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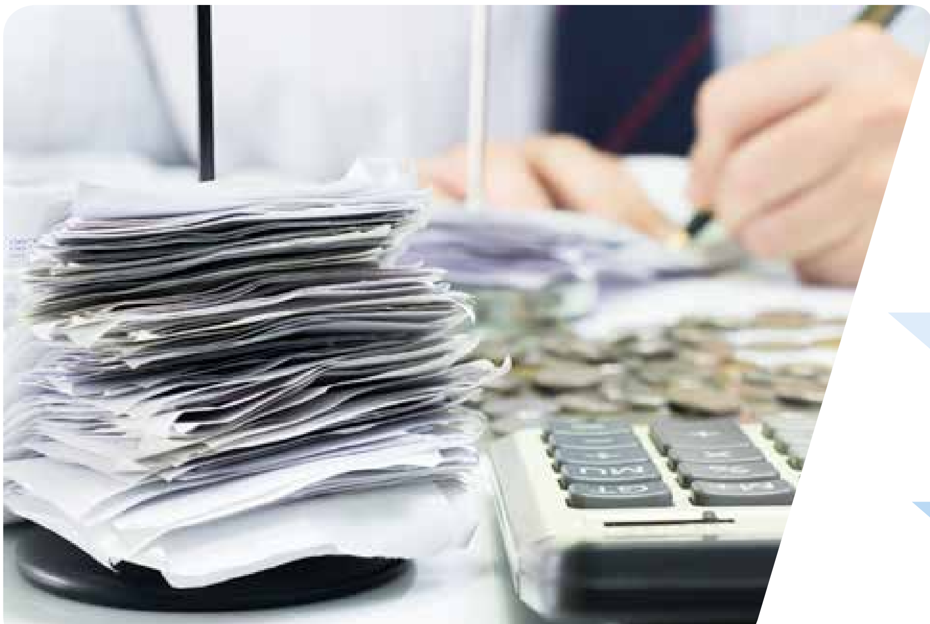
cutting through complexity

Retail Distribution Review 2014

Summary of proposals

Services provided – an activity based approach to defining advice and intermediary services

An activity based approach to defining advice and intermediary services is proposed. The types of activities and respective sub-activities typically provided by intermediaries have been defined, and it is proposed that these activities and sub-activities will be defined in the regulatory framework



PART 1 – SERVICES PROVIDED Services to customers
Proposal A: Forms of advice (financial planning, up-front product advice, ongoing product advice) defined, with related conduct standards
Financial planning, up-front product advice and ongoing product advice will be defined in the regulatory framework. The definitions will be used to set conduct standards regarding the provision of these forms of advice and specify disclosure requirements to customers. Fit and proper requirements will be set for intermediaries performing these activities.
Proposal B: Standards for "low advice" distribution models
In certain instances it may not be feasible for an intermediary to conduct a full suitability analysis, for example where products are sold through telephone call centres. The proposals have indicated that conduct standards will be set to manage and mitigate the risk associated with providing this type of advice.
Proposal C: Standards for "wholesale" financial advice
This relates to where advice is not provided directly to the end user of a financial product and the advice is provided to an intermediate entity such as an employer, retirement fund or medical scheme. Specific conduct standards will be set, requiring the advisor to demonstrate that, when providing advice, they took into account the circumstances of the affected employees/members who are the end customers and those who ultimately bear the cost of the advice given.
Services connecting product suppliers and customers Conduct standards will be set to define the services listed below. This will include disclosure requirements by intermediaries to customers and considerations around mitigating and managing certain conflicts of interest.
Proposal D: Standards for sales execution, particularly in non-advice models
Intermediaries will need to be able to reasonably establish the customer's financial capability in relation to the products offered through the non-advice model. There will be restrictions on the types of products or product features that may be distributed through this model, and will be restricted to simple products that comply with explicit product standards.
Proposal E: Ongoing maintenance or servicing of products
This type of service excludes of the provision of on-going product advice. Standards may also apply to post-sales servicing undertaken by the product supplier itself.
Proposal F: Insurance premium collection to be limited to qualifying intermediaries
For long-term insurance business or personal lines short-term insurance business, the collection of insurance premiums will only be permitted to be carried out by intermediaries where the intermediary complies with prescribed conduct standards for this service.
A transition period will be granted for intermediaries to become compliant with such standards or for insurers to either take over this function themselves or outsource it to third parties who are not intermediaries or associates of intermediaries.
Proposal G: Revised standards for investment platform administration
This activity relates to aggregating, safeguarding and administering investments offered to clients by more than one product supplier or investment manager on a single platform and will continue to be recognised as a specific, licensed regulatory activity.
Proposal H: Standards for product aggregation and comparison services
Specific conduct standards will be set to ensure that these types of activities are conducted in a way that delivers fair customer outcomes. This will include, enhanced disclosure around information about the service itself, the range of products or product suppliers and the provision of minimum product information, amongst others.
Proposal I: Standards for referrals and lead generation
The provision of this type of service will be subject to specific conduct standards related to disclosure of remuneration or other financial interests, management and disclosure of any potential conflict of interest and measures to ensure customer consent and protection of customer information in appropriate circumstances.
Where the referral or lead provision does not meet the relevant criteria to be regarded as financial intermediation, the service provided by the product supplier or intermediary may be subject to relevant standards for marketing and advertising activities, or for the outsourcing of activities.
Services to product suppliers
Proposal J: Other outsourced functions
The conduct standards in respect of these functions will be built on the approach applied in Directive 159.A.i: Outsourced Arrangements.
Financial Advisory and Intermediary Services (FAIS) regulations will be reviewed to develop more tailored conduct standards in relation to different types of outsourced services and who will be permitted to provide them.

