

Client Alert

March 2020

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MAS Proposes New Requirements for Allocating Charges and Expenses to Participating Funds

Insurers, their directors, senior management and appointed actuaries should note the [significant changes proposed by the Monetary Authority of Singapore \(MAS\)](#) to the MAS Notice 320 on the management of participating life insurance business (**Notice 320**)¹.

The following proposed changes are intended to safeguard policy owners' interests, and to avoid reductions in distributable bonuses and other ways which policy owners may be disadvantaged:

- a new "fair and reasonable" requirement for charges allocated to a Participating Fund (**Par Fund**), covering:
 - the new non-exhaustive list of expenses which must not be charged to a Par Fund;
 - agency schemes and arrangements with Financial Advisers (**FAs**);
 - frequency and scope of expense studies;
 - loading of expenses for pricing of participating products; and
- enhanced responsibilities on the insurer, its board of directors, senior management and appointed actuary.

We summarise below the proposed changes and examples of disallowed allocations provided by MAS, and questions posed by MAS for public comment.

Charge allocation to be "fair and reasonable"

MAS recognises the significant proportion of the life insurance business represented by participating insurance policies and MAS has observed instances of inappropriate charging of expenses. Accordingly, MAS proposes to require all insurers to ensure that any charge or expense allocated to the Par Fund is fair and reasonable.

The amended Notice 320 will define a "fair and reasonable" allocation of charges or expenses to a Par Fund as an allocation which is:

- not to the detriment of the participating policy owners' interests; and
- necessary for the ongoing management of the Par Fund.

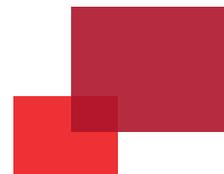
¹ please see Consultation Paper on Proposed Requirements on Insurers' Charging of Expenses to the Participating Fund published at:
<https://www.mas.gov.sg/publications/consultations/2020/proposed-requirements-on-insurers-charging-of-expenses-to-the-participating-fund>



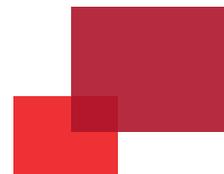
MAS seeks comments on the need for insurers to meet policy owners' expectations in a "fair and reasonable" manner, particularly when it comes to the allocation of charges and expenses to the Par Fund.

Summarised below are the types of prohibited allocations set out in the amended Notice 320, and examples of costs, charges, expenses and payments provided by MAS in its consultation paper which will be deemed as not fair and reasonable to be borne by Par Fund policy owners:

Types of allocations and exclusions	Examples of disallowed costs, charges, expenses and payments
1. Charges or expenses specified in the new Appendix D to Notice 320	<p>Costs incurred by the insurer due to preventable lapses or regulatory breaches, such as:</p> <ul style="list-style-type: none">• MAS or other regulatory fines or penalties• Charges or expenses, incurred, paid or payable in relation to:<ul style="list-style-type: none">○ activities in breach of the MAS or any other Singapore authorities' requirements; or○ items which MAS has conveyed in writing to the insurer or the industry's association to be non-chargeable to Par Fund. <p>Overriding benefits payable by an insurer to individuals outside of the three "manager, supervisor, representative" tiered structure as set out in Notice 306 on Market Conduct Standards for Life Insurers Providing Financial Advisory Services.</p> <p>Marketing or other costs are not related to the ongoing management of the Par Fund:</p> <ul style="list-style-type: none">• Allowance given to a representative of a licensed financial adviser or exempt financial adviser, other than the insurer, to subsidise the representative's cost of doing business, including transport costs, phone bills or meals.• Prizes or incentives offered to a representative of any licensed financial adviser or exempt financial adviser, which have an element of probability and do not



