



General Manager  
Retail Investment Division  
The Treasury  
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PARKES ACT 2600  
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Dear Sir/Madam,

**Re: Future of Financial Advice Consultation**

Thank you for the opportunity to make this submission regarding the Future of Financial Advice.

My experience in the financial services industry should be taken into account when assessing its credibility:

- Financial Services Consultant - Financial Management Research Centre at University of New England Armidale NSW (1989-1992);
- Founder and managing director of Strategic Consulting & Training which provides consulting and training services to financial advisers (i.e. financial planners, accountants) and institutions (banks, dealer groups, insurance groups, industry funds, government funds) that serve or employ these advisers (1993-present);
- Founder of The Dashboard<sup>®</sup> Reports which was Australia's largest independent collection (with approximately 1700 contributing advisory firms) of performance (i.e. financial, productivity, client, personnel and practice) benchmarks of financial advisory firms (1998-2009);
- Author of What Price Advice – The secrets to maximising success in a commission-free world (2009)
- Author of Delivering Certainty – The secrets to engaging financial advice clients (2012)
- Author of Seeking Certainty – The secrets to finding greater financial certainty in your life (2014)
- Founder and creator of the Cultivating Advice<sup>®</sup> Training (practice management, client engagement and management) workshops that have been delivered to over 500 Australian advisory firms (2004-present)
- Former Chair Practice Management Development Committee for Advanced Diploma curriculum for former Australian Securities Institute (now FINSIA)

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<sup>®</sup> *The Dashboard Reports* is a registered Trademark of Strategic Consulting & Training – All rights reserved

- Former judge for many industry, institutional and professional publication awards regarding best advice practices
- Monthly contributor of “ProfitPlus” column to FairFax Media “Asset” Magazine (2000-present)

I own and manage a small training and consultancy business that has worked exclusively with financial advisers and institutions that support and employ financial advisers since 1993.

I applaud the underlying objective of the initial FOFA reforms to improve the quality of financial advice whilst building trust and confidence in the financial advice industry.

I equally applaud the Abbott government’s intention to reduce compliance costs for small business, financial advisers and consumers who access financial advice.

The main purpose of my submission is to provide The Treasury with my insights into the significant and changing paradigm occurring at the ‘coal-face’ between advisers and everyday Australians.

There are underlying assumptions contained within the Draft Explanatory Memorandum that may have related to the delivery of past financial advice but do not represent the future of advice marketplace that my firm is witnessing in our day-to-day operations providing training and consulting services in areas of the:

- Up-front and on-going pricing of financial advice;
- Engagement (and re-engagement) of financial advice clients;
- On-going management of advice client relationships;
- Delivering value to financial advice clients.

### **Regarding Chapter 1 – Best Interests Obligation:**

(a) Removal of Corporations Act 2001 Subsection 961b(2) clause (g)

I believe the proposed government’s amendments to remove Corporations Act 2001 Subsection 961b(2) clause (g) will place it at significant future criticism and risk.

The underlying and potentially false assumption or omission is consumers are aware of the costs they pay.

In fact, everyday Australians, have to date, been painfully unaware of the inherent costs they pay for financial advice. In particular, they have not been aware of basis point charging used extensively by financial services institutions.

The legislators need to be aware that everyday Australians are becoming increasingly aware of the costs they pay financial advisers and specifically aware of the long term effect of basis point costs.

In particular, a financial advisory firm aligned today to a group such as AMP enjoys significantly less 'dealer fees' the more AMP product they sell. This is true today of most, if not all, vertically integrated dealer groups in the Australian marketplace. (It should be noted that there are a small and growing number of dealer groups, typically unattractive to the majority of today's aligned financial advisory firms as their dealer fees are not subsidised or affected by the amount of financial product sold.)

The lower 'dealer fees' are subsidised by higher product charges paid for by everyday Australians when they purchase superannuation, investment or insurance products.

