Explanatory Note on Licensing Requirements for Banking Sector under Regulatory Regime for Insurance Intermediaries

Insurance Authority
October 2019

1. Introduction

1.1 This Explanatory Note ("Note") which includes a set of frequently-asked questions ("FAQs") is issued by the Insurance Authority ("IA") to provide guidance on the licensing requirements in relation to banks[1] and bank staff under the regulatory regime for insurance intermediaries stipulated in the Insurance Ordinance (Cap. 41) ("the Ordinance").

1.2 Under section 64G of the Ordinance, a person must not carry on a regulated activity, or hold out that the person is carrying on a regulated activity, in the course of the person's business or employment, or for reward unless the person is a licensed insurance intermediary or is exempt under the Ordinance.

1.3 The regulatory regime for insurance intermediaries is activity-based and applies to any person carrying on a regulated activity. Accordingly, a bank staff who carries on a regulated activity (e.g. bank staff who gives advice to a client on a particular insurance product) or holds out that he/she is carrying on a regulated activity, would need to be licensed unless an exemption applies[2].

1.4 This Note aims to provide guidance on the extent to which certain bank-client interactions or ancillary banking activities related to insurance would be regarded as "regulated activities", thus requiring licensing of the relevant bank and bank staff.

1.5 This Note is not intended to be a comprehensive guide and does not constitute legal advice. Banks and their staff are advised to seek professional advice if they have any question relating to the application or interpretation of the relevant provisions of the Ordinance.

1.6 This Note does not have the force of law and should not be interpreted in a way that would override the provision of any law. The IA reserves the right to review and update this Note from time to time.

1.7 Unless otherwise specified, words and expressions in this Note shall have the same meanings as given to them in the Ordinance.

1.8 For the purpose of this Note, a "bank staff" refers to a bank's employee, and a "client" refers to a person who is a client of the bank and is also an existing or potential policy holder.

---

[1] For the purpose of this Note, "bank" means an authorized institution defined in section 2(1) of the Banking Ordinance (Cap. 155).

[2] Relevant exemptions are set out in section 123 of the Ordinance.

2. General Description of Regulatory Regime for Insurance Intermediaries

2.1 The regulatory regime for insurance intermediaries is an activity-based regime that requires the licensing of all persons carrying on or holding themselves out as carrying on "regulated activities" unless an exemption applies.

2.2 The scope of "regulated activity" is set out in section 3A of, and Schedule 1A to, the Ordinance.

2.3 A "regulated activity" includes any of the following acts:

a) negotiating or arranging a contract of insurance;
b) inviting or inducing, or attempting to invite or induce, a person to enter into a contract of insurance;
c) inviting or inducing, or attempting to invite or induce, a person to make a material decision;
d) giving regulated advice.

2.4 In this connection, a "material decision" refers to a decision made, and "regulated advice" refers to an opinion given, in relation to any of the following matters ("insurance matters"):

a) the making of an application or proposal for a contract of insurance;
b) the issuance, continuance or renewal of a contract of insurance;
c) the cancellation, termination, surrender or assignment of a contract of insurance;
d) the exercise of a right under a contract of insurance;
e) the change in any term or condition of a contract of insurance;
f) the making or settlement of an insurance claim.

2.5 Where a person wishes to carry on any regulated activity, the person is required to obtain a licence granted by the IA, unless an exemption applies. There are five categories of licensed insurance intermediaries under the Ordinance as follows:

a) Licensed insurance agency
b) Licensed individual insurance agent
c) Licensed technical representative (agent)
d) Licensed insurance broker company
e) Licensed technical representative (broker)

General guidance on relevant elements of "regulated activities"

2.6 In sections 2.7 to 2.9 below, we set out general guidance on certain expressions used in the Ordinance to define "regulated activities". Whether or not regulated activities are being carried on, however, will depend on the specific facts of any given situation. In this regard, the focus would not be on a particular snapshot of a singular communication or act in isolation, but would take account of the full factual context and circumstances and be viewed from an objective perspective.

2.7 ***"Inviting or inducing or attempting to invite or induce"***

Regulated activity includes inviting or inducing, or attempting to invite or induce, a person to enter into a contract of insurance or to make a material decision (see 2.3(b) and (c) above). As general guidance, the IA takes the view that "inviting or inducing" would require an element of encouraging, persuading or convincing a person to enter into a contract of insurance or to make a material decision. It follows that an act or communication which does not have any such element may unlikely constitute inviting or inducing (or attempting to invite or induce). Inviting or inducing may generally be distinguished from a communication which merely seeks to inform or educate a person about certain matters. Inviting or inducing may also be distinguished from the mere provision of information, which is not accompanied by any element of encouraging, persuading or convincing. A communication by a bank staff to a client on a particular insurance product, is more likely (from an objective perspective) to involve encouragement, persuasion or convincement to enter into or apply for a contract of insurance, than a communication involving generic information on types of insurance products. Ultimately, however, whether an act or communication amounts to inviting or inducing a person or attempting to invite or induce a person to enter into a contract of insurance or make a material decision, would be assessed objectively taking account of the full factual context and totality of interactions of which the act or communication forms part.

