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MINISTER FOR HUMAN SERVICES  
MINISTER FOR FINANCIAL SERVICES, SUPERANNUATION &  
CORPORATE LAW**

**MEDIA RELEASE**

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**OVERHAUL OF FINANCIAL ADVICE**

The Rudd Government is today announcing reforms to financial advice that will improve the trust and confidence of Australian retail investors in the financial planning sector.

The Minister for Financial Services, Superannuation and Corporate Law, Chris Bowen MP, said that the *Future of Financial Advice* reforms are designed to tackle conflicts of interest that have threatened the quality of financial advice that has been provided to Australian investors, and the mis-selling of financial products that culminated in high profile corporate collapses such as Storm Financial, Opes Prime, and Westpoint.

These reforms are the Government's response to the Parliamentary Joint Committee on Corporations and Financial Services' *Inquiry into financial products and services in Australia*.

"Australia is facing the challenge of an ageing population. Access to quality advice remains an important part of planning for the future," Mr Bowen said.

"These reforms will see Australian investors receive financial advice that is in their best interests, rather than being directed to products as a result of incentives or commissions offered to the financial adviser.

"ASIC's powers to act against unscrupulous operators will also be strengthened and professional standards for advisers will be reviewed by an expert advisory panel."

The *Future of Financial Advice* package includes the following:

- **A prospective ban on conflicted remuneration structures including commissions and volume based payments**, in relation to the distribution and advice of retail investment products including managed investments, superannuation and margin loans. The measure does not initially apply to risk insurance.
- The introduction of a **statutory fiduciary duty so that financial advisers must act in the best interests of their clients**, subject to a 'reasonable steps' qualification, and to place the best interests of their clients ahead of their own when providing personal advice to retail clients.
- Increasing transparency and flexibility of payments for financial advice by introducing '**adviser charging**' that will help align the interests of the financial adviser and the client; is clear and product neutral; and where the investor will be able to turn off the advice in response to a compulsory, annual renewal notice.

- **Percentage-based fees** (known as assets under management fees) will only be charged on ungeared products or investment amounts and only if this is agreed to with the retail investor.
- **Expanding the availability of low-cost 'simple advice'** to provide access to and affordability of financial advice.
- **Strengthening the powers of the Australian Securities and Investments Commission (ASIC) to act against unscrupulous operators.**
- The examination of a **statutory compensation scheme** by Mr Richard St John, who has significant corporate law experience.

The majority of these reforms will commence from 1 July 2012 and the Government will consult with industry on the implementation of the reforms.

"The expansion in the provision of low-cost, simple advice will be of particular benefit to individuals and families who may not currently have access to financial advice," Mr Bowen said.

Furthermore, the Government's progress on simple disclosure for investors and financial literacy will better enable individuals to understand, and therefore benefit from, the advice they receive.

"I welcome the significant efforts of industry, including the Investment and Financial Services Association (IFSA) and the Financial Planning Association (FPA) to remove commissions and improve professional standards. These reforms clearly support their efforts."

A summary of the Government's response to the PJC Inquiry and additional reforms is at Attachment A.

Attachment B provides an overview of the fees that can no longer be charged under the ban on conflicted remuneration structures.

## **BACKGROUND MATERIAL**

### **Reforms to Financial Advice - Summary**

- The reforms deliver improved quality of advice and enhanced retail investor protection.
  - It reduces key conflicts in adviser remuneration affecting the quality of advice. Advisers must have their own charging structure, which is 'product neutral';
  - It includes a statutory fiduciary requirement for advisers to act in the best interests of their clients and in so doing explicitly place their client's interest before their own;

- It boosts the powers of the Australian Securities and Investments Commission (ASIC) to act against unscrupulous operators;
- It expands the current scope of simple advice provided within a superannuation context to other areas of advice which will enhance the trustees' ability to give low-cost, simple, compliant advice within a member's superannuation fund;
- It removes the accountants' licensing exemption in relation to self-managed superannuation funds, with appropriate consultation on a more streamlined licensing replacement;
- It establishes an expert advisory panel to review professional standards for advisers;
- It appoints an expert, Mr Richard St John, to report on the need for a statutory compensation scheme;
- It reviews the appropriateness of the current method of classifying unsophisticated and sophisticated investors (i.e. retail and wholesale clients); and
- It simplifies the disclosure of advisory services provided to consumers.

## Timing and implementation of reforms

Stakeholders will be consulted on the implementation of these reforms, with particular emphasis on the adviser charging rules and statutory fiduciary duty, as well as on the legislation implementing the reforms.

The prospective ban on conflicted remuneration structures, adviser charging regime and statutory fiduciary duty will apply from 1 July 2012.

