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PRACTICE NOTE ON THE DISCLOSURE OF REMUNERATION BY FINANCIAL ADVISERS

Purpose

This Practice Note is issued pursuant to section 64 of the Financial Advisers Act (Cap.110) ["the Act"]. It provides guidance to financial advisers on their obligations under paragraphs 16 to 22 of the FAA Notice No: FAA-N03 [the "Notice"] on "Information to Clients and Product Information Disclosure" to disclose the remuneration that they receive or will receive for making any recommendations in respect of an investment product, or executing a purchase or sale contract relating to a designated investment product on their clients' behalf.

Definitions

2 For the purposes of this Practice Note:

"financial adviser" means a licensed financial adviser or a person exempt from holding a financial adviser's licence under section 23(1)(a) to (e) of the Act.

"investment product" has the same meaning as in section 2(1) of the Act, which is:
(a) any capital markets product as defined in section 2(1) of the Securities and Futures Act 2001 (Cap. 289);
(b) any life policy as defined in the First Schedule to the Insurance Act (Cap. 142); or
(c) any other product as may be prescribed by regulations made under the Act.

"designated investment product" has the same meaning as in section 25(6) of the Act, which is:
(a) any unit in a collective investment scheme;

(b) any life policy (including a group life policy); or
(c) any other investment product as the Authority may prescribe.

What obligation does a financial adviser have under the remuneration disclosure requirement?

3 All financial advisers, unless exempted, are required to comply with the remuneration disclosure requirement in paragraphs 16 to 22 of FAA-N03. Under the Notice requirements, a financial adviser must disclose, in writing, to a client all remuneration, including any commission, fee and other benefits, that it has received or will receive that is directly related to –

(a) the making of any recommendation in respect of an investment product to the client; or
(b) executing a purchase or sale contract relating to a designated investment product on the client's behalf.

4 When making recommendations and/or executing purchase or sale contracts relating to **life policies**, a financial adviser is only required to disclose to a client the "distribution cost" item in the benefit illustration. The financial adviser need not disclose the remuneration it receives or will receive for making the recommendation or sale. However, in the case of a life policy where a benefit illustration is not available, for example a group term life policy, the financial adviser is required to abide by the remuneration disclosure rule set out in paragraph 3.

5 The purpose of requiring remuneration disclosure is to enable consumers to be aware of the costs of the financial advisory services rendered, and for them to be better able to make informed decisions.

6 MAS notes that equivalent disclosure requirements are also applicable to financial advisers in overseas jurisdictions such as Australia, the US and the UK.

What does remuneration include?

7 Remuneration **that has to be disclosed** includes all fees, commissions and other benefits such as trailer fees, soft dollars, sales bonuses that a financial adviser receives or will receive for making any recommendation in respect of an investment product or executing a purchase or sale contract for any designated investment product on a client's behalf. The financial adviser needs only disclose the remuneration it receives or will receive arising directly or in connection with the making of the recommendation or the execution of the purchase or sale contract.

8 A financial adviser is not required to disclose any remuneration received or to be received by it for any other services it provides that are unrelated to its financial advisory activity. For example, profit mark-ups attributed to the financial adviser in its role as a product manufacturer need not be disclosed to a client when it recommends the product to the client or purchases/sells the product on the client's behalf.

When must a financial adviser disclose its remuneration?

9 The disclosure must be made to a client in writing, whether electronically or otherwise, at the time of making a recommendation in respect of any investment product or prior to the execution of a purchase or sale of any designated investment product.

10 For telesales or advice/deals concluded over the telephone, a financial adviser may orally disclose to a client the amount of remuneration the financial adviser will receive for the advice given or sale made. In these circumstances, the financial adviser should give written confirmation as soon as possible, but no later than three business days, after the date of the transaction.

How should remuneration be disclosed?

11 Remuneration disclosure should be worded and presented in a clear and concise manner. A financial adviser should use plain language and avoid the use of industry or legal jargon, where possible. If this is not possible, it should clearly explain the meanings of any technical or legal terms used. In addition, it should consider providing simple examples to help illustrate or explain more complex information. This is to ensure that clients are able to understand the information presented and use it to make informed choices.

12 For easy understanding by clients, a financial adviser should itemise and disclose each category of remuneration in actual amounts where possible, or otherwise as a percentage. Where remuneration is determined as a percentage, the financial adviser should disclose clearly the percentage and the base figure to which the percentage will apply, for example, x% of the total amount invested. This is to enable a client to compute the actual amount of remuneration that will be received by the financial adviser.

