

Members' Undertaking No. 49  
21 November 2012

To: Ordinary and associate members

**LIA STANDARDS FOR DISTRIBUTORS ON DETERRENCE OF UNDESIRABLE SWITCHING**  
(Incorporating MU 18/00 - LIA Guidance Notes on Monitoring Practices of Churning carried out by Insurance Intermediaries)

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**ACTION**

- 1. THIS MEMBER'S UNDERTAKING REPLACES MU 49/07 OF 23 NOV 2007 AND TAKES EFFECT ON 1 JAN 2013.**
- 2. FOR ORDINARY MEMBERS' COMPLIANCE**
- 3. FOR ASSOCIATE MEMBERS' INFORMATION**

**The LIA Standards for Distributors on Deterrence of Undesirable Switching are compulsory for LIA members, and are minimum principles or standards unless otherwise stated.**

The LIA Guidance Notes on Monitoring Practices of Churning carried out by Insurance Intermediaries set out recommendations to assist compliance officers in monitoring and detecting the practice of undesirable switching carried out by representatives.

2012 changes are highlighted in yellow.

**LIA SECRETARIAT**

## LIA STANDARDS FOR DISTRIBUTORS ON DETERRENCE OF UNDESIRABLE SWITCHING

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### A. SWITCHING

#### **Definition under FAA-N01**

The said Notice and any other relevant MAS directives, including FAA-G10 MAS Guidelines on Switching of Designated Investment Products, apply to both single premium and regular premium life insurance policies and other Designated Investment Products such as unit trusts.

"Switching" includes activities such as:

- Giving up a single premium policy, whether fully or partially; and followed by buying of another policy or unit trust or topping up of another policy.
- Giving up a regular premium policy, whether fully or partially, for another policy or unit trust.

#### **Definition under FAA-G10**

"Switching" includes a situation where a client disposes of, or reduces his interest in, all or part of an investment product to acquire, or increase his interest in, all or part of another investment product.

- Improper switching: Switch that is detrimental to client's interest.
- Types of switching: Internal or cross-FA switching.

#### **Replacement of regular premium policies**

Specifically, where a regular premium policy is replaced within 12 months previous to the new policy being purchased (minus 12 months) or after the purchase of the new policy (plus 12 months), no commission will be paid on minus 12 months cases; and commission will be clawed back on plus 12 months cases.

#### **Replacement of single premium policies**

Specifically, where a single premium policy is replaced within **120** days previous to the new policy being purchased (minus **120** days) or after the purchase of the new policy (plus **120** days), no commission will be paid on minus **120** days cases; and commission will be clawed back on plus **120** days cases.

The following practices are minimum and mandatory standards. Insurers may apply stricter requirements.

#### **Source of funds**

Rule applies to transactions involving the same source of funds, i.e. CPFIS policy replaced by CPFIS policy; Cash-funded policy replaced by cash-funded policy. (CPFIS-OA to / from CPFIS-SA is to be treated as same source.)

#### **Regular premium vs. Single premium**

Rule applies to replacement of similar policies, i.e. SP with SP; and RP with RP.

#### **Treatment of commission for different reinvestment amount**

When the reinvested amount is greater than the prior withdrawal, commission is to be paid only on any excess amount over the original investment amount.

### Appendices C and D

The appendices should not apply to Single Premium replacements, on the rationale that unlike RP policies, lump sum contracts are a one-off transaction for investment purpose.

### **Deterring switching of designated investment products that is to the longer term detriment of the consumer**

#### Objective

To warn the policyholder of the disadvantages of making a withdrawal, so that he can make an informed decision.

**Good practice:** It is good practice for financial advice to be provided where customers intend to purchase or surrender a life insurance policy.

#### Rationale

1. Consumers are principally responsible for their decisions to buy or sell financial products.
2. Effective disclosure is a positive step in the right direction for manufacturers and consumers.

### **Front-end controls**

All front-end controls should cover situations which involve switching between different designated investment products and different FAs.

Disclosures and client declarations should cover cross-product switching.

- A question on replacement is to be asked in the proposal form. However, the requirement of uniform verbatim wordings is lifted.

FAs should ensure that disclosure on the costs and disadvantages of switching is clearly presented and easily understood by clients.

