Janet Yuen
Mandatory Provident Fund Schemes Authority
Level 16, International Commerce Centre
1 Austin Road West, Kowloon,
Hong Kong.

16 July 2012

Dear Mrs Yuen,

Guidelines on Conduct Requirements for Registered Intermediaries

Thank you for forwarding the email from Darren McShane on 22 June 2012. We would also like to thank the Mandatory Provident Fund Authority (MPFA) for allowing the Institute of Financial Planners of Hong Kong ("IFPHK") the opportunity to review and comment on the draft Guidelines on Conduct Requirements for Registered Intermediaries (the "Guidelines"). The Mandatory Provident Fund (MPF) system has been in operation for over 10 years. The Government and the MPFA have been continuously working with the industry towards improving the system. One of the initiatives is to enhance the supervision of sales and marketing activities of MPF intermediaries. As such, the Mandatory Provident Fund Schemes (Amendment) (No. 2) Bill 2011 (the "Bill") was passed on 21 June 2012. After the passing of the Bill the long awaited Employee Choice Arrangement (ECA) and a new statutory regulatory regime for MPF intermediaries will be implemented on 1 November 2012. It is envisaged that the implementation of ECA will allow MPF members to transfer their accrued benefits derived from their own mandatory contributions made from an existing MPF scheme to another MPF scheme of their own choice once per calendar year (i.e. from 1 January to 31 December in any given year).

As a leading professional body serving the financial planning community, IFPHK is obliged to respond to policy changes that may have an impact on our members and their clients. Retirement planning is considered an important focus among the other financial topics discussed daily by financial planners. Today, out of the 14,000 IFPHK members in Hong Kong, approximately 42% are registered as MFP intermediaries. IFPHK submitted its opinion on the supervision of sales and marketing activities of MFP intermediaries in April last year. IFPHK also responded to the consultation documents on early withdrawal of MPF benefits in March this year. Hence, the IFPHK does have specific comments on the Guideline that we wish to highlight for your consideration:

1. **Difficulties implementing and executing specific requirements in the Guidelines**
   IFPHK understands that the Guidelines are to protect the 2.5 million scheme members, but some of the requirements are either too vague or too specific. As such they pose a great challenge to the registered intermediaries' operations and have resulted in high compliance costs. Unlike retail investment products, MPF products are mandatory. All the working population must make MPF contributions and likewise registered intermediaries do not have the discretion to reject clients' investments. Moreover, MPF products are subject to stringent product approval and investment restriction. It is doubtful whether the same investor protection measures for retail products could be applied to MPF products. In this regard, IFPHK would like to highlight some of the concerns that have been raised by our members on the requirements stated in the Guidelines:

   a) Care for clients with special needs
      Registered Intermediaries are required to provide "extra care" to clients with special needs ("vulnerable clients"). A vulnerable client is defined in the Guidelines as "a person who is not, or may not be able to fully understand the type of information to be

provided and discussed, or may not be able to make that key decision." A key decision is defined as "one which is discretionary and could have potentially materially detrimental impacts on the client." IFPHK and the industry players it interviewed consider that the definition is too broad and obscure as it involves judgment of a person's mental ability to make a key decision. It may therefore lead to confusion and varying interpretations. IFPHK suggests the MPFA to refine the requirements and provide more specific guidance to the intermediaries.

b) Suitability Assessment
It is stipulated in the Guidelines that registered intermediaries should fully assess a client's circumstances so that the regulated activity is appropriate to the client. As a minimum, a registered intermediary should conduct a "suitability assessment". According to the Guidelines, a suitability assessment should be conducted when there is a choice between two constituent funds ("constituent fund level"). So, if registered intermediaries advise on a transfer of accrued benefit from one registered scheme to another registered scheme where there is no advice on transfer of constituent fund, a suitability assessment is not required. Such practices will confuse consumers as they may have little knowledge on the difference between registered scheme level and constituent fund level. In our view the MPFA should educate the public on the scope of regulated activities to avoid different expectations.

c) Switching constituent funds without taking on advice
At present, it is very popular for scheme members to switch funds in a registered scheme using the provider's online platform. Such action may or may not involve an invitation, inducement or advice from a registered intermediary. Even if a registered Intermediary did provide advice, it is difficult for them to control exactly when a customer may decide switch funds. It is possible that by the time the customer has decide to switch funds using the online platform, the advice he or she relied upon may no longer be relevant to their circumstance. The situation may be complicated if the scheme members are investing in risk mismatched funds. Thus, it is problematic for registered intermediaries to identify those scheme members using online services whose actions are based on the advice of a registered intermediary and to perform the required procedure as stipulated in the Guidelines. Such requirements would be onerous to the industry and very inconvenient to customers.

