G.N. 781

INSURANCE ORDINANCE (Chapter 41)

Pursuant to section 133(1) of the Insurance Ordinance (Chapter 41), the revised Guideline on Underwriting Long Term Insurance Business (Other than Class C Business) (GL16) and the revised Guideline on Governance and Management of Fund(s) of Participating Business (GL34) are published by the Insurance Authority. The revised GL34 shall take effect on 31 March 2026, except for section 4 which shall take effect on 30 June 2026. The revised GL16 shall take effect on 31 March 2026, except that compliance with section 4 of the revised GL34 as referred to in paragraph 2.2 of Appendix 2 of the GL16 shall take effect from 30 June 2026.

6 February 2026 Clement CHEUNG *Chief Executive Officer, Insurance Authority*

GL16

GUIDELINE ON UNDERWRITING LONG TERM INSURANCE BUSINESS (OTHER THAN CLASS C BUSINESS)

Insurance Authority

Contents **Page**

1. Introduction

1.1 This Guideline is issued pursuant to section 133 of the Insurance Ordinance (Cap. 41) ("the Ordinance") taking into account the Insurance Core Principles, Standards, Guidance and Assessment Methodology ("ICP") promulgated by the International Association of Insurance Supervisors ("IAIS"). Specific references are:

(a) section 4A of the Ordinance stipulates that the Insurance Authority ("IA")'s function is to protect existing and potential policy holders. Section 4A(2)(c) states that the IA shall promote and encourage the adoption of proper standards of conduct, and sound and prudent business practices by authorized insurers; and

(b) as stipulated in ICP 19, the conduct of the business of insurance should ensure that customers are treated fairly, both before a contract is entered into and through to the point at which all obligations under a contract have been satisfied. The conduct of insurance business should help to strengthen public trust and consumer confidence in the insurance sector.

1.2 This Guideline applies to all authorized insurers underwriting long term business (other than Class C business).

1.3 Save as otherwise expressly stated, terms defined in the Ordinance and its subsidiary legislation shall have the same meaning when used in this Guideline.

2. Relevant Regulatory Documents

2.1 Where appropriate, this Guideline should be read in conjunction with other relevant codes/circulars/guidelines issued by the IA or other regulatory bodies, including but not limited to the following[1]:

(a) Guideline on Benefit Illustrations for Long Term Insurance Policies (GL28) issued by the IA;

(b) Guideline on Financial Needs Analysis (GL30) issued by the IA;

(c) Guideline on Governance and Management of Fund(s) of Participating Business (GL34) issued by the IA;

(d) Principles of Life Insurance Policy Illustrations (AGN 5) issued by the Actuarial Society of Hong Kong ("ASHK");

(e) Best Estimate Assumptions (AGN 9) issued by the ASHK; and

(f) all relevant rules, codes, circulars and guidelines administered or issued by Hong Kong Monetary Authority.

[1] The list is not exhaustive and may be subject to changes from time to time. Authorized insurers have the responsibility to ensure compliance with all the relevant requirements with due regard to their own circumstances.

3. Purpose

3.1 Both IAIS and the global insurance industry have placed increasing emphasis on fair treatment of customers. Fair treatment of customers encompasses:

(a) developing, marketing and selling products in a way that pays due regard to the interests and needs of customers;
(b) providing customers with information before, during and after the point of sale that is accurate, clear, and not misleading;
(c) minimizing the risk of sales which are not appropriate to customers' interests and needs;
(d) ensuring that any advice given is of a high quality;
(e) dealing with customer claims, complaints and disputes in a fair and timely manner; and
(f) protecting the privacy of information obtained from customers.

3.2 This Guideline sets out the requirements for authorized insurers underwriting long term insurance business (other than Class C business). In assessing whether the requirements have been duly followed by authorized insurers, the IA will consider the substance and nature of the matters involved. The name or form of the arrangements adopted by individual authorized insurers would be irrelevant.

4. Duties of the Board, the Controller and the Appointed Actuary

4.1 It is the duty of the Controller, as specified under section 13A(12) of the Ordinance, to ensure that requirements set out in this Guideline are observed throughout the life cycle of all long term (except Class C) insurance policies. It is also the duty of the Board to maintain general oversight over the implementation of measures in compliance with this Guideline and is ultimately responsible for ensuring fair treatment of customers.

4.2 It is a reasonable expectation for policy holders to expect to receive at least a fair proportion, if not all, of the non-guaranteed part of the illustrated benefits. It is the duty of the Controller, the Appointed Actuary and the Board to ensure that such policy holders' reasonable expectation is met.

4.3 It is a continuing duty of the Appointed Actuary to advise the Board of his or her interpretation of policy holders' reasonable expectations. For instance, in the context of the provision of benefit illustrations, it is the duty of the Appointed Actuary to adopt reasonable assumptions, as well as to provide regular and up-to-date assessment of such assumptions to the Board for making suitable amendments. When a significant change of the underlying assumptions is likely to take place, the Appointed Actuary should take all reasonable steps to ensure that the Board appreciates the implications for the reasonable expectations of the

policy holders.

4.4 Any attempt to circumvent the requirements prescribed in this Guideline would be regarded as acting in bad faith. In the case of Controllers, this may affect the "fit and proper" assessment under sections 8(2) and 13A(4) of the Ordinance. In the case of Appointed Actuaries, this may constitute non-compliance with professional standards under section 15C of the Ordinance, and may render the incumbent not acceptable to the IA under section 15AAA(2) of the Ordinance.

5. Product Design

5.1 Authorized insurers should develop, market and sell products with due regard to the interests and needs of customers. During the product design stage, authorized insurers should carry out a diligent review to ensure that the product meets the "fair treatment of customers" principle, including:

(a) delivery of the reasonably expected benefits;
(b) sustainability of the product;
(c) needs and affordability of the target customers;
(d) risks of the product; and
(e) distribution channels for the product.

5.2 When performing the diligent review mentioned above during the product design stage, authorized insurers are required to take a holistic view of all the relevant factors. For example, a product with complex features may not be suitable for distribution through the online channel, where advice to customers cannot be given during the sale process.

5.3 Authorized insurers are required to monitor the products after launch to ensure that they continue to meet the needs of the target customers, assess the performance of the various distribution channels with respect to sound commercial practices, and take the necessary remedial actions where appropriate.

5.4 In considering whether the design of a product meets the requirements of this Guideline and the "fair treatment of customers" principle, authorized insurers are required to look at all relevant factors in their totality, including the product features, insurance elements, added value/services to customers, fees/charges, surrender penalties (where applicable), remuneration structure etc.

5.5 Fees and charges (including charging basis, level of charges, applicable period etc.), where applicable, to be paid by the customers should be fair, commensurate with the insurance protection offered by the product concerned, and reflect the services/added value of the authorized insurer.

5.6 During product design, the determination of pricing assumptions should be based on the best estimate assumptions. For the guidance and considerations in setting best estimate assumptions, the Appointed Actuary should follow AGN 9 on Best Estimate Assumptions issued by the ASHK.

6. Provision of Adequate and Clear Information

6.1 Authorized insurers should provide customers with information before, during and after the point of sale that is accurate, clear, and not misleading.

6.2 The development of insurance products and distribution strategies should include the use of adequate information to assess the needs of different customer groups.

6.3 Authorized insurers should offer a product that delivers the reasonably expected benefits.

6.4 Authorized insurers should take reasonable steps to ensure that customers are given timely, clear and adequate information about an insurance product, enabling them to make informed decisions.

6.5 Product information (e.g. product brochure and benefit illustration) should be bilingual[2], clear and succinct, with the use of plain language and legible font size, and should be easily understandable by average customers. To facilitate understanding by customers, authorized insurers should avoid using technical or industry terminology.

6.6 Major product features and key risks to customers should be clearly disclosed in the product brochure and marketing materials, including the areas (where applicable) below:

(a) key exclusions alongside description of policy coverage;
(b) factors leading to premium adjustments made by the authorized insurer and the frequency and timing of such adjustments. For those products with premium adjustment features within the premium payment term, they cannot be labeled as "level premium";
(c) minimum premium payment term and the consequence of failure to settle premiums due, including loss of coverage, surrender penalty and financial loss incurred by the policy holder;
(d) conditions of making a decision to terminate the policy by the authorized insurer;
(e) factors for the determination of market value adjustment made by the

[2] For the avoidance of doubt, the English and Chinese versions of the product documents can be separated, but BOTH must be available to the customers. Authorized insurers should ensure consistency between English and Chinese versions of all the product documents (including product brochure, benefit illustration, policy contract, etc.).

authorized insurer on premiums paid within cooling-off period; and

(f) adverse impact of inflation (i.e. where the actual rate of inflation is higher than expected, and the policy holder might receive less in real terms even if the authorized insurer meets all of its contractual obligations).

6.7 For products with policy loan facility, authorized insurers should provide policy holders with information about the terms of the loan (including interest rate to be charged) before the loan is drawn down. For products with automatic policy loan facility, policy holders should be immediately notified that a loan has been first drawn down in accordance with the policy provisions and the interest rate being charged. Whenever there are changes to the policy loan interest rate, policy holder should be notified within a reasonable period before the new interest rate is effective. For ongoing disclosure, regular account statements to be sent to policy holders should contain information about the interest rate being charged, opening and ending loan balance as well as the interest amount charged in the period, with the relevant information highlighted to draw policy holders' attention.

