

## Response to Central Bank Discussion Paper on the Payment of Commission to Intermediaries

### **1. In your view, what aspects of how intermediaries are paid commission work well to deliver responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?**

Firstly the more commissions that are paid over a period of time and not front loaded via “initial commissions” ensure continued engagement of service and support non-selling of products for practices such as “quick sale, quick profit”. These should not be collected via trail commissions (i.e. those added to annual management charges) but renewal commissions which are clearly disclosed to the investor and which appropriately remunerate the intermediary for continued services at a rate commensurate with the service. Fund based trail commission has a much heavier impact on a consumers eventual outcome than high initial commission e.g. trail commission is particularly corrosive for ARFs.

### **2. In your view, what aspects of how intermediaries are paid commission do not succeed in delivering responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products or present particular risks in this regard?**

A trustee, given that (s)he occupies a fiduciary position, is forbidden to make a profit from the position unless explicitly authorised to do so, and should make every effort to avoid conflicts of interest. So, for example, trustees may not buy trust property or utilise information obtained as a trustee to their own financial advantage – the so-called ‘self-dealing rule.’ Intermediaries who are also pensioner trustees or professional trustees through the corporate veil to the same consumer are conflicted and should not be permitted. Intermediaries should only be allowed execute regulated products without also being the trustee. It is suggested it is not fair and appropriate that a pensioner trustee earns a fee for provision of services and then earns a commission as the intermediary on an executed investment.

For the moment, Trustee Annual Reports (TARs) issued for authorised Occupational Pension Schemes (OPSs) should require the principals or Directors of both sides to be disclosed so that the consumer can clearly see the potential conflict. There should also be a Statement on Conflict of Interest and how this is managed by such individuals.

Also, the use of the early encashment system in life and pension bonds seems to give the green light to intermediaries to move funds every five years or so. This needs redress.

# Trustee Decisions

### **3. In your view, are there any changes needed to commission arrangements in Ireland, regulatory or otherwise, to do more to encourage responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?**

Yes, prohibit intermediaries from also being the trustee to Executive Pension Plans (EPPs), Small Self-Administered Pension schemes and any type of OPSs. Examples of the conflict of interest can be clearly demonstrated by considering those companies who offer consultancy sales and administration services of such products.

Prohibit or significantly limit the payment of fresh initial commission on pension transfers; also the potential banning of the use of early encashment charge structures when used to facilitate allocation greater than 100%. In reality, the early encashment system is a form of the old discredited 'initial unit' system used in the past.

Also disclosure of commissions on policies issued to trustees of OPSs which is not required by the current Life Disclosure regulations needs redress.

It is suggested better disclosure of the impact of commissions through disclosure of Reduction In Yield (RIY) at all durations and not just at maturity, as currently used would be helpful.

### **4. Are there other features or types of commission arrangements that the Central Bank should take into account in considering this topic?**

Yes, for Delegated Consulting models, the delegated consultant will appoint and negotiate fees with the sub-managers. This can give rise to a conflict of interest as they are the consultant and the asset manager. It is not clear on these offerings whether there are any side agreements which in effect facilitate a rebate of fees to the delegated consultant (e.g. called "marketing and administration support" fees). In effect, these are non-transparent and unknown to the consumer.

In addition, it is not clear whether the promotion of delegated services are supported by internal financial incentives to staff which raises the question of whether the ultimate offering to Trustees/Members of OPSs is in their best interest or in the interest of the firm promoting the delegated solution.

