In November 2014 we saw the long-awaited Retail Distribution Review (RDR) discussion paper released by the FSB. This paper proposes the biggest set of changes for financial advisors since the introduction of FAIS eleven years ago.

As part of the consultation process the FSB invited feedback on the paper. So, over a period of about 12 weeks we as Masthead helped our brokers to come to grips with the RDR paper. We put together a number of special editions of our Mastering Compliance newsletters and supplemented these with video clips to help our members unpack RDR. We ran 20 workshops around the country, with over 700 brokers attending.

We used these sessions as well as numerous email and telephonic comments as input from financial advisors. Our feedback is therefore based on contributions and comments from the very people affected by the proposals in this paper.

What follows is a copy of the feedback that we submitted to the FSB in March 2015. This feedback is broken down into two parts:

- Some general comments in relation to each chapter of the RDR paper, and
- Our specific comments on the 55 RDR proposals set out in Chapter 4.

Customers need advisors to help them with appropriate advice and appropriate financial products. So, we need to do what we can to ensure appropriate advice is available to customers through this changing environment. That’s why we at Masthead will stay involved in helping our members and customers deal with the changes – Masthead will help to define and shape that change.

Ian Middleton
Managing Director
Chapter 1:

Re 1.2 – We support the cross-cutting approach.

Re 1.3 - We agree and support the objectives as set out on page 9 and would want to test the proposals at a detailed level against these.

With reference on p9 to a primary concern relating to "... significant conflicts of interest in the way financial products are distributed and the way financial advice is provided ...", there appears to be an absolute belief that the conflict is so widespread and endemic that everything is bad. There have been conflicts and there are still conflicts. However, we believe that the examples of conflict need to be seen in the context of the entire industry.

For 2013/14 there were ±9,500 new complaints submitted to the office of the FAIS Ombud, whose jurisdiction covers "parties furnishing advice or rendering intermediary service in respect of financial products". Of these complaints, just over 80% were either dismissed or referred to other areas (indicating, for us, that they have nothing to do with the advice). The percentages are not dissimilar for the preceding two years. While some of the complaints are related to remuneration, many are not. There are more than 6 million new business life policies sold in the country per annum. Therefore, in the context of all the business done in the country and all the advice dispensed, and all the products sold, we believe that the overwhelming majority of financial advice is provided and the majority of financial products sold are done so in the interests of the customers and without "significant" conflict.

Life insurance and savings products are "sold" not bought – this is an old saying in the industry and today it still rings true. Even with commission (deemed to be an incentive to sell) in place, there’s still under insurance, a shortfall in savings and not enough retirement provision. So can it be all that bad? Therefore, we need a model in place that supports balance in the market and doesn’t throw the good out with the bad.

We submit that in a changed system there should be shared accountability. We don’t want a system that makes product suppliers question their continued role in the IFA and/or multi-tied space because they get the liability, but not the control. If, in Figure 1, they move from position 1 to position 2 and therefore they pick up a disproportionate liability without the control, it could mean they exit the untied distribution space. That won’t be good.

Re 1.4 - Developments to date

There is no doubt that overall today we are in a more professional environment. Like the boiled frog, the increase in professionalism has been steady and incremental, not a
quantum leap, and therefore sometimes it seems as though there has been nothing. Figure 2 reflects the thoughts of an IFA.

We support TCF and would like to see it in action. There has been lots of response and system builds from the industry. It may now be time to see customers getting redress and public actions taken against those entities (in every step of the product life cycle) that haven’t, through their behaviour, bought into this.

Re section 1.4.4 - We are glad to have seen the response of the FSB in expanding the scope of the initial 2011 paper and it's pleasing to experience consultation in action. We know it's easy to criticise, so we welcome the process of genuine interactive engagement.

Re section 1.4.5 - We think it is appropriate to consider international environments and perspectives. We have faith that the FSB has and will take an approach of discriminate introduction for our environment.

**Figure 2**

It is a given that things have changed radically in recent years and I know that some of the changes have improved things for clients and for those of us who service them … and if the changes have served to lift standards in the industry then that is a good thing.

**Chapter 2**

Overall we commend the writers for a good account of the distribution landscape in this country. We set out our specific comments below:

**re 2.2.2 - Financial planning**

The International Organization for Standardization (ISO), based in Switzerland, has defined a process for personal financial planning (ISO 22222:2005) [https://www.iso.org/obp/ui/#iso:std:iso:22222:ed-1:v1:en]. This standard, based on 6 steps for personal financial planning together with competence, experience and ethics requirements was last reviewed in 2011. The local participant in this process was/is the South African Bureau of Standards (SABS).

While the ISO standard defines the personal financial planning process and specifies additional requirements for personal financial planners, it does not provide any “home” for financial planners. It does not fulfil any oversight or guardian role. It does not provide access or recourse to consumers in the event that something goes wrong in the interaction or engagement with the personal financial planner.

A financial planner needs to think about, think around and critically analyse holistically and broadly a client’s circumstances and objectives “within the 6 step process” in order to arrive at an appropriate outcome for the customer around which “professional advice” can be offered and where appropriate solution is offered and implemented. So, financial planners need knowledge and understanding of a range of things like legal implications of family relationships, labour law, psychology, culture, religions, accounting, legal and tax concepts and principles. They need to know what is going on in the world. For this reason, the view is held that following the steps of financial planning on their own is not enough to enable someone to call himself “professional”.

Masthead Feedback on RDR to FSB_March 2015
The words in Figure 3, offered by one of the Masthead members (who is a CFP), sums up an attitude to financial planning that differentiates it from simply the process of financial advice.

In our view, to have financial planning and financial planner written into regulation would not be complete if one didn’t recognise financial planning as a profession – this is different to a trade and is different to simply following a process. There is not just a level of technical knowledge, competence and specialised training needed, but also a commitment to a set of ethical standards and an obligation to focus on the interests of those being served. Members of a profession are held to higher standards and, importantly, they are held to account. It is, in our view, the professional aspect that sets financial planning apart from just process.

Every advisor (irrespective of whether that person is a financial planner by definition or not) is tested against the suitability of advice in relation to the circumstances of the customer. Every FAIS Ombud determination involves a question as to suitability and consideration of customer circumstances and appropriateness of the advice and the product solutions put in place.

One cannot emphasise the need for financial advice enough, irrespective of whether this advice is carried out by financial planners (as may be defined) or personal financial advisors who follow an advice process. There are many papers that espouse the value of advice, and for purposes of this feedback, we’re not going to saddle up that horse again.

**Re 2.2.3 - Financial Product Advice**

In the course of product advice, the advisor still has to go through a process of needs/information gathering, analysis and suitability application.

**Re 2.3 - Relationships between product suppliers and intermediaries**

**Re 2.3.1 - Independent financial adviser**

The paper refers to the definition of independent intermediary as being linked to the Long Term Insurance Act and commission regulations. Since the days when that was drafted what can today be described as an “independent intermediary” has moved significantly. Independent can mean different things to different people. Maybe it’s time to go back to the old definition.

The debate about status of advisor and possible definitions for the different types has provided much food for thought. Advisors describe their independence in simple terms - this is what one advisor thinks:

<table>
<thead>
<tr>
<th>Independent, tied, partially tied???? This I do not understand at all. What do I think independence is:</th>
</tr>
</thead>
</table>

*Figure 3*
I am independent, not because I have ALL the contracts in the market place, but because I have independently negotiated each contract I have. I do not receive any benefits from the financial institutions I deal with, nor do they provide me with any services other than possibly a broker consultant whose job it is to market their products to me, and some sort of background assistant/call centre that facilitates the implementation of the product I have sold/the client has bought. I mostly do not even get material from them - quotations and proposal forms are printed on my own stationery.

Unlike an agent, I am VAT registered....

Full disclosure already exists:

In my letter of introduction to clients, I am compelled to spell out the names of the companies with whom I hold contracts. I am also compelled to disclose who receives most of my business. SURELY that is enough? How is it going to provide more disclosure if I am now called by another name? I am independent because I did not want a manager looking over my shoulder for production all the time. I wanted my fees and commissions to vest with me and not with a company. I am definitely NOT tied in any way. As it is I see no harm in calling myself a broker or a salesman for that matter! It does not change what I do ... in fact it might be more honest than some of the other names being bandied about. It certainly doesn’t make me less professional. If by lifting the client’s horizon, allowing him/her to see what they need and helping them get it I am a planner or a salesman, I have helped that client make a provision they did not previously have. But I am NOT tied ... or partially tied!

IFA – Feb 2015

The reference on p15 to "... remunerated solely by fees paid to them by customers ..." is used as possible evidence for independence. But, we submit, this is not necessarily so – there is no perfect answer because any form of remuneration has potential conflict – eg. charging an hourly rate directly to a customer (whether by a doctor, accountant, lawyer, plumber or electrician) could encourage one to “pad the hours” or take longer to complete a job.

In reality, at a practical level, most advisors/intermediaries (defined currently as independent advisors) don’t have terms of business (contracts) with all suppliers. But, this doesn’t make them less independent when they advise. For that matter, doctors who are seen to be independent don’t distribute all drugs on the market.

The Law of Agency in South Africa regards an independent advisor as someone who acts as agent of or on behalf of the customer while a tied advisor acts as agent of the company (typically his employer).

Re 2.3.2 - Multi-tied

At a practical level most IFAs in this country have multiple contracts and therefore would (by UK standards) be Multi-tied. But, we submit that such a definition is only appropriate if we also accept what they did in the UK to define IFA as being "whole of market".

Re 2.3.3 - Tied advisor
We remember when, metaphorically speaking, the Toyota rep had a business card saying “Representative of Toyota”. He used to be able to offer you the range of Toyota vehicles only. Then general agency became fashionable to the extent that today the Toyota rep can sell almost anything as long as Toyota (his employer) has an agreement (often reciprocal) to sell the cars of other manufacturers (like BMW, Hyundai, etc).

Admittedly, this creates confusion and maybe the definition as set out in the FAIS Act coupled with the Law of Agency is where the definition or description of “tied” should settle. We should be going back to the “Representative of Toyota”. In that instance, what the customer sees is what the customer gets.

On p16 there is reference to bank representatives possibly being restricted to the products of the bank – it should perhaps be considered that most banks have product supplier licences (life, short term and/or investments) within their structures and therefore have their own product ranges. However, they have over the years projected themselves as independent in that they offer choice. Despite this we would agree with the sentiment that there is encouragement to offer the banks products over those of other product suppliers.

**Re 2.3.5 - Outsource service provider to product supplier**

It is widely accepted that admin has shifted from product suppliers to advisors over the years. We’d submit that there are a number of functions effectively outsourced by suppliers to IFAs without contractual formalities or remuneration/fee attached to such outsourcing. For example, completing application forms online and updating customer information online effectively obviates the need for someone at the insurer to do the work. It also shifts the risk for correct capturing onto the advisor. The short-term industry recognises this as an outsourced function and provides for the payment of an admin fee. We submit that it is appropriate to look at this in relation to long-term insurance business too. The printing referred to doesn’t only have to be actual policy documents – it can be all documents (especially application forms and any other brochures). While Figure 4 reflects the words of one IFA, it reflects the thoughts of many.

**Re 2.3.6 - Hybrids**

This description really indicates that the world of distribution has become grey. What you see isn’t necessarily what you get. Nothing else to add.

**Re 2.4 - Types of Remuneration**

**Re 2.4.1 - Fees paid directly by customer**

As indicated in the discussion paper these arrangements are rare. Where they are in place, they typically work on hourly rates or transaction rates, or by a fee calculated as a percentage of assets under advice (if one accepts that the customer authorises a product supplier to collect and pay the fee over to the advisor). While the first two methods may be acceptable in the high net worth (HNW) market, an assets under advice/management approach is quite common with regard to all lump sum investments.

With reference to the rebate construct on p17, one can debate whether this is really a fee model. To us it seems more like a financing structure. It is quite common in the investment field but is also workable on the life side. While there may not be regulated fees iro advisors
charging these, the free market and customers have driven these down to levels that are less/lower than maximum regulated commission (at least iro single premium investments).

Re 2.4.2 - Fees paid by customer, facilitated by product supplier (deducted from investment product values)

Technically these “fees” are deemed to be commission although practically they are funded by the customer and simply administered by the product suppliers.

Re 2.4.3 + 2.4.4 - Commission paid by product supplier – up-front and ongoing

While one can have as-and-when commission iro life products, there are often constraints that are generally systems-related within the life offices. For example some companies cannot administer as-and-when commission at an individual case level. They use the broking contract as the guide and if this is an “upfront commission” contract, they’ll default the payment of commission on all business to upfront.

Other constraints to an as-and-when model are cash flow impacts and the period over which commission would be payable – it is not be viable for an advisor to run a sustainable business on the basis that commission on a life policy pays over a period of something like 25 years. To be viable, one could be looking to make payment of this type of commission payable over a period closer to the period that the average life policy stays on books (currently about 6-7 years).

Re 2.4.5 - Salary or similar remuneration paid by product supplier

Reference is made in the paper to salary models being commonly used in the case of direct sales models. BUT, often (if not always), the person who sells more gets paid more. So, there is incentive or skin in the game. It is, in our view, commission by another word.

