



Australian Government

# Future of Financial Advice

## 2011

**Information Pack**  
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## FOREWORD



As the Minister responsible for financial services, I am firmly committed to implementing reforms that are in the best interests of consumers.

The *Future of Financial Advice* (FOFA) reforms represent a comprehensive Government response to the Parliamentary Joint Committee on Corporations and Financial Services' Inquiry (PJC Inquiry) into financial products and services, which was set up in the wake of collapses such as Storm Financial and Opes Prime. The recent Trio collapse is also relevant.

With around 1 in 5 Australians currently receiving advice, the public policy and industry challenge is to ensure more Australians have access to high quality and affordable advice, particularly as we enjoy the gift of longer life. There is little doubt that those who access quality financial advice are better off than those who do not.

In recognition of this, the FOFA reforms focus on improving the quality of financial advice and expanding the availability of more affordable forms of advice. The removal of regulatory barriers to the provision of different forms of advice will open up new markets for financial planners, helping them reach younger customers and those with less complex advice needs.

The key reforms include a ban on conflicted remuneration structures, including commissions and volume payments, a requirement for advisers to obtain client agreement to ongoing advice fees every two years and the expansion of limited advice.

I am optimistic that these reforms will genuinely enhance the confidence that consumers have in financial advice and reinforce the move towards the professionalism advocated by industry bodies such as the Financial Planning Association. Put simply, they ensure the practices of the leading advice firms become the industry and consumer standard.

The FOFA reforms also complement the Government's historic commitment to increase the superannuation guarantee to 12 per cent. We cannot encourage Australians to save more for their retirement without ensuring the retirement savings system is operating in their best interests.

Over the last year, the Government has engaged extensively with stakeholders. I sincerely thank all who have contributed to this important process which has been crucial in developing the Gillard Government's thinking. I also acknowledge the significant contribution of Bernie Ripoll who chaired the PJC Inquiry and that of my Ministerial predecessor, Chris Bowen. I also thank ASIC and the Australian Treasury for their hard work.

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

**The Hon Bill Shorten MP**  
**Assistant Treasurer and Minister for Financial Services and Superannuation**

## 1. SUMMARY

The *Future of Financial Advice* (FOFA) reforms are focused on improving the quality of advice and enhancing retail investor protection. They will underpin investor confidence and trust in the industry in the years to come. All Australians have a stake in the success of these reforms.

The April 2010 FOFA announcement included a number of key measures, including a prospective ban on conflicted remuneration structures, such as commissions and volume-based payments, a duty requiring advisers to act in the best interests of their clients when giving personal advice, and a requirement for advisers to obtain client agreement to ongoing advice fees (the opt-in). Additional measures also focused on improving access to advice.

At this time, further consultation on a number of matters was also announced including: whether the ban on conflicted remuneration structures should be extended to risk insurance; implementation of the opt-in and the scope and the best way of expanding the provision of low cost, simple advice.

Following an extensive consultation process and careful consideration, the Government has decided on these remaining areas, as well as providing further detail and clarity about how the announced reforms will operate. This is important for providing certainty, as we move forward with the FOFA arrangements and draft legislation implementing the reforms.

The new elements of the FOFA reforms are:

- A prospective ban on up-front and trailing commissions and like payments for both individual and group risk within superannuation from 1 July 2013.
- A prospective requirement for advisers to get clients to opt-in (or renew) their advice agreement every two years from 1 July 2012.
- A prospective ban on any form of payment relating to volume or sales targets from any financial services business to dealer groups, authorised representatives or advisers, including volume rebates from platform providers to dealer groups.
- A prospective ban on soft dollar benefits, where a benefit is \$300 or more (per benefit) from 1 July 2012. The ban does not apply to any benefit provided for the purposes of professional development and administrative IT services if set criteria are met.
- Expanding a new form of limited advice called scaled advice, which can be provided by a range of advice providers, including superannuation trustees, financial planners and potentially accountants, creating a level playing field for people who provide advice. Scaled advice is advice about one area of an investor's needs, such as insurance, or about a limited range of issues.
- A limited carve out from elements of the ban on conflicted remuneration and best interests duty for basic banking products where employees of an Australian Deposit-taking Institution (ADI) are advising on and selling their employer ADI's basic banking products. Basic banking

products are basic deposit products (e.g. savings accounts), first home saver account deposit accounts and non-cash payment products (e.g. travellers cheques and cheque accounts).

