



FSB

INSURANCE DIVISION

THE RETAIL DISTRIBUTION REVIEW (RDR)

Leanne Jackson
Head: Market Conduct Strategy
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Setting the scene

- RDR has been undertaken in the context of Twin Peaks market conduct mandate and the TCF framework
- Proactive and interventionist approach to identifying and remedying market failures
- Structural interventions to change incentives, relationships and business models where existing regulatory frameworks do not support delivery of fair outcomes

The RDR is a prominent example of this new approach



Scope of the RDR

- A mainly retail focus – wholesale market reforms being addressed through complementary processes
- A cross-cutting, cross-sectoral approach
- Particular focus on advice



Objectives of the RDR

To ensure that financial products are distributed in ways that support delivery of TCF outcomes and enable –

- Delivery of suitable products and fair access to suitable advice
- Customers to understand and compare the nature, value and cost of advice and other services
- Enhanced intermediary professionalism to build consumer confidence and trust
- Customers and distributors to benefit from fair competition for quality advice and services, at prices more closely aligned with the service provided
- Support sustainable business models for financial advice.



The current distribution landscape

The current landscape comprises different – often complex – combinations of:

- Types of services provided by intermediaries
- Relationships between product suppliers and intermediaries
- Intermediary remuneration models

A total of 55 RDR regulatory policy proposals are grouped under these headings



Risks and benefits of the current landscape

The current landscape poses risks to -

- fair customer outcomes
- intermediary sustainability
- supervisory effectiveness

Benefits of the current model include -

- customers more willing to pay for perceived “free” advice
- commission cross-subsidisation works for low income consumers
- ease of administration



An activity-based approach to defining advice & intermediary services

- Services to customer
 - Advice
- Services connecting product suppliers and customers (true “intermediary services”)
 - Sales execution - separate from advice, which may or may not be provided too
 - Ongoing product maintenance and servicing (including premium collection)
 - Investment platform administration
 - Aggregation & comparison services
- Services to product supplier
 - Binders and other outsourcing services



Financial advice

- Three forms of advice defined
 - financial planning
 - up-front product advice
 - ongoing product advicewith related conduct standards
- Standards for “low advice” distribution models
- Standards for “wholesale” advice



Services to product suppliers

Outsourced services on behalf of product suppliers to generally be more clearly identified and regulated

- approach to be modelled on principles in current insurance Outsourcing Directive (Directive 159)



Services connecting product suppliers and customers

- Standards for **sales execution**, especially in non-advice models – product standards; specific fit & proper standards; establishing financial capability; remuneration model to take into account that no advice applies
- Standards for ongoing product servicing
- Insurance premium collection limited to qualifying intermediaries
- Revised standards for investment platform administration
- Standards for product aggregation and comparison services .



Product supplier / intermediary relationships

- Three types of advisers defined – independent adviser (IFA), multi-tied adviser; tied adviser
- Adviser may only act in one of these capacities – but an investment products IFA may be multi-tied for insurance risk products and/or health benefits
- Slightly different terminology for short-term insurance and health benefits
- All business cards, letterheads, e-mails, websites, etc. must reflect the relevant status
- An adviser who meets standards to be a financial planner may use this designation too
- Regulator may 're-classify' an adviser .



Independent financial advisers (IFAs)

An IFA will need to meet two sets of independence criteria –

- Adequate product & product supplier choice. Further input is requested on how to determine these – but accept that “whole of market” is not feasible
- Freedom from product supplier influence – specific scenarios will exclude an adviser from qualifying as an IFA.