6.8 For policies to be used as collateral assignment (e.g. for premium financing), authorized insurers should ensure that the policy holder fully understands the relevant risks and limitations (e.g. interest rate risk, rights that the assignee may exercise on the policy on behalf of the policy holder, risk of release of information to the assignee).

6.9 Authorized insurers have the sole responsibility of ensuring accuracy of the product information vis-a-vis the policy provisions, with warning statements and other tools (e.g. FAQs) where appropriate to increase customers' awareness.

7. Suitability Assessment

7.1 Authorized insurers should obtain adequate information from customers for assessing their insurance demands and needs, before giving advice or concluding a contract. The information from customers will vary according to the type of product but will typically include:

(a) financial knowledge and experience;
(b) needs, priorities and circumstances;
(c) ability to afford the product; and
(d) risk profile.

7.2 Customers' needs should be properly assessed through the Financial Needs Analysis ("FNA") (where appropriate) set out in the Guideline on Financial Needs Analysis (GL30). Insurance policies should not be marketed to customers before their needs are properly analyzed.

7.3 Customers that have indicated their insurance needs should be presented with different options that are available to meet their specific needs and financial circumstances.

7.4 For insurance products with long term contribution commitment or investment elements, suitability assessment should include assessing the premium payment horizon, with due regard to the financial circumstances, planned retirement age etc. of customers.

7.5 The suitability assessment should be carried out whenever there are relevant changes to the circumstances of customers.

7.6 Authorized insurers have the duty to verify all available information and assess whether a particular product is suitable for the needs of customers during the underwriting process.

7.7 Authorized insurers should endeavour to reduce the risk of selling products that do not meet the needs of customers by:

(a) strengthening the training of licensed insurance intermediaries;
(b) assessing the affordability and suitability of products for customers during the underwriting process based on available information; and
(c) providing tools for licensed insurance intermediaries to facilitate the recommendation of suitable products to customers.

8. Advice to Customers

8.1 Authorized insurers and licensed insurance intermediaries should act with due skill, care and diligence when dealing with customers. They should have controls and processes in place to achieve this outcome, including appropriate measures to ensure that their employees, agents and technical representatives meet high standards of ethics and integrity.

8.2 Where advice is given to a customer, it should go beyond simply providing product information and constitute a personalized recommendation that takes into account the disclosed needs and circumstances of the customer in relation to the product.

8.3 After a customer has considered the options and is preparing to enter into an insurance contract, he/she should be properly apprised of all product features, including fees and charges (where applicable), surrender penalties (if any) as well as the product risks, key exclusions, 21-day cooling-off period etc.

8.4 A flowchart of the process encompassing completion of the FNA (if applicable),

confirmation of needs, comparison of different options (where FNA has been performed), and explanation of the key product features/exclusions is at the **Annex**.

9. Appropriate Remuneration Structure

9.1 Authorized insurers should ensure that the remuneration structure of licensed insurance intermediaries do not create misaligned incentives for them to engage in mis-selling, aggressive selling, fraudulent acts or money laundering activities.

9.2 Indemnity commission or any standing arrangements that offer advance payment of commission is strictly prohibited. In other words, authorized insurers should only pay commission on an earned basis.

9.3 Since misconduct, such as proven cases of mis-selling, aggressive selling, fraud and money laundering, often surfaces after the clawback period, authorized insurers should install a clawback mechanism to fully recover all commission paid in such proven cases.

10. Ongoing Monitoring

10.1 Authorized insurers and licensed insurance intermediaries should take all reasonable steps to identify, avoid and properly manage any conflicts of interest.

10.2 Making appropriate disclosures or obtaining informed consent from customers are helpful but have inherent limitations. Where conflicts of interest cannot be managed satisfactorily, authorized insurers or licensed insurance intermediaries should decline to act.

10.3 Authorized insurers should take all reasonable steps and put in place a proper mechanism to identify, avoid and properly manage conflicts of interest on an ongoing basis.

10.4 Authorized insurers are required to:

(a) service a policy appropriately until all contractual obligations have been satisfied; and
(b) disclose to the policy holder any contractual changes during the contract lifespan and other useful information depending on the type of product procured.

10.5 Authorized insurers should maintain the communication with policy holders at least annually as an integral part of expectation management (e.g. projections for

non-guaranteed benefits in anniversary statements).

10.6 Authorized insurers should take active steps to detect market response and experience (e.g. pattern of public complaints, lapsation rate) after launch.

11. Post-sale Control

11.1 Authorized insurers and licensed insurance intermediaries should establish, implement and monitor controls and procedures to achieve fair treatment of customers.

11.2 For the protection of vulnerable customers[3], authorized insurers are required to make audio-recorded post-sale confirmation calls if long term insurance products (except term insurance) or products with investment risks are involved. Authorized insurers are required to conduct post-sale confirmation calls within 5 working days of the date of policy issuance to ascertain that the customers understand the product procured and associated risks of the product, and are fully aware of their contractual rights and obligations.

11.3 Authorized insurers are required to:

(a) appoint a separate quality assurance team to make the post-sale confirmation calls;
(b) use their best endeavours to make the post-sale confirmation calls by reaching out to customers at different times of the day and different days of the week; and
(c) if post-sale confirmation calls are unsuccessful, send a confirmation letter alongside an email/SMS alert to draw the attention of the customers to the importance of the confirmation letter.

11.4 For customers who are visitors or who may be difficult to reach via post-sale confirmation calls, authorized insurers are encouraged to adopt alternative measures such as on-site recording at the service centre or immediate "dial-in" to or from the call centre.

11.5 Authorized insurers should collect sufficient information to enable them to identify vulnerable customers.

11.6 Authorized insurers are required to put in place an effective mechanism to identify possible cases of licensed insurance intermediaries abetting customers to evade the control measures, such as an abnormally high rate of unsuccessful post-sale calls.

[3] A vulnerable customer is a person aged 65 or older, whose education level is "primary level" or below, or who has no regular source of income.

11.7 Authorized insurers should have the internal controls and monitoring, which include retaining policy documents, records of the post-sale confirmation calls, confirmation letters and email/SMS alerts, as well as related control reports for quality control and monitoring.

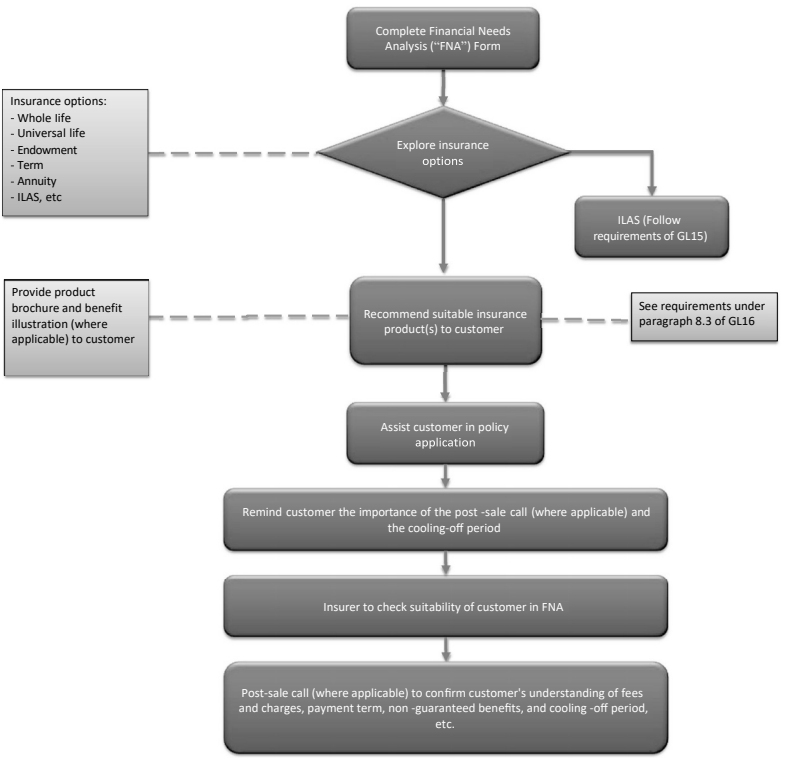
12. Commencement

12.1 This revised Guideline supersedes the previous version of this Guideline, and shall take effect from 31 March 2026, except that compliance with section 4 of the Guideline on Governance and Management of Fund(s) of Participating Business (GL34) as referred to in paragraph 2.2 of Appendix 2, shall take effect from 30 June 2026.

February 2026

Annex

Selling Process of Non-linked Insurance Products



Appendix 1

Requirements Applicable to Participating Policies

1. For the purpose of this Guideline, participating business has the meaning given by section 21B(11) of the Ordinance.

2. Expectations and considerations relating to the disclosure of participating policies[4] are elaborated in this Appendix. It should be read in conjunction with other relevant codes, circulars or guidelines issued by the IA.

3. Provision of Benefit Illustration

3.1 The purpose of benefit illustration is to provide customers with projected future performance which is broken down into guaranteed and non-guaranteed benefits, showing the benefits that may reasonably be expected in each policy year, based on specified assumptions and conditions.

3.2 High and low return scenarios must be provided in the benefit illustration to show the range of projected future performance and a wider range of scenarios is expected for investment strategy with higher volatility.

3.3 The benefit illustration should show the annual dividend (or reversionary bonus) and terminal dividend (or terminal bonus) separately, together with other information for customers to understand the implications on dividend/bonus if there are changes in, say, the underlying assumptions (e.g. the terminal dividends/bonuses may be more volatile than annual dividends/bonuses upon change in return assumption).

