

# **RESPONSE TO FEEDBACK RECEIVED - CONSULTATION ON DRAFT INFORMATION PAPER ON GOOD PRACTICES FOR LICENSED FINANCIAL ADVISERS AND EXEMPT FINANCIAL ADVISERS**

On 24 June 2004, MAS issued for public consultation the draft Information Paper on Good Practices for Licensed Financial Advisers and Exempt Financial Advisers ["the Paper"]. The aim of the Paper was to share with the industry good practices adopted by financial advisers ["FAs"] and to guide FAs in enhancing their advisory and sales process, complaints handling and compliance processes, and training and competency plans.

The consultation period closed on 24 July 2004. MAS received comments from 17 respondents (listed in the Annex), two of whom requested confidentiality. MAS has considered carefully all comments received and incorporated them in the Paper where appropriate.

MAS thanks all respondents for their feedback. We summarise below some of the comments received and our responses to the comments.

## **1 General comments**

1.1 Several respondents sought clarification on the legal status of the Paper. There was concern that the Paper imposed additional obligations on FAs in their provision of financial advisory services.

### MAS' Response

We wish to clarify that the Paper has no force of law. It is meant to share with FAs good practices that we have observed during our supervision of FAs so as to assist them in enhancing their systems and processes to render consistently high quality advice to their clients. Where applicable, we have stated the relevant FAA provisions in the Paper to set out the context of the subject so as to provide better guidance to the industry.

1.2 Some respondents were unclear as to whom the Paper was intended, and whether the Paper was meant to cover all aspects of financial advisory services regulated under the Financial Advisers Act ["FAA"].

### MAS' Response

The Paper is directed at sales practices of FAs that deal primarily with non-accredited retail investors. By sharing the good practices, we hope to see improvements in the standards of advisory and sales services of FAs dealing with non-accredited retail investors, as such clients are less able to look after their financial interest. The Paper is not intended to apply to: (i) specialised units of FAs that service high net worth individuals; (ii) FAs that deal with accredited investors, corporations, or persons whose business involves the acquisition and disposal of or holding of securities (whether as principal or agent); and (iii) FAs that provide financial advisory services through the issuance or promulgation of research reports, where the research reports do not have regard to the investment objectives, financial situation and particular needs of clients.

1.3 One respondent commented that FAs should not resort to using fine print or legal/technical jargon in their promotional materials. Advertisements should also not present facts in a way that may mislead investors.

### MAS' Response

FAA Notice on Information to Clients and Product Information Disclosure ["Notice FAA-N03"] requires advertisements and marketing materials used by the FAs to contain information that is clear, adequate and not false or misleading. In addition, Regulation 29 of the Securities and Futures (Offers of Investments) (Collective Investment Schemes) Regulations 2002 requires advertisements for collective investment schemes to be clearly legible and have a minimum font size of 8 point Times New Roman where they appear in newspapers, periodicals, magazines or letters, electronic mails or websites.

FAs are also expected to observe any guidelines on the use of marketing materials issued by the industry associations of which they are members.

## **2 Sales conducted with clients with limited knowledge of investment products**

2.1 One respondent commented that the recommended measures of having someone to accompany the clients or having the supervisor present during the sales presentation do not seem to achieve the objective of mitigating risk from poor or non-existent

translation as the FA has no assurance that the person accompanying the client is able to make an accurate translation. The respondent suggested requiring a person conversant in both languages to provide an English language certification that he has translated the document for the client and that the client appears to understand the document.

The respondent was also concerned that the recommended practice is not in line with the legal standard that if an investor does not understand a document, he should raise a plea of non est factum, which is a legal recourse.

#### MAS' Response

The measures suggested in the Paper are meant to be additional safeguards to protect the interests of a client who may have difficulty understanding the investment product being recommended by a representative. In cases where the FA is unable to satisfy itself that the client has understood the product, it should refrain from concluding the sale altogether.

Requiring an English language certification may be onerous and add to the operational costs of FAs. Nevertheless, FAs are free to include any other measures to help the client understand the product being sold to him.

Any additional measures put in place by the FA should not preclude clients from pursuing any legal recourse in the event of misconduct or mis-selling.