Multi-tied advisers

- A multi-tied adviser - any adviser that is not a tied adviser and also does not satisfy the criteria to be an IFA
- Additional conduct standards to manage conflicts arising from specific scenarios – for e.g. where unequal relationships exist with different product suppliers
- Multi-tied adviser will be required to keep records regarding the proportions of business placed with different product suppliers, with motivations



Tied advisers

- A tied adviser - any adviser whose contractual, ownership or other relationship with a product supplier restricts the adviser to providing advice on the products of that product supplier only
- For this purpose “product supplier” includes entities in the same product supplier group – to be defined and regulated to avoid abuse



Financial planners

- Conduct standards, including appropriate fit & proper standards, for financial planning
- Standards may be set with reference to membership of and/or qualifications provided by appropriate professional associations, or may take these into account
- A tied or multi-tied adviser may be a financial planner – but with appropriate standards to manage possible conflicts arising from limits on product/product supplier choice



Juristic intermediaries (adviser firms) and “hybrid” models

- Insurer tied advisers no longer able to provide advice on another insurer’s products
- “Juristic representatives” will be disallowed from providing advice
- An adviser may not act as a representative of more than one adviser firm
- Standards for the status of an adviser firm vis-à-vis its individual advisers
- General review of ownership arrangements between product suppliers & intermediaries.



Outsourcing

- General standard: No product supplier or investment management functions may be outsourced to a financial adviser, unless specifically permitted and regulated

- Permissible outsourcing to an adviser –
 - Binder functions, subject to the binder regulations
 - Issuing insurance policy documentsComment invited on other permissible functions

- Does not affect outsourcing to entities acting solely for a product supplier that are not advisers or associates of an adviser



Product supplier responsibility for multi-tied advisers

Product supplier shares responsibility for customer outcomes, with specific conduct standards regarding –

- Adequate product training
- Assessment of ability to deliver fair customer outcomes, including governance and culture
- Monitoring TCF indicators, with action to address identified poor outcomes
- Controls to identify and mitigate specific high risk activities
- Reasonable steps to monitor quality of advice (further consultation planned)
- Monitoring and resolving customer complaints re the adviser
- Monitoring adherence to fee guidelines



Product supplier responsibility

- Tied advisers: Product supplier wholly responsible for advice and all relevant compliance – including but not limited to standards as for multi-tied advisers
- IFAs: Some but not all responsibility standards as for multi-tied advisers will apply
- Non-advice sales execution: Product supplier responsible to ensure product standards and other conduct standards are met
- Product supplier responsibility to ensure adequate access to customer information held by intermediaries or outsource providers; and to provide advisers with appropriate customer information when authorised by customer (subject to safeguards).



Remuneration disclosure

General standards will be set for:

- Standardised terminology to describe types of services, fees and charges and to disclose the impact of these on benefits
- Production and accessibility of fee “schedules” or “menus”
- Content, timing and record keeping of remuneration disclosures
- Disclosure relative to fee guidelines or benchmarks to be set by the regulator.



Advice fees

Standards will be set for financial planning fees and up-front and ongoing product advice fees, including on -

- Customer consent, disclosure and regulatory reporting
- Product supplier monitoring and reporting
- The principle that advice fees should be reasonable and commensurate to services, and not allow for cross-subsidisation by product charges
- Benchmark “safe harbour” guidelines by the regulator
- Specific standards for ongoing fees – aimed at ensuring no fee without ongoing advice, and customer control



Product suppliers to facilitate advice fees

- Advice fees may – but need not be – charged directly to the customer.
- Product suppliers will be obliged to accept instructions from the customer to deduct up-front or ongoing advice fees – from contributions or investment product values – and pay these across to the appointed adviser
- Comment is invited on the range of fee deduction options product suppliers should be obliged to facilitate.



Remuneration for selling and servicing investment products

- Product suppliers, investment managers and LISPs prohibited from paying (and intermediaries from receiving) any form of remuneration to intermediaries
- Customer agreed advice fees will be the only form of intermediary remuneration available (subject to payment arrangements between adviser firms and their advisers)
- Costs of intermediary remuneration may not be included in product charges
- Exceptions for the low income market



Remuneration for life insurance risk business

- 50% up-front sales commission and 50% as-and-when service fee - further technical work and consultation on levels
- All sales commission at start of policy – no more “second year” commission, no more “mini policies” for contractual premium escalations
- Clawback of up-front commission to remain
- Further consultation on range of services that qualify for service fees and fee caps - no ongoing fee without ongoing service



Specific insurance remuneration conflicts

- Stricter conduct standards for “s14” retirement annuity transfers
- No commission or fees on replacement life risk policies – only customer agreed advice fees
- Commission basis for variable premium increases on “legacy” investment products to be brought in line with rules for new policies
- To be done together with other measures to further reduce early termination values on existing investment policies



Equivalence of reward

Standards will be set to clarify and strengthen the “equivalence of reward” principle, including –

- Confirmation that equivalence applies at individual adviser level
- Detailing the remuneration elements, tranches of business and time periods to be taken into account in determining equivalence
- Applying equivalence in relation to risk business only – remuneration for investment business may not exceed customer advice fees paid

Input is invited on whether the equivalence principle should be extended to short-term insurance business.



