

Topic 4
Topic 2
Topic 3
Topic 1
Topic 5

Topic1
p15, p21

Topic4
p15, p21

CONSULTATION PAPER

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Public Consultation on Revisions to Misconduct Reporting Requirements and Proposals to Mandate Reference Checks for Representatives

MAS

Monetary Authority of Singapore

Contents

1	Preface	3
2	Introduction	6
3	Part A: Proposed changes to misconduct reporting requirements	7
	Proposal 1: Scope to include Registered Fund Management Companies	7
	Proposal 2: Revisions to the categories of reportable misconduct	8
	Proposal 3: FIs to update MAS on the outcome of police investigations	14
	Proposal 4: FIs to notify representatives when they are under investigation and provide them with a copy of the misconduct report filed with MAS	14
	Proposal 5: Enhanced standards for FIs' investigation processes and requirement for FIs to submit investigation reports to MAS in a prescribed format	16
4	Part B: Proposed requirements relating to reference checks	17
	Proposal 6: FIs to conduct reference checks on prospective representatives and to share information on their representatives in response to reference check requests	17
	Annex A: List of questions	21

1 Preface

1.1 As set out in the Guidelines on Fit and Proper Criteria, a relevant person carrying out any activity regulated by Monetary Authority of Singapore (“MAS”) is expected to be fit and proper. This means being competent and honest, having integrity, and being financially sound. This provides MAS, the financial industry, and consumers with the assurance that participants in the financial industry conduct regulated activities efficiently, honestly, fairly, and act in the best interests of their customers. To this end, financial institutions (“FIs”) are currently required under the Securities and Futures Act (“SFA”), Financial Advisers Act (“FAA”), and Insurance Act (“IA”) to lodge a report with MAS when they become aware of any misconduct committed by their representatives or broking staff (henceforth collectively referred to as “representatives”¹), such as acts involving fraud, dishonesty, inappropriate advice, misrepresentation, or inadequate disclosure of information to customers. FIs are also expected to have in place a robust and transparent process to investigate possible wrongdoings by their representatives, and take appropriate disciplinary actions against their representatives for any misconduct committed.

1.2 Misconduct reports lodged with MAS serve as an important source of information that informs our regulatory and supervisory work. However, in the course of MAS’ review of these misconduct reports, we have observed differing practices and standards in the information submitted. There were instances where MAS had to engage FIs to re-classify misconduct under the appropriate categories. As such, MAS is consulting on proposed changes to the misconduct reporting requirements, to provide greater clarity on our requirements and reduce errors in the submission of misconduct reports.

1.3 MAS expects FIs to put in place a fair and transparent process when investigating and reporting misconduct committed by their representatives. In this regard, MAS is proposing to require FIs to provide their representatives with a copy of the misconduct reports lodged with MAS. This will also allow these representatives to provide full disclosure of their past misconduct when they apply to join another FI.

1.4 In addition, to enhance the standard of investigations conducted by FIs on misconduct committed by their representatives, MAS proposes to provide greater clarity

¹ References to “representatives” in this consultation paper refer to both existing and former representatives.

on the rigour and quality of investigations expected, and to require FIs to submit their investigation reports in a prescribed format set by MAS.

1.5 MAS expects all FIs to ensure that the persons they employ or appoint to conduct regulated activities on their behalf are fit and proper. Through the Circular on Due Diligence Checks and Documentations in respect of the Appointment of Appointed, Provisional and Temporary Representatives, MAS has set out the expectation for FIs to conduct due diligence checks on prospective representatives, such as reference checks with their former employers or principal companies (henceforth collectively referred to as “principal companies”). MAS has, however, observed that the types of information requested and level of details provided in these reference checks vary from FI to FI. MAS is therefore proposing to standardise industry practices by mandating FIs to carry out and **respond** to reference check requests on representatives, as well as setting out the mandatory information that must be provided in a reference.

