30 April 2014

Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600

Email: economics.sen@aph.gov.au

Dear Senator Bushby

Inquiry into the provisions of the Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014

CPA Australia and the Institute of Chartered Accountants Australia ('the Institute') welcome the opportunity to provide comments to the Senate Economics Legislation Committee inquiry into the Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014.

We support the Government's statement in its announcement in December last year that the changes are aimed at ensuring the integrity of the financial advice framework is maintained whilst delivering a system that offers affordable and accessible financial advice to the Australian community.

However, the ongoing public debate over these proposed reforms is already having an adverse impact, with the wider community seeing an industry debating fundamental issues around remuneration, transparency and engagement.

Further, the Future of Financial Advice (FoFA) reforms, passed by Parliament in 2012, are the most significant reforms to the financial services industry in over ten years.

The underling objectives of these reforms are to improve the trust and confidence of Australian retail investors in the financial services sector and improve access to advice. These are critical goals given the high profile cases of poor advice, the fact that only one in five consumers currently seek advice, Australia is faced with an ageing population and a growing retirement affordability challenge. Ensuring the provision of quality advice for Australians must be an important part of planning for the future.

The passage of the FoFA reforms was the result of extensive, wide spread consultation over many years. Its introduction marked a milestone opportunity for the sector to take a greater responsibility and refocus its efforts on providing and promoting quality financial advice in the best interests of the client, free from conflict and in a transparent manner.

We acknowledge and support the Government's commitment to reduce regulatory burden and compliance costs on business. However, it is essential that a balance is struck between further reform and acting in the best interests of consumers.

It is with these goals in mind that we must focus on not just the immediate cost of implementation, but the longer term benefits the FoFA reforms can deliver for both consumers and the industry.

The industry must strengthen its relationship with consumers and this requires trust, transparency and engagement in a simple manner than provides certainty to the consumer. We strongly believe that measures such as opt-in, fee disclosure statements and the banning of conflicted remuneration are all important elements in developing greater trust and confidence in the financial services industry.

In addition to benefitting new clients, these mechanisms will provide an opportunity for those financial advisers who do not already regularly engage with their clients to better engage and demonstrate the real value of their advice. It will also protect clients who have become disengaged over time as well as clients who are not yet fully engaged in the client/ financial adviser relationship from paying ongoing fees where they receive little or no service.

CPA Australia and the Institute believe that if the industry can begin to effectively communicate the benefits and value of seeking financial advice, the wider community will begin to understand the value of financial advice and to seek it out in order to guide better informed financial decisions.

If you have any questions regarding this submission, please do not hesitate to contact Keddie Waller (CPA Australia) at keddie.waller@cpaaustralia.com.au or Hugh Elvy (the Institute) at hugh.elvy@charteredaccountants.com.au.

Yours sincerely

Alex Malley
Chief Executive
CPA Australia

Lee White
CEO
Institute of Chartered Accountants Australia

About the signatories

CPA Australia and the Institute represent over 200,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally. Specifically members of the accounting profession are increasingly becoming involved more widely in financial services related advisory and service roles.

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'Best interests' obligations

CPA Australia and the Institute believe that the majority of financial planners provide quality financial advice that is in the best interests of the client. However, the introduction of the statutory 'best interests' obligation has embedded this obligation in the financial advice framework.

It ensures providers of financial advice make certain the interests of their clients remain paramount, above and beyond those of the adviser, licensee and any relevant associates.

We believe the existing general obligation of s961B(1) to act in the best interests of the client when providing advice in combination with the steps a provider can undertake to satisfy this duty in s961B(2), achieves an appropriate balance between a principles based approach and providing regulatory certainty. Importantly, noting that the steps in s961B(2) are not the only way a provider can meet their obligation to act in the best interests of their client.

However, we acknowledge that there has been some concern that the current requirements in s961B(2) may prohibit the provision of scaled advice.

Enabling the provision of scaled advice is important, as a client may only require, or importantly be able to afford, advice on limited or a single issue. This is supported by ASIC Report 224 *Access to financial advice in Australia*[1] which found that many Australians want piece-by-piece simple advice rather than holistic advice.