The low income market

A special remuneration dispensation – with some level of commission retained for investment products - will be developed for this market, after further consultation on:

- Product standards to qualify for this dispensation – including no or significantly reduced early termination charges
- Inter-relationship between this dispensation and the micro-insurance policy framework
- Types of intermediary and advice services, and types of product supplier / intermediary relationships, to qualify for this dispensation
- Permissible commission limits.



Remuneration for selling and servicing short-term insurance

- As-and-when model for selling and on-going servicing to be retained – but levels of commission and service fee to be reviewed
- Current provision for “section 8(5)” fees to be removed – instead, advisers will be able to charge a customer-agreed advice fee, separate from commission
- Services qualifying for the service fee component, and fee caps, require further consultation and technical work
- No ongoing service fee without ongoing service

Additional customer protections on policy cancellations



Remuneration for investment platform administration

- Platform administration fees to be disclosed, agreed to and paid for by the customer as the platform's only remuneration
- Payments from product suppliers or investment managers, including rebates, will be prohibited.



Binder fees

- Maximum binder fees to non-mandated multi-tied advisers to be capped
- Indicative caps for consultation:
 - Entering into, varying renewing = 2%
 - Determining wording, premiums, value of benefits = 2%
 - Settling claims = 1% to 3%
(depending on extent of services)



Outsourcing fees

- Limited outsourcing to advisers – where permitted, caps will apply
- Fee for issuing insurance policy documents – indicative fee for consultation = R100 flat fee (not permitted for binder holders)
- 22.5% commission cap for credit life schemes “with administrative work” to be scrapped – cap to be 7.5% for all credit life schemes (pending further group schemes review)



General standard re financial interests from product suppliers

The payment by a product supplier, and receipt by an intermediary, of any form of remuneration, incentive or other financial interest – whether direct or indirect – is prohibited unless it is specifically permitted in terms of legislation

- Further consultation on extending this to 'add-on' products or services, or setting other standards for distribution of these.



A phased approach to implementing RDR regulatory policy proposals

Proposals to be phased in as Twin Peaks legislative architecture evolves –

- Phase 1: Changes within current regulatory framework – estimated to be during first half of 2015
- Phase 2: Changes post effective date of Financial Sector Regulation Act – estimated 2nd half of 2015
- Phase 3: Changes post effective date of future overarching market conduct Act – estimated mid 2016



Priority RDR proposals

Proposals targeted for Phase 1 (first half of 2015), to prioritise addressing current inappropriate conflicted practices (not a closed list):

- Insurer tied advisers disallowed from advising on another insurer's products
- Adviser may not act for more than one adviser firm
- Restricted outsourcing to financial advisers – certain functions permitted (including issuing insurance policy documents)



Priority RDR proposals cont.

- General product supplier responsibilities re customer data
- Commission prohibited on replacement life risk policies
- Commission regulation anomalies on legacy insurance products & enhanced standards for RA transfers
- Equivalence of reward to be reviewed



Priority RDR proposals cont.

- Remuneration for selling & servicing short-term insurance
- Conditions for short-term insurance cover cancellations
- Binder fees to non-mandated multi-tied intermediaries to be capped
- 22.5% Commission cap for credit life group schemes reduced to 7.5%



Transitional measures

- Implementation date for “structural changes” to be confirmed:
 - depending on further consultation and the final Twin Peaks framework
 - unlikely to be before mid-2016
 - 12 months provided for system changes
- New standards will apply from implementation date – product suppliers / intermediaries must plan accordingly
- Transition measures for
 - Changes to the structure and level of commission for LTI risk products
 - Payment of “trail” commission on legacy products