



BANK NEGARA MALAYSIA
CENTRAL BANK OF MALAYSIA

Life Insurance and Family Takaful Framework

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PART A OVERVIEW

1. Introduction

- 1.1. On 7 November 2013, Bank Negara Malaysia (the Bank) published a concept paper on the Life Insurance and Family Takaful Framework (Framework) that sets out planned reforms to support the long-term development of the life insurance and family takaful industry. The Bank has received numerous responses and feedback gathered during a two-month public consultation period. These have been carefully considered and deliberated by the Bank to ensure that the interests of industry stakeholders and consumers are well-balanced and safeguarded.
- 1.2. The Framework aims to promote innovation and a more competitive market supported by higher levels of professionalism and transparency in the provision of insurance and takaful products and services. This will be achieved through specific initiatives introduced under the Framework, which can be broadly summarised under three main pillars as follows:
- a) **gradual removal of limits on operational costs to promote product innovation while preserving policy/certificate value**
Life insurers/family takaful operators will be given greater flexibility to manage their operating expenses, commensurate with their business strategy. However, consumers' interests will remain protected through appropriate safeguards that will preserve their policy/certificate value;
 - b) **diversified distribution channels to widen outreach**
Life insurance/family takaful products will be accessible to consumers through a wider range of delivery channels that are most convenient and appropriate. Diversified distribution channels can also contribute towards lowering the cost of life insurance/family takaful products by promoting consumer choice and competition in the market; and

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c) strengthened market conduct to enhance consumer protection

The level of professionalism of intermediaries will be enhanced to ensure consumers are given proper advice. At the same time, initiatives to facilitate informed decision making by consumers will be further pursued by strengthening product disclosure standards with greater transparency and clarity in order for consumers to better understand product features. This will be complemented by mechanisms introduced to facilitate meaningful and effective product comparisons.

- 1.3 Collectively, the initiatives under the Framework are expected to spur the innovation of a wider range of both products and delivery channels to suit diverse consumer needs based on individual risk appetites, financial goals and levels of financial capability. This in turn will contribute towards the broader objective of reducing the protection gap in Malaysia in line with efforts to increase the penetration rate to 75 percent¹ by year 2020 (2014: 55.5%)².

Implementation approach and timeline

- 1.4 In advancing the initiatives under the Framework, a phased approach will be adopted to take into account the current state of readiness of the life insurers, family takaful operators and intermediaries, and the level of consumer awareness and literacy. The implementation and sequencing of initiatives reflect the Bank's engagement with the industry on the time needed for individual institutions to align business strategies and operational frameworks with the aims of the Framework. Details on the implementation timeline of each initiative under the Framework are provided in the Appendix.
- 1.5 The Bank will issue standards, requirements and/or guidance under the Financial Services Act 2013 (FSA) and Islamic Financial Services Act 2013 (IFSA) to give effect to each initiative over the course of the Framework's development plan, beginning 1 December 2015.

¹ Based on the target set under the Economic Transformation Programme's "Entry Point Project 5: Insuring Most, If Not All, of Our Population".

² The penetration rate is the ratio of number of policies and certificates in force to the total population.

PART B INITIATIVES UNDER THE FRAMEWORK

2. Pillar One: Gradual removal of limits on operating costs

2.1 The operating cost control (OCC) limits that are currently applied to management expenses, commissions and agency related expenses (ARE) will be reviewed in stages to be gradually removed under the initiatives of Pillar One.

Limits on management expenses

2.2 The first set of OCC limits to be removed will be those on management expenses presently set out in the Guidelines to Control Operating Costs of Life Insurance Business³ issued on 10 August 2007 and Guidelines on Operating Costs of Family Takaful Business⁴ issued on 12 July 2007 (OCC Guidelines). This will provide life insurers/family takaful operators with greater operational flexibility in managing their operating expenses in line with their respective business and competitive strategies, while encouraging further product innovation. The limits will be disapplied with effect from 1 December 2015.