PART 2 – RELATIONSHIPS BETWEEN PRODUCT SUPPLIERS AND INTERMEDIARIES

A customer should understand what services are being provided, and in what capacity the intermediary is acting, in order to evaluate and compare the advice given. The proposals set out the criteria that will be used to determine different types of relationships between financial product suppliers and financial advisers, the terminology used to describe these relationships, and how elements of these relationships should be disclosed to customers.

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

Any person providing financial planning or financial product advice may only do so in one of the following three capacities and will be permitted to only use the following three terms to describe their status as an adviser:

- Independent financial adviser ('IFA')
- Multi-tied financial adviser
- Tied financial adviser

In the case of an adviser providing advice in relation to short-term insurance products the following terms may be used:

- Independent insurance broker
- Multi-tied insurance broker
- Tied insurance agent

In the case of an adviser providing advice in relation to health service benefits the following terms may be used:

- Independent health benefit broker
- Multi-tied health benefit broker
- Tied health benefit agent

In addition to one of the above terms an advisor may also use the term "financial planner" if it provides financial planning services.

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

With certain provisions, an adviser that meets the requirements of an IFA of investment products may be a multi-tied adviser for long-term insurance, short-term insurance or health benefit products.

Independent financial adviser ('IFA')

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

In order for an adviser to be classified as an IFA, the following independence criteria will need to be demonstrated:

- Able to offer advice on multiple products offered by a number a product suppliers and be able to demonstrate that they have provided advice across an appropriate range of products and product suppliers.
- The type of advice provided must go beyond making recommendations on a restricted set of products or product suppliers.
- The regulator recognises that the "whole of market" concept may not be feasible as the adviser must be able to demonstrate high standards of and adequate product specific knowledge to be able to provide appropriate advice.

The regulator invites input into areas of uncertainty, which include:

- Number of product types or categories, the number of specific products within a product type or category, and the number of product suppliers, per type or category of product, on whose products the adviser should be able to provide advice.
- Where investment product advice is offered, whether the designation "IFA" should require an adviser to offer advice across a minimum range of investment product types, classes and/or needs and what this minimum range should be.
- Where investment product advice is offered, the standards that should be set in relation to recommendations involving the use of investment platforms.
- Whether an IFA should be able to select a "panel" of products and / or product suppliers.
- Whether an intermediary providing advice in relation to long-term insurance risk products only, but not in relation to investment products, should be able to be described as an IFA.
- When providing advice in relation to short-term insurance products only, what is the number of short-term insurance product types and / or the number of short-term insurance product suppliers on which the adviser should be able to provide advice, in order to be described as an "independent insurance broker"?
- When providing advice in relation to health benefits only, what is the number of health benefit product types and / or the number of health benefit suppliers on which the adviser should be able to provide advice in order to be described as an "independent health benefit broker"?
- Should the nature of the remuneration earned by the adviser play a role in determining the category of adviser?

