Association of Financial Advisers Ltd
ACN: 008 619 921
ABN: 29 008 619 921
PO Box Q279
Queen Victoria Building NSW 1230
T 02 9267 4003 F 02 9267 5003
Member Freecall: 1800 656 009
www.afa.asn.au

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The Manager
Retirement Income Policy Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: FSRCconsultations@treasury.gov.au

Dear Treasury,

AFA Submission: Advice Fees on Superannuation

The Association of Financial Advisers Limited (**AFA**) has served the financial advice industry for over 70 years. Our objective is to achieve *Great Advice for More Australians* and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

The Board of the AFA is elected by the Membership and all Directors are currently practicing financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting wealth.

Introduction

The AFA disagrees with recommendation 3.2 on the grounds that the recommendation is based upon a flawed understanding of financial advice, a lack of awareness of the benefits of financial advice for clients, and the apparent premise that MySuper fund members should be prevented from accessing comprehensive personal advice. We have set out our arguments for this below.

With respect to Recommendation 3.3, we have made a separate submission in respect to Recommendation 2.1, and whilst we will not repeat our position as set out in the submission on Recommendation 2.1, we have set out below our feedback specific to the proposed changes to the SIS Act as has been set out in response to Recommendation 3.3. We do not believe that in the context of the changes to Annual Renewal that it should be necessary to provide a copy of client consent to the superannuation fund trustees every year.

Ensuring a Level Playing Field for Financial Advice

The Financial Advice sector has been subject to significant change over a long period of time and that pace of change has increased in more recent years. It is interesting to note the extent of that impact across the different forms of financial advice, from general advice, to Intra-fund advice, personal advice and wholesale advice. Wholesale advice stands out as having survived unimpacted by all the key changes. Intra-fund advice has been subject to change, but a much reduced level of impact. Personal advice has been impacted the most as is demonstrated by the following table:

Obligations of the Adviser	General Advice	Intra-fund Advice	Personal Advice	Wholesale Advice
Advice Documents	No	Yes	Yes	No
Best Interest Duty	No	Yes	Yes	No
Financial Advice Fee Disclosure	No	No	Yes	No
FASEA Exam and Education Standard	No	Yes	Yes	No
FASEA Code of Ethics	No	Yes	Yes	No
Fee Disclosure Statements	No	No	Yes	No
Client Opt-in	No	No	Yes	No

Such significant change to one segment of the advice market, without equivalent changes to the other segments creates an imbalance in the market and ultimately poorer outcomes for Australians looking to build their financial futures. The substantial pressure on the personal advice segment is driving some financial advisers to a segment that is not subject to the same level of regulatory change and intense oversight, to the detriment of the consumer, or otherwise leaving the sector altogether. We further note that as a result of changes to ASIC Regulatory Guide 97 on Disclosing Fees and Costs in PDSs and Periodic Statements, that intra-fund advice fees will no longer need to be separately disclosed in PDSs and annual statements, which increases the extent of the differences and is inconsistent with the increased transparency and disclosure that has been placed on the fully advised segment.

The legislation that is currently subject to consultation continues the ongoing trend, where all the reform is focussed on the personal advice to retail client segment, and is having no or little impact upon wholesale advice, general advice or intra-fund advice.

We also believe that Recommendation 3.3 opens a further distortion in the playing field. Since the requirement to provide a copy of the client consent to the superannuation fund will not apply to super funds who have their own financial advisers (since they will already have it), this will create a cost distortion between in-house advisers and stand-alone or external financial advisers. It may also present a disincentive for superannuation fund trustees to support access to the fund for external financial advisers, as this will create additional costs in obtaining and storing copies of client consents. This will create a bias in favour of vertically integrated models.

Recommendation
The unlevel playing field issue is one that we recommend the Government needs to investigate and rectify, in order to ensure access and affordability of personal advice for the benefit of consumers.

Understanding Intra-fund Advice

On page 242 and 243 of the Final Report of the Royal Commission, the following statement was made:

> "Finally, nothing I have said above (including in respect of MySuper) relates to what is known as 'intra-fund advice': the provision of advice that is not personal advice, to members of a

> particular fund about their interest in that fund, where the cost of the advice is charged collectively to members of the fund in accordance with the SIS Act. It was not suggested that any misconduct arose from such arrangements and I say nothing about them."

