FINANCIAL PLANNING
ASSOCIATION of AUSTRALIA

26 October 2018

Re. Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry – Interim Report

Dear Commissioner,

We welcome the opportunity to make written submissions in response to the Interim Report, of the Royal Commission. We have responded to questions raised in the Interim Report that are of particular relevance to financial planning and we have focussed on questions about the need for regulatory reform.

If you have any queries or comments, please do not hesitate to contact me at dante.degori@fpa.com.au or on 02 9220 4500.

Yours sincerely

Dante De Gori CFP®
Chief Executive Officer
Financial Planning Association of Australia[1]

[1] The Financial Planning Association (FPA) has more than 14,000 members and affiliates of whom 11,000 are practising financial planners and 5,720 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
- In 2009 we announced a remuneration policy banning commissions and conflicted remuneration on investments and superannuation for our members – years ahead of FOFA.
- We have an independent conduct review panel, Chaired by Graham McDonald, dealing with investigations and complaints against our members for breaches of our professional rules.
- The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices. This is being exported to 26 member countries and the more than 175,570 CFP practitioners that make up the FPSB globally.
- We have built a curriculum with 18 Australian Universities for degrees in financial planning. Since 1st July 2013 all new members of the FPA have been required to hold, or be working towards, as a minimum, an approved undergraduate degree.
- CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional bodies, eg CPA Australia.
- We are recognised as a professional body by the Tax Practitioners Board.

WRITTEN SUBMISSIONS OF THE FINANCIAL PLANNING ASSOCIATION OF AUSTRALIA TO THE ROYAL COMMISSION INTO MISCONDUCT IN THE BANKING, SUPERANNUATION AND INSURANCE INDUSTRY

INTERIM REPORT RESPONSE

This submission is made by the Financial Planning Association of Australia ('the FPA') and addresses questions posed in the Interim Report.

This submission is based on the following understanding of what financial advice is and why it is fundamentally important to consumers and the national economy.

What is financial advice?

Financial advice is about helping people set goals and devise a plan to prepare them for the future, manage their financial affairs, protection against risks and give them confidence about their financial security.

Financial advisers work with clients to identify and consider:

1. Each client's circumstances including their needs, goals and priorities.
2. The values, attitudes, expectations and financial experiences of their client, particularly in relation to risk tolerance and financial risk.
3. Their client's ability, both financial and in relation to their level of comfort, to tolerate loss of capital and income.
4. Their client's financial planning needs across the short term, medium term and long term.
5. Non-monetary matters that may affect their client's financial needs and goals.

Based on this information, a financial adviser will develop a financial plan with appropriate strategies that their client is comfortable with, to help them work towards their life goals.

A financial adviser's responsibilities are to make clear recommendations, outline the risks involved and communicate any possible strengths or weaknesses in the plan. The level of investment risk will be stated in the financial plan and should reflect the risks the client is comfortable with taking.

For those receiving long term financial planning (ongoing advice), the financial adviser will keep clients updated with changes that could influence their investments or financial plan, such as market downturns; ongoing legislative change; provide regular reviews of the financial plan; and regularly evaluate client's needs, financial goals and strategies.

Consumer benefits of quality financial advice

Quality financial advice is important for consumers as it can:

a) Reduce financial and social exclusion for consumers and help them navigate the financial marketplace and learn how to better manage their finances.
b) Deliver significant consumer benefits including changes in savings behaviour, setting proper budgets, following a plan for paying off debt, and organising finances and building wealth.

c) Change people's behaviour and habits of managing their financial affairs by teaching them sensible and simple practices that can be used in their everyday lives to prepare for their future financial needs.
d) Help improve the financial capability of consumers, enabling them to make informed judgements and effective decisions about the use and management of money throughout their lives, including an ability to articulate and prioritise their financial goals.
e) Help consumers with debt management and reduction, budgeting, cash flow management, a savings plan, superannuation, tax planning, home loan repayments, insurance, investments, and estate planning as well as planning for retirement.

A service of national public importance

Research shows there are clear societal benefits of quality financial advice which demonstrate that it is in the national public interest to ensure the professionalisation of the following services continues:

a) Reduced debt - increases disposable income for more productive purposes.
b) Building wealth - higher rates of return on investments over long periods and minimise the need for people to rely on social security.
c) Insurance protection – protection against financial loss and minimises the need for people to rely on social security.
d) Higher levels of savings – reduces reliance on government benefits during and after retirement.
e) Financial capability - encourages a financially literate and conscientious society that make better long-term decisions.

FPA'S RESPONSE TO THE ROYAL COMMISSION INTERIM REPORT

In response to questions raised in the Royal Commission Interim Report, the FPA is recommending a raft of interdependent measures to:

a) Ensure adequate and appropriate consumer protections are in place and effectively enforced;
b) Enhance the capacity of the emerging financial planning profession to perform its role in the provision of quality financial advice in the interests of the public the profession serves; and
c) Build trust in the profession.

The FPA has limited this submission to questions related to the provision of financial advice.

1. How does a financial adviser's employer encourage the provision of sound advice (including, where appropriate, telling the client to do nothing)?

