

19 February 2014

General Manager
C/- Bede Fraser
Retail Investor Division
The Treasury
PARKES ACT 2600

Submission by email: futureofadvice@treasury.gov.au

Dear Mr Fraser,

Future of Financial Advice – FoFA Amendments

The FSC thanks the Government and The Treasury for the opportunity to provide comments on the proposed amendments to the Corporations Act (*Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014*) and Regulations (*Corporations Amendment (Streamlining of Future of Financial Advice) Regulation 2014*) with regards to the Future of Financial Advice.

The Financial Services Council represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, trustee companies and Public Trustees. The Council has over 130 members who are responsible for investing more than \$1.9 trillion on behalf of 11 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world. The Financial Services Council promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

Principles of FoFA

The FSC, consistent with the government and regulator, is strongly of the view that financial advice is beneficial and indeed provides value for Australians who access advice. The FSC contents that accessible and affordable financial advice is therefore critical for Australians who seek advice and that this policy objective can be achieved whilst retaining the higher standards of consumer protection the Future of Financial Advice reforms sought to embed. To this end we support and commend the measures proposed by the government to deliver on this policy objective.

The FSC is happy to assist and discussing the contents of this submission and any drafting concerns Treasury may have with you. If you have any questions regarding the FSC's submission, please do not hesitate to contact me on (02) 9299 3022.

Yours sincerely



CECILIA STORNILO
SENIOR POLICY MANAGER



FSC SUBMISSION

CORPORATIONS AMENDMENT

(Streamlining of Future of Financial Advice) BILL 2014 and

CORPORATIONS AMENDMENT

(Streamlining of Future of Financial Advice) REGULTION2014

FEBRUARY 2014

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EXECUTIVE SUMMARY

The Financial Services Council (“FSC”) welcomes the opportunity to provide comment on proposed amendments to the Corporations Act (*Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014*) and related Regulations (*Corporations Amendment (Streamlining of Future of Financial Advice) Regulation 2014*).

The FSC has strongly supported the intent underpinning the Future of Financial Advice reforms which includes improving the quality of financial advice, bolstering trust and confidence in the financial advice industry - ultimately aimed at encouraging more Australians to access more advice.

The FSC also strongly believes in the value that quality financial advice delivers to all Australians who receive it as well as to the Australian economy. KPMG Econtech research commissioned by the FSC showed individuals with a financial adviser saved an additional \$1,590 each year (after the cost of the initial advice) when compared to a similar individual without a financial adviser. These savings equated to an additional \$91,000 upon retirement for a 30 year old Australian.¹ The KPMG Econtech research also found that if an additional five per cent of Australians received financial advice, national savings would increase by \$4.2 billion (or 0.3 per cent of GDP) by 2016-17.

Research by Queensland University of Technology shows that advice provided by licensed financial planners improves lifestyles not just financially, but also provides peace of mind and a greater sense of wellbeing.²

Given the significant value advice delivers, the FSC strongly supported the objective of promoting greater access to financial advice by removing legislative hurdles for example to enable a scalable advice framework that results in financial advice that is more accessible and more affordable for more Australians. However, to achieve a scalable advice framework which affords Australians the same protections, the enacted legislation needed amendment to allow a consumer of advice and their financial adviser the legislative ability and certainty to agree on what advice the client is seeking and ensure that all advice providers operate within the same legislative framework. The FSC welcomes the proposed amendments to bestow this right on consumers without curtailing the protection the Best Interest Duty in its current drafting offers consumers.

We anticipate the Future of Financial Advice reforms would transform the landscape not only for the financial advice industry but also change the way the entire Australian financial services sector would operate once legislated. The FSC believes that the four key measures³ contained in the

¹ KPMG Econtech, Value Proposition of Financial Advisory Networks Update and Extension, 2011

² Irving, K., Gallery, G., Gallery, N., Newton, C., (2011). I can’t get no satisfaction ... or can I? An exploratory study of satisfaction with financial planning and effects on client well-being, *JASSA The Finsia Journal of Applied Finance Issue 2*, p.36-44.

³ The four key measures include enhanced ASIC powers, ban of conflicted remuneration, statutory best interest duty and fee disclosure to the consumer (fee disclosure statement plus Opt-in).

Corporations Act legislated by the former government has had significant impact right across the financial services value chain, including restructure of entities and business models to ensure that the future advice businesses deliver quality best interest advice to their clients.

The FSC notes that the Future of Financial Advice legislation was and will continue to be comprehensive, complex and inter-related and are therefore are package of reforms rather than discrete individual measures and amendments in and of themselves do not water down consumer protections mechanisms built into the legislation. Critically the reforms impact almost all licensees operating a financial service in Australia. Given the complexity and scale of the reforms and the relatively short timeframe (between legislation passing and the commencement date), we submitted in the past of likelihood of unintended consequences. Many unintended consequences and practical complexities (that of operationalising policy) are now evident. It is for this reason that we welcome the proposed amendments as they eliminate and address many of the regulatory ambiguity which will result in lower costs in the provision of advice services thereby enabling advice to be accessible and affordable for those who seek advice whilst retaining the consumer protection mechanisms built into the reforms.

This paper provides comments on the draft Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014 and Corporations Amendment (Streamlining of Future of Financial Advice) Regulation 2014 – highlighting which proposed amendments are supported without amendments, which require amendments and making a number of recommendations – consistent with previously submissions where amendments remain outstanding to enable an effective, efficient Future of Financial Advice provisions for the benefit of Australians.

CHAPTER 1: BEST INTEREST DUTY

The FSC supports the foundation measure of the Best Interest Duty in which all financial advisers have a statutory legal obligation to place their client's interests first and above their own. The FSC has contended that comments that the Best Interest Duty as legislated remained undefined and afforded advisers no reasonable steps defence and prevented advisers from being able to scale advice.

The duty is supplemented by s961B(2) which sets out a series of steps – essentially a process, which the FSC has largely welcomed except for the duties inability to provide scaled advice and s961B(2)(g) which leaves the steps open-ended thereby creating ambiguity about other reasonable conduct/steps a provider must take in order to comply with the duty.

