Annex

Application of provisions in the existing guidelines issued by the IA to the design and offering of IUL products by authorized insurers and licensed insurance intermediaries exclusively to Professional Investors in Hong Kong

i) Definitions of terms used in this Annex:

Terminology	Definition
Indexed Universal Life ("IUL")	means a life insurance product that provides, along with a death benefit, a cash value that earns interest by tracking an index or indices (e.g. a stock market index). All references to IUL products in this Annex, unless otherwise specified, refer to IUL products offered to professional investors in Hong Kong.
Professional Investor ("PI")	means "professional investor" as defined in Schedule 1 to the Securities and Futures Ordinance (Cap. 571) ("SFO") and the Securities and Futures (Professional Investor) Rules (Cap. 571D) ("PI Rules").
Mechanism, Components	"Mechanism" refers to the formula-based mechanism that determines the actual crediting rate based on the performance of underlying index(ices), subject to the discretionary components ("Component") such as floor, cap and participating rate in the design of the Mechanism.
Index Account	means any account of an IUL product in which the actual crediting interest rate is determined using the Mechanism and the performance of relevant index(ices).
Budget	for the purpose of capturing the performance of the relevant index(ices), means the budget for the authorized insurer to implement derivatives, investment or a reinsurance strategy, which in turn determines the Components of the Mechanism.

ii) Requirements on IUL products:

Area	Item	Relevant section of GL	Application of requirements to IUL products
Product Design	1	Para 5.1 of GL15	During the product design stage, authorized insurer should carry out due diligence to ensure that the product meets the "fair treatment of customers" principle. Authorized insurer should cover areas such as level of fees and charges, the Components, and the choice of index. For the choice of index, it would be questionable whether the "fair treatment of customers" principle is met if the Index Account links to an index which is only recognized by or constructed by the authorized insurer, or if fees and charges are levied or embedded in the index.

Area	Item	Relevant section of GL	Application of requirements to IUL products
			Before adding or removing any choice of index available to an IUL product, authorized insurer must ensure the "fair treatment of customers" principle is met and the policy remains suitable for policy holder.
	2	Para 5.2 of GL15	The minimum requirement on death benefit, being 105% of the account value, is **not** applicable to IUL products.
	3	Paras 5.3 to 5.5 of GL15	The requirements on fees and charges, sustainability of the product and the "fair treatment of customers" principle apply to IUL products.
Governance	4	Section 2 of Appendix 1 of GL16[1], Section 2 of Appendix 2 of GL16	The IA expects an authorized insurer to have a corporate policy setting out detailed design for its IUL products, and in particular, how the amount of Budget and Component are determined.
	5	Section 2 of Appendix 1 of GL16	The IA expects the Appointed Actuary and the Board of the authorized insurer to observe the relevant requirements in relation to IUL products. The Board is ultimately responsible for ensuring fair treatment of customers. As such, the Board should decide whether the Appointed Actuary should submit regular report to the Board or its delegated committee recommending the change in Components. Such decision should be based on Board's assessment that is proportionate to the nature, scale and complexity of the IUL business, and the assessment should be carried out at least annually.
Provision of Adequate and Clear Information, and Disclosure on Non-Guaranteed Benefits	6	Paras 6.5 to 6.9 of GL16	The requirements on provision of adequate and clear product information and key product risks apply to IUL products. Where applicable, the information disclosure requirements relating to policy loan facility and collateral assignment prescribed in para 6.7 and para 6.8 also apply to IUL products.
	7	Paras 4.1(a)(i) to 4.1(a)(iv) of	The disclosure requirements relating to non-guaranteed benefits apply to IUL products.

[1] The provisions in GL16 referenced in this Annex are those which are specifically pertinent to IUL insurance business. The requirements in these provisions should form part of an effective governance and control system that an authorized insurer is expected to have in place in respect of its IUL business. Compliance with these requirements will be taken into account in assessing the fitness and properness of controllers, directors and key persons in control functions with responsibility for relevant aspects of the insurer's governance and control systems on its IUL insurance business.

