BY EMAIL ONLY

Members' Undertaking No. 72
14 March 2018

To: All Ordinary and Associate Members

LIA MU 72/18 - LIA GUIDELINES ON THE USE OF SIGN-ON INCENTIVES IN THE RECRUITMENT OF FINANCIAL ADVISORY REPRESENTATIVES

ACTION:

1. **MEMBERS' UNDERTAKING NO. 52 OF 17 AUGUST 2010 ON “LIA PRINCIPLES AND PRACTICES ON RECRUITMENT OF TIED AGENTS (THE CODE)” IS REPLACED BY THIS MU.**

2. **FOR COMPLIANCE OF ORDINARY MEMBERS WITH TIED AGENTS AND/OR RELATED FINANCIAL ADVISER FIRMS WITH IMMEDIATE EFFECT**

3. **FOR OTHER MEMBERS’ INFORMATION**

LIA promotes self-regulation and the recruitment activities undertaken by members should comply with the principles and measures set out in this Members’ Undertaking.

LIA SECRETARIAT

<u>LIA MU 72/18 - LIA GUIDELINES ON THE USE OF SIGN-ON INCENTIVES IN THE RECRUITMENT OF FINANCIAL ADVISORY REPRESENTATIVES</u>

COMMITMENT TO UPHOLD PROFESSIONALISM OF THE LIFE INSURANCE INDUSTRY AND SAFEGUARD CUSTOMER INTERESTS

1. LIA recognises that some insurers or their related FA firms may offer migration packages to recruit FA representatives. When such migration packages are offered, they must be done in a reasonable manner that does not undermine the professionalism of the industry, and most importantly, does not adversely affect the interests of consumers.

2. To achieve this, LIA members commit to abide by the following principles:

   a) We are committed to adopting ethical, professional and responsible recruitment practices.

   b) We encourage growth in the number and quality of representatives in the industry while continuing to maintain high standards.

   c) We strive to attract new entrants with the right ethics, motivation, aptitude and attitude.

   d) We acknowledge the individual's right to move between companies. However, such movements should not adversely affect the interests of consumers. They should be protected from, for instance, any resulting increase in the cost of insurance, unethical conduct such as improper switching and aggressive sales practices.

   e) We commit to adopt the measures set out in these guidelines, as well as any further measures required by MAS.

3. Should the insurer or its related FA firm intend to engage in mass recruitment (as defined in paragraph 8), it is to inform MAS of its plans early prior to the mass recruitment.

FUNDING OF COSTS

4. In line with section 17 of the Insurance Act, all costs, direct or indirect, that pertain to such acquisition of FA representatives should not be borne by the insurance fund. An example of direct costs would be compensation packages paid to migrating representatives. Examples of indirect costs would be additional compliance costs incurred in employing additional resources to perform more intensive checks on migrated representatives' sales transactions, as well as management expenses relating to the acquisition initiative. Accordingly, these costs should not be factored in members' pricing of products, as doing so would transfer the costs borne by the shareholders' fund to the insurance fund.

SCOPE OF MEASURES TO SAFEGUARD CUSTOMER INTERESTS

5. There are four measures to be followed.

6. Measures 1 and 2 apply to all representatives who are offered sign-on incentives tied to sales targets or a transition package.

7. Measures 3 and 4 will apply when the insurer or its related FA firm conducts mass recruitment.

Definition of mass recruitment

8. Mass recruitment is defined as the recruitment of 30 or more representatives from the same insurer or FA firm within a 60 day period (to be tracked on a rolling basis). Measures 3 and 4 will apply to this group of migrating representatives for at least 2 years.

9. Incentives that are tied to sales targets include both monetary and non-monetary incentives.

MEASURE 1: SALES TARGETS TO BE SET AT A REASONABLE LEVEL

Rationale

10. This measure seeks to mitigate the risk of representatives engaging in improper conduct such as mis-selling or improper switching in order to meet sales targets.

11. Sales targets set for Year 1 should not be higher than the representative's average of his annual achieved sales in the preceding 3 years.

12. Any increase in subsequent years' sales targets (after Year 1) should be set at a reasonable level having regard to factors including, but not limited to, the following:

    a) Representative's past sales performance
    b) Representative's compliance track record, e.g. BSC grades
    c) Representative's years of financial advisory experience
    d) Representatives' past persistency ratios
    e) Sales targets of representative's peers

MEASURE 2: PAYMENT OF SIGN-ON INCENTIVES TO BE SPREAD

Rationale

13. This measure seeks to incentivise representatives to stay on and service their customers for a longer period of time.

