

MESSAGE

To: consult/SFC@SFC
cc:

CEO Ext :

From: "Glenn Turner" <glenn.turner@altruist.com.hk>
Date: 31/12/2009 10:55 AM

Subject: IFAA RESPONSE to the SEPTEMBER 2009 SFC CONSULTATION PAPER

To Whom It May Concern

Securities and Futures Commission

Please find attached the response from the Independent Financial Advisors Association to the September 2009 SFC Consultation Paper on "*Proposals to Enhance Protection for the Investing Public*".

May we take this opportunity to thank Mr Chung Hing Hing and his supporting team for their perseverance, diplomacy and stamina so admirably displayed throughout the meetings and various communications between the SFC and the IFAA, which have led up to the construction of this response.

We will be sending an original copy of the (attached) response in due course.

Regards,

Glenn Turner

Chairman - Independent Financial Advisors Association



IFAA Position Paper (Final Version) Sep 09 SFC Consultation.doc

The Independent Financial Advisors Association's
Response to
the SFC's September 2009 Consultation Paper on Proposals
to Enhance Protection for the Investing Public

1. INTRODUCTION

The Independent Financial Advisors Association ("IFAA") is the first industry association specifically for corporations [IFA *firms*] engaged in the provision of financial advisory services in Hong Kong to the retail investing public. Founded by a group of industry veterans, the IFAA aims to reach out to three core audience groups, namely government regulatory bodies, IFAA members [that is, IFA *firms*] and the general investing public. The IFAA assists the IFA *firms* and their independent financial advisors in keeping abreast of international best practices.

The IFAA aims to provide and cultivate the development of professional independent financial advisory services to further enhance Hong Kong as the preferred regional financial services centre, and takes on the mission, as the voice of the IFA (*firms*) community in Hong Kong, to support and campaign for an equitable wealth management industry through advocacy of regulatory convergence in the insurance, banking and broking industries.

With its focus on financial advisory services in Hong Kong, the IFAA is interested in sharing its views with the Securities and Futures Commission ("SFC"), and therefore will, in the following sections, make general comments on the subject consultation paper, and give specific response to Parts III and IV of the consultation paper (respectively related to intermediary conduct and proposed cooling-off arrangements for financial products).

The IFAA has a mandate from its Members (IFA *firms*) to take positions on such issues.

2. General Comments

The IFAA supports the SFC's efforts in carrying out consultation with practitioners in the industry and members of the investing public for the design and implementation of suitable measures for protection of the interests of the investing public.

Therefore the IFAA agrees with the overall objectives of the subject consultation papers.

On the other hand, the IFAA believes that efforts should be made to achieve a balance between the following factors:

- (i) Genuine benefits to the investing public -- It depends on whether the proposals can lead to disclosure of meaningful information understandable by the investing public, and which will not cause unnecessary hindrance in terms of time and costs to their investment opportunities.
 - (ii) Costs to practitioners -- There should be a balance between costs/benefit efficiency.
 - (iii) Practicality -- New measures should be made easy to understand and implemented. Suitable guidelines and templates should also be provided to practitioners for consideration.
 - (iv) Level playing field -- There should be coordination amongst various regulators for different financial products, such as the SFC, the Insurance Authority, the H K Federation of Insurers, the H K Confederation of Insurance Brokers, the Professional Insurance Brokers Association etc., in order to ensure adoption of consistent protection measures across different spectrums of the financial service industry in Hong Kong. This is essential for the elimination of possible "regulatory, compliance and product arbitrage".
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3. IFAA's Specific Response

Q18:	<i>While it is proposed that these proposals will generally apply to all investment products (securities and futures products), the SFC would like to seek your view as to whether you agree that some of these proposals may be more applicable to unlisted investment products because of the different operation needs, information disclosure framework etc of such products?</i>
Ans.	<p>The IFAA is against either product or regulatory arbitrage. This means to us that an insurance Broker selling a unit-linked insurance product and an Agent under the HKFI/IARB regime selling a unit-linked insurance product should either <u>both have</u> to disclose remuneration or <u>both not have</u> to disclose remuneration (avoiding regulatory arbitrage). Similarly, a product such as unit-linked insurance, which we note has been carved out of the SFC consultation paper, and a product such as a mutual fund, which is included within the SFC Consultation paper, should <u>both have</u> either remuneration disclosure or <u>both not have</u> remuneration disclosure (avoiding product arbitrage).</p> <p>Nevertheless, the SFC has requested a response to Q 18 and we answer, but in the context of the preceding paragraph.</p> <p>Since the SFC has determined a course of action, which will undoubtedly add to the opportunities for product arbitrage we believe that remuneration disclosure should not even apply to ALL unlisted products but disclosure should apply to only some unlisted products. There are some unlisted products, which are simple in nature where the investing public does</p>

	<p>not commonly require advice from intermediaries (example, units in mutual funds). Disclosure would compromise the ease of the investing public to deal swiftly with such products.</p> <p>We therefore suggest that unlisted products, which have more than a 30% exposure to ISDA and other derivative products, should be subject to disclosure.</p>
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<p>Q19:</p>	<p><i>Do you think that intermediaries should, as part of their “know your client” procedures, seek clients’ information about their knowledge of derivatives and characterize those clients (other than those professional investors) with such knowledge as “clients with derivative knowledge” to assist intermediaries in ensuring that investment advice and products offered in relation to unlisted derivative products are suitable?</i></p> <p><i>Please give your views on the contents of the proposed measures for intermediaries to assess whether investors have knowledge of derivatives.</i></p>
<p>Ans.</p>	<p>No, the product universe and its constant evolution will always put the client in a ‘catch up situation’. The lack of clarity in the definition of derivative also makes it difficult. The IFAA would be interested to learn how other established markets are dealing with this concern.</p>