2.2 One respondent felt that there was no need to impose additional measures as representatives are required to conduct themselves professionally at all times, and the standard of care should not be dependent on the literacy level of the clients. The respondent suggested that clients be required to acknowledge that they have understood the nature of the product being recommended to them, and this should be in four languages so that clients that are not conversant in English will not be disadvantaged.

#### MAS' Response

MAS agrees that the standard of care should be the same for all clients. However, FAs may need to put in place different procedures in order to meet the same standard of care for different clients. The suggestion to obtain clients' acknowledgement and to state the acknowledgement in four languages may not be feasible for clients with low literacy levels.

2.3 One respondent commented that persons accompanying the clients should be restricted to family members.

#### MAS' Response

MAS is of the view that this should be left to the clients and the FAs to decide. The client should be comfortable that the person accompanying him is able to help him understand what is being presented by the representative during the sales process.

2.4 One respondent questioned whether FAs could require supervisors to review the sales recommendation within a certain period, rather than require the supervisor to be present during the sale.

#### MAS' Response

The purpose of having the supervisor present is to serve as an additional check to ensure that the client understands the product being recommended. It would not be possible for the supervisor to ascertain whether the client had indeed understood what was being presented to him during the sales presentation by just counter signing on the sales document without any contact with the client.

### **3 Sales conducted at seminars and promotional events**

3.1 One respondent sought clarification on what would be considered as a "conducive" environment for the conduct of fact-find.

#### MAS' Response

A conducive environment would generally be one in which FAs are able to conduct a proper fact-find and needs analysis for clients. This includes having the necessary financial planning tools, sales documents and other relevant information available at the event site. Clients should not be pressured into making an investment decision due to distractions and time constraint.

### **4 Use of gifts**

4.1 Several respondents requested clarification on what would be regarded to be a gift of nominal value.

#### MAS' Response

In ascertaining whether a gift is of nominal value, FAs should consider whether or not the value of the gift could influence a client to disregard a proper assessment of the investment and enter into a transaction that may not meet his needs. FAs should have controls and procedures to ensure that gifts do not become the main focus of any sales transaction.

## **5 Review of basis for recommendations made by representatives**

5.1 One respondent felt that there could be difficulty in determining a client's reasons for purchasing a product that is not recommended, as the client may not be willing to divulge the relevant information. It was suggested that FAs should only be required to document the fact that it was the client's decision to purchase a product that was not recommended, and to find out the reasons for the purchase only when the FAs have reason to believe that the client should not be purchasing that product.

#### MAS' Response

We agree with the feedback, and will clarify this in the Paper.

5.2 One respondent was of the view that it would be difficult to require supervisors to review all fact-find forms within the stipulated time, and suggested that supervisors be required to review all fact-find forms for clients that are in the high risk categories such as the elderly, and a random sample of the rest.

#### MAS' Response

FAs are required to ensure that there is a reasonable basis for any recommendation made on investment products. Supervisory review is a good practice to ensure that FAs and their representatives comply with the provisions of the FAA.

Life policies and unit trusts provide for free-look/cancellation periods, whereby investors can cancel their purchases within the stipulated period at minimal or no cost. It is good practice for supervisors to review the recommendations made by representatives within the free-look/cancellation period so as to enable them to take prompt corrective action should any recommendation be found to be unsuitable for the client.

## **6 Disclosure of information to clients**

6.1 Several respondents sought clarification on whether the information that is required to be disclosed to clients under Section 25 of the FAA and Notice FAA-N03 could be incorporated into a document that is currently being given to clients, such as "Your Guide to Life Insurance". Some respondents also enquired when disclosures should be made to clients.

#### MAS' Response

"Your Guide To Life Insurance" is a general document that is given to clients only during sales of life insurance. FAs who provide financial advisory services in respect of life policies only are free to decide if they wish to include general information about themselves and their representatives in this document.

As to timing of disclosure to clients, it is good practice for general information such as authorised activities of the FA and its representatives, the FA's mode of remuneration (fee-based, commission-based or both), and avenues for consumers to seek redress, to be provided to clients at the outset of the sales process. Information that is product-specific, such as the risks and benefits of the product being recommended, should be disclosed at an appropriate time during the sales process.