1.6 The proposed reference check requirement set out in this consultation paper will only apply to representatives of FIs. Given that employees who are not representatives may also commit various forms of misconduct, MAS is considering extending this reference check requirement to a broader segment of the financial industry beyond representatives. MAS will conduct a separate public consultation on this proposal in due course.

1.7 MAS invites interested parties to submit their views and comments on the proposals in this consultation paper.

Please note that all submissions received will be published and attributed to the respective respondents unless they expressly request MAS not to do so. Respondents who would like (i) their whole submission or part of it, or (ii) their identity, or (iii) both, to be kept confidential, must expressly state so in the submission to MAS. In addition, MAS reserves the right not to publish any submission received where MAS considers it not in the public interest to do so, such as where the submission appears to be libellous or offensive.

1.8 Please submit your views and comments by 6 August 2018 to:

Capital Markets Intermediaries Department I
(Attention: Misconduct **Reporting** Working Group)
Monetary Authority of Singapore
10 Shenton Way
MAS Building
Singapore 079117

Email: MisconductReview@mas.gov.sg

1.9 Electronic submission is encouraged. Please use the prescribed format for your submission.

2 Introduction

2.1 This consultation paper is divided into two parts.

- (a) Part A of the consultation paper proposes revisions to the scope of entities and the requirements on **reporting** of misconduct by representatives, as set out in the respective Notices² issued under the SFA, FAA, and IA (collectively referred to as “Misconduct Notices”). This section also discusses MAS’ proposals to enhance FI’s investigation processes.
- (b) Part B of the consultation paper sets out the proposed requirements for FIs to conduct and **respond** to reference checks on representatives.

² These Notices are (a) Notice on **Reporting** of Misconduct of Representatives by Holders of Capital Markets Services Licence and Exempt Financial Institutions (Notice SFA 04-N11); (b) Notice on **Reporting** of Misconduct of Representatives by Financial Advisers (Notice FAA-N14); and (c) Notice on **Reporting** of Misconduct of Broking Staff by Insurance Brokers (Notice MAS 504).

3 Part A: Proposed changes to misconduct reporting requirements

Proposal 1: Scope to include Registered Fund Management Companies

3.1 The current Misconduct Notices are applicable to the following FIs:

- (a) Capital Markets Services licence holders under the SFA;
- (b) Licensed financial advisers under the FAA;
- (c) Registered insurance brokers under the IA; and
- (d) Exempt FIs (banks, merchant banks, insurance companies and finance companies)³ conducting regulated activities under the SFA, FAA, and IA (in relation to insurance broking activities).

3.2 The misconduct reporting requirements currently do not apply to Registered Fund Management Companies (“RFMCs”). Nonetheless, RFMCs are already required to satisfy MAS that their shareholders, directors and representatives, as well as the RFMC itself, are fit and proper, in accordance with the Guidelines on Fit and Proper Criteria issued by MAS and pursuant to regulation 14A(2)(b)⁴ of the Securities and Futures (Licensing and Conduct of Business) Regulations (“SF(LCB)R”). Where there are issues that may impinge on the fitness and propriety of the RFMC, its shareholders, directors and/or representatives, including any misconduct or pending investigation of possible misconduct by its representatives, the RFMC is currently required to submit Form 23A⁵ to inform MAS and provide the relevant supporting documents.

3.3 For greater consistency in the handling and reporting of misconduct committed by representatives, and measures to satisfy FIs of the fitness and propriety of potential representative hires, MAS proposes to apply the misconduct reporting requirements to RFMCs. In this regard, RFMCs will be required to comply with the Misconduct Notice

³ These FIs are exempted from the licensing requirement under section 99(1)(a) to (d) of the SFA, section 23(1) to (e) of the FAA, and section 35ZN of the IA.

⁴ Pursuant to regulation 14A(2)(b) of the SF(LCB)R, any person (including its directors, shareholders and representatives) exempt under paragraph 5(1)(i) of the Second Schedule to the Regulations are required to be fit and proper.

