Pretium Services

Compliance for insurance people, by insurance people

September 2012 edition

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From Pretium

Associated Compliance – The Merger of Pretium Services (PS) and Intelligent Compliance & Education (ICE)

For over four years PS and ICE have been leveraging off each other's knowledge and practical experiences (we even share offices!). As both Compliance Practices operate primarily in the Category I space we often come across the same or similar opportunities.

Given this background a merger became the next logical step in the relationship. Between us we are the appointed Compliance Officers to more than 300 FSPs; including brokers, UMAs and a number of insurers.

Our new company, appropriately named "Associated Compliance", will be operative from January next year. Between us we will have eleven registered compliance officers operating throughout South Africa with one more about to be approved and three more busy with studies that will allow their move to Compliance Officer status.

The new company will operate with three distinct specialist divisions so that each can focus on the specific requirements of that market segment:

1. Brokers
2. UMAs and Insurers
3. Retail motor industry

Each division will be staffed by specific people handling the monitoring process, monitoring support and the licence profile change process as well as the overall management of the division.

ASSOCIATED COMPLIANCE

We will be working towards our target date of operating as Associated Compliance over the coming months as we look at integrating the staff operations, IT platforms and all other related business activities, which include expanding into the extra office

space that became available at our current home in Fairland.

Our new monitoring tool Associated Compliance Tool (ACT) and a new client relationship management tool (AC Clients) we have developed in conjunction with our IT providers will also roll out under the new Associated Compliance logo.

We look forward to your support as we move into this new phase of our business as we continue to provide you with unique and focused compliance services.

Should you have any questions please feel free to contact us.

Oops!

John Horsfall managed to fall off his bike – confirming Craig's view that exercise can be really bad for you – and as a result he will be out of circulation for a few weeks. We are not sure as yet just how long he will be out of action but we will keep all affected clients advised.

E-mails with attachments

We recently realised that we had not been receiving certain e-mails that had attachments. It is not clear when the problem started as we only realised there was a problem when the query arose as to why we had not done something or asked for information that the client understood we already had. As at the time of releasing this Newsletter the problem had not been resolved fully. So if you sent us something within the last month and have not had the expected response please give us a ring so we can check what we have received it.

We would like to suggest that you please ensure that when renaming scanned .pdf documents the following characters do not appear in the file name % . $ _ # @ –

Apologies for any inconvenience caused.

Broker Fees – their future

We started the discussion last month on this issue and since then nothing has developed. All present at the Compliance Institute of South Africa (CISA) meeting have accepted the minutes however we have been unable to escalate the debate into the insurance press as CISA are not happy to make any formal press release on the matter until such time as the FSB have released something more specific on the subject – so we will hurry up and wait.

The one public forum that we discussed this was the recent SAUMA AGM, held on 21 September, at which we were invited to talk on the legislation affecting UMAs (see article below).

We are also aware that the minutes from the initial meeting have been released to various clients of other Compliance Officers as evidenced by queries coming back at us from UMA/Insurer clients who have had queries from brokers who have been supplied with them.

So what happens in the meantime?

We certainly don't see that the FSB will suddenly start with regulatory action against brokers who continue to charge blanket fees to clients (outside of the changes needed for those that hold a binder or outsource agreement – on this aspect see later article). However, we do not recommend that you simply sit back and wait for the changes to be implemented. We would recommend the following course of action:

- Assess the income generated from current fees.
- Established what services you currently provide to your clients that do not fall within the definition of Intermediary Services i.e. sales, maintenance, renewal, claims, premium collection and establish what these cost to deliver.
- How are you currently obtaining clients' permission to collect the current fees? We would say that most rely on pure disclosure and use the fact that it has been disclosed and no questions have been asked by a client that equates to acceptance. This process will have to change as written approval will be needed going forward.
- Start considering the use of a client Service Level Agreement (SLA) if you are a member of the FIA you should be working on this already given that this is a

requirement of your Code of Conduct. For the rest of you we see this as something you will need. Our version of such a document would have you make it clear that you get paid for performing certain functions (i.e. Intermediary Services) and get remunerated for these via commission. If you have a binder and/or outsource agreement you will specify what these delegated functions are and how much you get paid for them. If you are providing additional services then you will specify these as well along with the fees that will be levied for these services. This document will then be signed by both parties.

