

## CIRCULAR

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To:	UTMC, IUTA, CUTA, PRS PROVIDER, IPRA AND CPRA (collectively known as "Distributors")		
Attn:	Authorised Representative / Chief Executive Officer		

### Sharing of The Federation of Investment Managers Malaysia's (FIMM) Supervisory Observations

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Reference is made to FIMM's *Industry Briefing – Sharing of Supervisory Findings* event held on 7 August 2019, where we shared our supervisory observations obtained from the following sources - *Mystery Shopping (MS) exercise conducted in 2018, submissions filed and complaints received*.

As part of our approach in creating awareness and educating the industry on FIMM's regulations, the purpose of this *Dear CEO letter* is to reiterate those supervisory observations. While some of the observations may not have originated from your organisation, we advise you to consider our findings and assess whether there is a need to review your organisation's existing compliance and supervisory frameworks to ensure they are aligned with the prescribed regulations by FIMM and related regulations issued by the Securities Commission Malaysia (SC).

#### 1. Mystery Shopping (MS)

In 2018, FIMM carried out an MS exercise on 341 branches, premises and booths set up by various Distributors to identify the sales practices adopted by their respective Consultants. The following are FIMM's observations based on the visits:

##### a. FIMM's Authorisation Card

86% of Consultants did not produce or display FIMM's authorisation card, when identifying themselves as a person registered to market and distribute Unit Trust and Private Retirement Schemes (collectively known as "Schemes") to potential investors. While subsequent checks revealed that these Consultants are registered with FIMM, the risk of

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a non-registered person conducting the act of marketing or distributing the Schemes remains a concern.

Hence, it is important for Consultants to display their authorisation card, as prescribed under *clause 3.1.8 of FIMM's Code of Ethics and Rules of Professional Conduct (Unit Trust Funds)* (Code of Ethics) to distinguish their status as a Registered Person.

**b. Disclosure to Investors**

98% of the Consultants did not provide a complete set of disclosure documents i.e. Prospectus and Product Highlights Sheet (PHS) to potential investors. Instead, Fund Fact Sheets were produced to explain the features of a recommended Scheme.

Prospectus and PHS are required to be produced as prescribed under the *Guidelines on Sales Practices of Unlisted Capital Market Products* (SPG) issued by the SC. Failure to do so is a contravention of the said Guidelines.

**c. Know-Your-Client (KYC) / Suitability Assessment Practices**

Approximately 30% of the Consultants assessed, failed to seek investors' key profile information, such as age, annual income and number of dependents as part of the KYC process. Additionally, these Consultants did not assess the investors' risk profile and investment knowledge.

Moreover, 72% did not conduct Suitability Assessment as they assumed that the investors had low or moderate risk profiles. For related details kindly refer to sub-paragraph d(ii).

It is critical for Consultants to obtain the necessary KYC information to enable them to recommend the appropriate Schemes, in line with investors' objective(s) and risk appetite.

In the event where investors do not follow the Consultants' recommendations, it should be properly documented to avoid future dispute(s).

#### **d. Appropriateness of Product Recommendation**

Shortcomings relating to product recommendations observed during the MS exercise include:

##### **i. Consultant's understanding on nature and characteristics of the Schemes**

20% of the Consultants were unable to explain the general characteristics of the Schemes, i.e. investment objective, strategy, risk, fees and charges. Such lack of understanding on the Schemes' features and terms has resulted in them recommending wholesale funds to non-sophisticated investors (more details in subparagraph (ii)).

Additionally, 94% did not explain the availability of 'Cooling-off period' (where applicable) to first-time investors.

##### **ii. Suitability of the recommended Schemes**

While 28% of the Consultants conducted Suitability Assessment on the investors, 3% did not recommend the relevant Schemes based on the outcome of the assessment. This resulted in Consultants recommending wholesale funds without ascertaining the investors' eligibility as well as requesting for evidence to substantiate that they were indeed 'high net-worth' individuals.

Consultants play a critical role in enhancing investors' financial. Hence, it is incumbent for Distributors to promote and embed a culture of responsible selling so as to provide an environment that protects the interests of the investing public.

We have reached out to the affected Distributors to alert them on the non-compliances for remedial purposes. We strongly recommend a review of distribution arrangements to ensure that your existing controls are adequate in addressing the abovementioned observations as well as other regulatory requirements in marketing and distributing the Schemes.

## **2. Complaints Lodged Directly With FIMM**

Based on the last three (3) years' (2016-2018) complaints lodged directly with FIMM, two-thirds relate to the following misconducts by Consultants:

- a. Unauthorised/ misappropriation of money;
- b. Falsification of investment statements/ forging of investor's signature;
- c. Acceptance of cash/ crediting proceeds into own personal accounts;
- d. Pre-sign/ pre-thumb print on forms; and
- e. Representing more than one (1) principal.

We also noted that there is an emerging trend where Consultants would get potential recruits to market the Schemes prior to being registered with FIMM, under the pretext of training. There were also proxy arrangements which allowed the Consultants to earn a 'referral fee' for recommending investors to other Consultants who are registered with a different principal.