2.8 ***"Material Decision"***

In determining whether a decision constitutes a material decision (see 2.4 above), the IA will generally have regard to the following matters:

a) whether the decision relates to a particular contract of insurance;
b) whether the decision relates to an insurance matter; and
c) whether the decision is made by a person in his/her/its capacity as an existing or potential policy holder.

Note: A policy holder includes a claimant[3], i.e. a person who makes an insurance claim.

2.9 ***"Regulated advice"***

In determining whether an opinion constitutes regulated advice (see 2.4 above), the IA will generally have regard to the following matters:

(a) whether the opinion relates to a particular contract of insurance;
(b) whether the opinion relates to an insurance matter;
(c) whether the opinion is given to a person in his/her/its capacity as an existing or potential policy holder; and
(d) whether only factual information is given.

Further, the IA generally takes the view that for an opinion to be regulated advice, it would need to go beyond the mere provision of information on the contract of insurance or insurance matter. Regulated advice would generally involve the provision of a recommendation to a client on the contract of insurance or insurance matter, or be a statement made with a view to the client placing reliance on that statement in respect of the contract of insurance or insurance matter. The IA would always assess this objectively, taking account of the full factual context and the totality of the interactions with the client of which the relevant communication forms part.

2.10 ***Bank being a Licensed Insurance Intermediary***

In the case of a bank that is a licensed insurance intermediary, any of the bank's staff intending to carry on regulated activities as representatives of the bank must be licensed technical representatives (agent) or licensed technical representatives (broker) appointed by the bank unless carrying on of the activity concerned only involves the discharge of clerical or administrative duties for the bank (section 123(2) of the Ordinance).

2.11 ***Referral of a Client to a Licensed Insurance Intermediary[4]***

In the course of referral of a client to a licensed insurance intermediary by a bank staff, the staff should make clear to the client that he (i.e. the staff) is neither acting in the capacity of a licensed insurance intermediary nor representing the

[3] Under section 2 of the Ordinance, a policy holder includes a person to whom, under a policy, a benefit is due.

[4] As regards receiving referral business from other parties, licensed insurance agents should comply with Standard and Practice 5.4 of the Code of Conduct for Licensed Insurance Agents, and licensed insurance brokers should comply with Standard and Practice 5.5 of the Code of Conduct for Licensed Insurance Brokers.

licensed insurance intermediary to whom the client is being referred for the purpose of arranging the relevant insurance policy.

In addition, if a bank is a licensed insurance agency appointed by an authorized insurer, the bank should ensure compliance with the terms and conditions in the relevant agency agreement entered into with the insurer if it intends to refer a client to another licensed insurance intermediary.

3. FAQs

3.1 The following FAQs are for general reference only and aim to illustrate examples of circumstances in which a bank staff may or may not be required to be licensed. If the factual circumstances are different or subject to other factors, the analysis and answer may be different. Each case should therefore be assessed on its own circumstances.

Referral of a Client:

Q1: When opening a bank account for a client, the bank staff takes the opportunity to talk with the client about an insurance product currently available in the market and provides the client with a marketing leaflet. Is the bank staff carrying on regulated activities?

A1: Since the bank staff takes the initiative to discuss a particular insurance product with the client and distributes a marketing leaflet to the client, these actions are likely to be regarded as carrying on regulated activities. The reason for this is that (from an objective viewpoint), the bank staff's communications and actions appear to be aimed at, and would be taken by the client as, encouraging or persuading the client to apply for the specific insurance product. This amounts to "inviting" or "inducing" a person to enter into a contract of insurance or to make an application for a contract of insurance.

Q2: A client approaches a bank staff to ask about possible retirement solutions as part of the client's retirement planning. The bank staff then introduces the concept of annuities to the client (informing the client that an annuity is an insurance product which helps people convert their money into a steady stream of income over the long term, and it may help people spend their retirement savings in a disciplined way etc.). The bank staff does not, however, refer to any specific annuity product or provider. When the client indicates an interest in learning more about the annuity products, the bank staff informs the client that he is unable to provide the client with product-specific information, but he can refer the client to a licensed insurance intermediary for further advice. Is the bank staff carrying on regulated activities?