Employers and licensees similarly encourage the provision of sound advice. However, it is the experience of FPA practitioner members that employers place more emphasis on culture, education, and the acquisition of ethical employees. In saying this, it is worth

noting that employees may be directly employed by an AFSL or may be employed by a practice authorised by an AFSL (i.e. an employee of a corporate authorised representative). This is generally due to the direct relationship between employer and employees that provides a direct influence on culture and ethics. It was felt that an employer tends to facilitate a more communal environment, engaging with clients more personally where client's best interests can be placed first. Whereas, an AFS functions more as a financial service provider and compliance advocate.

An employer encourages the provision of sound advice through:

- Authorisation and employment
- Remuneration - both salary and bonuses
- Balanced score cards
- File reviews and audits of advice
- Training
- Practice management
- Supervision and monitoring
- Qualifications and certifications
- Sourcing of clients
- Technology
- Service offers
- Advice tools/processes
- Mentoring and coaching
- Support staff

In most instances, these resources allow the financial adviser to focus exclusively on delivery of services to their client in a focused way which allows them to concentrate on quality advice provision without the need to focus on the sustainability of their own financial advice business more broadly. On the other hand, employees may feel they have less ability to influence the advice and services being provided due to the employee/employer relationship. This is where professional association membership can assist by supporting employee financial advisers understand professional norms in delivering advice services to their clients.

2. How do advice licensees encourage advisers aligned with the licensee to provide sound advice (including, where appropriate, telling the client to do nothing)?

The quality of sound advice correlates to the quality of the licensee. The nature of the complex regulatory environment is such that financial advisers often rely on the assistance of licensees to meet their legal obligations and provide advice in a timely manner.

To answer this question, the FPA surveyed our members to ascertain what licensees actually do (rather than just what is required under the law). The following feedback was received regarding how licensees assist advisers to provide sound advice:

- File reviews and advice audits - Licensees assist with annual file audits and feedback to ensure sound advice is being provided.
- Training - licensees provide training on legal requirements and changes, including AML, the best interest duty, adviser conduct, and research methodology. Advisers receive feedback through professional development workshops, job seminars and

client-focus discussions, to ensure quality and compliant advice is being provided to clients.
- Advice documentation and process - Licensees provide resources such as SOA templates, guidelines and strategy papers on the adviser best interest duty, to assist with the advice research process. Clear checklists and policy guidelines help advisers to follow due process around the collection of appropriate information and clearly define the scope of the advice and services provided.
- Technical tools - such as paraplanning software and services provided by licensees also assist with the provision of sound advice.
- Approved Product Lists (APLs) - The licensee's APLs provides individual financial advisers with additional due diligence on product viability, however a balance is needed between in-house products and compliance checks of other products required for advisers to provide sound advice (see response below to question 7 for further discussion on APLs).

While licensees also assist with recruiting advisers with adequate education, integrity and ethics, more could be done in this area. While licensees are obligated to verify that authorised advice providers meet relevant education, ethical and professional obligations as part of their onboarding process, the FPA believes there is a role for independent third parties such as professional associations to be involved formally as a check for any past disciplinary action taken against the adviser by the regulators and professional associations.

Based on member feedback, employers tend to facilitate a more communal environment, engaging with clients more personally where clients' best interests can be placed first; whereas a non-employer licensee functions more as a financial service provider and compliance advocate. In saying this, often financial advice practices non-employer licensees authorise which form part of the communities they operate in often have the closest personal relationship with the client.

This suggests there are differing level of influence on ethics between non-employee and employer licensees based on their ability to set day to day culture and ethics under employment arrangements, although as noted in the Commission's interim report, this does not always lead to perfect consumer outcomes. That is, licensees broadly can have a stronger influence for change and should be appropriately obligated to function as an advocate for ethical behaviour rather than solely a financial service provider.

While licensees already have obligations around ensuring their representatives meet the best interest duty and have conflicts of interest management in place, the FPA recommends that ideally there would be an obligation to facilitate a culture of ethics and integrity. A best interest duty on licensees under s 912A may assist in this regard.

3. Can conflicts of interest and duty be managed?

There are divergent views in the industry as to whether conflicts of interest and duty in financial advice can be managed. The FPA believe that conflicts of interest is embedded in all occupations and all business models and cannot be completely removed. Conflicts of interest and duty should be avoided or, if avoidance is not possible, effectively and appropriately managed, and in the case of financial advice - clearly disclosed.

Firstly, there must be the ability and willingness to recognise and understand conflicting situations at all levels and by all individuals within an entity, regardless of the business model

or structure. While the law may create regulatory obligations in this regard, this also comes down to culture and ethics.

At a licensee level, this must include ensuring that neither the parent company nor the product side of the business, place pressure on advisers to sell in-house products, make inappropriate requests, or provide inappropriate inducements of advisers. This should include the use of scorecards, remuneration, or rewards for achieving sales targets of specific products.

The regulatory regime must address the pressures and potential conflicts created within the licensing structure by the competing interests of the licensee.

The absence of a licensee best interest duty to support the adviser's best interest duty creates a significant conflict and tension for the financial services industry. Advisers can be 'stuck' between their legal obligations to the licensee as per their contract, and their 'best interest' legal and ethical responsibilities to the client. The resulting pressure and conflict created for advisers can jeopardise the consumer protection benefits of this measure, which may not be realised.

The authorising licensee duty to clients is usually directed towards the licensee's client base as a whole, whereas the duty on the individual providing the advice is directed towards that adviser's individual client.

The individual adviser owes duties to their licensee via employment contracts and/or authorising contracts. The contractual duties owed by the adviser to their licensee will often place the adviser's interests in conflict with their client's interests.