Proposal N: Criteria for IFAs to be free of product supplier influence
The adviser must be in a position and be seen to be in a position to make recommendations that are free from product supplier influence. Certain types of relationships with product suppliers preclude an adviser from being classified as an IFA: • Where the adviser has any form of employment; agency; representative; outsource service provider; or other mandated relationship with the product supplier. • Where the adviser is directly or indirectly subject to production or sales targets in relation to products of the product supplier. • Where there is a direct or indirect ownership or other financial interest in the adviser by the product supplier. • Where the adviser has a direct or indirect ownership or other financial interest, other than as an ordinary financial customer, in the product supplier. • Whereby the relationship in any way enables the adviser to directly or indirectly earn more remuneration or other financial interest from that product supplier, or in relation to any of that product supplier's products, than from any other product supplier. • The relationship in any way imposes restrictions on the adviser's ability to provide advice or earn remuneration in respect of any other product supplier or any other product supplier's product, in respect of which the adviser would otherwise be able to provide advice. • The relationship is such that the adviser is in any other way directly or indirectly influenced by the product supplier – or could be seen to be influenced – to recommend the products of the product supplier concerned. • The adviser chooses, for any reason, to limit the range of products or product suppliers in relation to which it offers advice to an extent that the adviser will not meet the product choice criteria to qualify as an IFA.
Proposal O: Status disclosures to be made by IFAs
Conduct standards will be set for disclosures that need to be made by IFAs to customers regarding what the IFA category means and the range of product types and product suppliers it is able to provide advice on.
Multi-tied financial adviser
Proposal P: Criteria for multi-tied advisers
An adviser can be classified as a multi-tied adviser where it does not meet the requirements to be described as an IFA, and it not a tied adviser. For any actual or potential conflicts of interest per Proposal N, additional conduct standards will be set.
Proposal Q: Status disclosures to be made by multi-tied advisers
Conduct standards will be set for disclosures that need to be made by multi-tied advisers to customers regarding what the multi-tied category means and the range of product types and product suppliers it is able to provide advice on.
Tied financial adviser
Proposal R: Criteria for tied advisers
A financial adviser can be defined as a tied adviser if: • An adviser whose contractual, ownership or other relationship with a product supplier restricts the adviser to providing advice in relation to the products of that product supplier only. The product supplier can include an associate, agent or representative of such product supplier. • The adviser has an employment or other relationship with or mandate from a product supplier which has the effect that the adviser is restricted to providing advice in relation to the products of that product supplier only.
Proposal S: Status disclosures to be made by tied advisers
Conduct standards will be set for disclosures that need to be made by tied advisers to customers regarding what the tied category means, the entity of the product supplier with which the adviser has a tied relationship, and the range of product types and product suppliers it is able to provide advice on.
Financial planner
Proposal T: Criteria for financial planners
Conduct standards will be set for the provision of financial planning services: • Fit and proper standards, including competency standards set with reference to membership of or qualifications provided by appropriate professional associations. • Standards on the level and extent of financial product knowledge required to provide financial planning services. • Standards for financial planners that are also multi-tied or tied advisers, with a view to ensuring that the restrictions in relation to product advice they may provide do not conflict with or compromise the quality of the financial planning service.
Proposal U: Status disclosures to be made by financial planners
Conduct standards will be set for disclosures that need to be made by financial planners to customers regarding what the financial planner category means, and the scope and purpose of the financial plan.

