

**IFPHK's Response to the Insurance Authority's
Consultation Paper on Draft Guidelines on Exercising
Power to Impose Pecuniary Penalty in Respect of
Regulated Persons Under the Insurance Ordinance
(Cap.41)**

December 2018

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IFPHK's Profile





Background

The Institute of Financial Planners of Hong Kong ("IFPHK") was established in June 2000 as a non-profit organization for the fast-growing financial industry. It aims to be recognized in the region as the premier professional body representing those financial planners that uphold the highest standards for the benefit of the public.

The IFPHK is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited ("FPSB") to grant the much-coveted and internationally-recognized CFP^{CM} certification and AFPTM certification to qualified financial planning professionals in Hong Kong and Macau.

It represents more than 6,800 financial planning practitioners in Hong Kong from such diverse professional backgrounds as banking, insurance, independent financial advisory, stockbroking, accounting, and legal services.

Currently there are more than 147,000 CFP certificants in 24 countries/regions; the majority of these professionals are in the U.S., Canada, China, Australia and Japan, with more than 4,700 CFP certificants in Hong Kong.

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IFPHK's interest in this consultation

The Institute of Financial Planners of Hong Kong ("IFPHK") was established in June 2000 as a non-profit organization for the fast-growing financial industry. It aims to be recognized in the region as a professional body representing those financial planners that uphold the highest standards for the benefit of the public. The IFPHK is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited to grant the much-coveted and

internationally-recognized CFP^{CM} Certification and AFPTM Certification to qualified financial planning professionals in Hong Kong and Macau. In view of the growing demand for knowledge in retirement planning products, the IFPHK, in 2016, pioneered in offering a retirement-centric qualification – the Qualified Retirement Advisor (“QRA”) – focusing on products and practical skills.

It is the IFPHK’s mission to promote the importance of financial planning. Financial planning refers to the process of setting, planning, achieving and reviewing life goals through the proper management of finances. Insurance is considered the cornerstone of financial planning. The effective and proper use of insurance products helps spread risk, which can minimize the impact of risk on families should events take a downturn. Insurance is therefore an important part of the IFPHK’s financial planning education and certification programme. Having knowledgeable insurance practitioners, proper consumer understanding of what insurance policies do, effective products, and financially sound underwriters is essential for those who seek financial planning.

In Hong Kong, financial planners work in different segments within the financial services industry. Financial planners can be insurance agents working in insurance companies, insurance brokers working in insurance brokerages, or Independent Financial Advisors (“IFAs”). At present, about 41% of the IFPHK’s members work in the insurance industry and 9% work as IFAs.

As the leading professional institute representing the interests of the financial planning industry, the IFPHK has a duty to respond to any consultation paper that may impact its members and their clients. The IFPHK has previously provided feedback on the Consultation Papers “[Proposed Establishment of an Independent Insurance Authority](#)” and “[Financial Services and the Treasury Bureau Consultation Paper on Key Legislative Proposals on Establishment of an Independent Insurance Authority \(“IIA”\)](#)”. The IFPHK always strongly supports the establishment of an Independent Insurance Authority, which we would consider to be the most important breakthrough of Hong Kong’s financial industry. We have provided our comments on the draft guidelines on both the fit and proper criteria for licensed insurance intermediaries, and their continuing professional development, and have interest in this public consultation paper in relation to future enforcement actions of the insurance industry.

IFPHK's representation

The IFPHK was founded by 30 members (the "Founding Members") to raise the standards of financial planners and highlight the importance of sound financial planning.

The IFPHK currently has 38 Corporate Members, including banks, financial advisors, insurance companies and securities brokerages. With our Corporate Members providing a full spectrum of client services and products, the IFPHK is well positioned to understand the needs, concerns and aspirations of the financial planning community.

The IA Consultation

On 26 October 2018, the Insurance Authority (IA) launched a two-month public consultation (the Consultation Paper) on the draft Guideline on Exercising Power to Impose Pecuniary Penalty in respect of Regulated Persons under the Insurance Ordinance (Cap. 41) (the “Guideline”). This consultation forms part of the IA’s preparation for the commencement of the new regulatory regime for insurance intermediaries tentatively starting from mid-2019 under which the IA will start direct regulation of insurance intermediaries. The submission deadline of the Consultation Paper is 27 December 2018.

The draft Guideline suggests that the penalty should be effective, proportionate and fair. The IA will consider all circumstances of the case and take into account a number of factors including the nature, seriousness and impact of the conduct, behavior of the person since the conduct was identified, and disciplinary record and compliance history of the person. The financial resources of the regulated person is also a factor the IA proposes to consider in determining whether to impose pecuniary penalty on the regulated person and the penalty amount.

