



FINANCIAL
SERVICES
COUNCIL

Review of the Quality of Financial Advice: Draft Terms of Reference

FSC Submission

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1. About the Financial Services Council

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advice licensees and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing \$3 trillion on behalf of more than 15.6 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.

2. Executive Summary

The FSC welcomes the *Review of the quality of financial advice: Draft Terms of Reference (the Review)*.

Financial advice is now a profession but an escalating regulatory burden has placed advice out of reach for most Australians with many advisers exiting the sector. As such, the Review's objective to achieve a regulatory framework that underpins the *affordability* and *accessibility* of financial advice in Australia is commendable.

The Review is an opportunity to chart a course of reform that eases the compliance burden on the sector. There are several areas where the final terms of reference could be expanded on or amended to ensure optimal focus on the major challenges facing the sector.

The FSC proposes several refinements to the Draft Terms of Reference to better focus on:

- the structural impacts of the legislative and regulatory framework that are adversely increasing the cost of advice;
- the different actors operating under that framework;
- the critical issues impacting licensees under this framework and;
- developments that have impacted the levels of insurance coverage in the community in addition to the Life Insurance Framework (**LIF**)

The FSC recommends the development of four separate 'issues papers' and a draft final report for public consultation. These papers would then underpin the overarching findings and recommendations in the Final Report.

The FSC would welcome the opportunity to discuss its submission with Treasury. The FSC intends to provide an active role in subsequent consultations for the Review following finalisation of the Terms of Reference.

3. FSC Recommendations

1. The FSC welcomes the Government's objective of affordability and access and the recognition of the need to reduce cost and that these costs are being worn by consumers. The Draft Terms of Reference should be amended to support its focus on delivering affordable and accessible financial advice.

- the structural impacts of the legislative and regulatory framework that are driving the cost of advice;
- the different actors operating under that framework and
- the critical issues impacting licensees under this framework

2. Add the words 'and other developments' to 3.1.5 so that it reads: The life insurance remuneration reforms, and the impact of the reforms and other developments on the levels of insurance coverage;

3. The consultation process should consist of four issues papers released ahead of a draft Final Report and Final Report to ensure sufficient consultation on the material issues impacting affordability and access. These papers should be themed on:

- The legislative and regulatory framework for consumer protection
- The financial advice process as it relates to the consumer experience and that of the advice sector being able to meet the requirements of that process
- Achieving sufficient regulatory certainty between the Regulator and the different parts of the advice sector (eg licensees and financial advisers)
- The Life Insurance Framework (LIF)

The Draft Final Report should be subject to public consultation to ensure its conclusions are robust. We would reject a process that sought to just receive submissions against the draft terms of reference and not on initial proposals or discussions of the issues.

4. The Independent Reviewer should have a detailed understanding of the issues driving cost in the advice sector as it pertains to its legislative and regulatory oversight. The Secretariat should have an equally sufficient level of recognised industry, knowledge and expertise to support the delivery of comprehensive recommendations in line with the Terms of Reference.

4. Purpose

Recommendation:

The FSC welcomes the Government's objective of affordability and access and the recognition of the need to reduce cost and that these costs are being worn by consumers. The draft Terms of Reference should be amended to refine its focus on:

- the structural impacts of the legislative and regulatory framework that are driving the cost of advice;
- the different actors operating under that framework and
- the critical issues impacting licensees under this framework

The draft Terms of Reference should be amended to strengthen this focus by capturing a number of issues critical to the Government's objective of affordability, access and reduced cost.

Structural

- **Code of Ethics:** The FSC supports a reissued Code of Ethics following the repeal of the safe harbour steps for meeting the Best Interests Duty. It is an integral tool to support an ultimately principles-based profession and as such, the Review should consider whether it is fit for purpose and necessary amendments under an improved framework.
- **Advice process:** There should be more emphasis on the advice process, and an examination of the the back-end and consumer-facing regulatory drivers against the overall value and benefit they provide the consumer, as interpreted by the advised consumer. The review should consider different models by which advice costs are covered by different providers of financial advice as this relates to the interests or position of individual consumers.
- **Definitions of advice:** Amend 3.1.1 to reflect the focus on creating a limited advice framework and consider a definition of financial advice in a manner that is agnostic of financial product.
- **Digital advice:** Explore how the regulatory regime can be made to be more flexible as to support digital advice and advancements in technology.
- **Remuneration:** The Review should identify opportunities to improve the flexibility consumers have to pay for the advice in a way suited to their circumstances under the current structure of remuneration.
- **Tax deductibility:** The Review should examine how the tax system can be leveraged to support access to professional financial advice.
- **Intra-fund advice and non-traditional advice pathways:** The Review should consider the function of intra-fund advice, its interaction with different advice frameworks and the sole purpose test. As the definitions of financial advice are also considered bringing intra-fund advice under one personal advice framework should be a central focus.
- **Professionalisation:** A broad discussion is needed on how the system can better recognise prior learning, on the job experience, industry-body standard setting for

providing specialised personal advice and ultimately, in time, self-regulation by the industry. The FSC outline comprehensive proposals in its White Paper for achieving this by 2030.