- The Government will explore whether the term 'financial planner/adviser' should be restricted under the *Corporations Act 2001* (Corporations Act).

This paper also contains an update on

- the formulation of the statutory best interests duty; and
- formulating a replacement for the accountants' licensing exemption.

## 2. THE REFORMS

### 2.1 APPLICATION OF THE BAN ON CONFLICTED REMUNERATION TO RISK INSURANCE

- The April 2010 FOFA announcement stated there would be consultation on whether to extend the ban on conflicted remuneration to risk insurance. This also enabled the Government to take into consideration the final recommendation of the *Super System Review* (Cooper Review) which was also looking into the issue of insurance arrangements within superannuation.
- There are some unique features of insurance provided within superannuation. Fees and charges within superannuation come at the cost of foregone retirement savings and expenditure on insurance is tax deductible to the fund.
- After careful consideration and extensive consultation, the Government has decided to ban up-front and trailing commissions and like payments for both individual and group risk within superannuation from 1 July 2013.
- However, the Government has decided not to extend the ban on conflicted remuneration to risk insurance outside of superannuation.
- The Government's position is consistent with the recommendation of the *Cooper Review* that insurance commissions within superannuation be prohibited as they have the potential to affect the quality of advice and the findings of ASIC shadow shopping surveys that illustrate that in case of poor advice, over half involved poor life insurance advice<sup>1</sup>.
- Given the above factors, the Government concluded that banning all forms of commissions within superannuation is in the best interest of consumers.

#### *Benefits*

- The quality of advice will improve as conflicted remuneration structures will be removed.
- Consumers will have the freedom to pay for insurance advice, but won't be charged for services they don't receive.
- Accessing insurance through superannuation will remain attractive as preferential tax arrangements will remain.
- Those consumers who want alternative payment arrangements have the choice and flexibility of doing so outside the superannuation environment.

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<sup>1</sup> Recommendation 5.12 of the *Super System Review* proposed that up-front and trailing commissions and similar payments should be prohibited in respect of any insurance offered to any superannuation entity, including self-managed superannuation funds (SMSFs), regardless of rules on commissions that might apply outside superannuation.

### *Other issues*

- The Government considers that other aspects of the FOFA reforms, such as the introduction of a best interests duty, will ensure that clients are only advised to switch policies when it is in their best interests. However, 'churn' and the broader impact of the ban on commissions within superannuation are areas that the Government will continue to monitor closely into the future.

## **2.2 OPERATION OF 'OPT-IN' UNDER THE ADVISER CHARGING REGIME**

- The announced FOFA reforms included a compulsory annual renewal 'opt-in' requirement where an ongoing advice fee is to be charged to a client. At that time the Government announced that it would consult on the implementation of opt-in, including the period after which the initial advice was given that it would apply.
- The policy reflects the need to ensure that advisers do not charge ongoing, open-ended fees where the client is receiving little or no service. It also empowers clients that are receiving an ongoing service to reconsider whether they are receiving value for money.
- After extensive consultation with stakeholders, the Government has decided to amend the opt-in policy, so that retail clients will have to agree (by opting in) to ongoing advice fees every two years from 1 July 2012.
- This will be supplemented by an intervening annual disclosure notice to be provided to the client detailing fee and service information for the previous and forthcoming year, informing the client of their right to 'opt-out' at any point in time to an ongoing advice contract.

### *Benefits*

- A two-year opt-in means advisers are in regular contact with clients, but provides some flexibility regarding implementation.