- The services that you can consider could include;
  - Risk management surveys and related advice,
  - Uninsured claim recoveries,
  - Client aggregate excess management,
  - Claims work beyond the "post office" service envisaged by Intermediary Services,
  - Visits to clients. The regulations do not specify that you need to actually visit a client to deliver advice so where your modus operandi is to do this then we see this as a justifiable service that can be charged for.
- The fees that you intend to charge need to be justified and "reasonably commensurate with the work undertaken." We see this as leading to the end of blanket percentage based fees on all policies for all clients. We expect that Rand based fees will become the norm and that these will vary across your client base depending upon the services delivered. For example: personal lines clients tend to receive the least visits and as such are likely to be the ones where you will be least able to levy a fee.

Fees where you hold a binder and/or outsource agreement

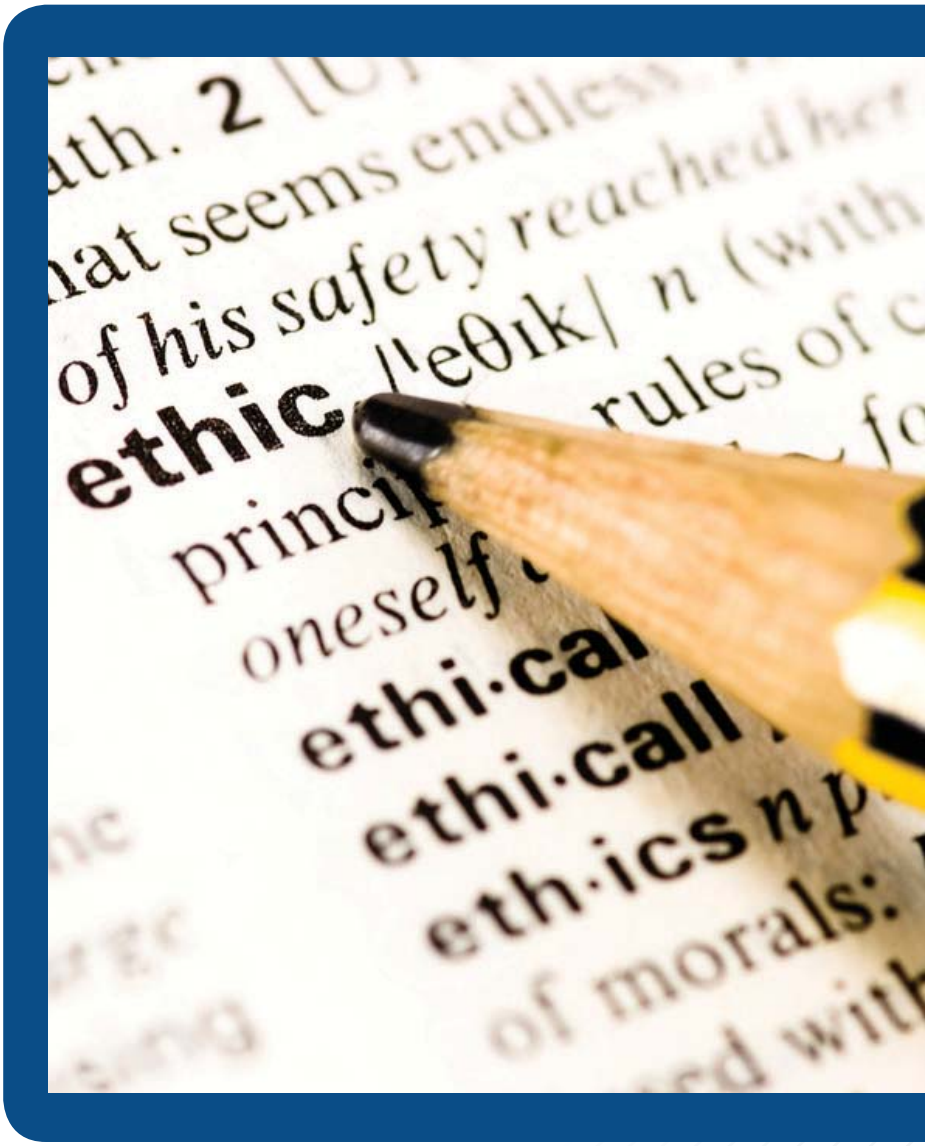
You will need to do all of the above but in your case you do need to make changes and make them now! The fee you are receiving needs to be specified in your Record of Advice and formal Disclosure Documentation. The current fees that you may be charging the client cannot replicate the fee being charged to the insurer. This may mean simply removing your client based fee altogether. If you are delivering justifiable additional services then a fee can continue to be charged but you will need to show that:

- The fee is indeed for services actually being delivered,
- That the fee is reasonably commensurate with those services. The fee can include a mark-up on your costs – but be sure you can establish what those costs are,

- That you have obtained the clients written approval to charge these fees. For new clients going forward this would be easier than for existing clients. A strategy will be needed for existing clients and we realise this may well take some time to achieve.

This process will need some amendments to your current documents. If this is likely to include IT developments we suggest that you "place your order" sooner rather than later.

We expect your insurer/s will expect an invoice from you each month for the fees to be paid – so make sure you can both identify the volume of business managed each month (assuming the fee will be premium based) and that you have the systems to issue invoices for them ready.



The implementation process is being hampered as most insurers have not yet delivered their proposed agreements and fee details to brokers but we urge those affected not to sit back and wait until they do – this will push your implementation into 2013 and cause you to be in breach of the regulations – a space you do not want to be in.

Are the issues around fees something your FAIS Compliance Officer need be concerned about? Yes they are as within section 3 (A) of the General Code of Conduct which state:

1. When a provider renders a financial service–

(a) representations made and information provided to a client by the provider–

(i) must be factually correct;

(ii) must be provided in plain language, avoid uncertainty or confusion and not be misleading;

(iii) must be adequate and appropriate in the circumstances of the particular financial service, taking into account the factually established or reasonably assumed level of knowledge of the client;

(iv) must be provided timeously so as to afford the client reasonably sufficient time to make an informed decision about the proposed transaction;

(v) may, subject to the provisions of this Code, be provided orally and, at the client's request, confirmed in writing within a reasonable time after such request;

(vi) must, where provided in writing or by means of standard forms or format, be in a clear and readable print size, spacing and format;

(vii) must, as regards all amounts, sums, values, charges, fees, remuneration or monetary obligations mentioned or referred to therein and payable to the product supplier or the provider, be reflected in specific monetary terms: Provided that where any such amount, sum, value, charge, fee, remuneration or monetary obligation is not reasonably pre- determinable, its basis of calculation must be adequately described; and

(viii) need not be duplicated or repeated to the same client unless material or significant changes affecting that client occur, or the relevant financial service renders it necessary, in which case a disclosure of the changes to the client must be made without delay.

So going forward we will need to be establishing and monitoring your structure and strategy on fees.

SAUMA AGM presentation

We were invited to do a presentation at this event held on 21 September. Our topic was "Current legislation – Impact on the UMA".

We touched briefly on issues such as:

- Treating Customers Fairly (TCF),
- Solvency Assessment and Management (SAM),
- Binders and Outsource agreements,
- The future of FAIS as the primary regulation of a UMA;

and the impact that these would have on the overall regulatory framework of a UMA. In short if they thought FAIS compliance was an issue for them they had better prepare for the new regime. As part of our new company structure we will be developing tools to assist the UMA and the insurer in monitoring at these levels.