- **Design and Distribution Obligations (DDO):** The introduction of the DDO and its impact on the advice process should be considered.
- **Breach reporting framework:** The reference to ‘regulatory tools’ should include the new breach reporting framework which adds a considerable onus on licensees and advisers to report a wide range of activity that constitutes breaches. Given the draft Terms of Reference focus on principles-based regulation, and reducing the overall cost of the advice process, the Review should consider the ultimate proportionality of the framework and how this would need to be re-categorised were it revised in tandem with reform proposed by the Review.

Licensees and other actors within the advice sector

- **Recognition of different parts of the advice sector:** For example, the Review should consider the interaction of licensees and product providers who are subject to alternative regulations making the existing legislative and regulatory framework for advice redundant.
- **Changing role of the licensee, their composition and impact:** the role and future of advice licensees as established vehicles of consumer protection given their resources and oversight of financial advisers, should be a more prominent consideration of the Review. The Review should also consider:
 - the different types of licensees working within their sector, in particular their size.
 - The varied level of scrutiny and obligations applied to different licensees dependent on size.
 - For example, larger advice licensees tend to have a larger human resources function with risk management frameworks (eg assurance, risk and internal audit streams, boards, committees, external audits, group insurance, investment in tech. Smaller licensees have different resources, with significant conflicts (a director, is an adviser, a compliance manager, a risk manager, a complaints officer).

External considerations

- **Analogous professions:** The Review should examine licensing, disciplinary and oversight frameworks in specifically the *legal* and *medical* professions.
- **Consideration of the role of external advice-like services and sources of information:** This would extend to financial counsellors and ‘finfluencers’, Australian Tax Office (ATO) calculators, ASIC’s MoneySmart website
- **Access to professional indemnity insurance:** The limited access to professional indemnity insurance is a live-issue and subject to a separate Treasury consultation for which the Review should have regard for.
- **Financial services entities:** Where the draft Terms of Reference states a focus on the “*role of financial services entities including professional associations*” this should

not extend to banks or organisations not in the business of providing financial advice and to reflect the structure of the sector.

- **Regulatory technology:** 4.4 should capture analysis of the sector's dependence on third party regulatory technology systems and providers, the limitations of these systems and how they impact licensees and advisers in delivering the advice process and meeting their disclosure obligations.
 - For example, if a company providing technology-based services to support compliance do not roll out a solution adequately or in a timely manner – this has downstream impacts.

5. LIF Framework

Recommendation:

Add the words ‘and other developments’ to 3.1.5 so that it reads: *The life insurance remuneration reforms, and the impact of the reforms **and other developments** on the levels of insurance coverage;*

To ensure that the Life Insurance Framework is aligned with the interests of providers of financial advice and consumer outcomes, the FSC recommends that other developments that may have contributed to levels of Life Insurance coverage should also be considered in the Quality of Advice review.

On 1 January 2019 the Life Insurance Framework was introduced to align the interests of providers of financial advice in the life insurance sector with consumer outcomes. It did this by removing the current exemption from the ban on conflicted remuneration for benefits paid in relation to certain life risk insurance products. However, since the introduction of the Life Insurance Framework, reforms in group insurance have had a significant impact to coverage levels of Life Insurance.

Reforms such as Treasury Laws Amendment (Putting Members’ Interests First) Bill 2019 which removed default group insurance from superannuation members accounts where balances were under \$6,000 as well as members under 25 years of age to ensure that account balances were not eroded by premiums. As well as the Treasury Laws Amendment (Your Future, Your Super) Bill 2021 which limits the creation of multiple superannuation accounts by ‘stapling’ an employee’s superannuation account to them to ensure unnecessary fees and insurance premiums are not paid on unintended multiple superannuation accounts.

While the FSC acknowledges that these reforms were focused on group insurance, the intended effect of these reforms are to ensure Australians receive value for money with their Life Insurance by removing multiple life insurance accounts which will have a flow on effect on measuring life insurance coverage levels.

In addition, this review should also consider any proposed reforms to Life Insurance provided through financial advice and their subsequent effect on life insurance coverage levels.

The FSC recognises how life insurance provided through financial advice is under consideration, and if the objective of 3.1.5 is to examine the Life Insurance Framework and its effect on insurance coverage levels, then a proper examination of all recent and proposed reforms should also be considered to ensure that a true evaluation of insurance coverage levels can be undertaken.