Its important to note that the Best Interest Duty is not a singular duty. Whilst the steps in s961B(2) are largely congruent with, they are **additional** to the duty an adviser owes their client under general law fiduciary obligations (profit and conflict rules) and under contract law (and torts). As such advisers will operate under a number of, each slightly nuanced, disparate legal 'best interest' obligations which adds to the complexity and cost of the regime.

The duty as legislated requires and advice provider to:

- Act in the best interest of the client (s961B(1));
- Comply with 6 broad principles based steps conduct requirements (s961B(2));
- Take an additional ("catch all") conduct step which would reasonably be regarded as in the client's best interest as determined by one of reasonable level of expertise and exercising due care (s961(2)(g));
- give appropriate advice (s961G), including continuing to comply with "know your client" and "know your product";
- warn the client if the advice is incomplete or based on inaccurate information (s961H); and
- prioritise the interests of the client where the provider knows or reasonable ought to know before the interests of the:
 - advice provider;
 - licensee or authorised representative; or
 - associate of the provider; or
 - associate of the authorised representative or licensee.

The combination of all the measures noted as making up the Best Interest and related duties provide significant bolstering to consumer protection mechanisms in the law. We note that the proposed amendments by the government only amend two of the steps in s961B(2) and do not repeal or amend any of the other significant consumer protection mechanisms built into the new legislative framework (including the duty of priority, which meets the only adviser obligation recommendation of the PJC inquiry).

Further to the ambiguity noted above, we have previously submitted that the term “best interests” appears in other legislative contexts e.g. section 52(2)(b) of the SIS Act and Section 181 of the Corporations Act there remains the potential for some degree of confusion or for incorrect assumptions to be made regarding its meaning in this context. Alternatively, the courts may interpret the duty based on the outcomes of the advice process that is as a “best advice” obligation, which is not only an impossible and unreasonable test for an adviser to defend but also contrary to the previous government’s stated policy that:

“the focus of the duty should be on how a person has acted in providing advice rather than the outcome of that action”.⁴

1.1 Catch-all

An advice provider will have significant practical challenges in positively proving, as required by the provisions, that the provider “based all judgements in advising the client on the client’s relevant circumstances” (s961B(2)(f)) – particularly where scaled advice is provided online or in an automated way as legislated in 2012. It would also be practically challenging for the provider to positively prove that the provider had “taken any other steps that would reasonably be regarded as being in the best interests of the client” (s961B(2)(g)). As these two obligations are non-exhaustive and involve interpretative professional judgements which reasonable minds may differ in their interpretation.⁵

Given the ambiguity and complexities noted, the FSC welcomes the repeal of s961B(2)(g) and the note to s961B(2).

The FSC Supports the repeal of s961B(2)(g) and the note to s961B(2).

1.2 Scaled Advice

The FSC has welcomes the Government’s intention to provide greater access to affordable advice for more Australians by amending the Best Interest Duty to enable the subject matter of the advice to be agreed between the client and the adviser.

Given the significant value advice delivers, the FSC strongly supports a scalable advice framework that results in financial advice that is more accessible and more affordable for more Australians. However, to achieve this, a fundamental principle of the scalable advice framework must be regulatory certainty and clarity for both licensees and financial advice providers. The financial advice industry must be able to have confidence in the regulatory framework. Providers of advice and their clients should be able to limit the scope of the advice service to be provided by agreement. This

⁴ Future of Financial Advice Information Pack 28 April 2011, page 12.

⁵ See Appendix 2 to the Financial Services Council Submission to the SEC January 2012.

clarity will enable clients to better select the advice level they desire and to better manage the cost which they will pay for advice.

An ability to legally limit the scope of an adviser's investigations, without limiting nor contracting out their legal 'best interest' duty to their client, will ensure that more Australians are able to access advice. That is, the ability to access more affordable piece by piece advice from a financial adviser legally able to provide it.

Contrary to comments in the media and to the situational example Treasury tested with the FSC, the ability to scope the advice does not mean that an adviser will not have a conversation with the client to seek to understand what advice the client is seeking. The conversation to arrive at a 'meeting of the minds' is critical. Whilst an important step that occurs in every client/service provider engagement, the conversation has varying degrees depending on the scope of the service offered and whether the service is provided by an individual or online. That is this meeting of the minds conversation should not be required to be a 'full fact find' as step 1 of the duty as is currently legislated. s961B(2)(b)(i) remains unchanged and requires the adviser to identify what advice the client is seeking whether implicitly or explicitly, which is achieved by having the qualifying conversation with the client. It is our view that the best interest duty consumer protection mechanism remains intact and does not lead to a contracting out of the duty. There is further opportunity to confirm in the Explanatory Memorandum that the step to identify the subject matter in s961B(2)(b) builds in the qualifying conversation to enable the client and the adviser to discuss and agree on what advice will be provided.

Amendments to Subsection 961B(2)(ba)

Once the client and the adviser have had an initial conversation to identify what advice the client is seeking (sought) as provided by step 1 of the safe harbour s961B(2)(b), the FSC submits that the client and the adviser are then able to agree what advice the client is actually seeking and agree on the exact scope of the service. A contract for the provision of advice is created at that point and the client moves from "seeking" advice on a topic to engaging advice on a topic/subject matter. On this basis, we recommend that s961B(2)(ba) should be amended to only apply to the extent relevant to the advice sought or, where the subject matter is agreed, the agreed subject matter by adding in s961B(2)(ba) after "client" the following: "relevant to the advice sought by the client".

Amendments to Subsection 961B(4A)

The ability to scale applies equally to the Best Interest Duty stipulated in s961B(1) and to the safe harbour steps in s961B(2). It is critical that s961B(4A) be amended after 'subsection' with the addition of "(1) or " so that the ability to scale is not limited to those whose advice model operates under s961B(1) and not the safe harbour provisions.

To enable the advice to be agreed between the client and the adviser the new “Client seeks scaled advice” subsection needs to be clear that the Duty s961B(1) and the safe harbour steps s961B(2) applies to the agreed scope where it is agreed. On this basis we recommend that s961B(4A) be amended:

- After “prevents a client” with the addition “and the provider”; and
- after ‘provider’ with the addition “and references to advice sought by the client shall mean the subject matter where so agreed”.