⁵ Paragraph 5(7)(a) of the Second Schedule to the SF(LCB)R states that an RFMC shall lodge with the MAS a notice of change of particulars in Form 23A providing any change in the particulars in the notice lodged under sub-paragraph (7), not later than 14 days after the date of the change.

issued under the SFA, the proposed changes to the misconduct reporting requirements (i.e. Proposals 2 to 5) and the proposed reference check requirement (i.e. Proposal 6) set out in this consultation.

Question 1. MAS seeks comments on the proposal to apply the requirements on reporting of misconduct by representatives and reference checks to RFMCs.

Proposal 2: Revisions to the categories of reportable misconduct

3.4 Under the Misconduct Notices, FIs are required to lodge a report with MAS no later than 14 days after the discovery of a representative's misconduct.⁶ FIs are also required to provide subsequent updates on the outcome of their investigations and disciplinary actions meted out. Where there is no reportable misconduct in the calendar year, FIs must submit an annual nil declaration. The list of reportable misconduct is listed in Table 1.

Table 1: List of reportable misconduct

	Relevant Acts	Categories of Misconduct
(i)	SFA, FAA, IA	Acts involving fraud, dishonesty or other offences of a similar nature (e.g. cheating, fraud, forgery, misappropriation of monies or criminal breach of trust)
(ii)	SFA	Acts relating to market conduct provisions under Part XII of the SFA (e.g. prohibited conduct or insider trading as set out in Part XII of the SFA)

⁶ Where any misconduct is identified through mystery shopping exercises, the misconduct is required to be reported to MAS. This is aligned with the requirements under the Notice on Requirements for the Remuneration Framework for Representatives and Supervisors ("Balanced Scorecard Framework") and Independent Sales Audit Unit (FAA-N20), where financial advisers are required to factor the findings from mystery shopping exercises into the representatives' performance under the Balanced Scorecard Framework.

	Relevant Acts	Categories of Misconduct
(iii)	FAA	Acts involving inappropriate advice, misrepresentation, or inadequate disclosure of information
(iv)	IA	Acts involving failure to exercise due care and diligence, misrepresentation, or inadequate disclosure of information
(v)	SFA, FAA, IA	Failure to satisfy the Guidelines on Fit and Proper Criteria
(vi)	SFA, FAA, IA	Any type of misconduct other than those set out in (i) to (v), resulting in – <ul style="list-style-type: none">• a non-compliance with any regulatory requirement relating to the provision of any regulated activity; or• a serious breach of the FI's internal policy or code of conduct which would render the representative liable to demotion, suspension or termination of the representative's employment or arrangement with the FI.

3.5 MAS proposes to revise the categories of misconduct set out in Table 1, to provide greater clarity on the intended types of misconduct that should be reported to MAS and to reduce overlap between the different categories of misconduct. Table 2 sets out the proposed revisions to the categorisation of misconduct to be reported to MAS.

Table 2: Revised categorisation of reportable misconduct

	Relevant Acts	Current Categories of Misconduct (as set out in Table 1)	Proposed Revisions to Categories of Misconduct (revisions made in bold)	Comments
(i)	SFA, FAA, IA	Acts involving fraud, dishonesty or other offences of a similar nature (e.g. cheating, fraud, forgery, misappropriation of monies or criminal breach of trust)	No change	-
(ii)	SFA	Acts relating to market conduct provisions under Part XII of the SFA (e.g. prohibited conduct or insider trading as set out in Part XII of the SFA)	Acts relating to market conduct provisions under Part XII of the SFA (e.g. insider trading or other prohibited conduct as set out in Part XII of the SFA, such as securities market manipulation and financial benchmarks manipulation).	The proposed revisions provide greater clarity on the intended acts that should be reported to MAS under this category. They are aligned with the expansion of market conduct provisions under Part XII of the SFA to specifically prohibit the manipulation of any financial benchmark. This expansion is set out in the Securities and Futures (Amendment) Bill 2017.