Re 2.4.9 - Outsource service fees

Reference is made on p20, in relation to Directive 159, to the need for fees to be “reasonable and commensurate”. This phrase is also mentioned later in the discussion paper (in relation to advisor fees), and therefore we believe that it is important to have greater clarity as to what it means and how its determined. We feel that there are a number of subjective factors that are at play, and therefore the ability to objectively determine these is difficult.

Chapter 3:

Re 3.1 - Risks to fair customer outcomes

Re 3.1.1 - Information asymmetry and customer sophistication

We support the objective to address information asymmetry to the extent that it exists. Having said that, as an industry (whether driven by regulation or not) we have bombarded customers with information without consideration of the ability or inclination of the customer to deal with or be interested in this information. We throw disclosures at customers in the hope that they are better informed and therefore will make better decisions. In many cases this hasn’t worked. Even where customers sign and, on paper, accept responsibility for certain decisions or actions, there are examples of findings (determinations) against advisors ... in the interests of fairness or because, in the opinion of a 3rd party, the advisor did not exercise due skill and care.
So, in our view, we need a balance – one the one hand, the customer must get enough relevant information, pitched at the right level so that he understands it and on the other hand, the customer must not be overwhelmed by information to the extent that he doesn’t actually take a product or the advice that he needs. If he’s struck by information overload that leads to decision paralysis – he does nothing. This information asymmetry runs across all LSM levels.

Also, if one looks at the types of customers in whose favour FAIS Ombud determinations were made, then (judging by compensation awards made), many tend to be middle to affluent customers.

Re 3.1.2 - Tripartite legal relationship creates conflicts

We submit that, except in so far as tied advisor or hybrids are concerned, most independent advisors (if not all) are already product supplier neutral. While there may be differences in commission levels between product types, there is parity between product suppliers because of the regulated nature of commission. So, to this extent, there is not a conflict. We further submit that where the customer is fully informed of the construct of the association (as in Figure 5), and understands the relationships between the parties, including commissions payable, it is the customer who is in the best position to determine a conflict. We therefore submit that with the appropriate disclosures, commission, as a method of remuneration does not prevent a person from advising independently.

On p21, the statement is made that “commission system is opaque and potentially misleading” and further on the same page reference is made to “the opaque nature of the costs…”. Since the introduction of the Policyholder Protection Rules in 2004, advisors have been compelled to disclose commissions payable in the sale of a product. In addition, customers know advisors don’t work for nothing. Most of them are fully aware that advisors are remunerated via commission funded (at the end of the day) out of the premium. The customer, just as the advisor and the product supplier in the tripartite relationship also has a responsibility to become informed.

We don’t necessarily agree with the view on p21 that because customers may not know or appreciate what they’re paying for advice that there is a weaker accountability mechanism when it comes to the quality of advice. There are a number of complaints structures available to customers. If anything, looking at the classification of complaints by an institution like the FAIS Ombud, there are far more complaints submitted than complaints deemed to be justiciable – for 2013/14 total new complaints submitted outnumber justiciable ones by almost 3 to 1. In fact, about ½ of all complaints submitted to FAIS Ombud are dismissed. These numbers seem to indicate that consumers do complain. Their complaints are about unfair or unrealised outcomes and it appears less relevant whether they’re fully conversant about commission and/or the cost of advice or not.

Commission on premium escalations is problematic. This is a quirky provision in most product supplier broking agreements that determines that commission flows to the advisor who sold the policy/product. Most advisors would be happy to have that changed – let the customer decide and let commission only flow at the election of the premium escalation.
On p21 it is stated that “entitlement to commission is not dependent on providing advice” and “the regulatory framework imposes no obligations on insurance intermediaries to provide advice before being entitled to commission”.

There may be nothing in regulation that makes commission dependent on advice, but in terms of obligations under FAIS and the common law duty of care, we believe customers have various options open to them if they are dissatisfied. They have recourse to the FAIS Ombud, who has ordered advisors to refund commission because it’s been paid without providing service or advice. Also, irrespective of whether there was advice or not, customers have the right to cancel within the cooling off period. And, because commission is disclosed, customers have the ability to question and negotiate amounts. Also, often customers who complain that they received no or inappropriate advice do not raise this themselves – they are “encouraged” by other advisors, driven by a different agenda, after the fact to take it further. And, lastly, even in a single need sale, unless there is an execution only sale, the advisor is bound to apply suitable product to customer’s needs. That's advice and should be paid for. So, while there may be no regulatory nexus between commission and advice, in practice it is there.

The statement is made on p22 that “commission as a percentage of premium can lead to mis-selling, there is an incentive for intermediaries to sell the highest premium/contribution possible…” Ironically, in both short term and long term insurance sales, the tendency has been to sell on lower premium, which goes slightly against the assertion.

The comment a little further on that “the intermediary’s cost of providing advice or other intermediary services may be very similar for a small premium product as it is for a large premium product, but the commission paid will be substantially different” tends to oversee an important point. Even if (for purposes of this example), the cost of service is similar, there is a direct relationship between premium size and the risk assumed by the financial advisor. Most often higher premiums equal higher risk cover or larger investment amounts and this can involve more admin and more complicated admin as well as a higher level of expertise expertise/knowledge and therefore a higher charge/fee. The advisor’s exposure and potential liability increases and it is reasonable that he is adequately compensated.

p22 – “Up-front commission creates inappropriate incentives”.

If one follows through the argument in its purest form, then any remuneration creates a possible inappropriate incentive. If this is so, then the only way to address it is to ban remuneration completely and/or place the onus on customers to “buy” life products rather than be sold them. Clearly this is not feasible. The converse is also true – no payment or reasonable remuneration leads to no new policy even where this may be appropriate.

We accept that there is always a risk of mis-selling if the interests of the commission-chasing advisor drive the sale. And granted, there may be severe costs if an individual policyholder is switched to risk products that are not appropriate to their individual circumstances or needs – but, this would be inappropriate advice and there are systems in place (eg. FAIS General Code of Conduct, the ASISA Code on Replacement, Replacement Policy Advice Records, access to the FAIS Ombud) to address inappropriate advice. This system appears to be working well and therefore, we would caution against introducing new/more regulation where there is adequate regulation. We would rather see intensified supervision.
We submit that there is no real evidence that churn increases the cost of life premiums. Improved medical science, better information, slicker underwriting, product innovation and other technological advances have resulted in a reduction in life cover premiums over the last 10 years – this despite what is seen as an increase in churn and a decrease in the average duration of a life policy. So, deal with savings products and the penalties in a different way, but iro pure life we submit that there is not the same compelling reason to change the system.

We agree with the comments made under the bullets dealing with fees over and above commission and unlevel playing fields iro investment product remuneration.

p22 - A potential bias towards tied advice models exists:

Equivalence of reward has not been raised as a big deal amongst independent brokers – they feel that there is ultimately a trade-off in that the tied advisor is limited in offering and what they can take/offer to customer. The main drivers towards tied have been (1) upfront payments, (2) ability to sell other non-home company products, (3) ability to be paid more for home company products and (4) the ability to keep a foot in the other (independent) FSP camp. This creates conflict and is where the real problem lies. Address this and, in our view, most of the other issues are addressed.

Re 3.1.3 - Conflict of interest risks arise from other forms of fees paid to intermediaries by product suppliers

It becomes very difficult to regulate all types of “potentially bad behaviour”. Place the onus on the advisor/business and then police and sanction, publicly.

Binder and outsourcing fees – to be able to address the issue, shouldn’t one therefore require an external 3rd party to sign off on the required oversight – similar to the need for FSPs to have a compliance officer?

We agree with the comment/principle that intermediaries should not be remunerated twice for the same service. Through all our interactions with advisors over the years, the reasonable and average advisor supports this concept … as long as one is clear on whose behalf the work is being done and who’s paying for what.

(p23) - Other forms of outsourcing fees.

We agree with the possibility of bias based on financial interest in the example set out. However, we wonder what makes this situation different to a vertically integrated model – eg. a product manufacturer with a distribution channel that openly declares the bias, but because the customer sees this, the money can flow?

Re 3.1.4 - Conflict of interest risks and complexity of charging structures arising from platform fees and rebates paid by product suppliers

The EAC model (currently being finalised through ASISA) should help to address the issues relating to effective disclosure.

If the asset manager tries to recover the cost of the rebate from the customer through a management fee then its product/fund becomes less attractive relative to the platform’s own funds.

Re 3.1.6 - Conflicts of interest arising from ownership or similar arrangements and relationships between intermediaries and product suppliers
We agree with the concern where cross-ownership between advisor firms and product suppliers influences advice (inappropriately) through indirect benefits or profit-share arrangements between the entities concerned. See our further comments under proposal N.

We agree with the comments regarding bancassurance models and would suggest that they incline towards “tied” advisor forces as set out later in the RDR discussion document.

Re 3.1.7 - Disclosure standards may not be adequate

If nothing changes at the structural level, then we agree with the comments about disclosure potentially not being adequate. However, if proposals iro structure are implemented and there is an effective ban on certain behaviours and/or practices, then we think that disclosure should be fair and appropriate as it stands.

Re 3.2 - Risks to intermediary sustainability

Re 3.2.1 and 3.2.2

We agree with the statement about the risk that advice is not valued as it should be by consumers. And, this has a wider impact than that referred to in the discussion paper. A widely held fear amongst advisors is that if there is simply a change to the remuneration structure and if customers are not brought along on this journey then they will take the easy option and will not want to pay for advice, and therefore not buy any advice. In our view therefore, there is work to be done on both sides – advisors being able to articulate the value that they add (especially in the advice space) and customers being able to understand that there is a fundamental change proposed in the way they pay and for what. This is complicated by the fact that many customers are quite comfortable paying for what they get through the commission structures.

Re 3.2.3 - Up-front commission system does not support a sustainable business model

An upfront revenue model for a long-term service obligation is problematic. Therefore we support the objective of trying to build value in a financial advisory business through an annuity income stream that can be sold as a going-concern, creating value in the business and enhancing business continuity and succession planning. There are practical issues that need to be overcome – not least of this is the reality that, depending on the mix of revenue in an advisor’s business, there are cash-flow issues linked to transforming a business. There is also the fact that the flow of ongoing revenue in almost all cases is currently linked to the existence of a broking contract between advisor and product supplier. This means that the ability to successfully sell and transfer a business as a going concern is dependent on product suppliers playing along. Our experience is that this is not a given.

Building a business involves building a customer base and looking after the revenue streams linked to those customers. We support the contention that ongoing revenue helps to promote the development of long-term customer relationships. Ironically, despite the upfront nature of remuneration linked to life insurance business over the last 30 years, many advisors have built solid long-term customer relationships – to the point where many of these business relationships have turned into personal friendships. In these cases, the relationships were built more on trust and appropriate advice than on the way the advisor was paid for the advice and/or product.
Re 3.3. - Risks to supervisory effectiveness

Re 3.3.1. - Imbalances in responsibility of product suppliers and intermediaries for customer outcomes

Just as there is a responsibility on advisors to “know your customer” we agree that there should be some responsibility on product suppliers to know the advisors with whom they do business. We would be cautious about placing too much responsibility on product suppliers to monitor advice and distribution outcomes – the responsibility needs to be reasonable in relation to the control that they can exercise over someone who is not acting as their agent. Representing IFAs, we would be concerned that companies take the view that the liability or risk (financial, reputation, admin, control) in dealing with independent advisors is not significantly less than having a tied force. If this is the case, we fear that they will take the business decision of not wanting to do business through independent channels and, in our view, this cannot be good for the market – customers, advisors or product suppliers.

Having said this, we believe there are easy ways to introduce reasonability checks that can go some way to address the concerns expressed by the regulator. One could look to the types of checks that are already in place in the FICA-related responsibilities.

On p25 reference is made to “… commissions, … exacerbate(ing) this imbalance by enabling product suppliers to incentivise intermediaries for volume-based product sales, with insufficient concomitant accountability in relation to the quality or outcomes of the sales process from a customer perspective.” Since long-term and short-term insurance commission is regulated (at the maximum) and Conflict of Interest Regulations are in place, there can be no additional incentive to advisors for placing volumes of long-term and short-term insurance business with one supplier over another. Spreading business equally around a number of suppliers versus placing all business with a single supplier will not lead to any more commission being paid to the independent advisor placing the business.

Re 3.3.2 - Fit and proper standards for intermediaries not always supportive of financial inclusion

We note and understand the regulator’s hesitance and concern in “regulating through exemptions” to apply the regulatory and supervisory framework proportionally and also to prevent unreasonable barriers to entry. One way of dealing with this is to recognise the different category or types of operators/players in the industry and set the rules/principles for each. The danger of course is arbitrage between category or types of operators with players trying to find the “best” rule to follow. Another danger is to try to get a one-size fits all approach, which by its very nature has unintended consequences.

Re sections 3.3.3, 3.3.4, and 3.3.5

We agree with the risks/concerns expressed under these sections. We recognise the inconsistencies, overlaps, confusion and regulatory arbitrage that comes with having various pieces of regulation and legislation applying to a single industry. We therefore welcome attempts to get to a single/level position where these issues are ironed out.