**Good practice:** Sales documents should allow the representative's supervisors to document the follow-up actions to be taken should they disagree with their representative's switching recommendation.

### **Back-end controls**

Disclosures and client declarations should cover cross-product switching.

FAs should ensure that disclosure on the costs and disadvantages of switching is clearly presented and easily understood by clients.

### **Disclosures and sign-offs in a form and a letter**

**Appendix A - Withdrawal Form (for investment-linked policies, whether single premium or regular premium)**

**Appendix B - Withdrawal Form (for traditional policies, whether single premium or regular premium)**

Appendix C - Letter to be issued where regular premium policy has been lapsed (minus 12 months)

Appendix D - Letter to be issued where regular premium policy is intended to be lapsed (plus 12 months)

### Scope of Appendix C

Letter in Appendix C applies to:

- Cases where lapsation took place up to 12 months previous to the new policy being proposed
- Cases involving policies of "this office" only or where the insurer is the "other office"
- With regards to: ☐ *Keep the new policy and reinstate the old policy* - where the insurer is the "other office", it is for the policyowner to take action to reinstate the old policy.

### Scope of Appendix D

Letter in Appendix D applies to:

- Cases where lapsation may take place up to 12 months after proceeding with the new proposal
- Cases involving policies of "this office" only or where the insurer is the "other office"
- Where the policyowner does not reply, it means that he wants to buy the new policy (and he may or may not lapse the existing policy).

During the two weeks given, underwriting of the new policy should proceed as per normal and cover should be extended provided premiums have been paid.

### Wordings for Appendices A, B, C and D

The texts of Appendices A and B are uniform wordings to be adopted by all insurers, subject to the following clarifications:

1. Items that are not applicable or not relevant to a particular insurer may be omitted, e.g. policy loan (does not apply to CPFIS policies).
2. Product-specific items may be added, e.g. surrender penalty (in place of item on bid-offer spread).
3. **Company-specific terminology may be used.**
4. More stringent requirements may be added.

The requirement of uniform wordings is lifted for Appendices C and D.

### Penalties

1. FAA penalty under S.58(5) applies: *any person who contravenes any requirement specified in a written direction issued by the Authority (which would include this Notice), shall be guilty of an offence and shall be liable on conviction to a fine not exceeding \$25,000 or to imprisonment for a term not exceeding 12 months or to both and, in the case of a continuing offence, to a further fine not exceeding \$2,500...*
2. Life insurers will additionally take appropriate actions including commission claw back and dismissal.

Specifically, where a regular premium policy is replaced within 12 months previous to the new policy being purchased (minus 12 months) or after the purchase of the new policy (plus 12 months), no commission will be paid on minus 12 months cases; and commission will be clawed back on plus 12 months cases.

### **Appeal under FAA Notice No. 05**

4 . . . *In addition, financial advisers should have an internal process for addressing the appeals made by their representatives with respect to the disciplinary action taken against them.*

Where a regular premium policy is replaced after the purchase of the new policy (plus 12 months), if the insurer accedes to its representative's appeal, claw-back will be waived.

## **B. TWISTING**

### **Prohibition on twisting**

The principal shall have a condition to prohibit an industry-experienced representative who joins his company from directing away any policy of a previous insurer to a new insurer where this would be detrimental to the interest of the customer.

Operational note: The requirement for such a prohibition is a minimum standard, but there are no uniform wordings to spell out this condition.

## **LIA GUIDANCE NOTES ON MONITORING PRACTICES OF CHURNING CARRIED OUT BY INSURANCE INTERMEDIARIES**

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Note: The terms used here pre-date FAA but have been left “as is”.

### **Practice of churning involves one or more of the following elements**

- Various modal premiums, i.e. regular premium policy, single premium policy or single premium top-up to a regular premium policy.
- Different types of policies, whereby a traditional policy is replaced by an investment-linked policy or vice versa.
- More than one insurer, whereby a policy of Insurer A is replaced by a policy of Insurer B. \*

\* Point of clarification:

The measures stated in these guidelines for prevention and detection of churning are to be applied only to ‘own company’ policies issued by the insurer that is carrying out the measures. The insurer is to check for ‘cross company’ churning only if a complaint has been received or such information has been brought to its knowledge.

