

Hong Kong Insurance Authority launches consultation on draft enterprise risk management guideline

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Introduction

The Hong Kong Insurance Authority recently released a 43-page draft guideline on enterprise risk management (ERM)⁽¹⁾ as part of Hong Kong's move towards a risk-based capital regime.⁽²⁾ Comments were sought by 6 July 2018.

This consultation exercise aims to:

- align insurers' capital requirements with the risks to which they are exposed; and
- strengthen insurers' risk management capabilities.

The draft guideline considers the recent consultation and review of the relevant insurance core principles (ICP) by the International Association of Insurance Supervisors (the global standard for the insurance industry) with an emphasis on risk-based supervision – in particular, ICP 8 and ICP 16 (which provide that insurers should have effective risk management systems with internal controls and an ERM framework to identify, measure, report and manage risks).

The objective of the draft guideline is to nurture a strong risk culture in the Hong Kong insurance industry, which will reflect the values, attitudes and norms of business behaviour. The Hong Kong Insurance Authority has specifically stated that the boards of directors and senior managers of insurers should take ownership of shaping insurers' risk culture, including the responsibility to establish, implement and oversee the ERM framework.

Features

The guideline adopts a principle-based approach, recognising that different risks are associated with different insurers. Consequently, the ERM framework and risk management policies should be proportionate to the nature, scale and complexity of the risks inherent to each insurer's business.

The Hong Kong Insurance Authority has proposed a three-tier approach to insurer supervision to avoid regulatory duplication with international groups which are already subject to group-wide or home supervision. The tiers are:

- insurance groups that are based in Hong Kong and under the insurance authority's supervision;
- insurance sub-group(s) within an insurance group which have significant operations in the Hong Kong insurance market; and

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- other insurers which are part of a group supervised by their home supervisors.

The three-tier supervisory approach is set out in Annex A to the draft guideline. To further avoid duplication, Guideline 10 (on the corporate governance of authorised insurers) will also be updated in accordance with the guideline.

Application

The draft guideline applies to all authorised insurers in Hong Kong, except:

- insurers which have ceased accepting new insurance business and are in the course of running-off their liabilities with an insignificant run-off portfolio in Hong Kong;
- Lloyd's;
- captive insurers; and
- marine mutuals.⁽³⁾

General requirements

The general requirements of the draft guideline include:

- establishing an appropriate governance structure to ensure safe and sound operation. The board of each authorised insurer is ultimately responsible for ensuring that the business maintains an effective ERM framework;
- putting in place ERM policies and procedures on risk management (including the process of identifying, assessing, measuring, monitoring, controlling and mitigating risks);
- establishing an appropriate management team with well-defined roles, responsibilities and reporting lines in order to maintain a sound system of checks and balances;
- setting a risk appetite statement based on the types of risk that the insurer will or is willing to take to achieve its corporate objectives and business strategies (through stress or scenario testing);
- developing a feedback loop to ensure continued effectiveness of the ERM framework, with regular reviews to ensure its responsiveness to changes in the risk environment and risk profile; and
- undertaking an annual own risk and solvency assessment to assess the insurer's current and future risk profile, adequacy of risk management and solvency and liquidity position, so that the insurer remains viable under both normal and stressed situations.

Comment

The Hong Kong Insurance Authority plans to finalise the draft guideline by late 2018 for implementation on 1 January 2020. Insurers should familiarise themselves with it and put in place advance measures in order to comply with the requirements on its implementation.

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Endnotes

(1) Available [here](#).

(2) Further information is available [here](#).

(3) A 'marine mutual' is an authorised insurer:

- which is a mutual company;
- which is restricted to insure its members against losses, damages or liabilities arising out of marine insurance; and
- whose articles of association, rules or bylaws provide for calling for additional contributions

from, or reduction of benefits to, its members.

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