3.4. Benefits of the current landscape

3.4.1. - Customers may be more willing to seek and obtain advice if they think it is for free

As part of the feedback we received from Masthead advisors, they asked: “Is commission really an issue? Is the separation of activities and who pays for what a real issue?
Ultimately, the customer is paying for the commission paid over – all product suppliers are simply collecting and paying across. So, is commission the real issue?”

One must not underestimate the resistance of customers to pay explicitly for advice. It is not something they have been used to. It is not unique to the SA landscape – it is an international issue. The solutions to the right problems should therefore be carefully considered. There are definite benefits to the existing system and, in most situations, the system works. Despite the system working and even if customers have thought this is for free, there is still a massive shortfall of insurance and savings in this country.

Data presented in National Treasury's discussion document\(^1\) shows little increase in the usage of financial products.

<table>
<thead>
<tr>
<th>Financial Product Usage Levels (% adults using a particular service)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Year</strong></td>
</tr>
<tr>
<td>Transactional account</td>
</tr>
<tr>
<td>Insurance</td>
</tr>
<tr>
<td>Credit active consumers</td>
</tr>
<tr>
<td>Savings</td>
</tr>
</tbody>
</table>

(Source: FinScope Survey and NCR credit market report (2009 to 2014))

Figure 6

In contrast, international evidence has shown that a positive customer experience in one market segment motivates the customer to try other products. In Figure 6 we don’t see this happening in South Africa, especially across savings and insurance products. Whatever the reason, it’s cause for concern. We therefore feel strongly that any change in remuneration structure should help to drive these numbers up – put another way, it can be a key measure of whether the change has worked.

We welcome the comment that any new system should cater for various ways that customers can pay for advice. Having said that, we fully expect product suppliers to provide limited options and trust that these are sufficient.

**Re 3.4.2 - Commission cross-subsidisation generally works in favour of low-income customers**

We note the comments in relation to cross-subsidisation, but are not sure about the relevance of linking this to commission being paid by suppliers. Our research and calculations show that it costs on average ±R3,000 upfront for an advisor to take on a new customer (that is without a profit margin). And, they don’t generate R3,000 of commission or remuneration upfront on ever new interaction. Therefore, the very nature of the business is that there will be an element of cross-subsidisation, but it’s at the customer level rather than the supplier level. It would be an ideal business if all customers were profitable in their own right. We fear that if that were the objective, advisors would be looking to migrate

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upwards and those “unprofitable” customers (who could be low income customers) would be abandoned. This would not be good for them or the advisor. This certainly doesn’t play to the broader objective of increasing access to advice.

Re 3.4.3. - Ease of administration

This is a key part of any new system and, given the position taken in the paper on the need to have mechanisms that allow for the easy collection of advice fees, has allayed some concerns of advisors who thought they may need to introduce invoicing and fee collection processes.

Chapter 4:

We think the paper is comprehensive and well set out. Overall, we support the objectives and the rationale for the changes. We are also encouraged by and have faith in the consultation process.

There is still detail that must be resolved on a number of issues (commission rates being one of the more important ones for financial advisors) and therefore our commentary in these areas is limited. We have a range of questions that are unanswered at this stage and which we’ve highlighted through our feedback on specific proposals.

The words of the Australian Minister for Finance (see Figure 7) resonate with us – also, sometimes the more rules and regulations there are, the more imagination one sees in people trying to work around them. But rules are necessary and so we support regulation that is appropriate (ie. it addresses a need or a concern), is cost effective to implement, and is easy to administer or follow.

We also believe that successful and effective regulation involves a balancing of roles and responsibilities of at least 4 key players – those are the customer, the regulator, the product supplier and the advisor. If there is an imbalance in responsibilities of one party relative to the others then, like a table (see Figure 8) with one leg too short or too long, the system will be out of balance. That will have a negative impact and impede success.

We accept that there are clear needs and concerns in our industry that should be addressed. In the context of this RDR paper we’re not sure about the cost of implementation and we have questions about the ease and practicality of administering some aspects of the proposals (eg. the expectation that product suppliers will check adherence to fee guidelines).

We’re concerned in so far as we see regulation appearing to be put in place for the exception, the outliers (eg. replacements, s14 transfers, juristic reps). We believe that one should regulate for the rule, and sanction for the exception. As part of our assessment of this paper and the proposals, we are looking to the regulator to
intensify supervision and impose meaningful sanctions. In our view this is key to successful implementation of the proposed measures and achieving the objectives. We submit that the regulator has TCF at its disposal – this is the perfect tool to make an example … and nothing focuses the mind like a public hanging!

We are concerned that there are a number of proposals that appear to be a one-size-fits-all approach. The problem is that they create unintended consequences and tend to throw the good out with the bad. Examples of these are: Proposal N (disqualifiers for being an IFA); Proposal Y (rep on two licences); Proposal Z (outsourcing of investment functions); Proposal MM (banning commission on investments); Proposal NN (life risk commission); Proposal OO (replacements); and Proposal QQ (s14 transfers). Having said this, we do see the regulator looking at different approaches in respect of low income and direct operators and we welcome this.

Our last general comment relates to education and awareness of consumers. RDR is proposing a fundamental change in the way customers will be expected to interact and pay for advice. We think that as an industry, and in the build up to a fee-based (partially or wholly) world, we should be publicly promoting financial advice and the benefits of that advice. We would suggest a PR and/or advertising campaign driven by the FSB, but with all of industry involved. In a way, we need to get customers looking forward to paying for advice. An example of something that can be done is what the FSA did in the UK with its Consumer Guide to RDR² (published in August 2012).

In closing, we know that we are a nation that is under-insured, under-saved and where most retirees don't have enough retirement provision. We believe that an advised customer is better off than unadvised customer. As such, we as an industry need to do what we can to ensure appropriate advice is available to customers.

For us a measure of success is to see whether there are more customers who have increased their financial security through appropriate advice and with appropriate financial products in place. And, customers need advisors to help them with appropriate advice and appropriate financial products. In fact, it's a symbiotic relationship between customer and advisor. That's why we've mentioned a number of times through our feedback, that we are very willing to participate in working groups as needed.

Chapter 5:

We’re comfortable with a phased approach to implementation. We’d also like to see some sort of timeline in respect of what many financial advisors regard as the big-ticket items (life risk commission, short-term commission, advice fees). From a decision and a planning point of view, the sooner they get the detail, the sooner advisors can take considered and appropriate action – whether that is staying in the industry and adapting or whether it is leaving and finding something else to do.

Reference is made on p65 that “an implementation period of approximately 12 months will be provided for from the date of the finalisation of more detailed proposals”. It's difficult to

² [http://www.fsa.gov.uk/advicechanges](http://www.fsa.gov.uk/advicechanges)
comment on whether this is sufficient – it’s the impact of possible changes that influence the view and therefore we would be in a better position once the details emerge. At the stage though, we would respectfully request that consideration be given to a transition period of at least 2 years after the date of promulgation.

We understand the need for urgency in relation to some of these proposals, but suggest the proposal in relation to replacements (proposal OO) is inextricably linked to proposal NN. Given our view, we’re not sure that a decision about the one can be taken without knowing the detail of the other. We would therefore urge a rethink in relation to implementing the change regarding replacements as proposed in the shorter term. As indicated in our feedback under proposal OO, we believe that there are mechanisms open to the regulator to address what is seen as inappropriate replacement activity. Further, given the other proposed changes in the shorter term in relation to conflicts, we think the risk is in any event mitigated.

Chapter 6:

In this chapter there are 14 measures set out that the proposed changes seek to achieve and we support them. However, we have a comment in relation to the 9th measure listed – the one that refers to “the impact of adviser remuneration on reasonable benefit expectations, particularly through eliminating the justification for penal early termination charges and inappropriate product replacements”. The impression appears to be that the cause of penalties is adviser remuneration. It was recognised as far back as 2006 that the cost of commission as a proportion of total charges is significantly lower than figures provided in submissions received from the Life Offices’ Association (LOA) to the FSB and National Treasury (in June 2005). At that stage the LOA calculated that commission accounted on average for 35% of all costs across endowment policies and retirement annuities.3 We therefore wish to reiterate that advisor commission/remuneration is but one of the charges in a policy and therefore but one of the causes that impact penalties and benefit expectations. Addressing reasonable benefit expectations can therefore only be done by viewing the full value chain.

3 National Treasury discussion paper on Contractual Savings in the Life Insurance Industry - March 2006, p8
**COMMENTS ON SPECIFIC RDR PROPOSALS SET OUT IN CHAPTER 4:**

**Proposal A:** Forms of advice (financial planning, up-front product advice, on-going product advice) defined, with related conduct standards.

Comment:

If “financial planning” is the only type of non-product advice catered for through RDR, then this may be problematic. There are many advisors who might not meet the standards to be a “financial planner” (if that term is to be defined in regulation), but they give both personal financial advice and product advice. They are not just product floggers. They follow steps of advice (probably even the 6-steps of financial planning) and they give product advice. As rightfully pointed out in the paper, most financial planners affiliated to the FPI provide product related advice too.

We would therefore suggest an additional form or type of advice is recognised, namely “personal financial advice” and that there are standards linked to these – these standards could be those of ISO TC 22222:2005. Masthead is happy to be part of defining these.

**Proposal B:** Standards for “low advice” distribution models.

Comment:

The trick here will be to define what are “low advice” distribution models. If they are not clearly defined, one runs the risk of persons arbitraging different distribution models to find the easiest outcome. We welcome the tightening of standards in relation to direct sales operators (call centres) because we feel that many customers are sucked into these through smooth advertising of great paybacks or other incentive deals, often at the expense of a proper explanation of the product that they’re really buying. In addition, given that they claim to be “information givers” vs “advice givers” they avoid the regulatory requirements that advisors need to comply with in relation to replacements.

**Proposal C:** Standards for “wholesale” financial advice.

Comment:

Nothing to add.

**Proposal D:** Standards for sales execution, particularly in non-advice distribution models.

Comment:

We are comfortable with the approach suggested. Refer also to our comments under proposal B.

Consideration should be given to traditional face-to-face advisors who may, in relation to a range of products, wish to offer some sale in execution services. Would they be treated the same as more traditional direct sales execution-only models?
Proposal E: Standards for ongoing product servicing.

Comment:
We are happy with standards being defined. As part of this, we would be cautious that there are not expectations placed on advisors that should more rightfully be placed on product suppliers. Where there are such expectations then it would only be right that the product supplier compensates the advisor on the basis that it is an outsourcing of functions.

We agree with specific standards being required in respect of premium collection and wonder whether the existing requirements that an FSP that receives/holds client funds aren’t sufficient.

With reference to the activity-based model (on p28 of the paper) we submit that premium collection is an activity performed on behalf of a product supplier rather than an activity connecting customers and product suppliers.

Proposal F: Insurance premium collection to be limited to qualifying intermediaries.

Comment:
See comments under proposal E.

Proposal G: Revised standards for investment platform administration.

Comment:
We have no comments here.

Proposal H: Standards for product aggregation and comparison services.

Comment:
We are comfortable with the proposal.

Proposal I: Standards for referrals and lead generation.

Comment:
We’re happy with regulations here, but would be concerned if there are suddenly a number of people who become “subject to the rules of the game when they never had any intention of playing the game in the first place”.

An appropriate way to deal with this may be to borrow the approach that SARS follows when they distinguish between a person who buys and sells shares incidentally/periodically vs someone who deals or trades in shares. In the former case, the individual is not subject to income tax (as opposed to capital gains tax) because the buying/selling is incidental while in the latter, the trader is subject to income tax because this is his business.
Proposal J: Outsourced services on behalf of product suppliers to be more clearly identified and regulated.

Comment:
We support the ability of companies to outsource functions to a third party. We are also happy that increased and clear standards are defined in relation to these, as well as the proposed principles listed under the proposal. We do, however, have a concern with the reference to “… standards in relation to specific forms of outsourced services and associated remuneration …” with the specific reference to “associated remuneration”. If this means standardising remuneration we fear that personal differences (e.g. skill, experience, infrastructure) of the parties to whom the outsourcing is given, could be ignored.

Proposal K: Types of adviser defined: Independent (IFA), multi-tied or tied.

Comment:
We welcome attempts to create clarity and uniformity in respect of the status of advisors. We believe that this is a major step forward in simplifying things for customers. It should get us to a position where, “what the customer sees, the customer gets” (refer to comments under section 2.2.3 above and our reference to “Representative of Toyota” – in financial services, there was the famous UK example, backed up by extensive advertising, of “the Man from the Pru”) – see Figure 9.

We understand the reason for three labels/designations in the UK because we know that the FCA has backed up the three labels with three distinct definitions. Our RDR proposals are using the same labels, but our definitions are not the same. For example, we (different to the UK) are not expecting an IFA to be “whole of market”. This means that an advisor can offer less than whole of market, but more than the “one” or restricted set that a “tied” advisor can provide. In the UK, that’s a “multi-tie” and it places the advisor neatly between tied on the one side and IFA on the other (see Figure 10).