### *Implementation processes*

- Since the original announcement, further details on the practical workings of the opt-in policy have been developed as a result of Government consultations. While consultation on practical details will be ongoing up until the release of draft legislation, current bedded down features of the policy will include:
  - The adviser being required to send a prescribed renewal notice no less than 30 days prior to the relevant (two year) anniversary date;
  - This notice would outline the fee the client paid in the previous year and a description of the services they received, and fee and service information for the forthcoming year (also alerting the client to the fact that they can opt out at any time);

- If the client does not respond to the notice or opts out, the adviser cannot continue to charge an ongoing advice fee, and nor can the client continue to expect management of their financial arrangements;
- If the client is unresponsive to the renewal notice, the adviser can continue charging the client for an additional 30 day 'grace period' after the anniversary date;
- Every second year where no opt-in renewal is required, a disclosure document would be required to be sent in its place, containing the same information normally contained in the opt-in renewal notice (for example, fee information); and
- If a client does not respond to a renewal notice, they are taken to have chosen to opt-out 30 days after the anniversary date, meaning the adviser's liability for ongoing advice ceases at the point that they can no longer charge an ongoing fee (advisers will still be liable for advisory services already rendered to the client).

- Only those advisers intending to charge ongoing advice fees to retail clients need to send the notice. Opt-in will apply prospectively, however issues around grandfathering arrangements will still be subject to further consultation.
- At this time, it is not automatically assumed that a penalty would apply where an adviser charges an ongoing fee without seeking a client's renewal, or where the client opts out. However, the Government will consult with industry and stakeholders on the possible need for a penalty provision for a breach of the opt-in policy as part of the ongoing implementation process.

## 2.3 BAN ON VOLUME PAYMENTS

- The April 2010 FOFA announcement included a ban on conflicted remuneration, including volume-related payments. The measure was targeted at removing payments that have similar conflicts to product provider set remuneration, such as commissions.
- Through the consultation process some industry participants proposed a more narrow application of this ban, for example by allowing volume bonuses to be paid from platform providers to financial advisory dealer groups in certain circumstances. Notwithstanding the merit of these proposals, if structural reform in the industry is to truly transpire, all conflicted remuneration, including volume rebates from platform providers to dealer groups, must cease.
- As such, there will be a broad comprehensive ban, involving a prohibition of any form of payment relating to volume or sales targets from any financial services business to dealer groups, authorised representatives or advisers.
- While this broad ban on volume payments will require some adjustment by industry, the measure will enhance competition, with platforms competing with one another purely on price and quality for the client, rather than by distributing their products through volume bonuses to dealer groups or advisers.

- The ban is intended to prevent any licensee, authorised representative or adviser from receiving a payment from any entity based on volume of product sales. Following the conclusion of formal consultations some industry stakeholders raised the issue of arrangements such as equity share schemes or special purpose vehicles being used to circumvent the ban on volume-based payments. The Government shares these concerns and will consult with consumer and industry groups on anti-avoidance provisions.

*Benefits*

- A broad ban points competitive pressures in the right direction.
  - It removes the monetary incentive to recommend usage of a platform;
  - In the future, platforms will need to compete for product distribution on the basis of quality and value for money, rather than by paying volume bonuses to dealer groups; and
  - With this change in emphasis, platform providers should be focusing on the consumer as the client, rather than the adviser.

*Scope of the ban*

- For clarity, the ban will include a prohibition on the following payments:
  - Any volume-based payment from a product provider, platform provider, or any other entity to a licensee, authorised representative or adviser in relation to distribution or advice for retail financial products.
  - Any volume-based payment by the product provider, platform provider or any other entity to the licensee or adviser which is generally conditional on the licensee having large funds under management with the product (except asset-based fees paid by a client to a licensee or adviser);
  - Any volume-based payment from licensees to their employee advisers or authorised representatives for distribution of retail financial products, contingent or based on meeting sales targets; and
  - Any volume-based shelf-space fees which are paid from the fund manager to the platform provider and from the platform provider to the licensee.
- It should be noted that this ban will not apply in relation to pure risk insurance, or where employees are advising on and selling their ADI employer's basic banking products only (see section 2.8).