## **7 Monitoring of sales practices of representatives**

7.1 Some respondents felt that it may be too stringent to impose a requirement for FAs to meet the 40% target for full and partial fact-find. There was also feedback that FAs should be given sufficient time to meet this target.

#### MAS' Response

We have observed that FAs with the proper systems and processes in place are consistently able to achieve at least 40% of their sales with full or partial fact-find. The target of 40% is a benchmark that all FAs should strive towards. We expect all FAs to improve the percentage of sales completed with full and partial fact-find over time.

## 8 Maintaining records on types of advice

8.1 One respondent felt that the Paper should not make reference to the four types of advice as it is primarily an insurance industry practice, and may not be suited for other designated investment products.

### MAS' Response

The four types of advice stated in the Paper follow the sales process adopted by the Life Insurance Association of Singapore ["LIA"]. Although the LIA's sales process was conceived with insurance products in mind, its objective of ensuring that clients receive proper advice based on their needs is in line with the requirements in the FAA. Furthermore, we note that many FAs have adopted this process for sales of all designated investment products, as it is practical to use a single sales process for analysing clients' needs.

The four types of advice mentioned in the Paper is a suggested way for FAs to maintain proper records in order to monitor the extent of needs-based advisory activities conducted by their representatives. FAs can maintain their records in other ways so long as they are able to properly monitor the extent of needs-based sales conducted by their representatives.

8.2 Two respondents were unclear about the difference between the following two types of advice - "Partial fact-find" and "Product advice".

### MAS' Response

In the case of a "Partial fact-find", the FA would gather sufficient information from a client relevant to the client's indicated priorities, preferences or expectations (eg. protection for dependents), and conduct needs analysis to identify the product that meets the client's needs. In the case of "Product advice", the client does not wish to undergo fact-find and needs analysis but only wants to receive advice from the FA on a particular type of product he is interested in. An example of product advice is when a client wishes to buy a unit trust that gives him exposure to Chinese equities and the FA selects one or more funds based on the client's specific instructions, and explains the product features of the selected funds to the client.

We will clarify the definitions of the two categories of advice in the Paper.

## 9 Measures to ensure quality of financial advisory services

9.1 One respondent was concerned that implementing mystery shopping and client callback exercises would add to the operational costs of FAs. The respondent was of the view that such measures should only be put in place as part of an investigation process, for situations where complaints on misconduct by representatives have been received.

### MAS' Response

The conduct of mystery shopping and client callback exercises could provide FAs with useful feedback on the quality of advice and services provided by their representatives. FAs may adapt the measures to their own specific needs, or implement other control measures to gather feedback from clients so as to ensure that their representatives provide high quality advice.

## 10 Training and competency

10.1 Some respondents felt that the recommendation of 45 training hours per year was too high as representatives were already subject to the minimum entry and examination requirements in the Notice on Minimum Entry and Examination Requirements for Representatives of Licensed Financial Advisers and Exempt Financial Advisers. There were also queries on how the training hours should be allocated between the various types of investment products, and between skills and knowledge training.

### MAS' Response

The Capital Markets and Financial Advisory Services ["CMFAS"] examination is only a minimum entry requirement. Given rapid changes in the financial market and the proliferation of new and more complex investment products, it is important for representatives to keep abreast of the latest developments and to remain competent in their provision of financial advisory services. Continuous training is essential for representatives to upgrade their knowledge and skills and improve their competency. MAS has aligned the minimum number of training hours with the life insurance industry norm of 30 hours per year. Notwithstanding the minimum number of hours recommended, FAs should ensure that training provided to representatives is sufficient for the nature of financial advisory services they provide.

We are of the view that FAs are in a better position to decide how the training hours should be allocated among the various types of investment products and between skills and knowledge training, depending on their requirements and those of their representatives.

## **11 Competency assessment**

11.1 One respondent commented that an annual competency assessment of representatives should not be necessary where the requirement for continuing education and training must be satisfied.

### MAS' Response

The competency assessment is a formalised process to assess the competency level of representatives. This would enable supervisors to identify areas of weakness or concerns that require correction or further training. It is therefore important for representatives to be assessed on their competency at least on an annual basis.