We submit that, given the differences between the UK and SA situations, one should collapse multi-tie and IFA into a single label. In this way, one effectively sits with tied on the one side and untied on the other and, for want of a better label, we would propose that this “untied” advisor go by the label “IFA”. A benefit of this approach would be that there are less definitions, rules and labels for the more creative boundary- pushers to play with. We believe that it would also simplify understanding for consumers – in a way it takes us back to when tied was a person representing a single product supplier (and proud of it) and untied was the “independent” broker. We suggest that it’s time to go back to those simple days – advisors knew what they were and customers knew who they were dealing with. Accordingly, and with respect, we suggest a
simplified set of advisor types. Our preceding comments should be read similarly in relation to short-term and health benefits advisors.

We have no additional comments with regard to financial planner except in so far as we have already commented and proposed the introduction of the term “personal financial advisor”.

We note the proposal suggesting that the regulator may re-designate an advisor from one status to another. We are not sure how this would happen in practice, but suggest that consideration could be given to some declaration annually, based on agreed criteria/standards.

We believe that if an individual can act as an IFA in some respects and a multi-tie in others (refer proposal L), it simply provides more confusion for customers. Therefore it does not, in our view, support the objective (stated on p9 of the RDR paper) that enables customers to adequately “understand and compare the nature, value and cost of advice and other services intermediaries provide”. We believe our suggestion therefore supports our position that these two labels should be collapsed into one.

**Proposal L:** An IFA may advise on certain products on a multi-tied basis.

Comment:

Given our comments under proposal K, we have nothing to add here.

**Proposal M:** Further input required on criteria for IFAs to offer sufficient product and product supplier choice.

Comment:

We are really nervous about trying to run the numbers game – it potentially creates something artificial in that it can cause people to feel they “have to offer something” so they don’t lose their IFA status. Therefore, our initial feedback here should be read as being based on our experience with independent advisors and what works for them and customers. Choice, variety or numbers is only one side of the IFA label – the aspect of control or influence may be even more important and should therefore be dealt through proper disclosure.

Re bullet 1: There is nothing wrong with an IFA deciding to specialise in a particular area (eg. planning for retirement or planning at retirement). So, independence is not linked to the breadth of services. Specialists, by definition know more about less, and the narrowness of their offering does not make them less independent.

We believe IFAs (who set their stalls out as personal financial advisors) should be able to analyse the general financial needs of customers and provide solutions to meet these needs. They should be able to advise on everything that deals with types or categories of needs/objectives and/or concerns that customers have – eg Retirement Planning; Investment Planning; Liquidity Planning; Building and protecting wealth; general risk analysis relating to personal assets (personal lines short-term insurance); commercial (short-term insurance) risk analysis.
As such, advisors should be able to provide a broad range of commonly available life and non-life products that fit the categories or disciplines within which they choose to operate.

The breadth of what an advisor can offer will be spelt out on his FSP licence and form part of the disclosure to customers.

Re bullet 2: No limit

Advisors should be able to discuss options with customers. So, typically in the investment world, an advisor should be able to talk about life-wrapped and non-life investment vehicles and be able to recommend that one that is suitable for the needs of the customer.

Re bullet 3: We don’t quite follow the question here. It may be covered in responses below.

Re bullet 4: No, if the advisor offers LISPs, direct UTs, life-wrapped investment products and more liquid investments like bank deposits, that should be sufficient.

We do not see a need to offer direct shares or the need for specialist or structured investments. If the advisor does this, it’s another string to his bow and potentially a differentiator or competitive edge for that person.

Re bullet 5: We don’t see much point in offering more than one investment platform, subject to it being able to provide sufficient fund choice, admin capability and competitive pricing. If it falls short, advisors can look to add a platform.

Asking one to estimate the range of investment portfolios or portfolio types available on such platforms is almost an impossible task – how long is a piece of string? The number of funds offered should be able to cater for the needs relative to the advisor’s customers.

Re bullet 6: We would support advisors creating a house view – this is effectively deciding who they want to do business with. It’s like a panel and they should use criteria to help decide, things like: regulated vs unregulated, company/brand, product range (features and benefits, pricing, etc), service (ease of doing business, claims ratio, after-sales service) and relationships (responsiveness and access to management, personalised support provided, respect for relationship between advisor and his customers).

If advisors stick to mainstream product suppliers we don’t see the need to do deep financial or actuarial due diligences. Taking a lead from the office of the FAIS Ombud, we think they can take “judicial notice” of the main, established and regulated suppliers.

Subject to nothing unusual happening, we don’t see any need to review more than annually.

Re bullet 7: Life products are largely commoditised. There are very few real differences between the life cover products of one insurer vs another. Premium rates tend to fluctuate amongst advisors with no clear cheapest or most expensive.
Therefore, we don’t see the need for more than 3 main suppliers. Where the advisor works specialised markets, he may want to add a niche player or two.

Re bullet 8: The problem in the short-term market is that product suppliers look to book size and underwrite or rate premiums accordingly. Therefore, spreading business too wide isn’t a good thing for customers of the smaller independent brokers.

We would say that for personal lines, one lead short-term provider and a secondary one plus perhaps a niche provider or two, depending on the market and customer needs, should be sufficient. For commercial short-term insurance, there may be more providers, depending on areas of specialisation relating to the types of businesses the advisor is advising.

We believe that in the short-term insurance world, it is less about the breadth of provider choice and more about the independence of the advisor – on whose behalf is he acting and is he under the control of the product supplier?

Re bullet 9: We understand that the Health Service Benefits is relatively small and therefore, in our opinion having two main providers should be sufficient.

Re bullet 10: No role at all.

Re bullet 11: Maybe an annual declaration of sorts. In addition, but this links to standards, the advisor should stay up to date with the product suppliers and the products he offers.

**Proposal N:** Criteria for IFAs to be free of product supplier influence.

Comment:

Specifically in relation to the bullet points under this proposal, our comments are set out below:

Re bullet 1: If the agency is with more than one supplier, then maybe there is no reason why this should disqualify the advisor.

Re bullet 2: Agreed. The difficult one is where “targets are imposed” on IFAs outside their control – e.g. a supplier that requires minimum production in order to keep a broking contract open. We believe that this practice, which is widespread, should be addressed as part of RDR. One implication of the cancellation of contracts is that where an advisor has put his customer into a product (appropriate and in the interests of the customer) and then has his contract cancelled, he is unable to perform his duties in relation to that customer. An additional implication is that any ongoing trail fees are cut off, and in the new world, we would suspect that the product supplier would stop collecting any fees on his behalf. At the very least, we would advocate a system whereby product suppliers create a facility for advisors to be able to continue to service their customers without them having to commit to new business.
If there is a target imposed on them, we would suggest that this does not become a disqualifier for an advisor to be regarded as IFA.

Re bullet 3: We don’t believe that the mere existence of an ownership stake creates product supplier influence. As such, we do not agree that it is an appropriate “disqualifier” to be an “IFA”.

Shareholding on its own does not create the conflict or bias – to effectively deal with this, we would suggest that there is a piercing of the corporate veil – get behind the structure and the relationship and determine whether there is real bias or conflict. We would suggest that there are mechanisms to address this – disclosures, annual returns, declarations by directors. We would also caution against trying to regulate or control every situation where there “may” or “possibly” (however unlikely) be some adverse or undesirable consequence. To manage this or write regulation in such a way that all of these “possibilities” are covered is almost impossible and will result in a number of unintended consequences. It means that the regulations need to be drafted so widely that a number of really good, solid and bona fide relationships and structures are negatively impacted just because a few have “pushed the boundaries”. It would also put pressure on supervision by the regulators. In our view, take these transgressors out with a sniper rifle rather than a shotgun.

We submit that this type of rule would take out or exclude what are very clearly IFA businesses. The way to address, rather than through a single rule disqualifying an advisor is by an individual review of the relationship.

Re bullet 4: We have no comment here.

Re bullet 5: Agreed, but surely if there is any chance that an adviser “earns” more remuneration from one or other product supplier this also needs to be disclosed.

Re bullet 6: Agreed.

Re bullet 7: In general, we agree with this comment subject to our previous comments in respect of product standards or targets imposed by product suppliers as a condition for a broking contract. We would suggest that the words “... or could be seen to be influenced ...” included as part of this proposal creates too much vagueness. We submit that whether the adviser is influenced by the product supplier is a question of fact. And, most probably something that can easily be verified. As a pre-emptive measure, we suggest that this is dealt with as part of the disclosures, not only to customers, but as part of an advisor return to the regulators. There is either influence or there is not and therefore, in writing any regulation, we strongly suggest that words/phrases like this are specifically excluded.

Re bullet 8: In principle, we agree, subject to the “choice” criteria in order to qualify as an IFA being reasonable.
Proposal O:  Status disclosures to be made by IFAs.

Comment:

We are comfortable with the first 2 bullets in terms of disclosure. However, we believe that the third disclosure proposal goes too far. Giving details of what was sold may not be relevant disclosure and could be misleading. We therefore question whether it contributes to a more informed customer – eg. if an advisor declares having sold/recommended only one company’s products over the last 12 months, a customer could conclude that this advisor is more tied than IFA. But, if the advisor works a particular segment of the market (eg. small businesses, self-employed people or medical professionals) he could have recommended the one supplier because it is best of breed or a clear leader in the field. However, to get this message across to customers so that they are fully informed involves more information and potentially more confusion. We therefore submit that this piece of the requirement is not necessary and should be scrapped.

We do however believe that there is place for disclosure in relation to product supplier and products, but could be dealt with in another way – we submit that the advisor should be able to show how and why he does/did business with the chosen product suppliers. He could do this by creating a house view and showing the process of due diligence that was followed to help decide on the suppliers and/or products he decided to carry. We would be happy to share thoughts on the creation of house-views and the types of issues to be dealt with as part of a due diligence.

Proposal P:  Criteria for multi-tied advisers.

Comment:

We have made our point about multi-ties and do not believe there is a place for this designation. To the extent that the regulator disagrees or that there is acceptance to a collapsing of IFA and multi-tie labels into one “untied” label, we agree that conflicts should be managed. However, we would caution against more and irrelevant admin that just increases the burden of bureaucracy on advisors.

Proposal Q:  Status disclosures to be made by multi-tied advisers.

Comment:

Adding to our submission above, reference to “tied” relationships in respect to multi-tie seems contradictory. Again, refer to our previous comments in this regard. Despite these, we believe some of the points of disclosure apply equally to IFAs and tied advisors. We do not, for reasons set out above, support the types of disclosures suggested in the last two bullet points.

Proposal R:  Criteria for tied advisers.

Comment:

We agree with first part of the proposal, but not the second piece that states that a person who is not a tied advisor is a multi-tie. If the intention is to do away with general agency and
therefore the ability of the traditional tied agent (company representative) to sell the products of another product supplier, there would be no need to provide for multi-tie.

While we generally agree with the concept of tied as proposed, we want to flag an issue in relation to existing “general agents”. If a tied advisor is limited to his own company’s products, and the Long-term Insurance Act is changed to prevent product suppliers from having broking agreements with other product suppliers, how does one cater for the servicing and ongoing support of customers who have purchased such products from these tied agents? We suspect that multi-tie may be the answer, but are not sure that it meets the need.

In respect of investments, it’s a little more tricky what with access to a range of funds through LISP. Should a tied advisor who is restricted to his company’s investment platform still be able to have access to a broad range of funds, even though these are not the funds of his company? It is in the interests of his customers and helps to diversify their portfolios, but it may be perpetuating a grey area between tied and independent. Whichever way, we feel strongly that there should be clear disclosure so that the advisor does not appear to be independent.

**Proposal S:** Status disclosures to be made by tied advisers.

**Comment:**
We agree with the proposed disclosure standards.

**Proposal T:** Criteria for financial planners.

**Comment:**
Generally, and subject to our earlier comments regarding financial planner versus personal financial advisor, we are comfortable with this proposal. We agree with membership of a professional body, but we would caution against an exclusive arrangement whereby only one organisation is the designated body. We believe that it should be open to any organisation meeting the necessary requirements for a professional body (as set out by SAQA) as well as the requirements laid down in terms of these and other appropriate RDR proposals.

**Proposal U:** Status disclosures to be made by financial planners.

**Comment:**
We agree with the proposal and submit that this is appropriate in relation to “personal financial advisor” too.

**Proposal V:** Insurer tied advisers may no longer provide advice or services in relation to another insurer’s products.

**Comment:**
Agreed – see earlier comments re status and disclosure.

We note the reference to the Long-term Insurance Act and point out that these general agency agreements have also been applied in relation to short-term insurance, where a
tied distribution channel of a long-term insurer (with a short-term insurer in the group) has entered into a broking agreement with another short-term insurer. Are we correct in assuming that the intent of this proposal would be to prevent these types of arrangements too?

The ability to earn ongoing remuneration (it would probably apply mainly to short-term insurance situations) is dependent on a broking agreement between an FSP (in this case product supplier A’s internal tied agency distribution channel) and a product supplier (in this case the product shop or the broker distribution arm of product supplier B). So, one question would be what happens to the ongoing remuneration? Logic says that the remuneration stops? This broking agreement also needs to be in place to provide ongoing advice in so far as changes on the products need to be made (eg. change in premium, risk cover, etc).

