Hong Kong Risk-Based Capital framework for insurance: draft Bill tabled before Legco

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Important milestone in the implementation of Hong Kong Risk-Based Capital

The Insurance (Amendment) Bill 2023 (**Bill**) was gazetted on 6 April, ushering in the introduction of the Hong Kong Risk-Based Capital framework (**RBC**). After almost a decade in development, the Hong Kong Insurance Authority (**IA**) is to be congratulated on reaching this important milestone. The Bill will proceed through the formal stages of House and Bills Committees before ultimately being passed and gazetted. With publication of the draft bill, minds can now focus on finalising the preparations for implementation and operationalise the production processes.

Key elements of the Bill

- Introduction of **Prescribed Capital** amount and **Minimum Capital** amount
- Establishment of **sub-fund for participating** business
- **Consequential amendments** to the Inland Revenue Ordinance (Cap. 112) and the Companies Ordinance (Cap. 622) to reflect RBC

Proposed amendments in line with expectations

The introduction of RBC to the Hong Kong insurance industry is welcome development for the Hong Kong industry. RBC will usher in a modern, risk-sensitive regime for the measurement of insurance company liabilities and minimum capital requirements, replacing the rules set out in the current Insurance Ordinance (Cap41) (**HKIO**).

The Insurance (Amendment) Bill 2023 sets out a series of amendments to the HKIO to enact RBC. The Bill also includes important amendments to the Inland Revenue Ordinance and the Companies Ordinance as a consequence of the adoption of RBC.

Determination of liabilities and solvency margin

Section 3C (Determination of value of assets and amount of liabilities)

The final rules to be made under S129(1)(a) are expected to closely follow the requirements set out in the Technical Specifications for HK RBC early adoption and will be market consistent

S10 (Meaning of capital requirement)

The Bill introduces the new prescribed capital amount (PCR) and the minimum capital amount (MCR) and the eligible capital resources. S35AA (Restoration plan or financial scheme) is updated to reference the PCR and MCR. The IA shall have power to vary capital requirements tor an insurer

Establishment of funds

S21B (Maintenance of separate accounts and funds in respect of long term business)

The funds will follow the long-term Classes of business C,G,H and other specified business. The latter fund will include at least one sub-fund for the participating business of the insurer

Appointments

S15AAA (Appointment of actuary)

An appointed actuary for long-term and general business

S32A (Requirement to provide reports)

The IA will be empowered to appoint a skilled person to provide a report in connection with any matter relating to the insurer

Powers to vary requirements and skilled person reports

The revised HKIO will give the IA greater powers than under the current HKIO. The liability valuation and the capital requirements will be set out in rules made by the IA under S129. S130 has been expanded to allow the IA to vary certain rules for individual firms. The major changes are contained in S10, which allows the IA to vary the capital requirements of an individual firm should they assess this is prudent, and S32A, which allows the HKIA to appoint a skilled person to report on any matter connected with an insurer.

Revisions to Inland Revenue Ordinance

The Bill also contains important measures to update the taxation basis for insurance business. The deemed basis for life business (the so-called "Premiums" basis) is unaffected; however, the assessment under the elected basis (the "Adjusted Surplus" basis) is affected. The adoption of RBC may see a material one-off emergence of (taxable) surplus, which the insurer shall be able to make an irrevocable election to spread over five years.

Revised profits assessment for insurance business

Deemed basis for life insurance business ("Premiums")	Elected basis for life insurance business ("Adjusted Surplus") now RBC
Non-life long-term business ("Adjusted Surplus")	General insurance business under RBC

Other long-term business (Classes D,F, and I) will also be taxed under an Adjusted Surplus basis. General business will also be measured under RBC. Both classes will include the irrevocable election to spread transition surplus evenly over 5 years. There is no change to the taxation basis of Classes G and H.

Please refer you to the taxation newsletter issued by PwC and we encourage you to seek advice from the PwC taxation team for this complex area.

Update to Companies Ordinance (Cap 622)

The Bill repeals the existing Section 293 of the Companies Ordinance (Cap. 622), which determines the realised profits and losses for companies which carry on long term business. With the repeal of S293, the determination will follow S291 and be defined with reference to financial statements prepared in accordance with GAAP.

Find out more about how RBC may affect your company

The adoption of RBC in Hong Kong is the culmination of many years of hard work and collaboration between the Insurance Authority, the insurance industry and the actuarial profession. With publication of the Bill, the industry will need to finalise its preparations for implementation and adapt its risk management processes. Finally, there will be taxation implications, which will need to be considered.

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