The Guideline will take effect upon commencement of regulation of insurance intermediaries by the IA. However, all cases of alleged contravention of applicable rules or requirements that occurred before the commencement date will be followed up and considered by the IA according to the applicable rules or requirements prevailing at the time when the contravention occurred. In such cases the range of sanctions (including pecuniary penalties) available to the IA will be the same as those that could have been imposed by the Self-Regulatory Organisations under the current regime.

IFPHK's Submission

The views expressed in this submission paper are not necessarily simply summaries of the views taken from the industry. They have undergone independent and critical analysis and consideration by the IFPHK as a professional body. As a result, not all the views collected by the IFPHK are recorded in this submission paper. Nor have all the views expressed in this paper been directly endorsed by the industry representatives or members consulted.

In considering the various proposals of the Consultation Paper, the IFPHK's comments are based upon the following principles and beliefs:

IFPHK's Principles

Aligning with International best practice

Globalization and financial market integration has increased rapidly in the past decade. As an international financial centre, Hong Kong is not immune from international financial market and regulatory development. This has been illustrated by the recent financial crisis where problems originating in one country quickly spread across the globe. Because of the global contagion witnessed during the current financial crisis, there have been greater calls for better coordination between regulators from different jurisdictions and for an increase in the convergence of financial regulation. International organizations such as the G20 and other political and supervisory bodies continue to drive financial services sector reform – both globally and at a local level. The adoption of International Association of Insurance Supervisors (“IAIS”) standards in October 2011 was a catalyst for many insurance supervisors to commence reform¹. The Insurance Core Principles, Standard, Guidance and Assessment Methodology (“ICP”) provides a globally accepted framework for the supervision of the insurance sector. It contains 26 principles that IAIS members are advised to observe and adopt. In consideration of the recent development, it is necessary for the insurance industry to keep up with global standards.

Enhancing consumer protection

The IFPHK regards that the reputation of the financial planning industry has been unfairly tarnished after the financial crisis due to varying standards of sales practice and professionalism. The confidence of consumers has not been restored after the crisis. In 2016, a territory-wide study

¹ KPMG, Evolving Insurance Regulation, Time to get ahead, February 2012.

by the IFPHK with GfK found that only 18% of respondents said their confidence in the markets had been fully restored after the 2008 Lehman Brothers incident.² According to the latest trust barometer report of Edelman, trust in financial services has been continuously declining in Hong Kong. The index has dropped from 55% to 47% this year, representing general population distrust of financial services institutions. Meanwhile, informed public trust in financial services has seen a double-digit decline, with Hong Kong's index decreasing by 15% to 48%³. As financial products get more complex and sophisticated, it is of utmost importance that investors/consumers are provided with proper and adequate protection under a sound and effective regulatory system. The IFPHK supports a regulatory system that would facilitate delivering better insurance products and services to the benefit of members of the public, as well as protecting them.

Ensuring a level playing field across distribution channels and different sectors of the financial service industry

It should be noted that the key assumption in this submission is that the proposed changes in legislation should be adopted consistently by all financial intermediaries servicing retail consumers operating in the financial advisory, banking and insurance sectors. IFPHK believes that failure to implement a consistent approach across the industry could result in significant negative consumer and industry consequences. IFPHK is frequently urged by industry professionals to highlight the need for implementing a consistent approach across the industry to establish a **'level playing field'** among all financial planners/advisors in the different distribution segments, i.e. banking, insurance and independent financial advisors. We have already expressed our views in our responses to various consultation documents. IFPHK strongly believes that such a consistent approach will reduce significantly any regulatory arbitrage that could potentially undermine the good intention of protecting investors.

Maintaining and enhancing the competitiveness and diversity of the insurance market

The insurance market in Hong Kong is very competitive, and it is somewhat surprising that such a small place is able to accommodate over 70,000 practitioners. The IFPHK has always stressed that a regulatory framework should deliver measurable benefits to the insurance industry in the medium to long term. It should also enable a healthy and sustainable business environment for the industry to thrive and develop. To preserve the fair competition and diversity of the market, the IIA

² The Value of Financial Planning and Awareness of CFP Certification: A Global Financial Planning Survey Hong Kong Results, FPSB and GfK, 2016

³ 2018 Edelman Trust Barometer

should not only be progressive and adhere to international standards when formulating its supervisory principles and details, but should have an explicit responsibility to strike a balance between regulation and market growth, keeping in mind the difference in business nature and operation model of the various market participants.

IA's proposal

Under the new regulatory regime, the IA is empowered to take a range of disciplinary actions against a person who is or was a regulated person. The new section 81 of the Ordinance, which gives the IA disciplinary powers over such persons, is set out in full in **SCHEDULE 1**. The new section 81 of the Ordinance applies to both current and former regulated persons (and, where used in this consultation paper and in the Guideline, the term “regulated person” covers both current and former regulated persons).

There are effectively two circumstances in which the IA may take disciplinary action(s) in respect of a person who is or was a regulated person.