13 Where a financial adviser is unable to ascertain accurately the actual amount for each type of remuneration at the time of making a recommendation or prior to executing a purchase or sale, it should, for items that are quantifiable, set out the actual amount of each remuneration item. For those items that are not quantifiable, the financial adviser should furnish the client with a description of how each item will be computed, or provide a range of amounts or rate of remuneration for each item.

14 As a matter of good practice, MAS encourages a financial adviser that is unable to disclose the actual amount of remuneration at the time of making a recommendation or executing a purchase or sale contract to provide this information to a client when it is available. This could be done through various means, including notifying the client through e-mails, letters, periodic statements or other client communications.

15 As a guide, a financial adviser may wish to consider the following sample wording when preparing its written statement of remuneration.

a) For fee-only services provided:

(At time of engagement) “For the financial advisory services we provide to you, we will charge you a fee of $3,800. If you decide to purchase the recommended investment product(s) through us, the commissions paid to us by the product providers or fund managers will be refunded to you, as soon as practicable, after deducting administrative and bank charges.”

(After the transaction) “For the unit trust you purchased through us, we have received commissions of $450 from ABC Fund Manager. After deducting administrative and bank charges of $30, the net amount to be refunded to you is $420. We will credit the refund to your bank account on xx xxx 2004.”

b) For fee-based services provided:

(At time of engagement) “For the financial advisory services we provide to you, we will charge you a nominal fee of $300. If you choose not to purchase the recommended investment product(s) through us, you will have to pay us this nominal fee in full.

If you purchase the recommended unit trust through us, we will receive a commission equal to 90% of the sales charge imposed by the fund manager. The sales charge is 5% of the total amount invested. If the commission we receive is more than the nominal fee, we will waive the fee. For example, if you invest $10,000, the sales charge would be $500 and we will receive a commission of $450 ie. 90% of $500 from ABC Fund Manager. In this case, as the commission exceeds the nominal fee, we will waive the $300 fee payable by you.

In the event that you decide to purchase the recommended unit trust through us and the commission received by us is of an amount lower than the nominal fee, you will be charged a fee equal to the difference between the nominal fee and the commission received by us. For example, if you invest $5,000 and the sales charge is 5% of total amount invested ie $250, we will receive a commission of $225, being 90% of $250, from ABC Fund Manager. In this case, we will charge you a fee of $75, being the difference between the nominal fee ($300) and the commission we received ($225).”

c) For commission services provided:

“If you purchase the recommended investment product, we will receive a commission equal to 90% of the sales charge from the product provider. The sales charge is 5% of the total amount invested. For example, if you invest $10,000, the sales charge will be $500 and we will receive a commission of $450, being 90% of the sales charge of $500.”

“If you purchase the recommended fund, we will receive from the fund manager a commission of $100 plus 3% of the total amount invested. This means that if you invest $10,000, we will receive a commission of $400. In addition, we will receive trailer fees from the fund manager. The trailer fees are based on the total amount of assets managed by the fund manager for our clients under the fund at year-end as follows:

Total Assets under Management	Trailer Fees (% per annum)
$500,000 - $1m	40% of annual management fees
> $1m - $2m	50% of annual management fees
>$2m	60% of annual management fees.”

“For the placement of the term life insurance under your company’s employee benefits programme, we will receive a commission of 10% of gross life insurance premiums from the insurer. For example, if the gross life insurance premiums amount to $50,000, we will receive a commission of $5,000 from the insurer.”

16 A financial adviser may prefer to disclose its remuneration for the different funds it distributes in a table format. A sample example is presented below:

Table 1: Remuneration Structure of ABC Financial Adviser [“ABC”] for the Distribution of Unit Trusts

Name of Fund	**Sales Charge (% of total amount invested)**	**Commissions received by ABC (% of Sales Charge)**	**Other Benefits**	
			Trailer Fees (% per annum of Assets under Management[1] [“AUM”])	**Others**
Fund A	5%	90%	0.25%	-
Fund B	4%	95%	AUM of $25 million and below – 0.25% AUM of more than $25 million to $50 million – 0.35% AUM of more than $50 million – 0.50%	-
Fund C	5%	90%	0.40%	
Fund D	4.5%	100%	-	50% of net total fixed annual recurrent fees[2]

[1] Calculated on monthly basis against monthly net asset values of products subscribed (net of redemptions) ie total net asset value of sales introduced (net of redemptions) x trailer commission % x 1/12.

[2] Includes management fees, maintenance fees, shareholder service fees and distribution fees.