Given the individual financial advisers best interest duty and common law fiduciary duties to the client must always prevail, there should never be a situation where the individual adviser has to make a decision between the duty to their client and their duty to their employer. The financial adviser must be able to carry out their duties to the individual client without fear or favour from their employer or licensee.

It should be recognised that the authorising licensee's interests are commercial – to act in the interests of their shareholders. It is the reality of economics that businesses must generate revenue and be viable to survive and be able to provide services to their clients. As evidenced in the case studies, there is a need to make sure licensees take appropriate measures to ensure that the licensee's commercial interests do not unduly interfere in the individual adviser's performance of his or her best interest duty to their client.

The licensee's interests may be constrained by the conditions placed on their license and other consumer protection measures in the Corporations Act, as well as their general law obligations. However, their interests are fundamentally commercial and therefore can be in conflict with the interests of their clients.

There will be many circumstances in which it is not possible for the individual adviser to know the (commercial) interests of the licensee. The practical reality is advisers are unlikely to have perfect knowledge of their licensee's commercial interests despite the disclosure obligations in place to obviate this risk.

A best interest obligation should be included under the licensee general obligations in s912A of the Corporations Act.

4. How far can, and how far should, there be separation between providing financial advice and manufacture or sale of financial products?

There is an inherent conflict of such a degree between the product manufacturers need to sell products and the advice businesses' legal and professional obligations to act in the client's best interest, that it is better for the community to restrict the combination of product and advice.

The FPA has long held the view that it is necessary to have a separation of advice and product. The reason for our position is the strong tension between the professionally constrained interests of advice businesses and the commercial interests of product businesses. Unless advice businesses are protected from undue pressure from product businesses, the tension between product and advice may not serve the interests of consumers.

Although there are benefits to vertical integration, such as economies of scale, adaptability and risk management, we believe these benefits can potentially be outweighed by the risks and costs to consumers of biased advice. Consumers are generally not in a position to assess the influence those pressures may have on the quality of advice as demonstrated through a number of ASIC reports (such as Report 279 at [22]) which show consumers are unable to discern advice that is not of good quality (Report 279 at [18]).

Another issue is the current reliance on the definition of 'financial product advice' is problematic as it ties the obligations for the provision of personal advice to financial products. This also excludes the provision of: budget management/cash flow; paying down debt; whether to lend money to family; property decisions around purchasing verse renting; whether to renovate or buy a new house; how to fund children's education (for example) from the personal advice regulatory obligations yet are common areas of enquiry by consumers.

The FPA therefore recommends that it is important to start with a rethink of the legislative definition of 'personal advice' being based on 'financial product advice' in the Corporations Act which explicitly ties advice to product.

Further, there needs to be clear identification that 'general advice' does not take a consumer's personal circumstances into account but is designed to sell a product to the consumer.

Finally, the relationship between the advice business and product business within a vertically integrated business must be considered.

5. Should financial product manufacturers be permitted to provide financial advice?
a. At all?
b. To retail clients?

As per our response to Question 4 above.

6. Should financial product sellers be permitted to provide financial advice?
a. At all?
b. To retail clients?

In addition to our response to Question 4 above, the FPA advocates changes to the general advice provisions.

It is clear that consumers do not understand the difference between when their personal circumstances have been taken into account to provide financial product advice, and when they are purely being sold a product. For this reason, it is important to relabel personal advice, general advice and factual information to make it clearer to consumers what is being provided to them.

The FPA supports the Productivity Commission's recommendation 10.2 to rename general advice to improve consumer understanding; and for the term 'advice' only to be used in association with 'personal advice' that takes into consideration a consumer's personal circumstances.

This should be a renaming of the term 'general advice' only. Licensing and all the other forms of regulation which currently apply to 'general advice' should remain in place and apply under the alternative terminology.

However, the Productivity Commission's Recommendation 10.2 is not sufficient to address the problems that can arise where financial products are sold under a general advice model. Additional changes are also necessary, including:

- Consumer warning – the current 'general advice' warning under s949A of the Corporations Act should be amended to require the warning to clearly state that:
  - the information does not include any advice in any form;
  - it does not take account of the consumer's objectives, financial situation or needs;
  - it is information only and the best interests of the consumer have not been considered in providing the information; and
  - if the sales representative will be remunerated via a commission or incentive payment for the sale of that product.
- Product obligations - An obligation on product providers to ensure products sold through 'general advice' must be fit for purpose and simple for consumers to understand and assess. This obligation must relate to product design, not just disclosure.
- Product provider 'target market determinations' should include a risk rating for financial products. Target market determinations of products with high risk ratings should be required to include a stronger warning and a recommendation to seek personal financial advice about the product. This could be achieved though regulatory guidance.
- Licensing exemption - The removal of the current licensing exemption for financial product issuers under regulation 7.1.33H.

7. Should an authorised representative be permitted to recommend a financial product manufactured or sold by the advice licensee (or a related entity of the licensee) with which the representative is associated?
a. At all?
b. Only on written demonstration that the product is better for the client than comparable third-party products?

An authorised representative (financial adviser) should be permitted to recommend a financial product manufactured or sold by the advice licensee with which the representative is associated, if that advice and product recommendation meets the requirements of the adviser's Best Interest Duty under s963B.

