
CHAMBERS GLOBAL PRACTICE GUIDES

Insurance & Reinsurance 2023

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Hong Kong SAR, China: Law & Practice

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Hong Kong SAR, China: Trends & Developments

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HONG KONG SAR, CHINA

Law and Practice

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1. Basis of Insurance and Reinsurance Law

1.1 Sources of Insurance and Reinsurance Law

The Insurance Ordinance (Cap 41 of the Laws of Hong Kong) is the principal source of law governing insurance and reinsurance in Hong Kong. It is supplemented by subordinate legislation covering matters such as the determination of capital requirements and the payment of fees and levies. While the codes and guidelines issued by the Hong Kong Insurance Authority (IA) are not legally binding as such, they contain many of the key regulatory obligations applicable to insurers and insurance intermediaries and are therefore of great importance in practice.

Hong Kong is a common law jurisdiction, so precedent judicial decisions are relevant to insurance law, in particular in relation to insurance contract law and claims. The law in relation to portfolio transfers is also to a large extent determined by judicial precedent.

2. Regulation of Insurance and Reinsurance

2.1 Insurance and Reinsurance Regulatory Bodies and Legislative Guidance

(Re)insurers and (re)insurance intermediaries in Hong Kong are regulated by the IA, which has issued detailed guidelines and codes governing the key aspects of regulation not exhaustively dealt with by the Insurance Ordinance and subordinate legislation. The guidelines are supplemented by interpretation notes, explanatory notes and other regulatory circulars.

The writing of unit-linked business, known locally as “investment-linked assurance schemes”, is to some extent also regulated by the Hong Kong Securities and Futures Commission (SFC), which has issued a code governing key aspects of such schemes.

While there is currently no cross-border legislation, there is a level of mutual recognition of prudential supervision of insurers between Hong Kong and Mainland China, and the scope of possible cross-border schemes permitting the sale of insurance products across the Greater Bay Area (an area including Hong Kong, Macau, Shenzhen and a number of other cities in Guangdong province) is currently under discussion.

2.2 The Writing of Insurance and Reinsurance

Subject to narrow exemptions, anyone carrying on insurance or reinsurance business in Hong Kong must be authorised by the IA under the Insurance Ordinance. Such business can be carried on either through a Hong Kong-incorporated company or through a branch of an overseas (re)insurer subject to regulation in its home jurisdiction. The exemption applicable to offshore reinsurers conducting reinsurance on a non-admitted basis is considered in **3.1 Overseas-Based Insurers or Reinsurers**.

In order to become authorised, a company must meet certain key criteria, including having sufficient regulatory capital, “fit and proper” directors, controllers and other key persons, adequate reinsurance (or retrocession) arrangements and a local office with a CEO and other relevant staff.

In terms of shareholder controllers, the IA will focus on their financial resources and ability to finance the insurer’s business operations and

future capital needs, as well as their industry experience and reputation.

2.3 The Taxation of Premium

An insurance levy payable by policyholders has been applied to premium payments for new and in-force policies since 1 January 2018, subject to certain exceptions. The levy is collected by the relevant insurers and ultimately paid to the IA. The levy rate starts at 0.04% of the insurance premium per policy year and increases gradually to 0.1%. The amount of the levy imposed on each policy is subject to a cap.

3. Overseas Firms Doing Business in the Jurisdiction

3.1 Overseas-Based Insurers or Reinsurers

Overseas-based direct insurers are not permitted to conduct insurance business in Hong Kong without authorisation.

Overseas insurers may accept business from Hong Kong on a “reverse solicitation” basis so long as they do not conduct insurance or solicitation activities in Hong Kong and do not hold themselves out as insurers in Hong Kong. In practice, the scope of such activity is very limited and typically relates to specialist policies written at the initiative of Hong Kong-based policyholders or their brokers.

Reinsurers are permitted to conduct reinsurance business in Hong Kong without authorisation if they do not have a local presence, do not act through an agent in Hong Kong and do not carry out any regulated intermediary activities.

There is currently no passporting or equivalence regime that would allow overseas insurers

or reinsurers to operate in Hong Kong without going through the usual authorisation process.

3.2 Fronting

Fronting is not permitted in Hong Kong and the general expectation is that each insurer retains a minimum share of the business it writes.

4. Transaction Activity

4.1 M&A Activities Relating to Insurance Companies

Hong Kong has been an active M&A market with regard to insurance companies in recent years. This has largely been driven on the one hand by the desire of Chinese and overseas players to enter what is viewed as a lucrative market with potential for future growth into Mainland China, and on the other hand by owners of small and medium-sized insurers seeking to exit a highly competitive and increasingly regulated market in which it is difficult to remain profitable without scale, especially where Hong Kong is not core to their strategy. The impending introduction of a risk-based capital regime, the reduced premium growth in life insurance due to COVID-19 and political uncertainty in Hong Kong has accelerated this trend.

