

**Guidance to Authorized Institutions (“AIs”) on  
Selling of Protection Linked Plan (“PLP”)**

**1. *Product due diligence (“PDD”)***

- 1.1 Before launching a new PLP, AIs should adequately conduct their own PDD, taking into account, among other factors, the nature, features and risks of the PLP (including those of the underlying investment options), the credibility and capability of the insurer, and other factors that may have an impact on the risk and benefit profile of the PLP (including those of the underlying investment options). Through the PDD process, AIs should also identify whether any underlying investment option of the PLP is linked to a derivative fund.
- 1.2 AIs should determine in what aspects the PLP is considered suitable for certain customers and identify the target customer group and their profile. The target customer profile should be taken into account in suitability assessment.
- 1.3 In determining the appropriate expected holding period of a PLP for matching with customer’s circumstances, AIs should take into consideration, among other things, the premium payment period, the surrender charge period, and the assessment on comparable payout required by the Securities and Futures Commission (“SFC”) for the authorisation of investment-linked assurance scheme (“ILAS”) products.
- 1.4 AIs that intend to distribute PLP for insurers that are their group companies should ensure that the level of remuneration they would receive from the insurer for distribution of the PLP is determined on arm’s length basis and commercially justifiable. There should not be any arrangement which may prejudice, directly or indirectly, the intermediaries’ remuneration disclosure requirements.
- 1.5 AIs should conduct PDD on a PLP (including the product risk ratings assigned to the underlying investment options) on a continuous basis at appropriate intervals and take follow-up actions where necessary. The independent risk management function of AIs should be involved in the PDD process, and all relevant departments such as risk control, legal and compliance should be consulted as appropriate.

## **2. *Suitability assessment and product recommendation***

- 2.1 AIs should ensure that the recommended PLP (including the underlying investment options) is suitable for a customer having regard to the customer's circumstances. Before recommending a PLP to a customer, AIs should seek to obtain adequate information about the customer's circumstances, and conduct suitability assessment in accordance with the relevant regulatory requirements, including the Financial Needs Analysis ("FNA"), the Risk Profile Questionnaire ("RPQ") and other requirements in Guideline on Financial Needs Analysis ("GL30"), Guideline on Sale of Investment-Linked Assurance Scheme ("ILAS") Products ("GL26") and Code of Conduct<sup>1</sup> issued by the Insurance Authority ("IA"). The rationales for the recommendation should be properly documented and explained to the customer.
- 2.2 RPQ should be conducted by licensed insurance intermediaries. In this connection, AIs are expected to arrange non-sales staff who is a licensed insurance intermediary to carry out the RPQ process for retail banking customers. In the situation where it is not practicable to arrange non-sales staff to conduct RPQ for retail banking customers, an independent review should be performed on the assessment conducted by sales staff<sup>2</sup>.
- 2.3 AIs should request the customer to set out the reasons/considerations for procuring PLP in the "Statement of Purpose" paragraph of the Important Facts Statement and Applicant's Declarations ("IFS-AD"), and have due regard to such information in assessing whether the PLP is suitable for the customer.
- 2.4 Where there are inconsistent answers given by a customer in the "Statement of Purpose" paragraph, FNA and/or RPQ, AIs should seek clarifications from the customer and properly document the justifications/reasons provided by the customer.
- 2.5 Among other things, AIs should ensure that the recommended PLP is suitable for the customer's needs and objectives, including the amount of insurance protection need and the protection period as evaluated in the FNA. In general, PLP is not suitable for a customer who does not have dual objective of insurance and investment; or who is not able and willing to make his/her own decision to choose or manage different underlying investment options under an insurance product. Where a customer

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<sup>1</sup> Code of Conduct for Licensed Insurance Agents or Code of Conduct for Licensed Insurance Brokers, as applicable.