Restricting the ability of financial advisers to consider and recommend certain products on the market would unfairly restrict consumer access to those products, products which may be in the best interest of and appropriate for the client given their circumstances. This may lead to consumers being unable to have their advice needs met, specifically on products they already own.

Financial products purchased by a retail client under personal financial advice is the only channel that includes an intermediary that has a legal obligation under the Best Interest Obligations under s963B in the Corporations Act, to:

- consider the appropriateness and suitability of the product for the individual consumer's circumstances,
- consider other products,
- put the consumer's interests ahead of their own and those of related third parties, and
- ensure they are competent to provide the advice and to recommend the consumer invest in/purchase the product.

These obligations provide additional consumer protection benefits that are not available to consumers who purchase financial products via general advice or direct sales. The Best Interest Obligation specifically requires an authorised representative to compare products and show how any advice they provide, including the products they recommend, would put the client in a better position.

Approved Product Lists (APLs) are commonly used by AFS licensees to provide a list of financial products for their representatives to consider when providing advice to their clients; and are used as a risk management tool to assist a licensee in meeting the legal obligations when it or its representatives provide financial product advice.[1] This highlights that APLs are used by two related but separate groups – licensees as a risk management tool; and individual financial advisers for additional due diligence on product viability.

The Best Interest Duty under s963B of the Corporations Act, and ASIC guidance, set strong requirements for how financial advisers use an APL and consideration of products both on and outside a licensee's APL.

However, there is no legal or regulatory requirement to have an APL. It is a requirement put in place by some Professional Indemnity (PI) insurers, particularly in relation to superannuation and investment products as the APL can offer additional consumer protections due to the plethora of products available on the market, some of which contain significant risk PI insurers are unwilling to underwrite.

While licensees conduct specific due diligence on and scrutiny of products listed on their APL which can offer consumer benefits, we are aware that there is current debate about whether the APL has limitations and is therefore detrimental to consumers. From a financial advice perspective, the law permits consideration of products both on and outside the APL and requires the adviser to seek permission from their licensee to recommend a product outside of the APL. It should be noted that this legal requirement was only introduced in 2014 as part of the Future of Financial Advice (FoFA) reforms and is therefore only now being tested. In relation to the application of the APL and any impact (positive or negative) it may have on consumers receiving financial advice, at this time the FPA supports the role of the Best Interest Duty. However, consideration should be given to more prominent and prescriptive disclosure of the parent company, as an appropriate consumer protection mechanism. The FPA will continue to monitor this matter to ensure any potential adverse consumer consequences of APLs are identified and appropriately addressed.

8. Should the grandfathered exceptions to the conflicted remuneration provisions now be changed?
a. How far should they be changed?
b. If they should be changed, when should the change or changes take effect?

The payment of ongoing commissions and service fees for which no, or unreasonably little, actual service is provided contravenes the FPA Code of Professional Practice and reasonable community expectations, regardless of whether the commissions and fees are grandfathered. For this reason, the FPA opposes payment of commissions and fees in these circumstances.

To help protect consumers from such payments being made in these circumstances, the FPA would support the removal of grandfathering for ongoing commissions and service fees. Specifically, we recommend that grandfathering of commissions for superannuation and investment advice should be phased out over a 3-year transition period.

Removing grandfathering would:

- remove certain ongoing payments that are not clearly identified by the product provider to the consumer as payments to third parties – this means that if these payments continue they would need to be separated out and labelled as third-party payments, which would ensure continual disclosure of their quantum and character;
- require these payments and the associated services to be disclosed on a periodic basis; and
- require the payments to cease after a certain period unless the client opts for the payments to continue.

Removing opaqueness, requiring periodic disclosure and terminating ongoing fee arrangements unless the client explicitly authorises them reduces the risk that consumers will pay for no, or unreasonably little, actual service or for services that are otherwise of less value to the consumer than their cost.

The FPA supports the phasing out of grandfathered commissions provided the following principles are met:

1. The change is in the client's best interest – no client will be worse off

2. Commission payments are actually refunded to clients and not retained by the product provider where the client has not authorised their payment to their adviser
3. Tax relief is provided for any adverse tax consequences (including CGT)
4. Centrelink benefits are protected from any adverse Centrelink consequences
5. Exit fees be banned in line with the Government's 2018/19 Budget proposal on both super and investment products.

Our position is consistent with the principles we established in 2009 for financial adviser remuneration, which reflect the importance that remuneration in the financial planning profession is clear, concise, comparable, and more than anything else, is aligned to a service that delivers value. These principles are:

6. Clients must be able to understand the fees they are paying.
7. Clients must be able to compare the fees they are paying.
8. Clients must be presented with a fee structure that is true to label.
9. Clients must be presented with fees that are separated between advice and product.
10. Clients must agree the fee with their financial adviser and can request that the fee is switched off if no on-going advice is required.
11. Clients, rather than product providers, should pay for financial planning services, so as to remove potential for bias.

Further, commissions are by their nature part of a product cost. In most cases the removal of an adviser does not provide any benefit to a consumer as the provider simply retains the amount that would have otherwise been paid to an adviser. For the removal of grandfathering of commissions to have any effect there would also need to be a substantial shift in the way historic products with commissions are treated by product manufacturers to ensure there is no consumer detriment. Where the commission payments stop, there needs to be a requirement that foregone commissions are rebated to the client by the product provider.

