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| **Hong Kong Insurance Authority: IA Levy**  **MARCH 2019** |

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# Purpose

The independent Insurance Authority (IA) was established on 26th June 2017 to replace the OCI in Hong Kong. The IA is to be self-financing with income streams both from the insurance industry and through the introduction of a policyholder levy (‘the levy’).

The long-term target is for the IA to be financially independent of the government, with about 70% of its expenditure being met by the levy and the remaining 30% by annual authorisation fees. These fees will consist of two elements, a fixed fee of HKD 300,000 for general insurers (HKD 600,000 for composite insurers) and a variable fee of 0.0039% on insurance liabilities (capped at HKD 7 million for general insurers or HKD 14 million for a composite insurer).

The purpose of this document is to explain how Lloyd’s will approach the payment of the levy to the IA, and the implications for HK coverholders and service companies.

# Summary

* The IA requires that insurers collect a premium levy from policyholders for certain lines of business to fund its operations from 1 January 2018.
* Due to complexities around reporting and audits, Lloyd’s syndicates will initially exercise a temporary option to centrally pay the levy on behalf of policyholders. No levy is to be directly collected from policyholders for a policy written on behalf of a Lloyd’s syndicate.
* The levy, payable centrally by Lloyd’s syndicates, only applies to a policy written by a Hong Kong domiciled Coverholder or service company, for risks located both in Hong Kong and overseas.
* A change has been made to the monthly risk bordereaux template to enable Lloyd’s to centrally report and pay the levy.
* Coverholders and service companies may be required to produce documentation for policyholders certifying that the levy has been paid.

# Implementation

## Affected Business

The levy applied to all business underwritten in Hong Kong on or after 1 January 2018, with the exception of Marine, Aviation and Transport business and all reinsurance contracts.

Marine insurance and reinsurance is exempt from the application of the levy, but the IA has stipulated that the definition of “marine” only encompasses classes 5 (Aircraft), 6 (Ships), 7 (Goods in Transit), 11 (Aircraft Liability) and 12 (Liability for Ships) as described in Part 3 of Schedule 1 of the Insurance Companies Ordinance (see below). Therefore, for example, coverage for freight forwarders, logistic operators, specie and stock, ports and terminals, warehouses, etc., would not be included within the definition of marine and are subject to the levy.

In the context of the Hong Kong regulatory reporting process this means that classes falling within Aircraft Damage and Liability, Ships Damage and Liability (Hull & Machinery; Local Vessels Liability; Forwarder Liability; Protection and Indemnity; Others) and Goods in Transit will only be exempt from the levy when the business falls within the definitions below. This will be of particular relevance to the Forwarder Liability, Ships Damage and Liability Others, and Goods in Transit classes.

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| --- | --- | --- |
| **Class** | **Description** | **Nature of Business** |
| 5 | Aircraft | Effecting and carrying out contracts of insurance upon aircraft or upon the machinery, tackle, furniture or equipment of aircraft. |
| 6 | Ships | Effecting and carrying out contracts of insurance upon vessels used on the sea or on inland water, or upon the machinery, tackle, furniture or equipment of such vessels. |
| 7 | Goods in transit | Effecting and carrying out contracts of insurance against loss of or damage to merchandise, baggage and all other goods in transit, irrespective of the form of transport. |
| 11 | Aircraft liability | Effecting and carrying out contracts of insurance against damage arising out of or in connection with the use of aircraft, including third-party risks and carrier’s liability. |
| 12 | Liability for ships | Effecting and carrying out contracts of insurance against damage arising out of or in connection with the use of vessels on the sea or on inland water, including third-party risks and carrier’s liability. |

## Levy Rate

The levy will be calculated as a percentage of the gross premium and the levy rate will gradually increase over the first 3 years, as set out in the table below.