## 2.4 BAN ON SOFT DOLLAR BENEFITS

- The announced ban on conflicted remuneration structures did not initially extend to soft dollar benefits. It was announced that the expert advisory panel, in its review of ethical standards, was to consider whether these payments are consistent with those standards. The panel has

held discussions in relation to the treatment of soft dollar benefits in light of the FOFA reforms and its review of ethical standards. The deliberations of the panel have been a factor in the Government's decision to ban soft dollar benefits as outlined below.

- A soft dollar benefit is 'any benefit received by a financial planning firm, its representatives or associates, other than basic monetary commissions or direct client advice fees'.<sup>2</sup> The definition includes some monetary payments as well as non-monetary benefits. There will be a prospective ban on soft dollar benefits, where a benefit is \$300 or more (per benefit) from 1 July 2012. Benefits received which do not exceed \$300 per benefit will be allowed subject to an 'infrequent or irregular test for identical or similar benefits'. The ban does not apply to any benefit provided for the purposes of professional development and administrative IT services provided set criteria are met.
  - The test for benefits below \$300 is subject to an 'infrequent or irregular test for identical or similar benefits' to ensure that small similar benefits are not given on a repeated basis.
  - The ban applies to the same products as the broader ban on conflicted remuneration. This means the ban applies to retail investment financial products and insurance within superannuation, but does not apply to risk insurance outside of superannuation (including both life and general insurance).
- Further details of the ban will be subject to implementation consultation, including the criteria for the exemptions for professional development and administrative IT services. Criteria for professional development could include a condition that the development take place within Australia as well as conditions to ensure the majority of the time at the conference is spent on professional development activities.
- The ban on soft dollar would apply from 1 July 2012, consistent with the commencement of other FOFA reforms relating to conflicted remuneration. Consideration will be given to appropriate transitional arrangements.

#### Some examples of the operation of the ban (not exhaustive)

Issue	Banned?	Why?
Free or subsidised business equipment or services, such as computer hardware, office rental and commercial software, over \$300.	Yes	These benefits have the potential to influence product selection and decision making.
Access to administrative information technology services, such as software to access a platform or access to a website to place orders.	No	So long as it can be shown that the administrative information technology services is relevant and tangible to the licensee's business, this is a benefit that will be permitted as it facilitates access to advice.

<sup>2</sup> A broad definition of soft-dollar benefits as used in ASIC Report 30 – *Disclosure of soft dollar benefits* (June 2004).

Entertainment and gifts over \$300.	Yes	Entertainment and gifts over this threshold may influence advice.
Conferences, seminars and training where a set percentage of time is spent on education.	No	It is important that licensees and representatives continue to increase their professional standards and development, and training can play an important role in this regard.

## 2.5 STATUTORY BEST INTERESTS DUTY

- Under the FOFA reforms, the Government announced that :
  - it would introduce a statutory best interests duty for financial advisers;
  - this duty would require advisers to act in the best interests of clients and give priority to the interests of the client above any other interests; and
  - the duty would include a reasonable steps qualification, so that advisers are only required to take reasonable steps to discharge the duty.
- Treasury has been consulting with stakeholders on various formulations of a duty that would require a person providing personal advice to a retail client to act in the best interests of the client and, if there is a conflict between the client's and the interests of the person providing personal advice or the providing entity, to give priority to the client's interests. This would be consistent with the formulation of the duty used elsewhere in the Corporations Act.
- The Government recognises that the focus of the duty should be on how a person has acted in providing advice rather than the outcome of that action. In addition, the duty should not be interpreted as imposing trustee-style obligations on financial advisers given the differences in roles between a trustee and a financial adviser.
- Compliance with this duty will be measured according to what is reasonable in the circumstances in which the advice is provided. What is reasonable in the circumstances is commensurate and scalable to the client's needs. This means that if the client's needs indicate that only limited advice is necessary, the adviser is not obligated to provide holistic advice.
- A person giving personal advice will not be required to broke the entire market or a subset of the market of all available financial products to find the best possible product for the client, unless this service is offered by the adviser or requested by the client and subsequently agreed to by both parties.
- The legislation will provide that a person providing personal advice cannot contract out of this duty. Any ability to contract out of the duty would severely impair the ability of the duty to appropriately protect consumers. If a person considers that they cannot provide advice that is

in the best interests of the client in accordance with the duty, they must refuse to provide the advice.