The rationale to repeal s961B(2)(a), which specifically includes 'by the client through instructions', is to facilitate an adviser to scale the advice they will provide to a limited or single issue. However, what is relevant to the advice being provided will be determined by the nature of advice, which should not be either intentionally or unintentionally limited by legislation. Further, given the existing obligation to identify the client's relevant circumstances, we do not believe the proposed amendment changes the enquiries an adviser would be required to make to discharge their duty.

There has also been some concern that the 'catch-all' provision, being s961B(2)(g), and s961E create a level of uncertainty given the open-ended nature of the obligation.

While we believe that these existing provisions are appropriate, their removal should address any concerns the industry has highlighted. Further, an adviser would still be required to show they have complied with the remaining six steps in s961B(2). This includes identifying the subject matter of the advice being sought by the client (explicitly or implicitly) and the client's relevant circumstances which would reasonably be considered as relevant to this advice.

Going forward this should still ensure an appropriate balance of a principles based approach that an adviser must act in the best interests of their client to positively encourage behavioural change while also facilitating the provision of scaled advice where appropriate.

[1] ASIC *Report 224 Access to financial advice in Australia*, December 2010 p.5

Ongoing fee arrangements

CPA Australia and the Institute continue to support the mandatory two year opt-in process as an important pillar of the FoFA reforms.

The opt-in requirements will assist clients who are actively involved in planning their financial future to assess whether the services they are receiving reflect value for money before they decide to renew an ongoing fee arrangement. In addition, it will encourage clients who are not actively engaged to become involved with their finances and their adviser, an important outcome given the low levels of financial literacy. It is also an opportunity for those financial advisers who do not regularly engage with their clients and seek their ongoing consent to charge advice fees to now demonstrate the real value of their advice.

Importantly, transparency and integrity are essential elements in a trusted relationship between a financial planner and a client. Implementing these mandatory ongoing disclosure requirements will ensure that these principles are upheld in all client engagements.

If the industry can begin to effectively communicate the benefit and value of seeking financial advice, the wider community will begin to understand these benefits and this may encourage more people to actively seek advice. This active engagement by clients will be a key element in improving trust and confidence in the industry.

Further, we believed the protection mechanism provided by 'opt-in' should have been afforded to both existing and new clients. However, the compromise of requiring the provision of an annual fee disclosure statement to all clients will assist in ensuring existing clients have the opportunity to make an informed decision whether they are receiving value for the ongoing fees they are being charged.

While we understand that implementing new regulatory requirements comes at a cost, we also acknowledge that a balance must be struck between amending existing obligations and ensuring new rules and regulations are in the consumer's best interests and deliver positive outcomes. Further, the continual changes (and debate) to the current regulatory requirements are already adversely impacting consumer confidence and trust in the financial services sector.

With the best interests duty, the opt-in provisions form an important element of the FoFA reforms and will promote trust, transparency and confidence. This will in turn deliver long term benefits to the industry and may encourage more people to confidently seek financial advice.

It is for these reasons that we do not support the proposed amendments to s960, 962F(1)-(3) or the proposal to repeal s962K-962N.

CPA Australia and the Institute also support the provision of fee disclosure statements to all clients. There have been statements that consumers currently receive a range of disclosure documents outlining the various fees a consumer may pay. However it is generally recognised that the current disclosure obligations are at times complicated for consumers to clearly understand. (This again should be considered in light of the low levels of financial literacy in Australia). Therefore there would be significant value in a single simple fee disclosure statement.

We believe this mandatory disclosure obligation will ensure the principles of transparency and integrity are upheld in all client engagements, which will have positive outcomes for not only clients but the wider industry.

It will also ensure a minimum level of engagement and communication between a financial adviser and a client, while acting as an important consumer protection mechanism for clients who are in an ongoing fee arrangement that is not subject to the mandatory biennial renewal.

We understand that these obligations come at a cost and that this is a consideration in a commercial environment. However, we believe that the immediate benefits of engagement and transparency and the longer term benefits of building trust and confidence if these measures are retained must not be underestimated.

Further, consideration must also be given to the potential impact on consumer perception and trust in the financial services industry if these measures, which were implemented to enhance retail investor protection, are now removed.