Distributors need to send a strong message to the Consultants that such practices are not allowed and can be subjected to disciplinary actions. These practices are not aligned with the requirements stated under *clause 3.3.1 of FIMM's Code of Ethics*.

## **3. Improvements Needed in Submissions to FIMM**

FIMM has identified the following issues related to submissions received from Members and Distributors:

### **a. Incompleteness of registration submission**

Examples of material issues identified are as follows:

- i. Candidate did not sign the Application Form;
- ii. Candidate's signature differs from the Statutory Declaration;
- iii. Validity of the Statutory Declaration is questionable as the date is not stated or incorrect sign-off date on the Application Form;
- iv. Inaccuracy of data arising from information not fully completed or wrong input/ spelling error on the Consultant's personal information in Application form/ Statutory Declaration;

- v. Amendment(s) in Statutory Declaration not countersigned by the Commissioner for Oaths;
- vi. Not meeting 'fit and proper' criteria, i.e. the candidate did not have the pre-requisite academic qualification;
- vii. Academic transcript was submitted instead of academic certificate;
- viii. Quality of photograph did not meet the prescribed standard, i.e. image is unclear or in the wrong format, i.e. ".pdf" instead of ".jpeg" or ".png" format; and
- ix. Delay in submission of Registration documents, i.e. documents were submitted after the examination registration closing date.

Moving forward, any submission with material issues will be returned or rejected with no fee refund, in accordance with *rules 3.1.7 and 3.1.9(a) of FIMM's Consolidated Rules (FCR)*.

**b. Accuracy of system tagging for terminated/ resigned Consultants**

From the disciplinary proceedings conducted and actions taken by FIMM, we have identified Consultants with recurring misconduct after being registered with a new Distributor.

One of the main contributory factors for such non-detection is the inaccurate designation of the reason for termination of Consultants in the Registration system by the previous Distributor. Consequently, such Consultants remain active and continue with their misconduct(s) under a different Distributor. Hence, it is essential for all Distributors to ensure that proper tagging for terminated/ resigned Consultants is done in the Registration system.

**4. Data Integrity**

As part of our systems enhancement review, we identified common usage of invalid emails, i.e. [dummy@dummy.com](mailto:dummy@dummy.com), [123@gmail.com](mailto:123@gmail.com) or [123@hotmail.com](mailto:123@hotmail.com) registered in our Registration system. Such data quality and integrity issues can undermine Distributors' ability to monitor, record or disseminate key information that is needed to effectively manage your risk and business activities.

While we are already looking at qualitative controls in filling up our forms, we strongly feel that it is equally important for Members and Distributors to carry out a review of its Consultants' records to ensure that it contains valid and updated information, which is consequently recorded into FIMM's Registration system. Particular attention should be made to ascertain that the information on Consultants with dual registration, i.e. as Unit Trust Scheme (UTS) Consultant and Private Retirement Scheme (PRS) Consultant are consistent in both I3 and PRS Registration systems.

#### **5. Timeliness of Submission**

FIMM observed that there were instances of delay by Members/ Distributors in providing the following submissions in 2018:

- a. Notification on funds lodgement was not submitted at least one (1) business day before the Scheme is marketed and distributed, as prescribed under *rule 3.4.4 of FCR*;
- b. The submission of Assets under Management/ Gross Sales of Schemes was not submitted by 10 January, as prescribed under *rule 3.4.7 of FCR*; and
- c. The Annual Compliance Review was not submitted within the specified timeline of 31 January 2019 (issued under a circular), as prescribed under *rule 3.4.6(e) of FCR*.

All Members/ Distributors are reminded to adhere to the various timelines stipulated under the FCR accordingly. Failure to do so is a non-compliance to the FCR, and FIMM, in accordance with *rule 2.1.3* may take any action it deems fit, against such non-compliance.

#### **6. Issues Identified in the Annual Compliance Review (ACR)**

The yearly ACR submission to FIMM is based on Members and Distributors' self-assessment and declaration on the state of compliance to the applicable rules and guidelines. It is paramount for corrective actions to be taken expeditiously on any gaps reported in the ACR since these may result in non-compliance to the rules and guidelines, which will subject Members and Distributors to regulatory actions.

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### **Next Step**

This *Dear CEO* letter is part of FIMM's industry education initiative based on observations made from our supervisory and disciplinary work. It is with the intention to develop the industry and strengthen investor protection. Hence, it is essential for all Members and Distributors to assess the observations highlighted and take remedial actions (where applicable) for any identified shortcomings. As part of good governance, we recommend that all gaps identified be reported to your Board of Directors or relevant Committee(s).

While FIMM continues to step up its supervisory efforts, Members and Distributors should consider carrying out independent assessments on Consultants' sales practices to ascertain the state of compliance and service level (e.g. investor call-back verifications, survey on investors' experience, mystery shopping).

Let's continue to collaborate in building a stronger sales culture that will strengthen trust and credibility, as well as working towards maintaining the good reputation of the Unit Trust and Private Retirement Schemes industries.

Thank you.

Yours Sincerely,

**FEDERATION OF INVESTMENT MANAGERS MALAYSIA**



**KALEON LEONG**

Chief Executive Officer