d) Post sales call
Post sale calls have to be made within seven working days with audio recording of the call made to a vulnerable client or when a client has invested in a constituent fund that does not match their personal profile. IFPHK acknowledges that there is similar practice covering the Investment Linked Assurance Scheme ("ILAS"). IFPHK would like to remind the MPFA not to underestimate the administration burden arising from these measures. ILAS is a product for which investors make voluntarily investment decisions, while MPF products are mandatory. The number of potential consumers is 2.5 million and therefore any compliance costs associated with post sales call will be material.

e) Guaranteed fund
In respect of the transfer in and out of guaranteed funds, industry players IFPHK interviewed believe that it might not be practical to make it compulsory for registered intermediaries to ask clients to check the offering document of the original scheme prior to any transfer. Industry players consider that the risk warning and explanation provided to clients are adequate to serve this purpose.

f) Fund comparison
It is sensible to require registered intermediaries to provide information on fees and charges of registered schemes or constituent funds. Nevertheless, fund comparison is only feasible at standard fee level. Since there are no standard forms of discount and

rebate, it is very difficult to provide a comprehensive like-for-like comparison of constitute funds.

It is generally believe that launching ECA will encourage competition and thus drive down fees and improve service. IFPHK considers that the benefits of ECA will also be to provide customers with more choices so that they can have more incentive to plan for and control their retirement. As a result, the focus of ECA should not only be on fee reduction. IFPHK anticipates that the conduct requirements in the Guidelines, if implemented fully, would add significant compliance and administration costs to the industry. Therefore it is unhelpful to focus solely on the fee reduction impact of ECA. Fee reduction is a result of economies of scale and an increase in public interest in retirement planning. The MPFA should clearly convey these messages to the public.

2. **Competency of MPF intermediaries**

Registered intermediaries are required to perform a suitability assessment by taking into account the client's personal profile. The personal profile includes an assessment of the client's existing investment portfolio, current age, intended retirement age, financial situation, investment objective, investment knowledge, investment experience, risk tolerance and the level of risk the client is prepared to accept. The registered intermediaries have to match the client's personal profiles with the risk profiles of the constituent funds. Such profile matching practice greatly resembles the financial planning six-step process IFPHK has promulgated. For IFPHK and others affiliates of the Financial Planning Standard Board ("FPSB"), the financial planning process consists of six steps that help clients take a holistic approach to assessing their financial situation. The process involves gathering relevant financial information, setting life goals, examining a client's current financial status and coming up with a strategy or plan for how clients can meet their goals given their current situation and future plans.

The Guidelines state that a principal intermediary should provide sufficient training to ensure that its subsidiary intermediaries are competent when engaging in regulated activities. That care, skill and diligence include understand MPF system, MPF products and relevant concepts and promoted registered schemes and constituent funds. However, by requiring intermediaries to perform suitability assessment and risk profiling, MPFA is expecting intermediaries to have a competency level that is beyond what is stated in the Guidelines.

Given the MPF is a unique product type where benefits accrue over the long-term, intermediaries should be equipped with financial planning skills and knowledge that enable them to perform a proper analysis of a client's personal profile and offer advice that could meet the client's life goals. IFPHK believes that product and basic investment knowledge alone will be insufficient to fulfill the upcoming demands of personal financial advisory and planning services after the implementation of ECA. In consideration of the interest of 2.5 million consumers, it is the priority of the MPFA to specify the body of knowledge required to perform a regulated activity. The MPFA should also include and increase coverage of financial and retirement planning into the core curriculum and in the examination and continuous professional education program in order to equip the 30,000+ intermediaries with the necessary skills and knowledge to confidently provide MPF related advice that suits customer needs and expectations.

3. **Level playing field**

In our previous submission to MPFA, IFPHK stressed the importance of adopting policy changes that applied to all financial intermediaries servicing consumers and that failure to implement a consistent approach across the industry could result in significant negative consumer and industry incidents. Though the Guidelines are a uniform standard for sales and marketing activities of MPF products, they could be interpreted or implemented in a number of ways if they are to be executed by different frontline regulators (FRs). Collaboration between different regulators and the efficiency of their joint supervision will be the critical success factor for the development of the MPF industry. Again, IFPHK is urged by industry professionals to highlight the need for implementing a consistent approach across the industry to establish a **'level playing field'** among all registered intermediaries in the different distribution segments, i.e. banking, insurance and independent financial advisors.