- Financial liability for any breach of the duty will rest with the relevant providing entity. This means that individual advisers will not be held financially liable for any breach of the duty. The imposition of this liability on the providing entity ensures that the providing entity has the necessary incentives to create working conditions for their advisers that facilitate compliance with this duty. However, the individual adviser who provides the advice may be subject to administrative penalties in the form of a banning order if they breach the duty.
- A number of more detailed issues relating to the formulation of the duty were raised with the Government following the conclusion of the consultation. These include:
  - The extent to which the scope of the advice or the client's instructions should be one of the issues considered in terms of the application of the duty;
  - The ability of the adviser to give priority to the interests of the client over the interests of the providing entity given the adviser may not have full knowledge of the interests of the providing entity;
  - The extent to which (if at all) the providing entity should have a separate duty to act in the best interests of clients being provided with advice through an adviser working under their authorisation;
  - Whether the duty should require an adviser to consider an appropriate sample of products prior to making any product recommendation; and
  - The extent to which further detail is necessary to ensure that the duty is concerned with how a person has acted in providing the advice rather than the outcome of that action.
- The Government will consider these issues as part of developing the legislation to implement this measure. Stakeholders will have an opportunity to provide comments on the legislation prior to its introduction.

## 2.6 ACCESS TO ADVICE

### *Scaled advice*

- ASIC research released in December 2010 indicates that many Australians, particularly those who have never previously accessed financial advice, want piece-by-piece simple advice rather than a complete financial plan.
- The Government is taking further steps to ensure that financial advice will be within the reach of a wider range of Australians, by facilitating the expansion of a new form of advice called "scaled advice".
- Scaled advice is advice about one area of an investor's needs, such as insurance, or about a limited range of issues. This contrasts to so-called "holistic advice" which is the traditional

advice model offered by many financial advisers. Under the holistic model, advisers make enquiries and provide advice to the client on all aspects of their financial circumstances in a full financial plan.

- Scaled advice can be provided by a wide range of advice providers, including superannuation trustees (intra-fund advice is a form of scaled advice), financial planners and potentially accountants, creating a level playing field for people who provide advice.
- It will also open up new growth opportunities for advice professionals by removing the regulatory barriers to the provision of advice for those with simpler needs, including younger investors.
- ASIC intends to release a consultation paper in June/July of this year that further sets out guidance about how simple, single issue advice can be provided, not only by superannuation trustees but also by anybody in the advice industry.
- To facilitate scaled advice, the Government will amend the existing reasonable basis for advice obligation in the *Corporations Act* to make it clear that this obligation is commensurate and scalable to the client's needs when providing advice. This will help address some concerns identified by industry that the provision of scaled advice is not consistent with their obligations under the *Corporations Act*.
- Treasury consultations with industry on this point have shown a good level of support for such a concept, provided appropriate consumer protections are maintained.

#### *Intra-fund advice*

- As part of its consultation process, ASIC will also consider whether its existing class order relief for intra-fund advice is still relevant or necessary in light of the work outlined above and whether it should be revoked.
- Given some of the concerns expressed by industry, there will be further consultation on whether intra-fund advice should be extended to facilitate simple, single issue personal advice on topics such as transition to retirement, intra-pension advice, nomination of beneficiaries, superannuation and Centrelink and retirement planning generally.
- Finally, intra-fund advice will be carved out of the FOFA adviser charging regime in accordance with the *Stronger Super* recommendations.

## 2.7 ACCOUNTANTS' LICENSING EXEMPTION

- Last year, the Government announced that the existing exemption permitting accountants to provide advice on the establishment and closing of self-managed superannuation funds without holding an Australian Financial Services Licence (AFSL) would be removed and the Government would consult on an appropriate replacement.