Therefore, we are concerned about what happens to customers who have been sold products of one of these other insurers by a tied agent if he can no longer advise or service that other insurer’s products. The product advice hasn’t become inappropriate simply because the advisor no longer has access to the other brand of product. And, we wouldn’t want the products to be rewritten because of access or remuneration.

Consequently, in our view, some provision should be made for tied advisors to be able to service those products and support those customers – we would suggest that one can allow a situation where no new business may be conducted with another insurer but the tied advisor is able to continue to service and update or change on that other insurer’s products that are in place at a given date. In order to avoid the rush, we would support the regulator applying a date “in arrears” similar to the way regulation relating to sign-on bonuses was applied. This approach would be similar to running a closed book of investment business with a ring-fencing of this customer group.

**Proposal W:** “Juristic representatives” to be disallowed from providing financial advice.

Comment:

We have no issues with this proposal. We see no reason why non-advice sales execution operations should be dealt with any differently.

**Proposal X:** Standards for juristic intermediaries (adviser firms).

Comment:

We agree with most of the proposal and specifically with adequate and appropriate disclosure standards needing to be in place, irrespective of the designation of juristic or natural intermediary.

**Proposal Y:** Advisers may not act as representatives of more than one juristic intermediary (adviser firm).

Comment:

We understand the mischief that the regulator is trying to prevent but submit that there are unintended consequences of an absolute ban as proposed. We regularly deal with cases where it makes sense to be a representative on more than one licence. As such, if the
proposal were implemented, the consequences would be negative and severe and we cannot agree with this proposal. Here are four solid, bona fide instances where it makes sense to be able to be a rep on more than one licence and we believe that they should be allowed to do this:

1. Building experience – eg. in a small FSP where a rep wishes to add a licence category but does not have the necessary experience he needs to be a rep on another licence in order to do so.

2. Succession – for small FSPs (especially one-man FSPs) it is quite common for the owners to be registered as reps across two licences. In that way there is not a cutting off of broking contracts, commission can continue to flow into the business and there is continuity until the surviving rep can fully take over the business of the deceased.

3. Some advisors wish to run different parts of their businesses in two separate legal entities. They may ring-fence the business operations that are distinct for accounting, risk, and tax reasons. Or, they may have a partner in respect of short-term business, but be alone in a long-term and investment business and they want to keep the businesses separate.

4. Advisors may want to transition or move customers into a new entity (perhaps as advisor, they have moved, or they have bought a business). To do so over a period of time, they need to be on two licences.

As an alternative to an outright ban, we would suggest that the mischief is dealt with on a case-by-case basis. The regulator has a list of all representatives across all FSPs/advisor firms and therefore could cross-reference individuals who are representatives on more than one licence or advisor firm. Each FSP/advisor firm can be called upon to explain the need/rationale for such. The regulator can then decide to approve such situation or not. Advisor firms could then make an annual declaration in which they explain the continuation of such a status.

Two other considerations may be (1) limiting the proposal to tied advisors or (2) allowing reps to be on other licences as long as there is no overlap in respect of licence categories (although this would not cater for the situations described in examples 1 and 4 above).

If the proposed ban were implemented (and we see the intent is to do so sooner rather than later) then we wonder how one would deal with those reps who currently do, but would no longer be able to act in this capacity. There is an expectation on advisors to provide ongoing service and to service the products that they put in place. An impact of such a ban may be that advisors can no longer service policies or keep them up to date because they can no longer access the licence through which the product was written. One doesn’t want advisors in this space to respond by switching or replacing the business.
Lastly, in Figure 11 is a view from an advisor of the types of discussion that have already started in relation to this RDR proposal, which gives an insight into the creativity that goes into finding ways around rules.

**Proposal Z:** Restricted outsourcing to financial advisers.

Comment:

We recognise that there are possible conflicts which could lead to an intermediary being biased and not acting in a clients’ interests but there must be ways of dealing with this other than an outright ban. A complete prohibition on this may limit good arms length business arrangements – eg. a small start-up asset manager looking to enter the market. We believe that this proposal may hamper competition and favour the bigger players.

We believe that the regulator can deal with this through disclosure. At least this way it’s in the open and everyone knows what we’re dealing with.

**Proposal AA:** Certain functions permitted to be outsourced to financial advisers.

Comment:

In addition to those activities listed under this proposal, we would suggest that there are a number of admin functions performed by advisors on behalf product suppliers - eg. capturing of applications online, changing customer details online (in fact, anything online that goes straight into the product supplier’s systems). To the extent that it can be monitored, we also believe that advisors should be able to be compensated for the printing that they undertake on behalf product suppliers. Then, there is the contentious issue of work that needs to be redone because someone has not done it right the first time – simple things like having to send documents in again because there is no trace of the first batch or an advisor having to go back to a customer because not all the requirements expected by the product supplier were set out the first time. Advisors are never compensated for duplicated effort. In Figure 12 is the sentiment expressed by one advisor in relation to the admin he’s expected to carry. This admin burden on independent advisors is even greater in the *platteland* for many product suppliers have slowly and systematically withdrawn admin offices from these areas. The result is that often the independent advisor becomes the contact point on behalf of product suppliers – they are the entry point to the company.

Think of it. We do most of the admin. Printing and costs, we carry most of the expenses. We phone call centres and sit hours on phones. We do lots of changes to existing policies like address changes, banking changes, beneficiary changes, claims etc. What is the company’s contribution? They sit and wait for fully completed documents the way they want it and we as their marketers must run round like ants to get all done - to put the cherry on the cake then companies even call our clients ie when a policy matures and say to clients we can help you OR you can call your broker. Why not call the Broker and ask if the Broker can’t do any then offer their services?  

Figure 12
**Proposal BB:** Product supplier responsibility for tied advisers.

Comment:

We see no problem with this in relation to tied advisors. The principle of vicarious liability is well-established in our Law of Delict.

**Proposal CC:** Product supplier responsibility for multi-tied advisers.

Comment:

Since we don’t believe in the need for multi-ties in our industry, we submit that product suppliers’ responsibilities should be split between what is reasonable for them to pick up on behalf of tied advisors vs independent ones.

**Proposal DD:** Product supplier responsibility for IFAs.

Comment:

We see no problem in relation to product accreditation and ongoing knowledge testing relative to independent advisors. Advisors are quite happy to go through this, because they know that they will "carry the can" if there is a customer complaint re advice – in fact, since they are the first port of call for all queries from customers, they are generally contacted first even if the complaint is about the product or the product supplier (see comment in Figure 13). Also, it is reasonable to expect that suppliers provide and advisors accept their respective responsibilities.

We submit that the suggestion that product suppliers monitor adherence by the IFA to the guidelines for advice fees is not practical – there are just too many uncertainties that would place an unreasonable burden, in our opinion, on product suppliers. This suggestion also raises the question whether the fee guidelines are prescriptive or merely guidelines. If they are the former, then suppliers would find it difficult to monitor and if only guidelines, they would effectively have nothing to say.

We also battle to grasp, at a practical level, how product suppliers would reasonably monitor and assist in resolving customer complaints relating to IFAs. We submit that this would compromise the nature of independence of the advisor and further, advisors would not take kindly to “being checked up on”. At the very heart of their independence is the fact they are not under the control of a product supplier.

We don’t believe it is reasonable or practical for product suppliers to pick up too much responsibility in relation to someone who is, by definition, independent and is acting as agent of the customer and not the product supplier. As stated earlier in our feedback, if there is too much responsibility placed on product suppliers relative to the control they can exercise, we fear that they will choose to pull back from the independent advisor market.
with the result that independent brokers, as we know them today, will be squeezed out of the industry.

**Proposal EE:** Product supplier responsibility for non-advice sales execution.

**Comment:**
We agree with the proposals and would add that as the actions/behaviours of call centres look more and more like advisors, they should be subject to the same responsibilities.

**Proposal FF:** General product supplier responsibilities in relation to receiving and providing customer related data.

**Comment:**
In the first paragraph, there is reference to “customer related data held by intermediaries and outsourced service providers”. However, there is no distinction made between intermediary/advisor acting in that capacity and an outsourced provider (eg. a binder holder). We’re not sure whether the regulators intended to treat both the same for purposes of this proposal. If not, we’re comfortable. But if the intent is to treat both the same for purposes of this proposal, then we would be worried about more admin obligations being cast upon advisors.

There are suppliers who refuse to give customer information to independent advisors if those advisors do not have broking contracts with them as product suppliers. This happens despite the advisor having the requisite power of attorney or authorisation from the customer.

We note the comment that “standards may also take into account whether the product supplier is satisfied that the adviser concerned has the requisite product specific knowledge in relation to its products held by the customer.”

If in such cases, as is suggested in the proposal, “the product supplier will be required to provide the information to the customer directly”, we don’t see the reason why the product supplier should be the one to decide that advisors cannot receive this information when they are duly authorised. Despite this suggested obligation on product suppliers, we can foresee that they may take the view that the customer will not understand that information. We see this potentially as an opportunity for product suppliers to intermediate via their own tied channels at the expense of the independent advisor – in other words, while they may be compelled to provide information to customers (per the proposal), they will say the information is too complex to give the information directly to the customer, but that they will get a tied advisor to give it to them and explain it to them. This is already happening when independent advisors approach retirement fund administrators for fund values of their customers. As such, we are very concerned about the ability of an advisor to build a customer-focused business if product suppliers can effectively get between them and customers.

In reality the customer will, in almost every case, be less informed that the advisor. Therefore we submit that, if the advisor is duly authorised, the supplier should be compelled to provide such information directly to the advisor. From a customer perspective, we think that there are checks and balances in relation to advisors potentially going beyond their field of knowledge – they have a common law duty of care to their customers and they
need to comply with the requirements set out in the FAIS General Code of Conduct. So, if an advisor provides advice on products he doesn’t understand, the system will pick this up and their customers have recourse.

Therefore, we support some formal regulation that secures access to customer information. We, however, do not see the need to differentiate between the types of advisors here - if the advisor is duly authorised by the customer, then that advisor stands in the shoes of the customer in relation to that information.

We agree that all of this is subject to appropriate confidentialities.

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<tr>
<th>Proposal GG: Ownership structures to be reviewed to assess conflicts of interest.</th>
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<td>Comment:</td>
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<td>We are comfortable with a review of ownership structures with a view to reducing conflicts, while at the same time, we are wary of too cautious a view – by that we mean that if one tries to regulate to the degree that any possible conflict, intended or unintended will never materialise, then we think that the outcome will be too restrictive. We believe that there are checks and balances in the system that allow for good business while protecting consumers from conflicts and therefore a set of regulations that are too rigid will inhibit good business practice. We also point readers back to our comments in relation to proposal N as well as our comments under section 3.1.6 of our feedback.</td>
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<td>As Masthead, we would be happy to be part of the engagement process in a way that achieves a balanced outcome.</td>
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<tr>
<th>Proposal HH: General disclosure standards in relation to fees or other remuneration.</th>
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<tr>
<td>Comment:</td>
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<tr>
<td>We support appropriate disclosure of fees.</td>
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<tr>
<td>As far as standardisation goes, we caution against boxing things too narrowly – if standardisation promotes clarity and understanding we support it. Where it creates a one-size-fits-all approach, we are concerned that it may be too limiting.</td>
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<tr>
<td>We support the creation/production of a schedule of fee types or methods to be used by advisors – in fact, the simpler, the better. We also welcome the development of a fee guideline by the regulator after input/consultation with industry.</td>
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<th>Proposal II: Standards for financial planning / risk planning fees.</th>
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<td>Comment:</td>
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<tr>
<td>We support upfront agreement with the customer regarding quantum, or calculation basis and/or some type of estimate. For us, this is a logical part of the customer engagement process. We are not sure what is meant by “regulatory reporting obligations in respect to fees earned”. Does this mean that advisors need to report to the regulators about their earnings? If so, we would be concerned about the additional administration burden on advisors – with admin comes cost. And, for independent financial advisors, it’s already done through their annual submission of financial statements to the FSB.</td>
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We note the regulator’s intention to publish guidelines or benchmarks, but believe that there cannot be a one-size-fits-all approach. What’s reasonable in one set of circumstances may seem unreasonable in another.

As Masthead, we are willing to be part of the process in helping to shape these.

**Proposal JJ:** Standards for up-front and ongoing product advice fees.

**Comment:**

Our comments above in respect to proposal II apply equally here. In addition, the following:

We don’t follow the point under the 6th bullet that standards will be set in relation to “limitations on the extent to which advice fees charged may vary between product types”- is this not for agreement between customer and advisor?

With reference to reasonable and commensurate, who decides? What is one man’s reasonable is another’s unreasonable – by nature it is subjective. Financial advice/planning businesses can vary substantially in expertise, offering, experience, qualification, resources, admin, systems, time spent, and process followed. We therefore find it difficult to visualise a situation or structure that may sit and decide what is hypothetically “Reasonable and Commensurate Remuneration”. The person best positioned to determine value vs price is the customer. That’s why some customers are happy to pay for meals at a 5-star restaurant whereas others only want the value and price that a fast-food joint provides.

