



Monetary Authority
of Singapore

Information Paper: Good Practices Relating to Disciplinary Action Framework in the Financial Advisory Industry

March 2021



Introduction

The MAS Information Paper on Culture and Conduct Practices of Financial Institutions (FIs) outlines the outcomes that FIs should work towards in promoting a culture of trust and ethical behaviour. Consequence Management has been highlighted as an area where FIs should put in place proper frameworks and processes to determine the severity of misconduct committed and the corresponding disciplinary actions (DA) to be taken.

A strong DA framework requires appropriate governance structures, including a robust set of policies and procedures (P&Ps) for sound implementation of the framework. Other important elements include having a robust decision-making process, ways to ensure accountability of supervisors, and keeping the framework relevant.

Having a robust DA framework will serve to shape the right behaviours among the representatives of financial advisers (FAs) as they will be aware of the consequences of committing misconduct and not acting ethically and professionally.

OBJECTIVES

The objectives of this Information Paper on Good Practices Relating to Disciplinary Action Framework in the Financial Advisory Industry are to:

- ✓ Provide guidance to financial advisers on sound principles in key areas of their DA framework, in order to achieve more consistent outcomes in their application of DA; and
- ✓ Raise standards among financial advisers through sharing of good practices

The good practices contained in this paper were compiled from a thematic review of the DA frameworks of FAs serving retail customers, comprising banks, insurers, licensed financial advisers, and insurance brokers. The review was conducted over the course of 2018 and 2019. The Life Insurance Association worked closely with MAS in producing this paper.

While this paper is meant to apply to financial advisers serving retail customers, other players in the financial services industry are encouraged to take guidance from the good practices in this paper and adapt them as necessary to suit their own circumstances and business needs.

12 good practices in these 4 areas:



Policies and Procedures



Decision-making process



Accountability of Supervisors



Relevance of the DA framework

Summary of good practices

POLICIES AND PROCEDURES (P&Ps) – FAs should set out clear guidelines on the conduct and behaviours expected of their representatives, and provide a set of factors that decision makers should consider when meting out DAs so that these are fair and consistent.

- 1** The P&Ps provide descriptions of various misconduct and the applicable DAs.
- 2** The P&Ps set out examples of aggravating and mitigating factors for consideration when meting out DAs.
- 3** FAs adopt a combination of remedial measures and DAs in their DA framework, depending on the nature and severity of the misconduct committed.

DECISION-MAKING PROCESS – FAs should have an independent, structured and well-documented decision-making process for handling DAs and appeals.

- 4** The Disciplinary Committee (DC) and Appeal Committee (AC) comprise independent and senior staff from diverse functions.
- 5** There are clear principles in place to guide decision makers in deliberating DAs to be taken and reviewing appeals.
- 6** In the absence of a DC and/or AC, serious misconduct and appeals are escalated to senior management for deliberation and approval.
- 7** There is proper documentation of the basis of decisions made on DAs and appeals.
- 8** There is a clear timeline for representatives to lodge an appeal and for FAs to respond to the appeal.

ACCOUNTABILITY OF SUPERVISORS – FAs should hold supervisors accountable for the misconduct committed by representatives under their supervision in cases where the misconduct resulted from dereliction of their supervisory duties.

- 9** FAs perform a holistic assessment of the accountability of supervisors for all misconduct committed by the representatives under their supervision and take appropriate action against the supervisors.

RELEVANCE OF THE DA FRAMEWORK – FAs should regularly review their DA frameworks to keep them relevant and robust.

- 10** The DA framework is reviewed regularly to take into account evolving business practices and emerging risk areas.
- 11** The DA framework, including any updates, is approved by appropriate approving parties.
- 12** FAs share case studies of past misconduct via various channels such as townhalls, team meetings, risk forums, newsletters and training sessions.

Policies and Procedures

Having robust P&Ps is an important element of a strong internal governance framework for managing market conduct risks. P&Ps document a set of guidelines for all representatives, on the conduct and behaviours expected of them and the consequences if they fail to comply with the guidelines. The P&Ps also set out the factors to consider when deciding on the appropriate DA to mete out when misconduct has been committed.

1 The P&Ps provide descriptions of various misconduct and the applicable DAs.

- FAs should define the different types of misconduct and the corresponding DAs to be meted out in the P&Ps after considering various factors, including severity of the misconduct (e.g. breach of law and regulations). The DA should be commensurate with the severity of the misconduct. For example, representatives found to have committed egregious acts such as deliberately misrepresenting product features to clients or falsifying client's information should be suspended or terminated.
- Where possible, examples or case studies should be included in the P&Ps. This facilitates the DC or other decision makers in meting out DAs that are fair and consistent, and educates representatives on the do's and don'ts in their conduct of FA services.