Area	Item	Relevant section of GL	Application of requirements to IUL products
		Appendix 1 of GL16	At the point of sale, authorized insurers should also highlight details of the account(s) available to the policy holder, arrangement or options to transfer among accounts, details of the Mechanism, how the Budget and Components are determined[2] under the terms of the IUL policy, and the relevant restrictions on change of policy ownership.
	8	Para 4.1(a)(v) of Appendix 1 of GL16, para 4.2 of Appendix 2 of GL16	Para 4.1(a)(v) of Appendix 1 of GL16 refers to the disclosure requirement on fulfillment ratios and is **not** applicable to IUL products. The disclosure of crediting interest rate history is optional for IUL products. However, if an authorized insurer decides to disclose such history, it must disclose the history of all product series of IUL products and maintain the same level of disclosure going forward.
	9	Para 4.3 of Appendix 2 of GL16, para 4.2(j) of GL26	The requirement on disclosure of key risks applies to IUL products. Authorized insurers are reminded to disclose the lapsation risk due to zero account value, especially if, after policy issuance, further payment of premium is planned but flexible and the authorized insurer does not incentivize the policy holder to pay such premium[3]. Licensed insurance intermediaries have a duty to disclose and explain to customers the risks associated with IUL products.
Suitability Assessment, Advice to Customers, Fair	10	Paras 4.2(a) to 4.2(d) of GL26, para 6.1, para 6.3	Authorized insurers and licensed insurance intermediaries may opt out of the FNA process required by GL26 in carrying on their IUL business. They must, however[4]:

[2] For the avoidance of doubt, while the investment strategy should be disclosed, it is optional to quantify the linkage, if any, between the amount of Budget and return of the investment in the disclosure.

[3] Payment of premium is considered as incentivized by the authorized insurer if the cessation of premium will incur additional policy's fees or charges, or if premium charge will be levied regardless of the actual payment of premium, or if incentive is provided for the actual payment of the premium.

[4] Provided that all the requirements outlined in this Annex are complied with, authorized insurers and licensed insurance intermediaries that carry on long term business are deemed to have consent from the IA per Para. 6.3 of GL30, to opt out of the FNA process in GL26 in their offering and sale of IUL products to PIs. This deemed consent also permits authorized insurers and licensed insurance intermediaries to opt out of the FNA process mentioned para 4.2(e) of GL26 (see item 11). Per para 3.3 of GL26, this Circular also provides further guidance, to be taken into account by the IA, on the application of the standards and practices in GL26 to IUL insurance business.

Area	Item	Relevant section of GL	Application of requirements to IUL products
Treatment of Customers in the Sale, Advice to Customers		and Para 6.5 of GL30	i) restrict the offer and sale of IUL products to customers who satisfy the definition of PIs as defined in Schedule 1 to the SFO and the PI Rules; ii) establish and implement adequate and effective controls and processes to ascertain whether a customer qualifies as a PI as defined in Schedule 1 to the SFO and the PI Rules during the onboarding or know-your-client process, before introducing any IUL product to the customer[5]; iii) take steps to ascertain the investment knowledge and experience of customers who are **individual** PIs looking to acquire IUL products, so as to ascertain the sufficiency of the customer's understanding of risks associated with IUL products[6]; and iv) the intermediary management function of authorized insurers must ensure that licensed insurance intermediaries that refer applications for IUL policies to the insurers, adhere to the requirements above and have such controls and processes in place to achieve this. For the avoidance of doubt, if authorized insurers and licensed insurance intermediaries choose to opt out of the FNA process required by GL26, they are still required to comply with the statutory conduct requirement under section 90(d) of the Insurance Ordinance (Cap. 41) ("IO") and General Principle 6 under the Code of Conduct for Licensed Insurance Agents / Code of Conduct for Licensed Insurance Brokers issued by the IA in relation to the suitability assessment. In light of this, such assessment should at the minimum cover the following aspects: 1. ascertain whether the customer has the need(s)/objective(s) which match(es) with the nature and features of the IUL product; 2. explain clearly to the customer how the IUL product matches with the customer's need(s)

[5] For the avoidance of doubt, objective evidence (e.g. bank/portfolio statements) must be obtained for ascertaining whether a customer is qualified as a PI, and solely relying on a customer's self-declaration is not sufficient.