This is wrong on more than one level. As has been made clear through the Parliamentary committee process, by Senator Andrew Bragg and ASIC, intra-fund advice is personal advice. The reason that there were no suggestions of misconduct with respect to intra-fund advice was in part as a result of the fact that, at that stage, ASIC had not done any comprehensive analysis of the quality of intra-fund advice. ASIC did release report 639 (Financial Advice by Superannuation Funds) in December 2019 that indicated that only 56% of the intra-fund advice that was assessed, complied with the Best Interest Duty and related obligations. This meant that 44% of this intra-fund advice was non-compliant. This outcome was broadly consistent with the results for personal advice. This is an outcome, at significant odds to the premise of the Royal Commission, that there was no misconduct in the intra-fund advice segment and was therefore excluded from all reform measures.

It is not surprising that the mistake was made with respect to understanding whether intra-fund advice was personal advice, as Section 99F of the SIS Act is worded in a particularly complex manner. It is also understandable that the Commissioner would have assumed that there was no evidence of issues with the quality of intra-fund advice, given that no report had previously been undertaken or released by ASIC. It was however known that ASIC had not looked at intra-fund advice at that stage. It is critical to appreciate that the Royal Commission report will be implemented by the Government, despite the existence of these material misunderstandings. It is appropriate to reflect upon whether the recommendations of someone who did not fully understand this market and the many structures and rules, should be implemented without question and without due process. We would argue not.

Recommendation
The AFA recommends the reconsideration of this recommendation to ban advice fees from MySuper accounts, which was made on a misguided understanding of the market and superannuation legislation and structures.

AFA's Response to Recommendation 3.2 – Banning Advice Fees in MySuper

Recommendation 3.2 is that there should be no deducting advice fees from MySuper accounts. Specifically, the recommendation states:

> "Deduction of any advice fee (other than for intra-fund advice) from a MySuper account should be prohibited."

The final report also states:

> "It is difficult to imagine circumstances in which a member would require financial advice about their MySuper account. If a member wants financial advice, the cost of that advice should be charged to and paid by the member directly."

This view is flawed as a result of the fundamentally incorrect assumption that the need for financial advice is linked to the investment option chosen (or taken by default) by the client. The AFA devoted significant effort trying to explain to the Royal Commission the value of financial advice for clients, but clearly without any success, based upon some of the comments that were made. Strategic advice is as important or more important than product advice. We acknowledge that in the superannuation context, understanding the value of strategic financial advice is somewhat restricted by the application of the Sole Purpose Test, which limits the scope of the advice that can be paid for from the

superannuation account. Nonetheless, financial advice that may be required by members of a MySuper product include the following:

- Advice on the consolidation of superannuation funds (which it should be noted cannot be provided under intra-fund advice).
- Advice with respect to whether the MySuper option is the most appropriate option for the member or whether it remains the most appropriate option. We need to recognise that some people consciously choose the default option, however their circumstances may change over time and it may no longer be the most appropriate investment option for them.
- Advice on salary sacrificing into super, which can deliver significant financial and tax benefits, enabling a more rapid accumulation of superannuation savings.
- Advice on making non concessional contributions, potentially as a result of an inheritance or through the investment of a retrenchment benefit.
- Retirement advice, including advice in preparation for retirement in the short to medium term.
- Advice on insurance arrangements that may be complex due to occupation, health conditions and family related matters.
- Guidance on death benefit nominations, taking into account issues such as blended families and the different tax consequences of the payment of death benefits to dependents and non-dependent children.

Each of the above types of advice, are completely unrelated to the investment option of the member and therefore equally applicable to clients in choice products and MySuper products.

This ban will also prevent members of MySuper members from paying for once-off advice, when they need it, which was surely not the point that Hayne was making when he talked about money being taken out of super accounts invisibly.

Whilst limited services may be available to the member under an intra-fund advice option, it should be recognised that not all superannuation funds offer an intra-fund advice service. In this event, the MySuper members would be virtually completely excluded from accessing financial advice.

The suggestion that the member should pay the fees directly, which presumably means from their bank account, neglects the fact that this might place the client at a disadvantage for the following two important reasons:

- Fees paid directly by the superannuation fund would have access to a 15% tax deduction, that would not be available through payments directly from a bank account.
- For the many people in Australia who have large mortgages or operate from pay cheque to pay cheque, they may not have available cash flow to fund the advice, without going into further debt. Whilst access to financial advice may deliver significant financial benefits, many may simply feel that they cannot afford to pay for the advice. This is a common reason why people do not access financial advice. The assumption that if people are not prepared to pay for financial advice from their bank account, that they do not value financial advice is simply fundamentally incorrect. Not everyone has the cashflow to easily afford financial advice.