The FSC Supports

The proposed amendments contained in the Bill to the Best Interest Duty namely:

- Item 10 which repeals s961B(2)(a);
- Item 11 after s961B(2)(b) the addition of a new s961B(2)(ba). However we recommend the new subsection read as follows

“(ba) identified the objectives, financial situation and needs of the client that are relevant to the advice sought ~~disclosed to the provider~~ by the client.”

- Item 12 the amendments to s961B(2)(f);
- Item 13 the removal of s961B(2)(g);
- Item 14 repealing the note in sub section 961B(2);
- Item 17 repeal of s961E and
- The addition of item 16 after subsection 961B(4). However we recommend this section be redrafted as follows

“Client seeks scaled advice

(4A) To avoid doubt, nothing in subsection (1) or (2) prevents a client and provider from agreeing the subject matter of the advice sought by the client with the provider and references to advice sought by the client shall mean the subject matter where so agreed.”

CHAPTER 2: PERMISSIBLE AND EXEMPTED BENEFITS/REMUNERATION

2.1 General advice exemption

The FSC supports the amendments proposed in the Draft Bill at items 24 and 25.

The FSC recommends the amendment of the reference to “financial product advice” to “personal advice” in section 963A so as not to cause ambiguity in interpretation as a result of the proposed amendment.

2.2 Client directed payments

The FSC supports the express exemption of a fee for service being payable from a client’s financial products on the clients consent.

FoFA explicitly aims to carve out “fee for service” from the definition of conflicted monetary remuneration (section 963B(d)). A fee for service arrangement is one where a client pays the advice directly for the service provided. The consumer retains the right to choose not only how much they are willing to pay for the advice service they want but also from where that monies comes from to pay for that service. That is, if a consumer wishes to pay an adviser from their bank account, with a credit card, via a payment plan or via monies in their Managed Investment Scheme or Superannuation account, a client should retain this right of direction. We submit that the law enabled a consumer to expressly consent where their fee for service payment is to be funded and paid to an adviser. However, there has been some conjecture by the regulator to the ability for a client to pay for the fee for service from their financial product such as their super or managed investment account. As such we have sought for the law to expressly state that a fee for service (section 963B(d)) can be expressly paid from a financial product on the clients direction. We submit that the note at the end of s963A proposed by the Draft Bill at item 26 is better than the current law. The proposed “note” needs to be amended to expressly state that “giving a benefit” includes a benefit paid by way of a deduction from a financial product to solve for this legal ambiguity.

Further, we also submit that the following sentences be deleted from the draft Explanatory Memorandum as it causes legal ambiguity given that consent can mean authorised (depending on the relevant facts of the particular situation):

- From paragraph 3.15: Last sentence, delete “and with the client’s clear consent”.
- From paragraph 3.3.56: Second last and last sentence, delete “with the client’s clear consent. However, the mere fact that a client consents to a benefit to be paid, does not mean that the benefit is caused to be authorised by the client.”

We acknowledge and do not support that a client has provided consent merely by signing a financial product application form. However, this mischief can be highlighted by way of illustration in the Explanatory Memorandum.

The FSC supports:

- **The addition of a proposed note after s963A with amendment.**

The proposed “note” needs to be amended to expressly state that “giving a benefit” includes a benefit paid by way of a deduction from a financial product to solve for this legal ambiguity

The FSC recommends the following amendments to the draft Explanatory Memorandum:

- **From paragraph 3.15: Last sentence, delete “and with the client’s clear consent”;**
- **From paragraph 3.3.56: Second last and last sentence, delete “with the client’s clear consent. However, the mere fact that a client consents to a benefit to be paid, does not mean that the benefit is caused to be authorised by the client.”; and**
- **The draft Explanatory Memorandum add after paragraph 3.56 an example of a fee for service being consented to for a deduction from a financial product like a superannuation or managed investment scheme account. This can occur through a variety of means such as a separate authority, SoA and authority to proceed.**

2.3 Mixed Benefits

The FSC supports the Government’s proposed amendments to the Future of Financial Advice provisions to enable practical methods of complying with the reforms but still enable employees and representatives to earn salary and to be paid permissible, exempted and grandfathered payments.

The FSC supports the proposed amendments at item 27 of the draft Bill without amendment. Similarly with regards to item 33 of the draft Bill relating to section s963C.

The FSC supports the proposed amendments at item 28 and item 34 without amendment.

The FSC supports the proposed amendments at item 18 of the draft regulations without amendment.

In relation to item 17 of the draft regulations, the FSC is concerned with the draft regulation 7.7A.12I. Currently, the exemption allows components of **one benefit** to relate to different activities or services. However, the new exemption does not deal with different components of one benefit. It

only deals with **separate benefits** and whether or not they can be provided at the same time. We believe that as the exemptions deal with different issues, that the current regulation 7.7A.12I is still required.

For example, if a benefit relates to an exempted product, general advice, and where the whole bonus has an overarching compliance and behavior criteria, the new regulation 7.7A.12I will not assist as the bonus cannot be split up into separate parts.

In addition, the new “extent of” wording and the removal of the word “solely” in the draft legislation will not assist as it is not clear that the bonus can be said to relate to basic banking products or to only relate to basic banking products to a certain extent due to the combined nature of the bonus.

The draft regulations should be amended so that the current 7.7A.12I is not repealed, but the proposed 7.7A.12I should be inserted instead after regulation 7.7A.12I as a new regulation 7.7A.12IA.

We also note that the current regulation 7.7A.12I does not work as intended because if a relevant provision restricts its operation in any one way (e.g. as contemplated under (2)(a)), 7.7A.12I(1) cannot be relied on at all (e.g. to permit the provider to also provide other services at the same time even if the relevant provision does not expressly restrict this).

For example, the bonus referred to above will not satisfy proposed new section 963D and will not be exempt. This is because of the restriction in 963D that advice not be provided at the same time on other financial products. Because of this restriction, 7.7A.12I(2) says that 7.7A.12I(1) cannot be relied on at all and so the whole benefit will not be exempt.

So 7.7A.12I(2) can stop the operation of (1) entirely if there is a restriction in the particular regulation. In practice, this means, for example, that , if there is a mixed advice restriction in the relevant provision, 7.7A.12I(1) cannot be used to pay a bonus that relates to other matters even though those other matters are exempt.