14. Payment of sign-on incentives is to be spread over a minimum period of 6 years, with a cap in the first year, and the rest to be spread evenly over the next 5 years or more.

15. The first year payment is capped at 50% of the representative's average annual remuneration in the last 3 years, and the remaining payments are based on a level percentage.

Illustration for a rep whose sign-on incentives are set at 150% of the average annual remuneration[1] paid by the previous FA firm in the past 3 years

Sign-on incentives are spread over a minimum period of 6 years

Total sign-on package offered	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6
150% of average annual remuneration in past 3 years	50% (max)	20%	20%	20%	20%	20%

First year payment is capped at 50% of the average of the representative's annual remuneration in the past 3 years

The remaining payment to be evenly spread out over the next five years or more

Assuming that a rep's average annual remuneration in the past 3 years is $100,000, the sign-on incentives payable each year would be spread as follows:

$150,000	$50,000	$20,000	$20,000	$20,000	$20,000	$20,000

[1] Remuneration is defined as - a) any monetary commission, incentive, benefit or reward; b) any non-monetary incentive, benefit or reward.

MEASURE 3: PEGGING THE SIGN ON INCENTIVES TO THE PERSISTENCY OF POLICIES SERVICED BY THE REPRESENTATIVE AT THE PREVIOUS FIRM

Rationale

16. This measure seeks to deter representatives from giving inappropriate advice to former customers to replace their existing policies with new policies from the hiring insurer or related FA firm.

17. When mass recruitment (as defined in paragraph 8) has occurred, the previous insurer or related FA firm will track the block of regular premium life policies and accident and health policies ("ring-fenced policies") serviced by the representative at his/her previous firm, calculated 2 years after the representative has left the previous firm. At the end of the 2 year period, the previous firm should share the persistency of the ring-fenced policies with the hiring firm. The persistency will be calculated on a case-count basis.

18. To ensure effectiveness of this measure, LIA members undertake to share information regarding persistency ratio of insurance products when asked by other FA firms.

19. Depending on the persistency of the ring-fenced policies, the hiring firm is required to adjust the representative's entitlement to sign-on incentives as follows:

Persistency ratio of ring-fenced policies	Proposed Penalty
75% to 100%	No clawback or adjustment to rep's entitlement of sign-on incentives (buffer to allow for policy lapses due to changing client needs/situation and other factors beyond the migrated rep's control)
50% to <75%	Representative's entitlement to his sign-on incentives to be proportionate to his persistency ratio when it falls below 75%: ▪ 74% persistency ratio corresponds to 26% clawback ▪ 50% persistency ratio corresponds to 50% clawback
0% to <50%	For representatives with persistency ratio below 50%, the hiring firm is required to effect 100% clawback of sign-on incentives as such a low persistency ratio is indicative of improper conduct and/or competency issues.

20. The insurer or related FA firm is required to appoint an independent external party to verify and report to MAS that it has complied with Measure 3 at the end of the 2 year period.

MEASURE 4: ENHANCED MONITORING OF REPRESENTATIVES FOR AT LEAST 2 YEARS

Rationale

21. This measure seeks to encourage quality advice from representatives.

22. When mass recruitment (as defined in paragraph 8) has occurred, the insurer or related FA firm is to engage an independent external party to conduct a pre-transaction survey of all (100%) transactions involving representatives that receive sign-on incentives pegged to sales targets.

23. The proposed independent external party and the scope of work to be performed by this entity should be discussed with MAS.

24. Minimally, 50% of the surveys are to be conducted through a call-back. The remaining customers may be surveyed through other means. The pre-transaction surveys should be completed within

the free-look or cancellation period of the product. Where the recommendation is made for an investment product which is time sensitive, the firm should complete the pre-transaction checks within 5 business days from the effective date of the transaction.

25. The work done by the independent external party is to be reported to the insurer's/ FA firm's Board and MAS on a quarterly basis. The insurer/FA firm will be required to engage MAS on the suitability of the proposed entity and the work scope to be carried out.

26. In addition, the representatives are to be subjected to the requirements that are imposed on "Selected Representative" under the BSC framework, i.e. subject to the higher sampling size of 10% for post-transaction documentation review.

** End **