3.4 Authorized insurers should follow the requirements outlined in the Guideline on Benefit Illustrations for Long Term Insurance Policies (GL28).

4. Disclosure of Non-Guaranteed Benefits

4.1 Apart from benefit illustrations, an authorized insurer is required to make the

[4] Authorized insurers should refer to the Guideline on Governance and Management of Fund(s) of Participating Business (GL34) regarding the requirements on governance and corporate policy relating to applicable participating funds (as defined under paragraph 2.1 of GL34).

following disclosures:

(a) at the point of sale:
  (i) key factors that will significantly affect the determination of dividends/bonuses, including but not limited to:
    (aa) claims – mortality and morbidity experience;
    (bb) interest rate – interest income, outlook of interest rates and effects of capital gains and losses;
    (cc) market risks – types of market risks (including emerging or evolving risks) that could adversely impact investment outcome significantly;
    (dd) expenses – direct expenses (such as commission, underwriting, issuance and maintenance costs) and indirect expenses (such as general overheads); and
    (ee) persistency – lapsation rate and surrender experience; and the corresponding impact on investments;
  (ii) investment strategy (e.g. target asset and currency mix / geographical allocation / use of derivatives and securities lending), asset classes (e.g. equities, bonds, deposits) and concentration (e.g. sovereign and corporate bonds, high yield bonds);
  (iii) the objectives of the investment strategy;
  (iv) philosophy of determining dividends/bonuses (in the product brochure) which is also available on the authorized insurer's website;
  (v) fulfillment ratios (which represents the average ratio of non-guaranteed dividends/bonuses declared against amounts illustrated at the point of sale) for each product series which has new policies issued since 2010 and in-force policies during the reporting year, unless otherwise agreed by the IA, and the website where these fulfillment ratios can be found;
  (vi) appropriate details of fulfillment ratios based on the benefits associated with each product type, as follows:
    (aa) annual dividends (including accumulated dividends and interest);
    (bb) reversionary bonus (including the cash value of accumulated reversionary bonus); and
    (cc) terminal dividend/bonus (including the payout of a terminal dividend or cash value of a terminal bonus); and
  (vii) a statement that historical trend is not an accurate indicator of future performance;

(b) during the policy lifespan:
    (i) maintain timely communication with policy holders at least annually (or more frequently upon anticipated changes to benefits) on both actual non-guaranteed benefits declared for the year and a refreshed up-to-date in-force re-projection illustration reflecting the latest conditions and outlook to manage expectations of policy holders; and
    (ii) inform policy holders of any change of dividends/bonuses (or philosophy of their determination) by written communication or information contained in the annual statements with explicit reasons leading to the change;

(c) for premium offset options with the use of non-guaranteed dividends/bonuses to pay a portion of future premiums:
    (i) present scenario analysis covering, especially the situation where the premiums cannot be fully offset by declared dividends;
    (ii) remind customers that they have contractual obligation to make timely premium payment for the prescribed policy lifespan, while "vanish", "vanishing premium" or similar terminologies suggesting that the policy has been fully paid up should not be used;
    (iii) where declared dividends are used to pay premiums for medical riders, alert customers the risk brought about by medical inflation and premium increase, and/or dividend fluctuations and update them regularly through effective means; and
    (iv) if the product offers a variety of premium payment terms, mention the shorter payment term only as an alternative, warn customers that sustainability of the premium offset option depends on dividend payment which is not guaranteed, that they may have to resume premium payments as a result, and that other factors including dividend withdrawals, change in dividend options and addition of optional policy benefits should not be overlooked;

(d) for the illustration of withdrawal option or partial surrender option, a warning that withdrawal or partial surrender will affect future benefits and the disclosure to ensure that the customers fully understand the risk involved (e.g. illustrated withdrawal amounts, which depend on non-guaranteed dividends, might not be sustainable).

Appendix 2

Requirements Applicable to Universal Life Policies

1. Introduction

1.1 For the purpose of this Guideline, universal life business has the meaning given by rule 2 of the Insurance (Valuation and Capital) Rules (Cap. 41R).

2. Governance of Universal Life Business

2.1 Authorized insurers should establish governance frameworks on the determination of crediting interest rates, cost of insurance charges, fees and charges, as well as other discretionary benefits. These frameworks should be clearly documented, approved by the Board and made available to the IA upon request.

2.2 In addition to complying with this Guideline, authorized insurers should apply paragraphs 3.1, 3.2, 3.5, 3.6 and 3.7, and also section 4 of the Guideline on Governance and Management of Fund(s) of Participating Business (GL34), with modifications for the universal life context where relevant and applicable, to the governance and corporate policies in relation to universal life business referred to in paragraph 2.1 of this Appendix.

3. Provision of Benefit Illustration

3.1 The purpose of benefit illustration is to provide customers with projected future performance, including the total benefits payable under different scenarios. The illustration should show the benefits that may reasonably be expected in each policy year, based on specified assumptions and conditions.

3.2 In the benefit illustration, all fees and charges (current and maximum scales, if applicable) should be shown clearly, with an explicit message that the current fees and charges could be subject to change.

3.3 Authorized insurers should follow the requirements outlined in the Guideline on Benefit Illustrations for Long Term Insurance Policies (GL28).

4. Disclosure of Non-Guaranteed Benefits

4.1 Authorized insurers should follow paragraphs 4.1(a) and 4.1(b) of Appendix 1 on disclosure of non-guaranteed benefits with suitable modifications for the universal life policies context, except for paragraph 4.1(a)(v) and 4.1(a)(vi) where the related disclosures are not required. For example, terminology may be modified from "dividend/bonus" to "crediting interest rate".

4.2 Authorized insurers should disclose on their websites the historical crediting interest rates for each product series which has new policies issued since 2010 and in-force policies during the reporting year, unless otherwise agreed by the IA. Customers should be informed of the relevant website address.

4.3 In addition, key risks applicable to universal life policies (including fees and charges, lapsation risk due to zero account value etc.) and different crediting interest rates for each product series (if applicable) should be disclosed.

GL34

GUIDELINE ON
GOVERNANCE AND MANAGEMENT OF FUND(S) OF PARTICIPATING BUSINESS

Insurance Authority

Contents **Page**

1. Introduction

1.1 This Guideline is issued pursuant to section 133 of the Insurance Ordinance (Cap. 41) ("the Ordinance") and sets out the Insurance Authority's ("IA") expectations for sound and prudent business practices to be implemented and followed by authorized insurers in establishing and maintaining funds in respect of participating business. This Guideline also takes into account the Guideline on Underwriting Long Term Business (other than Class C Business) (GL16) issued by the IA, and the Insurance Core Principles, Standards, Guidance and Assessment Methodology ("ICP") promulgated by the International Association of Insurance Supervisors, in particular ICP 19 which stipulates that in their conduct of insurance business, insurers should treat their customers fairly.

1.2 Pursuant to section 21B of the Ordinance, participating business refers to any long term business in relation to which a policy holder has a right to receive, at the discretion of the insurer, a financial benefit that is determined based on a profit-sharing mechanism as a share of the insurer's profits in respect of the insurer's business or a part of the insurer's business. An authorized insurer must maintain at least 1 separate account and 1 separate sub-fund for its participating business ("participating fund"). Insurers should always uphold the principle of equitable and fair treatment of customers in managing a participating fund.

1.3 Whenever an authorized insurer exercises its discretion in the management of its participating business, it should pay due regard to the interests of policy holders. It should also take reasonable care to ensure the policy holders are treated fairly and the participating business is managed in a sustainable manner. It should not provide any undisclosed, or otherwise unfair, advantage to shareholders or to other stakeholders of the participating fund(s).

1.4 This Guideline focuses on the minimum standards and practices for governance of participating funds. An authorized insurer to which this Guideline applies should clearly document the manner in which this Guideline is complied with in its corporate policy on governance of the participating business, as approved by its Board of Directors ("Board") and demonstrate its adherence to such corporate policy to the IA upon request.

The IA may require the insurer to appoint an independent person to assess whether the policy has been applied consistently, effectively and fairly.

1.5 It is the duty of the controllers (as defined in section 13A(12) of the Ordinance) of an authorized insurer to ensure the insurer observes the requirements set out in this Guideline in carrying out any participating business. Further, it is the duty of the Board to maintain adequate oversight over the implementation of measures in compliance with this Guideline and, having fully considered the advice of the actuary appointed by the insurer in relation to its long term business under section 15AAA(1)(a) or (b) of the Ordinance ("Appointed Actuary"), the Board is ultimately responsible for ensuring fair treatment of customers.

1.6 A failure to comply with or any circumvention of the requirements in this Guideline may adversely impact on the IA's opinion of the continued fitness and properness of the controllers and directors of the authorized insurer in question. The IA may also take guidance from this Guideline in considering whether there has been an act or omission by an insurer that is likely to be prejudicial to the interests of policy holders or potential policy holders (albeit the IA will always take account of the full context, facts and impact of any matter before it in this respect). The IA may also take account of the standards and practices in this Guideline in considering whether grounds exist to exercise any intervention powers under the Ordinance, including the appointment of a skilled person to prepare a report pursuant to section 32A of the Ordinance.

1.7 Save as otherwise expressly stated –

(a) terms defined in the Ordinance and its subsidiary legislation shall have the same meaning when used in this Guideline; and
(b) authorized insurers should continue to observe GL16.