Types of allocations and exclusions	Examples of disallowed costs, charges, expenses and payments
	<p>have a direct relation to the sales of participating products or the ongoing management of the Par Fund.</p> <ul style="list-style-type: none"> • Operating expenses incurred by any related party of the insurer which distributes the insurer's products (see para 2. below for examples). • Costs incurred for corporate restructuring including mergers and acquisitions, demerger, changes involving shareholding structure and management buyout, but excluding internal reorganisation of the insurer's processes or workforce. • Costs incurred for marketing non-participating or investment-linked products (see para 3. below for examples). • Tax on shareholders' entitlement in relation to participating bonus distribution
<p><i>MAS seeks comments on the proposed list of non-chargeable expenses for Par Fund.</i></p>	
<p>2. Payments to a related party (defined as any of the insurer's associates or subsidiaries, its holding company or any subsidiary of its holding company)</p>	<p>While an insurer may need to pay its parent company or regional office for services and support rendered to the insurer, it will not be allowed to allocate charges or expenses not commensurate with the goods or services provided by the related party.</p>
<p><i>MAS seeks comments on this proposed requirement.</i></p>	
<p>3. Marketing-related charges or expenses (excluding Par Fund branding campaigns)</p>	<p>Marketing-related charges and expenses which:</p> <ul style="list-style-type: none"> • are not directly related to the sales of the insurer's Par products; or • do not contribute to the improvement in the future sales of the insurer's Par products or growth of the insurer's Par Fund, <p>such as:</p>



Types of allocations and exclusions	Examples of disallowed costs, charges, expenses and payments
	<ul style="list-style-type: none"> • fixed monthly marketing allowance paid or payable to the FA firm's representatives, which is not directly related to the sales of the insurer's Par products; • reimbursement of marketing allowance to an insurer's staff for expenses incurred in entertaining an FA firm's representatives; and • reimbursement of the costs incurred by the exempt FA firm, such as a bank, on a marketing event to promote the insurer's investment-linked products, since it is not directly related to the sales of the insurer's Par products. <p>Before being allowed to allocate any marketing-related charges and expenses to the Par Fund, the insurer must clearly document:</p> <ul style="list-style-type: none"> • the basis and justification for such allocation; • how the marketing-related charges or expenses have been shared between the insurer and the FA appointed to distribute its products, and • the rationale and methodology applied in apportioning the marketing-related charges or expenses between the relevant Par funds
<p><i>MAS seeks comments on this proposed requirement.</i></p>	
<p>4. Operating expenses incurred by any other distribution channels (excluding a tied agency force which is not a separate legal entity, and mainly promotes the insurer's products)</p>	<p>Par Fund to bear the operating expenses of the FA firm when the FA firm (either owned or appointed by the insurer) is:</p> <ul style="list-style-type: none"> • a separate legal entity; • is responsible for its own set of operating expenses; or • is already being remunerated for sales of the insurer's Par products.



Types of allocations and exclusions	Examples of disallowed costs, charges, expenses and payments
<p><i>MAS seeks comments on this proposed requirement.</i></p>	
<p>5. Certain payments to insurance agents and FAs (excluding payments to new representatives joining the insurer's tied agency force who had not been representatives of another insurer or FA firm for the past 2 years or have less than 2 years of experience, in aggregate, as a representative in the insurance industry)</p>	<p>Remuneration or incentives paid selectively or paid above the norm to representatives of the same distribution channel that are of the same tier, rank and scheme.</p> <p>Payment of the following:</p> <ul style="list-style-type: none"> • expenses incurred from organising contests which are only open to certain agency units when others can also fulfil the qualifying criteria set; • expenses incurred as a result of a higher override scale offered to a particular Tier-3 manager compared to peers of the same tier, rank and scheme; • retention bonus to certain individuals or units, but not others of the same tier, rank and scheme, to ensure they stay longer with the insurer; and • recruitment packages to encourage representatives of another FA firm to join or sell for the insurer.
<p><i>MAS seeks comments on this proposed requirement. MAS also seeks comment on:</i></p> <ul style="list-style-type: none"> • <i>the circumstances where an insurer would expect to operate more than one agency scheme; and</i> • <i>(for insurers presently having more than one agency scheme, and the insurer is of the view that it is operationally impractical to consolidate them)</i> <ul style="list-style-type: none"> ○ <i>what are the key factors which differentiate the schemes; and</i> ○ <i>what challenges, if any, inhibit the reduction in number of schemes.</i> 	
<p>6. Upfront charges and expenses for setting up or acquiring distribution channels, or tie-up with any FA, including amortising such costs (excluding</p>	<p>Examples include:</p> <ul style="list-style-type: none"> • facilitation fees paid to a bank when an insurer enters into an exclusive tie-up with the bank; and