<sup>2</sup> See the HKMA's circular "Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products" dated 25 September 2019.

indicates that he/she does not need and want insurance/investment products, AIs should not recommend PLP. In addition, if (i) high level of protection is not applicable to a customer at the inception and throughout the entire premium payment period of the PLP (e.g. due to the age of the customer); (ii) the period of high level of protection offered by the PLP is shorter than the target period for high level of protection of a customer; or (iii) a customer has low insurance protection need, the PLP is generally unlikely to be suitable for the customer. If a PLP is recommended despite any one of the scenarios (i) to (iii) above, the AI must have sufficient justification to substantiate how the PLP is still suitable for the customer and comply with paragraph 2.10 below.

- 2.6 Customer's affordability should be duly considered in suitability assessment. AIs should develop and adopt proper methodologies and criteria for assessing the customer's affordability during the entire premium payment period. The overall financial circumstances of the customer should be considered, including the customer's income, liquid assets, expenses (including premium payable for other insurance policies held by the customer), financial liabilities/commitments, source of fund for premium payment and its sustainability, the impact of the customer's retirement plan, the amount of funds and the period that the customer is willing and able to make premium payment, etc. Prudent thresholds should be adopted to assess the customer's capability in terms of the amount and period (e.g. taking into account the customer's intended retirement age and financial capability after retirement) to pay the premium. Moreover, given the risks and consequences of exercising premium holiday, when assessing the customer's affordability, AIs should not assume that the customer will exercise premium holiday or attempt to induce the customer to assume that premium holiday option will be exercised in deciding whether to take up a PLP (for example, by advising that the policy is affordable if the premium holiday option is exercised).
- 2.7 AIs should not recommend a PLP to a customer if the customer's preferred investment horizon is shorter than the expected holding period of the PLP. Moreover, given that PLP is generally a longer term product, AIs should ensure that due regard is paid to a customer's liquidity need and retirement plan in the suitability assessment and that the surrender charges of the PLP will not create financial hardship on the customer after retirement.
- 2.8 AIs should take into account a customer's concentration risk<sup>3</sup> in the

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<sup>3</sup> See the HKMA's circulars "Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products" dated 25 September 2019 and "Frequently Asked Questions on Investor Protection Measures" dated 23 December 2020.

suitability assessment and put in place reasonable methodologies and thresholds for assessing such risk. AIs should take into account, among other relevant factors, the cumulative concentrations in ILAS products (including non-PLP products), and in the underlying investment options having regard to the customer's total investments. In measuring the amounts of ILAS products and the underlying investment options for calculating asset concentrations, the total amount of premium payable by the customer within the premium payment period and other relevant factors such as how long the customer intends to hold the policy should be taken into consideration.

- 2.9 Where a customer wishes to choose an underlying investment option which is linked to a derivative fund, AIs should ensure that the customer understands the nature and risks of that underlying investment option which is linked to a derivative fund. If such customer does not have knowledge of derivatives, AIs should warn the customer about the choice, and provide appropriate advice to the customer as to whether or not the choice is suitable for the customer in all circumstances having regard to the information about the customer. If, despite the advice, the customer insists on choosing the underlying investment option which is linked to a derivative fund, the customer must provide sufficient explanation, with confirmation in writing, for the decision to proceed. If the choice is assessed to be unsuitable for the customer, AIs may only proceed if to do so would be in accordance with the principle of "treating customers fairly" and the relevant justifications should be documented in writing. Record of the warning and other communications with the customer should be maintained.
- 2.10 In addition, AIs should take extra care in handling transactions with mismatch(es) or exception(s) and put in place adequate controls in accordance with the existing regulatory requirements<sup>4</sup>.

#### *Top-up and switching*

- 2.11 It is a common feature of PLP that top-up investment and subsequent switching between underlying investment options are allowed. At the point-of-sale of PLP, AIs should disclose the channels through which the customer may make top-up investment or switching transaction, and alert the customer to the possible risk that such top-up investment or switching of underlying investment options after policy inception may be inconsistent with the risk profile of the customer.

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<sup>4</sup> Including the HKMA's circular "Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products" dated 25 September 2019.