We chose to look at the fee issues around binders and outsource agreements, which included the future of the broker fee, as outlined earlier in this Newsletter. We challenged the UMAs to consider the following as part of their strategy of complying with their new binder agreements:

- What should a UMA who currently charges a policy/admin/debit order fee do with those fees remembering that the intention of the regulation is to shift the cost burden of the extra layers of administration from the client to the insurer. If the UMA were to collapse the fee into the premium thus leaving the cost to client the same would this be seen as fair or even ethical? Had TCF been in place now we doubt this would be seen as treating the customer fairly.
- What responsibilities a UMA (and insurer) would have in the "control" of broker fees where they are being asked to collect them on behalf of the broker. This was not a popular idea but in our view unavoidable if the insurer is seen as needing to do so as they would need to delegate this to their UMA.
- Do they want to outsource policy issuing to brokers? And pay a "reasonably commensurate" fee for that?
- Can they deliver the changes in their systems in time?

For those of you operating with binders or outsource agreements and sub-brokers and you need some help getting the overall message around these regulations and impact on aspects such as fees we are prepared to assist with a workshop for your broker clients using our SAUMA presentation as the basis. Please contact Anke at our offices should you be interested in discussing the arrangements needed.

Higher Certificate Qualification via Milpark

With the release of the updated approved qualification listing from the FSB this qualification has been rated as Specific for Personal Lines and Generic for Commercial Lines, which is contrary to what students were told would be the case when enrolling. Milpark have advised us that they are appealing the rating.

So when is a specific qualification not a specific qualification? Milpark also provided a

neat summary on this issue that deals with this riddle:

"Just a point of clarity regarding the 'S' and 'SP' status as per the FSB's qualifications list: the relevant date here is 1/1/2010 as anyone first appointed in a FAIS role prior to this date may rely on 'S' as well as 'SP' status in respect of a specific subcategory. Anyone first appointed after 1/1/2010 may only rely on 'SP' status for exemption purposes.

It doesn't matter when a specific module is completed – completion of the full qualification is required. Currently the Commercial Lines subcategory only has 'S' status – meaning that someone appointed in a FAIS role prior to 2010 may get the exemption for that second level Regulatory Exam.

Remember that date of completion of the qualification is not relevant for exemption purposes on the second level Regulatory Exams – date of first appointment in a FAIS role is."

We expect that the expected Board Notice on the exemption process will further deal with this issue that is sure to cause confusion for months, if not years, to come.

Value Added Products and CPA disclosures: Many brokers and even UMAs have add-ons to their product offerings that are not actually insurance products but merely services provided by a variety of service providers.

In our view these offerings should not be "mixed in" with the insurance sections on the policy schedule nor should the cost be referred to as premium. The services and cost should be detailed as non-insurance products below the insurance sections on the schedule.

The providers of the services should be clearly stated so that the client is well aware of who is providing the service and who to contact in the event of a complaint i.e. The Consumer Commissioner as the FAIS & Short-term Ombud have no jurisdiction on non-insurance offerings.

Even when offered to clients who fall outside the protection of the CPA we believe the correct lay out is still essential.

This view is currently not the norm and is an area generally being overlooked by all concerned – but that does not make it correct does it?

From the FSB

RE exam deadline extended

This is probably old news by now but just in case anyone has been on leave and missed the news. For those who had not passed their first level RE exam by 30 June and were subject to the 30 September deadline now have until 31 March 2013 to complete the exam if they have not already done so. Exactly what caused the extension had not been published at the time we were "going to press" but it has to be based on poor success rates from those attempting it.

Binder & Outsource agreement implementation seminar

We attended this but found that nothing really new came out of the session. There were a number of questions where clear answers were not provided.

One of these key questions was around *"what is a reasonable rate of return?"* given that a UMA or broker can charge the insurer cost plus a reasonable rate of return. No real guidance was provided by the FSB except to say that they would be monitoring the various mark ups being allowed in their various monitoring processes and we have to assume from this that as they see what they believe is abuse that this will be dealt with. Over time we think we will see the playing fields level out somewhat after the initial implementation process.

The FSB were asked if the FSB even wanted to see the continuance of the UMA model, to which they replied that they did indeed see that the UMA model was important.

Delegation of a binder function by a UMA is not allowed but apparently the FSB are

looking at allowing certain functions to be further delegated – however no specific details were provided. A UMA can further delegate outsource functions to brokers, the main one being policy issuing, but this would need the agreement of the insurer/s concerned as the insurer would still be responsible for ensuring that all the required standards are in place and maintained by that broker. Any fee payable to the broker would be for the UMA's account.

