



## CONSULTATION PAPER ON DRAFT INSURANCE (GROUP CAPITAL) RULES

### SUBMISSIONS

1. The Insurance Authority released a *Consultation Paper on the Draft Insurance (Group Capital) Rules* (“Consultation Paper”) on 19 August 2020 for views and comments.
2. The Law Society of Hong Kong makes the following submissions on the consultation questions posed, with specific comments on the legal and/or drafting aspects of the *Draft Insurance (Group Capital) Rules* set out in a **Schedule**. Unless otherwise stated, the Law Society adopts the definitions set out in the Consultation Paper.
3. As initial comment, we note that in the Consultation Paper, it is stated that “*The Group Capital Rules will apply to designated insurance holding companies, being holding companies (incorporated in Hong Kong) of insurance groups, in relation to which the IA is performing the role of group supervisor in accordance with the relevant international standards including the ICP and ComFrame promulgated by the IAIS.*” We believe it is not entirely clear if the Group Capital Rules would apply to a regional holding company, incorporated in Hong Kong, which is part of a larger group, whose parent company is in some other jurisdiction. Our understanding is that ComFrame may also not be clear on this issue.

**Question 1:**

**Is the proposed definition of “regulated entity” sufficiently broad to cover all types of regulated entities in an insurance group?**

**Law Society's Response:**

4. Consideration should be given to include other entities such as:
  - (i) entities which provide a payment or stored-value service; and/or
  - (ii) entities which provide services related to the issuance or storage of digital tokens or crypto-currency; and/or
  - (iii) entities related to such other businesses or entities that may be designated by the Authority from time to time.

**Question 2:**

**Having regard to the intention in paragraphs 29 and 30 in the consultation paper, is there a need to specify the definitions and adjustments that are applicable to "IFRS shareholder equity less goodwill and any other intangible assets" in the Group Capital Rules or guidelines?**

**Law Society's Response:**

5. No comment.

**Question 3:**

**Are there other arrangements or holding structures that may require adjustments to be made to eliminate double-counting?**

**Law Society's Response:**

6. We consider that draft Rules 7(1) and (2) appear to work properly in all cases where the regulations of the jurisdiction of the first supervised group member (FSGM) would require the FSGM to hold at least the required capital, in respect of the second supervised group member (SSGM), as required by the regulator of the SSGM. Query whether this is always the case.
7. Draft Rule 7(3) does not seem to always work appropriately where the jurisdiction in which the entity is incorporated or formed has lower capital requirements than the regulations of some other jurisdiction in which that entity does business. This concern is not merely hypothetical; for example it could be the situation in respect of many insurers that operate in Hong Kong but which are incorporated in Bermuda (in the scenario that the Bermuda capital requirements are lower than those under the Hong Kong rules).

**Question 4:**

**Do you agree with the proposed tiering approach for non-regulated entities?**

**Law Society's Response:**

8. No comment.

**Question 5:**

**Do you agree with the criteria for defining a “material supervised group member” in Rule 10(6) of the Group Capital Rules?**

**Law Society's Response:**

9. No comment.

10. By way of concluding remark, we note that the proposed subsidiary legislation will be introduced into the Legislative Council in the 2020-2021 legislative session. We ask that we should be engaged in reviewing the draft subsidiary legislation, when available.

**The Law Society of Hong Kong**  
**29 September 2020**

## SCHEDULE

### Specific comments on the legal and/or drafting aspects of the *Draft Insurance (Group Capital) Rules*:

(1) Rule 2 – Interpretation

**“group minimum capital requirement** – see rule 4;” -

We suggested that this term be defined as **“group minimum capital requirement** – the amount determined under Rule 4;”

**“group prescribed capital requirement** – see rule 5;” –

We suggested that this term be defined as **“group prescribed capital requirement** – the amount determined under Rule 5;”

**“laws relating to regulatory capital”** –

Query whether “and” at the end of paragraph (b) should be “and/or”

**“regulated entity”** –

Please see above our Response to Consultation Question 1.

