Institute of Financial Planners of Hong Kong
香港財務策劃師學會
IFPHK

IFPHK's Response to the Securities and Futures Commission's Further Consultation on Proposed Disclosure Requirements Applicable to Discretionary Accounts

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Institute of Financial Planners of Hong Kong (IFPHK) Profile

Background

The IFPHK was established in June 2000 as a non-profit organization for the fast-growing financial industry. It aims to be recognized in the region as the premier professional body representing those financial planners that uphold the highest standards for the benefit of the public.

The IFPHK is the sole licensing body in Hong Kong authorized by Financial Planning Standards Board Limited to grant the much-coveted and internationally-recognized CFP^{CM} certification and AFP^{TM} certification to qualified financial planning professionals in Hong Kong and Macau.

It represents more than 6,800 financial planning practitioners in Hong Kong from such diverse professional backgrounds as banking, insurance, independent financial advisory, stockbroking, accounting, and legal services.

Currently there are more than 147,000 CFP certificants in 24 countries/regions; the majority of these professionals are in the U.S., Canada, China, Australia and Japan, with more than 4,700 CFP certificants in Hong Kong.

CFP^{CM}, CERTIFIED FINANCIAL PLANNER^{CM}, CFP^{CM}, CERTIFIED FINANCIAL PLANNER ™, AFP^{TM}, ASSOCIATE FINANCIAL PLANNER^{TM}, AFP® and ASSOCIATE FINANCIAL PLANNER® are certification marks and/or trademarks owned outside the U.S. by Financial Planning Standards Board Ltd. The Institute of Financial Planners of Hong Kong is the marks licensing authority for the CFP marks and AFP marks in Hong Kong and Macau, through agreement with FPSB.

IFPHK's interest in this consultation

The mission and vision of the IFPHK is to promote the importance of financial planning. Financial planning refers to the process of setting, planning, achieving and reviewing life goals through proper management of finances[1].

Since its inception, the IFPHK has been striving to raise public awareness of the financial planning industry in Hong Kong and highlight the high standards that CFP professionals adhere to. In 2006, with contributions from our patrons, leading industry practitioners and experts, the IFPHK published the *IFPHK Practice Guide for Financial Planners*. The Guide is the first set of guidance materials for financial planners practicing in Hong Kong. To supplement this effort, the IFPHK launched the Guidance Note entitled *Suitability of Advice Obligations: Documenting your Financial Advice* for its members.

It is also the IFPHK's mission to protect public interest. In 2009, we provided our comments to the proposal to enhance the protection of the investing public. The proposal was put forward by the SFC as a result of the aftermath of the Lehman Brothers Minibond Saga. In 2010, the IFPHK submitted a response to the consultation paper on the proposed establishment of an Investor Education Council and a Financial Dispute Resolution Centre. In 2014, we responded to the Consultation Document on having an effective resolution regime in Hong Kong. In 2016, we

[1] www.fpsb.org

provided comments on Hong Kong's Financial Competency Framework and Hong Kong's Strategy for Financial Literacy. The list of the IFPHK's responses to the various consultation papers can be found on our website (http://www.ifphk.org/ee/importance-of-advocacy).

Last year, IFPHK submitted our opinion on the proposed enhancement in point of sales transparency. Part of our feedback has been summarized in the Consultation Conclusion. In view of the above, the IFPHK is interested in expressing its views on this further Consultation Paper.

IFPHK's representation

The IFPHK was founded by 30 members (the 'Founding Members') in order to raise the standards of financial planners and highlight the importance of sound financial planning.

The IFPHK currently has 37 Corporate Members including banks, independent financial advisors, insurance companies, and securities brokerages. With our Corporate Members providing a full spectrum of the client services and products, the IFPHK is well positioned to understand the needs, concerns and aspirations of the financial planning community.

Executive Summary

On 16 November 2017, the Securities and Futures Commission (SFC) released consultation conclusions on proposals to enhance asset management regulation and point-of-sale transparency (Note 1). The SFC also launched a further consultation on disclosure requirements applicable to discretionary accounts. The two-month consultation is on the proposed requirements for disclosure of monetary and non-monetary benefits by licensed or registered persons to discretionary account clients. The submission deadline is on 15 January 2018.

Consistent with our previous submission on the proposals of enhancing point-of-sales transparency, our submission is based on the following principles:

1. Advocating the six-steps financial planning process

2. Aligning with international best practice

3. Enhancing consumer protection

4. Promoting responsible investing attitudes of consumers through financial education

Based on the above principles, the IFPHK agrees with the current proposals set out in the Consultation Paper.

Out of the two options for disclosure of monetary benefits under explicit remuneration arrangement, IFPHK considers option 2 – specific disclosure of the aggregate amount in percentage term maybe more appropriate to provide an overall picture to clients. However, the intermediaries must ensure that clients understand the underlying assumptions of the disclosures.

As stated in our previous submission, IFPHK advocates non-salary compensation should be disclosed to the client in a manner that is clear, concise, understandable and comparable, and aligned to services that deliver value to the client. The cost for financial planning advice should be separately and clearly identified from the other services provided by the financial planner and disclosed as an amount rather than a percentage, unless the total costs are unknown at the time of disclosure. Regardless of the compensation model used, the financial planner should communicate to the client sufficient information about the likely consequences to the client as a result of using a particular charging model.

In light of consumer protection, the IFPHK thinks it will be useful to disclose in the statement the actual trailer fees received in dollar amounts on annual as well as on accumulated basis.