Hong Kong-based insurance groups continue to invest in Mainland China as well as the other growth markets in the region, in particular South-East Asia. Acquisitions linked to bancassurance or other distribution arrangements have been particularly popular.

5. Distribution

5.1 Distribution of Insurance and Reinsurance Products

Insurance products are most commonly distributed through:

- individual insurance agents engaged by insurers;
- insurance agencies such as banks and other corporates;
- insurance brokers; and
- directly by insurers, including through the internet.

Bancassurance typically falls within the second bullet point since banks act as insurance agencies, although some banks act as insurance brokers. The staff acting for corporate agencies or brokers in the sale of policies are referred to as technical representatives.

Reinsurance contracts are typically written through reinsurance brokers or based on existing relationships between cedants and reinsurers.

Insurance intermediaries that carry on regulated activities in Hong Kong must be licensed by the IA, subject to narrow exemptions. “Regulated activities” is broadly defined and includes a wide range of solicitation and intermediary activities.

6. Making an Insurance Contract

6.1 Obligations of the Insured and Insurer

The insured must avoid making misrepresentations and must disclose all material facts which are or ought to be known to them and which are material to the formation of the contract. “Mate-

rial” in this context means that the fact would influence the judgement of a prudent insurer in determining whether to accept the risk and in fixing the premium where the risk is accepted.

The law in Hong Kong reflects the traditional common law position and does not incorporate the reforms that have been undertaken in this area in other jurisdictions, including England and Wales.

While the common law does not impose obligations on insurers to seek information proactively, the Code of Conduct for Insurers issued by the Hong Kong Federation of Insurers, which is not legally binding, provides that insurers should ask clear and specific questions in relation to matters which insurers generally consider to be material to the type of insurance in question. A serious failure to ask pertinent questions could also constitute misconduct under the Insurance Ordinance and have other regulatory implications.

The rules are not generally different as between consumer and commercial contracts, but the courts and regulator are likely to impose higher standards on insurers with regard to questions asked of consumers.

6.2 Failure to Comply With Obligations of an Insurance Contract

The insurer is entitled to avoid the policy (ie, to treat it as if it had never existed) if the insured fails to comply with its obligation to disclose material facts.

The non-binding Code of Conduct for Insurers issued by the Hong Kong Federation of Insurers provides that an insurer should not refuse a claim by a policyholder on the grounds of non-disclosure of a material fact which the policy-

holder could not reasonably have been expected to disclose. The exact scope of that proviso is unclear and does not, in any event, change the legal position that an insured must disclose all material facts.

6.3 Intermediary Involvement in an Insurance Contract

Insurance brokers act for insureds and owe them contractual and fiduciary duties. In addition, they are subject to statutory duties which at least partly overlap with the contractual and fiduciary duties owed to the insured. The key obligations are:

- to act honestly, fairly and in the best interest of the (prospective) insured;
- to exercise an appropriate level of care, skill and diligence;
- to have regard to the circumstances of the (prospective) insured to ensure that the insurance cover sought is suitable;
- to disclose sufficient information to the (prospective) insured;
- to avoid conflicts of interest; and
- to handle the monies of the insured in an appropriate manner.

Insurance agents (whether corporates or individuals) act for an appointing insurer and owe fiduciary and contractual obligations to such insurer. They are also subject to the same statutory duties vis-à-vis insureds as apply to brokers, including an obligation to act in the best interest of the insureds. Some of these obligations are hard to reconcile with their role as agents of the insurers, which has been subject to extensive criticism during the legislative process that applied the statutory duties to insurance agents.

Detailed regulatory obligations applicable to insurance brokers and agents are set out in the respective codes of conduct issued by the IA.

6.4 Legal Requirements and Distinguishing Features of an Insurance Contract

Features of Insurance Contracts

The distinguishing features of an insurance contract are determined by reference to English case law, namely as an arrangement under which consideration is paid for the provision of benefits upon the happening of an uncertain event that is adverse to the insured. The common law does not require insurance contracts to be in writing, but there are legal and regulatory requirements in relation to the issuance of policy documents and it is universal practice for insurance contracts to be issued in written form.

Generally speaking, there are no specific minimum terms for an insurance contract to be legally valid, but the key terms must be agreed with reasonable certainty or there must be a mechanism for unresolved terms to be agreed at a later stage. In practice, premiums and cover will usually be clearly set out in the insurance policy (or the reinsurance treaty in the case of reinsurance). There are also numerous regulatory requirements in relation to the structure and terms of certain types of policies.

Insurable Interest

For life insurance contracts, the insured must at the outset have an insurable interest in the person whose life is being insured. Certain persons are legally regarded as having an unlimited interest in the life assured (ie, the person whose life is being insured under the policy), such as the life assured themselves and their spouse. Parents are also deemed to have an insurable interest in the lives of their children under Hong

Kong law. For other relationships, the insured will usually need to have an economic interest in the relevant life in order for the policy to be valid.

While an insurable interest is not strictly speaking required for most types of general insurance contracts, they must not amount to gambling or wagering, and the insured must typically prove loss after the insured event occurs.