The FSC supports the insertion of the new regulation 7.7A.12I but believes that the current regulation 7.7A.12I is still required and should not be repealed. The current regulation should continue in tandem with the new regulation.

Additionally, 7.7A.12I needs to be made clearer so that (2) does not stop the operation of (1).

Section 963D needs been added in as a prescribed provision (we assume this was intended, and

2.4 Insurance

The FSC interprets the Government's PJC dissenting report and 20 December 2013⁶ policy to mean that the Government's policy intent is to allow commissions for life risk insurance (regardless of the insurance policy offered by the superannuation trustee – that is be it an individual life risk policy or group policy) inside super (outside super is currently permitted) providing that personal advice is provided to the client.

While the addition of personal advice to the 'conflicted remuneration' definition makes it clear that conflicted remuneration is proposed to only apply to circumstances where personal advice is provided, it also makes item 29 of the proposed draft Bill (section 963B(1)(b)) unworkable.

The combined effect of the item 29 and 31 of the proposed amendments to the Bill means that commission is only banned on life risk insurance provided for MySuper members in circumstances where personal advice has been provided. This is clearly not the intention of the Government.

The FSC notes that drafting to achieve the Government's policy intent is complex and given the time we have had to consult on the proposed amendments we have been unable to draft options for the government to consider to achieve its objective. We would be happy to work with the government on drafting that enables the policy to be practically implemented. We also highlights that drafting that may impact MySuper may need to consider the MySuper Acts and SIS to ensure there is no regulatory gaps.

The FSC supports the Government's policy intent but does not support the drafting proposed at items 29 and 31 of the Exposure Bill on the basis that the drafting does not achieve the statement government policy.

2.5 Execution only exemption

The FSC supports an amendment to the execution only exemption contained in s963B(1)(c) because the drafting does not cover all dealing activities and does not require a causal link between the advice provided and what the client may choose to execute. We have noted previously that this provision is complex if not administratively impossible to ensure compliance.

Whilst we welcome the draft as proposed at item 32 of the proposed Bill, we note that the drafting requires amendment to extend it to all dealing activities (not just issue or sale) and to require a link between the advice and execution of the advice.

⁶ Life insurance inside super: The ban on conflicted remuneration will only apply to commissions on risk (life) insurance products inside superannuation in circumstances where no personal financial advice about these products has been provided i.e. where automatic coverage is provided inside a default (MySuper) superannuation fund.

The FSC supports proposed amendments to the draft Bill at item 30 without amendment.

The FSC supports proposed amendments to the draft Bill at item 32 with amendment. The provisions must extend to cover all dealing services (not just issue or sale) and must provide a link between THE advice provided and THE execution undertaken in the 12 month period to qualify for the exemption (i.e. the execution must be as contemplated or recommended in the advice).

The FSC also recommends that regulations 7.7A.12E remain as currently enacted without amendment.

2.6 Training exemptions

This amendment seeks to enable advice providers to receive appropriate training on the breadth of running a financial services business and not just be limited to financial product advice. This is a welcome amendment.

The FSC supports the amendments proposed in the Draft Bill at item 35 without further amendment.

2.7 Benefits for employees of an ADI

The FSC supports the amendments proposed in the Draft Bill at item 36.

The FSC supports comments noted in the ABA's submission on amendments required to this section to ensure the law practically enables (as intended) different corporate structures and staffing arrangements without inadvertently restricting the operations of these provisions.

We draw attention to 963D(c)(iii) and note that "consumer creditor insurance" should read "consumer credit insurance".

2.8 Balanced scorecard remuneration arrangements

The FSC welcomes the amendment to allow the payment of a "low" benefit defined as a conflicted benefit using a balanced scorecard approach as we believe it reflects the intention of the legislation to allow payments that will not "influence" advice but provides industry with a degree of certainty in the absence of any materiality requirement on the influence test.

The FSC recommends it 16 of the proposed regulation (7.7A12EB) requires the following amendments:

- The reference to “financial product” in (e) should be changed to “financial products”.
- Sub-regulation (1)(a) excludes particular parts of the benefit where that part of the benefit is already exempted under another provision of the Act. The drafting suggests that the benefit must not relate to a particular “financial product” as listed, however the sub-regulations (i) to (v) relate to exemptions and not financial products. The drafting in (a) should therefore be amended to clarify that a benefit must not be exempt under one of the exemptions listed in (i) to (v). We believe that this is the intention (i.e. that the regulation only applies to benefits that are not otherwise exempt).
- Sub-regulation (2)(f) refers to the requirement to “encourage the giving of personal advice that is in the client’s best interest”. The intention appears to be consistent with the other requirements of FoFA and we are supportive of including a compliance requirement in the provision to reflect the balanced scorecard concept. However, we are concerned that the test to “encourage the giving of personal advice that is in the client’s best interest” will be different from actually complying with the best interest requirement. This adds another layer of uncertainty in relation to this exemption, that is, what does a client’s best interest mean in this context? Does this best interest differ to the duty required by s961B? What does “encourage” require above and beyond having robust compliance arrangements in place? We submit that the provision needs to be amended to link it back with the test in s961B. For example, the wording in (f) could be amended to require that the benefit be given in circumstances that are likely to further the giving of personal advice that complies with section 961B.
- We recommend the provision be redrafted to enable a benefit, in whole or part, which is not conflicted remuneration and does not become conflicted remuneration only because it is given with another benefit.
- The current draft only allows this exemption for employees. We believe that this exemption should also apply in relation to representatives of AFS licensees. To this effect we are also support the ABA’s submission with regards to defining employees.
- We query the need to state a % in the draft Explanatory Statement (ES) noting that proving ‘low’ is evidentiary on the facts and ASIC has developed a pragmatic Regulatory Guide providing a number of factors a provider must consider to comply with ‘low’. To the extent that the reference to a % remains in the ES the words should be changed to “no more than 10%” rather than ‘less than 10%’.

We note the following example to illustrate that low does work and that a set % does not need to be referenced in the ES.

Example:

Employee's salary is \$50,000.

Employee's total performance bonus is \$1,000. The amount of remuneration in the performance bonus that would otherwise be considered conflicted remuneration, apart from the performance bonus exemption, is \$100.