A couple of unrelated questions also came up:

1. Are UMAs to continue to be governed by FAIS? The FSB did confirm that FAIS is to remain as such for now and that they are looking into alternative, more suitable, methods of regulation. What this may be and what time frames are involved was not given. If they don't decide before the second level regulatory exams need to be completed will we see more exemptions for the UMAs?

2. Cell captives and the non-mandated intermediary – what regulation will be seen? The FSB advised that there will be some detail released by the year end that will further indicate where the FSB want to go with regulation in this area.

Whist not specifically addressed at the seminar all Insurers and UMAs need to be identifying all those service providers that the insurers, and therefore the UMA, currently outsource functions that could be done in house by the insurer. Examples of this would include:

- Assessors/Adjusters,
- Compliance,
- Actuarial services,
- IT system providers (insurance processing rather than hardware support),
- Claims recovery agents,
- Surveyors.

All of these need a Directive 159 (Outsourcing) agreement.

We have seen instructions from one insurer that goes on to say car hire companies and panel beaters also need such an agreement but we are not in agreement with this as these are functions an insurer would not typically conduct in-house and thus would fall outside the Directive 159 requirements.

Where a broker has its own outsource agreement and further delegates this functionality they would also need to ensure that these service providers have the required agreement from the insurer, assuming of course that the insurer is happy to allow further delegation of responsibility.

We believe all agreements have to be drawn up in conjunction with the insurer/s concerned so that there is consistency of approach and agreed wording.

The initial assessment of the capability of any entity subject to such an agreement and the on-going monitoring of the performance and standards will be the responsibility of the insurer. As we mentioned earlier we will be offering services that will assist in this area from the New Year.

The UMA and direct business

We have had two cases this month of the FSB raising a concern over the UMA's website that invited the general public to submit details to obtain a quote. The restrictions contained in the binder regulations around a UMA acting as a broker were breaches cited. It is not clear if these issues were raised via a complaint being lodged with the FSB or by a general exercise being undertaken by the FSB. The issues had not been resolved by publication so we are not sure whether the matter will result in any regulatory action being taken once the websites have been corrected – we will keep you posted but in the meantime please ensure that your own website does not have a similar profile.

Poor advertising standards

On a related matter we had another broker client who had released an adverting "flyer" to a client base to which they had just been appointed as the broker advising the clients of the product offering available. The problem was:

- No FSP number of the three FSPs (2 brokers and 1 UMA) mentioned on the flyer
- No mention of the risk carrier.

Not one of the three FSPs involved had referred the advert to their respective Compliance Officers so now each FSP is in a defensive position with the FSB to illustrate that they have corrected the error and hope no regulatory action (i.e. fine) will be imposed. We will keep you posted as to how this one goes.

This one appears to have been a complaint lodged by the outgoing broker. What do they say? Hell hath no fury like a broker scorned!

So the moral of the story is: get our sign off on your adverts BEFORE you release them.

Name approval exercise

The exercise has been started by the FSB to write to all FSPs that they maintain had not had the required approval for the use of terms such as "insurance" in their company name. Whilst they started and some of you have received letters not all letters have been submitted. We have tried to get details of who has had and who not as well as identifying who may have a problem but this is proving difficult so we would ask that if you do receive a letter on this subject that you please send us a copy.

The stance being taken is that if you were to apply and approval would be granted e.g. ABC Insurance Brokers, they are merely stating that a blanket approval has been given as "the description of your business or undertaking" complies with the regulations i.e. your registered business description must clearly state what your company business is.

For those that do not receive this blanket approval an application must be made for such approval. We have challenged this requirement on two cases where prior approval had been given, we are told, in error, on the basis that the cost of a name change is considerable and that to simply expect a company to rebrand when the original approval was an error on the part of the FSB is simply not acceptable. In these two cases the FSPs are UMAs and thus removed from direct contact with the public thus avoiding any potential confusion as to their role in the insurance distribution chain. The results of this approach are awaited.

