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Regulator Introduces New Requirements for Participating Business in Singapore

by Ken Hung and Eng Hun Yeoh

The Monetary Authority of Singapore (MAS), regulator of the financial industry in the country has recently introduced a new regulatory notice for life insurers writing traditional participating business in Singapore. This Notice, *MAS Notice 320: Management of Participating Life Insurance Business,* covers both the corporate governance and disclosure aspects of running a participating business, and has an expected implementation date of Jan. 1, 2008 and March 1, 2008 respectively.

Background

MAS Notice 320 is the result of a review of participating business conducted by MAS in consultation with the life insurance industry. Participating business still forms a significant share of new business of the life insurance industry in Singapore, and it had been obvious from policyholder complaints and queries that the average policyholder had a rather poor understanding of par policies. In addition, Singapore insurers employ a variety of approaches to surplus distributions, including both American-styled cash dividends and U.K.-styled reversionary bonuses. Compared to many markets, there are also relatively larger numbers of bonus series, and greater variance in bonus philosophy. All these make par business relatively difficult to understand.

At the same time, there had been various regulatory initiatives in other jurisdictions to improve the governance and transparency of par business, key among them the requirement for par funds in the United Kingdom to have a Principles and Practices of Financial Management (PPFM) document. In the same vein, an objective of the review of participating business was to improve the governance of par business in Singapore. It was noted that in the Singapore context, bonus philosophies tended to not be clearly stated, and mainly rested in the judgment of the Appointed Actuary. A change in Appointed Actuary could thus result in significant shifts in bonus philosophy, which could be avoided by improved governance procedures.

An industry workgroup, consisting of representatives from MAS, the Life Insurance Association (LIA), the Singapore Actuarial Society and industry players, was formed to conduct the review. MAS also conducted a public consultation of the workgroup's recommendation. MAS Notice 320 was a result of these efforts.

Internal Governance Policy

Under the new Notice, all life insurers which have established or will be establishing a participating fund shall put in place an internal governance policy on the management of its participating life insurance business. The purpose of this governance policy is to set a clear framework for the management of the participating life insurance business to ensure that the business is efficiently managed and policyholder interests are safeguarded.

The governance policy will cover areas such as bonus determination, investment of participating fund assets, risk management and expense allocation to the participating fund. Key principles that should be reflected in the governance policy include equity to policyholders and maintenance of the solvency of the participating fund. Once put in place, the governance policy shall be reviewed annually to ensure it remains relevant.

Traditionally, par fund management has been seen as primarily the responsibility of the Appointed Actuary. According to the Insurance Act, the role of the Appointed Actuary includes responsibility for premium rate setting, allocation of surplus, assistance in formulating investment policy, financial condition investigation, etc. The Appointed Actuary shall also provide a written report to the Principal Officer and Board of Directors on any matter that has material adverse effect on the financial condition of the insurer and requires rectification by the insurer.

While not diluting the role of the Appointed Actuary, MAS Notice 320 emphasizes the

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principle of Board accountability. According to this Notice, the onus is on the Board of Directors to ensure that the participating fund is managed in accordance with the governance policy. While not a departure from previous practice, the formalization of this principle highlights the need of Directors to be vigilant in matters related to the participating fund.

Disclosure to Policyholders

The new disclosure framework is achieved via a combination of mandatory regulatory requirements as set out in MAS Notice 320, and industry guidelines provided by the LIA.

The disclosure requirements in the Notice address the need to improve the policyholders' understanding of traditional participating policies. This is to be achieved by increasing disclosure to participating policyholders both at point-of-sale and post-sales. The new point-of-sale disclosure requirements affect the Product Summary, while post-sales disclosure requirements affect the Annual Bonus Update.

In the Product Summary, additional disclosure is required in areas such as bonus determination (e.g. what risks affect the level of bonus, how these risks are shared with other plans, how bonuses are smoothed, actual bonuses declared in the past three years), investment of participating fund assets (asset allocation, actual investment performance and investment expense ratio over the past three years), fees and charges imposed on participating policies, and any potential conflict of interest.

The Annual Bonus Update that should be sent out on an annual basis is the main document affected by the new post-sales disclosure requirements. New information that is required in the Annual Bonus Update include a description of the past performance and future outlook of the par fund, and an explanation of how this will impact future bonus allocations; disclosure of reversionary and terminal bonus rates in the past three years; and a revised projection of surrender and maturity values upon any revision (or expected revision) of bonus rates.

In conjunction with the release of the Notice, LIA has released new industry guidelines setting out a new benefit illustration format. The new format shows the projection of policy benefits on two different investment rates of return instead of one. This provides the policyholder with a better understanding of the potential of lower returns, should investment returns be below expectations.

At the same time, LIA has also released a new guide to the policyholders called "Your Guide to Participating Policies" which contains the basic information on how a participating policy works.

To ensure that these additional disclosures are useful and can be better understood to customers, the LIA commissioned a consumer survey on the proposed disclosure documents. The industry is hence confident that the disclosures will be meaningful to the customers, and do not unnecessarily add to compliance costs.

Industry Reaction

This Notice follows several rounds of close consultation with the Life Insurance Association (LIA), the industry group representing life insurers in Singapore. The new requirement was generally well received by the industry, and is seen as a positive step towards reinvigorating the role of the participating policy in today's insurance landscape. ☐