<p>Q20:</p>	<p><i>Should a high net worth investor be considered to have specific knowledge and expertise if: -</i></p> <p><i>(a) he is currently working, or has previously worked in the relevant financial sector for at least one year in a professional position that involves the relevant product; or</i></p> <p><i>(b) he has undergone training or studied courses which are related to the relevant product?</i></p> <p><i>Do you have any other suggestions?</i></p>
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Ans.	<p>(a) Yes, we agree with the idea of making use of 'deemed knowledge' in assessing the investor's actual knowledge, but in relation to the overall "Professional Investor" mechanism, we need to be clear as to what relaxations are applicable for a Professional Investor and what restrictions there will be for non-PI's. It will be for the benefit of the industry as well as the investing public if there is a specific (<i>prescriptive</i>) way of dealing with PI and non-PI clients, particularly in relation to complicated products.</p> <p>(b) Yes, but the IFAA considers it necessary to set a specific time frame. Thus, IFAA would like to see the requirement for signed client declaration to the effect that training and study was undertaken within the last 12 months and controls for ensuring that the material studied was not outdated.</p>

Q21:	<i>What amount should the minimum portfolio requirement be set at? Please give your reasons.</i>
Ans.	The IFAA does not consider the change of current level of HK\$8M will have little impact on the theme of the present consultation, that is, investors protection, and therefore sees no reason for it to be increased in the near future.

Q22:	<p><i>Where a distributor and/or any of its associates explicitly receives or will receive monetary benefits from a product issuer (directly or indirectly), which of the following three disclosure options would be more appropriate? Please explain your views.</i></p> <p><i>Option 1.1 – Disclosure of dollar amount or percentage</i></p> <p><i>Option 1.2 – Disclosure of percentage bands or ceiling</i></p> <p><i>Option 1.3 – Generic Disclosure</i></p>
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	IFAA believes that Option 1.3 Generic Disclosure would be the most sensible format to use. We believe that Generic Disclosure, which is what practitioners in the IFA industry are currently doing via existing client agreements, is easier for the investing public to understand.
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Note: IFAA adopts similar response to questions 23 to 25 based on its response to question 22.

Q26:	<i>Do you consider it appropriate to restrict distributors from offering investors supermarket gift coupons, audiovisual equipment and other kinds of gifts having monetary value (except discount of fees and charges) in promoting a specific investment product to investors?</i>
Ans.	Yes, we consider it appropriate to eliminate the offering of gifts. Focus should instead be on whether the promoted financial products will be suitable for clients, and we don't feel it appropriate to offer cash or voucher based incentives for undertaking investments.

Q27:	<i>Do you have any comments on the proposed information content of the Sales Disclosure Document which includes (a) capacity (principal or agent) (b) affiliation with product issuer (c) monetary and non-monetary benefit (d) discount of fees and charges available to investors?</i>
Ans.	IFAA supports the inclusion of (a) and (b) as proposed, as well as (c) for generic disclosure for unlisted complicated structured products. For (d) The IFAA believes there is no need for this to be included in the document because it may lead to confusion.

Q28:	<i>Do you think audio recording of the client risk profiling process and the advisory or selling process for investment products should be made mandatory or the current record keeping requirements are sufficient? If audio recording is made mandatory, how long do you think these audio records be kept for? Please explain your views.</i>
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Ans.	<p>No, we believe it to be impractical and it tends to unnecessarily and significantly prolong investment procedures.</p> <p>We do believe that there are currently sufficient requirements for practitioners to conduct suitability checks before or at the time of sale, and from time to time each product provider or distributor should be able to make post sale internal compliance checks.</p>
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Q29:	<p><i>Do you believe that a cooling-off period would generally be beneficial for investors, or do you believe that costs associated with its implementation would outweigh the benefits for investors?</i></p>
Ans.	<p>First of all, we would need clarification of product type before being able to answer the question satisfactorily. For example, if it refers to unlisted mutual funds, it seems to be unnecessary since investors will already have opportunities to realize their holdings.</p> <p>Further, generally speaking, a cooling off mechanism may lead to more costs than benefits to investors. By way of example, in light of the opportunity to cool off, they may tend to pay less attention to suitability, and one has to be mindful that cooling off can hardly be available at no cost, since there is always the need to make adjustments for actual market performance at the time of cooling off, and administrative costs will also be incurred.</p>

Note: IFAA adopts similar response to questions 30 to 31 based on its response to question 29.

Q32:	<p><i>On the basis that a cooling-off period is incorporated in an investment product and a client has exercised his right under the mechanism, do you consider that a distributor should promptly pass on to the client the full amount of refund (including the sales commission) received from the product issuer less a reasonable administrative charge? Please explain your views.</i></p>
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Ans.	<p data-bbox="288 309 1070 342">IFAA reiterates its stance regarding cooling-off period.</p> <p data-bbox="288 376 1404 528">On the assumption mentioned in the question itself, IFAA says "yes", and considers it a must for the distributor to pass on to the client the full amount of refund on "cooled off" structured or term products, in cases where the distributor has received the same from product provider.</p>
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