Types of allocations and exclusions	Examples of disallowed costs, charges, expenses and payments
<p>existing facilitation fee agreements: which may be grandfathered on approval by MAS after the amendments to Notice 320 take effect where the insurer is able to demonstrate to MAS that it has adequate controls to ensure that Par policy owners are not disadvantaged)</p>	<ul style="list-style-type: none"> arrangements where an insurer decides to bear the upfront facilitation fees from its shareholders' fund initially and recover the expenses from the Par Fund subsequently when actual sales take place. <p>This prohibition is aligned with MAS' position in disallowing the charging of sign-on incentives, on the basis that upfront costs do not guarantee future sales will happen as projected. The insurer can choose to remunerate as and when sales occur.</p>
<p><i>MAS seeks comments on this proposed requirement and on the proposed approach for existing agreements with facilitation fees to be grandfathered.</i></p>	

Responsibilities imposed on the insurer, its directors, senior management and appointed actuary

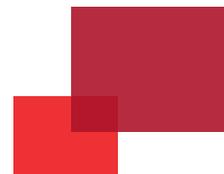
The current Notice 320 requires all Par Fund insurers to put in place an internal governance policy (**IGP**) to clearly document the processes and controls in the management of its Par business, to be approved by the insurer's Board of Directors and reviewed annually by the Board.

However, MAS has observed instances where IGPs are broadly worded and may not provide sufficient information on how the Board assesses that the insurer's expense allocation methodologies are fair and reasonable to the Par policy owners.

The amended Notice 320 sets out added responsibilities and duties on the insurer, its directors, senior management and appointed actuary, which we summarise below.

MAS also seeks comments on these new responsibilities.

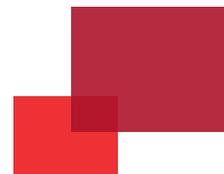
Responsible party	New Notice 320 responsibility
<p>Insurer</p>	<p>Ensure that any charge or expense allocated to the Par Fund is fair and reasonable.</p>
	<p>Establish robust processes to ensure that expenses charged to the Par Fund:</p> <ul style="list-style-type: none"> comprehensively considers policy owners' interests; and



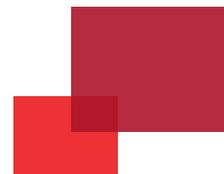
Responsible party	New Notice 320 responsibility
	<ul style="list-style-type: none">• are necessary for the ongoing management of the Par Fund. <p>Where charges and expenses are materially different across different groups or classes of products within the Par Fund, or across the different sub-funds; either:</p> <ul style="list-style-type: none">• consider tracking the asset shares separately; or• clearly document both:<ul style="list-style-type: none">○ the reasons for the decision to not separately track the asset shares even though their charges and expenses are materially different from one another; and○ the controls to mitigate cross-subsidisation across different groups or classes of products or across different sub-funds. <p>Ensure that "expense loading" for Par product pricing is consistent with its latest expense study assumptions account for all relevant expenses to avoid the risk of under-pricing its new Par product by undertaking the following:</p> <ul style="list-style-type: none">• ensuring any deviation between the expense study assumptions and expense loading is clearly documented and justified;• properly monitoring consistency between the expense loading and actual charges and expenses allocated to the relevant Par product; and• promptly repricing or withdrawing the affected Par products when actual charges and expenses materially deviate from the expense loading or exceeds expectation due to insufficient business volume. <p>(for newly set up a Par Fund, an exception is made for deviations between the insurer's expense loading and expense study assumptions during the first 3 years following the launch of its first Par product.)</p> <p>Ensure that the Par Fund does not bear the differences between the expense loading and actual charges and expenses incurred, due to any deliberate under-provision of expense loading in the pricing of its Par</p>