2 The P&Ps set out examples of aggravating and mitigating factors for consideration when meting out DAs.

- FAs should set out a set of aggravating and mitigating factors in their P&Ps to ensure that the DAs meted out are effective, consistent and fair.

Examples of aggravating and mitigating factors (non-exhaustive)

Aggravating factors

- Representative committed multiple substantiated misconduct involving the same client.
- Representative displayed recalcitrant behaviour.
- Client and/or FA suffered detriment such as financial loss, erosion of trust/reputational risk and loss of insurance protection.
- Client belonged to the vulnerable group¹.
- Representative attempted to frustrate or impede investigations into the misconduct.
- Representative committed misconduct over multiple occasions in a short span of time.
- Representative displayed malicious intent for self-gain.

Mitigating factors

- Representative has no prior disciplinary record.
- Client and/or FA did not suffer detriment.
- Representative was co-operative during the investigation or voluntarily owned up to the misconduct.
- Representative did not derive any benefits from the misconduct.
- Representative's misconduct arose from the FA's poor controls or inadequate training and guidance provided to them.
- Representative did not display malicious intent.

¹ Minimally to include selected clients, i.e., individuals who meet two or of the following criteria:

(i) aged 62 years or older (ii) is not proficient in written or spoken English and (iii) has below GCE 'O' level or 'N' level qualifications, or equivalent academic qualifications. Some FAs have identified vulnerable clients beyond selected clients such as individuals who are mentally, physically or visually challenged.



Observations of Demerit Points System

Some FAs adopt a Demerit Points System (DPS) to complement their DA framework. In addition to the DAs meted out, demerit points are issued to errant representatives and supervisors, depending on the severity of the misconduct. Harsher actions will be taken against representatives and supervisors as the demerit points accumulate.

A well-calibrated DPS has its merits as it provides gradation to the DAs taken. This allows FAs to mete out harsher DA when necessary, similar to how firms consider aggravating factors when deliberating DAs. It may be effective in deterring recalcitrant behaviour if more severe penalties are taken as demerit points accumulate. However, over-reliance on DPS may result in a mechanistic approach in meting out DAs and result in the DA framework being more lenient if it is not properly calibrated. Hence, FAs should consider holistically whether a DPS is useful or necessary for the FA, taking into account how robust its DA framework currently is.

Elements of an ineffective DPS

- The same demerit points are issued to most types of misconduct, resulting in insufficient gradation of severity in the different types of misconduct committed.
- The points thresholds are set too high, resulting in more severe DAs being meted out only after the representative has committed several serious misconduct.
- A short reset period may result in the DA framework not taking into account past misconduct, thereby not properly penalising representatives who commit multiple misconduct over an extended period of time.

Elements of a robust DPS

- The demerit points threshold is well-calibrated, where:
 - Demerit points increase with the severity of misconduct.
 - More severe penalties are imposed on recalcitrant representatives as their demerit points accumulate.
- There is a longer reset period before demerit points are refreshed to a clean slate.



Policies and Procedures

3 FAs adopt a combination of remedial measures and DAs in their DA framework, depending on the nature and severity of the misconduct committed.

- FAs should impose additional measures such as re-training and close supervision on top of the usual DAs (i.e. verbal/written forms of DA, suspension, and termination) where necessary, so that the resulting actions are more effective in remediating errant behaviour.

Examples of additional remedial actions (non-exhaustive)

Re-training and coaching

Close supervision / joint field work

Suspension from promotion / receiving incentive and awards

Commission claw-back



Decision-making process

The decision-making process for handling DAs and appeals should be robust and transparent. In order for representatives to have trust in the decision-making process, the DAs issued should be fair and consistent. FAs should also provide an avenue of appeal to representatives.

Some FAs appoint committees to assess DAs and appeals while others rely on independent functional units or senior management to do so. There is no one-size-fits-all model. FAs should assess what works best for them based on the nature of their business and needs. It is more important to ensure that the decision-making committees (such as the DC/AC) or the departments/individuals responsible for meting out DAs and appeals are independent and comprise staff of sufficient seniority.

4 The DC and AC comprise independent and senior staff from diverse functions.

Diversity and composition of DC/AC

- DC/AC members from a diverse range of functions such as human resources, finance, operations, risk/compliance and sales will be able to provide expert views based on their domain expertise. This will, in turn, result in the decisions of the DC/AC being more robust.

Independence of DC/AC

- If individuals from the sales and advisory function are represented in the DC/AC, the FA should ensure that their presence do not pose any conflicts of interest (e.g. these individuals are not directly involved in the sales process or do not supervise the representatives that are the subject of the DA or appeal).

Composition of AC

- To minimise conflicts of interest and promote alternative views, the DC and AC should comprise different personnel.
- The AC should generally comprise more senior members than the DC, where possible, given that the AC is responsible for reviewing the decisions made by the DC.