The "low" test is calculated by $\$100/\$51,000 = 0.20\%$

Which means the "low" test is satisfied because the remuneration that would otherwise be conflicted (the \$100) is less than 10% of the employees total remuneration. The remuneration must still meet the other requirements of the provision, and ASCI's regulatory guidance.

2.9 Permissible Payment and grandfathering

The FSC welcomes the proposal in draft Regulation 7.7A.12HA that benefits that are not conflicted and calculated by reference to exempt benefits are also exempt. With regards to exempted benefits, we strongly support the notion that a benefit once exempt should remain exempt and should not need to be retested when being passed on to representatives.

The FSC recommends that the drafting permits the passing through of permissible and exempted benefits. We note that the draft should be amended to add a third option (c) to say "combination of (a) and (b)".

We query whether this provision needs to consider adding an extra option for the avoidance of doubt grandfathered benefits should also be able to be passed through.

Further, we note that the heading to this Regulation states that it applies to grandfathered benefits. However, the FSC is concerned that Regulation 7.7A.16F may prevent Regulation 7.7A.12HA applying to grandfathered benefits. Regulation 7.7A.16F appears to operate as a restriction on the circumstances in which grandfathered benefits can be passed on to advisers – not only does it state that no more than 100% of the benefit can be passed on Regulation 7.7A.16F(b) also states that benefits can only be passed on if give under an arrangement entered into before 1 July 2013. Unless this paragraph is removed from 7.7A.16F, there will at best be uncertainty whether Regulation 7.7A.12HA can operate in relation to grandfathered benefits irrespective of the reference to them in its heading. The amendments in Item 23 of the draft Regulations only mean that grandfathered benefits can be passed on to representatives where they move from being an employed to an

authorised representative of the same licensee or where authorised representatives move between licensees. It will not allow passing on of grandfathered benefits generally.

The FSC recommends that consideration be given to ensure that permissible, exempted and grandfathered payments are able to be passed on.

CHAPTER 3: GRANDFATHERING

3.1 Grandfathering adviser's book of business on movement from one licensee to another

The FSC welcomes the proposal to amend Regulation 7.7A.16F to permit movements of authorised representatives between licensees and to permit employed representatives to become authorised representatives and to permit grandfathering to extend to purchasers of businesses under draft Regulations 7.7A.16A(5A) and 7.7A.16B(4A).

However, these changes do not address all of the concerns relating to restrictions on adviser movements. In particular, the change to permit authorised representatives to move between licensees will not in fact allow authorised representatives to take grandfathered remuneration with them when they move licensees where the remuneration is received by their current licensee and passed on by the licensee to the representative. In this most common scenario, the Regulations will not permit the new licensee to receive the grandfathered remuneration from the relevant product issuers where the new licensee does not have an existing pre FOFA arrangement with those product issuers for payment of remuneration in relation to the relevant products.

The FSC submits that there needs to be an explicit exemption given to permit grandfathered remuneration to be paid to an adviser's new licensee where the adviser ceases to represent a licensee to whom grandfathered remuneration was being paid in respect of the products held by the adviser's clients. It is important that the exemption applies to any new licensee – in other words, the exemption should not be limited to the first time an adviser moves between licensees after 1 July 2013 but should permit the adviser to change licensees whenever they desire (subject to the terms of their agreement with the licensee) to avoid advisers becoming locked into a licensee relationship with all the problems that gives rise to. One way to achieve this outcome is to allow licensees to enter into agreements with product issuers to allow payment of remuneration on products issued prior to 1 July 2013 where those products were already commission paying i.e. the rights to that remuneration simply ceases to the 'outgoing' licensee in respect of those products and is taken on by the 'incoming' licensee in respect of those products

The FSC also believes that the extension of grandfathering to purchasers of businesses needs to reflect the fact that businesses are not always transferred in one transaction. The changes to Regulations 7.7A.16A and 16B should expressly recognise that the sale can relate to only part of the business. This may apply where an adviser sells part of their book, eg as part of a succession plan or sells their business to more than one purchaser.

The FSC recommends that the draft regulation at item 23 requires amendment to be an explicit exemption given to permit grandfathered remuneration to be paid to an adviser's new licensee where the adviser ceases to represent a licensee to whom grandfathered remuneration was being paid in respect of the adviser. It is important that the exemption applies to any new licensee.

3.2 Grandfathering arrangement for the ban on conflicted remuneration

Item 19 inserts a new (5A) after sub regulation 7.7A.16A(5) regarding a person who purchases a business having the same rights as the seller would have had. As regulation 7.7A.16A constrains the grandfathering that would otherwise be available under regulation 7.7A.16. The FSC submits that it is essential that a sub regulation like (5A) be added to 7.7A.16, in addition to 7.7A.16A to ensure consistent treat to ensure market neutrality is achieved as intended.

FSC recommends that a sub regulation like (5A) be added to 7.7A.16, in addition to 7.7A.16A

Also regarding item 19, the explanatory statement states that the new sub regulation clarifies that when a business is sold **and that business is acting in the capacity of a platform operator** the rights to the grandfathered benefits are transferred. However, the restriction in bold is not found in the regulations.

The FSC recommends that suggest deleting that portion of the explanatory statement (bolded above) so that the provision can operate where the business that is sold is the platform operator or the other party to the arrangement.

Further the FSC recommends that the Explanatory Statement and both redrafted regulation(s) should refer to the “purchase” of all or part of a business

We note that the intent of item 20 of the proposed Regulations is to give the same effect of item 19 to those businesses which are not acting in the capacity of a platform operator. We note that reference to the same rights “under this regulation” in item 20 needs consideration as non platform operators need to be referenced through 1528 (1) of the Act and regulations not just regulations as Platform operators and submit that this part of the draft regulation should be deleted.

The FSC recommends “under this regulation” should be deleted from item 20 of the draft regulations.

Item 21 of the draft Regulations provides grandfathering of certain superannuation to pension switches. We agree with the substance of item 21 but request a small amendment to also cover the steps leading up to the receipt of the pension, namely the election itself.