### 3. *Product disclosure*

- 3.1 At the point-of-sale, AIs should provide to the customer, in the preferred language of the customer (i.e. Chinese or English), all the relevant product documents, such as product brochure, investment choice brochure, Product Key Facts Statement (“KFS”), IFS-AD, illustration documents including the Supplementary Sheet of the Benefit Illustration Statement, etc.
- 3.2 With reference to the product documents provided, AIs should make adequate disclosure and explanation of the nature and the key features and risks of the PLP and its underlying investment options at the point-of-sale, so as to ensure that the customer is properly apprised of the product and able to make informed decision. AIs should allow sufficient time for the customer to understand the information and seek independent professional advice or advice from relatives or friends where necessary. The disclosure and explanation should include, among other things, the following items, to the extent applicable:
- (a) **Product nature** – AIs should make it clear to the customer at the outset that the product is an investment-linked insurance product which provides both insurance protection and investment element with reference to the underlying investment options chosen. AIs should not (i) make any representation to the effect that the PLP is equivalent or similar to any kind of deposit or savings plans, or investment funds without any insurance element, or (ii) make any description that disguises the insurance or investment element of the PLP.
  - (b) **Tenor** – AIs should disclose and explain the timeframes for relevant features of the PLP to the customer (e.g. policy term, expected holding period, surrender charge period, payment period of bonus). AIs should also alert the customer to the consequences of surrender and early termination and that the PLP is designed to be held for a medium/long term period.
  - (c) **Investment options and risks** – AIs should disclose and explain the nature and the key features and risks of the underlying investment options of the PLP, including the details of arrangement to facilitate de-risking of the customer towards retirement. AIs should make it clear, where applicable, that there is no guarantee of the repayment of principal.

- (d) **Credit risk** – AIs should disclose and explain that the customer is subject to the credit risk of the insurer, including that the premium the customer pays will become part of the assets of the insurer, and that the customer will not have any right to or ownership of the underlying funds of the underlying investment options.
- (e) **Premium payment and policy loan** – AIs should clearly disclose and explain to the customer the amount and the frequency of premium payment, the premium payment period and the consequences of late payment and non-payment of premium (including the exercise of premium holiday). Where the PLP allows for premium holiday and/or provides policy loan, AIs should specifically alert the customer to how the feature operates (e.g. whether premium holiday will be automatically triggered when the customer does not pay a premium payment that is due) as well as the possible consequences (e.g. the value and, where applicable, the amount of death benefit of the PLP may be reduced as the fees and charges are still deductible during the premium holiday; loss of entitlement to bonus or no-lapse guarantee; interest and charges of policy loan; and possible termination of the policy when the value of the PLP is insufficient to cover the fees and charges or the outstanding loan and accumulated interest).
- (f) **Fees and charges** – AIs should provide disclosure and explanation in relation to the fees and charges at both the policy level (e.g. cost of insurance, upfront charge/surrender charge and ongoing platform fee) and the underlying fund level (e.g. management fee and performance fee). AIs should also disclose and explain that due to the fees and charges, the amount of premium available for investment under the PLP will be reduced and the return on the PLP as a whole may be lower than the return of the underlying funds of the underlying investment options. Moreover, AIs should alert the customer that the cost of insurance may increase significantly during the term of the PLP due to factors such as age and investment losses, and this may result in a significant or even total loss of the premium paid. AIs should also draw the customer's attention to the key restrictions imposed on surrender and/or partial withdrawal of the PLP.
- (g) **Insurance protection and surrender value** – AIs should disclose and explain the amounts of and the bases of determining the death benefit and the surrender value, including:

- (i) the number of years that the PLP will provide high level of protection to the customer and the minimum amount of death benefit during that period;
- (ii) the customer's age at which the amount of death benefit may be significantly reduced due to the end of the high level of protection period, the minimum amount of death benefit from that age onwards, and that the death benefit may not be sufficient for the customer's insurance protection need;
- (iii) the fact that the assumed net rates of return adopted in the illustration documents are net of any fees and charges at the underlying fund level and are not indicative of the actual return of the policy; and
- (iv) the fact that the actual amounts of death benefit and surrender value are subject to market risk and/or foreign exchange risk (where applicable).

AIs should also disclose and explain the impacts on death benefit (e.g. amount of death benefit would be downward adjusted) in case of non-payment of premium or partial withdrawal.