Limits for investment-linked insurance/takaful products

2.3 The maximum limits⁵ currently applied to the amount of commissions and ARE payable on investment-linked policies/takaful certificates to the agency force and other intermediaries will also be removed. These limits will be disapplied with effect from 1 January 2019.

2.4 Concurrent with the withdrawal of these OCC limits a Minimum Allocation Rate (MAR), which specifies the minimum proportion of premium/contribution payable by the policy owner/takaful participant that will need to be retained in the unit fund(s) of choice before deduction of any charges, will be introduced. The MAR is to complement the existing Sums Assured Multiple (SAM) rule.

³ Paragraph 8 under Part IV of the Guidelines to Control Operating Costs of Life Insurance Business issued on 10 August 2007.

⁴ Paragraph 20 under Part V(c) of the Guidelines on Operating Costs of Family Takaful Business issued on 12 July 2007.

⁵ Paragraphs 18 and 19 of the Guidelines on Investment-Linked Insurance/Takaful Business issued on 20 July 2011.

This safeguard is to ensure that the policy owner/takaful participant's unit fund(s) will be preserved.

- 2.5 Hence, with effect from 1 January 2019, for annual premium/contribution investment-linked policies/takaful certificates of a term greater than 20 years, life insurers/family takaful operators will be required to comply with the MAR as follows:

Policy/Certificate Year	MAR
	Annual Premium/Contribution
1 – 3	60%
4 – 6	80%
7 – 10	95%
11 onwards	100%

The MAR for investment-linked policies/takaful certificates with single premium/contribution and annual premium/contribution which have a term less than 20 years will be specified in amendments to the Guidelines on Investment-Linked Insurance/Takaful Business when issued in due course.

- 2.6 The removal of the OCC limits combined with the application of the MAR will have an effect on the operating environment of the life insurance and family takaful industry, particularly for investment-linked insurance/family takaful business. The phasing of this initiative is intended to allow life insurers/family takaful operators sufficient lead time to adapt to the new environment and to manage the ongoing transition arising from other existing regulatory initiatives, including the structural adjustments involved for those insurers/takaful operators converting from composite business to a single business.

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Limits for ordinary life insurance/family takaful⁶ and annuity products

- 2.7 For ordinary life insurance/family takaful and annuity products, the existing maximum limits on the amount of commissions and ARE payable set out in the OCC Guidelines will be gradually removed by product types beginning in 2017.
- 2.8 The existing limits imposed on commissions payable to all intermediaries will first be removed for all pure protection products related to term, critical illness and medical and health insurance/takaful. This will be conditional on all life insurers/family takaful operators offering the products commission-free through direct channels as described in paragraph 3.5 of this document.

Limits under Agency Financing Schemes

- 2.9 Consistent with the gradual removal of limits applied to yearly commissions and ARE, the existing limits on Agency Financing Schemes (AFS)⁷ as set out in the Policy Document on Granting of Credit Facilities issued on 28 June 2013, will be removed with effect from 1 December 2015.
- 2.10 Any credit facility granted by a life insurer/family takaful operator to its insurance/takaful agent shall continue to be provided only from the life insurer's/family takaful operator's shareholders' fund⁸ and the relevant capital requirements⁹ on credit facilities in the Risk-Based Capital Framework/Risk Based Capital Framework for Takaful Operators, as the case may be, will also continue to apply.

⁶ Ordinary life insurance/family takaful products include individual/group products, and all supplementary contracts/certificates or riders attached to basic life policies/takaful certificates, but exclude investment-linked and annuity products.

⁷ Appendix II of the Policy Document on Granting Credit Facilities issued on 28 June 2013. Several other requirements in paragraphs 8 and 9, and the same appendix of the above policy document will also be removed or modified at the same time.

⁸ Paragraph 8.1 of the Policy Document on Granting of Credit Facilities issued on 28 June 2013.

⁹ Appendix I of the Risk-Based Capital Framework for Insurers and Risk-Based Capital Framework for Takaful Operators issued on 20 June 2013 and 26 June 2013 respectively.