With the introduction of Recommendation 2.1 and the particularly demanding and prescriptive rules with respect to the requirements for FDSs, annual renewals, and consent forms, isn't there sufficient protections for MySuper members to ensure that they are not unnecessarily paying for financial advice that they do not get or need? To have these strict rules in place, yet consider it necessary to also ban financial advice fees for MySuper accounts, is over-kill many times over.

We fundamentally see no logical argument to preclude the MySuper segment of the Australian population from accessing financial advice, and paying for it in an efficient and cost effective way, which may contribute significant benefit to the member.

We ask the question, what MySuper clients should do when they need advice? This could include the period just prior to retirement or maybe at a point later in their careers when they are subject to a retrenchment and receive a payout. What options do these members have, if they wish to have the advice paid for out of their superannuation fund, as opposed to directly from their bank account? One option is for them to move to a choice product, or they could just move some of their money to a choice product. It seems likely that superannuation fund trustees would need to consider what solutions might be available to assist these members to access financial advice, however it may not be in their best interests to move funds from the MySuper option to another option, or to put funds in a cash account for a limited period. Moving money from one option to another will create transaction costs and incur buy-sell spread costs. This ban will result in the need for arrangements to work around it. We also ask the question of what will happen to clients who are in MySuper products, and are currently accessing financial advice, that is paid for from their superannuation fund, and they wish to continue with this arrangement? It is our view that this is discriminating against members in MySuper accounts.

We are concerned that the Government agreed to the Royal Commission recommendations too quickly, without consultation or consideration of the consequences. This is one recommendation that will only disadvantage a large segment of the Australian population, if and when, they seek financial advice. It is important to carefully analyse the likely unintended consequences, including the fact that it will discourage people from accessing financial advice when they most need it.

Recommendation
The AFA recommends that the proposal to ban financial advice fees for MySuper accounts be discontinued in order to avoid discriminating and disadvantaging members in MySuper accounts.

AFA's Response to Recommendation 3.3

Commissioner Hayne made the following statement in the Royal Commission final report on page 241:

> "Given the limited nature of the advice that may be paid for from a superannuation account, it might be thought that there are few circumstances in which paying fees for ongoing advice of that kind would be in the best interests of a member.
>
> Perhaps a superannuation member invested through a platform would benefit – or believe they would benefit – from ongoing financial advice in respect of their superannuation investments. But such benefits would be relatively modest, and would accrue to relatively few members."

It is clear from this statement, that Hayne did not understand what financial advice is or the value of financial advice and his openly judgemental statement reveals a pre-disposition to dismiss financial advice. Accordingly, we hold the view that the response to his recommendations needs to take into account his position and the potential disadvantage to financial advice clients if his recommendations are not carefully considered and the consequences examined. The draft legislation to implement Recommendation 3.3 is simply taking the proposal with respect to Recommendation 2.1 somewhat further. The draft Explanatory Memorandum also, however, includes some additional expectations for trustees that do not appear to be entirely consistent with the legislation.

We are conscious of the reasons for tightening up on the charging of advice fees, however it is our view that extending renewal requirements to all ongoing fee clients and reducing the timeframe to annual, should have been sufficient to increase the level of control. To also mandate a requirement for financial advisers to obtain separate consent from clients and to provide a copy of this to the superannuation fund trustee each year is simply excessive red tape and duplication. This is unnecessary bureaucracy that will only serve to increase the cost and reduce the value for consumers.

We have set out a detailed review of the draft legislation in the points below:

- Section 99FA(1)(b) refers to a written consent of the member. What is not clear in the draft legislation or the draft Explanatory Memorandum is what form a written consent must take. We ask this question, as the initial discussion on Opt-in prior to the FoFA Bill being passed in 2012, was that Opt-in could be facilitated by the means of a text message. How could this consent be obtained from a client who is away on holiday and may not have access to equipment like scanners? Is an email response sufficient? Everything should be done to increase the automation and streamlining of the consent requirement. More needs to be done to consider how this can be done electronically.
- Section 99FA(1)(a) refers to an agreement, whilst Section 99FA(1)(b) refers to a written consent of the member. Does this imply that they are separate documents, or alternatively is it possible that these can be the same document?
- The requirement in Section 99FA(1)(a) is to ensure that the cost is paid in accordance with an agreement entered into by the member, yet there is no obligation for the trustee to obtain a copy of the agreement. If they don't have a copy of the agreement, then how can they confirm that the cost is paid in accordance with the agreement? We also question whether it is appropriate for the trustee to have a copy of the agreement between the financial adviser and the member, as it may have been contained in a Statement of Advice (SoA) that could contain confidential information that would be inappropriate for the trustees to have a copy of it.
- Section 99FA does not define the frequency of obtaining consent, whereas this is clearly set out in the related Corporations Act sections.
- The Corporations Act (Section 962T) sets up a power for ASIC to establish the requirements for a client consent, and this has been leveraged in Section 99FA(1)(c)(ii) for ongoing fee arrangements, yet Section 99FA(1)(d)(ii) provides that ASIC could separately determine, via a legislative instrument, the requirements for a consent form for fee arrangements other than an ongoing fee arrangement. We would argue that there should only need to be one set of requirements for consent forms. Duplication of the requirements will only cause confusion and the risk of mistakes.
- Section 99FA sets out requirements for obtaining consent for fee arrangements other than ongoing fee arrangements (being one-off fees and fee arrangements for up to 12 months). Similar obligations do not apply with non-superannuation products, where the fee arrangement is 12 months or less. We question the inconsistency between the super and the non-super environments. Once again this will cause confusion and lead to mistakes.
- In terms of application, we do not agree with a different commencement date for pre-FoFA and post FoFA clients and would suggest that both of these groups of clients should commence no earlier than 1 July 2021. Given the direct relationship with recommendation 2.1, a two year transition period will better allow the new arrangements to be implemented and reduce any need to modify the current disclosure and renewal cycle.