Therefore, the FSC recommends that when the Quality of Advice review examines the Life Insurance Framework, it should also examine other developments to ensure a proper evaluation of the Life Insurance Framework and its effect on insurance coverage levels.

6. Process

6.1. Consultation

Recommendation:

The consultation process should consist of four 'issues papers' released ahead of a draft Final Report, and a Final Report, to ensure sufficient consultation on the material issues impacting affordability and access. These papers should be themed on:

- The legislative and regulatory framework for consumer protection
- The financial advice process as it relates to the consumer experience and that of the advice sector being able to meet the requirements of that process
- Achieving sufficient regulatory certainty between the Regulator and the different parts of the advice sector (eg licensees and financial advisers)
- The Life Insurance Framework (LIF)

The Draft Final Report should be subject to public consultation to ensure its conclusions are robust. We would reject a process that sought to just receive submissions against the draft terms of reference and not on initial proposals or discussions of the issues.

Treasury should consider a participatory approach to developing its recommendations through industry roundtables or other fora to ensure has the level of insight and support it needs to generate comprehensive solutions to the complex regulatory challenges identified in its scope. An example of this might be working with industry model more practical forms of documentation.

6.2. Independent Review

Recommendation: The Independent Reviewer should have a detailed understanding of the issues driving cost in the advice sector as it pertains to its legislative and regulatory oversight. The Secretariat should have an equally sufficient level of recognised industry, knowledge and expertise to support the delivery of comprehensive recommendations in line with the Terms of Reference.

The Independent Reviewer should be a recognised eminent person of public standing, professional suitability and who is well qualified to the degree that would be expected for a Government review as significant and as broad as this one. The financial advice sector has been subject to various reviews in the last decade with the cost drivers relating to advice worsening. It is important the leadership of the Review brings a perspective cognisant of this with a view to amending the legislative and regulatory framework to reduce the cost of providing financial advice to consumers.

6.3. Data

There should be a transparent approach to use of data and industry should be invited to provide its data sets as these are collated by Treasury and ASIC

Need for transparent approach by Treasury and ASIC to the data used to support the Review's insights. If data differs dependent on source, then they need it from all sources. Needs to be balanced. Get the data you need and conduct a balanced review.

6.4. Outcomes of the Review

The Review should produce recommendations for legislative change to reduce the cost of advice. Regulator-led efforts to reduce the cost of advice while a positive step are limited in their effect on the legislative overlay that has exacerbated the overall costs of production.

The FSC has outlined the direction future reform should take in the form of its White Paper on financial advice with research undertaken by KPMG to support its proposals. Not only do these reflect the broad consensus of the sector, many of these recommendations have been called for by the sector for some years. It underlines the importance of the Review producing recommendations that resolve the issue of escalating cost and complexity in advice while also assesses the impact of LIF.

The FSC will contribute to the Review in further detail as the Terms of Reference and process for consultation are finalised.

7. Sequencing and timeline of reform

Many key solutions to reduce the cost of providing financial advice have been well canvassed. What reforms are *prioritised* is of equal importance to the *effectiveness* of the reforms. Pursuing reform after the Review would follow an intensive period of professionalisation and rapid adoption of substantially higher legislative and regulatory obligations arising from the Hayne Royal Commission that have all occurred in the past decade. As such the timing and priority as to which reforms should be implemented and the sequence in which they occur is critical to reducing the cost of providing advice.

The FSC for this reason has provided in its *White Paper* a reform program that prioritises changes to the advice process (removal of the safe harbour steps, the introduction of the Letter of Advice and changes to the definitions of financial advice) remove the largest drivers of unnecessary cost and improve the consumer experience. A set of reforms following this would complement these changes to support a world class self-regulating profession.

8. Appendix: Reform timeline

The FSC notes the below timeline for reforming the advice sector to inform Treasury's Review from its White Paper on financial advice released in October 2021.

By 2023	By 2026	By 2030
<ul style="list-style-type: none"> • Safe harbour steps abolished • Code of Ethics amended • Letter of Advice with scalable advice obligations introduced • Statement of Advice and Record of Advice abolished • Wholesale client asset test threshold increased and indexed • Breach reporting framework revised • Consult and clarify framework for licensees and advisers to support individual registration • Regulatory Guidance to become more exemplary than prescriptive • ASIC Advice Unit established 	<ul style="list-style-type: none"> • Legislate personal advice and general information – abolish redundant terms and separate product from advice • Update licensing and registration framework • Introduction of a 'practising certificate' • Prior learning and equivalent pathways recognised • Accreditation to be conducted by universities and Registered Training Organisations (RTOs) • Commencement of principles-based regulatory framework • Tax deductibility or rebate for all financial advice 	<ul style="list-style-type: none"> • Self-regulation by the industry • Principles-based regulatory framework fully implemented • Increased role for professional bodies and industry standards