considerations in exercising the power to impose pecuniary penalties on authorised insurers.

Updated guidelines GL 1 to 18 are now in effect - they were gazetted last Friday (23 June 2017) and can be accessed [here](#).

In addition, the IA has agreed that the codes and guidelines promulgated by the Hong Kong Federation of Insurers (**HKFI**) (which set out the standards and conduct requirements for authorised insurers when carrying on insurance business) will continue to have effect and be administered by the HKFI under the existing self-regulatory regime.

WAY FORWARD

Although it is too early to tell how the IA may exercise its newly conferred powers, it is likely that we will see a more structured approach in the regulation of insurers, including regular inspections. Given that the new regulatory regime is modelled on the SFC's regime, the IA will likely make reference to the SFC's approach in exercising its regulatory functions.

In terms of the issues which the IA will focus on in the near future, the IA has indicated that various initiatives, including the development of a risk-based capital regime and the introduction of a policy holders' protection scheme, are in the pipeline.

In addition, the IA held its first meeting with the Future Task Force of the Insurance Industry (**FTF**) in December 2016. The FTF is chaired by Dr Moses Cheng, the Chairman of the IA, and comprises experts and professionals from the insurance industry and the academia. It is stated that its major goals are to identify socio-economic and demographic factors that will shape the insurance industry in the future, and to draw up recommendations to promote the sustainable development of the insurance industry and to protect the interests of policy holders.

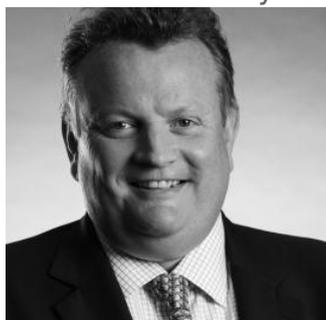
Currently there are three working groups under the FTF to review the following matters which have been identified as important:

- fintech;
- risk-based capital regime; and
- image building for the insurance industry and enhancing the public's understanding of insurance.

1. The self-regulatory organisations are the Insurance Agents Registration Board established under The Hong Kong Federation of Insurers, The Hong Kong Confederation of Insurance Brokers and the Professional Insurance Brokers Association.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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