"Hybrid" advice models
Proposal V: Insurer tied advisers may no longer provide advice or services in relation to another insurer's products
The current definition of "representative" in Part 3 of the Regulations of the Long-term Insurance Act provides that a representative may render services in relation to policies of "another insurer which has entered into a written agreement with that insurer in terms of which persons employed or engaged by that insurer may render services as an intermediary in relation to the other insurer's policies". This will be removed from the Regulations.
Proposal W: "Juristic representatives" to be disallowed from providing financial advice
The current landscape allows a "representative" to be a natural person or a juristic person – the use of juristic representatives have been extended from 28 February 2015 to 30 June 2015 per FAIS Notice 87 of 2014. Both the juristic entity and all natural persons who provide advice or intermediary services on the representative's behalf are regarded as "representatives" of the FAIS licenced financial services provider. The juristic representative structures used to provide financial advice will thus be disallowed and as a result, any individual natural person providing advice must either be a tied advisor, IFA or multi-tied adviser, or a representative of a juristic entity.
Juristic intermediaries (adviser firms)
Proposal X: Standards for juristic intermediaries (adviser firms)
An adviser firm may not be described as being independent or offering independent advice unless the firm itself meets the independence criteria set out for an IFA around product and product supplier choice and the relationship with the product supplier. Where an individual adviser acts as a representative of an independent adviser firm, the individual adviser cannot be described as independent or providing independent advice unless the individual adviser also meets the criteria as being independent. If the criteria is not met, the individual adviser may act as a multi-tied adviser, however appropriate disclosures will need to be made to avoid consumer confusion. An adviser firm can be classified as a multi-tied adviser if it meets the criteria for being described as a multi-tied adviser. Where an individual adviser acts as a representative of a multi-tied adviser firm, individual advisers can be described as multi-tied advisors. The individual adviser will not be able to be described as an IFA. Appropriate disclosures will need to be made if an individual representative cannot offer the same range of products or product suppliers as the multi-tied advisory firm. An individual adviser acting as a representative of an independent or multi-tied advisory firm may not be restricted to the products of one product supplier. This means that the individual representative will not be able to operate as a tied adviser.
Proposal Y: Advisers may not act as representatives of more than one juristic intermediary (adviser firms)
Individual IFAs or multi-tied advisers acting as representatives for adviser firms may not provide advice for more than one adviser firm.
Outsourced service providers, including binder holders
Proposal Z: Restricted outsourcing to financial advisers
As a general standard, the outsourcing of product supplier functions or investment management functions or activities will be prohibited, other than those which are specifically identified and monitored.
Proposal AA: Certain functions permitted to be outsourced to financial advisers
Despite the above, the following are permitted: • Binder functions, subject to the Binder regulations. • Administration functions carried out by authorised administrators on behalf of retirement funds or medical schemes, where the administrator also operates an adviser function. • Issuing of policy documents on behalf of insurers • Where an intermediary is a binder holder, the issuing of policies by the intermediary is seen as incidental to the activity of concluding new contracts with policyholders or concluding policy renewals or endorsements, and hence is not deemed to be separate from the binder function, nor may it be separately remunerated when performed under a binder agreement.
Responsibility of product suppliers for advice and intermediary or outsourced services provided
Proposal BB: Product supplier responsibility for tied advisers
Product supplier responsibilities include: • Advice provided by tied-advisers • Ensuring the tied-advisor's compliance with relevant regulations • Ensuring the tied adviser has the requisite generic and specific product knowledge • Ensuring the adviser's delivery of TCF outcomes • Will include responsibilities in respect of multi-tied advisers in addition to the above

Proposal CC: Product supplier responsibility for multi-tied advisers

It is reasonable to expect product suppliers to share in the responsibility of quality of advice provided by the multi-tied advisor to the shared customer base. This will include paying more attention to the general customer treatment culture and supporting controls the multi-tied advisor may have in place:

- Ensuring that the advisers are adequately equipped to provide appropriate information and advice on the product suppliers' products.
- Ensuring that the adviser meets specific levels of generic and product specific product training, failing which the product supplier may not enter into any form of arrangement with the adviser in relation to its products.
- Taking reasonable steps before entering into any such arrangement, and in the course of the arrangement, to satisfy itself that the adviser will be in a position to deliver fair customer outcomes and provide advice suitable to the needs of the type of customer base and product types concerned.
- Reasonably monitoring appropriate fair treatment indicators, at adviser level, in relation to the adviser's book of business, and taking appropriate action to address or mitigate identified poor customer outcomes.
- Identifying specific types of activities that pose a high risk of poor customer outcomes and putting reasonable risk mitigation measures in place.
- Having processes in place to monitor and resolve customer complaints relating to the multi-tied adviser's services, and take appropriate action to mitigate unfair customer outcomes identified.
- Monitoring adherence by advisers to the fee guidelines for advice.

Proposal DD: Product supplier responsibility for IFAs

The relationship between a product supplier and an IFA is at arms' length thus product suppliers cannot reasonably be expected to exercise the same degree of control in relation to customer outcomes for IFAs. As a result, product suppliers are only required to take responsibility for aspects of the conduct of IFA's who provide advice on their products:

- Where the product supplier pays any form of commission or facilitates the payment of any advice fee to an IFA, the product supplier will be required to ensure that the adviser meets the same levels of generic and product specific product training as applicable in respect of a multi-tied adviser.
- Identifying specific types of activities that pose a high risk of poor customer outcomes and putting reasonable risk mitigation measures in place.
- Where an advice fee facilitation arrangement is entered into with the IFA, monitoring adherence by the IFA to the fee guidelines for advice.
- •Taking reasonable steps to monitor and assist in the resolution of customer complaints relating to the IFA's services, and take appropriate action to mitigate unfair customer outcomes identified.

