Transcripts of Speech by Mr Lee Chuan Teck, Chairman, Financial Advisory Industry Review Panel, Assistant Managing Director, Monetary Authority of Singapore, 16 January 2013 on the occasion of presentation of "Financial Advisory Industry Review (FAIR) Panel Report".

Introduction

1 Good afternoon. It gives me great pleasure to present the Financial Advisory Industry Review (FAIR) Panel report (Annex 1) today. This report is the result of 8 months of intense deliberations by the Panel. From the beginning, we recognized that the Panel does not have a monopoly on ideas to improve the industry. Thus, we had consulted widely with industry veterans, foreign regulators, consumer bodies and industry groups. We solicited and received more than 1300 comments and suggestions from the public. Many of the recommendations presented here germinated from these suggestions.

2 Before going into the recommendations, let me re-cap why we embarked on FAIR in the first place. First, we needed to raise the standard of practice in the Financial Advisory (FA) industry. This was demonstrated starkly by the mystery shopping exercise that MAS conducted at the end of 2011. In the sample of 500, 30% of the products recommended were clearly unsuitable. Second, various studies suggested that Singaporeans are not doing adequate financial planning. For example, Life Insurance Association, Singapore (LIA)'s report last year showed that Singaporeans are under-insured by about 3.7 times their annual income. A separate survey in 2011 found that 4 out of 10 people do not make any financial plan for their retirement or for contingencies.

3 Clearly, an FA industry that can deliver better quality advice in a more efficient manner is critical to enhancing the financial preparedness of Singaporeans. Our recommendations will be assessed on 3 parameters: the quality of advice, the efficiency of the industry and ultimately, the state of financial preparedness of Singaporeans. MAS will develop Key Performance Indicators (KPIs) to measure each of these over time.

4 The Panel has made 28 recommendations, grouped under 5 thrusts. A summary of these recommendations is provided (Annex 2). Rather than describing each recommendation in detail, I intend to just highlight the essence of the recommendations under each thrust, and explain our thinking and deliberations behind them.

Thrust 1: Raising the Competence of Financial Advisory Representatives

5 Under this first thrust, we recommend raising the minimum entry requirement for new representatives from the current four GCE 'O' level passes to a full GCE 'A' level certificate, an International Baccalaureate (IB) or a diploma. This higher requirement will only apply to new entrants. Existing representatives will not be affected.

6 We considered two counter arguments to raising entry requirements. The first is that an academic qualification in itself is not a good measure of a representative's competence. An

experienced, financially savvy representative with 'O' levels may well be a better adviser than a green-horn with a degree. The second counter argument is that we already have the Capital Markets & Financial Advisory Services (CMFAS) exams that representatives must pass before they can practise. CMFAS exams are arguably a more relevant assessment of a representative's knowledge at the point of entry.

7 Both arguments have merits. Nonetheless, the Panel also recognized that it is important that representatives not only have the necessary knowledge at the point of entry, but also over the life-time of their career. Financial products and client needs are becoming more complex. A higher level of education will better enable representatives to keep up with these developments.

8 Besides academic qualifications, the Panel felt that it is even more important to pay attention to Continuing Professional Development (CPD). Financial representatives will be required to undergo at least 30 hours of formal training annually. Of these, at least 8 hours have to be on rules and regulations and 4 hours on ethics.

Thrust 2: Raising the Quality of Financial Advisory Firms

9 The recommendations under Thrust 2 apply mainly to licensed financial advisory firms. There are 62 of these firms. They play a crucial role in our industry because advising is their primary business and they are usually not tied to any specific product manufacturers. While we value their focus and independence, we also need to ensure that these firms have adequate management structures, expertise and financial resources to conduct their business. Recommendations 4-8 address all these areas. We have sought to calibrate the requirements so that they commensurate with the volume and type of services that the firm provides. The changes are significant and sufficient time should be given for firms to meet these new requirements.

Thrust 3: Making Financial Advising a Dedicated Service

10 The primary issue we sought to address here is financial advisers doing non-financial advising work. About 1 in 5 representatives do this, from holding full-time jobs to running their own businesses to selling other products like real estate. Inherently, there is nothing wrong with financial advisers doing non-FA activities and some, arguably, may be synergistic to financial advising. But there are 3 risks we should be mindful of: conflict of interest, tarnishing the image of the industry, and dilution of focus.