	Relevant Acts	Current Categories of Misconduct (as set out in Table 1)	Proposed Revisions to Categories of Misconduct (revisions made in bold)	Comments
(iii)	FAA	Acts involving inappropriate advice, misrepresentation, or inadequate disclosure of information	Acts involving inappropriate advice or recommendation , misrepresentation, gross negligence , or inadequate disclosure of information which have material adverse impact on the interests of the client or impinges on the fitness and propriety of the representative	The proposed revisions provide greater clarity on the intended acts that should be reported to MAS under this category. They are consistent with the classification of Category 1 infractions under the Balanced Scorecard framework.
(iv)	IA	Acts involving failure to exercise due care and diligence, misrepresentation, or inadequate disclosure of information	No change	-
(v)	SFA, FAA, IA	Failure to satisfy the Guidelines on Fit and Proper Criteria	Removed	Given that the misconduct in the current Categories (i) to (iv) would impinge on the fitness and propriety of representatives, there is overlap in Category (v) and the other categories. For instance, an offence involving criminal breach of
(vi)	SFA, FAA, IA	Any type of misconduct other than those set out in (i) to (v), resulting in –	Removed	

	Relevant Acts	Current Categories of Misconduct (as set out in Table 1)	Proposed Revisions to Categories of Misconduct (revisions made in bold)	Comments
		<ul style="list-style-type: none"> a non-compliance with any regulatory requirement relating to the provision of any regulated activity; or a serious breach of the FI's internal policy or code of conduct which would render the representatives liable to demotion, suspension or termination of the representative's employment or arrangement with the FI. 		<p>trust would fall within Category (i) on acts involving fraud, dishonesty or other offences of a similar nature and Category (v) on failure to satisfy the Guidelines on Fit and Proper Criteria.</p> <p>In addition, the internal policies and codes of conduct of FIs usually take reference from the Guidelines on Fit and Proper Criteria. They also typically prohibit acts that are set out as misconduct in the current Categories (i) to (iv).</p> <p>As such, MAS proposes to remove Categories (v) and (vi) to reduce overlap with the other categories.</p>

	Relevant Acts	Current Categories of Misconduct (as set out in Table 1)	Proposed Revisions to Categories of Misconduct (revisions made in bold)	Comments
(vii)	SFA, FAA and IA	-	Acts involving illegal/improper monetary gains, or which may lead to erosion of trust in the financial system, such as money laundering	This is a new category to capture acts that may render a representative unfit to conduct regulated activities, but do not fall under other categories. Examples of such acts include failing to exercise sufficient care and judgment, or being complicit, in relation to customers' money laundering or tax evasion offences.

3.6 MAS will no longer require FIs to submit an annual nil declaration when no misconduct is reportable in the calendar year.

Question 2. MAS seeks comments on:

- (i) The proposed revisions to the categorisation of misconduct as shown in Table 2; and
- (ii) Whether there are other **categories** of serious misconduct, which have a direct bearing on a representative's fitness and propriety, that should be included in Table 2.

Proposal 3: FIs to update MAS on the outcome of police investigations

3.7 The current Misconduct Notices require FIs to lodge a police **report** and submit a copy of the police **report** to MAS when they have reasons to **suspect** that their representatives have committed any **offence** involving cheating, dishonesty, fraud, forgery, misappropriation of monies, or criminal breach of trust. FIs are also expected to provide information to MAS on the name of the police officer investigating the case, and update MAS on the progress of the police investigation and results of the criminal proceeding.

3.8 To ensure that FIs update MAS on the outcome of police investigations in a timely manner, MAS proposes to require FIs to update MAS no later than 14 days after they become aware of the outcome of police investigations. This would enable MAS to conduct timely assessment on whether to take regulatory or supervisory action on the representative upon conclusion of police investigations.

Question 3. MAS seeks comments on requiring FIs to update MAS no later than 14 days after they are aware of the outcome of police investigations.