### **5. Are there practices or features of commission arrangements in other jurisdictions to which you think the Central Bank should have regard to?**

In the UK, there is a question as to how successful RDR has been but it has highlighted one feature – there is a cohort of consumers who are willing to pay a fee plus VAT for a service which is related to the professional service and execution of a product versus being remunerated via a commission which is related to the size of the investment. That said, it is suggested that this percentage is the minority in Ireland but it raises the question if there should be a cap on how much commission one can earn. For example, a 3% commission on a

[www.trusteedecisions.com](http://www.trusteedecisions.com)

# Trustee Decisions

€1m Approved Retirement Fund (ARF) would appear to be immoral and unrelated to the level of work required to advise a client who on a fee basis might pay up to €5,000 plus VAT? A reference to the Pensions Council work on this is a good reference point to this.<sup>1</sup> To be clear there is no suggestion that an intermediary should not be remunerated appropriately for their services, however, a question must be asked if the amount is reasonable and if it is made fully transparent to the consumer. Again it is believed that despite regulations for material disclosures, many consumers do not understand jargon terms like allocation rates, bid/offer spreads, annual management charges, trail commissions etc.,

It is suggested the outright banning of commissions will lead, as in the UK, to an advice gap where independent advisers will stop dealing with low to middle earners and concentrate on high earners.

## **6. Are there any changes to these practices which you consider necessary or appropriate to better promote responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?**

Yes, trail commissions should be prohibited – it is suggested these were created by product providers in finding another way to remunerate and incentivise intermediaries. Fund based trail commission has a much heavier impact on consumer monies than high initial commission e.g. trail commission is particularly corrosive for ARFs<sup>1</sup>. The fund manager justifies their management charge as they are managing the assets, however, there is no obvious logic or rationale to adding a “trail” commission for the intermediary.

## **7. Are there features of the current consumer protection framework that you would highlight as strengths in the context of commissions specifically?**

Annual Management Charges (AMCs) and Total Expense Ratios (TERs) are useful but it is suggested that the requirement to quote the Ongoing Charges Figure (OCF) may be a better disclosure method as this all charges (e.g. includes performance fees and one-off charges) which may otherwise be lost on consumers. Whilst suggesting this, there would be a requirement to provide an understandable definition for consumers which helps inform them and empower them to make an informed decision.

## **8. Are there weaknesses or gaps in the current consumer protection framework in the context of commissions specifically?**

Overall, it is suggested that despite best efforts, many individuals suffer from inertia when choosing to take advice and invest in products. Whilst the Central Bank can do little about individual behaviour, certain prohibitions would be useful like banning trail commissions.

In addition, it is suggested that members of group employer OPSs should be required by law to sign a declaration to say that they have received independent advice BEFORE signing a proposal form. This in turn should have to be acknowledged in writing by the trustee to the OPS from which the member is transferring out of or drawing down a pension or ARF.

---

<sup>1</sup> <http://www.pensionscouncil.ie/en/Reports/>

# Trustee Decisions

**9. Do you have any other observations on the current domestic framework as it relates to the practice of paying commissions in Ireland?**

Yes, any commissions which have been paid to intermediaries should be easily available upon presentation of a Letter of Authority from the insurance company and/or product provider. At present, a newly appointed intermediary is unable to get this information in full from a life assurance company and this thwarts efforts to reveal actual factual information for consumers. It should not be a requirement for individuals to engage professional advisors or legal professionals and at their expense to get this information. In effect, this practice injures trust and promotes non-transparency.

There should be a real effort to standardise the tax and regulatory structures around pensions. It is unnecessarily complicated which leads to additional costs to individuals and works against trust and transparency.

**10. Do you have any general views on the potential benefits to consumers of properly designed commission structures outlined in this section?**

It is agreed that clawback arrangements, cooling off periods and loyalty bonuses support qualitative engagement by the intermediary and sales that remain in place.

Whilst material disclosures on individual products are clearly set out by the Central Bank's regulatory requirements, it is suggested that these could be replicated to members of OPSs in the interest of providing a 'level playing pitch' for consumers. It is suggested that not all members of OPSs who are members of group insured schemes are aware of the allocation rate or bid/offer spread which impact their pension investments. The same may be true of Additional Voluntary Contributions (AVCs).