11.2 Another respondent sought clarification on the manner and content of the competency assessment to be undertaken in order that there are consistent standards across the industry.

### MAS' Response

Such details are best determined by individual FAs based on their own circumstances and needs. Competency assessments could take various forms including conducting tests and role-plays, and observing representatives in the conduct of the advisory and sales process.

11.3 One respondent suggested that MAS specify the number of joint field visits supervisors have to conduct with newly recruited representatives under their charge.

### MAS' Response

The objective of having supervisors observe new representatives in the advisory and sales process is to ensure that the new representatives are competent before they are allowed to conduct advisory and sales activities independently. The number of accompanied sales that supervisors should conduct with the new representatives should be determined by the supervisors based on their assessment of the competency level of the representatives.

## **12 Span of control for supervision of representatives**

12.1 Several respondents provided feedback that the guidelines on span of control of 15 representatives per supervisor and 10 supervisors per manager was restrictive, and suggested that different ratios could be set for different groups of supervisors and managers based on their level of experience.

### MAS' Response

The ratios stated in the Paper are meant to be guidelines for FAs. FAs may allow managers/supervisors to have higher span of control if they are satisfied that the managers/supervisors have the ability to manage more supervisors/representatives, and they have in place proper systems for monitoring the performance of the managers/supervisors. In cases where the FAs are concerned as to the ability of the supervisors/managers, they should lower the span of control of these supervisors/managers to less than the recommended ratios.

## **13 Recruitment process**

13.1 Several respondents sought guidance on how they should conduct their recruitment process.

### MAS' Response

It would not be appropriate for MAS to prescribe how FAs should conduct recruitment of their representatives. FAs should ensure that the representatives they recruit meet the fit and proper criteria set out in the Guidelines on Fit and Proper Criteria. A good practice FAs may consider implementing is to conduct reference checks with the former employers of potential representatives to ensure that the candidates satisfy the fit and proper criteria. FAs may also check against MAS' register of persons against whom a prohibition order has been made under Section 59 of the FAA.

13.2 Some respondents also requested guidance on how co-operation between institutions on the conduct of reference checks can be achieved.

#### MAS' Response

We note that members of the LIA have entered into an undertaking requiring them to cooperate with one another in the conduct of reference checks. We strongly urge the rest of the industry to establish similar working arrangements amongst themselves.

13.3 One respondent commented that the conduct of reference checks should be confined to financial institutions.

#### MAS' Response

The purpose of conducting reference checks is for FAs to satisfy themselves that the potential representatives meet the fit and proper criteria. FAs have to determine for themselves whether limiting the conduct of reference checks to financial institutions would achieve this objective.

## **14 Complaints handling process**

14.1 One respondent sought clarification on who would be considered an "independent party" in the complaint handling process.

#### MAS' Response

An independent party is one who is independent of the advisory and sales function.

## **15 Compliance**

15.1 Several respondents commented that line departments should still take responsibility for day to day compliance matters, although overall responsibility for ensuring compliance should reside with a centralised compliance function. There were also comments that not all compliance departments report to the Board of Directors or Audit Committee.

#### MAS' Response

MAS agrees that individual line departments should have responsibilities for ensuring compliance. MAS is concerned when line departments are given sole responsibility for compliance, without any oversight from a centralised compliance function. We have amended the Paper to clarify this position.

MAS also agrees with the feedback on reporting lines for the compliance function, and has amended the Paper accordingly.

MONETARY AUTHORITY OF SINGAPORE

17 November 2004

## **ANNEX**

### **LIST OF RESPONDENTS TO PUBLIC CONSULTATION**

Aon Re Asia Pte Ltd  
DBS Bank Ltd  
General Agents and Managers Association Singapore Chapter  
Goldman Sachs (Singapore) Pte  
Insurance and Financial Practitioners Association of Singapore  
J P Morgan Chase Bank  
Life Insurance Association of Singapore  
Malayan Banking Bhd  
Mercer Human Resource Consulting (S) Pte Ltd  
Oversea-Chinese Banking Corporation Ltd  
S L Tan & Co: Advocates and Solicitors  
Schroder Investment Management (Singapore) Ltd  
Singapore Society of Financial Analysts  
Standard Chartered Bank