- The Government believes it is in the interests of accountants and their clients, for accountants to be able to consider a broader range of financial issues when advising clients, particularly in relation to the establishment of self-managed superannuation funds. The Government also recognises that many accountants are not financial advisers, and may not wish to provide holistic advice or recommendations to clients to purchase specific financial products. Expanding the supply of this type of financial advice is in line with the Government's objective to improve access to lower-cost, simpler financial advice for all Australians.
- The Government recognises it is important to achieve this outcome with minimal cost and disruption for accountants but also ensure that the interests of their clients are protected. Treasury, ASIC and the accounting bodies are now working together on various initiatives that maintain a level playing field for what is needed to provide financial advice but at the same time will assist accountants to obtain a licence.
- The measures discussed by ASIC, Treasury and the accounting bodies to date to achieve these objectives include ASIC recognising relevant experience of accountants for licensing purposes; granting licences that relate to classes of financial products rather than specific financial products (i.e. 'non-product financial advice') in order to reduce ongoing compliance costs; and providing specific guidance about how a typical accountant might apply for a licence.
- Discussions are ongoing and all parties are committed to achieving a workable outcome. Treasury will report to Government on the outcome of these consultations at the end of May this year and a decision will be made at that stage as to whether any broader legislative changes are needed and what transition period is appropriate for these reforms.

## 2.8 LIMITED CARVE-OUT FOR BASIC PRODUCTS FROM THE BAN ON CERTAIN CONFLICTED REMUNERATION STRUCTURES AND BEST INTERESTS DUTY

- The FOFA reforms announced a ban on conflicted remuneration structures including any form of payment relating to volume or sales, as well as the introduction of a best interests duty. The ban on payments relating to volume or sales also extends to employee remuneration calculated based on sales and volume targets.
- During implementation consultation, some concerns were expressed about the measures, particularly relating to their application to the more straightforward retail banking products, given the compliance burden of the measures as well as significant changes to employee remuneration and workplace arrangements, in light of arguments that there is not the same level of conflict, risk and potential impact on the advice process.
- As part of the consultation process, the Government was not made aware of any evidence of severe consumer detriment as a result of inappropriate selling of products of this nature and these products are less complex in nature relative to managed investments or life insurance.

- There will be a limited carve-out from the ban on volume payments and best interests duty for basic banking products where employees of an Australian Deposit-taking Institution (ADI) are advising on and selling their employer ADI basic banking products.
- As these basic banking products are often sold by frontline staff, the carve-out is largely intended to address the more routine activities of frontline staff, such as tellers and specialists. While these employees may provide either general or limited personal advice in relation to these basic banking products, these products are generally easier for consumers to understand, and consumers more readily understand that the frontline employee of the ADI is in the business of selling the employer's product.
- The ban on conflicted remuneration structures and the requirement to act in the client's best interest would not apply where:
  - It involves the advice or distribution of a 'basic banking product' that is either a basic deposit product (e.g. savings accounts), a first home saver account deposit account and/or non cash payment products (e.g. cheque accounts, travellers cheques etc); and
  - The advice or distribution of the 'basic banking product' is through an employee of the ADI who issued the basic banking product.
    - : It is a carve-out that applies in relation to both general and personal advice (while the best interest duty is only relevant to personal advice; the ban on conflicted remuneration structures applies to both general and personal advice).
- Importantly, the carve-out does not apply where an employee of an ADI provides advice on a combination of 'basic banking products' and other more complex financial products. Therefore the carve-out cannot be relied upon by a fully fledged financial planner who is also an employee of an ADI where they provide advice on a combination of 'basic banking products' and more complex products.

## 2.9 RESTRICTION OF THE TERM FINANCIAL PLANNER/ADVISER

- Treasury will provide the Government with a recommendation as to whether the term 'financial planner/adviser' should be defined in the Corporations Act and its use restricted.
- Some stakeholders have argued that restricting the use of the term 'financial planner/adviser' would carry consumer protection benefits, including that consumers would have a clearer understanding of whether a planner or adviser has met certain educational and professional standards. Against this, there are concerns that it may create a regulatory barrier to entry and unnecessarily increase the cost of advice.

## 2.10 UPDATE ON OTHER AREAS OF FOFA REFORMS

- There are a number of other areas in which work is ongoing in relation to the implementation of the FOFA reforms.