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

Product suppliers will be responsible for ensuring that:

- The products concerned meet the requisite product standards for the distribution model.
- Any individual providing factual information as part of the non-advice sales process meets the requisite fit and proper standards.
- Any other conduct standards, including disclosure standards, relating to non-advice sales execution are met.

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

Conduct standards will be set to clarify product supplier responsibilities in relation to ensuring ongoing access to and monitoring of customer related data held by intermediaries and outsourced service providers. This will be required to ensure that the product supplier's ability to monitor delivery of TCF outcomes to customers is not undermined, and will build on the approach already included in the binder regulations and outsourcing directive. Standards may differ for IFAs and multi-tied advisers, and 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.

Ownership and similar relationships between intermediaries and product suppliers

Proposal GG: Ownership structures to be reviewed to assess conflicts of interest

The various proposals in the RDR relating to the relationships between product suppliers and intermediaries are aimed at reducing conflicts in these relationships. Certain ownership structures may nonetheless still exhibit conflicts, and the regulator will be engaging on these issues to understand how ownership structures may compromise customers' ability to assess the status of advice. This will also allow the regulator to determine whether any additional prohibitions or controls may be required to further mitigate any potential advice bias.

PART 3 – INTERMEDIARY REMUNERATION RDR aims to produce greater clarity on activities that make up advice, intermediation and outsourced fees, and on whose behalf they are rendered. Remuneration should meet the following criteria: • Should not contribute to conflicts of interest • Recognise the range of services, and the related remuneration, which should be reasonable and commensurate with the actual services • Strike a balance between compensation for upfront activities, and support of on-going services, and on-going fees to only be paid if on-going services are actually provided • Cannot be paid twice for same service • Must be motivated, disclosed and explicitly agreed to by customer, and should be readily comparable • Promote a level playing field Proposals will aim to achieve the above principles. The proposals are set out in accordance with the activity-based model with specific proposals for each of the following: • Services to the customer • Services connecting customers and suppliers • Services to product suppliers
Proposal HH: General disclosure standards
Over and above specific standards, the regulatory framework will set general standards relating to standardised terminology and methodologies, disclosures and record keeping obligations.
Fees for financial planning / non-life insurance risk planning (service to customer)
Proposal II: Standards for financial planning / risk planning fees
Remunerated by a planning fee, pre-agreed and negotiated directly with the customer in a clearly disclosed charging structure. Nature and extent of planning services must be clear. Fees should match the services rendered, taking into account the level of expertise of the planner, and although regulations will not prescribe the quantum or charging basis, benchmark guidelines may be published. Product supplier to monitor tied advisers, including the planning fees charged and the quality and scope of planning services.
Upfront and ongoing product advice fees (service to customer)
Proposal JJ: Standards for upfront and ongoing product advice fees
Remunerated by means of an advice fee, negotiated with and paid by the customer. The principle should apply across all product types, with the exception of low-income market products. The product supplier should not dictate the fee, but may facilitate the payment of the fee (instead of the customer paying the adviser directly), however it must be clear that the advice fee is separate from and in addition to product charges. The quantum of the upfront or ongoing fee will not be prescribed, but certain disclosures will be required. Cross-subsidisation by product charges is not allowed. Product supplier to monitor tied advisers and report to the regulator, including the advice fees charged and the quality and scope of planning services. Product supplier to monitor multi-tied advisers, including the advice fees charged and the quality and scope of planning services.
Proposal KK: Additional standards for ongoing product advice fees
The customer must agree to receive ongoing advice, and there must be ongoing advice in order to receive the fee. The customer should also be able to 'opt-out' if the fee is paid periodically and the advice is not provided; conversely the adviser may stop the advice if the fee is not paid.
Proposal LL: Product suppliers to facilitate advice fees
For investment products, product suppliers will be obliged to offer a facility to customers to deduct the fees (upfront or periodic) and pay these to the adviser. This facility offered by the product supplier should be the same regardless of the adviser (IFA, multi-tied or tied), and the fees which form part of this facilitation service must be clearly disclosed to the customer. The customer can elect whether the fees will be paid from the amount of any investment contribution paid or from the value of the investment product. The customer may also cease or amend the deductions.
Remuneration for services connecting product suppliers and customers – sales execution ("selling") and ongoing product maintenance and servicing by intermediaries
Proposal MM: Remuneration for selling and servicing investment products
In respect of investment products, product suppliers will be prohibited from paying any form of remuneration to intermediaries, and intermediaries may only earn advice fees paid for by the customer. Product suppliers may therefore not include any costs associated with intermediary remuneration in the structure of the product charges. Exceptions will apply to products targeted at the low-income market.
Proposal NN: Remuneration for selling and servicing life risk products
It is proposed that 50% of the remuneration payable is paid upfront as sales commission and the remaining 50% be paid on an as-and-when basis. The level and the structure of the commission and service fee will continue to be subject to regulation caps. Commission 'clawback' provisions will be retained. Under certain circumstances, where an intermediary performs ongoing product maintenance or servicing on behalf of the insurer, the life insurer may pay a fee to the intermediary for providing such services.