6.5 Multiple Insured or Potential Beneficiaries

Beneficiaries and Unnamed Insureds

It is common for persons other than the insured/policyholder to be beneficiaries of a life insurance policy. Where certain close family members are named as beneficiaries, this creates a statutory trust in their favour.

It is also possible for certain unnamed persons to obtain rights against the insurer, for instance on the basis of the Contracts (Rights of Third Parties) Ordinance. The ordinance enables third-party enforcement if the contract expressly provides that the third party may enforce the insurance contract or the contract purports to confer a benefit on the third party. However, the operation of the ordinance is typically excluded by policy wording in Hong Kong.

Unnamed persons may also receive the benefit of group insurance policies, such as insurance taken out by employers for the benefit of all their employees. Beneficiaries may also be described generically by reference to certain characteristics.

There are other cases where unnamed persons can become insureds on the basis of agency considerations, but those cases are rare and will not be considered further here.

Impact on Disclosure Obligations

The impact of a wider group of insureds on disclosure obligations is that material facts in relation to the risk arising from those insureds must be disclosed. Where the cover extends to unnamed persons (rather than the unnamed persons just being beneficiaries/payees of the insurance proceeds), the disclosure obligation is therefore also correspondingly extended.

6.6 Consumer Contracts or Reinsurance Contracts

From a legal perspective, the position is generally the same for consumer contracts and reinsurance contracts. However, detailed regulatory obligations apply to direct insurers with regard to the issuance of policies to their policyholders, such as processes in relation to application forms, suitability assessments, disclosure of information and issuance of policies. Most of those regulatory obligations do not apply to reinsurance contracts.

7. Alternative Risk Transfer (ART)

7.1 ART Transactions

New ILS Regime

Hong Kong introduced a specific regime in relation to insurance-linked securities (ILS) in 2021 and two ILS have been issued under this regime to date. The protection provided by the issuer of the ILS is treated as insurance for the purpose of Hong Kong insurance law, but is subject to specific rules.

Requirements for Issuance

In order to issue ILS under the Hong Kong regime, the issuing entity must be authorised by the IA for “special purpose business”, which is a separate class of insurance. In order to be authorised, the entity must normally appoint two

or more directors and an administrator, all of whom must be “fit and proper” for the purposes of Hong Kong regulation (including by virtue of the administrator having the relevant experience with regard to ILS).

Another key criterion is that the special purpose insurer must be fully funded – ie, its assets (which are typically held in a trust account) must be sufficient to meet the liabilities of the insurer in all reasonably foreseeable circumstances.

ILS can only be sold to certain types of institutional investors specified by Hong Kong legislation.

Challenges

The current challenge with regard to ILS in Hong Kong is that it is a nascent product and the issuance of ILS in the local market therefore takes longer and is procedurally more challenging than in established ILS markets.

7.2 Foreign ART Transactions

There is no specific regime for the recognition of overseas ART transactions. Whether such transactions will be treated as reinsurance for the purposes of the Hong Kong regulatory regime would therefore depend on whether they meet the common law definition of insurance (see 6.4 **Legal Requirements and Distinguishing Features of an Insurance Contract**).

8. Interpreting an Insurance Contract

8.1 Interpretation of Insurance Contracts and Use of Extraneous Evidence

Insurance contracts are generally interpreted in the same way as other contracts. The ordinary meaning of words is typically the starting

point for interpretation, but circumstances may be taken into account as part of the process. While evidence in relation to market understanding and customs in the market are admissible in evidence, previous negotiations between the parties and their subjective intent are generally not admissible.

The *contra proferentem* rule generally applies for the benefit of the insured where there is ambiguity in the policy wording, in particular with regard to exclusions from policy coverage. In those cases, the interpretation that is more favourable to the policyholder will generally be adopted.

The rules are generally the same for consumer and business contracts. However, the courts are more likely to strictly follow the wording of the contract in a business context. In the interpretation of reinsurance contracts, custom and market understanding play a greater role than in consumer insurance policies given the technical and industry nature of reinsurance.

8.2 Warranties

Contractual terms can become warranties on the basis of express identification as warranties or by implication, commonly by virtue of “basis of the contract” clauses, which are provisions set out in the proposal form or in the insurance contract to the effect that all answers to the questions in the proposal will form the basis of the contract.

Warranties are different from other contractual terms in that they require strict compliance and any breach permits the insurer to disclaim liability, whether or not the breach was material to the insured risk.

Hong Kong is still subject to the common law approach to insurance warranties and has not

implemented reforms that have been undertaken in other jurisdictions, including England and Wales.

8.3 Conditions Precedent

Contractual terms need not be expressly described as conditions precedent in order to be treated as such. While express designation as a condition precedent is a common approach, the classification may also be derived from the contractual wording – eg, a provision that the insurers have the right to refuse a claim if a particular condition is not complied with.

The consequences of a breach of a condition precedent depend on the contractual wording and the nature of the condition. Failure to comply with a condition will typically preclude the insured from bringing a claim; it may also, if sufficiently fundamental, entitle the insurer to terminate the policy.