### **Forms of churning**

Churning may be effected through many forms of activities and/or mechanisms. Some examples are:

- Terminating a policy within a short period of time or before its maturity date and buying a new policy soon after.

(In principle, policies without a fixed duration should be sold on a medium to long term basis and are therefore expected to be kept for at least five years.)

- Terminating a cash policy and buying a similar CPFIS policy, or vice versa, when a change of payment source or conversion could have been exercised.
- Withdrawing from old funds or plans and buying into new funds or plans without using the facility available in the policy for switching of funds where commissions are not payable.
- Generating funds in order to buy a new policy, by:
  - exercising various methods of withdrawing monies from an existing policy, including making partial surrender, withdrawing from investment-linked policy, taking policy loan, cashing out reversionary bonus; or
  - exercising various methods of reducing or ceasing an existing regular premium commitment, including advance premium loan, vanishing premium, reduction of sum insured, conversion of the existing regular premium policy to paid-up policy or extended term insurance.

(Old policies sold on the basis of vanishing premium illustration produced by the insurer are accepted.)

Examples of how such funds may be generated include the use of the following types of mechanisms:

- Policy termination
- Partial withdrawal
- Advance/Automatic premium loan
- Policy loan

- Premium holiday
- Surrender of bonus
- Reductions in premiums

### **Measures for prevention and detection of churning**

#### **Prevention**

The insurer may adopt preventive measures. Some measures are:

- In the training of insurance intermediaries, insurers should:
  - emphasise the seriousness of the prohibition on churning;
  - warn that they are not authorised to give their own opinions to clients on the types of investments that are suitable, investment trends, or the timing to make withdrawals and purchases especially with respect to investment-linked policies, all of which amount to the giving of investment advice and unless they hold an investment adviser's license.

#### **Detection**

The insurer may conduct regular checks for possible trends of churning activities carried out by insurance intermediaries. Some indicators of churning are:

- Policies terminated within a short period of say a year or two, or immediately after payment of the final/last commission due.
- New policy/ies taken up soon after the termination of an old policy (say within six months) or vice versa.
- Either the new additional policy or the old policy is subsequently terminated due to over-commitment arising from client's purchase of that new additional policy.
- Surrenders/withdrawals made that resulted in investment losses to the policyholders.
- Monies withdrawn from investment-linked policies and reinvested at a higher price.
- Old and new policies funded from the same source, e.g. CPF savings.
- Funds for new policies channeled from old policies through mechanisms such as surrender (full or partial), top-ups, withdrawal, conversion to paid-up, reduction in sum insured/premium and lapsation.
- A new policy that provides benefits similar to the discontinued policy but which is funded from a different source, e.g. replacing a cash-funded endowment with a CPF-funded endowment.
- A significant portion of the agent's/broker's cases, production or earnings from replacement activity.
- High number of replacement cases.
- Unusual trends such as switching after the "window period" (LIA replacement rules).
- High number of replacement cases when new funds or new products are launched.
- Mechanism to assess the risk of cross-product switching, i.e. from life policy to unit trust or vice versa.
- Poor persistency.

[Note: It is a requirement for this section to be laid out in a box.]

### **IMPORTANT NOTICE**

#### **What you should know about early full or partial withdrawal of your Investment-Linked Policy**

1. An insurance policy is intended to meet your long-term financial needs. Therefore, it may be disadvantageous for you to fully or partially withdraw a policy before its maturity date. Some disadvantages are:

- You are losing valuable benefits from the policy:
  - You are losing the insurance protection offered by your policy;
  - You may not be able to achieve your intended financial objective;
  - This may result in losing the financial benefit accumulated over the years.
- It may not be possible for you to obtain a similar level of protection on the same terms in the future.
  - You may not be insurable on standard terms;
  - You may have to pay a higher premium in view of higher age;
  - Withdrawing your insurance policy for another policy could result in loss of specific policy features due to changes in age or health.

2. **Additional Charges/Fees**

If you withdraw your investment-linked policy, fully or partially and then buy a new investment-linked policy or other investment product, or top up on your existing investment-linked policy or other investment product, you will incur new charges. These may include:

- **Distribution Fee**

Commission is paid to Agents/Financial Advisers on all new insurance policies / investment products.