As noted above, while the FPA believes that clients, not product providers must pay advice fees, flexibility and choice are important for consumers in deciding how to pay for advice. For this reason, the FPA believes that where the advice is provided in relation to superannuation and therefore complies with the sole purpose test, the member should be able to direct the advice fee to be taken from the member's superannuation account.

The FPA believes however that all advice fees must be transparent, and regularly disclosed to consumers. The FPA therefore also recommends that all fees become disclosable on fee disclosure statements, including the source of the fee to ensure consumers are able to clearly identify the source and implication of all fees paid to their financial advice provider. As per the statutory opt-in provisions, clients should also be able to request that the fee is switched off if no ongoing-advice is required. This will ensure consumers are appropriately protected, but also ensure that there is flexibility in the ability for consumers to pay and receive financial advice from appropriately authorised financial advisers.

We also believe that to cover circumstances where it is in the client's best interest to move out of a commission-paying superannuation product, CGT and social security rollover relief be available to the consumer upon the move. This will spare consumers from immediate adverse CGT consequences and loss of potentially favourable grandfathered

social security means testing as an unintended consequence of ceasing the payment of grandfathered commissions.

9. Should the life risk exceptions to the conflicted remuneration provisions now be changed?
a. How far should they be changed?
b. If they should be changed, when should the change or changes take effect?

The FPA recommends that life insurance commissions not be changed. Life insurance arrangements were recently reviewed, and major changes are being implemented through the Life Insurance Framework (LIF). The LIF commenced on 1 January 2018 with a review scheduled for three years from the date of commencement. The FPA does not believe another review of these arrangements is appropriate and urges the Commission to allow the agreed time frame to run before further reviews of life insurance commission arrangements are conducted.
Furthermore, increased professional standards being introduced by the Financial Adviser Standards and Ethics Authority (FASEA) under the Corporations Amendment (Professional Standards of Financial Advisers) Bill 2016 will also play a role in the outcomes from the LIF.

Financial advisers are required to research life insurance products to ensure any product recommendation is appropriate for their client's circumstances and is in their client's best interest. In addition to the initial advice, financial advisers also provide ongoing reviews, portfolio adjustments, ongoing market testing, policy administration and claims management under their remuneration structure. The market testing and ongoing client reviews are usually conducted annually and include assessing if there are any changes to the policy or premium conditions, other policies in the market, and whether the policy continues to be appropriate for the client and their current circumstances.

The LIF was a significant change for the advised insurance market place. The intent of the LIF is to "reduce the financial incentive for financial advisers to churn consumers into new life insurance policies where there is no consumer benefit"[2]. We believe the behavioural and advice quality changes the LIF was designed to achieve are already being seen across the industry. However, the full impact of this change, supported by the Best Interest obligations and the new education and professional standards framework, needs to be experienced and assessed before further changes are considered.

10. Should any part of the remuneration of financial advisers be dependent on value or volume of sales?

The FPA opposes remuneration and incentive policies that reward financial advisers primarily for revenue generated for a licensee or employer. Where remuneration is linked to a sales-based culture focused on product, funds under management (FUM) and client numbers, this can influence inappropriate behaviours. Therefore, a financial adviser's remuneration should be linked to the provision of financial advice services and the fees collected from their clients for providing these services.

The FPA recommends banning other forms of conflicted remuneration including: volume-based payments, rebates, profit sharing and shelf space fees. This was not addressed in FoFA and should be rectified.

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[2] http://kmo.ministers.treasury.gov.au/media-release/007-2017/

11. Should all financial advisers (including those who now act as authorised representatives of an advice licensee) be licensed by ASIC?

Licensee/dealer groups play an important role in supporting financial advisers so that they can provide best practice quality advice to their clients. The FPA does not have a policy position advocating for individual licensing as a preferred licensing model and maintains its position as being neutral and agnostic regarding the licensee model structure. The role of a licensee is critical to the current regulatory system and each financial adviser must decide which licensee structure and/or business model works best for them and their clients.

The FPA would note, however, that financial advisers are already required to be individually registered on the ASIC Financial Adviser Register and with the Tax Practitioners Board (TPB) as either a tax agent or tax (financial) adviser (personally or via a supervision model), both of which can be considered individual registration or licensing standards. Both ASIC and the TPB already have the power to ban or exclude an individual from providing financial advice or tax (financial) advice services (respectively) where they breach their legal obligations.

12. Are current product and interests disclosure requirements sufficient to allow customers to make fully informed choices?

The current disclosure regime does not adequately serve the interest of consumers sufficiently to allow customers to make fully informed choices.

The focus on "process regulation" rather than "outcomes regulation" in Chapter 7 in particular has led to a tick-a-box approach to compliance for many financial services entities and ASIC. The legal requirements around disclosure have resulted in the legal drafting of lengthy documents that are cumbersome and difficult for consumers to understand, and particularly difficult for consumers to assess how the information relates to their personal circumstances.

The product disclosure regime introduced under the Financial Services Reform (FSR) Act 2001, was intended to improve consumer protection by improving the availability of product information to consumers. Since the commencement of the FSR it has been shown that disclosure does not provide protection for consumers. Disclosure is the provision of information. It therefore relies on the information to be provided to consumers in a manner that is understandable for each consumer to increase the chance of consumers reading, digesting, and assessing the information prior to making a decision and acting on the information. The current system falls down as, in the main, disclosure documents are not easy for consumers to read or understand, and this discourages consumers from reading them.