9. Insurance Disputes

9.1 Insurance Disputes Over Coverage Coverage Disputes

Disputes over coverage under an insurance contract are typically settled through the Insurance Complaints Bureau (in the case of consumer contracts) or through litigation or arbitration (see [9.7 Alternative Dispute Resolution](#) for further details).

Limitation Period

Pursuant to the Limitation Ordinance (Cap 347), the insured generally has six years from the date on which the cause of action accrued to issue proceedings against the insurer. However, the insurance policy will typically specify periods during which claims must be brought following the occurrence of the insured event or the

insured's awareness of such event (as applicable).

Enforcement of Insurance Contracts by Third Parties

See [6.5 Multiple Insured or Potential Beneficiaries](#) regarding the enforcement of insurance contracts by third parties.

9.2 Insurance Disputes Over Jurisdiction and Choice of Law

In practice, insurance contracts typically include jurisdiction and governing law provisions. Hong Kong courts will generally recognise and enforce these provisions provided that they are bona fide (ie, made in good faith), legal and are not against public policy. Disputes over jurisdiction and choice of law in insurance contracts are rare.

Where the contract does not contain a jurisdiction or governing law clause, the court will apply the usual common law principles and examine a variety of factors to determine these issues. In considering choice of law, the court will consider the place of intended performance and the insurer's head office location to determine which law has the closest and most real connection with the insurance contract.

9.3 Litigation Process

Depending on the nature of the claim and the amount involved, insurance claims are generally heard in the District Court or the Court of First Instance in Hong Kong.

The main stages in civil proceedings include:

- issuing and service of originating process by way of writ of summons, originating summons, or petition;
- filing pleadings such as the statement of claim, defence and reply;

- discovery and inspection of documents;
- exchange of factual witness statements;
- filing of expert reports (if required); and
- trial.

9.4 The Enforcement of Judgments Domestic Judgments

The most common ways to enforce domestic judgments in Hong Kong include the following.

- Garnishee proceedings – where a third party (the garnishee) owes money to the judgment debtor, the judgment can be enforced directly against the garnishee. The garnishee will then pay its debts to the judgment creditor instead of the judgment debtor. This option is commonly used against the judgment debtor’s bank.
- Charging order/order for sale of assets – judgment creditors can obtain security over the assets of the judgment debtor.
- Writ of fieri facias – also known as a fifa order, this allows an officer of the court to seize and sell the judgment debtor’s goods and chattels.
- Bankruptcy or insolvency proceedings may also be considered.

Foreign Judgments – Statutory Registration Scheme

A foreign judgment can be enforced in Hong Kong either through the statutory registration scheme based on reciprocity under the Foreign Judgments (Reciprocal Enforcement) Ordinance (Cap 319) (FJREO) or at common law.

Under the FJREO, judgments from “superior courts” of 15 countries (namely, Australia, Austria, Belgium, Bermuda, Brunei, France, Germany, India, Israel, Italy, Malaysia, the Netherlands, New Zealand, Singapore and Sri Lanka) are enforceable by the simple procedure of registra-

tion through an application to the Court of First Instance provided that the application is made within six years of the original judgment.

Once leave is granted, the foreign judgment can be enforced in the same way as a Hong Kong judgment.

Foreign Judgments – Common Law

If the foreign judgment is not from a country listed under the FJREO, it can only be enforced at common law. In this case, the foreign judgment will form the basis of a cause of action and the judgment will be treated as a debt between the parties. To be enforceable at common law, the following requirements must be met:

- the foreign judgment must be for a debt or a definite sum of money, and the defendant must have submitted to the jurisdiction of the foreign court;
- the foreign judgment was final and conclusive;
- the foreign judgment was not obtained by fraud, and was obtained against the same defendant;
- the foreign judgment was not contrary to Hong Kong rules of public policy or notions of natural justice;
- the foreign court had jurisdiction over the defendant according to Hong Kong rules; and
- an action in Hong Kong based on a foreign judgment must be brought within 12 years from the date on which the foreign judgment became enforceable.

Mainland Judgments

Enforcement of People’s Republic of China (PRC) judgments is governed by the “Arrangement on Reciprocal Enforcement of Judgments in Civil and Commercial Matters” and the Mainland Judgments (Reciprocal Enforcement) Ordinance

(Cap 597) in Hong Kong (MJREO). The MJREO makes provision for mutual enforcement of Hong Kong and PRC judgments in civil or commercial matters. It also applies to the enforcement of money judgments on disputes arising out of commercial contracts.

In order to register a PRC judgment in Hong Kong:

- the judgment must be from a court which is a designated court under the MJREO (ie, courts at the Intermediate People's Court level or above and specified Basic People's Courts);
- the judgment must be final and conclusive and enforceable in the PRC;
- the judgment must order the payment of a sum of money (not being a sum payable in respect of taxes, fines or penalties); and
- the application to the Court of First Instance must be made within two years from the date of the judgment.