Proposal 4: FIs to notify representatives when they are under investigation and provide them with a copy of the misconduct **report** filed with MAS

3.9 The current Misconduct Notices set out the expectation for FIs to conduct investigations into the misconduct of representatives, which include conducting interviews with the relevant parties such as the representative, his or her supervisor, and the affected customer. Nonetheless, MAS has observed differing practices and standards in the investigations conducted by FIs. For example, some FIs may not conduct interviews with the representatives concerned or may not inform the representatives that they are under investigation or the outcome of their investigations, particularly when the representatives concerned have left the FIs. This has resulted in instances where representatives were unaware that they were being investigated or that their principal companies have submitted misconduct reports on them with MAS. Consequently, these representatives were not able to make full or accurate disclosures on their **compliance** history and past misconduct record when applying to join a new principal company. The prospective principal company is also hampered in its ability to conduct a proper assessment on the suitability and fitness and propriety of these representatives before recruiting them.

3.10 In view of the issues outlined in paragraph 3.9, MAS proposes to require FIs to notify their representatives when they are under investigation. Where an FI lodges a misconduct report with MAS, MAS also proposes to require the FI to provide the affected representative with a copy of the misconduct report (including any subsequent updates), regardless of whether the representative is still appointed with the company. The only exception to this is when a disclosure would tip off the representative or compromise the quality of the FI's investigation. This proposal will ensure that the representative is aware of the misconduct report filed against him or her and is given an opportunity to disclose and explain the misconduct to his or her prospective principal company.

3.11 To protect the confidentiality of customers' details, FIs should ensure that the misconduct report does not contain any confidential customer information. Please refer to Annex B for the proposed misconduct report template. In addition to revisions arising from the changes to the categories of reportable misconduct (as set out in Proposal 2), the proposed misconduct report template includes revisions to obtain information on whether the misconduct constitutes a breach of any laws or regulations and whether a police report has been filed by the FI.

3.12 FIs will not be required to inform representatives that they are under investigation or provide representatives with the misconduct report if this would tip off the representative or compromise the quality of the FI's investigation. Examples of such cases are misconduct relating to money laundering, financing of terrorism, or other offences that may require the lodgement of Suspicious Transaction Reports under the Corruption, Drug Trafficking and Other Serious Crimes (Confiscation of Benefits) Act and the Terrorism (Suppression of Financing) Act.

Question 4. MAS seeks comments on:

- (i) The requirement for FIs to notify their representatives when they are under investigation and to provide their representatives with a copy of the misconduct report filed with MAS as well as subsequent updates provided to MAS; and
- (ii) The proposed misconduct report template.

Proposal 5: Enhanced standards for FIs' investigation processes and requirement for FIs to submit investigation reports to MAS in a prescribed format

3.13 The current Misconduct Notices set out the expectation for FIs to conduct investigations into misconduct committed by their representatives and keep proper records of investigations conducted. The records that should be maintained include facts and documentary evidence of the misconduct, interviews with the relevant parties, the investigator's assessment and recommendation, and disciplinary actions taken against the representative. FIs are also expected to take appropriate disciplinary actions against their representatives for misconduct that have been substantiated.

3.14 MAS has observed varying standards in FIs' investigation processes. As such, MAS intends to provide greater guidance on our expectations with regard to the rigour and quality of FIs' investigations into misconduct committed by their representatives. This will include steps FIs should take when conducting an investigation, such as performing customer call-backs, transaction reviews, and interviews with the representatives and customers involved, as well as ensuring proper documentation of the evidence collected and interviews conducted. FIs are also expected to put in place a **holistic** and fair assessment on whether the misconduct is substantiated.

3.15 MAS also proposes to require FIs to submit their investigation reports in a prescribed format to ensure that consistent and sufficient information is provided to MAS. This is also aligned with MAS' move towards requiring data to be submitted in machine-readable formats. The prescribed template will require information such as details of the customer, product in dispute, nature of misconduct, the investigator's assessment and recommendation, as well as the FI's course of action. Please refer to Annex C for the proposed investigation **report** template.