2. Scope and Application

2.1 This Guideline applies to authorized insurers in respect to the participating funds they maintain under section 21B of the Ordinance which comprise

the participating business they carry on in Hong Kong [1] (hereinafter referred to as ***"applicable participating funds"***), unless otherwise specified. It does not apply to non-HK insurers which (a) have ceased accepting any new insurance business in Hong Kong (i.e. run-off non-HK insurers), and (b) have been granted by the IA a permission under section 22A or a permission for being exempted from this Guideline.

2.2 Without prejudice to paragraph 2.1, where an authorized insurer carries on participating business both in and outside Hong Kong, the insurer may choose whether to establish and maintain 1 participating fund or more than 1 participating funds under section 21B of the Ordinance based on the circumstances of its business and operations and taking into account its corporate policy on identifying assets to support its participating business and defining its profit-sharing mechanism.

2.3 An authorized insurer should apply the level of granularity that is fit for the purpose of defining its profit-sharing mechanism so long as the mechanism is incorporated in its corporate policy on governance of the participating business as approved by its Board. Such level of granularity does not necessarily need to be the same as that required to meet the requirements in section 21B of the Ordinance or that used for the purpose of determining the MA portfolios under the Insurance (Valuation and Capital) Rules (Cap. 41R).

3. Governance of Participating Business

3.1. The Board of an authorized insurer carrying on participating business is ultimately responsible for the management and oversight of the participating business. In determining policy holders' reasonable expectations, declaring dividends/bonuses, and addressing other aspects of the applicable participating funds, the Board should duly consider the principle of fair treatment of customers, and equitably balance the interests of shareholders and policy holders.

[1] In other words, this Guideline does not apply to a participating fund which does not comprise any participating business carried on in Hong Kong.

3.2. When designing products that include non-guaranteed benefits, it is the Appointed Actuary's duty to ensure that the projected non-guaranteed returns are reasonably achievable. The Appointed Actuary should therefore define the underlying philosophy for determining non-guaranteed benefits, clearly articulate the associated assumptions and advise the Board accordingly.

3.3. At the same time, each authorized insurer is required to establish a Participating Business Committee ("PBC") to provide independent and objective advice to the Board in respect of applicable participating funds, including but not limited to advice on recommendations made by the Appointed Actuary on the allocation of distributable surplus/profits and declaration of dividends/bonuses. The PBC should operate independently and report directly to the Board, so as to support informed decision making by the Board which takes into account the principle of fair treatment of customers and equitable balance between shareholders and policy holders.

3.4. The Board should seek and consider advice from the PBC when making decisions on key matters related to the management of participating business.

Role and Responsibilities of Appointed Actuary

3.5. The Appointed Actuary plays a critical role in ensuring the fair and sustainable management of participating business. Thus, the Appointed Actuary should advise the Board on the exercise of discretion with respect to the management of participating business, including the interpretation of reasonable expectations of policy holders and fair treatment of customers.

3.6. The Appointed Actuary should report to the Board, at least annually, and more frequently if required, recommending the allocation of distributable surplus/profits [2] and the declaration of dividends/bonuses and other discretionary benefits, and providing a written opinion to the Board on the allocation of expenses and charges [3], addressing the considerations

[2] Please refer to section 8 of this Guideline.
[3] Please refer to section 7 of this Guideline.

regarding the exercise of the Board's discretion mentioned in paragraph 3.5. At a minimum, the following items should be covered:

(a) consistency of the exercise of discretion with the corporate policy on governance of the participating business;
(b) potential impact of the exercise of discretion on the interests of the policy holders;
(c) whether the recommendation or allocation may adversely impact the sustainability of the participating business; and
(d) any deviations from information previously communicated to existing or potential policy holders (including but not limited to benefit illustrations) resulting from the recommendation or allocation.

3.7. The Appointed Actuary's communications and reports to the Board should be made available to the IA upon request.

Composition of PBC

3.8. Subject to paragraph 3.10, the PBC should consist of at least 3 members. To ensure a balanced and effective governance structure:

(a) at least half of the PBC members should be independent of the authorized insurer;
(b) the chairperson of the PBC should be an independent member;
(c) the PBC should include members with an adequate spread of skills, knowledge and relevant experience[4]; and
(d) authorized insurers should ensure that the size and composition of the PBC is commensurate with the scale, complexity and risk profile of the applicable participating funds.

3.9. The Board should assess the independence of PBC members, considering their character and judgment, and whether there are relationships or circumstances which may affect, or appear to affect, their objectivity or impartiality. The IA is not likely to be satisfied that a PBC member is

[4] Examples of relevant skills, knowledge and experience include actuarial, legal, investment, risk management, accounting, finance, etc.

independent if, within the past 3 years, the member:

(a) has been or is a shareholder controller[5] of the authorized insurer;
(b) has been or is an employee or director (including an independent non-executive director ("INED")[6]) of either the authorized insurer, a shareholder controller[7] of the insurer, or an entity of the group of companies (within the meaning given by section 2(1) of the Companies Ordinance (Cap. 622)) to which the insurer belongs;
(c) has received or receives any variable remuneration from the authorized insurer in relation to the insurer's business performance, has participated or participates in the insurer's share option or a performance-related pay scheme, or has been or is a member of the insurer's pension scheme that is linked to the insurer's business performance;
(d) has had or has a material business relationship[8] with the authorized insurer either directly, or as a partner, shareholder, director or senior management of a body that has such a relationship with the insurer;
(e) has had or has significant links with the authorized insurer's directors through involvement in other entities, including but not limited to common directorships, shareholding or partnership in such entities, which are likely to impair the member's independence;
(f) has close family ties[9] with any of the persons set out in paragraphs (a) to (e);
(g) has been or is a PBC member of the authorized insurer for more than 9 consecutive years, measured from the date of their first appointment in any continuous period of service, including any

[5] Within the meaning given by section 2(1) of the Ordinance.
[6] A director (including INED) owes a fiduciary duty to the authorized insurer to act in the best interests of the insurer and its shareholders which potentially conflicts with the role and responsibilities of the PBC.
[7] Within the meaning given by section 2(1) of the Ordinance.
[8] A business relationship is likely to be considered material if the person or the authorized insurer directly or indirectly obtains financial benefits from the relationship, which cumulatively constitute a material portion of the revenue of that person or the insurer. For this purpose, a materiality threshold (for example, 15%) may be applied, as determined by the insurer. For the avoidance of doubt, serving as a PBC member does not, by itself, constitute a material business relationship.
[9] Close family members of a person are those who may influence, or be influenced by, that person in their dealings with the entity, and include:
(a) that person's parents, children, siblings, or spouse/domestic partner;
(b) children of that person's spouse/domestic partner; and
(c) dependents of that person or of that person's spouse/domestic partner.

sequence of consecutive appointments and disregarding any break in service of less than the cooling off period of 3 years[10]; or

(h) has been or is subject to any other circumstances that may give rise to a conflict of interest in relation to the roles and responsibilities of the PBC.

3.10. If an authorized insurer's total amount of insurance liabilities (gross of reinsurance) for all applicable participating funds is less than HKD 1 billion as at 30 September 2025, or if they initially exceed HKD 1 billion but subsequently decline below this threshold for 4 consecutive reported quarters after 30 September 2025, the insurer may appoint a PBC consisting of two members or replace the PBC with a person acting as a Participating Business Advisor ("PBA"). In either case, the PBA or at least one PBC member should be an independent member who satisfies the independence assessment under paragraph 3.9 or an INED. If an insurer's total insurance liabilities (gross of reinsurance) for applicable participating funds increase to HKD 1 billion or above for 4 consecutive reported quarters following 30 September 2025, the insurer is required to establish a PBC in accordance with paragraphs 3.8 and 3.9 within 6 months after the end of the fourth quarter.

Appointment of PBC members

3.11. The Board of an authorized insurer is responsible for appointing PBC members. In doing so, the Board should consult the chairperson of the PBC on the appointment of other PBC members to ensure that the PBC, as a whole, has an appropriate balance of different skills, knowledge and experience[11] in areas relevant to the management of participating business, as needed for the effective functioning of the PBC. The chairperson of the PBC should have sufficient experience and independence to guide the committee effectively and facilitate balanced and objective decision-making. Where a PBA is appointed, the Board should satisfy itself that the

[10] This means that breaks in service of less than 3 years are not included in the counting of consecutive years and also do not affect the continuity of service. However, a break of 3 years or more resets the clock and restarts the counting of years of continuous service. For example, if an individual serves as a PBC member for 6 years and takes a 2-year break (which is disregarded because it is less than 3 years), they can be re-appointed for up to 3 more years to make up the total of 9 consecutive years. However, after 9 consecutive years (measured in this way) have been served, a cooling-off period of at least 3 years must be observed before the individual may be appointed again as an independent PBC member.

[11] See footnote 4 above.

person has the appropriate skills, knowledge and experience needed to effectively discharge the responsibilities associated with the role.

3.12. An authorized insurer should establish policies and procedures for the nomination, appointment and tenure of PBC members. PBC members should be appointed for a fixed term, typically 3 years, with the possibility of reappointment. If a PBC member is appointed, or a PBC member's appointment ends before completion of the full term, the insurer should notify the IA within 1 month after the appointment date or the termination date, as the case may be. In the case of termination of an appointment before completion of the full term, the insurer should provide reasons for early termination and a replacement plan.