Individuals who avail of personal pensions (RACs or PRSAs), Permanent Health Insurance (PHI), EPPs, Business Protection or any life assurance product or stockbroker product should be provided with a formal Letter of Engagement and Terms of Business. These should clearly set out the scope of services and fee arrangements applicable to the product.

**11. Are you aware of any additional potential benefits to consumers? If so, please describe them.**

It is suggested that the above recommendations support clear terms of reference, how business is written and on what terms. This can only support certainty of cost of services, consumer confidence and promote trust between the intermediary and the consumer.

**12. Have you observed any of these potential benefits? If so, please provide examples and describe the kind of benefit that has accrued.**

Yes, through operating our business we have developed a loyal client base that pay fees year on year which has become an endorsement of trust and service that has mutually benefited both parties.

# Trustee Decisions

**13. Would you weight any of these potential benefits over others as requiring special consideration or attention, and if so why?**

No comment to this question.

**14. Do you have any suggestions as to how the current regulatory framework could be improved or changed so as to enhance the potential benefits to consumers that arise from the payment of commissions to intermediaries so as to better promote responsible business conduct, fair treatment of consumers and avoidance of conflicts of interest when consumers are sold financial products?**

While writer understands that the Central Banks Consumer Protection Code (CPC) requires Letters of Engagement, Terms of Business and Declarations of Independent Advice to be provided by intermediaries, we have evidence where this is not the case. Therefore, it is suggested the Central Bank should ask for sample copies from all intermediaries.

Public confidence and trust has been injured by the actions of a few in the financial services industry e.g. Custom House Capital<sup>2</sup>, Source<sup>3</sup>.

It is suggested that the many professional intermediaries who are operating in the industry which are regulated by the Central Bank and the Pensions Authority could be supported by the Central Bank introducing a Trust Mark or Quality Mark which is only attained by satisfying an independently qualified monitor who reports to the Central Bank that this is the case. This would encourage intermediaries to not just satisfy compliant standards (which are a testament in themselves) but would work to promote excelling these standards and operating to a higher standard of corporate and consumer governance.

Apart from the above, it would be useful for the Central Bank to enhance its engagement with consumer focus groups to elicit actual consumer experiences and take feedback and improve consumer understanding and decision making process.

**15. Do you have any general views on the potential risks to consumers of commission structures outlined in this section?**

From time to time, life assurance companies run “campaigns” which offer enhanced commission. This practice, plus “over-ride” commission which is paid to intermediaries for achieving pre-agreed sales volumes conflict intermediaries from advising a consumer in their best interests. Accordingly, such practices should be prohibited.

---

<sup>2</sup> <https://www.centralbank.ie/press-area/press-releases/Pages/UpdateonCustomHouseCapital.aspx>

<sup>3</sup>

[http://www.pensionsauthority.ie/en/News\\_Press/News\\_Press\\_Archive/The\\_High\\_Court\\_directs\\_the\\_removal\\_of\\_Source\\_Pensions\\_Administration\\_and\\_Trustee\\_Company\\_Limited\\_as\\_trustee.html](http://www.pensionsauthority.ie/en/News_Press/News_Press_Archive/The_High_Court_directs_the_removal_of_Source_Pensions_Administration_and_Trustee_Company_Limited_as_trustee.html)

# Trustee Decisions

**16. Do you consider the potential risks to be accurately described? If not, please explain why & 17. Are you aware of any additional potential risks to consumers? If so, please describe them.**

Whilst the potential risks in general may exist, there is a concern that over-selling is perhaps the biggest issue e.g. take a consumer who invests in a Personal Retirement Bond (PRB) and then subsequently invests in an Approved Retirement Fund (ARF) - where commission is taken, there can be a double payment on the monies invested and there could also be a potential penalty to the consumer if the monies are moved between both products within a certain period of time e.g. 3 to 5 years (depending on the commission structure in place)

Whilst certain developments are made with the best of intentions following representation by consumers and industry e.g. the June 2016 Announcement by the Minister for Finance allowing Defined Benefit Buy Out Bond proceeds to be drawn down as ARFs, it is suggested there is a possibility of a small number of intermediaries who may use this as an opportunity to avail of this on a commercial basis as ARFs potentially provide a higher level of commission compared to an annuity purchase (Compulsory Purchase Annuity, CPA). Currently, there is no process in place to monitor or control this potential practice so the consumer will remain unaware.