**“tier 1 group capital** – see subrule (1) of rule 8;” –

We suggested that this term be defined as **“tier 1 group capital** – the amount determined under subrule(1) of rule 8;”

**“tier 2 group capital** – see subrule (3) of rule 8;” –

We suggested that this term be defined as **“tier 2 group capital** – the amount determined under subrule (3) of rule 8”

(2) Rule 4(3) – Calculation of the Group Minimum Capital Requirement

Please clarify what is the meaning of “involved supervisor”. (*see* 2<sup>nd</sup> line of Rule 4(3))

(3) Rule 4(4)

We consider that “or another supervised group member in the same supervised group” can, and perhaps should, be deleted, because:

- a. “directly or indirectly” is already stated, in respect of the designated holding company; and
- b. it is possible that the holding by such other company could be less than the total indirect holding by the holding company.

The following amendments to Rule 4(4) are therefore suggested:

“If the percentage shareholding in a supervised group member, held directly or indirectly, by the designated insurance holding company is less than 100%, the percentage of such shareholding, multiplied by the minimum capital requirement applicable to the supervised group member, is the amount that must be included in the group minimum capital requirement for the purpose of subrule (1).”

(4) Rule 5(2)(a) – Calculation of the Group Prescribed Capital Requirement

We suggest that “would not give rise to” be changed to “would not give rise to the possibility of” (*see* 6<sup>th</sup> line of Rule 5(2)(a)).

(5) Rule 5(3)

It is unclear what is the meaning of “involved supervisor”. (*see* 2<sup>nd</sup> line of Rule 5(3)).

(6) Rule 5(4)

For the same reasons as under Rule (4)(4), the following amendments to Rule 5(4) are suggested:

“If the percentage shareholding in a supervised group member, held directly or indirectly, by the designated insurance holding company is less than 100%, the percentage of such shareholding multiplied by prescribed capital requirement applicable to the supervised group member, is the amount that must be included in the group prescribed capital requirement for the purposes of subrule (1).”

(7) Rule 6(3)(a) – Eligible Group Capital Resources

We suggest that a comma be inserted after “eligible capital resources” (*see* 1<sup>st</sup> line of Rule 6(3)(a)).

(8) Rule 6(3)(b)

We suggest that a comma be inserted after “eligible capital resources” (*see* 1<sup>st</sup> line of Rule 6(3)(b)).

(9) Rule 6(3)(b)(i)

We suggest that “the” before “recognized international” be deleted (*see* 2<sup>nd</sup> line of Rule 6(3)(b)(i)).

(10) Rule 6(3)(b)(ii)  
We suggest that “satisfy the criteria of Schedule 1 and 2” be replaced by “meet the requirements of Rule 8 applicable to non-regulated entities”.

(11) Rule 6(4)  
We suggest that “or another supervised group member in the same supervised group” be deleted (see 2<sup>nd</sup> and 3<sup>rd</sup> lines of Rule 6(4))

(12) Rule 7 – Treatment of double-counting  
Please see above our response to Consultation Question No. 3.

(13) Rule 8(2) – Tiering of Eligible Group Capital  
We suggest that the wordings be replaced by:

“If the amount of eligible capital resources that only satisfy the criteria for tier 1 limited group capital in Schedule 1 and that are eligible capital resources of supervised group members that are non-regulated entities would, but for the application of this sub-rule 8(2), exceed 10% of the group minimum capital requirement of the supervised group, then:

- (a) such amount shall be restricted to 10% of the tier 1 capital of the supervised group; and
- (b) the amount so calculated, in excess of the amount under Rule 8(2)(a), shall be the amount referred to in sub-Rule 8(3)(c).”

(14) Rule 8(3)  
We suggest to delete Rule 8(3)(b)(i), and collapse Rule 8(3)(b)(ii) into Rule 8(3)(b); and add a new Rule 8(3)(c):

“(c) the amount referred to in sub-Rule 8(2)(b).”