The FSC recommends an amendment to 7.7A.16B(5)(b) and the 2nd last line in the new regulation 7.7A.16B(5A) as follows “....do not treat the election or the receipt of the interest”

3.3 Changes to conflicted remuneration: further grandfathering required for employees

Current Regulation 7.7A.16C set an application date for benefits to employees of 1 July 2014 if not under an enterprise agreement, or where the benefits are given under an enterprise agreement, on a date related to expiry of the enterprise agreement. For some organisations, the relevant date will be 1 April 2014. This extension from 1 July 2013 was welcomed both by institutions that face the task of redesigning and renegotiating enterprise agreements, and by licensees of self-employed authorised representatives, who need to give practical guidance and training to hundreds of individual adviser business on exactly what changes these businesses may need to make to existing individual employment arrangements. The extent and cost of both of these exercises is significant. The government has announced its intention to amend a number of provisions relevant to employee benefits. The final form of the regulations will not be known before late March at the earliest, when they are made (assuming they are not set aside).

The FSC recommends, given the uncertainty faced by industry, that it would be practical and efficient to extend the dates set under Regulation 7.7A.16C by a further 6 - 12 months to make it possible for employers to renegotiate their remuneration arrangements with employees once, after the law is settled, rather than to subject all parties to a second round of negotiations and amendments (once to comply with existing law and a second to comply with the amendments).

3.4 Changes to grandfathered arrangements

The FSC welcomed regulations in June 2013, which recognised that changes to an arrangement did not necessarily void grandfathering.

However, the FSC believes that there needs to be some adjustment to the grandfathering provisions to permit changes to be made to the arrangement without loss of grandfathering. Even in the few months since FOFA commencement considerable difficulties have begun to be experienced by licensees in relation to existing arrangements. The legislation states that remuneration is grandfathered when paid under an arrangement entered into before 1 July 2013. However, there is considerable uncertainty about the extent to which changes can be made to such arrangements without loss of grandfathering. ASIC has indicated that changes can be made provided they are not material changes. However, while this position is welcome it is not expressly reflected in the language of the statute.

To avoid uncertainty and the additional cost and impediments on adjusting terms of arrangements with representatives, there needs to be an express recognition of the ability to amend arrangements without losing grandfathering and the circumstances in which that should (and should not) be permitted. We believe that a Regulation should be introduced to expressly permit the following changes to arrangements:

We believe that a Regulation should be introduced to expressly permit the following changes to arrangements:

- **Changes which do not affect the remuneration paid to representatives, agents and employees; or**
- **Changes which do not have any material change to the remuneration paid to representatives, agents and employees; or**
- **Where a representatives, agents and employees has an entitlement to grandfathered benefits under an arrangement, the arrangement can be updated, amended or varied and the rights to the grandfathered revenue is not lost, as long as the entitlement to grandfathered revenue does not exceed 100% of the existing entitlement; or**
- **Changes which are intended to reflect a change in a role (job description) of representatives, agents and employee;**
- **Any combination of the above changes.**

CHAPTER 4: OTHER AMENDMENTS

4.1 Fee Disclosure Statements

4.1.1 Prospective Fee Disclosure Statement obligations

Paragraph 2.6 of the draft Explanatory Memorandum confirms the government's intent to amend the FoFA provisions to make the Fee Disclosure Statement prospective, which is required to be issued to an advice client who enters into an ongoing fee arrangement with an adviser from 1 July 2013. The FSC submits that the repeal of the requirement to provide an Fee Disclosure Statements to existing clients should take effect retrospectively to the date of the announcement. However, we note that the Draft Bill and Regulations do not give effect to the policy announcement. Therefore s1513D should be amended to reflect this. Advisers and licensees should be given certainty that no penalty or liability can arise where they were not able to comply with the Fee Disclosure Statement requirements for existing clients, including where they have been relying on the Government's promise to remove this requirement.

The FSC supports the amendment to amend the Fee Disclosure Statement obligations so the obligation is prospective for ongoing fee arrangements entered into from 1 July 2013.
The FSC submits that the Draft amendments as currently drafted to not achieve this policy intent.

4.1.2 Amending the 30 day requirements to 60 days

Paragraph 2.21 of the draft Explanatory Memorandum confirms that sections 962G(1) and 962H(1)(bi) require statement to be provided before the end of 30 days beginning on the 12 month anniversary of the date the arrangement was entered into or before the end of 30 days beginning on the 12 month anniversary of the day immediately after the final day of the year for which disclosure is provided. We have previously contended that 30 days is an administratively challenging period in which an adviser can achieve this obligation and in fact these specific obligations were tabled in Parliament on the day the FoFA Bills were passed so the industry had limited capacity to comment on the administrative complexity these timeframes create. We reiterate that the current timing requirements for Fee Disclosure Statements (FDSs) are too restrictive. The FDS timing issue was not included in the Government's announced changes, and remains a significant "red tape" issue that must be addressed.

The current drafting of s962G and s962H provides that:

- FDSs must be issued within 30 days of the anniversary date (s962G); and
- the information required in the FDS must relate to the period of 12 months that ends on a day that is no more than 30 days before that on which the statement is given (s962H).

The currently legislated FDS period is too restrictive because if the FDS lodgement is late for any reason (for example, illness) – then the FDS must be re-created using a different 12 month period.

The ability to issue a FDS to a client within 30 days is very difficult. The problem lies in the delay in the flow of information. To start, many product providers only have the capability to send the information to licensees once a month. Then a delay can occur between the product provider sending the FDS information, and the licensee receiving the information. Finally, a further delay can occur before the individual adviser receives the information as it needs to be loaded into the licensee's particular software and modified as necessary.

An additional complexity occurs when an adviser or practice changes licensees. Issuing the FDS to the client within 30 days is extremely difficult when an adviser changes licensees due to all the work required to transfer client data at the product provider level and to then load the client data onto the new licensee's FDS software.

More flexibility is needed in relation to the timing requirement for issuing an FDS. Failure to provide more flexibility will result in multiple and frequent breaches of the timing requirements, each requiring a breach report to ASIC. In addition, costly rework will be required each time a breach occurs because the FDS must be re-created for the new 12 month period.

The FSC recommends that sections 962G(1) and 962H(1)(bi) be amended to read 60 days and not 30 days.

4.2 Opt-In

The FSC supports the Government's proposed amendments to repeal items 20-23 of the draft Bill.