11 Because individual cases are so varied, the Panel took the view that it would not be appropriate to prescribe exactly what activities advisers can engage in. Rather, we have crafted a set of principles to guide FA firms. These are presented in Para 3.5 of the main report. Specifically, we have indentified money lending, promoting junkets for casinos, selling real estate and marketing investment products that are not regulated under the Financial Advisers Act (FAA), as examples of activities that should not be conducted by financial advisers.

12 There is a second issue under Thrust 3 regarding FA firms engaging non-financial advisers as introducers. Recommendations 12-16 address this.

Thrust 4: Lowering Distribution Costs

13 How do we lower distribution costs? Let me touch on 2 ideas that the Panel considered but did not adopt. The first was to re-impose a hard cap on commissions. The experiences with price controls, in Singapore before 2002, and in other jurisdictions that still have them, were not compelling. Commissions tend to gravitate towards the cap and stay there. This means we will need to ensure that the cap is set at the right level all the time. If it is too high, consumers will end up paying too much. If it is too low, consumers may end up being under-served. The second idea was to ban commissions altogether and switch to fees as the United Kingdom and Australia have done. However, it was not clear that fees would necessarily be cheaper than commissions. In fact, it was more likely that customers with smaller investments ended paying more. When we started this review, we did an on-line survey on Singaporean's receptivity towards a fee-based model. 80% were not prepared to pay an up-front fee for advice. A pre-mature switch may again result in Singaporeans being under-served.

14 We believe that a better approach to lowering costs is through harnessing competitive market forces. The Collective Investment Schemes (CIS) and securities markets are already fairly competitive. In the insurance market, however, consumers can be further empowered in three ways. First, we want to make it easier for consumers to compare products. The Panel recommends that MAS works with the industry to develop a web aggregator that allows consumers to easily compare pricing, benefits and other features of similar products offered by different insurers. A person keys in some basic information – type of policy, age, gender, smoking or not, etc. – and the aggregator can give him the approximate pricing and features of different providers. This will enable him to make a more informed choice.

15 Second, for basic insurance products, where minimal advising is required, the commissions paid to representatives are mainly for their effort in seeking out passive consumers - what the industry terms as prospecting. This is an important role that representatives play. However, consumers who are self-directed should not be required to pay the same commission. We thus, recommend that life insurance companies provide a direct channel, through which self-directed customers can buy basic insurance products directly from the insurer for a nominal fee. The direct channel provides an important cross-channel competition for basic insurance products and can help limit distribution costs. If commissions become too expensive, more consumers will switch to the direct channel.

16 Because there is no advice in the direct channel, the products have to be simple. We envisage that the products that can be bought through the direct channel will include term insurance, whole life insurance and stand-alone critical illness protection.

17 Third, consumers will be able to make more informed choices if the information on distribution costs is made readily apparent and easily understandable. Recommendations 19-22 deal with increasing disclosure of distribution costs for specific products.

Thrust 5: Promoting a Culture of Fair Dealing

18 The Panel recognized that a fair dealing culture cannot be instilled by rules alone. It needs to be embedded into remuneration structures and management responsibilities. We made 3 sets of recommendations under this thrust.

19 The first set deals with representatives' remuneration. We believe that representatives' remuneration, which is largely tied to sales volume now, should be better aligned with customers' interests. To this end, we propose:

- Distributing total commissions paid on life insurance products more evenly, with no more than 40% of the commissions to be paid in the first year.
- Requiring all FA firms to adopt a balanced score-card framework to remunerate representatives, incorporating non-sales KPIs like the quality of advice and the suitability of recommendations.
- Banning all product-specific incentives. Representatives should not be given special bonuses to sell specific products as these may bias their advice to their clients.

20 The second set deals with management responsibilities. Specifically, we believe that the Board and Senior Management should be responsible for building a fair dealing culture in their firm. This will be incorporated in MAS' risk and regulatory assessment of the firm. We also recommend strengthening the complaints handling and resolution processes.

21 Third, we believe that the industry associations can play an active role in promoting a culture of fair dealing. We recommend that the Association of Banks in Singapore (ABS) and LIA develop KPIs for their members and monitor this through regular mystery shopping exercises and after-sales surveys.

Conclusion

22 I have given a quick summary of the recommendations. The Panel's report is now presented to MAS. Over the next few months, MAS will consult on these recommendations and then decide if they should be adopted.

23 Finally, it leaves me to thank my Panel members for all their hard work and their invaluable contributions to this report. I believe the recommendations here will put the industry on a stronger footing and improve the financial well-being of Singaporeans for the long term.

Thank you, we are happy to take your questions.