3.13. While prior approval from the IA is not required, the IA may raise an objection to the appointment of a PBC member if it deems the member unsuitable for fulfilling the responsibilities. Before raising an objection by written notice served on the authorized insurer, the IA will first discuss its intention to object and reasons for the objection with the insurer and the PBC member, further to which the insurer and the PBC member may, either jointly or separately, make written or oral representations to the IA. Any representations made will be taken into account by the IA before serving a notice of objection on the insurer.

3.14. In exceptional circumstances where the number of PBC members temporarily falls below the requirement under paragraph 3.8, the authorized insurer should seek approval from the IA for a temporary exemption, supported by valid justification. The exemption period will be determined on a case-by-case basis.

Role and responsibilities of PBC

3.15. An authorized insurer should establish clear terms of reference for the PBC containing, at a minimum, terms which set out the role, responsibilities and procedures of the PBC to assess, report, and provide advice to the Board on the insurer's management of its applicable participating fund (particularly the discretion exercised by the insurer), including, but not limited to, the relevant matters set out in paragraphs 3.16 and 3.18 to 3.21. The insurer should ensure that the terms of reference are up-to-date.

3.16. The IA expects the Board to seek and duly consider advice from the PBC on key matters relating to the management of applicable participating funds. In providing its advice, the PBC should consider whether policy holders are being treated fairly, having regard to the rights and interests of different groups, classes, or cohorts of policy holders. Having regard to the requirements under this Guideline, the PBC should consider the following key matters, at a minimum, in advising the Board:

(a) whether the level of future discretionary benefits provided in the benefit illustration is clear, fair and reasonably achievable;
(b) the policy and mechanism for allocation of distributable surplus/profits and dividends/bonuses declaration mechanism (including any smoothing mechanisms), taking into account reasonable expectations of policy holders (including but not limited to their expectations relating to reasonable achievement of discretionary benefits), fairness and equity, as well as sustainability;
(c) fairness, equity and reasonableness in allocation of expenses and charges to and within applicable participating funds;
(d) the risk and investment profile of applicable participating funds, including the appropriateness of the risk appetite and risk level taken, the management and reasonable balance of risk and return, etc.;
(e) the impact of any management actions planned or implemented[12];
(f) the authorized insurer's strategy for future sales of insurance policies in applicable participating funds and their impact on surplus;
(g) the use, purpose, and terms of any shareholder capital support to an applicable participating fund;
(h) the authorized insurer's communications with existing and potential policy holders relating to applicable participating funds, including fairness and transparency of disclosed information which may affect policy holders' decisions[13]; and
(i) any other issues which the authorized insurer or the PBC considers appropriate in relation to the insurer's management of its applicable participating fund.

[12] For example, a dividend adjustment that is made in addition to that based on the dividends/bonuses declaration mechanism prescribed by the authorized insurer.
[13] For example, information relating to risks and benefits.

3.17. An authorized insurer should provide the PBC with the resources it needs to perform its responsibilities effectively, including but not limited to:

(a) prompt notification to the PBC by the Board or management of the insurer of any material changes in business plans, practices (including risk and investment practices) or other circumstances which may affect the fair treatment of participating policy holders;
(b) adequate support from the insurer's internal resources and functions, access to external professional advice at the insurer's expense, and sufficient time to enable PBC members to give fully considered input on the issues to be considered by the PBC; and
(c) access to data and systems that the PBC reasonably requires, e.g. information relating to customers' complaints.

3.18. If the Board decides to deviate from the advice given by the PBC, the Board should inform the PBC. If the PBC considers that the deviation may adversely affect the interests or decisions of policy holders, the PBC should inform the Board accordingly and should notify the IA about the matter and how the interest of policy holders is affected as soon as practicable.

PBC Meetings and Reporting

3.19. The PBC should meet at least once per year and convene additional meetings as needed. A quorum for any meeting or decision to be made by the PBC requires at least half of the total number of PBC members, with at least half of the quorum being formed by independent members.

3.20. The PBC should report directly to the Board at least once per year, providing advice on the management of applicable participating funds and communication of relevant information to existing and potential policy holders. The report should cover matters discussed and resolved under paragraph 3.16, particularly those involving discretion exercised by the authorized insurer. The report should provide sufficient details to enable a reasonable reader to understand the issues raised by the PBC and the relevant outcomes to resolve the issues. The PBC's communications and reports to the Board should be made available to the IA upon request. Additionally, the PBC should directly respond to any inquiries from the IA concerning the performance of the PBC's functions.

3.21. To provide transparency, an authorized insurer should publish a description of the PBC's duties and an annual statement from the PBC on the insurer's website. This annual statement should cover, amongst others, a list of the PBC members and whether the PBC is satisfied that the insurer has exercised its discretion fairly and reasonably during the relevant reporting period. The PBC should determine the appropriate timing for publishing the annual statement, taking into account the review cycle of the dividends/bonuses determination. Please refer to **Annex 1** for a sample of such a statement. Insurers are expected to consider disclosing information regarding the establishment and duties of the PBC in other reports or communications with policy holders, such as their annual reports (if applicable), where doing so would enhance transparency.

3.22. Where an authorized insurer appoints a PBA in accordance with paragraph 3.10, the provisions of this section (paragraphs 3.3, 3.4, 3.9, 3.11 through 3.18, 3.20, and 3.21) relating to governance of participating business and the independence, appointment, role and responsibilities, reporting and disclosure requirements applicable to the PBC shall apply to the PBA, with necessary modifications to reflect the appointment of a single individual rather than a committee. References in these paragraphs to the PBC, its chairperson or members shall be read as referring to the PBA and the relevant processes or actions to be undertaken by that individual. For clarity, paragraph 3.19 regarding meetings and quorum does not apply to the PBA.

4. Corporate Policy in Relation to Participating Business

4.1. To ensure appropriate governance of participating business, an authorized insurer should establish a corporate policy in relation to participating business which covers the allocation of distributable surplus/profits between shareholders and participating policy holders, as well as the declaration of policy holder dividends/bonuses and other discretionary benefits. This policy should be clearly documented, approved by the Board and made available to the IA on request. The corporate policy should be clearly indicated as such and could comprise a single document or a set of documents.

4.2. At a minimum, the policy in relation to applicable participating funds should take into account the input of the Appointed Actuary and the PBC or the PBA, as the case may be, and cover:

(a) a description of the parties involved in the management of participating business, e.g. the Board, the Appointed Actuary, the PBC or the PBA, as the case may be, the investment committee (if any), etc., and their respective roles and responsibilities;
(b) the overall philosophy in setting non-guaranteed policy benefits, including the sharing of surplus/profits or experience, smoothing and guarantees;
(c) maintenance of the principle of fairness between different products and generations;

<u>Dividends/bonuses declaration mechanism</u>

(d) the approach to sharing surplus/profits or experience, including the items to be shared and their quantification (if any);
(e) the methodology used to define the scope and derive the value of the underlying pool of assets for the purpose of dividends/bonuses determination;
(f) application of the principle of fairness to the determination of dividends/bonuses[14], covering:
    (i) whether and how dividend/bonus classes are set at policy issue and whether they can be adjusted afterward;
    (ii) consistency in the treatment of policy holders with similar characteristics within the same dividend/bonus class;
    (iii) whether there is any undue or material cross-subsidization among different dividend/bonus classes;
    (iv) whether the materiality in dividends/bonuses determination is judged from the point of view of each dividend/bonus class (even if this represents a relatively small block of business), as opposed to the point of view of the total participating fund;
    (v) whether dividends/bonuses declaration mechanisms are consistent from the product design stage through the life of relevant insurance policies; and

[14] Authorized insurers should be able to demonstrate how the principle of fairness is applied upon request from the IA.

(vi) any other considerations that have been taken into account in applying the principle of fairness;

Allocation of distributable surplus/profits

(g) documentation requirements relating to the allocation of distributable surplus/profits as set out in section 8 of this Guideline, including but not limited to, the basis and justification for allocating distributable surplus/profits from the part of long term business for which each applicable participating fund is maintained, to policy holders and shareholders and among different groups of policy holders;

Expenses and charges

(h) documentation requirements for the expenses and charges set out in section 7 of this Guideline, including, but not limited to, justification for more complex charges such as charges for guarantees or capital; justification as to whether a charge is incurred for operating an applicable participating fund or should be considered as profit in nature (and thus subject to the requirements set out in section 8 of this Guideline); and the basis and justification for allocating expenses and charges to an applicable participating fund, as well as among the sub-funds or cohorts within an applicable participating fund;

Smoothing

(i) the methodology for smoothing payouts, which should be explained with quantitative justification of the following:
   (i) whether it is expected to be on average cost-neutral to shareholders and policy holders, or to not adversely impact policy holders' interests;
   (ii) whether the volatility of payouts is genuinely reduced;
   (iii) whether it significantly impacts on the sustainability of the applicable participating fund and the authorized insurer; and
   (iv) whether it operates fairly for all policy holders, or results in any undue or material cross-subsidization among different dividend/bonus classes;

Management of assets

(j) investment strategy, including ongoing management of the asset mix, the policy on the use of derivatives or other tools, the policy on making a loan to or investment in any other related companies and the policy on investment in new asset classes including prior approval arrangements for such investments;

(k) the asset and liability matching strategy and management of applicable participating funds or sub-funds of applicable participating funds where appropriate;

(l) documentation requirements for how the assets are held and the physical segregation of assets as set out in section 10 of this Guideline, including, but not limited to, maintaining separate custodian/bank accounts, earmarking assets which are exempted from physical segregation requirements under applicable participating funds, designating an approving authority for the transfer of assets out of applicable participating funds, and procedures and controls for the settlement of interfund balances;