The reasons for these proposed changes in Rules 8(2) and (3) are that, existing draft Rule 8(3)(b)(i) creates uncertainty, because it refers to an excess over 10% of tier 1 capital, but does so in a rule that refers to an individual supervised group member’s capital calculation – but this would leave uncertainty as to which such group member’s tier 1/tier 2 capital contribution are changed by the rule. While this may be acceptable, it seems better to be consistent throughout the rule, such that the change (in respect of the amount above 10%) only affects the calculation at the group level.

- (15) Rule 8(4)  
In the definition of “**tiering approach to regulatory capital**”, please consider changing “based on the following” to “based on all or some of the following” (see 4<sup>th</sup> line of this definition)

The reason for this proposed change is that each regulatory regime’s criteria may be slightly different. Also, please consider including a discretion for the Authority to make a determination as to what is tier 1 or tier 2 capital, if the criteria applied in a particular jurisdiction do not closely match those indicated here.

In the definition of “**highest tier regulatory capital**”, based on the same reasons as above, please also consider changing “in terms of” to “in terms of all or some of the following” (see 5<sup>th</sup> line of this definition).

- (16) Rule 9 – Transitional arrangements in relation to Group Capital  
We have no specific objection to this rule, but it is not clear as to exactly what type of instrument it is intended to cover. Please clarify.

- (17) Rule 10(1)(i) – Submission of reports on group capital adequacy to the Authority  
It is not clear what could constitute a “material change” – is it just a significant change in a calculated number? If so, what is the necessary extent of the change? It seems that more guidance should be provided.

- (18) Rule 10(4)  
It is unclear whether the date in Rule 10(4)(b) is the only deadline, or whether a copy should be submitted earlier, even if not in electronic format.

- (19) Rule 10(6)(a)(i)  
We suggest that “supervised group member” be changed to “the supervised group member” ; and a comma after “member” be inserted (see 1<sup>st</sup> line).

- (20) Rule 10 (6)(a)(ii)  
We suggest that a comma after “member” be inserted (see 1<sup>st</sup> line).

- (21) Rule 10(6)(a)(iii)  
We suggest that a comma after “member” be inserted (see 1<sup>st</sup> line).

- (22) Rule 10 (6)(a)(iv)  
We suggest that a comma after “member” be inserted (see 1<sup>st</sup> line).

- (23) Rule 11(1) – Report to the Authority of certain events  
We suggest that “the directors” be changed to “the board” or “any of the directors” (depending which meaning is intended). Please also consider requiring the notification within a specific period of time, not just “forthwith” – otherwise, there is no particular deadline applicable.
- (24) Rule 11(1)(a)  
We suggest that the “or” at the end be removed.
- (25) Rule 11(1)(b)  
We suggest that a comma after “knowing” be inserted; and a comma at the end be inserted.
- (26) Rule 11(3)(c)  
Please consider also including: being charged or indicted of a criminal offence.
- (27) Rule 11(3)(d)  
It is noted that this seems to overlap the requirement under Rule 11(1)(a).
- (28) Rule 11(3)(e)  
We suggest that “to” be changed to “on” (*see* 1<sup>st</sup> line).
- We consider that this paragraph is overly broad. For example, if a company is significantly capitalised above the requirements, would this paragraph be triggered if an event led to a significant drop in capitalisation, even though the group remained capitalised significantly above the minimum requirements?
- (29) Rule 12 – Public disclosure in relation to group capital  
We suggest that “subrule (1)” be changed to “subrule (1) or (2)”.
- (30) Schedule 1 – 1.(b) Tier 1 group capital for the purposes of subrule 8(1)(b)  
Are the words, “included in tier 1 group capital” circular, given we are defining here what is tier 1 group capital?
- (31) Schedule 1 – 2. Tier 1 limited group capital for the purposes of subrule 8(2)  
Query whether the reference to “subrule 8(2)” in the title, and the first line of 2(1), is correct.