A2: In this scenario, the bank staff does not provide, explain or discuss with the client any information relating to a particular insurance product. Rather, the bank staff is introducing the generic insurance concept of annuities to the client (i.e. providing generic information on a type of insurance product). This would unlikely be considered to be regulated activities as the bank staff is merely seeking to inform or educate the client about certain matters (in this case what annuities are). In other words, this is mere provision of information. The elements

of encouraging, persuading or convincing are not present and hence, there is no inducement or invitation.

The introduction of the client by the bank staff to a licensed insurance intermediary may be considered to be an inducement to contact the licensed insurance intermediary regarding the services the intermediary may provide (rather than an inducement to enter into or apply for a contract of insurance). As such, the mere introduction to the intermediary in these circumstances is also unlikely to constitute regulated activities.

The bank staff should, however, be mindful not to persuade, encourage or convince the client to purchase a particular annuity product from the licensed insurance intermediary whom he is introducing, otherwise this may stray into carrying on regulated activities. (This may be the case, for example, where the bank staff indicates to the client that the client may obtain preferential rates of premium if the client purchases an annuity through the particular licensed insurance intermediary).

Q3: When handling a property mortgage application, the bank staff notifies the client that it is the bank's credit requirement that property collateral must be covered by fire insurance, but the bank does not designate which particular fire insurance policy should be purchased by the client. When the client wishes to learn more about fire insurance, the bank staff informs the client that he can choose to obtain a fire insurance policy from an insurer partnered with the bank. With the client's consent, the bank staff passes the client's contact details to a licensed insurance intermediary so that the insurance intermediary may approach the client directly. Is the bank staff carrying on regulated activities?

A3: The bank staff informing the client of the precondition to have in place a fire insurance in relation to a property if the client wants to apply for a mortgage from the bank on the property, would unlikely constitute regulated activities. The bank staff does not introduce or discuss any particular insurance product with the client, or request the client to purchase a particular contract of insurance. Rather, the bank staff is merely explaining a term of the mortgage (being the provision of information).

Q4: Further to Q3 above, the client successfully applies for a property mortgage loan from the bank, and selects the insured amount for his fire insurance policy based on the replacement cost of the mortgaged property. A year later, the replacement cost of the mortgage property increases. The bank staff contacts the client and informs him that the insured amount of his fire insurance policy needs to be adjusted in order to continue to fulfil the terms of the mortgage loan. Is the bank staff carrying on regulated activities?

A4: The bank staff informing the client of the effect of the change in replacement cost of the mortgaged property on the required insured amount of the fire insurance policy, would unlikely constitute regulated activities. Rather, the bank staff is merely providing updated information to client in relation to the client's obligations under the mortgage i.e. the updated replacement cost of the property collateral and the continuing need for the client to satisfy the term in the mortgage requiring the property collateral to be covered by fire insurance.

Q5: During the interaction with a corporate client, the bank staff becomes aware that an employee of the client is a "key man" to the client's business operation and the death, disability or absence of this employee could be detrimental to the client's business ("key man risk"). The bank staff reminds the client of its key man risk, and asks if the client would like to receive information related to key man life insurance from a licensed insurance intermediary. When the client indicates an interest in learning more, the bank staff arranges a meeting for the client with a licensed insurance intermediary. Is the bank staff carrying on regulated activities?

A5: Identifying the "key man" risk of a corporate client and highlighting this to the client, would unlikely be considered as regulated activities. Similarly, simply asking the client if it would like to be placed in contact with a licensed insurance intermediary to discuss insurance options for the key man risk, is also unlikely to be considered as regulated activities.

However, the bank staff should not seek to persuade, encourage or convince (e.g. through numerous reminders) the client to buy key man insurance through the licensed insurance intermediary (as this may amount to inviting or inducing a person to enter into a contract of insurance or to make an application for a contract of insurance). Further, if after identifying the key man risk, the bank staff discusses with the client any specific insurance product or provides an opinion on the features of any particular insurance product which can help mitigate the risk, then this is likely to be regarded as regulated activities.

Q6: In return for each successful referral of a client by a bank staff to an insurer or licensed insurance intermediary, the bank receives a referral fee from the insurer or licensed insurance intermediary. The bank's staff remuneration policy takes into account such referral as an indirect component for consideration, amongst various aspects of staff performance. When making a referral, the bank staff does not provide, explain or discuss with the client or give an opinion (e.g. suitability, merits) on any particular insurance product or its details (e.g. features, terms). Is the bank staff required to be licensed under the Ordinance?