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3. Pillar Two: Diversification of distribution channels

3.1 Through initiatives aimed at diversifying distribution channels, it is envisioned under the Framework that by 2020, the market share of regular premium/contribution products sold/marketed via non-agency channels should exceed 30% with improved performance, for example, in the form of higher persistency for life insurance/family takaful products sold/marketed. For distribution channels such as bancassurance/bancatakaful, the expectations under this Framework are for the life insurance and family takaful industry to achieve a penetration target of 10% of the total banking population by 2020.

Limits for bancassurance/bancatakaful

3.2 The limits on commissions for annual premium/contribution life insurance/family takaful products (except for credit/financing-related products) sold/marketed via bancassurance/bancatakaful will be aligned with limits applicable to corporate agents with effect from 1 January 2017.

3.3 The above initiative accords life insurers/family takaful operators greater flexibility to structure incentive schemes that can better leverage bancassurance/bancatakaful arrangements in improving overall penetration. The improved incentive structures will be accompanied by the more effective implementation of non-sales based key performance indicators (KPIs) to foster behaviour that is consistent with the fair treatment of consumers.

Building presence of direct channels

3.4 All life insurers/family takaful operators will be required to offer commission-free standalone pure protection products namely term, critical illness and medical and health insurance/takaful through at least one direct channel. These non-intermediated channels are to be made widely accessible for consumers to purchase/participate in pure protection products directly from life insurers/family takaful operators, either at their head office and branch premises, or online through their websites.

3.5 Term products must be available through direct channels with effect from 1 January 2017, followed by critical illness and medical and health

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insurance/takaful products by 1 January 2018. The commission limits for these products offered through other distribution channels will correspondingly be removed once the respective products are available via direct channels. Further requirements that must be complied with by life insurers/family takaful operators in respect of these products will be specified by the Bank in 2016.

Enhance financial advisers framework

3.6 Financial advisers are intermediaries approved by the Bank to provide financial advice to the public on the range of insurance/takaful products offered by life insurers/ family takaful operators. To promote financial advisers as a viable distribution channel and to support insurance/takaful agents that wish to scale up and become financial advisers, several initiatives have already been implemented as follows:

- (a) the minimum paid-up capital unimpaired by losses for financial advisers was reduced from RM100,000 to RM50,000 with effect from 1 January 2015.
- (b) qualifying requirements to become a financial adviser's representative (FAR) have also been rationalised since 1 September 2014 to focus on the key knowledge areas¹⁰ which are relevant to advice on insurance/ takaful products, and to recognise equivalent qualifications from higher learning institutions recognised by the Malaysian Financial Planning Council and Financial Planning Association of Malaysia.

3.7 To support the ability of financial advisers to professionally, independently and competently advice consumers on a wide range of life insurance/family takaful products available in the market, life insurers/family takaful operators will be required to provide financial advisers access to the full range of life insurance/family takaful products offered by them.

¹⁰ The key knowledge areas cover (i) foundation in financial planning; (ii) risk management; (iii) insurance planning; and (iv) investment planning.

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Introduction of online product aggregator

3.8 To help consumers compare suitable life insurance/family takaful products, online product aggregators, which are websites that will generate a comparison of products offered by different life insurers/family takaful operators, will be established. The requirements relating to the establishment and operations of the product aggregators will be specified by the Bank in 2016.

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4. Pillar Three: Strengthening market practices

4.1 Various market conduct practices will be strengthened to elevate the level of professionalism in the life insurance and family takaful industry. These enhanced practices are important preconditions for the removal of the OCC limits for life insurance/family takaful products to ensure that the interests of consumers continue to be adequately safeguarded.

Implementation of balanced scorecard for intermediaries

4.2 The remuneration policy for all insurance/takaful intermediaries will be enhanced through the introduction of the balanced scorecard (BSC) to foster behaviour that is consistent with fair treatment of consumers.

4.3 The implementation of the BSC aims to achieve the following key outcomes:

- (a) suitability of advice and recommendations based on a consumer's financial needs and circumstances;
- (b) continuous servicing of life policies/family takaful certificates throughout their terms; and
- (c) continuous professional development of intermediaries and maintaining a strong focus on ethical and professional conduct in the sale/marketing of life insurance/family takaful products by insurance/takaful intermediaries.