Recommendations:

The current statutory requirement for a financial adviser (fee recipient) to provide a client a renewal notice at least every two years is an important pillar of the FoFA reforms and as such must be retained.

Annual fee disclosure statements for all clients engaged in an ongoing fee arrangement must be retained. They are an important tool which will improve transparency and engagement between adviser and client, with longer term benefits in building trust and confidence in the financial services industry.

Conflicted remuneration and other banned remuneration

CPA Australia and Institute are of the view that all commissions have the potential for real and perceived conflicts of interest and should therefore be removed. Remuneration models based on a commission structure do not align with the services generally provided by a professional.

We believe the current ban on conflicted remuneration has been integral for the industry to move forward and minimise or remove conflicts of interest from the provision of advice.

Further, when combined with the best interests duty, we believe it creates the foundation for rebuilding confidence and trust, which are both necessary to encourage consumers to actively seek financial advice.

Proposals to loosen this ban and permit commissions on general advice not only undermines the principles of the FoFA reforms, they return to encouraging a sales culture in the industry rather than focusing on provision of quality personal advice. The industry is endeavouring to move away from a sales and product culture to focus on the provision and benefits of quality financial advice. Therefore it is imperative that conflicted remuneration structures, especially those usually aligned with sales, are removed.

The Draft Explanatory Memorandum to the Bill states that the objective of this measure is to properly target the advice that has the greatest ability to influence a retail client's financial decisions and to ensure that parties not directly involved in providing advice are not unintentionally captured.

Only one in five consumers currently seek personal advice from a licensed financial adviser. However, we know that one of the major influences on advice is marketing information[2].

Arguably this creates a greater risk, as a consumer may receive general advice about investing in a complex product from an adviser, who is remunerated via the sale of the product, yet does not have to take into consideration any of the client's relevant circumstances as they are only providing general advice.

Despite the fact that general advice does not take into consideration a client's circumstances, the intention remains to influence the sale of a product otherwise there would be little value in remunerating general advice via a conflicted remuneration model.

We do not believe this is in the public interest.

Further, we are concerned returning to a conflicted remuneration model for general advice may adversely impact the community's perception of the broader financial services industry including those licensed advisers who provide personal advice. Given the very public debate over these reforms, and the number of consumer advocates engaged, this is a very real concern.

Finally, as previously stated, low levels of financial literacy in Australia must be considered, as this factor substantially increases the risk that consumers may not be able to appropriately differentiate between general and personal advice. Placing this onus on the consumer adds further complexity and uncertainty on those consumers who choose to seek advice.

Recommendation:

The proposed changes in section 963A not be progressed as they undermine the principles of the FoFA reforms and do not promote the broader public interest policy.

Currently, commissions are permitted on execution only services, provided financial product advice in relation to the product, or products of that class, has not been given to the person as a retail client by the licensee or representative in the 12 months immediately before the benefit is given.

The proposal to remove this link, creates the potential for practices to establish general advice models that may lead to the provision of execution only services. Further, there would be no obligation for the adviser to disclose to the client the commission they will receive, except in the product disclosure statement.

We do not believe creating an environment where this type of model is permissible is in the public interest or in the interests of the broader financial services industry. We believe this model places the consumer at risk, especially given concerns around financial literacy and the increasing complexity of financial products.

In the interests of consumer protection, we do not support the proposed amendments to s963B(1)(c) and consequently the proposed implementation of s963B(3) and (4) in the draft legislation.

[2] ASIC *Report 384 Regulating complex products*, January 2014 p.32

Recommendation:

Section 963B(1)(c) be retained and the proposed amendments to subsections 963B(3) and (4) not implemented. This is to ensure that execution only services can only be provided where the client has not received advice, be it general or personal, in the preceding 12 months about that financial product, or products of that class.

We also believe inconsistencies in how commissions received on insurance for life risk products within superannuation adds unnecessary complexity and may encourage the retention of conflicted remuneration models and this should be considered.

CPA Australia and the Institute are however supportive of the amendments to the education and training requirements. Education and training relevant to the operation of a financial services business, which includes the provision of financial product advice, are valuable skills that should be encouraged for the benefit of the industry.