Financial products and contracts are complex and complicated. It can be extremely difficult for a consumer to understand and assess the product contract and information.

The FPA notes the Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 currently before Parliament and under Inquiry by the Senate Economics Legislation Committee. This Bill would see the introduction of product regulation including an obligation on product providers to produce 'target market determinations' to ensure that products are targeted at the right people; and a product intervention power for ASIC when there is a risk of significant consumer detriment.

While the target market determinations to be introduced under this Bill are a positive step forward, some products are complex and present a significant risk to consumers that may not be fully represented or understood under the requirements in the Bill. Consideration should be given to the addition of a risk rating for financial products, provided through ASIC guidance. Target market determinations of products with high risk ratings should be required to include a stronger warning and a recommendation to seek personal financial advice about the product. The FPA is not suggesting mandating personal financial advice on complex and high-risk products or requiring sign off by a financial adviser, but noting the complexity and risk for the consumer and that a financial adviser is able to assist in ensuring it is an appropriate product for the consumer to invest in.

The interests of consumers would also be best served with a greater focus on consumer protection rather than attention on compliance with disclosure requirements. Consumer protection would be improved by the introduction of a positive obligation on the provider and distribution channel to ensure the consumer understands the information they have received and the product they are purchasing and requires the consumer to provide informed consent for the purchase to proceed. This positive obligation should include reference to the Cooling-off period for return of a financial product under s1019B of the Corporations Act 2001.

Regarding remuneration, the FPA believes that all advice fees must be transparent, and regularly disclosed to consumers. The FPA therefore also recommends that all fees become disclosable on fee disclosure statements, including the source of the fee to ensure consumers can clearly identify the source and implication of all fees paid to their financial advice provider. As per the statutory opt-in provisions, clients should also be able to request that the fee is switched off if no ongoing-advice is required, or the services provided are not commensurate for the fee being charged. This will ensure consumers are appropriately protected, but also ensure that there is flexibility in the ability for consumers to pay and receive financial advice from appropriately authorised financial advisers.

The FPA also supports more prominent and prescriptive disclosure of the parent company, as an appropriate consumer protection mechanism.

13. Should the period after which a client must positively review an ongoing fee arrangement be reduced from two years to one?

The FPA does not support the need in changing the ‘opt-in’ requirements for ongoing fee arrangements from two years to one year.

The FPA has conducted research on the impact of the opt-in requirement. The most consistent and substantial feedback from FPA members highlights concerns that clients do not understand the significance of not responding to the opt-in renewal notice, and the impact this has to the advice engagement and ongoing services they receive, and routinely fail to respond on time.

As required under the Regulations, if the client fails to respond on time the adviser must cease the provision of all services, including any advice and investment management or other services agreed to under the ongoing fee arrangement. It is then common for clients come back at a later stage wanting to continue the advice relationship, stating they never had any intention for the engagement or services to cease.

Impacts clients have experienced due to the opt-in requirement include:

- Unable to receive timely advice when they needed it as they failed to opt-in within the required timeframe leading to a new service agreement to be put in place
- Unhappy, frustrated and feeling hassled with additional paperwork and reminders to respond
- Confusion and questioning about why they must opt-in to an arrangement they have previously agreed to and know they can cancel at anytime
- Defensive about the latent threat of cessation of advice services (that they value) if they do not opt-in
- Do not perceive any value in the requirement as they have a contract already in place and therefore do not give it due attention
- Face a barrier to the time critical advice service if they have failed to opt-in and therefore need to go through the process of re-engagement
- Higher costs reflected in higher advice fees.

These consumer impacts would be exacerbated if the renewal period was decreased from two years to one year.

14. Should platform operators be permitted to deduct fees on behalf of licensees without the express authority of the client of the platform operator?

Clients must agree the fee with their financial adviser and can request that the fee is switched off if no on-going advice is required and clients, rather than product providers, should pay for financial planning services, so as to remove potential for bias. This shouldn’t limit the ability of advice fees to be collected by platform operators, but only where the client has provided authority.

15. When an employee or authorised representative is terminated for fraud or other misconduct, should a licensee inform their clients of the reason for termination?

The FPA would support a requirement for the licensee to inform the clients of an employee or authorised representative terminated for fraud or misconduct, if the fraud or misconduct has been determined by a court, an independent body or Regulator, where this information has not already been disclosed. This would increase transparency and encourage clients to agree to a review of the advice they have received to ensure they have not been impacted by the fraud or misconduct, and the advice provided is appropriate. It is also in line with the requirement to provide financial products and services ‘efficiently, fairly and honestly’.

16. When an employee or authorised representative is terminated for fraud or other misconduct, should a licensee review all the files or clients of that employee or intermediary for incidents of misconduct?

A licensee should review all the clients of an employee or authorised representative who is terminated for fraud or other misconduct. This would ensure licensees have considered and investigated whether the fraud or misconduct is likely to have been repeated with other clients or poses a potential risk for other clients, particularly in large scale organisations. Licensees should also consider where monitoring and supervision

arrangements or systems can be enhanced to ensure fraud and other misconduct are identified (where they occur) earlier to better protect consumers.

17. Should negotiation and settlement be the main approach for a regulator?

Where the regulator is able to negotiate an appropriate outcome with a licensee or individual and reach a settlement which meets the community's expectations, there should be no undue pressure on the regulator to seek to take the case through the legal system. The benefit of negotiated outcomes and settlements is they will generally be achieved in a more expedient manner, and without the additional costs and delays associated with the legal system.