4.4 The BSC will capture non-sales KPIs as a basis for remunerating intermediaries, with adequate weightage given to such KPIs to foster behaviour supportive of the above outcomes. The remuneration policy should address any inherent product bias which can increase mis-selling risks.

4.5 As the primary role of intermediaries is to provide consumers with quality advice and suitable recommendations, the proportion of their remuneration subject to the BSC should reflect this primary role.

4.6 To allow insurance/takaful agents to adjust to the new framework as well as to monitor the impact of the BSC on the industry, life insurers/family takaful operators are required to introduce the BSC on a pilot basis (with no impact

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on the agents' commission) in the second half of 2016 prior to actual implementation in 2018.

- 4.7 For insurance/takaful agents whose performance exceeds the minimum requirements for non-sales KPIs, life insurers/family takaful operators will be able to increase the commission payable accordingly. For life insurance/family takaful products that are still subject to existing commission limits, the higher commission payable will need to be paid by the life insurers/family takaful operators from their shareholders' fund.

Enhance product disclosures in sales illustrations

- 4.8 To facilitate consumers' understanding and ability to evaluate the different types of insurance/takaful products, life insurers/ family takaful operators will be required to provide sales/marketing illustrations to all prospective policy owners/takaful participants at the point of sale/marketing to assist them in making informed decisions.
- 4.9 Improvements to the sales/marketing illustrations for participating life policies and family takaful products will be introduced from 1 January 2017. This will include the following features:
- (a) a summary page that contains key elements of the product as well as a comparison with a term plan for the same coverage period and guaranteed death benefit amount. Where the life insurer/family takaful operator does not have a term plan which matches the duration of the policy/certificate, the term plan with the closest duration will need to be indicated with the appropriate explanation;
 - (b) a sales/marketing illustration table that will provide a detailed year-to-year illustration of benefits, namely survival, death and maturity benefits and surrender value; and
 - (c) in the case of a participating life policy, a segment on important information regarding the policy that provides an explanation on the different types of bonuses payable under the policy and how these bonuses are determined.

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The format for participating life insurance policies have been specified in the Policy Document on Management of Participating Life Business. For family takaful products, the format and other details will be specified by the Bank in 2015.

Availability of online account facilities

4.10 Similar to the concept of an online banking account, life insurers/family takaful operators will be required to provide online access to insurance and takaful accounts for their policy owners/takaful participants with effect from 1 July 2016.

4.11 This will allow policy owners/takaful participants easy access to information on the status of their policies/certificates, obtain real-time updates to policy/certificate details and to download forms for transactions. The life insurance and family takaful industry will also benefit from opportunities to leverage on electronic documentation and information updates to improve data management and enhance quality of services provided to consumers.

Introduction of service guide for consumers

4.12 A service guide to enhance consumer awareness of financial advisory services for insurance and takaful products will be introduced from 1 July 2016. The guide aims to increase the transparency of services provided by intermediaries and allows consumers to be aware of, and anticipate the level of service when purchasing insurance/takaful products.

4.13 While the insurance and takaful industry associations have agreed to come together to develop the content for the service guide, life insurers/family takaful operators will be free to individualise their own service guide to differentiate themselves from their competitors.

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5. Submission of business strategy and plan

5.1 In order to ensure effective implementation of the initiatives under the Framework, each life insurer/family takaful operator will need to carefully review its overall business plan and projections over the next five years (2016-2020) and inform the Bank by 30 June 2016 of key changes in respect of product and distribution strategies, operational frameworks and risk management priorities arising from the transition to the new environment. The Bank will provide further details on reporting by individual life insurers/family takaful operators and conduct industry engagements for this purpose.

6. Conditions for further liberalisation

6.1 The Bank will assess the performance of the industry and impact of initiatives implemented over the course of the period to inform the industry on strategies for progressing to the next phase of development.

APPENDIX