- **Administration Charge**

There could be some sales charge/withdrawal fee that is charged for each new policy / investment product.

The sales charge/withdrawal fee can be as high as  $x\%$  of your investment-linked fund. Hence, on a single premium investment of S\$10,000, a sales charge of S\$ $x00$  would be deducted. [Operational note: For insurers to use own example.]

- **Policy Fee**

A policy fee is usually incurred for each policy.

3. **Fund Switching Facility**

When the fund you have bought is not meeting your initial or current investment objective, you may switch to other fund(s) offered by the Company at its bid price without incurring any charges.

4. **Other Options**

You may enquire whether there are other options available under your policy to meet your short term financial needs. Some options are:

- Opt for a premium holiday if your policy has accumulated cash value. This allows you to temporarily stop paying premiums; or
- Reduce the policy regular premiums (applicable only to regular premiums policies). This allows you to reduce your ongoing financial commitment to the policy.

5. **Seeking Advice From Your Adviser**

Therefore, it is important to seek advice from your Adviser before early full/partial withdrawal of your investment-linked policy or other investment product. Your Adviser can advise you on your options other than withdrawing the policy, explain the implications of each option and provide appropriate recommendations to you, taking into account your investment objectives, financial situation and particular needs.

#### **Policyowner / Trustee / Assignee's Acknowledgement**

|                                                         | Yes                      | No                       |
|---------------------------------------------------------|--------------------------|--------------------------|
| Were you advised by an Adviser to withdraw this policy? | <input type="checkbox"/> | <input type="checkbox"/> |

If "yes", please ask your Adviser to complete the "Adviser's Acknowledgement" below.

I have read and understood the above statements. I am aware that should I wish to buy a similar policy in future I may incur additional charges and I may not be able to secure similar terms and conditions.

I want to withdraw my policy (fully or partially) ☐

I want to maintain my policy \* ☐

\_\_\_\_\_  
Signature of Policyowner/Trustee/Assignee      Date

[\* Operational note: For insurers, this is an optional item.]

Adviser's Acknowledgement

I have explained to the above Policyowner / Trustee / Assignee the alternative options available and the implications of early withdrawal of this investment-linked policy. I have recommended (*the policyowner may not be his client yet*) the withdrawal of this policy for the following reasons:

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_  
Signature of Adviser      Adviser's Code

\_\_\_\_\_  
Name of Adviser      Date

[Note: It is a requirement for this section to be laid out in a box.]

### **IMPORTANT NOTICE**

#### **What you should know about early surrender of your Insurance Policy**

1. An insurance policy is intended to meet your long-term financial needs. Therefore, it may be disadvantageous for you to surrender a policy before its maturity date. Some disadvantages are:
  - You are losing valuable benefits from the policy:
    - You are losing the insurance protection offered by your policy;
    - You may not be able to achieve your intended financial objective;
    - This may result in losing the financial benefit accumulated over the years.
  - It may not be possible for you to obtain a similar level of protection on the same terms in the future.
    - You may not be insurable on standard terms;
    - You may have to pay a higher premium in view of higher age;
    - Surrendering your insurance policy for another policy could result in higher premiums and loss of specific policy features due to changes in age or health.
2. **Additional Charges/Fees**

If you surrender your policy and then buy a new policy or other investment product you will incur new charges. These may include:

  - **Distribution Fee**  
Commission is paid to Agents/Financial Advisers on all new insurance policies / investment products.
  - **Policy Fee**  
A policy fee is usually incurred for each policy.
3. **Other Options**

If your policy has acquired a cash value, you may choose to:

  - Apply for a cash loan to meet short term financial needs; or
  - Convert to a reduced or paid up extended term insurance policy; or
  - Reduce the policy regular premiums (applicable only to regular premiums policies).
4. **Seeking Advice From Your Adviser**

Therefore, it is important to seek advice from your Adviser before early surrender of your policy. Your Adviser can advise you on your options other than withdrawing the policy, explain the implications of each option and provide appropriate recommendations to you, taking into account your investment objectives, financial situation and particular needs.