As input to the debate about fees payable by customers, recent research in the UK (done on behalf of findawealthmanager.com) shows that most investors will be happy with higher fees for stellar performance and unhappy with poor returns even if the fees are at rock bottom.

**Proposal KK:** Additional standards for ongoing advice fees.

**Comment:**

We are happy with the proposal.

In addition, we suggest that advisors are allowed to put fee agreements in place that bind customers to pay what was agreed. There is a concern amongst advisors that even with an agreement in place if the advice fee is collected in instalments by a product supplier, and the customer stops the product, the outstanding amount owed by the customer to the advisor is lost. Advisors know they have a legal right to claim this, but the admin and time required to chase debts is a concern.

We’re comfortable with the approach that if customers do not pay “the adviser may stop providing the ongoing advice” – we’d add to this that the advisor is absolved from liability too.

We support the principle of “opt out”.

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We believe the details of this proposal should form part of a customer awareness/education campaign driven by the industry players, including participation by the regulators in the rollout of change.

**Proposal LL:**  Product suppliers to facilitate advice fees.

**Comment:**

Currently it is a pre-condition that to submit business to a product supplier, there must be a broking agreement between an advisor and product supplier. We are comfortable with the facilitation of advice fees by product suppliers. This is a great relief for advisors who had visions of having to set up fee collection units in their businesses. In giving effect to this fee collection by product suppliers, the instruction by a customer has to override the terms and conditions of the broking agreement. The broking agreement cannot serve to prevent the wishes of two parties (customer and advisor) being carried out.

We understand that customers should be able to switch off fees to advisors … but only in respect of future fees for future work. If the customer is compensating the advisor (eg. for doing upfront work) on an instalment basis, where the instalments are collected by a product supplier, then the product supplier should not simply act on the customer’s request or instruction to amend or cease the deduction. Doing so may put the advisor out of pocket and effectively be a reneging by the customer on a deal agreed with the advisor. We’re not sure how to deal with this in practice, but somewhere the advisor needs to be part of the “request to cancel”.

As part of this proposal the regulator has sought comment on the possible range of fee deduction options which product suppliers should be required to facilitate. Our thoughts are as follows:

In respect of investments, there should be provision for deducting the following:

- a lump sum (upfront or *ad hoc*) to be paid from a new or existing investment,
- an ongoing fee linked to assets under management/advice,
- an instalment fee based on a rand amount to be collected over a defined period,
- regular rand fixed amount to collected over time.

In respect of life/short term risk products, there should be provision for deducting a regular amount per month – this could be a fixed rand amount (ongoing or for a fixed period) or a percentage of the premium. We believe that one can administer this similar to the way short term insurance works. In the example in Figure 14, the total payable by the customer is R1,100 pm, with R900 going to the product supplier for risk premium and the balance of R200 (advice fee + commission) being paid to the advisor. Currently short term is administered on a single debit order and works well. So, we don’t see the need for a second debit order.

![Figure 14](image-url)
We could also see this model working in relation to life risk business. It helps to keep the cost and complexity down.

As a last point under this proposal, we would request support from the regulator by helping to initiate and drive approval from SARS for the advice fees to be tax deductible for customers.

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<th>Proposal MM:</th>
<th>Remuneration for selling and servicing investment products.</th>
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Comment:
In relation to lump sum investments (irrespective of whether they are life-wrapped or LISP), this proposal is welcomed. In respect of non life-wrapped investments (direct unit trusts or investments through LISPs), this is effectively already in place. So, this is no big deal. And, what's more, the market has deregulated the commission/fee rates across the single premium investment spectrum. Very few customers are charged maximum regulated rates. Advisors would find themselves uncompetitive if they tried to do this.

We are not sure whether this proposal applies to regular premium investments – we ask this because in the preamble to proposal NN, it is stated that “commission regulations will be changed to consistently apply the same commission basis to variable premium increases on legacy products as is applied to new generation contractual savings policies”. Can we therefore read into this that the proposals under MM in relation to investments do not apply to regular premium savings products, but that they will be dealt with in terms of the changes introduced in 2009? If this is the case, we support such a move.

If however, this proposal applies to regular premium investments, we have concerns and therefore raise the following points:

- There are hybrid products – eg. retirement annuities that have a savings element and life and disability cover. Are these supposed to be administered separately?

- If there were no commission or fee paid for the introduction or facilitation of business to a product supplier, that product supplier effectively gets the business for nothing. In the investment world that means that they grow their assets under management (AUM) and they generate investment management fees and that influences their share price without paying for that business from an independent intermediary. This doesn't seem right in a free-market system. In an extreme view, it's like a cartel of product suppliers having the monopoly for contractual savings and investment products.

- We note the point about penalties on regular premium savings/investment products. However, commission is only one piece of the penalty. When the debate raged back in 2006/2007 about penalties on early terminations and which led to the signing of the Statement of Intent, it was shown/highlighted that commission accounted for only about a ¼ of penalty amounts in respect of on early terminations. We are not sure whether the implementation of the Statement of Intent has been successful. From our position, we believe that the customer is better off, even though there may still be room to improve.

- Commission rules were changed in 2009 – they effectively reduced the upfront commission component to 2½% of premium x term and made it subject to clawback from the advisor during the first 5 years. This means that the impact of commission on
the value in the investment (in so far as provision for penalties go) is even less than it was pre-2009.

- Cost reduction on a policy because of no commission. We would be interested to see whether this has as large an impact as asserted by product suppliers back in 2006/07 when the Pension Fund Adjudicator was making determinations on the destruction of value caused by the impact of penalties on early termination.

- If there is no significant reduction, in a way that there is a real difference, the addition of an advice fee to the premium will make the product more expensive than a current commissionable product and therefore customers will vote financially – they won’t buy investment plans like retirement annuities. They will be discouraged from investing and this has a knock-on the larger National Treasury initiative on retirement fund reform.

In the second paragraph of this proposal reference is made to product suppliers needing to show, after the changes, how they have reduced product charges in light of the prohibition on commissions. We agree with the point, but wonder whether there isn’t an unintended arbitrage opportunity created between old commissionable investment products and new non-commissionable ones.

As mentioned above, we are very comfortable with the approach in relation to single premium or lumps sum investments, but would urge a rethink in relation to regular premium investments. If this proposal applies to regular premium investments, then we submit that possible ways of addressing the concerns raised in the paper in relation to investments are as follows:

- Leave as is – after all, it was changed in 2009 to address the concerns.
- Limit the term for purposes of calculating commission, irrespective of investment term. This could apply in addition to the above point.
- Default to as-and-when commission.
- Deal with regular premium investments in the same way as proposed for life insurance.

Whichever method is finally proposed, we would be happy to be involved in further development work with the regulator.

**Proposal NN: Remuneration for selling and servicing life risk policies – mix of up-front commission and as-and-when service fees.**

Comment:

Principally, we support the concept of upfront plus ongoing commission. As previously submitted, the ability to build ongoing or trail revenue plays well towards creating capital value in a business. However, such a model does not come without its dangers. In our view two major keys to success lie in the numbers (level of commission) and the time period for transition available for advisors to be able to convert their businesses. For purposes of this proposal, we are not repeating our comments relating to how receptive or willing customers will be to paying advice fees (refer to proposals II through to KK), which fees should balance the total remuneration available to advisors in this life insurance space.

According to the ASISA stats for life insurance business for the year ending December 2013:
• Around 6.3 million recurring premium new business life policies were issued.

• Total premiums linked to these policies amounted to about R16.2 billion.

• Advisors (tied and brokers) were responsible for 55% of all recurring premium policies sold.

• Advisors (tied and brokers) were responsible for 83% of all premiums linked to these policies.

From these numbers we can see the importance of the advisor in the market, but still the average monthly premium in respect of these policies was ±R326 pm.

**Crunching the numbers**

Using current commission rates (at 3.25% x premium x term), the average recurring premium life policy (using a 20 year term) would yield upfront commission of R2,543, with a secondary payment in month 13 of R848.

Under a possible new dispensation the numbers start to look very different. If the commission rates stay at the current level, and assuming for the argument that it is this number that is split 50/50, then the upfront and ongoing commission amounts are calculated on just over 1.6% of premium. Again, using the ASISA numbers and averages, the upfront component comes in at R753 (with no secondary payment) and the monthly ongoing commission at R64. Assuming that the policy stays on books for the industry average (around 6 years), this R64 will have a buying power of around R48 in year 6.

An ongoing commission rate at this level is really low – to build a gross revenue flow of R20,000 pm will take 312 customers paying at this level. This will seriously impact many advisors and doesn’t look too favourable for attracting new advisors into industry. As we state further in this feedback (under proposal UU) in relation to short-term insurance commission, the rate or percentage of commission will be absolutely critical to the sustainability of small advisory businesses. At this stage, without knowing what rates the regulator is considering, we would suggest consideration of rates that are not less than the current investments/savings commission rates (ie. 5% split 50/50 upfront and ongoing).

An alternative to only paying a 50/50 split is to use a sliding scale – if the advisor takes 100% as-and-when, make the commission rate say 15% of premium (the equivalent of short-term commission), but if he chooses 50/50, make the upfront 2½% and the ongoing 2½%, similar to the current endowment and retirement annuity commission rates. As an additional suggestion, one could allow a continuation of a full upfront commission rate, but at a lower percentage. Because a model like this incentivises the ongoing remuneration structure, we would expect advisors to do the sums themselves and transition to such a model.

With reference to the proposal that the up-front commission component will be payable at the start of the policy only, based on the inputs we received, most advisors would prefer to keep the payment as is – iow, splitting the total commission (year 1 + year 2) into two payments, with ¾ in year one and ¼ in year two. This incidence of payment has positive cash-flow impacts and provides for good business planning.

Persistency or retention rates indicate that the business has stayed on books. In the industry it is a proxy for good quality of business. So, an additional comment or suggestion is that the regulator considers rewarding advisors who have higher persistency
or retention rates with perhaps a higher rate of commission maybe a bonus or “agterskot” for keeping business on books.

If this is not acceptable, then we submit that the ¼ top-up payment (in month 13) should, in fairness be added to the total commission payable at the start of the policy. This means that effectively there should be an increase in the rate of commission by the quantum of the top-up payment.

If this proposal is implemented as proposed, and all upfront commission is paid at the start of the policy, then we submit that it is only reasonable that the clawback period is reduced from the current 24 months to 12 months.

For us, there are too many assumptions relating to future escalations to base an upfront payment on them – eg.

- What if the escalation were on a life policy for maximum term (say 25 years). Is the commission on these premium escalations based on the expectation of increases for this entire period or is there an assumption that the policy will never reach full term?
- What happens to the clawback period in relation to the commission payments – does it last for the term of the policy?
- What if the customer keeps the policy in force, but the premium escalation is removed?
- Do pre-ticked premium escalation blocks lead to commission payable?
- A number of life policies these days are age-rated, which means that the premiums escalate as the insured customer gets older. Will these premiums be considered when looking to pay commission upfront?

We submit that a premium escalation is a decision and an advice event just as much as putting the policy in place initially. As such, it involves a review of the customer’s circumstances and an annual decision whether to do so or not. Generally, it is not a decision that can be taken years in advance. Commission payment should follow at that time.

One of the benefits of having small commission payments paid annually (subject to the premiums increasing) is that it creates a positive cash-flow impact.

Therefore, considering the above, we submit that rather than change the commission basis to include this in the upfront commission amount, we suggest that it is left as is. Let the customer decide and let commission only flow once the customer elects the premium escalation.

In our view, the main problem with premium escalations is linked primarily to the structure of most product supplier broking agreements that determine that commission flows to the advisor who sold the policy/product. This means that the commission follows the advisor who put the policy in place even if the customer has long since moved to another advisor. Even where the original selling advisor is no longer in the industry the commission is still levied against the policy – it may or may not be paid to another advisor. Most advisors would be happy to have this changed. They’d be happy to enable the customer to redirect the commission flow.

We have set out extensive commentary with regard to replacements in our views on proposal OO, specifically in relation to replacement vs churn and some of the drivers. We
whole-heartedly support attempts to minimise mis-selling and we note the regulator’s reference to “voluminous anecdotal evidence” of upfront commission driving mis-selling and replacements. As we’ve previously submitted, when one looks at the number of complaints in the industry as a percentage of total business written (by case count), then the number of complaints is tiny as a percentage.

We submit that the changes being proposed here are far-reaching enough that one needs to get it right. We therefore extend our willingness to be part of finding a solution that meets the objectives that seek to build consumer confidence and trust in the industry while at the same time enabling advisors to run sustainable business models.

With reference to the last bullet with its 5 sub-points, our comments are the same as under proposal UU (ST insurance).

Technical work and input

We have read various press reports and listened to numerous comments in relation these RDR proposals – they range from absolute support to absolute rejection. From the Masthead advisors there is an earnest request that in bringing change to ensure customers are treated fairly, the regulator doesn’t tighten the screws in relation to advisor remuneration so much that existing advisors are squeezed out or that no new advisors are attracted to the industry. One only has to look at the average age in the industry to see that we need new young blood.