[6] In ascertaining a customer's investment knowledge and experience, authorized insurers and licensed insurance intermediaries may take into account his/her work experience, academic/professional background, previous transactions executed or with reference to the customer's self-declaration.

Area	Item	Relevant section of GL	Application of requirements to IUL products
			and/or objective(s); and 3. no IUL product should be sold where the information available reveals any issue of concern about the customer's affordability[7]. As general guidance, authorized insurers and licensed insurance intermediaries should not opt out of the FNA process required by GL26 when dealing with vulnerable customers for IUL products, unless there are exceptional justifications for doing so. If an authorized insurer and licensed insurance intermediary choose to adopt the FNA process required by GL26 in the sale of IUL products, it still needs to comply with the requirements in (i) to (iv) above, which are necessary for establishing the PI status and knowledge of the prospective policy holder, as well as all the requirements outlined in this Annex. Where a policy owner submits a request[8] to change the policy ownership of the IUL policy, before processing the request, the authorized insurer must ascertain that: i) the (proposed) new owner satisfies the definition of PI as defined in Schedule 1 to the SFO and the PI Rules; ii) the (proposed) new owner possesses sufficient understanding of risks associated with IUL product; and iii) that the IUL product is suitable for the (proposed) new owner.
	11	Para 4.2(e) of GL26	The requirement to perform FNA and RPQ for top-up investment does **not apply** to IUL products. However, authorized insurers and licensed insurance intermediaries should ensure that the policy holder remains qualified as a PI before processing the relevant top-up[9] investment.

[7] As an example, over-leveraging could be one of the issues of concern about customer's affordability. Refer to circular issued on 1 April 2022 pertaining supervisory standards and key requirements on the use of premium financing for further details.

[8] This does not apply to any contingent ownership arrangement in which the transfer of policy ownership will not be executed until the death of the original policy owner.

[9] This does not apply to policy holders' payment of any amount that is necessary to keep the policy inforce by having sufficient amount of account value for the deduction of fees and charges.

Area	Item	Relevant section of GL	Application of requirements to IUL products
	12	Para 4.2(f) of GL26	The requirements on disclosing, explaining and apprising the product features apply to IUL products, except that a product key facts statement is **not** required. For the avoidance of doubt, fees and charges should include cost of insurance ("COI") in case COI is charged for the protection offered by the policy.
	13	Para 4.2(g) of GL26	IFS is required for IUL products. A template of IFS and Applicant's Declaration for IUL products are enclosed in the Appendix to this Annex[10].
	14	Para 4.2(h) of GL26	No IUL product should be recommended to a customer unless and until all requisite information has been provided by the customer.
	15	Para 4.2(i) of GL26	If an IUL product has any unusual features (e.g. switching between indices, guaranteed rate etc.), licensed insurance intermediaries are required to take additional care when explaining these unusual features at the point of sale.
	Items 16 to 20 below apply in cases where an authorized insurer or licensed insurance intermediary chooses to conduct an FNA process to ascertain the information for the purpose of Item 10 above.		
	16	Para 10 of GL26	The requirement on certification of copies of FNA applies to IUL products.
	17	Para 6.4 to 6.11 of GL30	If an authorized insurer or licensed insurance intermediary chooses to adopt the FNA process required by GL26 in the sale of IUL products, the requirements in paras 6.4 to 6.11 of GL30 on handling of the FNA process (as well as all the requirements outlined in this Annex) should be followed.
	18	Para 6.12 of GL30	If the customer has indicated that he/she does not want to link his/her policy benefit to the performance of any market index (as may be offered by an IUL product), no IUL product should be introduced or recommended to the customer. If the customer has indicated that he/she has no experience or knowledge in investment, no IUL product should be recommended to the customer.
	19	Para 6.13 of GL30	When an IUL product is recommended to a customer, a participating policy that meets the customer's investment objective is **not** required to be provided to the customer as an option.