#### **Policyowner / Trustee / Assignee's Acknowledgement**

|                                                          | Yes                      | No                       |
|----------------------------------------------------------|--------------------------|--------------------------|
| Were you advised by an Adviser to surrender this policy? | <input type="checkbox"/> | <input type="checkbox"/> |

If "yes", please ask your Adviser to complete the "Adviser's Acknowledgement" below.

I have read and understood the above statements. I am aware that should I wish to buy a similar policy in future I may incur additional charges and I may not be able to secure similar terms and conditions.

I want to surrender my policy ☐  
 I want to maintain my policy \* ☐

\_\_\_\_\_  
 Signature of Policyowner/Trustee/Assignee

\_\_\_\_\_  
 Date

\_\_\_\_\_  
 Policy Number

[\* Operational note: For insurers, this is an optional item.]

#### **Adviser's Acknowledgement**

I have explained to the above Policyowner / Trustee / Assignee the alternative options available and the implications of early surrender of this insurance policy. I have recommended *(the policyowner may not be his client yet)* the surrender of this policy for the following reasons:

\_\_\_\_\_  
Signature of Adviser                      Adviser's Code

\_\_\_\_\_  
Name of Adviser                      Date

The requirement of uniform wordings is lifted for Appendices C and D.

Disclosures and client declarations should cover cross-product switching.

FAs should ensure that disclosure on the costs and disadvantages of switching is clearly presented and easily understood by clients.

**Letter to be issued on discovery of replacement through lapsation of RP policy**

[dd/mm/yy]  
[Name of Insured]  
[Address]

Dear Sir/Madam/Name of Insured

Old Policy No: XXXXXXXXXX      Status: Lapsed on dd/mm/yy  
New Policy No: XXXXXXXXXX      Status: New Policy commenced on dd/mm/yy

We noticed that you have terminated your old policy within 12 months of your purchase of a new policy.

We wish to emphasize that it is usually disadvantageous to replace an existing life insurance policy with a new one. Some disadvantages are:

- You may not be insurable on standard terms;
- You may have to pay a higher premium in view of higher age;
- This may result in losing the financial benefit accumulated over the years.

In your own interest, we would advise that you consult your adviser of the terminated policy for a review of the lapse. We wish to offer you two options shown below in the event that you were not aware of the disadvantages of replacing one policy with another and wish to reinstate your terminated policy.

**Please indicate your choice below and return this letter to us in the self-addressed envelope.**

**If we do not hear from you within 2 weeks from the date of this letter, we will assume that you want to continue with the new policy and leave the old policy as lapsed.**

Thank you.

Yours sincerely

**Replacement of Policy - Confirmation by Policyowner**

Name of Policyowner: \_\_\_\_\_ (New) Policy No: \_\_\_\_\_

I confirm that I am aware of the disadvantageous of replacing my old policy with a new one and I have decided to (please tick one of the boxes below):

- ☐ Keep the new policy and reinstate the old policy.
- ☐ Reinstate the old policy and cancel the new one. (The premiums paid under the new policy will be refunded to me upon reinstatement of my old policy.)

\_\_\_\_\_  
Signature of Policyowner

\_\_\_\_\_  
Date

The requirement of uniform wordings is lifted for Appendices C and D.

Disclosures and client declarations should cover cross-product switching.

FAs should ensure that disclosure on the costs and disadvantages of switching is clearly presented and easily understood by clients.

**Letter to be issued when proposer informs that the  
proposal is to replace or is intended to replace an RP policy**

[dd/mm/yy]  
[Name of Insured]  
[Address]

Dear Sir/Madam/Name of Insured

Plan Proposed: XXXXXXXXXX  
Date of Proposal: dd/mm/yy

We notice from your proposal form that you are replacing an existing policy with the new policy proposed.

We wish to advise that it is usually disadvantageous to replace an existing life insurance policy with a new one. Some disadvantages are:

- You may not be insurable on standard terms;
- You may have to pay a higher premium in view of higher age;
- This may result in losing the financial benefit accumulated over the years.

In your own interest, we would advise that you consult your adviser of the decision. If you have sent in premiums with the proposal, we wish to offer you a refund of the premiums in the event that you were not aware of the disadvantages of replacing one policy with another and do not wish to proceed with the proposal.

**If we do not hear from you within 2 weeks from the date of this letter, we will assume that you want to continue with the new policy.**

Yours sincerely