Specific report on new requirements being phased in

Insurance (Financial and Other Requirements for Licensed Insurance Broker Companies) Rules (Cap. 41L) - Savings and Transitional Arrangements

The Insurance (Financial and Other Requirements for Licensed Insurance Broker Companies) Rules (Cap. 41L) ("Broker Rules") came into force on 23 September 2019. The Broker Rules set out the requirements applicable to licensed insurance broker companies for minimum share capital, net assets, professional indemnity insurance, the keeping of proper books and records, and contents for audited financial statements and auditor's report.

The requirements in the Broker Rules which are new (compared to the requirements under the previous self-regulatory regime) are being phased-in for "specified insurance broker companies" over a period of years until 1 January 2024 in accordance with the Savings and Transitional Arrangements in the Broker Rules ("Transitional Arrangements"). "Specified insurance broker companies" [1] in this respect are licensed insurance broker companies which were previously registered under the self-regulatory regime (and which continue to be licensed under the new regulatory regime).

The purpose of this phasing-in approach is to give specified insurance broker companies sufficient lead-in time to make changes to their processes so that they can gradually bring themselves into compliance with the new requirements in the Broker Rules.

Having reviewed the financial statements and compliance reports submitted to the IA each year so far, we set out below our observations as to how specified insurance broker companies are progressing with the new requirements as they are being phased in, in line with the Transitional Arrangements. We also provide a reminder of the forthcoming requirements being phased in, so advanced arrangements can be made by specified insurance broker companies to bring themselves into compliance.

A. Requirements for Audited Financial Statements for each financial year beginning on or after 1 January 2021 onwards

According to rule 8(2) of the Broker Rules, the financial statements provided by a licensed insurance broker company must include the company's:

(a) insurance brokerage income for the financial year distinguishing between general business and long term business;
(b) aggregate balances of cash held in its client accounts as at the end of the financial year; and
(c) insurance premiums payable as at the end of the financial year.

Specified insurance broker companies have been required to comply with rule 8(2) of the Broker Rules, **for each financial year beginning on or after 1 January 2021 onwards**.

[1] Specified insurance broker company means a company which was immediately before the commencement date (i.e. 23 September 2019) registered with an approved broker body as a member and regarded as having been granted an insurance broker company licence under section 66 of Schedule 11 to the Insurance Ordinance on the commencement date.

From our review of the financial statements submitted for the financial year ended 31 December 2021, however, a significant number of specified insurance broker companies have not complied with these requirements. Whilst the failure rate has been reducing since then (following circulars we have sent out through the Hong Kong Institute of Certified Public Accountants), there are still a number of non-compliances with these requirements being noted. All broker companies must take this reminder seriously and ensure they comply with these requirements so as to avoid the prospect of disciplinary action.

B. Requirements for Share Capital and Net Assets as from 1 January 2022

As from 1 January 2022, the amount of paid-up share capital and net assets which a specified insurance broker company must maintain at all times increased from HK$100,000 to HK$300,000 (pursuant to rules 3 and 4(1) of the Broker Rules).

From the financial statements submitted so far by licensed insurance broker companies with their financial year ending on dates between 1 January 2022 to 31 March 2022, we have noted that only 2% failed to increase their paid-up share capital and/or net assets to meet these new requirements. Broker companies will appreciate that, given the importance of these requirements as a policy holder protection measure, compliance with it is imperative. In the event of non-compliance, disciplinary action can be expected.

C. Requirements for Share Capital and Net Assets which will apply as from 1 January 2024

As from 1 January 2024, the amount of paid-up share capital and net assets which a specified insurance broker company must maintain at all times increases further from HK$300,000 to HK$500,000 (pursuant to rules 3 and 4(1) of the Broker Rules).

To comply with these requirements from 1 January 2024, specified insurance broker companies (which have not already done so) must increase their paid-up share capital and net assets to an amount of not less than **HK$500,000 by 31 December 2023**.

D. Requirements for Professional Indemnity Insurance which will apply as from 1 January 2024

As from 1 January 2024, the deductible amount under the professional indemnity insurance policy maintained by a licensed insurance broker company must not be more than 50% of the company's net assets as at the end of its financial year immediately before the commencement date of the policy period under the policy (pursuant to rule 5(5) of the Broker Rules).

Accordingly, each specified insurance broker company should ensure that if its professional indemnity insurance policy with a policy period commencing on or after **1 January 2024**, includes a deductible, then that deductible must not be more than 50% of the company's net assets as at the end of its financial year immediately before the commencement date of the policy period. Furthermore, as a professional indemnity insurance policy usually has a policy period of one year (at least), a specified insurance broker company should ensure compliance with these new requirements when purchasing a professional indemnity insurance policy with a policy period of one year, where the policy period commences **after 1 January 2023 (with the policy period ending on or after 1 January 2024)**.