9.5 The Enforcement of Arbitration Clauses

Arbitration clauses in commercial insurance and reinsurance contracts can be enforced, so long as they comply with the formal requirements under Section 19 of the Arbitration Ordinance (Cap 609). These include that an arbitration agreement must be in writing, and there must be a reference of the dispute to arbitration. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement.

9.6 The Enforcement of Awards

Under the Hong Kong Arbitration Ordinance (Cap 609), there are four main categories of arbitral awards:

- convention awards (which are awards issued in states or territories that are party to the New York Convention, other than the PRC);
- Mainland awards (which are awards issued in Mainland China);
- Macao awards (which are awards issued in Macao); and
- awards issued in Hong Kong and Taiwan, and any awards not captured by the first three categories.

Hong Kong is not a contracting state to the New York Convention. In 1997, following the PRC's resumption of the exercise of sovereignty over Hong Kong, the PRC extended the application of the New York Convention to Hong Kong. The PRC's reciprocity and commercial reservations made under Article I(3) of the New York Convention are binding on Hong Kong. As a result, Hong Kong recognises awards issued in the territory of another contracting state to the New York Convention, and arising out of commercial disputes. Enforcement may only be refused pursuant to the limited grounds set out in the New York Convention.

Arrangements in place allow for the enforcement of arbitral awards between Mainland China and Hong Kong (namely the 1999 and 2020 Arrangements Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region). All arbitral awards issued pursuant to the Hong Kong Arbitration Ordinance can be enforced in Mainland China. All arbitral awards issued pursuant to the PRC Arbitration Law can be enforced in Hong Kong. Simultaneous enforcement applications may be commenced in the courts of Hong Kong and Mainland China.

There is also an arrangement resulting in mutual recognition of arbitral awards between Hong Kong and Macao.

There are separate provisions in the Hong Kong Arbitration Ordinance concerning the enforcement of awards under these categories. With the leave of the court, arbitral awards (including interim awards), whether domestic or foreign, are enforceable in the same manner as a Hong Kong court judgment.

9.7 Alternative Dispute Resolution

Alternative dispute resolution (ADR), including arbitration, mediation and adjudication, is commonly used in insurance disputes in Hong Kong. Since the introduction of the Civil Justice Reform in Hong Kong in April 2009 and Practice Direction 31 in January 2010, parties to litigation are required to attempt settlement by mediation. Adverse costs orders may be made against a party which unreasonably fails to engage in mediation, regardless of the outcome of the litigation.

Consumer Contracts

For consumer insurance disputes, the Insurance Complaints Bureau (ICB) provides a mechanism to assist in the resolution of insurance disputes arising from personal insurance policies. These disputes must be monetary in nature, including complaints regarding claim decisions of insurers and maladministration on the part of the insurer.

The ICB handles claim-related complaints by way of adjudication under the Insurance Claims Complaints Panel, and non-claim-related complaints by way of mediation provided by the ICB List of Mediators.

- Adjudication involves an independent adjudicator (usually an expert) who considers the

claims of both parties and issues a binding decision.

- Mediation is a voluntary procedure whereby a professionally trained and impartial mediator helps the parties settle their dispute. A mediator will not make a decision for the parties, but will assist the parties in exploring the merits of their own cases, as well as in identifying possible solutions in order to facilitate settlement.

Policyholders are not bound to refer their disputes to the ICB. If they choose to litigate or arbitrate their case instead, the ICB does not have jurisdiction unless and until those proceedings are resolved. However, since consumer insurance policies typically do not contain arbitration provisions, ADR outside the ICB would be uncommon for consumer insurance disputes. The ICB has no jurisdiction to handle disputes arising from industrial, commercial or third-party insurance.

Reinsurance Contracts

Reinsurance contracts often contain arbitration clauses, and it is common to arbitrate reinsurance-related disputes (see 9.5 The Enforcement of Arbitration Clauses).

9.8 Penalties for Late Payment of Claims

Subject to general contractual obligations between the insurer and the insured under an insurance policy, and unlike in the United Kingdom, there is currently no provision in Hong Kong which confers a statutory right of damages if insurers delay payment of claims.

9.9 Insurers' Rights of Subrogation

Subrogation, in the context of insurance, is the right of the insurer to pursue third parties for claims in which the insurer may be liable to the insured. Where the insurer pays for a claim under

an insurance contract, the insurer becomes entitled to “step into the shoes” of the insured and is subrogated to all of the insured’s rights and remedies in respect of that subject matter. The insurer is only entitled to the rights and remedies which are available to the insured and the insurer has no greater right than that of the insured.

10. Insurtech

10.1 Insurtech Developments

Insurtech developments in Hong Kong are similar to those in other jurisdictions. For example, online sales and online claims portals, digitally customisable products, online brokers (such as comparison websites), blockchain-based products and products involving connected devices are all seen in the market. There is great interest in insurtech solutions, including those developed in nearby markets with strong insurtech ecosystems, such as Mainland China and Singapore.