#### Review of the classification of clients as wholesale or retail

- As part of the FOFA reforms, the Government announced there will be a review of the appropriateness of the distinction between wholesale and retail clients.
- An options paper was released in January this year which sought feedback from stakeholders on a range of options for the classification of clients as retail or wholesale. Submissions closed on 25 February. Around 45 submissions have been received. The Government is currently considering submissions.

#### Simplification of Financial Service Guides

- As part of the FOFA reforms, the Government announced that Financial Service Guides (FSGs) will be improved, so they are more effective at disclosing material restrictions on advice, any potential conflicts of interest and remuneration structures.
- Consultations on the form and content of the FSG are underway. To an extent, the content of the FSG will depend on the outcome of other FOFA reforms and therefore will not be finalised until the detail of other reforms are settled. Regulations to support the simplified FSG will be in place by 1 July 2012.

#### Changes to ASIC's licensing and banning powers

- As part of the FOFA reforms, the Government announced that the powers of ASIC in relation to the licensing and banning of individuals from the financial services industry will be strengthened. The announced changes to ASIC's licensing and banning powers will be included in the exposure draft of legislation implementing the reforms.

#### Statutory compensation scheme

- A consultation paper entitled *Review of compensation arrangements for consumers of financial services* was released on 20 April 2011 and seeks submissions by 1 June 2011. The paper has been prepared by Richard St. John as a key step in his review of the need for, and costs and benefits of, a statutory compensation scheme for financial services. Mr St. John invites comment on a number of issues raised in his paper and expects to finalise his recommendations to the Government as soon as possible after a further process of consultation.

#### Asset-based fees on geared investment amounts

- As part of the FOFA reforms, the Government announced that percentage-based fees (known as assets under management fees) will only be charged on ungeared products or investment amounts.
- The feedback from stakeholders to date is that for this ban to have proper effect it must apply where there is any leverage involved in a retail client's investment strategy. This would mean that where any component of a retail client's investible funds is geared, an asset-based fee

cannot be charged, even on the ungeared component. Consultation on this issue will be ongoing as part of the implementation process.

## 2.11 NEXT STEPS

- Consultation on each of the elements outlined above will continue to resolve any outstanding issues as part of the development of legislation.
- The Government is expected to release draft legislation for public comment after the middle of this year.
- Consistent with the timetable announced last year, legislation giving effect to these reforms will be introduced into Parliament before the end of the year.

### 3. SCOPE OF THE REFORMS

As the April 2010 announcement outlined, the FOFA reforms are focused on tackling conflicts of interest that have threatened the quality of financial advice provided to Australian investors, and in particular the inappropriate selling of financial products that culminated in high profile corporate collapses such as Storm Financial, Opes Prime and Westpoint. It is in this context that the precise application of the reforms are primarily focused on personal financial advice provided to retail clients, rather than the provision of general financial advice, or financial advice provided to wholesale investors. Where certain reforms also have application to the provision of general advice, this is generally for practical reasons and regulatory simplicity.

It should be noted that while the reforms generally only apply to retail clients of financial advice, the Government is currently considering the appropriateness of the current criterion under which a client is classified as retail or wholesale.

A summary table of the key FOFA measures and the scope of their application in relation to advice can be found below.

FOFA measure	Description	Scope/application
Ban on conflicted remuneration	A ban on conflicted remuneration structures, including commissions and volume-based payments	Provision of general and personal advice to retail clients
Compulsory renewal (opt-in)	A requirement for advisers to renew client agreement to ongoing advice fees every two years	Provision of personal advice to retail clients
Best Interests Duty	Requirement for advisers to act in the best interests of their clients	Provision of personal advice to retail clients only
Ban on soft dollar benefits	A ban on soft dollar benefits over \$300 per benefit	Includes provision of general and personal advice to retail clients
Basic banking products carve-out	Relief from best interests duty and ban on conflicted remuneration where employees of ADIs are selling their employer's basic banking products	The carve-out will apply in relation to general and personal advice in relation to the products mentioned