- (h) **Early termination risk** – AIs should disclose and explain the condition that will trigger early termination of the policy (e.g. value of the PLP is negative due to poor investment performance or is insufficient to cover the ongoing fees and charges; failure of the customer to make premium payment) and the consequences (e.g. loss of all premium paid and benefits). AIs should draw the customer's attention to (i) whether and when the PLP would early terminate under the assumed net rates of return as set out in the illustration documents, and that partial withdrawal may cause the PLP to be terminated even earlier; and (ii) the return of investing in underlying investment options with low risk rating, which generally have a lower expected return, may not be sufficient to cover the ongoing fees and charges of the PLP.
- (i) **Intermediaries' remuneration** – AIs are required to disclose and explain to the customer the information set out in the "Licensed Insurance Intermediaries' Remuneration" section of the IFS-AD. Among others, AIs should disclose and explain to the customer his/her right to ask for details of the remuneration of the AI in connection with the distribution of the PLP. If the customer wishes to know more about the remuneration of the AI, the AI should provide details including the types, actual levels, actual amounts, actual basis of calculation, timing of receiving, etc. of the

remuneration. Where the customer chooses a premium payment term for which the standard remuneration disclosure statement prepared by the insurer does not disclose the specific remuneration due to the adoption of a banding approach<sup>5</sup>, AIs should disclose and explain to the customer his/her right to ask for the specific remuneration disclosure statement based on the chosen premium payment term, and should facilitate provision of such specific disclosure statement to the customer upon request.

- (j) **IFS-AD** – Apart from intermediaries’ remuneration, AIs should also disclose and explain every paragraph in the IFS-AD to the customer. AIs should not proceed with a PLP application if any of the applicable confirmations in the IFS-AD has not been properly signed by the customer and the sales staff. A copy of the duly signed IFS-AD, among other documents, should be provided to the customer at the point-of-sale.

- 3.3 AIs should explain to the customer the pros and cons of PLP as compared with direct investment in the underlying funds of the underlying investment options (which can be through asset-based fund platform or otherwise) and taking out a life insurance policy separately<sup>6</sup>. The AI should also disclose the maximum level of remuneration receivable by it if the customer directly invests in the underlying fund(s) of the underlying investment option(s) through the AI, should the underlying fund(s) of the underlying investment option(s) chosen by the customer be available on the AI’s investment selling platform. In this connection, AIs should only arrange licensed insurance intermediaries who have adequate knowledge and experience in investment products to handle the sale of PLP.

#### **4. *Audio recording and record maintenance***

- 4.1 AIs should audio record the selling process of PLP for retail banking customers and ensure that such audio records are adequately maintained and readily accessible as and when necessary to demonstrate that the selling process has been duly conducted<sup>7</sup>. This should at least cover, to the extent applicable, (i) customer risk profiling; (ii) suitability

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<sup>5</sup> This refers to the disclosure format for regular payment ILAS products set out in paragraph 7.3 of Appendix 2 to the interpretation notes of GL26 issued by the IA.

<sup>6</sup> Disclosure of the conceptual pros and cons may suffice. It may not necessarily require a technical comparison involving actuarial information.

<sup>7</sup> See the HKMA’s circular “Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products” dated 25 September 2019.



assessment and product recommendation (including handling of mismatches, provision of alternatives and rationales for the recommendation); (iii) disclosure of product nature, features (including but not limited to benefits) and risks; (iv) steps taken to ascertain whether the customer is purchasing the PLP policy as a policy replacement; (v) explanation and completion of applicable important facts statements, including IFS-AD and important facts statement for policy replacement; (vi) comparison of PLP against direct investment in the underlying funds of the underlying investment options and taking out a life insurance policy separately; and (vii) disclosure of the maximum level of remuneration receivable by the AI if the customer directly invests in the underlying fund(s) of the underlying investment option(s) through the AI. Opt-out of this audio recording arrangement is not allowed. For transactions with non-retail banking customers, AIs should also maintain proper audit trail to demonstrate that the selling process has been duly conducted.

