

11 October 2010

Division 3, Financial Services Branch
Financial Services and the Treasury Bureau
18/F, Tower I, Admiralty Centre
18 Harcourt Road
Hong Kong



ACTUARIAL SOCIETY
of
H O N G K O N G
香 港 精 算 學 會

Dear Sir/Madam,

Actuarial Society of Hong Kong's submission for the Consultation Paper on the Proposed Establishment of an Independent Insurance Authority

Thank you for the opportunity to provide comments for the proposed establishment of an independent Insurance Authority. The Actuarial Society of Hong Kong ("ASHK") and its members have had involvement working with the OCI on the development of insurance standards and guidance notes over many years which has served both the insurance industry and the public. ASHK is keen to continue this contribution into the future.

ASHK supports the government initiative to establish an independent Insurance Authority (IA) and would like to provide the following comments to the Consultation Questions.

Consultation Questions 1 & 2 – Principles for establishment of an independent IA

In general, ASHK supports the establishment of an independent IA along the principles set out in paragraph 2.6.

As a prudential regulator and supervisor of the insurance industry, the effectiveness of the independent IA will depend on a solid prudential framework, including prudential standards, prudential guidance notes and prudential rules. Insurance regulators around the world, including many in Asia, have been highly active in introducing new standards to their markets in recent years, and we expect this trend to continue in particular as the approach to solvency reserving evolves and new product types emerge. We draw attention to the many new standards which have been introduced recently in the United States, Europe, China, Taiwan, Malaysia and elsewhere in Asia.

In our view the IA will need to devote significant time and resources to setting, implementing and monitoring new regulatory standards over the coming years. Many of these standards are expected to be actuarial standards. A comparison with other countries has indicated that the responsibility for the development of actuarial standards does vary from one jurisdiction to another.

For example, in the UK, the Board of Actuarial Standards is part of the Financial Reporting Council, which is the UK regulator responsible for corporate governance and promoting investment. In Australia, from 1995 to 2008, the Life Insurance Actuarial Standards Board

was an independent body which operated under the Life Insurance Act. This approach gave the prudential supervisor, APRA, time to develop and strengthen its actuarial function so that effective from January 2008, the role of setting actuarial standards was assumed by APRA. In the United States, the Actuarial Standards Board is an independent entity supported by the American Academy of Actuaries. Similarly, in Canada, the Actuarial Standards Board is supported by the Canadian Institute of Actuaries.

We believe that the efficient development of actuarial standards and guidance notes may be achieved by having an independent Actuarial Standards Board, which has statutory backing, with the sole responsibility of developing standards, to respond effectively to changing market needs and the changing environment.

We therefore propose the setup of an Actuarial Standards Board in conjunction with the establishment of the independent IA. Unlike the HKICPA, which is a statutory recognized body, the ASHK does not have such authority to issue actuarial standards which have statutory backing. The Actuarial Standards Board will add considerable strength to the development of the prudential standards and guidance notes and also provides an arrangement to access required levels of technical expertise over sustained periods of time.

In addition, the independent IA may also consider strengthening its actuarial function (e.g. an organizational structure which includes the Office of the Actuary, or such similar office) since this is expected to be an integral part of the supervision of insurance industry as it becomes more complex with new solvency and capital regulations.

The ASHK would welcome the opportunity to discuss these proposals in further detail with the Financial Services Branch.

Consultation Questions 3 & 4 – Role of the IA

ASHK supports the expanded role of the independent IA to include the supervision of insurance intermediaries and protection of policyholders by effective prudential and conduct regulation. We believe that this is in the interest of the long-term viability of the insurance industry.

As actuaries, we have a responsibility for the protection of policyholders and their reasonable expectations. We would welcome the opportunity to work with the independent IA on this for the healthy and sustainable market development of the insurance industry.

With regards to Question 4, on the role of enhancing the competitiveness of the insurance industry, we believe that this is in conflict with the need for the independent IA to ensure security of the insurance industry, and are in favour of removing the words “and enhance the competitiveness of the insurance industry” from paragraph 3.4. We feel that the IA should see itself as an integral part of the insurance community in Hong Kong and should act in a manner which contributes to the long-term development of insurance in Hong Kong and of Hong Kong insurers and which is aligned with the long-term needs of the industry’s policyholders and the community in which they exist. There may be occasions when this is not consistent with the short-term competitiveness of the insurers.

Consultation Questions 6 & 7 – Supervision of intermediaries

As mentioned in our response to Question 3, we support the direct supervision of insurance intermediaries by the independent IA.

In the case of the sale of insurance products through banks, we believe that the licensing requirements and supervision should be consistent with the regulations which apply to other insurance intermediaries. In the event that there are inconsistencies, there is the potential for confusion, lack of clarity, or even regulatory arbitrage which favours one distribution channel over another. In particular, we are mindful of recent events concerning the distribution of certain financial products in Hong Kong and the potential for inconsistency when there is a lack of clarity of roles. We also feel that the regulation of insurance business requires specialist knowledge and specific expertise. The combination of these points suggests that the sale of insurance business would be more consistently and therefore more effectively regulated by a single body in the form of the IA, and we would wish to see much more detailed information regarding the interaction between the IA and the MA before supporting the proposals set out in paragraph 5.14.

The above argument in favour of consistency also supports our position with regard to Question 6.

Consultation Question 8 – Structure of the independent IA

As mentioned in our response to Questions 1 & 2, we believe that the structure of an independent Standards Board can provide strength for the development of a solid prudential framework, including prudential standards, prudential guidance notes and prudential rules, which responds effectively to changing market needs and changing environment.

Consultation Questions 10 & 11 – Funding mechanism

The proposed funding mechanism seems to focus on the insurance manufacturer. We propose that funding should take into account all activities involved in the insurance value chain, including distribution, administration and funds management in order to arrive at a funding mechanism which is fair for all insurers.

We note that few details behind the funding calculations are shown, and would be interested to see how the cost benchmarks against other insurance regulators in various jurisdictions. Of particular interest to ASHK is the actuarial function.

Related to this, we feel that it is likely that the workload for insurance regulators around the world will increase significantly in the near future, and that many additional staff with deep industry experience will be required. An example of high relevance to actuaries is Solvency II, which is currently being implemented by European insurers and regulators. This is a highly complex and detailed undertaking for regulatory authorities, both in its initial implementation and on an ongoing basis thereafter. From public comments made by the IA in recent years, we have inferred that an approach similar to Solvency II will be

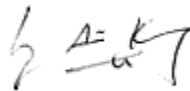
considered for application in Hong Kong in the future. If this is the case, it would be of great interest to benchmark the effort, resource requirements and cost incurred by European insurance regulators in estimating the impact for the IA. Relating to this, we would also like to note that the significant impact of new regulations such as Solvency II is one of the key reasons why ASHK is supportive of the proposals for the IA to become an independent body.

Again, thank you for the opportunity to comment on the Consultation Paper. We look forward to working with the new independent IA. Please do not hesitate to contact ASHK staff member, Pat Kum at patkum@netvigator.com, if you wish to discuss any of the above comments.

Yours sincerely,



Simon Walpole
President



Sim Ng
Secretary & Chairman of Publications Committee