Question 5. MAS seeks comments on:

- (i) The proposed standards that FIs should uphold when conducting investigations; and
- (ii) The proposed investigation **report** template and any other types of information that FIs should provide in their investigation reports.

4 Part B: Proposed requirements relating to reference checks

Proposal 6: FIs to conduct reference checks on prospective representatives and to share information on their representatives in response to reference check requests

4.1 Internationally, there has been an increased focus on the importance of stemming “rolling bad apples” (i.e. movement of individuals with a history of misconduct across FIs). For instance, the Financial Stability Board Working **Group on Governance Frameworks** is a cross-jurisdiction effort which, among other things, seeks to strengthen **governance** frameworks to deter and prevent the perpetuation of misconduct by individuals at different FIs.⁷ One measure that is regarded as key to the cause is the conduct of reference checks within the industry. When FIs recruit representatives to conduct regulated activities, the companies the candidates used to work for serve as useful sources of **independent** information to verify the information disclosed by the candidates as well as to **assess** their fitness and propriety.

4.2 The practice of conducting reference checks is not new in Singapore. MAS’ Circular on Due Diligence Checks and Documentation in Respect of the Appointment of Appointed, Provisional and Temporary Representatives (the “Circular”) sets out expectations for FIs to carry out due diligence on the fitness and propriety (including previous conduct) of representatives they appoint to conduct regulated activities on their behalf. Industry associations have also issued guidance on conducting reference checks, including templates for reference check forms. Nonetheless, MAS has observed differing standards in FIs’ practices when conducting and responding to reference check requests. This is due to the absence of internal **policies** and procedures, inadequate understanding of the importance of reference checks, or concerns about potential legal risks or challenge from representatives.

4.3 Given that late, ambiguous, or partial reference check responses would hinder the industry’s collective efforts to ensure that only fit and proper individuals are appointed as representatives, MAS proposes:

⁷ The Financial Stability Board (FSB) is an international body which, among other things, has assumed a key role in promoting reform of international financial regulation. More details on the work of the FSB Working **Group on Governance Frameworks** are available at <http://www.fsb.org/2017/05/fsb-sets-out-next-steps-on-work-to-strengthen-governance-frameworks-to-mitigate-misconduct-risks/>

- (a) to make it mandatory for recruiting FIs to conduct reference checks on their prospective representatives. Such reference checks should be conducted with all previous employers of the representative i.e. principal companies which are FIs regulated by MAS as well as companies not regulated by MAS.⁸ Such reference checks may be conducted after the prospective representative's employment or appointment has ceased with his or her current principal company and should minimally cover the representative's employment history in the past 10 years; and
- (b) to require FIs to provide a set of mandatory information on their representatives in response to reference check requests from the representatives' prospective principal companies which are FIs regulated by MAS.

4.4 Regardless of whether a representative is still appointed with an FI, the FI owes the representative a duty of care in preparing and communicating references. FIs should exercise reasonable care to ensure that information provided in the references is accurate, objective, clear, balanced, and based on verifiable facts. This will also **mitigate** potential legal risks to FIs providing references.

4.5 To standardise practices in the industry and improve the effectiveness of reference checks, MAS proposes to require FIs to provide the following mandatory information (where applicable) no later than 14 days from the date of receipt of a reference check request:

- (a) information pertaining to the individual's appointment history with the FI, the duration of appointment, the roles and job functions of the individual (including last position held), and the reason for the cessation of the appointment (such as resignation, termination, or cessation of contractual tenure);
- (b) **compliance** records on the individual's fitness and propriety, including but not limited to the following:

⁸ MAS notes that FIs may encounter difficulties when conducting reference checks with companies that are not regulated by MAS. FIs must, on a best effort basis, take reasonable steps to conduct reference checks with such companies.