A number of purely digital life and general insurers have been authorised by the IA.

10.2 Regulatory Response

The IA has two primary initiatives in relation to insurtech.

Fast Track

One initiative is a “fast track” authorisation process for purely digital insurers, which has been used by a number of new entrants to the life and general insurance markets. Such “fast track” insurers are generally limited to distributing their products through their digital platform and are not permitted to sell them through traditional agent or broker channels.

Sandbox

The other initiative is a “sandbox” which allows insurers to work on insurtech applications and products with the IA before they are launched to the market. Since the launch of the sandbox, this has included online sales platforms and non-face-to-face sale models involving videoconferencing tools. Certain requirements apply to participation in the sandbox, including a reasonably mature insurtech application, solid testing, exit and customer protection measures and the compliance of the application with law and regulation.

11. Emerging Risks and New Products

11.1 Emerging Risks Affecting the Insurance Market

Catastrophe risk (including more severe typhoons as a result of climate change) is regarded as one of the key emerging risks in Hong Kong. The newly established regime for ILS (see 7.1 **ART Transactions**) is a key response of the regulator to such risk, which affects not only Hong Kong, but Mainland China and the wider region as well and may give rise to an increased demand for risk transfer to the capital markets.

The other regulatory initiatives in Hong Kong have been primarily focused on the emerging protection gaps for an aging population. Many Hong Kong residents have no or limited private health insurance and only limited pensions or other retirement protection. This has resulted in the design and promotion of new products with the assistance of the IA and the Hong Kong government – see 11.2 **New Products or Alternative Solutions**.

11.2 New Products or Alternative Solutions

The new ILS regime has been described in 7.1 ART Transactions.

In the last few years, the Hong Kong insurance industry, supported by the Hong Kong government, has developed a number of products that are designed to address existing protection gaps.

This includes voluntary health insurance scheme (VHIS) products that provide indemnity coverage for hospital treatments in accordance with standards set by the Food and Health Bureau.

The newly developed products also include qualified deferred annuity plans, which are deferred annuity plans meeting certain requirements set by the IA and permit taxpayers to claim a tax deduction for their premiums up to a defined maximum limit.

In November and December 2021, the IA and the Securities and Futures Commission (SFC) provided updated guidance on unit-linked products, which are locally known as “investment-linked assurance scheme” (ILAS) products. The guidance sets out new requirements that such products must meet in relation to various aspects (such as cost of insurance charges, fees and surrender charges) in order to benefit from a swifter approval process involving both regulators.

12. Recent and Forthcoming Legal Developments

12.1 Developments Impacting on Insurers or Insurance Products Relaxation of Rules Relating to the Sale Process

In response to COVID-19, the IA relaxed the requirements relating to the sale of certain types of insurance products. Those relaxations continue to apply while the pandemic continues and are intended to facilitate non-face-to-face sales of products that are not regarded as complex.

As insurers sought to sell a wider range of policies through videoconferences between agents and customers, the IA adopted new rules on the conduct of such sales and required insurers to have the process for such sales approved by it through the insurtech sandbox.

Policy Coverage

A number of insurers have adapted their policies to cover specific COVID-19-related risks, such as under travel or health insurance policies.

The cases conducted in other jurisdictions such as England and Wales in relation to the scope of coverage for business interruption caused by COVID-19 have been closely followed in Hong Kong, since similar coverage issues arise under local insurance policies and reinsurance contracts.

13. Other Developments in Insurance Law

13.1 Additional Market Developments Cross-Border Regimes and ILS

The proposed cross-border insurance regimes for the Greater Bay Area referred to in 2.1 Insur-

ance and Reinsurance Regulatory Bodies and Legislative Guidance and the new ILS regime set out in 7.1 ART Transactions are key recent market developments.

Risk-Based Capital Regime

The IA is working on the final rules for a new risk-based capital regime that is expected to replace the current formula-based “Solvency I” style regime in 2024. This follows years of extensive quantitative testing and consultation with the industry. The new risk-based regime follows a three-pillar approach similar to Solvency II and other risk-based frameworks. It is complemented by a new group-wide solvency regime for Hong Kong-regulated insurance groups, which was implemented in 2021.

Policyholders’ Protection Fund

Following a 2012 consultation regarding the establishment of a Policyholders’ Protection Fund (PPF), the Hong Kong government is preparing the legislation needed for such a PPF. The fund will consist of two schemes, one for life and one for general insurance, and will be available to pay claims in the event of an insurer’s insolvency. There are existing compensation funds in relation to motor and employees’ compensation insurance, which will be carved out from the new PPF.

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Trends and Developments

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Key Commercial and Regulatory Trends in the Hong Kong Insurance Industry

Insurtech

Insurers in Hong Kong continue to focus heavily on the incorporation of technology in key parts of their operations. Insurance sales and distribution, data analytics and underwriting, and policy servicing and administration are all areas in which technology plays an ever-increasing role.