Funeral operators who need to be FSPs

In what appears to be an attempt to pull in funeral operators to the FAIS fold a 12 month exemption has been granted that allows such operators to continue trading as an FSP provided an application for approval has been submitted to the FSB and that they have started with implementing the required controls needed.

In addition such operators, including those licenced for friendly society benefits, have been given a 5 year exemption from the requirement to hold PI and/or FG covers.

The need for additional (Section 19(3)) audited financial statements: The FSB have

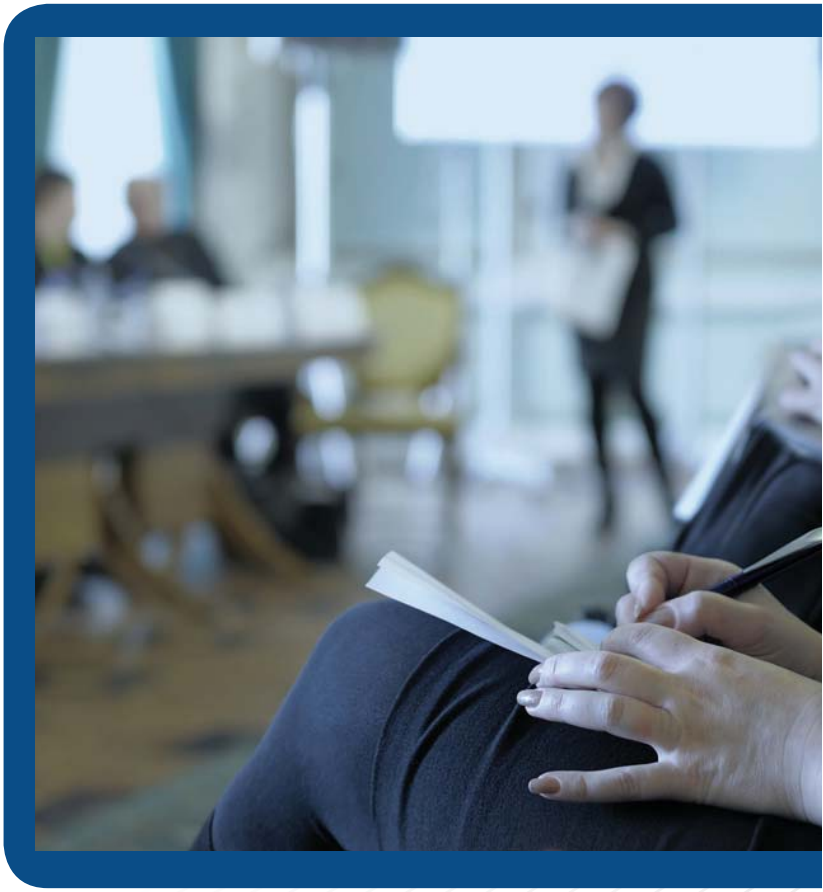
recently been nagging FSPs for the additional audit required for FSPs handling client funds. FSPs that only handle short-term premiums and have an IGF in place do not need a S 19(3). After complaining about this sudden incorrect focus we eventually received the following explanation:

> ***"System developments have been made and we are no longer using the same system as in in previous years. If the FSP's profile reflects a separate bank account, even though they only collect short-term insurance premiums and have an IGF in place, the system will automatically require a section 19(3) report. The FSP will thus have to remove the separate bank account on its profile to ensure that the 19(3) is not requested every year"***

It would have been nice to have been advised of this to avoid the hassles but nevertheless we will now be removing all references to the second account to avoid this problem in the future so you may well receive an acknowledgement of the request once we submit your profile change.

From the FAIS Ombud

Sharemax broker loses court battle with Ombud



Sharemax broker Deeb Risk has failed in his quest to challenge the Fais Ombud in court. Deeb Risk was contesting the Ombud's jurisdiction to rule on advice given whereby Deeb Risk advised several elderly clients to invest in two of Sharemax's most toxic syndications.

When these schemes collapsed, some of Deeb Risk's clients laid complaints against him with the FAIS Ombud. The Ombud rules on financial advice. If she finds that bad advice was given, she has the power to order an adviser to refund a client.