[10] The template is issued by the IA per para 7.3 of GL26.

Area	Item	Relevant section of GL	Application of requirements to IUL products
	20	Para 6.14 to 6.21 of GL30	The requirements on recommending a product following suitability assessment, the handling of mismatch cases, and the control, procedure and record keeping apply to IUL products.
Risk Profile Questionnaire ("RPQ") Process	21	Para 6 of GL26, para 9.2 of GL26, para 10 of GL26	Authorized insurers and licensed insurance intermediaries may opt out of the RPQ process when IUL products are offered only to PIs. However, they are still required to assess diligently during the sales process whether the risk return profile, characteristics and risk exposures of the recommended IUL products are suitable for the customer by taking into account the customer's circumstances (e.g. the customer's risk tolerance, investment knowledge and experience etc.). As general guidance, authorized insurers and licensed insurance intermediaries should not opt out of the RPQ process required by GL26 when dealing with vulnerable customers for IUL products, unless there are exceptional justifications for doing so.
IFS, Applicant's Declaration	22	Paras 7.1 to 7.3 of GL26	The Applicant's Declarations and Remuneration Disclosure requirements apply to the sale of IUL products, except that the product key facts statement and the investment choice brochure are **not** applicable to IUL products.
	23	Paras 7.4 to 7.6 and para 8 of GL26	The requirements on IFS and Application's Declaration apply to IUL products.
	24	Para 9.2 of GL26	The requirements on sending the customers copies of certain documents (i.e. the signed IFS, Applicant's Declarations and FNA (if applicable)) apply to IUL products.
Appropriate Remuneration Structure / Avoidance of Conflict of Interest	25	Paras 9.1 to 9.4 of GL15	The requirement on remuneration structure applies to IUL products. In addition, authorized insurers should prorate the commission for regular payment[11] IUL products to the licensed insurance intermediaries in such way that aligns the interests between policy holders and the licensed insurance intermediaries[12].

[11] This does not apply to single premium IUL policy that, after the issuance of the policy, further payment of premium is planned but flexible and the authorized insurer does not incentivize the policy holder to pay such premium. Refer to remark no.3 on circumstances that payment of premium is considered as incentivized by the authorized insurer.

[12] Refer to the example specified in para 5.4 of "*Note on the Green Light Process for Assessment of Investment-Linked Assurance Scheme ("ILAS") Products against Standards in Guideline on Underwriting Class C Business (GL15)*" in respect of how commission should be pro-rated.

Area	Item	Relevant section of GL	Application of requirements to IUL products
	26	Para 7.3 of GL26	The requirements on authorized insurers to follow and adopt the template issued by the IA from time to time in relation to the IFS and the Applicant's Declarations (including the disclosure of licensed insurance intermediaries' remuneration) apply to IUL products.
Post-sale Control	27	Para 4.2(k) of GL26, Paras 9.3 to 9.5 of GL26	The requirements on post-sales call or point-of-sale audio recording do not apply to IUL products, except for vulnerable customers (as defined under GL16) where authorized insurers are expected to conduct post-sales controls (e.g. post-sales call or point-of-sale audio recording).
	28	Para 9.6 of GL26	The requirement on licensed insurance intermediaries to remind their customers of the importance of the cooling-off period (and post-sales controls in the case of vulnerable customers) applies to IUL products.
Ongoing Monitoring	29	Paras 10.3 to 10.6 of GL16	The ongoing monitoring and communication requirements apply to IUL products.
	30	Para 4.1(b) in Appendix 1 of GL16	The requirement on disclosure during policy life (including but not limited to providing refreshed up-to-date illustration) applies to IUL products. For the avoidance of doubt, Item 32 applies to the refreshed up-to-date illustration. In addition, if there is any change to the Components or their underlying philosophy, the authorized insurer should inform the policy holders of the change as soon as practical, by writing to the policy holders or by disclosing it on the insurer's website. The insurer should provide the policy holders with the link to the relevant website at the point of sales.
Clients' Investments and Assets	31	Paras 11.1 to 11.2 of GL15	The investment of authorized insurers should reflect the policy holder's choice on allocation among accounts, if the IUL policy offers multiple accounts. Authorized insurer should also, in all material respects, adopt an investment strategy, derivative strategy or reinsurance strategy that delivers the crediting interest rate in accordance with the Mechanism and the performance of the relevant index(ies) of the Index Account or of the IUL policy as a whole, if the policy does not offer multiple accounts.