A6: As indicated above, whether or not regulated activities are being carried on (thereby requiring licensing) will depend on the specific facts of any given situation. In considering this, one would not focus solely on a particular snapshot

of a singular communication or act in isolation, but take account of the full factual context and circumstances and view the matter from an objective perspective. In this respect, whilst the mere fact of a referral fee being paid to the bank or bank staff (and the amount of such fee) would not be conclusive as to whether or not regulated activities are carried on, it would form part of the factual context in considering the matter.

Whether or not a bank staff carries on regulated activities (as stated throughout this Note) will depend on matters such as whether, factually, the staff has sought to encourage, persuade or convince a client to enter into a contract of insurance or make a material decision (thereby inviting or inducing or attempting to invite or induce), or given an opinion which involves a recommendation on insurance matters (regulated advice). If the bank's remuneration structure is set up so as to directly incentivize bank staff to encourage, persuade or convince clients to enter into or apply for insurance contracts, then this would be a key fact to consider in any dispute over whether or not regulated activities have taken place. Accordingly, banks should review their remuneration structure for such activities, and put in place proper controls and monitoring to ensure bank staff do not carry on regulated activities.

Policy or Premium Financing

Q7: A client has a life insurance policy or (after discussion with a licensed insurance intermediary) has decided to apply for a life insurance policy and approaches a bank staff to enquire about obtaining possible financing options from the bank using the policy as collateral for receiving a loan facility. The bank staff informs the client that the bank can offer financing using insurance as collateral and explains the bank's credit underwriting criteria and the arrangement of the financing to the client. Is the bank staff carrying on regulated activities?

A7: Where the client already has an in-force life insurance policy, there can be no element of inviting or inducing the client to enter into or apply for a contract of insurance. Similarly, where the client has already decided to apply for a particular life insurance policy after discussion with a licensed insurance intermediary, then there is unlikely to be any element of inviting or inducing the client to apply for a contract of insurance. Further, if the bank staff is merely providing its underwriting criteria or its lending terms to the client, for the client to consider, then this is likely to be the mere provision of factual information and the bank staff is unlikely to be regarded as carrying on regulated activities.

However, if the bank staff goes beyond the mere provision of factual information, and tries to persuade, encourage or convince the client to apply for financing and assign the insurance policy to the bank as collateral, then this action may

constitute regulated activities as it may be regarded as "inviting or inducing, or attempting to invite or induce a person to assign a contract of insurance".

The situation would also be different, if it is not the client who approaches the bank staff, but rather the bank staff, on discovering that the client has an insurance policy or is applying for a particular insurance policy, who takes the initiative to approach the client to introduce a policy financing arrangement. This, from an objective viewpoint, is likely to be considered as attempting to invite or induce the client to make a material decision (i.e. a decision in relation to the assignment of a contract of insurance).

Q8: A bank staff on reviewing a client's investment/banking portfolio takes the initiative to introduce premium financing to the client as a means of enabling the client to purchase a particular life insurance product. Is the bank staff carrying on regulated activities?

A8: In this scenario, the action of the bank staff is very likely to be regarded as carrying on regulated activities, as the bank staff's actions in taking the initiative to introduce premium financing to the client with respect to a particular insurance product, would almost certainly from an objective viewpoint be seen as encouraging or persuading the client to enter into or to apply for an insurance product (i.e. inviting or inducing or attempting to invite or induce). Further, if during his discussion with the client the bank staff offers an opinion on the product, which is a value judgement on the favourability of the product, then this would also likely be regulated advice.

<u>Policy Assignment</u>

Q9: A corporate client is engaged in the export trade business and has a number of account receivables. Together with the bank staff, the client explores the types of credit facilities available to it. The bank staff explains to the client that the bank's receivable services (also known as factoring) may be suitable for it, but there is a precondition that the client has to purchase a credit insurance with any authorized insurer in Hong Kong and assign its rights under the insurance policy in favor of the bank as collateral. However, the bank will not designate which particular credit insurance policy should be purchased by the client, and only require that the policy is issued by any authorized insurer in Hong Kong. Is the bank staff carrying on regulated activities?

A9: In this scenario, the bank staff is not seeking to encourage, persuade or convince the client to purchase trade credit insurance in favour of the bank, but merely stating that the purchase of such insurance is a precondition for the bank providing factoring credit facilities to the client. Further, the bank staff neither requests the client to purchase any particular insurance product nor discusses

with the client about any specific insurance product. Under these circumstances, it is unlikely that the bank staff will be regarded as carrying on regulated activities.