We remain concerned about the financial impact on advisors businesses. They have a number of commitments under FAIS and responsibilities to their customers and their costs are high – see email in the block below received from a financial advisor during the course of our workshops. So, specifically in relation to this proposal on remuneration we need to see more detail unfold, and are willing to be part of a more detailed process. With that, we will seek to develop confidence that the outcome will serve the interests of both customers and advisors.

My feelings on RDR changes are mixed. It is uncertain how our remuneration will change. I would like to point out that for someone starting out in this industry, there is usually no basic salary. We have to find our own clients. Finding our own clients sounds easier than the reality we face when we talk to strangers who are often rude. We drive long distances to see a client who might not be interested in the proposal and only wanted to hear what we have to say. All these are obstacles faced by new financial advisors. Some might even start out without a car and borrow money from friends, family and other sources just to be able to have the opportunity to get on a taxi to go to a prospective clients’ office who might not even take the product, resulting in no earnings and just debt piling up. It takes a certain kind of resilience to go a month or months without being paid and to still come back and work harder than before. The realities of this cannot be illustrated strongly enough in words.

It gets better with time and experience, but this cycle of trying to make usually lasts about two years. Most brokers fail and quit this tough industry because of these obstacles even with the current remuneration structures. My question is, how many more will fail or quit if the remuneration is changed negatively. How many people will be able to enter into such an industry if the barriers to entry are
tightened? A negative change in remuneration will have a negative impact on the 
industry that brings wealth protection and creation to a nation that is in need of 
such.

Proposal OO: Product supplier commission prohibited on replacement life risk policies.

Comment:
Churn rate, when applied to a customer base, (according to Wikipedia\(^5\)), refers to the proportion of contractual customers or subscribers who leave a supplier during a given time period. It is a possible indicator of customer dissatisfaction, cheaper and/or better offers from the competition, more successful sales and/or marketing by the competition, or reasons having to do with the customer life cycle.

In our industry the word churn is used less in relation to customer, and more in relation to the product or policy that the customer may hold with a product supplier. More specifically, it relates to a customer replacing one product with a similar one, and is most often associated with life insurance policies. In this context the word churn conjures up negative associations – the default view seems to be that all replacement is bad or inappropriate and therefore something should be done to stop it. Churn is often used synonymously with replacement, but has, in our view a decidedly different meaning and it is important to distinguish between them.

Replacement is a natural part of a customer and product life cycle. People replace all sorts of things during their lives – they replace cell phones, cars, or clothes when newer versions or models come out. They replace items when they get tired of the old one, when there is a newer one with better features or when the newer one is cheaper. And, they replace items when their circumstances change and a newer one meets their needs better. Things are no different in relation to life policies – circumstances change, needs change, and policies change (see Figure 15). Therefore, in relation to life policies, “replacement” can be regarded as natural and normal. It amounts to replacing an old policy with something that is newer, better, cheaper – something that, based on the customer’s circumstances, is more appropriate. The appropriateness and benefit to customer is paramount and the fact that it leads to commission is incidental. Example 1 below sets out a fairly common anomaly in the system.

**Example 1**

An advisor speaks to a customer who has a need to increase cover from R2m to R3m. The premium on the R3m new policy is cheaper than the combined premium on a R1m new policy and the R2m existing policy. Therefore, in this case the appropriate thing to do for the customer is to write the new policy. But, the whole thing will be deemed to be a replacement and therefore no commission. So, a dilemma?

Example 2 illustrates the decision/choice that advisors face on a daily basis relating to appropriate advice.

**Example 2**

Customer earns R40,000 pm. Has life and disability cover in place, last amended 5 years ago. His expenses are too high and he is looking for a saving on his premiums. Advisor considers circumstances and recommends 2 changes:

1. Double the life cover for man and wife
2. Convert disability cover to trauma cover – customer can’t afford both and advisor’s experience shows more trauma claims (heart attack, cancer) than disability claims.

Now, does the advisor change the existing policy or write a new one? Changing the existing policy increases the premium by R642 pm. Writing a new one costs the customer R20 pm less than he’s currently paying. That’s a swing of R7,944 per annum. What do you do?

So, for us there is good, appropriate replacement, driven by the needs of customers and then there is inappropriate replacement, driven by other needs – these needs could be those of advisors or they could be the needs of product suppliers. Inappropriate replacement we call churn. Under the current regulations, commission flows for the sale of a policy – there is no distinction between appropriate and inappropriate sale of policy. Effectively there is a one-size-fits-all commission regulation that caters for most situations, but not the exceptions. So, it’s not perfect.

Example 3 below shows a recent product development in the industry that provides a good argument for appropriately replacing existing policies. This is innovation in action and is part of a healthy financial services system.

**Example 3 - disability income benefits**

Product supplier A used to pay disability income benefits to a maximum of age 65 years. They recently changed the benefit and it is now available as a lifetime benefit (if you claim you can receive an income for life and increasing in line with inflation).

In response to developments like these, the question has to be asked as to the advisors’ responsibility to advise their customers and, if suitable and affordable, to replace the old with the new. It is certainly within the scope of their duty of care to customers as well as meeting their TCF responsibilities to do so and one could go so far as to say that advisors may be negligent if they do not present these opportunities to their customers. Proper
presentation thereof (meeting all FAIS and customer responsibility requirements) will undeniably involve time and effort on the advisor's part and one will look for fair treatment of the advisor in this process too.

On the other hand “churn” of life policies is, in our view, driven by an income objective, often coupled with questionable ethics. This could be an overriding need for new business premium flows (and the income that comes with that) by a product supplier or a need for new business by an advisor because that generates new commission – it starts with the intent. The appropriateness and benefit to customer is incidental.

It is widely accepted that a lot of churn has been linked to the activities around sign-on bonuses, and specifically the need to provide the payer of the sign-on bonus with a return on that outlay. This Return on Investment (ROI) will generally, in the case of life products, come through the profit released through the product. Now, given that sign-on bonuses are no longer permissible, we would suggest that this is in itself a mitigation of the risk of inappropriate replacements. When coupled to the implementation of proposals V and Y in the shorter term and proposal RR in the medium term, this should sort itself out.

In a strange way one of the drivers of replacements is innovation. All companies continually bring out newer policies (enhanced benefits, cheaper premiums, simplified or more advanced products) and customers that have the old ones are now candidates for the new ones. There is fierce competition between suppliers – competition for share of the customers' wallets. This innovation is therefore coupled to the marketing drives of the companies to get their product to market and sold. Independent advisors, with access to choice, find themselves in a difficult position. If a product supplier reduces its premiums it can be in the customer's interest to move.

There is also a view that part of what is driving replacements is premium patterns as part of the product design. Many of these create the opportunity for customers to get the same level of life cover for a lower premium. When affordability is an issue, this becomes a driver for change/replacement.

(Unintended) consequences of banning commission

In studying this proposal and talking to advisors, we have three key concerns with regard to consequences of the proposal as it stands.

(1) Exception or rule?

We know that annually there are upwards of 6 million new business life policies sold in this country. We have not seen statistics of replacements per annum, but we hear a number of ±140,000 (that’s 2.3% of all policies sold) and an estimate that 75-80% of these may be inappropriately replaced or churned policies (that’s 1.9% of all policies sold). It doesn’t say that the policy wasn’t needed or appropriate, it just says that there was commission paid on the policy where it had previously been paid.

If one refers back to our three examples above, then all of these would be classified as replacements and we submit, that in all three cases the advice and implementation for customer would (subject to due process being followed) have been appropriate.

Therefore, we submit, with respect, that an outright ban on commission on replacement life risk policies is a catch-all approach and is not an appropriate solution to the issue. While it
catches the “bad” replacements (the churn), this total ban at the same time creates a penalty for those effecting “good” replacements.

(2) Suitable products and fair access to suitable advice for financial customers

This is one of the stated objectives of the RDR paper and it is an important one. We are concerned that this catch-all rule, with its commission impact will result in customers not replacing when in fact they should. The reason is that customers do not initiate the change of policy discussion - advisors recommend policy changes and/or replacements to customers.

If the intent is that the advice fee payable by customers for product advice equates to roughly half of the total cost/remuneration to the advisor (the logic being that the other half is made up of product commission payable by the product supplier), then it is submitted that, at best, the advisor would be out of pocket by half. Advisors run businesses and if there is not adequate remuneration (irrespective of whether customer or product supplier pays) they will opt out of this market. The consequence is less such suitable advice and therefore less replaced policies put in place, even if these are suitable. So, if the benefits of innovation are things like enhanced benefits, cheaper premiums, simplified or more advanced products then there will be more customers sitting with old generation products that do not have these qualities. And, that’s not good either.

(3) Impact on life premiums

Will we see premium reductions on replacement business?

The premiums of life policies are made up of different expenses and provisions (eg. cost of risk cover, admin expenses, selling expenses and profit margin). The selling expenses (which would include commission) are typically costed/provided for at ±20% of the premium – so, ±20% of what the customer pays on a life policy premium relates to selling/commission expenses. It therefore follows that if there is no commission payable on a replaced policy, such a policy should be cheaper … at the very least by the quantum of commission that would have been payable, but which is now stripped out. Figure 16 shows the difference in a life insurance policy quote drawn recently with and without commission. So, logic says we should (if the proposal is implemented as is) see two sets of premium rates for life policies – one with commission for new business and one for policies that are sold as replacements. In our real-life example above, that’s a 10% saving on each premium. Again, following logic, one should be able to get the same policy, with the same cover for less once this proposal kicks in – because the new policy (being a replacement policy) will not have a provision for commission expenses. If this is the case, then every advisor should, subject to their responsibilities as required its FAIS and common law, be rewriting their customers’ life cover as soon as the new rule is in place. We can only conclude that this was not the intent behind the proposal.

Some input and questions

In responding to this proposal, we have difficulty in a few respects:
Where there is a replacement policy appropriately put in place, the product supplier gets business now without having to pay for that. So, acquisition costs are lower for the product supplier.

There is no less work to be done by the advisor in relation to a replacement – if anything, there’s more. So, his acquisition costs don’t reduce. Therefore, in line with our view that a total ban on commission on replacement business is inappropriate, we feel strongly that the advisor should be appropriately compensated for putting suitable product solutions in place.

We view commission on replacements and commission on new business life policies as two sides of the same coin and therefore find it unsuitable to ban commission on replacements without having clarity on the detail about advice fees and the final model in respect of life risk commission.

We are concerned that the proposal seeks to regulate for the exception.

How will a replacement be defined – as broad as possible or more narrowly?

How will one ensure that there is a true record of the replacement?

What regulation will happen at the product end? Will there be a review on the product design issues that create the opportunity for replacements (eg. premium patterns)?

Can one not regulate or deal with this type of issue through TCF?

**Suggested ways of dealing with this**

If one accepts a difference between churn and replacements and because they have different ethics involved, we believe that one should be dealing with the two differently. Stamp out churn while still allowing for replacement. We asked advisors what they thought would help to reduce inappropriate replacements or churn.

The most-repeated suggestion was that more emphasis should be placed on the replacement form. Tighten up the existing provisions relating to the Replacement Policy Advice Record (RPAR) – so that it is taken seriously (see Figure 17). Advisors feel that the original selling advisor should be protected because this person is financially exposed during the commission clawback period.

**Specific focus and attention**

There was a very strong view amongst our members that there should be intervention – strong regulatory supervision and sanctions where appropriate. The culprits (recidivists, if you want) should be targeted. They should be specifically and individually targeted, not through a catch-all mechanism. That way, the message gets sent loudly and clearly to advisors, product suppliers and the industry in general. It also sends a confident message to the majority of advisors, who do the right thing, that they enjoy the protection of the regulator. There were even suggestions that there should be some form of tribunal set up to assess whether replacements were appropriate or not.
There are, in our view, mechanisms to deal with the above. The regulator already has the new business figures from all life offices and can easily call for records to show the incidence of replacements – companies should be keeping records of these. An intensive and intrusive analysis of these should help to identify commonalities, patterns, and trends, which in turn will point the regulator to potential dens of problems. That way, specific and individual action can be taken, rather than a broad sweeping action.

**Specific comment and alternatives**

As expressed above, our view is that it is inappropriate to ban commission on all replacements.

If this is not acceptable to the regulator, then we would suggest two possible alternatives:

- Have consistency across all life business - in other words, deal with commission on replacements in the same way as proposed in relation new life risk policies set out in proposal NN.
- Pay as-and-when commission on replacements. Going further, but perhaps more difficult to monitor is, pay as-and-when commission on churned business and normal commission on appropriate replacements.

**Recourse to customer**

As a final word, we believe that the beneficiary of the suitable advice, the customer, enjoys protection irrespective of the way an advisor is remunerated.

Apart from the ASISA replacement form, there is an obligation laid down in the FAIS General Code [s8(1)(d)] that requires advisors to make full disclosure to customers so that they can make an informed decision in relation to a replacement. Despite these steps taken by advisors, if customers are not happy, they can complain to advisors and to product suppliers. They have access to complaints mechanisms through the FAIS Ombud and the Long-term Ombud. So advisors are already open to scrutiny and possible penalty for poor advice.