## ATTACHMENT A

### The PJC's recommendations and the Government response

**Table 1: Summary of the Government response**

Rec	PJC Recommendation	Summary of Government response
<b>1</b>	The committee recommends that the Corporations Act be amended to explicitly include a fiduciary duty for financial advisers operating under an AFSL, requiring them to place their clients' interests ahead of their own.	Support.
<b>2</b>	The committee recommends that the Government ensure ASIC is appropriately resourced to perform effective risk-based surveillance of the advice provided by licensees and their authorised representatives. ASIC should also conduct financial advice shadow shopping exercises annually.	Support in principle. ASIC is appropriately resourced to perform its functions.
<b>3</b>	The committee recommends that the Corporations Act be amended to require advisers to disclose more prominently in marketing material	Do not support.

	restrictions on the advice they are able to provide consumers and any potential conflicts of interest.	
4	The committee recommends that the Government consult with and support industry in developing the most appropriate mechanism by which to cease payments from product manufacturers to financial advisers.	Support with additional strengthening.
5	The committee recommends that the Government consider the implications of making the cost of financial advice tax deductible for consumers as part of its response to the Treasury review into the tax system.	The Government's response to the <i>Independent Tax Review</i> will be released on 2 May 2010
6	The committee recommends that section 920A of the Corporations Act be amended to provide extended powers for ASIC to ban individuals from the financial services industry.	Support.
7	The committee recommends that, as part of their licence conditions, ASIC require agribusiness MIS (managed investment scheme) licensees to demonstrate they have sufficient working capital to meet current obligations.	Support in principle, noting that implementation is a matter for ASIC.
8	The committee recommends that sections 913B and 915C of the Corporations Act be amended to allow ASIC to deny an application, or suspend or cancel a licence, where there is a reasonable belief that the licensee 'may not comply' with their obligations under the licence.	Support.
9	The committee recommends that ASIC immediately begin consultation with the financial services industry on the establishment of an independent, industry-based professional standards board to oversee nomenclature, and competency and conduct standards for financial advisers.	Do not support.
10	The committee recommends that the Government investigate the costs and benefits of different models of a statutory last resort compensation fund for investors.	Support.
11	The committee recommends that ASIC develop and deliver more effective education activities targeted to groups in the community who are likely to be seeking financial advice for the first time.	Support in principle.

<b>Additional Government Proposals</b>		
1	Remove the exemption for accountants from the requirement to be licensed when providing advice concerning the acquisition or disposal of an interest in a self managed superannuation fund, and consult on an appropriate replacement.	Additional Government proposal
2	Improve and simplify disclosure on the nature of financial services offered to investors.	Additional Government proposal
3	Consult on the appropriateness of the current criterion under which a client is classified as retail or wholesale.	Additional Government proposal
4	Improve access to simple or limited advice to assist in the affordability of advice, by removing regulatory barriers.	Additional Government proposal

**Table 2: Summary of the differences between the PJC’s recommendations and the Government response.**

Rec	Summary of the difference (if any)	Explanation for the difference
3	<p>The PJC recommended that advisers disclose more prominently in marketing material restrictions on advice they can provide and potential conflicts of interest. Rather than focusing on disclosure through marketing material, the Government considers it is more appropriate to improve the disclosure of financial advice services to investors through the simplification of disclosures made in the Financial Services Guide (FSG).</p>	<p>The PJC recommendation is not supported because it is difficult for a range of restrictions on advice and conflicts of interests to be meaningfully disclosed to consumers in the form of various kinds of marketing material. The Government acknowledges that it is important for consumers to better understand the nature of advice services on offer. For example, it is important for investors to understand any potential conflicts of interest, such as whether their adviser is independent from product providers. Here the Government is already acting to improve the disclosure of advisory services to consumers, through simplifying the disclosure of advisory services contained in the Financial Services Guide (a pre-sale disclosure document). This will be achieved by applying the principles of disclosure simplification developed by the Financial Services Working Group (Working Group), such as designing the disclosure to be concise and engaging, focusing on the information the investor needs to know in order to make an informed decision, and using clear and unambiguous language.</p>
4	<p>The PJC recommended that the Government consult and support industry in developing an appropriate mechanism to cease payments from product manufacturers to financial advisers. The Government proposal strengthens the recommendation by introducing a legislative ban on conflicted remuneration structures, including payments from product providers to financial planners. Furthermore, the reforms strengthen the PJC recommendation by including other conflicted incentives such as asset-based fees in relation to geared products or investment amounts and extending these standards to superannuation products and services.</p>	<p>The legislative approach is important to support the steps that some industry members have been taking in transitioning away from commission payments, by establishing a single legislative framework that applies to the retail financial services industry as a whole. This is necessary for the ban to be effective in addressing the distortions the remuneration structures create.</p>
9	<p>The PJC recommended that ASIC consult on the establishment of a Professional Standards Board. The Government proposal involves a review of professional standards, including competency and conduct standards, with a view to enhancing conduct standards for advisers in order to improve the quality of advice. This would involve establishing an expert advisory panel which may include members from the industry, professional associations, academia, consumer representatives and ASIC officers.</p>	<p>The Government acknowledges that the current arrangements for professional standards could be enhanced, and may benefit from increased stakeholder participation in the setting of competency and conduct standards. However, the Government considers that the establishment of a Professional Standards Board (PSB) is a matter for Government not ASIC. Furthermore, the Government is concerned about the costs of a separate PSB, which may be passed to consumers, and for the potential for significant overlap with the role of ASIC in enforcing competency and conduct standards.</p>
<p><b>Discussion of additional Government proposals</b></p>		