Risk management

(m) the policy on risk management, covering the exposure of applicable participating funds to business risks and the potential implications for policy holders, particularly any risks disproportionately affecting policy holders as compared to shareholders and how those risks are managed;

New business

(n) considerations when writing new business into applicable participating funds (or sub-funds), including:

  (i) whether there will be any material adverse impact on existing policy holders' interests;

  (ii) how new business strains will be supported, e.g. by using surpluses from in-force policies, or by injecting additional capital into the relevant applicable participating fund, etc.; and

  (iii) whether new business strains will unduly impact the sustainability of the applicable participating fund or the authorized insurer;

(o) actions that the authorized insurer would take if it ceases to take on new business, and an assessment of the impact on the interests of existing policy holders, particularly with respect to the continuing allocation of expenses, charges and the transfer of surplus/profits;

(p) documentation requirements for capital support as set out in section 9 of this Guideline, including any terms and conditions governing its use and withdrawal;

Communications with existing and potential policy holders

(q) the principles and practices applied in determining the projected non-guaranteed benefits of a standard benefit illustration at the point of sale and in in-force re-projection illustrations, potentially including additional information regarding the profit sharing ratio between shareholders and the participating policy holders;

(r) measures to manage the potential conflict between the authorized insurer's duty to policy holders and its duty to shareholders, particularly in relation to the declaration of dividends/bonuses for policy holders; and

(s) the authorized insurer should provide information about the principles and practices under paragraph (q) and the measures under paragraph (r), either in the product brochure or in a separate leaflet provided to customers at the point of sale, or on its website (with a link to the website address included in the product brochure).

4.3. Authorized insurers should review their policy in relation to participating business at least once per year to ensure that the policy remains appropriate, taking into account the development of risks and the profiles of the funds, the market environment, product sustainability, evolving best practices and other relevant considerations.

4.4. The authorized insurer's policy in relation to applicable participating funds, including its dividends/bonuses declaration mechanism, should be made available to the IA for regulatory review. The IA may require the insurer to appoint an independent party at the insurer's expense to assess and report to the IA directly on whether the policy has been applied completely, consistently and fairly.

5. Identification of Assets and Liabilities

5.1 For the purpose of establishing and maintaining a participating fund, an authorized insurer is required to identify the assets and liabilities attributable to the participating business.

5.2 An authorized insurer should have regard to the nature of each distinguishable part of its long term business when determining whether such insurance liabilities are attributable to its participating business.

5.3 Any riders, funds on deposit or prepaid premiums attached to a base policy of any long term business should be considered separately from the base policy. However, if according to the profit-sharing mechanism, the riders, funds on deposit or prepaid premiums are expected to have any substantive impact [15] on the dividends/bonuses determination of the participating policies, such riders, funds on deposit or prepaid premiums should be classified as part of the participating business. In such cases, the requirements of this Guideline are applicable to such riders, funds on deposit or prepaid premiums.

5.4 Pursuant to section 22 of the Ordinance, an authorized insurer must maintain books of account and other records necessary to identify the assets representing each participating fund maintained under section 21B of the Ordinance and to identify the liabilities attributable to the part of its business for which the participating fund is maintained. (See section 10 for the physical segregation requirements.)

5.5 The Board, having fully considered the advice of the Appointed Actuary, should certify that the authorized insurer has on 1 July 2024 (i.e. the commencement date of Insurance (Amendment) Ordinance 2023) identified the assets and liabilities attributable to the part of its business for which each applicable participating fund is maintained, having regard to the principles set out in paragraphs 5.1 to 5.4.

[15] It should be based on the principle of substance over form, taking into consideration the occurrence and amount of the impact.

6. Opening Balance

6.1 On 1 July 2024, an authorized insurer should ensure that the opening balance of assets in an applicable participating fund is no less than the amount of assets that is attributable to that participating business on the date immediately before 1 July 2024, having taken into account the underlying pool of assets as reflected in the established profit-sharing mechanism for dividends/bonuses determination.

6.2 When determining the opening balance of an applicable participating fund, any changes made by an authorized insurer since 1 January 2019 to the basis for determining the amount of assets attributable to the participating business and any one-off distributions made by an insurer since 1 January 2019 from the participating business, that serve to accelerate the release of surplus asymmetrically to shareholders prior to 1 July 2024 would be considered to be an exceptional case. The insurer should seek opinion from an external independent person about the change of basis and/or the one-off distribution in accordance with paragraph 11.10.

6.3 From 1 July 2024 onwards, if the amount of assets in an applicable participating fund is insufficient to cover the liabilities attributable to that participating business, having regard to the requirements under this Guideline and section 22 of the Ordinance, the authorized insurer should promptly transfer additional assets into the fund to make good the deficit. The insurer should also comply with the requirements relevant to capital support as set out in section 9 of this Guideline.

6.4 The Board, having fully considered the advice of the Appointed Actuary, should certify the sufficiency of the opening balance of each applicable participating fund, having regard to the principles set out in paragraphs 6.1 to 6.3.

7. Expenses and Charges

7.1 The allocation of any costs by an authorized insurer, whether as expenses or charges, to an applicable participating fund, as well as within an applicable participating fund, e.g. among the sub-funds or cohorts, or

between in-force and new business, has to be fair, equitable and reasonable. The allocation is considered fair, equitable and reasonable if:

(a) the allocation is in line with the interests of the relevant policy holders;
(b) the costs are necessary to cover the ongoing operations of the fund or sub-fund; and
(c) the costs are justified by the expected benefit to the relevant policy holders.

7.2 An authorized insurer may only allocate to an applicable participating fund costs which are incurred for operating the fund. This may include a fair and proportionate share of overheads attributable to the management of the participating business. Having regard to the principle of substance over form, charges that are not commensurate with the costs of operating the participating business are considered as profit in nature and should be treated as allocations of distributable surplus/profits to shareholders (thus subject to the requirements set out in section 8). An insurer should perform appropriate analysis to ascertain whether the charges are commensurate with costs that are required for operating the participating fund. The cost analysis performed should be proportionate to the nature, scale and complexity of the charges[16].

7.3 In the case of allocating costs arising from related party transactions, an authorized insurer should assess whether such costs are charged at arm's length. Expenses or charges that are artificially inflated are considered not commensurate with the costs of operating the participating business. Attention should also be paid to the basis of allocating intragroup expenses.

7.4 The IA expects an authorized insurer to be able to justify any costs allocated to an applicable participating fund, based on appropriate analysis with proper documentation that demonstrates the expected benefit to the relevant policy holders if incurring such costs. Disproportionate expected benefit to the shareholders versus to the relevant policy holders may cast doubt on whether such costs incurred are genuinely necessary for the policy holders and if they are attributable to the participating fund.

[16] For instance, charges for guarantees and/or capital are considered as examples of more complex charges.

Attention should also be paid to whether any one-off or exceptional costs should be allocated to the participating fund.

7.5 An authorized insurer should not allocate to an applicable participating fund any costs that comprise, directly or indirectly, any of the following:

(a) fines or penalties imposed by the court, a regulatory authority or a law enforcement agency;
(b) expenses or charges incurred in relation to activities in breach of any regulatory requirements or that reflect inappropriate management of participating business, as assessed by the PBC or PBA, as the case may be, established in accordance with section 3 of this Guideline, including payments to a skilled person for preparing a report required by a regulatory authority where the report indicates that the insurer has, or may have, failed to satisfy its regulatory obligations; or
(c) payments of compensation or redress due to policy holders for any act or omission for which the insurer should be responsible.

7.6 The basis and justification for determining the allocation of expenses and charges to an applicable participating fund, as well as among the sub-funds or cohorts within an applicable participating fund, should be set out clearly in the authorized insurer's corporate policy and endorsed by its Board. Such policy should have regard to the principles set out in paragraphs 7.1 to 7.5 and map out a clear framework for assessing the nature of different types of expenses and charges.

7.7 The Appointed Actuary should, annually or more frequently if it is required, provide a written opinion to the Board on whether the expenses and charges are allocated to each applicable participating fund, or each sub-fund or cohort within an applicable participating fund, in a fair, equitable and reasonable manner, having regard to the principles set out in paragraphs 7.1 to 7.5.

7.8 An authorized insurer should demonstrate compliance with the principles set out in paragraphs 7.1 to 7.5 to the IA upon request.

8. Allocation of Distributable Surplus/Profits

8.1 In respect of each applicable participating fund, an authorized insurer should establish a clear framework for allocating distributable surplus/profits based on a defined profit-sharing mechanism. The allocation of distributable surplus/profits arising from the participating business to policy holders and shareholders, as well as among different groups of policy holders, should be:

(a) fair and equitable;
(b) in line with the reasonable expectations of policy holders;
(c) sustainable; and
(d) compliant with the corporate policy on governance of the participating business as approved by the Board.

8.2 Examples of allocation of distributable surplus/profits to participating policy holders include any payment of cash dividends/bonuses, payment of terminal dividends/bonuses, and declaration of reversionary bonuses in the form of a permanent addition to policy benefits.

8.3 Any allocation of distributable surplus/profits, arising from the part of long term business for which an applicable participating fund is maintained, to shareholders should be in line with the interests of policy holders. An authorized insurer should ensure a fair balance of risk and reward[17] between participating policy holders and shareholders, and among different groups of policy holders.