- a. The first is when the regulated person is/was guilty of misconduct, which is defined in the new section 80(1) of the Ordinance.
- b. The second is when the regulated person fails or failed to be fit and proper. The new section 64ZZA sets out the matters the IA must have regard to in determining whether a person is a fit and proper person.

One of the disciplinary actions the IA may take is imposing a pecuniary penalty not exceeding the greater of HK\$10 million or three times the amount of the profit gained or loss avoided

The IA must not exercise a power under the new section 81 without first giving the person in respect of whom the power is to be exercised a reasonable opportunity of being heard

To this end, the IA will issue a Notice of Proposed Disciplinary Action (“NPDA”). The NPDA will set out the IA’s initial findings and proposed disciplinary action(s) (where applicable, including the proposed amount of the pecuniary penalty). The person concerned may then make

representations, written or oral, on the initial findings and proposed disciplinary action(s). If, after taking into account the representations made (if any), the IA decides to proceed with exercising a power under the new section 81 in respect of a person, the IA must inform the person of its decision to do so by a Notice of Decision (“NOD”) in writing and where applicable the NOD must include, amongst other information, the amount of the pecuniary penalty to be imposed under the decision and the period within which it is required to be paid. Any person in respect of whom a decision is made, may apply to the Insurance Appeals Tribunal (“IAT”), for a full merits review of such decision.

Pursuant to the new section 83(1) of the Ordinance⁶, the IA must not exercise the power to impose a pecuniary penalty unless it has published, in the Gazette and in any other manner it considers appropriate, guidelines to indicate the way in which it proposes to exercise that power, and in exercising that power, it has had regard to the guidelines so published. Moreover, the new section 83(3) requires the IA to consult the Monetary Authority before publishing such guideline.

Whilst always taking into account the need to protect existing and potential policy holders, the IA recognizes the need to take a balanced approach and appreciates the importance of pecuniary penalties being effective, proportionate and fair. The IA therefore proposes to take into account a range of relevant factors including whether a pecuniary penalty may cause financial hardship to the regulated person concerned. Finally, pecuniary penalties will be imposed by the IA following a thorough process of review/investigation and the decision to take disciplinary action will be taken independently and objectively.

The IA also regards a pecuniary penalty as a more severe sanction than a reprimand, and a public reprimand as more severe than a private reprimand. As a matter of policy, the IA may publicize its decisions to impose a pecuniary penalty.

The IA proposes that when considering whether to impose a pecuniary penalty and the amount of the penalty, it will consider all the circumstances of the particular case and take into account a number of factors where relevant including the following non-exhaustive factors (in respect of which non-exhaustive examples have been given):

- a. the nature, seriousness and impact of the conduct;

- b. the behavior of the person since the conduct was identified;
- c. the previous disciplinary record and compliance history of the person; and
- d. other relevant factors.

The IA is conscious of the potential consequences that high fine levels may have on a person. To include in the draft Guideline that they consider the financial resources of the regulated person – a pecuniary penalty should not have the likely effect of putting the regulated person concerned in financial jeopardy;

Furthermore, the IA will consider the results of criminal actions (not just civil actions) taken against a regulated person before imposing a pecuniary penalty.

The IA has decided not to adopt a tariff-based approach (e.g. a list/ menu of the types of conduct for which a person may be disciplined and set certain levels of fine for each type of conduct). In view of the diverse range of regulated activities that will be carried on by licensed insurance intermediaries and the wide variety of types of licensed insurance intermediary (ranging from licensed individual agents tied to major insurers, bank staff directly selling insurance products and employees of major international insurance broking firms) all of which will be covered by the Guideline, a tariff-based approach would unlikely achieve effective, proportionate or fair outcomes.

IFPHK's Response

The IFPHK considers that the best regulations would need proper enforcement to yield results. IAIS ICP Principle 11 - Enforcement states that "The supervisor enforces corrective action and, where needed, imposes sanctions based on clear and objective criteria that are publicly disclosed." Clause 11.6 said "there are sanctions by way of fines and other penalties against insurers and individuals where the provisions of the legislation are breached. The sanctions are proportionate to the identified breach." We consider it makes sense to equip IA with the exercising power to impose pecuniary penalty as other regulator such as the Securities and Futures Commission (SFC) also equip with such power.

In our previous submission on establishment of an independent insurance authority, we have comments on the fine amount of \$10,000,000. As many brokerages are small in their business size and scope, a maximum penalty of \$10,000,000 is disproportionate to their business models.

As such, some practitioners IFPHK interviewed consider that disciplinary action should be linked to the nature and size of the business.

Notwithstanding with the above, IFPHK thinks it is sufficient to state in the penalty guideline that nature and size of the business is one of the considering factors when determining a disciplinary action. It is not necessary to set a penalty cap at three times the amount of the profit gained or loss avoided.