Deeb Risk has been ordered to repay complainants a total amount of R2.2m.

Deeb Risk's application was an attempt to get his client's complaints heard in court. He disputed the Ombud's jurisdiction and suggested that her adjudication methods were unfair and unconstitutional.

Deeb Risk used Section 27(3)c of the FAIS Act and Section 34 of the Constitution to support his case.

Section 27(3)c states:

> ***"The Ombud may on reasonable grounds determine that it is more appropriate that the complaint be dealt with by a court or through any other available dispute resolution process, and decline to entertain the complaint."***

Section 34 of the Constitution states:

> ***"Everyone has the right to have any dispute that can be resolved by the application of law decided in a fair public hearing before a court or, where appropriate, another independent and impartial tribunal or forum."***

It was found that neither of these two sections conferred on Deeb Risk a right for complaints against him to be heard in court. It was also noted that Deeb Risk had failed to make use of his right to appeal before attacking the Ombud's jurisdiction.

For a copy of the full judgement, please contact our offices.

From the FIC

You may have received a mail from the FIC in the last week or so. This mail required all FSPs who completed their FIC registration prior to January 2011 to now verify their information on the system. All the affected FSPs need to log onto the FIC website and verify their information. Failure to do this will result in penalties being occurred. For those of you who incorrectly added our details as the contact person: please note that the correspondence makes no reference to your company so please login and verify that your registration is complete.

From CIPC

CIPC has released Practice Notes pertaining to various topics. Each month, we will discuss a practice note in order to enlighten all those that it applies too.

Practice Note 1 – Postal and Physical Address Requirements

CIPC requires that all postal and physical addresses required by an electonic and manual form be structured in a specific manner in order to allow for better statistical records and data quality.

The following information must be provided to CIPC:

Physical Address:

- Street Number
- Street Name
- Suburb/ Town/ City
- Province
- Street code for your suburb

Postal Address:

- Postal number of description
- Suburb/ Town/ City
- Province
- Postal Code

If the address is outside the Republic, the country description must also be indicated. Any form that does not comply with the above requirements will be rejected by CIPC.

Interesting articles we have read

A job advertisement in one of the popular electronic magazines;

"Have you considered Standard Bank Insurance Brokers for your long-term career advancement? If you have passed your RE exams, are FAIS compliant and have a minimum of five years' commercial experience, we would like to meet you"

If you employ such a person/s we expect to see more approaches like this.

Insurance Gateway September 2012

POPI (and if you know what POPI is you must read) approval could see companies in hot water over ineffective document destruction practices. Read more

FIA launches new initiative to combat fraud. Read more

COVER magazine – August 2012

Santam to start adjusting vehicle values at anniversary date based on the Auto Dealers Guide. Many brokers still do not do this believing that by highlighting to a client that it should be reviewed is sufficient and they are reluctant to make assumptions on aspects such as mileage, condition and extras which affect value. Whilst we appreciate these concerns the alternative is exposing the account to attack by a competitor who will adjust the value and the very likely possibility that the client overpays for a number of years as the value is never adjusted. The previous FAIS Ombud, Mr. Pillai, questioned the practice of insurers increasing values on aspects such as buildings and contents but not on the motor. It will be interesting to see if the Santam approach will change brokers approach or other insurers for that matter.

The same edition of COVER has two related articles on the issue of motor values. One argues for motor insurance premiums not reducing over time based on age and value of the vehicle and one offering a product that does just that – reduces the premium each month based on the declining value of the vehicle.

So who is right?

FA News Magazine – August 2012

An article for all binder holders – especially brokers moving into this space for the first time, by Sandra Sithole of Norton Rose on the importance of ensuring clients receive

communications such as claims repudiations with the laid down time frames allowed.

FA News e-magazine

Replacement product standards in the life sector. Read more.

It is time for brokers to speak with one voice

Read more.

Moonstone Monitor

30th August edition

FAIS Ombud ruling with specific emphasis on commission & fee disclosures on investments. Read more.

3rd click here & 6th September click here: A look at the methodology of awards being made by the FAIS Ombud

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