**18. Have you observed any of these potential risks at play? If so, please provide examples and describe the impact of the risk?**

In the UK there has been a *scorpion campaign* to warn of the danger of pension scams.<sup>4</sup> We should learn from this experience and perhaps adopt a joint regulatory initiative between the Central Bank and the Pensions Authority to highlight the issue.

In addition, there are certain international pension transfer consultants operating in Ireland who promote transferring pension funds overseas which has caused the Pensions Authority to issue a Note on pension transfers outside the State<sup>5</sup>. This is a hugely complex area and not without risks and one wonders if such products are in the best interest of pension investors and consumers.

**19. Would you weight any of these potential risks over others as requiring special consideration or attention, and if so why?**

No comment to this question

---

<sup>4</sup> <http://www.thepensionsregulator.gov.uk/press/pn16-15.aspx> & <http://www.thepensionsregulator.gov.uk/pension-scams> & <https://www.ft.com/content/dccf8404-f421-11e5-96db-fc683b5e52db>

<sup>5</sup>

[http://www.pensionsauthority.ie/en/search/?cof=FORID%3A11&cx=015257361179021475946%3Awyxnxhnn\\_sq&ie=UTF-8&q=note+on+transfers+outside+the+state&sa.x=0&sa.y=0&sa=Search](http://www.pensionsauthority.ie/en/search/?cof=FORID%3A11&cx=015257361179021475946%3Awyxnxhnn_sq&ie=UTF-8&q=note+on+transfers+outside+the+state&sa.x=0&sa.y=0&sa=Search)

# Trustee Decisions

**20. Do you have any suggestions as to how the current regulatory framework could be improved or changed so as to better manage the potential risks to consumers that arise from the payment of commissions to intermediaries?**

While it is assumed that there is a Memorandum of Understanding between the Central Bank and the Pensions Authority, it is suggested that more information be shared between both entities thereby supporting a unified engagement to support cross sharing of information and consumer confidence and to show to the regulated community that there is joined up regulation in this area.

# Trustee Decisions

## **James Kavanagh B.A.(Econ), QFA, CDipPens, FIIPM, QPT(IIPM) and AffSAI**

James Kavanagh is Managing Director of Trustee Decisions Limited, a professional trustee company (TCSP) and a Director of Ailesbury Capital Limited which is regulated by the Central Bank of Ireland<sup>6</sup>.

James started his career, in 1989, working in what is now AON Hewitt. In 1999 James joined the pensions consulting division of Ernst & Young. James then moved to what is now Willis Towers Watson as a Senior Consultant when the Ernst & Young pension consulting division was sold in 2006.

James was appointed to the Office of Peace Commissioner by Alan Shatter, Minister for Justice in September, 2013.

James is Chairman of the Corporate Governance Association of Ireland (CGAI) and a member of the European Corporate Governance Institute (ECGI), the International Corporate Governance Network (ICGN), as well as having membership in the Centre for Economic Policy Research (CEPR), the Association of Pension Lawyers in Ireland (APLI), the Institute of Directors (IOD), the Institute of International and European Affairs (IIEA) and the Defined Contribution Institutional Investment Association (DCIIA).

James is a regular columnist and contributor to the media (e.g. Irish Times and Sunday Business Post).

James is a former Director, Council member and Chair of the DC Committee of the Irish Association of Pension Funds (IAPF). James is also a former Chairman, Director and Council Member of the Retirement Planning Council of Ireland (RPC).

James is currently a Doctoral Candidate at UCD (Doctor of Governance).

---

<sup>6</sup> <http://trusteedecisions.com/>