1	The PJC did not make a recommendation on the accountants' exemption because superannuation was outside the scope of the Inquiry. However a number of submissions to the PJC (and the Cooper Review) raised concerns with and highlighted the shortcomings of the accountants' licensing exemption.	Since 2004, recognised accountants (who have membership of at least one of three specific accounting bodies) have been exempt from the requirement to be licensed when providing advice concerning the acquisition or disposal of an interest in a self-managed superannuation fund (SMSF). However, various stakeholders, including those representing self-managed superannuation, have raised issues about the appropriateness of the exemption. The Government agrees that the exemption is not operating appropriately, and proposes to remove it. Furthermore, proposed consultation with the industry (including relevant professional bodies) would consider all options to replace the exemption, such as a more streamlined licensing regime.
2	See discussion under recommendation 3 above, relating to improved disclosure of FSGs.	
3	The PJC did not make a recommendation in relation to the categorisation of wholesale and retail clients.	<p>The distinction between a retail and wholesale client is important in the regulation of financial services. The obligations placed on financial services providers in relation to retail clients recognise the greater protection that unsophisticated investors need.</p> <p>The Government proposal will involve consulting with industry and reviewing the appropriateness of the current criterion under which a client is classified as retail or wholesale. The Government considers that a review of mechanisms for determining whether a client is classified as wholesale or retail is appropriate, to ensure the distinction remains relevant, including a review of current thresholds for determining wholesale or retail status.</p>
4	The PJC did not make a recommendation in relation to simple advice but did consider the affordability of advice generally.	<p>The Government considers that access to simple advice is an important issue, where this suits the client's needs. The provision of simple advice also assists with the affordability of advice issue. Some industry members have suggested there is uncertainty concerning whether the current regulatory regime enables the provision of simple financial advice.</p> <p>The Government's proposal builds on the existing success of the intra-fund advice project on superannuation advice, and seeks to address broad issues raised by industry around regulatory barriers to providing low-cost, compliant, simple advice.</p>

## ATTACHMENT B

### Reforms to Financial Advice– Adviser Remuneration

Form of Remuneration	Description	Permitted under the new regime
Initial/upfront commission	Advice fee charged as a percentage of the client's initial investment. The fee is an arrangement between the product provider and the adviser or the adviser's licensee and built into the product. The fee may be funded by a matching contribution or entry product	Not permitted. There must be separate fees for the product and advice.

	fee.	
Trail commission	Charged as a percentage of the client's assets (for example annually). The fee is an arrangement between the product provider and the adviser or the adviser's licensee and built into the product. The fee may be funded by a product administration fee.	Not permitted. There must be separate fees for the product and advice.
Fee for service charged as an asset-based fee on <u>un-gearred products</u> or <u>investment amounts</u> .	A fee for service, agreed between the client and the adviser, charged as a percentage of the client's funds under management and paid by the client to the adviser or licensee in relation to the provision of advice.  This asset-based fee can be deducted from the client's investment, at the direction of the client.	Permitted.
Fee for service charged as an asset-based fee on geared products or investment amounts.	Advice fee charged as a percentage of the client's funds under management and paid by the client to the adviser or licensee in relation to the provision of advice.	Not permitted.
Other types of fee for service for advice	May be charged, for example, as an hourly rate, flat fee per service provided, fixed annual fee (a retainer) or performance or outcome based fees. This may be paid up front, deducted from the client's investment funds at the direction of the client or through a payment plan (if offered by the adviser).	Permitted.
Any form of payment based on volume or sales targets (examples are below)	Whether this is in the form of a payment, from a product provider, or from any financial services business, in relation to the distribution or advice for retail financial products.	Not permitted.
<i>Volume based</i> Volume bonus and fee rebate	Paid by the product provider to the licensee or adviser and is generally conditional on the licensee having large funds under management (FUM) with the product.	Not permitted.
<i>Volume based</i> Volume based payments or sales incentives	Payments from licensees to their employee advisers or authorised representatives for distribution of retail financial products, which are calculated based on meeting sales targets or are volume based.	Not permitted.
<i>Volume based</i> Shelf space fee payments (based on volume)	Payments based on volume that are paid from the fund manager to the platform provider and from the platform provider to the licensee.	Not permitted.
Shelf space fee payments (not based on volume)	Payments not based on volume that flow to and from the platform, including a product access payment (provided that payment is not based on volume).	Permitted.

Note: Any form of non-permitted remuneration described above would not be allowed after 1 July 2012. The reform applies to all financial products, with the exception of risk insurance. The application of the reforms to risk insurance will be considered at a later date.