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

In respect of replacement of life risk policies, long-term insurers will be prohibited from paying any form of commission or fee to intermediaries, and intermediaries may only earn advice fees paid for by the customer.

Proposal PP: Commission regulation anomalies on ‘legacy’ insurance policies to be addressed

Commission regulations under the Long-term Insurance Act will be amended to consistently apply the same commission basis to variable premium increases on ‘legacy’ investment policies as is currently applied to new investment policies.

Proposal QQ: Conflicted remuneration on retirement annuity transfers to be addressed

Strengthened disclosure requirements will be required to ensure the cumulative impact of the transfers is communicated clearly. Specific obligations on both the transferring and receiving funds and / or product suppliers is being considered.

Proposal RR: Equivalence of reward to be reviewed

Relates to the basis on which long-term insurers may remunerate their tied advisers. This equivalence applies at the level of each individual tied adviser. The standard will detail the nature of the remuneration and benefits to be taken into account in assessing equivalence, and apply guidance as to when to apply the principle of equivalence.

Proposal SS: Standards for remuneration arrangements between adviser firms and their individual advisers

Any portion of the individual adviser’s remuneration attributable to advice or sale of an investment product may not in aggregate exceed the value of customer advice fees paid over an appropriate period.

Proposal TT: Special remuneration dispensation for the low income market

Elements to be considered include permissible commission limits, permissible product supplier / intermediary relationships and the types of intermediary and advice services qualifying for this dispensation.

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

The as-and-when model will be retained, and the level of the commission and service fee will continue to be subject to regulation caps although the new maximum commission and service levels are still to be determined. Additional fees over and above commission will be removed as short-term advisers will be able to earn advice fees from customers, separate to commission. The service fee component of the intermediary’s remuneration will be subject to certain conditions.

Proposal VV: Conditions for short-term insurance cover cancellations

Confirmation that the client is aware of the cancellation is necessary, and in the event of cancellation by an insurer, the original insurer should remain on risk until confirmation is received.

Remuneration for services connecting product suppliers and customers – direct non-advice sales execution; aggregation and comparison services; and investment platforms

Proposal WW: Remuneration for direct non-advice sales execution

Standards will seek to ensure that remuneration models are commensurate with the fact that no advice or ongoing product maintenance or servicing is provided.

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

The current regulatory provisions will be reviewed, and standards to address potential conflicts of interest from “commission sharing” or “commission splitting” may be put in place. Remuneration should be reasonable, transparent and not conflicted.

Proposal YY: Remuneration for investment platform administration

Remuneration should be by means of a platform administration fee which the customer agrees to and pays for and which is disclosed to the customer. Payments from product suppliers or investment managers to LISPs are prohibited

Remuneration for outsourced services (services to product supplier)

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

Maximum binder fee, per binder activity, will be prescribed ranging between 1 and 3% of premium, per activity.

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

The current provision will be removed from the Long-term Insurance Act. The extent of additional remuneration available will be informed by the proposals relating to binders, outsourcing or ongoing product servicing / maintenance.

Proposal BBB: Outsourcing fee for issuing insurance policy documents

No separate fee over and above the binder fee may be paid if the intermediary is a binder holder, as the service is incidental to the binder function of entering policies. If the intermediary is not a binder holder, an initial fee may be paid (initially proposed at R100 per policy).

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

Any form of remuneration, incentive or other financial interest paid by the product supplier to the intermediary is prohibited unless it is specifically permitted in terms of legislation.

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