The SFC Consultation

On 16 November 2017, the Securities and Futures Commission (SFC) released consultation conclusions on proposals to enhance asset management regulation and point-of-sale transparency. The SFC also launched a further consultation on disclosure requirements applicable to discretionary accounts. The two-month consultation is on the proposed requirements for disclosure of monetary and non-monetary benefits by licensed or registered persons to discretionary account clients.

The Consultation Paper contains three questions relating to the aforementioned proposals.

1. Do you have any comments on the proposed disclosure requirement in relation to monetary and non-monetary benefits for discretionary accounts set out above?

2. Do you have any comments on the suggested manner of disclosure set above? Do you have any other suggestions to ensure the disclosure will be clear, fair, meaningful and easy to understand for investors?

3. Do you think a six-month transition period following the gazettal of the final form of the amendments to the Code of Conduct is appropriate? If not, what do you think would be an appropriate transition period and please set out your reasons.

IFPHK's Submission

Consistent with our previous submission, the IFPHK's comments are based upon the following principles and beliefs which are:

1. Advocating the six-steps financial planning process

2. Aligning with international best practice

3. Enhancing consumer protection

4. Promoting responsible investing attitudes of consumers through financial education

Please refer to IFPHK's previous submission for the details of the above principles.

Questions raised in the Consultation Paper

It is stated in the Consultation Paper that some intermediaries may have incentives for their clients under discretionary products which bring higher rewards or benefits to themselves. This gives rise to potential conflicts of interest. Addressing some respondents commented that it would be impossible to provide specific details as to the nature and amount of the monetary benefits they would receive and retain for products purchased for their clients under discretionary portfolios prior to each transaction, the SFC proposed the following disclosure options for discretionary account in the Consultation Paper:

A. Monetary benefits (under explicit remuneration arrangement)

Option 1 – Specific disclosure by type of investment product
Under this option, an intermediary will disclose the maximum percentage of monetary benefits receivable by it and/or any of its associates by type of investment product. Monetary benefits include those benefits receivable by intermediaries and their associates under an explicit remuneration arrangement, including initial commission rebates and trailer fees.

Option 2 – Specific disclosure of the aggregate amount in percentage terms
Under this option, an intermediary will disclose an estimated maximum percentage of monetary benefits receivable by it and/or its associates. This is proposed to be calculated by aggregating the maximum monetary benefits receivable from each product type according to the proportion such product type represents in a client's investment portfolio.

B. Monetary benefits (under non-explicit remuneration arrangement) and non-monetary benefits

- An intermediary may purchase an in-house product for its clients which without an explicit remuneration arrangement.
- In such cases, the intermediary will be required to make a generic disclosure that it will benefit from purchasing in-house products for a client under a discretionary portfolio.

- Where an intermediary will receive non-monetary benefits from a product issuer when purchasing an investment product for a client, it will also be required to make similar generic disclosure

All the proposed disclosures are to be made to investors at the account opening stage or prior to entering into a discretionary client agreement. The disclosure must be made in writing, electronically or otherwise.

In line with the existing position under the Code of Conduct, intermediaries will not be exempt from this proposed disclosure requirement with respect to clients who are Individual Professional Investors, but may be exempt with respect to Institutional and Corporate Professional Investors.

Question 1:

Do you have any comments on the proposed disclosure requirement in relation to monetary and non-monetary benefits for discretionary accounts set out above?

IFPHK's Response

We are grateful that the SFC has incorporated IFPHK's comments on the enhancement on the point of sales transparency into the consultation conclusion. We have the following feedbacks on the current proposals in this further consultation paper:

Under explicit remuneration arrangement
Out of the two options for disclosure of monetary benefits under explicit remuneration arrangement, IFPHK consider option 2 – specific disclosure of the aggregate amount in percentage term maybe more appropriate to provide an overall picture to clients. Nonetheless, the disclosure is based on the asset type allocation estimated by the intermediary's manager; as such the intermediary is obliged to clearly disclose the underlying assumptions of the disclosure to clients.

Under non-explicit remuneration arrangement
We have no major disputes on the monetary benefits under non-explicit remuneration arrangement and non-monetary benefits.

Question 2:

Do you have any comments on the suggested manner of disclosure set out above? Do you have any other suggestions to ensure the disclosure will be clear, fair, meaningful and easy to understand for investors?

IFPHK's Response

The IFPHK generally agrees with the proposed changes as they are consistent with our principles.

As stated in our previous submission, the FPSB's white paper said non-salary compensation should be disclosed to the client in a manner that is clear, concise, understandable and comparable, and aligned to services that deliver value to the client. The cost for financial planning advice should be separately and clearly identified from the other services provided by the financial planner and disclosed as an amount rather than a percentage, unless the total costs are unknown at the time of disclosure. Regardless of the compensation model used, the financial planner should communicate to the client sufficient information about the likely consequences to the client as a result of using a particular charging model.

In light of consumer protection, the IFPHK thinks it will be useful to disclose in the statement the actual trailer fees received in dollar amounts on annual as well as on accumulated basis.

Question 3:

Do you think a six-month transition period following the gazettal of the final form of the amendments to the Code of Conduct is appropriate? If not, what do you think would be an appropriate transition period and please set out your reasons.

IFPHK's Response

We wish the SFC could provide more guidelines to the industry in the form of FAQs in order to ensure that practitioners fully understand the new requirements. The 6-month transition period is sufficient provided that the SFC answers specific questions of the industry via FAQs.