Responsible party	New Notice 320 responsibility
	<p>product, by avoiding such deliberate acts of expense loading under-provisioning as:</p> <ul style="list-style-type: none">• not fully accounting for all variable and fixed costs that the Par product would reasonably be expected to bear, on the pretext that these costs can be absorbed by the in-force block of Par business;• not fully providing for potential higher remuneration scales payable to certain FA firms; and• assuming (with no compelling reasons why) a significant portion of sales to come from the distribution channel with the lowest remuneration, when past sales figures do not bear this out. <p>(for newly set up a Par Fund, an exception is made for deviations between the insurer's expense loading and expense study assumptions during the first 3 years following the launch of its first Par product.)</p>
Board of directors	<p>When conducting any review of the IGP, the Board must:</p> <ul style="list-style-type: none">• Pay attention to any past material deviations from the insurer's IGP in managing the Par Fund;• Assesses the proposed charging and expense allocation to the Par Fund for each year, at least annually, to ensure that the allocation is fair and reasonable to the Par policy owners;• Be informed of the following when the Board assesses whether the proposed allocation of charge and expenses to the Par Fund is fair and reasonable:<ul style="list-style-type: none">○ any proposed change to the categories of charges or expenses to be allocated to its Par Fund, including a reclassification of charges or expenses; the inclusion of new categories of charges or expenses; and the removal of existing categories of charges or expenses;○ any one-off charges or expenses proposed to be allocated to the Par Fund;○ any charges or expenses to be allocated to the Par Fund that has been determined by the



Responsible party	New Notice 320 responsibility
	<p>insurer's appointed actuary to be exceptional; and</p> <ul style="list-style-type: none"> ○ any proposed material change to the existing charging and expense allocation methodology, including the reclassification of charges or expenses, and changes to the drivers in allocating common expenses that affect the Par Fund.
Senior management	<p>In addition to establishing adequate controls and processes to ensure effective implementation of the Board-approved IGP, senior management will be responsible for:</p> <ul style="list-style-type: none"> • implementing safeguards to satisfy the proposed Notice 320 requirements; • ensuring appropriate allocation of charges and expenses to the Par Fund; and • setting and implementing clear policies and guidelines on the allocation of charges and expenses to the Par Fund, which at the minimum, must: <ul style="list-style-type: none"> ○ set out the basis for the allocation of charges and expenses to the Par Fund, consistent with the basis as approved by the appointed actuary; ○ set out the type of charges and expenses which can be allocated to the Par Fund, consistent with the appointed actuary's advice; and ○ provide that whenever there is any ambiguity on whether a charge or expenses can be allocated to the Par Fund, the appointed actuary's advice must be sought.
Appointed actuary	<p>Notice 320 will explicitly recognise the appointed actuary's role in the appropriate charging of expenses to the Par Fund with the following responsibilities:</p> <ul style="list-style-type: none"> • recommending guidelines to the Board for allocating charges and expenses to the Par Fund in a way that is fair and reasonable and reviewing these guidelines at least annually or whenever there are material changes to the insurer's circumstances;



Responsible party	New Notice 320 responsibility
	<ul style="list-style-type: none">• highlighting to the Board and senior management:<ul style="list-style-type: none">○ whenever material charges or expenses have been inappropriately charged to the Par Fund or to be;○ where any charges or expenses have been allocated to the Par Fund and such charges or expenses are material, viewed as potentially detrimental to Par policy owners' short-term interests even though it is deemed as ultimately favourable for the Par policy owners' long-term interests, and provide an opinion in writing whether such an allocation is justifiable;• approving the detailed basis for allocating charges and expenses to the Par Fund and any changes to the basis, aligned with the guidelines;• advising on the type of charges and expenses which can be allocated to the Par Fund; and• documenting for the Board's and senior management's attention, as appropriate, any material reservations regarding the allocation of charges and expenses to the Par Fund; and• where such reservations cannot be satisfactorily addressed, alerting MAS of the concern within 30 days from the time that the matter has been brought to the appointed actuary's attention.

Implementation Timeline

The consultation closed on the 9 March 2020 and MAS, proposing the amended Notice 320 to take effect from 1 April 2020, has sought comments on the proposed effective date for implementation of the changes.

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