8.4 Further to the principles set out in paragraph 8.1, any distributable surplus/profits, arising from the part of long term business for which an applicable participating fund is maintained, should generally be allocated to policy holders and shareholders, as well as among different groups of policy holders, in a systematic and rational manner. An authorized insurer should strike an appropriate balance between ensuring fair payouts to

[17] For example, it would be questionable whether it is fair to the interests of the policy holders if participating policy holders bear most of the insurance/investment risks while shareholders are expected to receive a disproportionately high portion of the distributable surplus/profits through elevated fixed or upfront profit charges.

exiting policy holders and the security of benefits for continuing policy holders in an applicable participating fund.

8.5 An authorized insurer should not accelerate the distribution of surplus/profits from an applicable participating fund asymmetrically to shareholders [18], unless it can be ascertained that the distributions, individually or cumulatively, are unlikely to result in any material adverse effect on the security of policy holders' contractual rights and their reasonable benefit expectations, including the prospects of non-guaranteed benefits, or the financial soundness of the fund.

8.6 For any prior allocation of distributable surplus/profits to shareholders that is related to declared dividends/bonuses but yet to be transferred out of an applicable participating fund, the corresponding balance and subsequent transfers out of the fund should be tracked and reported to the IA on an annual basis.

8.7 The basis and justification for determining an allocation of distributable surplus/profits arising from the part of long term business for which each applicable participating fund is maintained, to policy holders and shareholders, as well as among different groups of policy holders, should be set out clearly in the authorized insurer's corporate policy on governance of the participating business as approved by its Board. Such policy should have regard to the principles set out in paragraphs 8.1 to 8.5, and provide sufficient details that allow the IA and any other knowledgeable independent reviewer to assess the insurer's ongoing compliance with those principles. Such policy should also be consistently applied from year to year and not be subject to arbitrary changes.

8.8 The Appointed Actuary should submit a report to the Board recommending an allocation of distributable surplus/profits arising from the part of long term business for which each applicable participating fund is maintained, annually or more frequently if it is required, and the recommendations should be justified based on the principles set out in paragraphs 8.1 to 8.5.

8.9 An authorized insurer should demonstrate compliance with the principles set out in paragraphs 8.1 to 8.5 to the IA upon request.

[18] Including any profit charges, referred to in paragraph 7.2, which accelerate shareholder distributions.

9. Capital Support

9.1 In cases where capital support is provided by shareholders to an applicable participating fund, the amount of the financial support provided, along with any terms and conditions governing its use and withdrawal, should be clearly documented with proper oversight and governance by the Board. In applying such oversight, the Board should always uphold the principle of fair treatment of customers.

9.2 Any capital support provided to an applicable participating fund may only be withdrawn, with the approval of the Board, having fully considered the advice of the Appointed Actuary.

10. Physical Segregation of Assets

10.1 Subject to paragraph 10.2, an authorized insurer is required to physically segregate assets attributable to the part of its business for which an applicable participating fund is maintained separately from its other long term business. At minimum, the physical segregation requirement applies to each of the applicable participating funds. An insurer may also, if it wishes, maintain multiple physically segregated sub-funds within one applicable participating fund, in line with its corporate policy on governance of the participating business.

10.2 If an authorized insurer's total amount of insurance liabilities (gross of reinsurance) of all applicable participating funds is less than HKD 1 billion as at 1 July 2024, the insurer is exempted from the requirement to physically segregate each of its applicable participating funds from its other long term business (albeit the insurer is encouraged to physically segregate each of its applicable participating funds for the sake of proper management of the fund). If the insurer's total amount of insurance liabilities (gross of reinsurance) of all applicable participating funds increases to HKD 1 billion or above for 4 consecutive reported quarters subsequent to 1 July 2024, the insurer is required to physically segregate each of its applicable participating funds from its other long term business within 6 months from the end of the fourth such reported quarter. Once an insurer has physically segregated its applicable participating fund(s), the

insurer should continue to maintain the physical segregation even if the amount of liabilities may subsequently fall below the HKD 1 billion threshold.

10.3 To avoid doubt, the requirements on establishing and maintaining participating funds under sections 21B to 23 of the Ordinance, together with the requirements under this Guideline (save for the requirements on physical segregation of assets) equally apply to those applicable participating funds which are exempted from the physical segregation requirements described in paragraph 10.2. Despite exemption from the physical segregation requirements, the relevant authorized insurer is still required to earmark [19] the assets attributable to each applicable participating fund at minimum, or at a more granular level (than at the participating fund level) for the purpose of determining dividends/bonuses.[20]

10.4 An authorized insurer should maintain separate custodian/bank account(s) to hold the assets for each of its applicable participating funds for physical segregation purposes. Where more than one custodian/bank account is established, the insurer should establish policies and mechanisms to clearly distinguish the accounts for each of its applicable participating funds. For non-HK insurers (other than designated insurers and those insurers being exempted under paragraph 2.1), custodian/bank accounts should be specifically identified as belonging to its Hong Kong branches, though they may take the form of sub-accounts of custodian/bank accounts maintained at the insurer's head office. The following assets[21] are exempt from being held in such custodian/bank accounts but should still be earmarked in the name of the relevant applicable participating fund(s) and properly recorded in the insurer's books and accounts:

- land and buildings directly held by the authorized insurer;

[19] "Earmark" refers to assigning or designating an asset for a specific purpose. Once the asset is earmarked for the purpose of supporting participating business, it should remain designated for such purpose unless changes arise from transactions.

[20] To avoid doubt, any MA portfolios of participating business without physical segregation are not eligible for applying the long term adjustment of the matching adjustment under rule 24 of the Insurance (Valuation and Capital) Rules (Cap. 41R).

[21] These assets are generally considered as unable to be held under custodian/bank accounts or unable to be split into separate custodian/bank accounts from other parts of the business due to regulatory or legal restrictions.

- loans and receivables;
- bonds under Northbound Bond Connect;
- right-of-use assets; and
- deferred tax assets.

10.5 Assets held by an authorized insurer through a third party[22] and over-the-counter derivatives entered into by the insurer with a third party are considered to be physically segregated if the third party establishes a separate fund account for each applicable participating fund. If this is not feasible, as an alternative, the third party's statements should demonstrate the separation of the amounts or units identified for each applicable participating fund. There should also be sound governance procedures for the exchange of assets between different funds, which take into account the controls within the insurer's operation and those between the insurer and the third party.

10.6 When allocating assets that are exempt from the requirement to maintain separate custodian/bank accounts as specified in paragraph 10.4, the basis and justification for the allocation should be set out clearly in the authorized insurer's corporate policy on governance of the participating business or relevant fund management policies and procedures, and the allocation should be applied consistently.

10.7 An authorized insurer is required to designate an approving authority within its organization for the transfer of assets out of an applicable participating fund (including any applicable participating fund exempted from the physical segregation requirements under paragraph 10.2). For a non-HK insurer (other than a designated insurer and an insurer who is exempted under paragraph 2.1), personnel of the Hong Kong branch should be involved in approving the transfer. Transfer of assets includes any withdrawal of assets from the fund and the exchange of assets with businesses outside the fund[23]. The approving authority for the transfer should be established based on factors such as the nature of assets or threshold amounts, considering the insurer's controls and governance

[22] "Third party" refers to financial institution, fund house, asset management company, or investment vehicle.
[23] Section 23 of the Ordinance states that an authorized insurer must only exchange assets at fair market value.

policy. In general, the larger the amount[24] of assets transferred or the more complex the transaction, the higher the level of the approving authority[25] should be. The insurer should have necessary controls in place to ensure a check and balance between the signatories of the relevant custodian/bank accounts and the approving authority for the transfer of assets out of these accounts for applicable participating funds. The insurer should be able to justify its designation of the approving authority to the IA upon request.

10.8 If there is any interfund balance due to an operational time gap (for example, premiums collected in a common bank account before being transferred to corresponding funds' accounts), the authorized insurer should settle the interfund balance with financial assets swiftly, and within 3 months at the latest to ensure that the physical segregation of funds is maintained. The shorter the operational time gap the better.

10.9 An authorized insurer should have clear operational policies and procedures for the settlement of interfund balances, including proper controls and frequency for the settlements, in order to ensure that interfund balances are settled swiftly and accurately and that the integrity of physical segregation is maintained.

11. Independent Report of the Establishment of Participating Fund(s) upon the Commencement of the Insurance (Amendment) Ordinance 2023

11.1 An authorized insurer is required to submit to the IA, in respect of each of its applicable participating funds, certification signed by its Board as specified in paragraphs 5.5 and 6.4 and supported by an independent report by 31 March 2025 (i.e. within 9 months of the commencement of the Insurance (Amendment) Ordinance 2023).[26]

[24] Authorized insurers may consider the threshold on an accumulated (instead of individual) basis where it is considered that individual amounts should be treated as a whole in substance.
[25] For example, Appointed Actuary, senior management or Board.
[26] As for other participating funds established under section 21B of the Ordinance which do not comprise any participating business carried on in Hong Kong, authorized insurers should ensure the establishment is appropriate with proper books and records.

11.2 The independent opinion should provide the level of granularity that is at least consistent with the applicable participating fund(s) established under the Ordinance. An authorized insurer can also opt to supply the independent report at a more granular level having regard to how the insurer manages the applicable participating fund(s).

Requirements of the person to provide the independent report

11.3 An authorized insurer should appoint an external independent person ("Independent Professional") to provide an independent report under this section 11, who should be qualified, capable and experienced with regard to the scope of the independent report.