The rate for determining the levy will be determined by the policy inception date or anniversary date (i.e. renewal date). The same rate will apply throughout the policy year irrespective of whether the policy year straddles more than one levy band and irrespective of the period of coverage by the policy.

|  |  |
| --- | --- |
| **A policy inception date, or a policy inception anniversary date (as the case may be) which marks the beginning of a policy year** | **Rate** |
| From 1 January 2018 to 31 March 2019 (both dates inclusive) | 0.040% |
| From 1 April 2019 to 31 March 2020  (both dates inclusive) | 0.060% |
| From 1 April 2020 to 31 March 2021  (both dates inclusive) | 0.085% |
| From 1 April 2021 onwards  (inclusive of that date) | 0.100% |

## 

## Method of Collection

An insurer can choose whether to directly collect the levy from the policyholder (the Actual Remittance Approach) or absorb the levy themselves (the Alternative Remittance Approach).

Under the Actual Remittance Approach, insurers may adopt a “cash basis” approach (whereby the levy is collected by the insurer when the premium is paid) or an “accrual basis” approach (whereby the levy is deemed to have been collected by the insurer once the premium is due, irrespective of when the actual premium is paid) for the reporting and remittance of the levy.

### Lloyd’s Approach

Following consultation with the market, Lloyd’s has determined that the Alternative Remittance Approach will initially be followed. Lloyd’s will adopt the Alternative Remittance Approach until it has determined how best it can collect, report and pay the levy to the IA. It should be noted that the IA are currently only allowing a maximum three year transitional period.

Under the Alternative Remittance Approach, a remittance will be made twice a year to the IA by Lloyd’s, once by 31 May (for the period 1 October to 31 March) and once by 30 November (for the period 1 April to 30 September). The remittance return will include the calculation of the remittance amount, which will be compiled by Lloyd’s using the information provided by coverholders and service companies in the monthly risk bordereaux.

Lloyd’s will also be required to submit an annual remittance report to the IA, which will be subject to examination by an auditor appointed by Lloyd’s. The audited remittance report will be submitted in April each year.

## Alternative Remittance Approach Process

# Action required by those responsible for HKR bordereaux submission

## Changes to the monthly risk bordereaux template

Three columns were added to the HKR template after the “Management Expenses” column and are named “Coinsurance”, “Total Gross Written Premium” and “Levy Amount”.

The inclusion of these columns provides Lloyd’s with the relevant data to ensure it can meet the reporting and payment obligations relevant to the levy to the IA under the Alternative Remittance Approach and also help aid the transition to the Actual Remittance Approach. Providing that all risks are accurately reported within the HKR template that is submitted, with the correct levy calculations, the most relevant stakeholder can be assured that Lloyd’s will report and pay the necessary levy to the IA. A copy of the HKR Template and HKR file specification are available on the CMR website.

These columns should be completed as follows:

### Coinsurance (with non-Lloyd’s insurers)

The IA has advised that where a syndicate leads a co-insurance policy with non-Lloyd’s insurers that they are required to remit the levy for the 100% share of the policy. Therefore, it is critical for Lloyd’s to be able to identify when a risk has been written on a co-insurance basis and whether in a lead or following capacity.

Where syndicates or coverholders are following a local company market lead insurer, that insurer will be responsible for collecting or paying the full levy remittance in respect of the policy. If the coverholder has confirmation that the lead is not taking responsibility for paying the full levy, the coverholder will need to record this. This will allow Lloyd’s to identify these scenarios and calculate the levy accordingly.

In the scenario of two or more Lloyd’s binders insuring a risk together, they would all be required to report their portion of the risk on their bordereaux as normal. The levy to be paid to the IA will be attributed to both the lead and following Lloyd’s market in accordance with their participation on the levy.

The column must be populated with one of the following options:

“L”: Lead: where Lloyds is the lead on a co-insurance arrangement.

“F”: Follower: where Lloyd’s is the follower on a co-insurance arrangement and the lead has confirmed they’re paying the levy on behalf of the follower.

“N”: N/A: where this is not a co-insurance arrangement.

“X” Follower: where lead has confirmed they're not paying the levy on behalf of the follower

### Total Gross Written Premium

This is the total amount of the gross written premium charged for the risk to the insured both in relation to the Lloyd’s portion and any other company market co-insurance participants. The original GWP column (column W) should only include the amount relevant to Lloyd’s proportion of the risk whereas the ‘Total Gross Written Premium’ column should be used solely in cases where the risk is a mixture of Lloyd’s and company market capacity, and therefore needs to show the total premium of the entire risk.