To this point however, and given the findings made in the interim report by the Commissioner in relation to the performance of the regulators, it would seem appropriate for the regulator to test determinations, negotiated outcomes and settlements through a formal committee structure made up of both industry experts and consumer advocates, either as part of the agreement process, or on a review basis. In either instance the regulator can learn and iterate their decision-making process based on feedback from the community it serves.

18. Should there be greater focus on general deterrence in regulatory strategy?

In the FPA's view, there is a sufficient level of general deterrence present in the financial services industry in terms of the role and possible outcomes available to the regulator, particularly once the ASIC Enforcement Review recommendations have been implemented which close some current gaps and otherwise enhance ASIC's powers. The issues highlighted in the interim report appear to be that the regulator has at times preferred to negotiate outcomes which are more beneficial to the licensee or individual than the consumers affected.

As noted in response to question 17, the FPA would recommend that the community be consulted on outcomes of specific deterrence determinations to ensure the robustness of the overall general deterrence strategy for the entire financial services industry. Further, it is important to ensure all deterrents are commensurate with the breach behaviour exhibited. This will make it more likely that licensees and individuals will work with ASIC to achieve the appropriate outcomes in terms of redress and remediation for consumers, and broader improvements in the consumer protections framework.

19. Should a component of enforceable undertakings be the acknowledgment of specific wrongs?

The FPA supports requiring the party to the enforceable undertaking to acknowledge specific wrong doings. The FPA supports greater transparency in this area.

20. Should self-reported breaches of the Corporations Act generally attract legal sanctions unless some special circumstances exist?

The FPA supports a package of enforcement penalties and legal sanctions for breaches of the Corporations Act, to be applied on a scale based on the severity, intent and systemic

nature of a breach, and consumer detriment caused, regardless of how ASIC becomes aware of the breach - whether through self-reporting, complaint or other means.

Not reporting a significant breach to the Regulator is, in and of itself, a breach of the Act and therefore should act as a means of encouraging self-reporting. A failure to report or significant delay in reporting should attract additional legal sanctions.

21. Should banning orders continue to be preferred to civil penalty proceedings in case of licensee/adviser misconduct?

The FPA supports a package of enforcement penalties and legal sanctions for breaches of the Corporations Act, to be applied on a scale based on the severity, intent and systemic nature of a breach, and consumer detriment caused. The severity and intent of the misconduct, and consumer detriment caused, can vary significantly and should therefore be assessed to determine the appropriate sanction.

While we support the use of both banning orders and civil penalties, an enhanced penalty regime, such as that proposed by the ASIC Enforcement Review, should include significant penalties that clearly identify and create boundaries around those who are licensed to provide financial services and products to retail clients, and those who are not.

We suggest enforcement options within the law should be proportionate to the wrongdoing and consistently applied across the sector based on consumer risk and detriment. The regime should also be tough on offenses of fraud, dishonesty and gross misconduct. Given these kinds of offenses create most risk to the community, the use of banning orders is a useful step in ensuring the offender is removed from the system. While civil penalties are useful in repatriating profits of illegal activity by the regulator, they do not necessarily provide protection to the broader community from the offending individual the way a banning order does.

We would note that neither banning's nor civil penalties necessarily lead to the remediation of clients who may still end up with no resolution.

22. Should ASIC make more use of its Section 916G power to give a licensee information about a person who is or will be a representative of the licensee?

Where ASIC has become aware through reporting from a licensee, AFCA, a code monitoring body or another regulator that an individual is not fit to be employed or authorised by another licensee due to reported breaches of the law, ASIC should make this information available to the potential new licensee to ensure there is appropriate monitoring and supervision of the individual provided, or consider whether the authorisation is appropriate. Where this information is not shared, the new licensee may be placing their clients and consumers more broadly at risk of financial harm or further misconduct, despite their best endeavours to undertake due diligence.

We would note however that unless ASIC has concluded an investigation and made a determination on misconduct, this information should not be made publicly available to ensure judicial fairness to the individual.

23. Does Section 916G need to be amended so as to be more effective?

The FPA believes that where ASIC become aware of misconduct or has a concern about an individual's ability to provide financial services in the best interest of consumers, ASIC should also share information with other regulators, code monitoring bodies, and AFCA who may be in a position to take action against the individual based on additional information they have access to, or may be able to assist ASIC in their investigation more effectively and efficiently. Again (as per question 22), judicial fairness needs to be considered for the individual.

24. Should there be more focus on criminal proceedings against licensees rather than individual advisers?

Financial services laws and regulators should focus on encouraging financial services entities to place consumer needs at the heart of their products and services. Laws should ensure entities can be held to account to their obligations to consumers, maintain services which meet community expectations and comply with their legal and regulatory requirements. Regulators should enforce the legal requirements in a timely manner that meets community and industry expectations.

In the context that misconduct may be intentional or unintentional, a person who acts with the intent of deliberately doing the wrong thing or encouraging this type of behaviour must be held accountable. Where licensees are aware and do nothing, or actively encourage these types of behaviours, it is incumbent on the regulator to have in their punishment regime criminal proceedings, and to be seen to use them where appropriate to ensure other licensees understand the general deterrents available and maintain behaviours in line with community expectations.