Decision-making process

5 There are clear principles in place to guide decision makers in deliberating DAs to be taken and reviewing appeals.

- While most FAs have guiding principles to help decision makers in deliberating DAs to be taken, this is less evident in the case of reviewing appeals. The P&Ps or the Terms of Reference should set out additional areas for decision makers to consider when reviewing appeals. For example, firms could set out guiding principles on when to accept or reject appeals, or which appeals may result in a harsher penalty.

6 In the absence of a DC and/or AC, serious misconduct and appeals are escalated to senior management for deliberation and approval.

- Serious misconduct should be escalated to persons of higher seniority (e.g. Heads of Department or CEO). This ensures that there is proper management oversight and governance to deal with serious misconduct and appeals.
- FAs can consider establishing an approval protocol (e.g. committee, forum or designated staff) to deal with misconduct of different severity and their corresponding DAs.

7 There is proper documentation of the basis of decisions made on DAs and appeals.

- FAs should document the basis of their decisions (e.g. in the minutes of meeting), especially when there is a deviation from precedent cases or recommended actions set out in the DA framework and P&Ps.
- Proper documentation allows easy reference of precedent cases, which in turn promotes more consistent DA outcomes. It also provides an audit trail in the event of dispute between FAs and their representatives.

8 There is a clear timeline for representatives to lodge an appeal and for FAs to respond to the appeal.

- FAs should set out clear timelines in their P&Ps so that all parties are aware of their rights and obligations. This will also minimise disputes between FAs and their representatives.



Accountability of Supervisors

Besides managing the sales performance of their representatives, supervisors are also accountable for how their representatives conduct their FA activities. Supervisors should discharge their supervisory duties diligently and impart the right values to their representatives through coaching, training and regular interactions with them.

As supervisors play a crucial role in shaping the right conduct and values among their representatives, FAs should hold supervisors accountable when the representatives under their supervision commit misconduct or when their conduct fall short of the standards expected of them. The impetus to do so is greater in cases where the misconduct arose due to the supervisor's dereliction of his or her supervisory duties.

9 FAs perform a holistic assessment of the accountability of supervisors for all misconduct committed by the representatives under their supervision and take appropriate action against the supervisors.

- The DA framework should provide guidance on the DAs to be meted out against supervisors, taking into account their own conduct as well as that of the representatives under their supervision.
- Besides penalising the representative involved in the misconduct, FAs should also consider appropriate actions to take against the supervisor whose failure to properly discharge his or her supervisory duties led to the representative committing the misconduct.
- FAs should review the market conduct trends, compliance history and other key indicators (such as the number and nature of complaints received and misconduct committed, Balanced Scorecard grades and persistency rates) of the agency units or branches of their supervisors and take appropriate action against supervisors with a poor track record of misconduct and complaints in their agency units or branches.



Relevance of the DA framework

In order to maintain a robust and effective DA framework, FAs should keep the framework relevant and fit for purpose, given that the modus operandi of misconduct and the firm's business model may evolve over time (e.g. new distribution channels, use of social media for marketing and advertising, and new financial products being sold).

10 The DA framework is reviewed regularly to take into account evolving business practices and emerging risk areas.

- It is important that FAs conduct regular reviews of their DA framework or introduce separate frameworks to keep pace with changes in their business model as well as new and emerging risk areas.
- To ensure that the DA framework is effectively implemented and properly adhered to, FAs should include their DA framework in compliance and/or audit reviews.

11 The DA framework, including any updates, is approved by appropriate approving parties.

- There should be an appropriate approval process to approve the DA framework and any subsequent changes. In addition, the Board and/or senior management should be kept informed of major changes.

12 FAs share case studies of past misconduct via various channels such as townhalls, team meetings, risk forums, newsletters, and training sessions.

- Sharing case studies (both internal and external) of past misconduct committed by representatives with all representatives on a regular basis enables FAs to educate their representatives on what constitutes an offence or misconduct, what conduct or behaviour is considered unethical, and helps increase risk awareness among representatives.
- It also allows FAs to reinforce their corporate culture and values, as well as the standards and behaviours expected of their representatives.



Conclusion

FAs should review their existing DA framework regularly and benchmark them against the good practices set out in this information paper. Where gaps or shortcomings are identified, FAs should take steps to enhance their frameworks.

MAS looks to the Boards and senior management of FAs to ensure that their DA framework and processes are robust and effective in inculcating ethical and professional conduct among their representatives and supervisors, and in deterring misconduct in the industry.

MAS will continue to work with the industry to elevate standards of culture and conduct among FAs and in the financial sector as a whole.



Monetary Authority
of Singapore

**Information Paper:
Good Practices Relating to
Disciplinary Action
Framework in the Financial
Advisory Industry**

March 2021