4. Investor Education

The industry's reputation is tainted by scheme members' misunderstanding and misconception regarding the MPF and retirement planning. MPF has a negative reputation with its "high fees" and "poor performance". A survey conducted by Convoy in 2011 found that "more than 80% of the respondents believed that the current MPF scheme was inadequate to provide a satisfactory retired life"[1]. A similar result was found in a survey by Manulife. The survey revealed that 81 percent of respondents claimed that their pensions would not be able to cover the costs of inflation and rising living expenses once they stopped working.[2]

IFPHK acknowledges MPFA continuous efforts in promoting the MPF system. MPF education programs are visible in the mass media, which successfully raise public awareness of MPF investment in recent years. The survey by Convoy revealed that the public has growing concerns about their MPF investment. Nearly half of respondents actively reviewed or adjusted their investment portfolio in their MPF accounts, and 70% of them were aware of whether their accounts made a gain or loss[3]. Despite this growing awareness in MPF performance, few persons have plan for their retirement. The survey conducted by Manulife indicated that even if the respondents thought that MPF could not support their retirement living, only 22 percent had even considered additional retirement planning. Fewer than 40 percent of respondents had actually made any inroads into their retirement saving plans. On average, respondents began such planning at age of 43 for a retirement they expected to begin just 13 years later at age 60[4].

Hong Kong has one of the world's fastest growing ageing populations. It is expected that MPF and retirement planning will become more prominent within our society over the coming few years. Therefore the government and MPFA should be prepared for the increase in demand for education and knowledge from the industry and the public. The report from Ernst & Young commissioned by the Joint Industry Group pointed out that there is an absence of personal financial advice to help MPF members make an informed choice[5]. IFPHK thinks the Implementation of ECA is a golden opportunity to enhance the professional standards of MPF intermediaries and to develop the financial and retirement planning industry in Hong Kong. IFPHK and its members are ready to assist in this development.

To summarise, there are four important messages conveyed by IFPHK in this letter:

1. Consumer protection requirements of retail investment products may not be applicable on MPF products. The MPFA, as the lead regulator, should continue to work together with the industry to refine the Guidelines. It should avoid implementing requirements that are onerous to the industry and work towards reducing the regulatory burden and compliance costs without jeopardizing consumer protection.

2. It is apparent that MPF intermediaries need to be equipped with more financial and retirement planning knowledge and skills in order to meet the conduct requirements of the Guidelines and to meet the expectations of the 2.5 million customers. IFPHK strongly suggests MPFA include financial planning and retirement planning in the core curriculum

[1] Convoy's Survey Finding – Public's Growing Concern about MPF Scheme, Convoy Press Release, 14 December 2011
[2] "Hong Kong Citizens Aren't doing enough for retirement, Insurance International News, 10 February 2012.
[3] Convoy's Survey Finding – Public's Growing Concern about MPF Scheme, Convoy Press Release, 14 December 2011
[4] "Hong Kong Citizens Aren't doing enough for retirement, Insurance International News, 10 February 2012.
[5] "The evolving MPF system: an objective assessment", Ernest & Young, HKFI, HKIFA and HKTA, May 2012

of MPF education and CPD requirements.

3. Any policy change should be aimed towards building a level playing field across distribution channels and different sectors of the industry. IFPHK believes that failure to implement a consistent approach across the industry could result in significant negative consumer and industry consequences and could expose the risk of regulatory arbitrage. IFPHK reminds the MPFA as the lead regulator to co-ordinate and communicate with other FRs to avoid any difference in interpretation and application of the Guidelines that would result in an unlevel playing field.

4. Continue to improve and enhance the investor education programs. Greater emphasise should be placed on promoting the need for retirement planning, and the availability of a financial and retirement planning advisory service that can assist clients in making informed MPF decisions and retirement plans.

In conclusion, IFPHK believes that qualified intermediaries and well-educated scheme members are the cornerstone to the successful implementation of the ECA.

Once again, we would like to thank you for allowing us the opportunity to be involved in the consultation. Please note that the views expressed above have not been arrived at after a full consultation with our members. We would be happy to undertake a more broad-based member consultation if you believe any of the above points require further investigation. Please do not hesitate to contact us if you would like to discuss any of the above suggestions in greater detail.

Yours sincerely,

Dennis Lau
Chief Executive Officer
Institute of Financial Planners of Hong Kong