

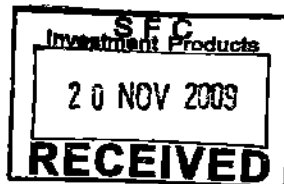
CIB 香港保險顧問聯會
**THE HONG KONG CONFEDERATION
OF INSURANCE BROKERS**

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Our Ref: IS0911082/el

19 November 2009

Securities and Futures Commission
8/F Chater House,
8 Connaught Road Central,
Hong Kong



Dear Sirs,

Re: Consultation on proposals to enhance protection for the investing public

We are pleased to submit herewith our response to the above-mentioned consultation for your consideration.

There is no objection to our views being published or publicized for public discussion and debate, and we look forward to receiving any feedback from the Commission to our suggestions.

Thank you for your attention.

Yours faithfully,
For and on behalf of
The Hong Kong Confederation of Insurance Brokers

A handwritten signature in black ink, consisting of several loops and flourishes, positioned above the typed name 'CIB Secretariat'.

CIB Secretariat

Encl.

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**Response to the
Consultation Paper on Proposals to Enhance Protection for the Investing Public**

19 November 2009

Preamble

The Hong Kong Confederation of Insurance Brokers ("CIB") is a professional association and self-regulatory body of insurance brokers authorized by the Insurance Authority. Incorporated in 1993, CIB currently represents 251 corporate member firms of insurance brokers.

CIB welcome this Consultation Paper issued by the Securities & Futures Commission ("SFC") and input to it with the following comments and suggestions.

On Investor Education

- (1) CIB welcome the initiative of enabling individual investors to address their investment needs and look forward to the upcoming proposal to establish an Investor Education Council.
- (2) Meanwhile CIB would like to highlight its concern in the question of whether adequate resources have been put into continual education of the practising professionals.
- (3) The education of investor in their understanding of "their signatures count" seems to be the first lesson for all.

On Resolution

- (4) CIB appreciate the effort of the Government in proposing the establishment of a Financial Services Ombudsman and will participate in the consultation of the proposal to be released later this year.

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- (5) Nevertheless, CIB would like to point out at this juncture a related issue, i.e. how financial service providers could make themselves financially ready to meet any resolution – should financial institutions/intermediaries taking out professional indemnity insurance be mandatory?

On Products

The Handbook:-

- (6) The proposed new clause 1.2 of the Code on Investment-Linked Assurances Schemes, which says:

“Authorized Insurers are under the prudential regulation of the Insurance Authority. The intermediaries selling investment-linked assurance schemes, including insurance agents and brokers, are subject to a self-regulatory system through self-regulatory organizations of the insurance industry. These organizations are also subject to the oversight of the Insurance Authority. Therefore, issues such as how the Authorized Insurers operate, their financial conditions or their business conduct are not within the Commission’s regulatory ambit.”

It refers to insurance intermediaries at the outset but omits them in the latter part, resulting in its incompleteness. CIB suggest SFC stating its stance on whether the business conduct of insurance intermediaries are or are not within its regulatory ambit, and if so, when and how. The SFC Circular dated 13 August 2009 has cast some light onto this, though also lacking certainty.

- (7) Clause 5.3 of the Code on Investment-Linked Assurances Schemes refers to the illustration document for Investment-Linked Assurances Scheme. The proposed amendment to Clause 5.3, particularly the phrases of concern is highlighted below:

“An illustration document must be prepared by the Authorized Insurer in conjunction with each proposed investment by each prospective scheme

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~~participant. Alternatively, the Commission may allow the provision of a standard illustration for each scheme, provided that the surrender values illustrated are for a contract with a term based on a maximum commission scale and a minimum premium requirement.~~

CIB understand that the amendment would mean that standard illustration will no longer be allowed, and each prospective scheme participant will receive a tailor-made illustration document reflecting the exact details of what he/she intends to take, including the contract term, premium payment term, premium amount. CIB welcome this enhanced disclosure requirement, but wish to point out that it affects the day-to-day operations of both Authorized Insurers and insurance intermediaries, that sufficient transition period should be allowed before effecting the enhancement. CIB consider the 9 to 12 months as proposed for the "Long Stop Date" as from the "Effective Date" to be appropriate in this regard.