Without Corporations Act 2001 Subsection 961b(2) clause (g), AMP advisers can today satisfy best interests.

But as consumers inevitably come to understand basis point charging and that the AMP superannuation product at, say, 80 basis points, is inflated by up to, say, 40 basis points because they pay a component of the dealer's fee, I believe future Australians will harshly judge the government's 'reduction of red tape' intent as subsidising the 'big end of town' at their expense.

I acknowledge the 'significant legal uncertainty' that Corporations Act 2001 Subsection 961b(2) clause (g) provides the industry. I agree that current drafting of this legislation needs tightening to provide greater clarity to advice providers and reduce unintended court cases that this clause has been widely criticised for.

I contest that more significant work today to clarify inherent conflicted product costings which are loaded by dealer groups will not match the level of significant resentment and potential damage that everyday Australians will inflict on the government as they inevitably come to understand the business subsidisation costs they are paying under advice considered 'in the best interest'. These fees are significantly affecting their lifetime returns, and their confidence in the advisory.

(b) Removal of Corporations Act 2001 Subsection 961b(2) clauses (d) to (f) for agents or employees of an ADI

The industry and government superannuation funds have successfully divided the advice marketplace by their belligerent 'compare the pair' advertising campaign based upon their competitors (i.e. retail funds) use of 'commission' payments to its distributors versus their own 'non-commission' based products.

This proposed amendment will increase the distraction for everyday Australians as ‘commission-payments’ will continue as their primary means of accessing quality advice away from a required focus upon the achievement of quality advice outcomes.

Allowing any agent or employee to receive unlimited bonuses or commissions from the sale of financial products from a huge profit-making employer<sup>1</sup> grossly underestimates everyday Australians trust in today’s financial institutions.

Again, I predict a significant future backlash from everyday Australians who will wonder why the focus of five years of FoFA deliberations eventually focussed on the ‘red tape’ and cost reduction of suppliers of financial advice, rather than their desire for greater financial certainty through improved financial advice.

## **Regarding Chapter 2 – Ongoing Fee Arrangements**

### **(a) Removal of ‘opt-in’ requirement**

The need not to ‘opt-in’ each year (or two years) is core to the business models of most of Australia’s financial advisory firms.

The need not to actively explain to purchasers of financial advice on an on-going basis as to the extent and costs of such advice or on-going management has created:

- An sales-based industry focussed primarily on up-front advice/product conversations;
- An industry dominated by up-front product providers (i.e. banks, insurance and investment firms earning product revenues) and not on-going service providers (e.g. accounting, legal earning non-aligned advice fees);
- Artificially inflated advice firm business valuations created by product providers guarantee client-base buy-backs (mis-termed buyer of last resort as it predominantly is buyer of first resort) of their distributor firms client-bases to ensure future un-contested revenue streams remain with the original product provider.

From my consultancy experience in business benchmarking and analysis at the University of New England’s Financial Management Research Centre, I ensured from the very beginning of my own consultancy firm, that business benchmarking was central to any business consultancy proposition my firm offered.

An essential benchmark used to track professional advice firm is the “*Active/Inactive Client Ratio*”. Essentially this ratio shows the percentage of ‘Active’ clients as compared to the total number of clients a firm might have signed agreements for the provision of ‘ongoing’ services. For the purposes of our reporting an ‘Active’ client was defined as have at least one face-to-face appointment per annum, or for

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<sup>1</sup> For instance, the Commonwealth Bank’s statutory net profit after tax for the half year ending 31/12/2013 was \$4.207B – a 16% increase on previous years.

geographically distant or impaired client, it meant have an 'active' review phone conversation restating the objectives and performance of the advice relationship.

Unfortunately the majority of firms (at its peak my Dashboard® Reports collected and analysed the results from 1700 Australian businesses) we benchmarked from throughout Australia had inactive client bases. That is, the majority of the benchmarked firm's client-base (approx. 75%) were not actively advised face-to-face each year.