Paragraphs 1.29 and 1.34 of the draft Explanatory Memorandum discuss obligations for the superannuation fund trustee(s) to be satisfied that a fee is permitted under an arrangement and determining whether the requirements of an ongoing fee arrangement are met. This seems impractical and unreasonable. The agreement is between the financial adviser and the client and the trustee is not a party to the agreement. How can they even set out to confirm that the agreed services have been provided? How will they know if an annual review has been provided and if the member has received an advice document? Financial advisers are a regulated group and superannuation fund

trustees should be able to rely upon the conduct of another regulated entity. It may be more sensible to have sample based audit processes, rather than to expect that each member will be subject to some impossible oversight process. Indeed, we ask why this is considered necessary?

We note that there is no specific obligation on trustees for record keeping. This is the subject of a comment in paragraph 1.48 in the draft Explanatory Memorandum document, which states that they would be expected to keep records. We find the difference between a failure by a financial adviser to comply with the record keeping obligations being an offence, yet there is no specific obligation for trustees to keep records and therefore no penalty provision. We would expect greater consistency. We have been repeatedly told that the focus of the Royal Commission was on large institutions, yet the most harsh legislative response, has been focussed upon individuals and small business. Why is this the case?

Recommendation
The AFA recommends that financial advisers should not be required to provide a copy of the consent form to superannuation trustees each year. In our view, every three or five years would be more reasonable
Commencement should be 1 July 2021 and transition arrangements for both pre-FoFA and post-FoFA client groups should be extended to two years.

Other Related Issues

In addition to the issues raised above, we would also like to make the following points:

- APRA is currently reviewing the guidance on the Sole Purpose Test, which is nearly 20 years old. We believe that it is important that this review results in greater clarity in terms of what fees can be paid from a superannuation account. We believe that this should include all forms of advice, that will maximise the retirement savings of clients, including advice on budgeting to enable members to commence a salary sacrifice contribution arrangement. We also suggest that the Sole Purpose Test should not prevent the release of money to pay for any type of advice fee for clients in pension accounts, given that they have already met a condition of release and can withdraw funds at any time. We trust that APRA will engage with financial advice associations as part of this review.
- We note that the name of the draft Bill is Financial Sector Reform (Hayne Royal Commission Response—Protecting Consumers (2020 Measures)) Bill 2020, however the name of the draft Explanatory Memorandum is FINANCIAL REGULATOR REFORM (NO. 2) BILL 2019. This alternate name is also repeated in the Glossary.

Recommendation
The AFA recommends that the Sole Purpose Test be reviewed and that, all forms of financial advice should be able to be paid from a pension account.

Concluding Remarks

The AFA opposes the ban on financial advice fees for MySuper accounts, arguing that these Australians need access to financial advice like any other Australian and this recommendation was based upon a flawed understanding of financial advice and the value of financial advice.

With respect to Recommendation 3.3, it appears to us that the expectations of trustees checking the provision of services that they are not a party to, and do not have visibility of, is an unreasonable and unrealistic expectation. We have set out above a number of issues with this proposal and have

suggested some options for improvement. With the other changes to the Annual Renewal regime, we do not believe that it should be necessary to provide the consent form to the trustee each year.

The AFA welcomes further consultation with Treasury, should it require clarification of anything in this submission. If required, please contact us on (02) 9267 4003.

Yours faithfully,

Philip Kewin
Chief Executive Officer
Association of Financial Advisers Ltd