On the other hand, for mistakes or unintentional breaches, the punishment regime should encourage cooperative early disclosure by the individual or licensee rather than encourage concealment. Regulators should be encouraged to reward these types of behaviours to ensure licensees maintain an open and honest dialogue with the regulator and can be seen to be maintaining appropriate monitoring and supervision over all staff and authorised individuals.

The ASIC Enforcement Review focused on the enforcement tools available to the Regulator, with the Regulator stating that its past enforcement activity has been restricted by the current penalty regime and its enforcement toolkit. The ASIC Enforcement Review proposes changes to the penalties for civil and criminal provisions in the Corporations Act and ASIC Act. An enhanced penalty regime should include significant penalties that clearly identify and create boundaries around those who are licensed including criminal penalties where misconduct justifies them.

The FPA suggest enforcement options within the law should be proportionate to the wrongdoing and consistently applied across the sector based on consumer risk and detriment. This must also be mirrored by clear enhanced accountability measures to ensure ASIC is performing its regulatory functions in an appropriate and effective manner that meets the expectation of both consumers and those in the industry who are doing the right thing.

25. Is the regulatory regime too complex? Should there be radical simplification of the regulatory regime?

The FPA would highlight that to provide financial advice services to consumers, financial advisers are required to comply with four laws regulated by seven regulators. The legislation includes:

- Corporations Act 2001
- Tax Agent Services Act 2009
- Anti-Money Laundering and Counter-Terrorism Financing Act 2006
- Privacy Act 1988

The regulators include:

- Australian Securities and Investment Commission (ASIC)
- Tax Practitioners Board (TPB)
- Office of the Australian Information Commissioner (OAIC)
- Australian Transaction Reports Analysis Centre (AUSTRAC)
- Australian Prudential Regulatory Authority (APRA)
- Australian Taxation Office (ATO)
- Financial Adviser Standards and Ethics Authority (FASEA)

This is prior to considering the technical aspects of financial advice covering aspects of superannuation, insurance, investing, estate planning etc. which also require a detailed knowledge of legal and regulatory rules.

This regulatory complexity where one piece of personal financial advice is regulated by 7 regulators, all administering Acts and regulatory requirements using different language and imposing different compliance requirements on financial advisers and licensees has significantly contributed to the issues identified by the Commissioner in the interim report. In addition, the same piece of advice will have oversight and interpretation by the Courts, the new Australian Financial Complaints Authority (AFCA), Australian financial service licensees and professional bodies such as the FPA.

This creates a significant risk that the regulatory and compliance requirements under one Act and Regulator may differ to those of others, leaving financial advisers at risk of breaching one regulation in order to meet the requirements of another set of regulatory requirements. Financial advisers must interpret how each different set of regulatory requirements for each different Regulator differ from other regulators to ensure they do not inadvertently breach requirements. This has a significant impact on costs and efficiencies, particularly on small licensees who do not usually have the in-house expertise or economies of scale to meet the regulatory demands.

Even small differences in requirements, significantly drives up process and compliance costs for businesses, ultimately impacting on the cost of providing advice to consumers and the sustainability and competitiveness of each business, and the risk of adverse consumer outcomes. Given the constant regulatory changes administered by each of these seven regulators, businesses have become paranoid about the plethora of regulatory requirements making them less inclined to invest capital or be innovative.

It also makes it more challenging for consumers to comprehend, trust and engage with the financial system, and understand their rights and the consumer protection mechanisms available to them.

The plethora of regulatory requirements from all the Regulators, professional bodies, and licensees, and the lack of stability in the financial advice regulatory environment, are overwhelming particularly for providers of financial advice who must understand and adhere to all the requirements.

It is recognised that genuine multiplicity of regulators may offer regulatory benefits for consumers and the regulated population as it can reduce the chances of a single approach to the administration of the laws, each of which serve a specific purpose in Australian society. It is also recognised that the laws administered by each of these seven regulators applies to a significantly broader regulated population than just financial advice providers.

The FPA recommends that consideration must be given to the extra complexity and cost associated with having multiple regulators, compared with the pros and cons of a monopolistic regulator for financial advice. We suggest the Commission draw on data from comparable foreign jurisdictions and compare consumer outcomes in jurisdictions with a monopolistic regulator with jurisdictions with competing regulators, to assess whether the benefits offered by a multi-regulator approach outweigh the extra complexity and cost associated with having seven regulators overseeing each piece of financial advice.

26. Should industry codes relating to the provision of financial services, such as the 2019 Banking Code of Practice, be recognised and applied by legislation like Part IVB of the Competition and Consumer Act 2010 (Cth)?

The FPA does not support this suggestion. In relation to financial advisers, the new education and professional standards introduced to the Corporations Act include an obligation to comply with a legislated Code of Ethics to be set by the new Financial Adviser Standards and Ethics Authority (FASEA).

The FPA supports the application of Codes of Conduct which set higher and industry specific obligations than the requirements in the law, are enforceable and enforced, and require a binding commitment on the signatories to the Code to comply with the codified standards. The FPA supports the legal permission for ASIC, under s1101A of the Corporations Act, to approve codes of conduct that relate to the activities of AFS licensees, their representatives or issuers of financial products. ASIC's *Regulatory Guide 183: Approval of financial services sector codes of conduct* sets strenuous and detailed requirements and procedures for code approval.

The approval of any Code of Practice should include appropriate and lengthy stakeholder consultation to ensure duplicate or conflicting standards are not introduced across the financial services industries.