In terms of customer-facing applications, non-face-to-face onboarding and insurance sales (such as through videoconference tools) have been implemented by many insurers in light of the COVID-19 pandemic. Virtual onboarding and sales are generally subject to approval of the insurer's processes and governance by the Hong Kong Insurance Authority (the Insurance Authority) through its insurtech sandbox.

Insurers have also enhanced their digital policy administration and claims platforms. A number of insurers (particularly in the area of general insurance) have developed platforms for online submission of claims, thereby reducing the effort and time expended by policyholders in the claims process.

A number of leading insurers have established specific internal governance and issued guidelines for the use of sales and AI algorithms, although Hong Kong does not yet have specific regulation on such matters that is applicable to insurers.

A handful of digital-only insurers have been authorised in recent years under a "fast track"

regime put in place by the Insurance Authority. While virtual insurers continue to grow their product offerings and businesses, their growth is currently limited by restrictions on their licences under which they are generally limited to distributing products through their own digital platforms.

A further constraint on digital sales is that the Insurance Authority continues to take the view that more complex life insurance products should not be sold through online platforms.

Distribution

Technology also plays a key role in distribution channels of traditional insurers. Many traditional insurers have strengthened their digital sales channels, and although their overall contribution to insurance sales is modest in the life sector, their importance is growing, particularly among younger customers.

While insurance agents and bancassurance remain the key distribution channels for life insurance, insurers have also continued to enter into partnerships with digital partners, such as digital platforms and online service providers. Often, those digital partners have to be licensed as intermediaries, but the Insurance Authority has issued guidelines indicating that such a licence may not be required if the sale is conducted in a particular technological form.

Products

While the overall potential for premium growth in the dominant life sector has been limited by the COVID-19 pandemic and the closure of the

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border with Mainland China, products championed by the government and subject to favourable tax treatment, in particular voluntary health insurance schemes (VHIS) and qualified deferred annuity products (QDAP), have remained popular.

Most recently, the Insurance Authority and the Securities and Futures Commission have revised the approval process for linked products, locally known as investment-linked assurance schemes (ILAS). Linked products with a specified minimum mortality protection element and simple features (also known as protection-linked plans) are subject to an expedited approval process. However, despite the streamlined process, some insurers continue to regard the approval conditions and process for ILAS as onerous.

Reinsurance and alternative risk transfer

In recent years, there has been a trend towards Hong Kong life insurers reinsuring large blocks of legacy business to internal and external offshore reinsurers, often based on regulatory capital considerations. This trend is expected to continue as insurers prepare for the new risk-based capital regime (see the **Risk-Based Capital** section).

In terms of alternative risk transfer, a new legal and regulatory regime for insurance-linked securities (ILS) came into effect in 2021. Following the example of Singapore, Hong Kong put in place a grant scheme to support initial ILS issuances from Hong Kong. To date, there have been two catastrophe bond issuances under the new regime. While the length of the approval process and the relative lack of local expertise with regard to such issuances continue to raise concerns, Hong Kong's preferential status with Mainland China is likely to result in further risk

transfer of Chinese risks to the capital markets through Hong Kong-based ILS.

Development roadmap

The Financial Services and the Treasury Bureau published a roadmap for Hong Kong's insurance industry in December 2022. A number of key points are set out in the roadmap:

- Hong Kong will continue to pursue and strengthen its role as a global risk management centre;
- Hong Kong's insurance industry plays an important part in national initiatives, such as the Greater Bay Area, China's "Belt and Road" initiative and the "dual circulation" economy (meaning a focus on both domestic and international markets);
- there will be an increased focus on talent acquisition, technology and data, including devising mortality tables for the Greater Bay Area that may assist with the development of cross-border life and health products.

A number of these points are considered in more detail below.

Insurance Connect and the Greater Bay Area

The Insurance Authority and relevant government departments continue to liaise with Mainland Chinese regulators on the finalisation of arrangements for Hong Kong insurers to open service centres in designated Mainland locations, such as Qianhai and Nansha. The service centres will allow Hong Kong insurers to service policies issued to Mainland Chinese customers, including with regard to claims and complaints handling.

Discussions are also ongoing regarding the design of an eagerly awaited "Insurance Connect" regime under which Hong Kong-author-

ised insurers would be permitted to sell certain products in the Greater Bay Area (an area comprising Hong Kong, Macau and a number of cities in Guangdong province). The features of such a regime remain challenging, particularly given the strict exchange control regulations in the Mainland, which cannot be addressed in the same way as for existing “Connect” schemes for stocks and bonds.

Another aspect of the integration of the Greater Bay Area is the design of cross-border products, such as motor insurance covering Hong Kong-registered vehicles for travel into other parts of the Greater Bay Area and medical products covering policyholders across the Greater Bay Area. Due to the complex legal and regulatory issues raised by cross-border insurance products, such products currently remain under development.

Group-wide supervision

The Insurance Authority has recently implemented the supervisory regime for Hong Kong-based insurance groups. The regime is built on the principles issued by the International Association of Insurance Supervisors (IAIS). Three insurance groups are currently subject to group supervision, namely AIA, FWD and (the formerly UK-based) Prudential.