<table>
<thead>
<tr>
<th>Proposal PP:</th>
<th>Commission regulation anomalies on “legacy” insurance policies to be addressed.</th>
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Comment:

In principle, we have no concerns with this approach.

<table>
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<tr>
<th>Proposal QQ:</th>
<th>Conflicted remuneration on retirement annuity policies to be addressed.</th>
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Comment:

Through the preamble to proposal QQ reference is made to “... there may be incentive-driven churn...”; “intermediaries ... may be driven to earn additional asset trail fees ...”; and “... even if this may not be in the client’s best interest ...”. There are always possibilities that these things may happen, but this paragraph in the paper makes it look like these behaviours are common practice – they are not. It therefore appears to us that there is a finger pointing (and, in our view, not entirely fairly) only at intermediaries and what they “may” do. It looks like a case of having rules in place in case there’s something inappropriate.
From a practical point of view, one cannot try to regulate or prevent every possible scenario by trying to write a rule that seeks to cater for every possibility (however remote) that something inappropriate may happen. Viewed from an advisor perspective, there are more satisfied customers than dissatisfied customers, there is more good advice dispensed than bad advice, and there are more good advisors than bad advisors. It feels at times that the worldview of advisors and therefore the starting point for decisions or change is that advisors “may do the wrong thing” and therefore rules or controls need to be put in place. That sounds like regulating for the exception, and to this extent, we cannot support that.

Customers have access to a number of complaints mechanisms and we shouldn’t ignore these as control mechanisms.

We absolutely agree with standards in relation to disclosures (eg. in relation to penalties, advice fees, product charges) if these are currently not adequate, based on customers suffering loss or that there is widespread abuse in this market. We also support the need for clear and understandable communication in this process.

However, we are sceptical about the part of the proposal that may place obligations on the funds (transferring and receiving) and/or product suppliers “… to satisfy themselves that the transfer is in the fund member’s interests …”. We question whether the fund, especially the transferring fund (the one that would lose the assets under management), is objectively positioned to “satisfy itself” that the transfer is in the interest of the member/customer. Surely they are conflicted?

Any decision that reduces the chance of customers saving and/or providing for retirement should not be taken lightly. As though to sound a warning, there are some really concerning numbers coming out of the latest Sanlam BENCHMARK Survey (released in 2014). The number of retirement fund members whose investment decisions are based on advice from a financial advisor or broker decreased from 50% last year to 37% between 2013 and 2014 – that’s a 26% drop. The survey further finds that just under half (47.3%) of retirement fund members take their own financial decisions regarding retirement and investments and only 14% of retirement fund members contact a personal financial advisor or broker for advice and assistance relating to their retirement benefits. According to Dr Johan van Zyl (CEO: Sanlam), “One of the key messages that emerged from this year’s results is the crucial importance of qualified financial advice. There is concerning evidence that even though retirees have an express need to talk to a professional, most spend insufficient time and energy on the all-important exercise of obtaining professional advice.”

These types of results are supported by further research findings that 85% of respondents\(^6\) in Old Mutual’s Retirement 2013 Monitor felt that not having enough money to retire was their greatest retirement concern.

In line with the above points, and given the importance of retirement provision, we are of the view that if it is appropriate (with the interests of the customer being paramount) to transfer from one fund to another, and the right process has been followed, and the right disclosures made and the customer agrees to pay an ongoing advice fee, then that should

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\(^6\) Old Mutual 2013 Retirement Monitor; p24
be ok. If legislation has the impact of preventing this, then we believe it is inconsistent with the broader objectives of this RDR paper, and that the legislation should be amended.

**Proposal RR:**  Equivalence of reward to be reviewed.

Comment:
As mentioned earlier in our feedback, equivalence of reward has not been raised as a big deal amongst independent brokers – they feel that there is ultimately a trade-off in that the tied advisor is limited in what they can take/offer to customer.

Having said that, the areas that IFAs define as the types of things that could be considered when reviewing/evaluating Equivalence of Reward include the following:

- Compliance costs; accounting fees; secretarial salaries; cost of computer hardware (including support); computer software programmes (CRM database, financial needs analysis programmes; anti-virus software; office packages like word processing, spreadsheets - eg MS Office; email; cloud storage and backups); broadband line; internet service provider subs; office rental; car allowance; club or association memberships; regulatory licence fees (eg. FSB, Medical Schemes); cost of Professional Indemnity Insurance; other insurance and risk cover; contributions to funds (eg. retirement and medical aids).

**Proposal SS:** Standards for remuneration arrangements between juristic intermediaries (adviser firms) and their individual advisers.

Comment:
Reference is made to “… paid by customers in respect of such products over an appropriate period.” Our comments/questions here are what would an “appropriate period” be, how would this be determined and who would determine this? A vague or broad definition may provide arbitrage opportunities that work against the intent to avoid placing “… larger adviser practices … at an unfair advantage over smaller purely fee-earning advisers …”.

**Proposal TT:** Special remuneration dispensation for the low income market.

Comment:
We have no specific commentary but support the objective of a different dispensation for the low-income market.

We note the comment that there are “difficulties of defining “low-income sector” products”.

**Proposal UU:** Remuneration for selling and servicing short-term insurance policies.

Comment:
There is positive reaction to the proposed continuation of the as-and-when commission as the basis of remuneration for the selling and ongoing servicing of short-term insurance business. The biggest concern amongst advisors is the quantum of commission. Until there is an indication of the percentages being considered, it is premature to comment too much.
There are already rumours in the market that are making advisors really nervous … to the extent that a number of them are questioning their futures in the industry.

Reaction to the proposed removal of the s8(5) fee\(^7\) is tempered by the indication that this can/will be replaced by an advice fee.

We have no issue with the part of the proposal that would require insurers to include the cost of fees in the premium and explicitly disclose to customers. Effectively this is already done in the short-term industry and is set out similar to that reflected in Figure 14 of our feedback. An additional piece of disclosure would be information regarding the purpose of the fee. Our only caveat here would be too much disclosure – if it’s useful and helpful to customers we support this. If it’s not or it’s confusing, we would rather leave it out.

We question how insurers will monitor ongoing service and how they will determine whether advisors provide ongoing service. It is potentially in their interests to make a call that there is no ongoing service and simply stop payment of the fee. We are concerned that insurers will be able to decide to stop charging the service fee against the policy.

Our comments in other relevant parts of this feedback regarding product suppliers adjusting product charges after implementation of similar provisions in relation to life and investment products apply equally here.

Short-term insurance involves a lot of admin on the part of the advisor and often there is a blurred line between what the advisor is doing on behalf of the customer and what he’s doing on behalf of the product supplier. We would therefore welcome a fresh view (aligned to the activity basis set out in this paper) of what is done and who it’s being done for. Linked to this is our principle support for the regulating of service fees. The devil however, lies in the quantum.

**Proposal VV:** Conditions for short-term insurance cover cancellations.

Comment:

We recently heard of a situation where a short-term product supplier “bought out” a broker for a 6x P/E, subject to him moving his book within 3 years. These are the easy situations to want to police. So, we are generally comfortable with a tightening of standards driven by suspect motives and we understand the motives driven by money (binder fees or other). We fully support a situation where the customer is fully informed, agrees upfront and doesn’t have a break in cover.

However, there are genuine situations where so-called bulk transfers are necessary and are driven by the interests of the advisors for their customers – eg. insurers that no longer provide certain cover or benefits; insurers that want to move/change the servicing points for the advisor (eg. to a binder holder who is also a brokerage); insurers that want to cancel the broking contract of the broker (because of production targets); insurers who apply a high premium increase on the advisors entire book (eg. because of weather-related claims); insurers that look to the profitability of an advisors book (this can be especially

\(^7\) s8(5) of the Short-term Insurance Act
harsh on smaller advisors); and, insurers that relate premium to customer on “size of book” (or portfolio) basis.

Considering these we would caution against additional conduct standards being too onerous (at an admin level) or placing the advisor in a situation where an insurer can effectively disintermediate him.

**Proposal WW:** Remuneration for direct non-advice sales execution.

Comment:

We support the setting of standards as proposed.

We also suggest that direct sales operators be required, in their disclosures (including their advertising) to emphasise the fact that, not only do they not give advice, but that customers who are buying through them are taking the risk of ensuring that what they bought is appropriate for their circumstances. We suggest that, in an attempt to level the playing fields, they be compelled to disclose the way their call-centre sales people are remunerated, including any volume incentives.

We would propose that there is a tightening up on replacements – the direct operators claim that because they only give information and the customer executes, they don’t have responsibility with regard to replacements.

Please also refer to our previous comments in relation to direct sales operations.

**Proposal XX:** Remuneration for referrals, leads and product aggregation and comparison services.

Comment:

We have no comments in this regard, but welcome a review.

**Proposal YY:** Remuneration for investment platform administration.

Comment:

We anticipate that this will have an immense impact on the existing LISP industry and accept that there will be plenty of commentary from that industry.

We have already seen platforms starting to narrow their fund choices – they’re “coming closer to home”. This may make it very difficult for fund managers, who do not have their own distribution capability or their own platforms, to get their funds in front of customers. It makes us wonder whether this increases or reduces competition – is there a real place for the small asset manager or do the bigger just get bigger and more dominant?

LISPs provide a great benefit to advisors and customers – they co-ordinate and provide information of customers’ investments in a single place. If there is too much narrowing of fund choices through LISPs (because of proposed changes), we see some significant impacts on advisors:

1. Advisors will need to do the admin iro reporting themselves. That means collating information from a range of product suppliers (fund managers) and putting it into a single understandable report for customers.
2. Advisors' admin is increased in having to deal with a range of asset managers directly.

3. If advisors continue to work through LISPs, they will need to work with more than one LISP so that they preserve their independent status.

4. It may see an increase in activity of what in the UK are called “Discretionary Fund Managers” – these are entities that help to create risk profiled or model portfolios. They effectively act as an outsourced investment committee on behalf of the advisor. They come at a cost, typically in a range between 0.15% and 0.25% bps.

The way we see things, the product supplier (fund manager) is outsourcing certain functions to the platform – it is therefore reasonable to expect them to pay for that. It could be as simple as buying shelf-space. This is a common practice in the FMCG retail industry as well as the motor industry. Wholesalers pay shopkeepers (Pick-n-Pay for example) for the front-end of the display gondola. Or, I can sell my motor car by “renting” space on a motor dealer's showroom floor. It's the seller that pays, not the end buyer, so we don't follow the rationale for advocating that all charges should be paid for by the customer.

We support the intent to promote full and clear disclosure of all costs and we feel that there must be a way to deal with the concerns and “lack of transparency” in a way that doesn’t take away the benefit of platforms.

**Proposal ZZ:** Binder fees payable to multi-tied intermediaries to be capped.

Comment:

We support the setting/defining of standards regarding binder fees if it enhances oversight and governance. In principle, the capping of binder fees is acceptable – the real issue is at what level and in whose favour? In doing this we would request that there is consideration of various business models and what the binder holder performs – in other words, apply the proportionality rule.

We are not in a position to comment on the percentages suggested in the discussion paper and therefore have no further comment at this stage.

**Proposal AAA:** Commission cap for credit life insurance schemes “with administrative work” to be removed.

Comment:

We have no comments here.

**Proposal BBB:** Outsourcing fees for issuing insurance policy documents.

Comment:

We agree with the first paragraph.

We principally agree with the second paragraph, although in setting reasonable fees for outsourced functions, there would be a number of considerations. At this stage therefore, we cannot comment on whether R100 is the right number.

With regards to the third paragraph, we have a different view in relation to advisors capturing information directly onto/into an insurer’s system. We believe (as stated earlier in
our feedback under Chapter 2) that this function effectively replaces the need for data capturing at the insurer. If the advisor were simply completing forms (eg. application or claims forms) and emailing them, faxing them or handing them to the product supplier, that product supplier would have to get it onto their system through their own resources and at their own expense. So, effectively, by advisors doing this, they are performing outsourced functions on behalf of product suppliers. Performing these functions also shifts the risk for correct capturing onto the advisor.

Outsourcing is a business decision for the outsourcer (product supplier) and the entity that does it (eg. an advisor) and it often speeds service up to the customer. If it is no longer viable for the outsourced company/advisor to do the work, they’ll just bounce it back to the product supplier.

Principally we see no difference between this capturing and the subsequent transmission of the policy to the policyholder, which is recognised under this proposal as being an insurer function that may be outsourced to an intermediary.

**Proposal CCC:** General standard: No financial interests may be provided by product suppliers to intermediaries unless specifically provided for in the regulatory framework.

Comment:

We find it difficult to support this proposal in the absence of more detail and therefore would suggest further discussion around this aspect. Principally we are concerned that this seeks to regulate through a catch-all, with attendant unintended consequences.

We submit that it is easier to add a prohibition to a set of regulations at a later stage if there is found to be a gap, rather than to delete or rescind a rule that may be found down the line to be inappropriate.

Accordingly, we would suggest that financial interests should be allowed unless they are specifically prohibited. In addition, we believe that the regulator has the tool of “fair outcomes to customers” at its disposal to be able to take action.