### Levy Amount

This relates to the levy amount that is due on the risk and is to be paid by Lloyd’s to the IA.

Where Lloyd’s is the lead co-insurer on a risk written by Lloyd’s syndicates and company market insurers then the levy amount should be calculated using the appropriate rate from the table shown in section 3 above and applied to the Total Gross Written Premium.

Where Lloyd’s is a following market on a co-insurance risk, then there is no need to provide the levy amount as it will be the responsibility of the lead co-insurer to pay the 100% share.

Where the risk written is not on a co-insurance basis, and solely written at Lloyd’s, then the levy amount should be calculated using the appropriate rate from the table shown in section 3 above and applied to the Gross Written Premium (column W) and the Total Gross Written Premium field should be left empty.

## Billing of Levy

Service companies and coverholders are required to either set out the levy in billing documents, showing the levy proportion of the premium, or at least once a year send to policyholders the following statement:

‘Levy collected by the Insurance Authority has been imposed on this policy at the applicable rate. For further information, please visit <coverholder / service company website> or contact: <coverholder / service company phone number>.

Please note, the above statement is a suggested wording and can be updated to reflect a particular Coverholder/service company’s circumstances.

This can be done via any means of communications; e.g. premium collection notices, email or SMS.

## Proof of Levy Payment

Insurers are required to produce written proof of the levy payment to policyholders upon request. This is because it is the policyholder’s legal responsibility to pay the levy, whilst in practice insurers are the entities collecting and paying over the levy on behalf of policyholders. As such, the following general statement should either be included on anniversary statements sent out to policyholders or provided to them upon request:

‘Levy collected by the Insurance Authority has been imposed on this policy at the applicable rate and will be remitted in accordance with the prescribed arrangements. For further information, please visit <coverholder / service company website> or contact: <coverholder / service company phone number>.

# Frequently Asked Questions

1. **I have noticed that the ‘Note on Collection of Levy on Insurance Premium’ refers to a cap of the levy to be paid, how does this apply?**

Whilst Lloyd’s is reporting using the Alternative Remittance Approach, the levy amount due will be calculated using the rates included in the table above without the application of a cap.

1. **What happens when a return premium (RP) is reported?**

Levy refunds are permitted for all return premium transactions. As Lloyd’s will be paying the levy on behalf of the policyholder, then return premiums will be deducted from the next levy payment due.

1. **Are there any audit implications for the managing agent/coverholder?**

Lloyd’s anticipates that other than the annual audit sampling process, that managing agents/coverholders/service companies are already familiar with, that there will be no further implications. By undertaking the collection, reporting and payment of the levy centrally, Lloyd’s is hopeful that all audit requirements can be met centrally too, however, since the first audit report is not due for submission until April 2019, Lloyd’s are still in discussions with the auditors as to what evidence they require.

1. **How will the levy work in cases of co-insurance?**

The IA has placed the responsibility for the reporting and payment of the levy for co-insurance business on the lead insurer. Once the lead insurer has paid the levy (100% share) to the IA and reports as such to the IA, there is no need to report on details of the collection of the levy on behalf of the other underwriters on the programme. How the lead insurer distributes the share of the levy amongst other underwriters of the co-insurance programme is a matter for the insurer to determine. The lead insurer may forgo collecting the levy as long as the lead insurer remits the levy (100% share) to the IA. Lloyds has taken the stance that where we lead on a co-insurance, we will be responsible for the payment of the levy for the entire contract. Where an insurer is following on a co-insurance, confirmation must be sought that the lead is collecting and remitting the levy on behalf of all parties to the contract. Where the lead has confirmed that they will not be paying the levy on behalf of the follower, this must be indicated using the correct code in CMR.

**5. Is an endorsement that is payable after 1 January 2018 under a master policy with an inception date that falls before 1 January 2018, subject to the levy?**

Only unscheduled endorsements payable on or after 1 January 2018 are subject to the levy. To determine whether a premium payment is categorised as scheduled or unscheduled, the terms of the insurance contract would need to be considered. If a payment can be attributed to a particular term within the contract it would be scheduled.

# Further Information

For further information, please contact:

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Or

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