Area	Item	Relevant section of GL	Application of requirements to IUL products
			Details of the investment strategy, derivative strategy and reinsurance strategy should be made available to the IA upon request. Authorized insurers should determine the non-unit reserve of the IUL insurance business in accordance with Insurance (Valuation and Capital) Rules (Cap 41R). For the purpose of rule 15(4) of such Rules, unit reserve of IUL insurance business is zero. Authorized insurers are also reminded to strictly observe the requirements under sections 21B, 22 and 23 of the IO regarding segregation and application of assets for IUL insurance business, taking into account that IUL products belong to Class C (linked long term) business.
Specific Requirements for Benefit Illustration Documents	32	Appendix I of GL28	The "*specific requirements for benefit illustration documents of ILAS policies*" apply to IUL policies, except that the scenarios of net annual rate of return of 0%, 3%, 6% and 9% should be replaced by two scenarios of crediting interest rate: Scenario 1: A crediting interest rate that is equal to or not higher than the existing floor[13] of or minimum crediting interest rate, and Scenario 2: A crediting interest rate that is equal to or not higher than the existing cap of or maximum crediting interest rate, or if such rate is not specified by the policy, a rate that is equal to or not higher than 9% p.a.. It would be questionable whether the benefit illustration is adequate and clear in substance, if there is a massive gap between the crediting interest rates adopted in the scenarios available in the benefit illustration. As such, additional scenario(s) of crediting interest rate can be shown provided that:

[13] In case an IUL policy offers multiple accounts with multiple floors, minimums, caps or maximums, the relevant authorized insurer may refer to the weighted average of such amount calculated by reference to the choice of allocation percentages among different accounts. Account that does not link to any index should also be taken into consideration if there is a significant allocation to such account in the policy. The allocation among accounts should be clearly disclosed in the benefit illustration document.

An illustrative example on how weighted average is calculated is shown below, assuming:

- 50% allocation on account A with crediting interest rate of 8%, and
- 50% allocation on account B with crediting interest rate of 9%

On the merit of simplicity, the weighted average is 8.5% based on the assumption of constant allocation.

Area	Item	Relevant section of GL	Application of requirements to IUL products
			i) The crediting interest rate is not lower than that of scenario 1 and is not higher than that of scenario 2, and ii) The crediting interest rate should **not** be interpreted as "current assumed basis" that is based on the authorized insurer's best estimate, and the authorized insurer or the licensed insurance intermediaries should **not** mislead the customer that the crediting interest rate represents a projection or estimation of the future returns. For the avoidance of doubt: i) The numerical illustration should take into account the fees and charges imposed by the authorized insurer, and they must not be lower than the current scale of fees and charges, and ii) Authorized insurer should ensure that the wordings and terminologies are accurate and reflect the nature of the IUL products.
Supplementary Illustration	33	Section 6 of GL28	The requirement on supplementary illustration applies to IUL products.
Green light process and submission requirement	34	Supplementary note of GL15	For the avoidance of doubt, other than the example on how commission should be pro-rated for the purpose of Item 25, the requirements specified in the "*Note on the Green Light Process for Assessment of Investment-Linked Assurance Scheme ("ILAS") Products against Standards in Guideline on Underwriting Class C Business (GL15)*", including the requirement to submit product documents to the IA, do **not** apply to IUL products.