4.3 Intra Fund Advice

A key element of the former government's FoFA announcements made in April 2010, was the consideration of the provision of "low cost simple advice (known as Intra-Fund Advice)".

The former government's commitment to low cost simple advice was warmly welcomed by the industry. The ability to provide simple advice (at a lower cost) would deliver significant benefits for Australian consumers namely in the form of increasing accessibility and affordability of advice.

Importantly, access to affordable and scaled or piece by piece advice⁷ is increasingly preferred by Australians over more complex/holistic advice, which is legally required to be provided in the Best Interest of the client.

Critically, the FSC has always advocated for a product and channel neutral approach to scaled advice. That is, scaled advice which should not be limited to superannuation (as Intra Fund Advice has been). Additionally, scaled advice was always expected to be subject to FoFA requirements – namely the best interest duty.

As a result, the FSC has previously submitted on numerous occasions to Treasury that the concept of Intra-Fund Advice – which includes general and personal financial advice provided by a superannuation product provider (the Trustee or by a third party advice provider engaged by the Trustee to provide the advice) – should be extended beyond superannuation so that Australians that invest in savings, managed investments and insurance products can also be afforded this low cost type of advice and providing a market neutral framework. OR Intra Fund Advice be narrowed to only the provision of general advice collectively charged by the Trustee regardless of who accesses the service.

The previous government announced on 8 December 2011⁸ what Intra Fund Advice includes. Then the former government legislated in mid 2013 how Intra Fund Advice could be charged to members collectively by way of an administration fee. The legislation permits superannuation funds to offer Intra-Fund Advice⁹ which will be able to provide ***any general and personal advice limited to the member's beneficial interest in the superannuation fund (the sole purpose test)*** and:

“there will be new restrictions on the types of advice that can be provided under intra fund advice rules. Specifically, the following are excluded:

- Advice relating to whether the member should consolidate their existing superannuation accounts

⁷ ASIC report *Access to financial advice in Australia (REP224)*, December 2010 paragraphs 53 and 62.

⁸ Intra-Fund Advice is today only permitted to be offered by superannuation funds under a Class Order exemption [CO09/210]. Under a Class Order exemption [CO09/210], trustees of regulated superannuation funds are currently permitted to provide personal financial product advice in respect of various matters relating to the superannuation fund, and are exempted from section 945A of the Corporations Act in doing so. (Other licensed advisors are required to comply with section 945A). Hence, superannuation trustees relying on the Class Order can provide personal financial product advice without determining the client's relevant personal circumstances (“knowing your client” requirement), or considering and investigating the subject matter of the personal advice (“knowing your product” requirement). The superannuation trustee is also exempted by the Class Order from the section 945A requirement to provide appropriate advice. FoFA Best Interest Duty obligations replace s945A of the Corporations Act. Class Order 09/210 has not been repealed by ASIC at the time of writing this submission.

⁹ The MySuper legislation (not limited to MySuper) creates the ability for a superannuation fund to charge a superannuation member advice fees collectively without disclosure to the member.

- Advice to switch the member away from the superannuation fund into another superannuation fund except to the extent the advice relates to moving the member from an accumulation product into a retirement product offered by the same registrable superannuation entity
- Advice that contains recommendations in relation to financial products that the member holds outside of superannuation
- Advice in relation to investment choice outside of the trustee-prescribed investment options”

Given the previous government did not narrow Intra Fund Advice to general advice only or broaden it so that it was not limited to superannuation only, the FSC welcomes the Governments proposed amendments to the Best Interest Duty to expressly permit scalable advice and the carve out of general advice from the conflicted remuneration provisions as these two measures will enable a similar (albeit not identical) form of low cost advice to be delivered by providers of advice other a Trustee to their superannuation members.

With regards to Intra Fund Advice, we note that an advice provider can not receive benefits from the trustee nor can the trustee pay the advice provider for the advice services the adviser provides the trustee’s superannuation members as the benefit falls foul of the Conflicted Remuneration provisions of FoFA namely section 963A and s963B as currently legislated. Superannuation legislation enacted allows superannuation trustees to charge advice fees collectively (that is to all members regardless of whether you access the service or not) bundled with the administration cost of the fund. The advice service is permitted by superannuation law, to be provided by superannuation trustee or advice licensees to whom a superannuation trustee outsources the advice function. The exemption of general advice from conflicted remuneration will enable general Intra Fund Advice fees to be paid by a Trustee to an advice provider. However, a gap remains for the personal advice provided. The government’s proposal to define Intra Fund Advice is important, because it define what services an advice provider under an arrangement with a Trustee is able to provide and be paid pursuant to s99F of SIS Act. But as the payment of the benefit may be for personal Intra Fund Advice, then an amendment to section 963B is required to exempt personal advice Intra Fund Advice monetary benefits to flow from the superannuation trustee to the adviser.

As such, we supported the government’s proposal to define what intra-fund advice is as a precursor to exempting this type of advice benefit to be paid by a superannuation Trustee to a financial advice provider and for the advice provider to receive the benefits.

However the proposed amendments (item 9 of the draft Bill) does not define what Intra Fund Advice is and further, there is no exemption of Intra Fund Advice from the conflicted remuneration provisions at s963B.

Item 9 of the draft Bill is a “note” to the Act which is therefore not a defined term. The “note”:

- does not explicitly define what advice may be provided as Intra Fund Advice:
- states that Intra Fund advice is provided by a trustee of a superannuation fund when it can also be provided by a third party provider to whom a trustee of a superannuation fund has outsourced the function;
- references only that section 99F of the Superannuation Industry (Supervision) Act regulates which costs can not be collectively charged by passing costs onto another member but fails to note that s99F also regulates those costs which can be collectively charged to all members of a superannuation fund regardless of whether they access the service for the purposes of Intra Fund Advice.

The FSC supports the carve out of general advice from conflicted remuneration provisions.

The FSC supports the policy intent to define Intra Fund Advice.