- (8) Clause 5.4 of the Code on Investment-Linked Assurances Schemes set out the minimum requirements for the information to be included in the illustration document. The emphasis remains with the Surrender values. The experience of CIB in dealing with complaints in relation to this type of product reveals that the investors' uninformed application of premium holiday after the minimum premium payment term, commonly known as Initial Contribution Period, is one of the major sources of grievance. "Premium holiday" is in fact included in the Product Key Facts Statement Template for Investment-Linked Assurance Schemes as one of the key risks. CIB suggest that the financial implications of applying premium holiday should be included in the illustration document, that can be achieved by illustrating in a new column for either the accumulative fees and charges of the product or the reduction in yield. The warning should also include the decision to apply premium holiday for an extended period of time, that it is better to amend it as follows:-

"Warning: You should only invest in this product if you intend to pay the premium for the whole of your chosen premium term. Should you terminate this

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product early or should you cease paying the premium early, you may suffer a significant loss."

CIB further suggest that the Declaration section should also be amended to reflect the fact that the client having been given, having read and understood the Product Key Facts Statement.

- (9) This Clause 5.4 further mentions that further guidance as to the assumed rates of return to be used in the illustration document will be available on the Commission's website. There is no discussion on the rates of return to be assumed. CIB believe there are merits to bring up this discussion at this juncture, and would urge that, in light of the lessons learnt from the financial tsunami, in addition to the current two percentages at +5% and +9%, which show only the upside of investment, the downside risk, i.e. the impact of investment loss, should be illustrated. CIB finds it sensible to include -5% and -9% to offer a balanced view to prospective scheme participants about the nature of investment. The illustration of zero return will also help. Or if it is considered too much, both a negative and a positive rates of return at the same gravity, say 9%, plus a zero return will be good enough.
- (10) Clause 5.16 of the revised Code on Investment-Linked Assurances Schemes uses the term "insurance company" while in other text, this term is amended to "Authorized Insurer".
- (11) Clauses 7.8 to 7.10 of the Code on Investment-Linked Assurance Schemes refer to Advertising materials. It is a grave concern of CIB that there is no way an insurance intermediary can tell whether an advertisement or other invitations to invest in a scheme which is provided by Authorized Insurer has been authorized or exempted to be authorized by the SFC. CIB suggest that either SFC maintains a publicly accessible web-based archive of such authorized materials with an authorization code and also requiring the issuer of such materials be quoting such code, or SFC stipulates that a statement to the effect that the advertisement or invitation has been authorized or exempted to be authorized by SFC is to be included in any such advertisement or invitation.

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- (12) In the "Information to be disclosed in the principal brochure" which is the Appendix A to the Code on Investment-Linked Assurance Schemes, "warning statements" are proposed to be included. One of them is about the nature of Investment-linked assurance schemes being insurance policies. Meanwhile, the requirement on the name and type of scheme is of a generic nature, asking them to "not be misleading to potential scheme participants and should be an accurate reflection of the type of scheme and its objectives." CIB welcome the insertion of warning statement to highlight the nature of this type of product, but suggest that it to be more effective of requiring such key words "long-term" and "insurance" to be incorporated into the name of the scheme, or at least forming part of a sub-title of the name, which is the most accurate reflection of the type and objectives of the scheme.
- (13) Again in this "Information to be disclosed in the principal brochure", CIB ask that on Fees and charges, the frequency and the duration of each fee and charge should be stated not only in the text but also in the summary of fees and charges.

The Product Key Facts Statement:-

- (14) CIB welcome the initiative and suggest the following items to be included
- Specify it to be a life insurance policy (emphasis added);
 - Specify the duration for which the fees and charges will apply.
 - Liquidity risk – fund withdrawal from the policy may be affected by the trading terms of the underlying funds;
 - Reminder: "Your signature counts."

On Intermediaries Conduct

Suitability Test:-

- (15) Points 6 and 19 of Part III of the Consultation Paper ask that:

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"the intermediary should, when making a recommendation or solicitation, ensure the suitability of the recommendation or solicitation for that client is reasonable in all the circumstances." (emphasis added).

CIB hold the view that in reality no one can foresee the future, therefore no one can ever ensure the suitability for client is reasonable in ALL circumstances which will effectively include those in future. Intermediary should only be required to ensure the suitability to be reasonable in the circumstances when making that recommendation.