- 4.2 For top-up investments or switching transactions processed by AIs, AIs should have audit trail demonstrating that the customer is aware of the possible risks of mismatch arising from the top-up investments or switching transactions. In addition, the audio recording and record maintenance requirements for new policy are applicable to switching transactions that involve solicitation/recommendation and all top-up investments. For switching transactions that do not involve solicitation/recommendation, AIs should have proper audit trail, e.g. audio records, of the customer's acknowledgement that the switching did not involve solicitation/ recommendation by the AI and, where the customer switches into an underlying investment option which is linked to a derivative fund, the suitability assessment (including the handling of mismatch/exception) for processing the switching<sup>8</sup>.
- 4.3 AIs should not adopt non-face-to-face ("non-F2F") distribution channel for selling PLP to retail banking customers if audio recording of the selling process is not practical, except for switching transactions that do not involve solicitation/recommendation by the AI.

## **5. *Management oversight***

- 5.1 AIs should have adequate management oversight of the sale of PLP and establish appropriate management information system for this purpose. High risk areas and exceptions (e.g. transactions with vulnerable customers, transactions with mismatch, affordability issue or asset

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<sup>8</sup> See A19 of the interpretation notes of GL26 issued by the IA.

concentration) should be subject to monitoring and be covered in the regular reviews by independent units (e.g. those by the AI's compliance function). AIs should promptly take appropriate follow-up actions on any irregularity discovered.

## **6. *Vulnerable customers (“VCs”)***

- 6.1 AIs should exercise extra care in selling PLP to VCs. In this connection, AIs should conduct holistic assessment to determine whether a customer is a VC and comply with the relevant regulatory requirement (e.g. companion requirement for retail banking customers)<sup>9</sup>. AIs should also arrange vetting of the audio records of the transactions conducted with VCs as soon as practicable and in any case no later than the expiry of the cooling-off period of the policy. The vetting should be conducted by staff who is not responsible for handling the sale of the PLP and should cover whether the sales process was duly audio recorded and properly conducted. AIs may adopt a risk-based approach in the sampling, and the sample size should be appropriate. Any irregularity identified in the vetting should be followed up promptly with necessary remedial actions to address any prejudiced interest of the customer.

## **7. *Other applicable HKMA's circulars***

- 7.1 This circular has incorporated all relevant regulatory requirements in the three earlier HKMA's circulars relating to ILAS products:
- (a) “Enhanced Regulatory Requirements on Selling of Investment-Linked Assurance Scheme (ILAS) Products” dated 14 March 2011;
  - (b) “Selling of investment-linked assurance scheme (ILAS) products” dated 22 April 2013; and
  - (c) “Disclosure of Remuneration Receivable in respect of Sale of Investment-Linked Assurance Scheme (“ILAS”) Products” dated 17 December 2014.

For the avoidance of doubts, the above circulars are not cancelled, save for those paragraphs and requirements that have become obsolete<sup>10</sup> or

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<sup>9</sup> Including the HKMA's circulars “Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products” dated 25 September 2019 and “Frequently Asked Questions on Investor Protection Measures” dated 23 December 2020.

<sup>10</sup> Upon the commencement of the licensing and regulatory regime for insurance intermediaries under the Insurance Ordinance (Cap. 41) on 23 September 2019 or the end of the transitional periods for the relevant guidelines and interpretation notes of the IA.

have been superseded<sup>11</sup>. In particular, AIs may refer to the circular in (b) above for common issues identified in the thematic on-site examinations conducted back then in avoiding those issues.

- 7.2 In selling PLP, besides this circular, AIs should also comply with the relevant regulatory requirements applicable to ILAS as stipulated in the HKMA's circulars "Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products" dated 25 September 2019 and "Frequently Asked Questions on Investor Protection Measures" dated 23 December 2020, including but not limited to physical segregation, on-going disclosure of a higher product risk rating, and mystery shopping programme, where applicable.

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<sup>11</sup> For example, paragraphs set out in Annex 2 to the HKMA's circular "Investor Protection Measures in respect of Investment, Insurance and Mandatory Provident Fund Products" dated 25 September 2019.