The bank staff should, however, take care not to stray into recommending any particular trade credit insurance product or discussing the merits of particular products in the market, as this would likely amount to providing regulated advice. Further, the bank staff should be mindful not to compare particular credit insurance products for the client and their relative merits with regard to the client's circumstances, as such action is likely to be viewed as carrying on regulated activities rather than merely providing factual information.

Q10: The bank decides to cancel certain credit facilities, where the client has assigned its insurance policy to the bank as collateral. The bank demands the client to repay all outstanding debt. Upon full repayment, the bank discharges the assignment of insurance or effects a re-assignment of the insurance policy to the client. Is the bank carrying on regulated activities?

A10: The bank, in this scenario, is not inviting or inducing the client to make any material decision on a particular insurance policy or assignment of the policy, or providing any regulated advice with respect to a particular insurance policy or its assignment. Rather, the re-assignment of the policy (or discharge of the assignment) is an act consequential upon the repayment of the outstanding debt. As such, in this scenario, it is unlikely the bank is carrying on any regulated activities.

<u>Exercising a Right under an Insurance Policy</u>

Q11: A client assigned its insurance policy to a bank as collateral for a credit facility. The client defaults on its loan repayment. The bank as a lender and assignee of the insurance policy exercises its rights to surrender the policy for its cash value. Is the bank carrying on regulated activities?

A11: The bank's exercise of its right as an assignee of the insurance policy to directly cancel, surrender, or terminate a contract of insurance with an insurer is unlikely to be regarded as regulated activities. The act of cancellation, surrender or termination is consequential upon the client's default of the loan repayment and the bank is thereby merely exercising its rights consequential upon the assignment. There is no element of invitation or inducement, or any regulated advice being provided.

Q12: As a mortgage loan lender, the bank requires a client to make an insurance claim in order to preserve collateral value. For instance, the bank requests the client to lodge a claim under a fire insurance in order to restore damaged mortgaged property. Is the bank carrying on regulated activities?

A12: If the bank, in requesting the client to make an insurance claim in order to preserve the collateral, is exercising a right under the terms and conditions of the mortgage agreement, then this is unlikely to amount to the carrying on of regulated activities. The bank in this scenario is not seeking to encourage, persuade or convince the client to make the insurance claim (being the elements normally associated with "inviting or inducing"). Rather, the bank is exercising a right under the terms and conditions of the mortgage loan agreement, requiring (mandating) the client to submit the claim in performance of the term or condition under the mortgage loan agreement.

Trust Arrangement

Q13: A client asks a bank staff about holding structure options for certain insurance policies. The bank staff suggests the client to consider, among other options, holding the insurance policies on trust as an option, but also recommends that the client seek further advice from a licensed insurance intermediary. Is the bank staff carrying on regulated activities?

A13: The answer as to whether the bank staff is carrying on regulated activities in this situation, would depend on more than just the facts stated in the question.

If the bank staff is only providing factual information about possible holding structure options (e.g. trust is one of the options), and recommends the client to seek advice from the licensed insurance intermediary, then such activities are unlikely to be regarded as regulated activities.

If the bank staff gives an opinion (suggesting that the policies should be held on trust) as an answer to the enquiry about the structure in which the policies should be held, then giving such opinion may be viewed as regulated activities (i.e. regulated advice). However, the fact that the opinion is provided at the client's request and the suggestion is made by the bank staff that the client should seek further advice from a licensed insurance intermediary, leaves the question of whether the bank staff is indeed carrying on regulated activities finely balanced. It is suggested that if the bank staff, in these circumstances, makes clear to the client that he is not making a recommendation, but merely suggesting that the client may wish to explore trust options with a licensed insurance intermediary for further consideration before making any decisions, then this may be sufficient to demonstrate that the bank staff is not carrying on regulated activities.

Q14: After discussing the matter with a licensed insurance intermediary, a client intends to purchase a particular insurance policy. The client would like to put the insurance policy into his trust currently administrated by the bank, and he approaches a bank staff for this purpose. In this connection, the bank staff reminds the client that he should check with the relevant licensed

insurance intermediary if the policy can be held by a trust, since certain insurers may restrict policies they issue being held on trust. After checking, the client decides to purchase another insurance policy without such restriction. Is the bank staff carrying on regulated activities?

A14: Solely reminding the client to check with his licensed insurance intermediary about the terms and conditions of the insurance policy is unlikely to be regarded as carrying on regulated activity, since it does not involve giving any opinion in relation to the insurance matters. However, if the bank staff having informed the client about a term or condition or restriction in a particular insurance policy then recommends that the client purchases or not to purchase that particular insurance policy, the situation may be different, as the recommendation may constitute regulated advice.

*****