- i. past or ongoing internal or external investigations that the individual is or has been subjected to, and the outcome of the investigations;
 - ii. incidents which relate to the individual's honesty or integrity, and the extent of consumer detriment;
 - iii. incidents where the individual had been found to be in breach of legal or regulatory requirements, and the extent of consumer detriment;
 - iv. whether misconduct reports were filed with MAS against the individual and, if so, details on the nature of the offences committed and the extent of consumer detriment; and
 - v. disciplinary actions taken against the individual;
- (c) last four balanced scorecard grades assigned to the individual within the past 10 years; and
- (d) persistency of insurance **policies** sold by the individual and the methodology used in computing the persistency.

4.6 The proposal in paragraph 4.5 allows an FI to conduct a proper assessment of the representative's fitness and propriety at the point of recruitment. It is also the duty of FIs to ensure that their representatives are fit and proper on an ongoing basis. MAS recognises that information on a representative could change after references are provided. For example, a misconduct may only be uncovered or substantiated after a representative leaves or after a response to a reference check has been provided. Some regulators mandate FIs to provide updates on prior responses to reference checks when new information on their former representatives surfaces. This would accord FIs with relevant and up-to-date information to **assess** the fitness and propriety of their representatives. However, MAS is also cognisant that this may pose operational challenges given the need for FIs to track references that they previously provided to different FIs. As such, MAS seeks views on the alternative approach of requiring representatives to provide their current or prospective FIs with any misconduct **report** that has been filed against them, including subsequent updates to the misconduct report. This approach factors in Proposal 4 at paragraph 3.10 where MAS is proposing to require FIs to provide representatives with a copy of the misconduct **report** and subsequent updates filed with MAS against them.

4.7 For the avoidance of doubt, MAS also proposes to apply the requirements relating to reference checks as described at paragraphs 4.3 to 4.6 to RFMCs and insurance

brokers. In addition, the expectations set out in the Circular will apply to the recruitment of representatives for RFMCs and fund management companies which are licensed under the Venture Capital Fund Manager Regime, as well as broking staff for insurance brokers. The Circular will be amended to reflect the scope of applicability more clearly.

Question 6. MAS seeks comments on:

- (i) The requirement for FIs to conduct reference checks on prospective representatives and to **respond** to reference check requests;
- (ii) The list of mandatory information FIs are required to provide in response to a reference check request and the prescribed timeline of 14 days for responding to reference check requests;
- (iii) Whether representatives should provide their current or prospective FIs with any misconduct **report** that has been filed against them, including subsequent updates to the misconduct report; and
- (iv) Whether there are other standards or requirements that should be mandated to enhance the effectiveness of reference checks.

Annex A

LIST OF QUESTIONS

Question 1.	MAS seeks comments on the proposal to apply the requirements on reporting of misconduct by representatives and reference checks to RFMCs.	8
Question 2.	MAS seeks comments on:	13
(i)	The proposed revisions to the categorisation of misconduct as shown in Table 2; and	13
(ii)	Whether there are other categories of serious misconduct, which have a direct bearing on a representative's fitness and propriety, that should be included in Table 2.	13
Question 3.	MAS seeks comments on requiring FIs to update MAS no later than 14 days after they are aware of the outcome of police investigations.	14
Question 4.	MAS seeks comments on:	15
(i)	The requirement for FIs to notify their representatives when they are under investigation and to provide their representatives with a copy of the misconduct report filed with MAS as well as subsequent updates provided to MAS; and	15
(ii)	The proposed misconduct report template.	15
Question 5.	MAS seeks comments on:	16
(i)	The proposed standards that FIs should uphold when conducting investigations; and	16
(ii)	The proposed investigation report template and any other types of information that FIs should provide in their investigation reports.	16
Question 6.	MAS seeks comments on:	20
(i)	The requirement for FIs to conduct reference checks on prospective representatives and to respond to reference check requests;	20
(ii)	The list of mandatory information FIs are required to provide in response to a reference check request and the prescribed timeline of 14 days for responding to reference check requests;	20
(iii)	Whether representatives should provide their current or prospective FIs with any misconduct report that has been filed against them, including subsequent updates to the misconduct report; and	20

(iv) Whether there are other standards or requirements that should be mandated to enhance the effectiveness of reference checks. 20