- (16) Point 8 of Part III talks about matching the risk return profile of each investment product with the personal circumstances of each client to whom the product is recommended. CIB hold the view that a holistic approach should be applied in assessing appropriateness of the risk matching.

To consider an example: where the client residing in Hong Kong is maintaining a very conservative investment portfolio by putting all monies in HK\$ time deposit at blue chip bank in Hong Kong, while his risk appetite is of a medium type that he can afford an investment loss at 5%. A recommendation of an investment-linked insurance policy with value linked to a number of bond funds, carrying an estimated risk of 8%, accounting 2% of his total investment portfolio, will increase marginally the risk exposure of his total portfolio but such exposure definitely remains low relatively to his risk appetite. Having said so, any matching would only be based upon the information as disclosed by the client to the intermediary, as it is a reality that clients might not be willing to fully disclose their financial portfolio to the intermediary.

Average investor, Professional investor and Unlisted derivative products:-

- (17) Point 20 of Part III refers to "average investor", but no definition is given. If a definition is to be added, it may be defined as investor who has the experience of losing monies in any financial investment authorized by SFC.
- (18) Points 21 to 25 refer to unlisted derivative products and there are proposals on intermediaries when recommending this type of products to clients with or without

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knowledge of derivatives. CIB understand that whether a product being listed or unlisted may have a bearing on the liquidity risk (while trading of listed product may also be suspended in some occasions) that the client may have to take into account, but in terms of intermediary conduct and product suitability, what is the relevance of the product being listed or unlisted to client's knowledge in derivative?

- (19) Point 26 aims to define what constitute a client with knowledge of derivatives, and Points 36 to 40 to define what constitute a professional investor in terms of knowledge and experience. CIB hold the view that the proposal will eventually evolve into a qualification framework for investors with training courses to be accredited. For prior trading/investment experience, CIB consider that one has to pay to learn a lesson, hence only those resulting in financial loss to the client should count.

Pre-sale disclosure of monetary and non-monetary benefits:-

- (20) CIB hold the view that specific disclosure of dollar amount or percentage is impractical, because at the point of pre-sale, intermediary will have no idea of the exact dollar amount of commission which in most cases a variable of the investment amount, duration and other factors to be decided by the clients. The commission earnings would usually include a trailer that even an exact percentage of the investment amount cannot be known.
- (21) If disclosure is a must, CIB suggest the disclosure to be in ceiling percentage, or maximum percentage, since the lower end of a range is meaningless to client.
- (22) Points 67 and 68 refer to a business model with back-to-back transaction. It is suggested that any trading profit is similar to the commission that may otherwise generated, hence it should be disclosed. CIB hold the view that whether intermediary should be allowed to conduct back-to-back transaction, that is re-selling investment product, is debatable, since this involves conflict of interest where the intermediary is in fact the seller in this scenario. The nature of trading profit is fundamentally different from that of commission earnings, hence it makes little, if any, sense of compelling this type of business model to



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disclose the profit margin, lest this will set a very bad precedent that in future all product manufacturers will be required to disclose their profit margin when selling a product.

- (23) For investment-linked assurance scheme, such disclosure can be incorporated into the illustration document, instead of the proposed new "Sales Disclosure Document", which is both anti-environmental and redundant.

Use of gifts:-

- (24) Points 75 to 79 explores the pros and cons of restricting intermediaries from offering investors gifts. CIB hold the view that the Singapore model should be adopted where there is no restriction to the gift offering, but the financial institutions should have proper systems and controls to ensure that the basis for any recommendation is not compromised as a result of offering gifts. This view has taken into account the practicality issue with the question of what would constitute "gifts with low resale values", the cost offsetting impact of transaction cost to client, and the concurrent proposal of benefit disclosure by intermediaries.

Sales disclosure document:-

- (25) For investment-linked assurance scheme, the proposed items to be included in this new document, i.e. capacity to act, affiliation to product issuer, benefit disclosure and generic terms of receiving discount of fees and charges, can be incorporated into either the Client Agreement (the former two) and the illustration document (the latter two). CIB consider it undesirable to introduce another piece of paper in this regard.

Audio recording:-

- (26) It is simply impractical to most business models where the sales work is performed outside the office setting.

- THE END -

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