11.4 For the purposes of this section 11, the IA expects the Independent Professional to be –

(a) A qualified actuary who possesses any of the overseas qualifications prescribed in the Insurance (Actuaries' Qualifications) Regulation (Cap. 41A) or equivalent, in respect of long term business, or
(b) A certified public accountant (practising), a CPA firm or a corporate practice as defined by section 2(1) of the Accounting and Financial Reporting Council Ordinance (Cap. 588).

11.5 There is no restriction against the Independent Professional to carry out the independent review jointly with the external auditor of the authorized insurer, provided that there is no conflict of interest[27]. A conflict of interest is one which creates a threat to the objectivity and independence of the Independent Professional. Matters to be considered for ascertaining the independence of an Independent Professional include whether, for example:

- the person holds a material financial interest in the insurer;
- the person is a family member or has other personal relationships with the Appointed Actuary, controllers, key persons in control functions, shareholder controllers or senior management of the insurer;

[27] To avoid doubt, the Independent Professional can be the external auditor, subject to independence assessment.

- the person provides non-assurance services that directly involves the preparation of information that is related to the scope of the independent opinion;
- the person is an employee of the insurer; and
- the total fees charged by the person from the insurer represent a large proportion of the total fee income of the person.

Scope and requirements of the independent report

11.6 The independent report regarding the establishment of participating fund(s) should be based on the position as at 1 July 2024 and at least cover the following areas:

(a) the identification of assets and liabilities attributable to each applicable participating fund pursuant to section 5;
(b) the sufficiency of the opening balance of each applicable participating fund pursuant to section 6;
(c) the policy on allocation of costs as expenses or charges pursuant to section 7; and
(d) the policy on allocation of distributable surplus/profits pursuant to section 8.

11.7 The independent opinion should be based on procedures performed and evidence obtained by the Independent Professional on each of the relevant areas addressed by the opinion. While the nature and extent of the procedures performed and evidence obtained could vary in order to fit the circumstances of the authorized insurer, the below lists out the IA's minimum expectations. The Independent Professional may perform alternate procedures considered appropriate to achieve the same objective.

(a) Identification of assets and liabilities attributable to each applicable participating fund

- Review the basis and justification for identification of assets and liabilities for each applicable participating fund;
- Review the identification of assets and liabilities having regard to the nature of riders, funds on deposit and prepaid premiums;

- Review whether proper books of account and other data records are maintained to support such identification; and
- Review the assets identified as attributable to each applicable participating fund to match those physically segregated, earmarked or allocated, as the case may be.

(b) Sufficiency of the opening balance of each applicable participating fund

- Review if the opening balance of assets in each applicable participating fund is no less than the amount of assets that is attributable to that participating business on the date immediately before 1 July 2024, according to the corporate policy on governance of the participating business;
- Review the determination of the amount of assets attributable to the participating business on the date immediately before 1 July 2024 against the corporate policy governing the management of participating business;
- Review if any changes have been made since 1 January 2019 to the basis for determining the amount of assets attributable to the participating business or any one-off distributions from the participating business since 1 January 2019 which could constitute an acceleration in the release of surplus asymmetrically to shareholders prior to 1 July 2024;
- Review the sustainability of each applicable participating fund having regard to the illustrated dividends/bonuses, reasonable expectations of policy holders and, assess if any additional capital support may be necessary; and
- Review if the value of assets is no less than the amount of liabilities determined on the basis of Insurance (Valuation and Capital) Rules (Cap. 41R) in respect of each applicable participating fund.

(c) Policy on allocation of costs as expenses or charges

- Review whether a clear policy is in place to provide the basis and justification for determining the allocation of expenses and charges to each applicable participating fund; and
- Review whether the policy, together with any supporting documents, contains both qualitative and quantitative (as

appropriate) analysis to justify the allocation of expenses and charges, as well as to identify charges that are profit in nature.

(d) Policy on allocation of distributable surplus/profits

- Review whether a clear policy is in place to provide the basis and justification for determining the allocation of distributable surplus/profits to policy holders and shareholders, and among different groups of policy holders; and
- Review whether the policy, together with any supporting documents, illustrates how the basis and justification are in line with the principles set out in paragraphs 8.1 to 8.5, having regard to any consequential changes arising from the establishment of participating fund(s) upon the commencement of the Insurance (Amendment) Ordinance 2023.

11.8 In a case where the independent opinion indicates that the identification of assets and liabilities has been inappropriate, the opening balance has been insufficient, and/or the policy on allocation of expenses/charges or the policy on allocation of distributable surplus/profits has not been clear or justifiable, the authorized insurer should rectify the situation as soon as practicable, and restore each of the applicable participating funds to the position it should be in as if such identification, opening balance or policies had been rectified since 1 July 2024.

11.9 The Independent Professional should express opinion in the form of a written report on the following matters:

(a) whether the authorized insurer has properly identified the assets and liabilities of each participating fund established under section 21B of the Ordinance which comprises participating business carried on in Hong Kong, and any findings that would cast doubt on the insurer's compliance with section 5;

(b) whether the insurer has maintained sufficient assets to meet the requirements on the opening balance of each applicable participating fund and any findings that would cast doubt on the insurer's compliance with section 6;

(c) whether the insurer has a clear policy in place on allocation of costs as expenses or charges, and any findings that would cast doubt on the insurer's compliance with section 7;
(d) whether the insurer has a clear policy in place on allocation of distributable surplus/profits, and any findings that would cast doubt on the insurer's compliance with section 8;
(e) if there are any findings in item(s) (a), (b), (c) or (d) which require rectification, details of such findings, rectification taken by the insurer and the outcome after the rectification; and
(f) any limitations and key risks of non-compliance identified.

11.10 Pursuant to paragraph 6.2, the Independent Professional should also provide additional opinion on any changes which the authorized insurer has made since 1 January 2019 to the basis for determining the amount of assets attributable to the participating business and/or any one-off distributions it made since 1 January 2019 from the participating business, that would accelerate the release of surplus asymmetrically to shareholders prior to 1 July 2024[28]. The insurer should explain to the Independent Professional the reasons behind the change of basis and/or one-off distributions and justify how, despite such change of basis and/or one-off distributions, the principle of fair treatment of policy holders is maintained and that the change of basis and/or one-off distributions, individually or cumulatively, are unlikely to result in any material adverse effect on the security of policy holders' contractual rights and their reasonable benefit expectations, including prospects of non-guaranteed benefits, or the financial soundness of the applicable participating fund. The Independent Professional should provide opinion on whether such justification is reasonable. If the insurer is unable to provide such justification or the Independent Professional cannot confirm the insurer's justification is reasonable, the change of basis and/or one-off distributions have to be rectified to safeguard the interests of the participating policy holders. In such case, the independent report should provide details of such findings, rectification taken by the insurer and the outcome after the rectification.

[28] For example, acceleration of the release of surplus asymmetrically to shareholders that results in the reduction of the applicable participating fund amount leftover for further sharing between policy holders and shareholders.

12. Commencement

This Guideline shall come into effect on 31 March 2026, except for section 4 which shall come into effect on 30 June 2026.

February 2026

Annex 1

Sample of an Annual Statement from the PBC (or PBA)[29]

As the [Participating Business Committee ("PBC") / Participating Business Advisor ("PBA")] for [Company name] ("the Company"), [we / I] issue this statement pursuant to the Guideline on Governance and Management of Fund(s) of Participating Business (GL34) issued by the Insurance Authority ("IA").

[We / I] have provided [our / my] opinion to the Board of the Company on the Company's exercise of discretion over the period from [date] to [date] relating to participating funds which comprise the participating business carried on in Hong Kong. [We / I] consider that the Company has [or has not] taken into account the interests of participating policy holders in a reasonable manner, and such interests are [or are not] consistent with the disclosures made to participating policy holders. Specifically, [we / I] have assessed the following areas –

- the Company's dividends/bonuses determination and declaration for the year [ended / ending] [date];
- determination of dividend/bonus rates used in the benefit illustrations for [new policies and/or in-force policies];
- the Company's mechanism for allocating distributable surplus/profits between policy holders and shareholders;
- the reasonableness of expenses and charges imposed by the Company on participating policies;
- the reasonableness of the participating funds's risk and investment profile;
- the communications with potential and existing policy holders;
- the Company's strategy for future sales of insurance policies and the impact on the participating fund;
- [management actions planned or implemented by the Company (if any)];
- [the use, purpose, and terms of shareholder capital support to the participating fund (if any)]; and
- [Any other areas as the PBC thinks fit]

[29] PBC or PBA, as the case may be, should tailor the annual statement to fit the Company's circumstances.

[Our / My] opinion is based on the information and explanations provided to [us / me] by [input as appropriate – the Appointed Actuary, the directors and management of the Company, information available as reasonably relevant, etc.], and on [our / my] knowledge gained and investigations conducted during the year. In forming [our / my] opinion, [we / I] have taken into account the Guideline on Underwriting Long Term Insurance Business (other than Class C Business) (GL16) and Guideline on Governance and Management of Fund(s) of Participating Business (GL34) [input as appropriate – other applicable guidelines, regulations] issued by the IA.

[Name of the Chairperson of the PBC / Name of the PBA]

[On behalf of the PBC / PBA] of [Company name]
[Date]

[List of members of the PBC]
[Changes to the list of PBC members / PBA (if any) during the period to which the statement relates]