The group supervision regime imposes group-wide capital requirements, generally based on an aggregation of capital requirements and eligible capital resources of local operations in the relevant jurisdictions. It also includes requirements for capital instruments that need to be met for such instruments to be recognised as Tier 1 or Tier 2 capital on a group basis. The requirements are generally aligned with corresponding IAIS recommendations.

In addition, the group-wide regime imposes extensive group-wide governance requirements. Among other changes, major acquisitions made by an insurance group have to be assessed through a framework specific to the insurance group and, if assessed to be material, approved by the Insurance Authority. Key persons of the “designated holding company” of the group are subject to fit and proper requirements and approval of the Insurance Authority. Implementation of the group-wide supervision regime has been a focus for the three insurance groups in question.

Risk-based capital

Another regulatory focus has been the risk-based capital (RBC) regime that is expected to apply to all insurers from 2024. Rules have been fine-tuned in consultation with the industry and are in the process of being finalised. In line with other RBC regimes, the Hong Kong rules will be based on three pillars, namely:

- quantitative requirements for the determination of a “prescribed capital requirement” reflecting the risks to which the insurer is exposed;
- qualitative assessment of risks, including through an own risk and solvency assessment (ORSA); and
- disclosure of solvency-related information to the regulator and the public.

There has been an early implementation of the second pillar, so the requirement to prepare ORSAs is already in force.

The change is significant for insurers since Hong Kong has been one of the last jurisdictions in Asia operating under a formula-based capital regime. Several leading insurers have obtained approval for early adoption of the quantitative

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regime, allowing them to calculate their capital requirements under the new risk-based capital regime.

While the Hong Kong RBC regime is similar to Europe's Solvency II and other risk-based regimes, it is generally regarded as simpler and more pragmatic than some of the existing regimes, in particular Solvency II.

ESG

Many Hong Kong insurers, in particular the large international insurance groups, increasingly take into account ESG issues as part of their operations. The trend manifests itself in amended investment policies and mandates (which may no longer permit investments in certain "black-listed" sectors or entities and may require a certain level of investments in "green" securities). In addition, many insurers and reinsurers reflect ESG issues in their underwriting process – eg, by rejecting coverage of objects or companies that are problematic from an ESG perspective.

Some insurers have adopted nuanced approaches to underwriting. Rather than rejecting coverage altogether, they may set underwriting conditions in relation to ESG standards that policyholders must meet, or engage with corporate customers to bring environmental or social standards to an acceptable level before coverage is provided. Such an approach enables insurers to bring about positive change, while reducing ESG risks for both the insurer and the policyholder. However, the approach requires significant ESG expertise on the part of the insurer to be successful.

Many insurers have issued internal ESG guidelines and incorporated ESG issues into their risk and governance regimes. While there is currently no mandatory ESG disclosure regime for insur-

ers in Hong Kong, the Insurance Authority and a task force of the Hong Kong Federation of Insurers are working on "green insurance" and disclosure matters. It is expected that a recommended disclosure standard – potentially aligned with the recommendations of the Task Force on Climate-Related Financial Disclosures – will be issued at some point.

Policyholders' protection scheme

A policyholders' protection scheme with regard to the insolvency of Hong Kong insurers has long been under consideration and the Insurance Authority has very recently announced that it will launch a further consultation on the proposal in December 2022. There is currently no industry-wide scheme (although a few sectoral schemes exist). This is a further measure designed to align the level of policyholder protection in Hong Kong with the standards in other advanced jurisdictions.

Enforcement

There has been a clear trend towards more proactive investigation and enforcement by the Insurance Authority in the last few years. An early focus was on compliance with anti-money laundering requirements, and the first-ever fine was recently imposed by the Insurance Authority on two insurers in this area.

The Insurance Authority has recently focused on insurers' complaints handling and compliance with their filing and notification requirements under the Insurance Ordinance and undertakings given by them. Detailed investigations of perceived regulatory or compliance failures, including investigations involving reports written by law or accountancy firms, are more common now, and it can be expected that the trend towards proactive enforcement will continue.

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Sales practices of insurers remain another focus area, in particular where products are sold through insurance agents. Insurers invest heavily in agency training and compliance programmes to mitigate the mis-selling risk.

Talent

Talent remains a concern for Hong Kong insurers, particularly in the actuarial and technology areas, and the industry (with support from the Insurance Authority) is actively trying to attract additional insurance talent to Hong Kong while also enhancing local education and training in these areas.

M&A

Although the level of insurance M&A in Hong Kong has declined due to current economic circumstances, significant activity persists, particularly in the “middle tier” of insurance companies. There is a trend towards consolidation, the key drivers of which include the difficulty of achieving profitability without scale, the incoming risk-based capital regime and an increasing regulatory burden. Buyers typically include existing Hong Kong insurers and other market participants with existing insurance holdings in Hong Kong or other leading jurisdictions.

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