The FSC recommends that the draft Bill be amended to

- **define Intra Fund Advice not by way of a note to the Corporations Act but as a definition for inclusion in section 960;**
- **That the definition state what advice can be provided by an advice provider aligned to advice that SIS will allow to be charged pursuant to section 99F;**
- **Expressly exempt Intra Fund Advice (defined term) from monetary benefits section 963B.**

4.4 Division 5 Volume Based Shelf Spaced Fees

The intent of this section as proposed by items 37-39 of the draft Bill is not to capture fees that represent annual or one-off dollar based fees (not related to “volume”) charged by the platform to the fund manager.¹⁰ However, the drafting of the proposed amendment to this provision does not appear limited to volume based payments, despite the heading to the section (which is unchanged). It therefore appears that the changes will also ban dollar based fees which the FSC does not believe has ever been the intention of the ban.

Subsection 964A(2) currently presumes all payments which are dependent on the total number or value of a fund manager’s financial product are “volume based shelf space fees”. However, this language is proposed to be removed from the ban and instead new tests relating to whether the payment will influence the total number of fund manager products included on a platform (although the language used in this limb is somewhat unclear in its application) or to give preferential treatment to the fund manager’s products.

The effect of this drafting is that genuine “dollar-based” shelf spaces fees charged by platforms are caught by the ban. The FSC submits that this has never been the intent of the ban. While we welcome the move to define the types of fees caught by the ban and to turn the circumstances in which it does not apply into proper exemptions, we believe that the concept of it needing to be volume based should be retained in the definition of “volume based shelf space fee”.

The FSC welcomes the proposal to expressly exemption life and general insurance products from the ban as was always the intention of the ban as they are not provided by 'fund managers'. However, we submit that this exemption should also be extended to banking products which are also not provided by fund managers and to platforms which only have wholesale clients.

The section inadvertently prohibits the payment of volume based shelf space fees in relation to platforms that are restricted to wholesale clients. The FOFA reforms are intended to only apply to retail clients and so custodial arrangements with only wholesale clients should be carved out from the prohibition.

¹⁰ The purpose of this payment is for the ongoing administration and management of the Fund Manager’s products on the platform. This can include costs the platform operator incurs for reporting, distribution processing, Anti Money Laundering / Counter Terrorism Financing compliance and other activities platform conduct for the direct benefit of the fund managers. It is usually a standard access fee charged per fund.

The FSC supports amendments to Division 5 of the FoFA provisions to enable clarity in the law regarding banned payments. We recommend that items 37-39 proposed in the draft Bill is broadly drafted and requires amended to ensure that the policy intent is legislated including

- The ban should only applies to retail clients – the remit of FoFA;
- The redrafted ban inadvertently ban payments the previous draft and policy permit for example, genuine “dollar-based” shelf spaces fees charged by platforms are caught by the ban.

4.5 Wholesale/retail client distinction

We note these amendments are required to enable certain wholesale clients (eg sophisticated investors with an accountants Certificate) to be recognised as wholesale client for the purposes of the Future of Financial Advice provisions.

The FSC supports amendments proposed in items 1-5 of the proposed regulations.

However, we note that the amendments to Regulations 7.6.02AB, 7.6.02AC, 7.6.02AD, 7.6.02AE and 7.6.02AF require reference to sub section 1368 in place of the draft reference to 1364.

4.6 Stamping Fee Exemptions

The FSC supports the amendments in items 6-9 of the proposed draft Regulations.

The FSC recommends that amendments are required to the proposed regulations 7.7A.12B(1) (b(ii) to ensure that the regulations make it clear that part of the benefit (rather than only the whole benefit) can be passed on from a licensee to a representative from the provider of the benefit.

The FSC support amendments in the AFMA’s submission with regards to stamping fee exemptions.

4.7 Buying and Selling of financial planning businesses or registers

Recommendation 10(ii) in the then Opposition’s dissenting report to the PJC provided:

(ii) That the proceeds of the sale of a financial planning business between a licensee and its authorised representatives should be specifically exempt from the ban on conflicted remuneration;

The exemption has not been provided. A different type of exemption had been provided but is not consistent with the Coalition commitment to effect the above recommendation. The current regulation refers to formulas for being able to value a financial services business and goes into values for in-house products versus external products. The Opposition policy was to allow for the **proceeds** of the sale of a business to be exempt, without qualification as to how it was calculated. Sales, in whole or part need to be catered for in the amendment.

A specific problem is forward sale agreements that were entered into long before FOFA, some even as long as 20 year ago with specific formulas for valuation that will apply at the eventual date of sale. Grandfathering of these arrangements will not apply because the forward sale agreement will include all products on the register as at the date of sale, even products that are issued after 30 June 2014, when grandfathering runs out.

To keep the current exemption means that a FOFA standard is being applied retrospectively to agreements entered into long before FOFA and applying after FOFA has begun. This also raises constitutional issues given that the contracts were in place and the guarantee of purchase on particular terms was given long before FOFA.

We therefore seek the Government fulfil its election promise to exempt the *proceeds* of the sale of a register or a business, in whole or part, from the ban on conflicted remuneration. The additional conditions i.e. paragraph(c) from regulation 7.7A.12EA should be removed, to be consistent with the election commitment and Recommendation 10(ii). The best interests duty will cater for product recommendations from 1 July 2013 so there is no need to put such a condition into the valuation of a business.

4.8 ASIC Powers

The FSC notes that the Future of Financial Advice provisions of the Corporations Act provide few if any relief powers for ASIC which is quite out of line with other sections of the Corporations Act (including those pertaining to financial services).

The FSC seeks additional relief powers for ASIC (and by regulation) to facilitate transition and address unintended adverse impacts. Relief powers permit ASIC to carry out its role most effectively and alleviate the need for ASIC to have to include no action positions in their regulatory guides, which do not provide sufficient comfort to industry participants as there is no legal protection against third party claims.

The FSC recommends that general exemption and modification powers be included in the FOFA provisions both by regulation and by ASIC relief as is the case with other equivalent parts of Chapter 7 of the Corporations Act.

4.9 Definition of Basic Banking Products

The FSC is supportive of the ABA's submission with regards to these amendments.

4.10 The FSC supports the remaining following proposed amendments from the draft Bill:

- **Items 1-8.**
- **Items 17-19.**
- **Items 40** – albeit we could not locate the table item 22
- **Item 41 and 42**
- **Part 10.18: items 43 and 44.**

4.11 The FSC notes that it remains unclear which regulations may be repealed and which retained in light of these draft amendments.