I fear the government might be assuming that the 'opt-in red tape' and its 'unnecessary costs' is driving the push for its removal. The government should be aware the real driver to obstruct 'opt-in' is not the costs of associated red tape.

As our statistics of active/inactive clients might suggest, there is a real fear by the majority of today's financial advisers that when the majority of the advisory firm's client base is informed of the services provided and associated costs they will have difficulty explain their 'on-going' value has this has not been their focus beyond past-compliance requirements.

Financial advisers and agents do not have to do anything for their clients today to extract their on-going revenue from their client's products. These fees paid for by clients are a real tangible cost yet under the proposed amendments there is no need to inform them of these costs.

### **Regarding Chapter 3 – Conflicted remuneration and other banned remuneration**

#### **(a) General advice is exempt from the ban on conflicted remuneration**

As per our Active/Inactive Client benchmark findings, the majority of client bases within Australia's financial advisory business can be considered 'inactive' (i.e. no frequent contact) and therefore considered purchasers of 'general advice'.

Therefore the majority of clients will be exempt from the ban on conflicted remuneration.

I fail to understand how the government will achieve the objective of building trust and confidence in the financial advice industry whilst enabling advice to be conflicted by sales bonuses.

Everyday Australians are increasing relying upon themselves for ensuring the achievement of their financial destiny. The GFC was a significant trust-breaking point between the provider of financial advice and consumer not only in Australia but around the globe.

Consequently the trend is that an increasing number of Australians will perform their own do-it-yourself approach to fund their fast-approaching retirement tending to seek

financial products (i.e. general advice) rather than personal advice. Testament to this are the 520,000 established self-managed superannuation funds which hold assets of some \$531b.

As Australians face an increasingly daunting and disadvantaged task of staying vigilant to best achieve their retirement aspirations, the government is allowing the use of sales bonuses as incentives by the much-advantaged product manufacturers.

Everyday Australians lack the time, the experience, the objectivity, the technical knowhow and an understanding of the marketplace mechanisms to properly assess their financial product (i.e. general advice) purchasing decisions.

The previous government's own estimates from last year's Pre-Election Economic & Fiscal Outlook of forward government expenditures suggested annual spending of \$75.5b on health, \$34.0b on Education and a massive \$158.5b on welfare by 2016/17FY. That is, for every dollar spent on education it intends to spend \$4 on welfare. Governments are understandable focussed on improving Australians confidence in the present financial advice channels to best control future welfare costs.

Hoping that increasing financial literacy of Australians will help control and manage their increasing financial complexity seems ill-founded. Studies<sup>2</sup> are showing little variance in ability to alter or influence financial behaviours.

In conclusion it must be acknowledge that today's government is committed to better financial advice by launching the first inquiry into the financial services sector in 17 years to be headed up by prominent Australian, David Murray. Since the last inquiry - the Wallis Inquiry - the Australian pool of superannuation has grown seven-fold to \$1.7T.

Thanks to global financial crisis, more examples of financial advisers abusing the trust place in them, a growth in the complexity and number of financial products, more everyday Australians are rightly concerned about the funding of their long-anticipated retirement.

The growth in superannuation is thanks largely to past government's vision to grow the pool of retirement savings. The Murray inquiries over-arching goal to determine how Australia's financial systems could be best positioned to meet the needs of the country and all Australians is timely.

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<sup>2</sup> For example refer "*Financial Literacy, Financial Education and Downstream Financial Behaviours*" Daniel Fernades, John G Lynch, Richard G Netemeyer – (October 2013)  
<http://ssm.com/abstract=2333898>



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The current government has an important opportunity to continue the vision of greater financial freedom for all Australians with less reliance on government pensions. Whilst the reduction of regulatory costs is to be admired, the current proposed amendments to FoFA do not act for the public good of Australians seeking greater financial certainty.

Yours sincerely,

Jim Stackpool  
Managing Director  
Strategic Consulting & Training Pty Limited