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Mr Shon Fletcher
Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
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Dear Mr Fletcher,

Future of Financial Advice (FOFA) reforms

The Australian Bankers' Association (ABA) appreciates the opportunity to provide comments to the inquiry into the *Corporations Amendment (Future of Financial Advice) Bill 2011* and *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011*, and accompanying Explanatory Memorandums ("FOFA legislative package").

1. Introductory remarks

The ABA supports the Federal Government's efforts to implement law reforms intended to improve the quality of financial advice, the regulation of financial planners, and the professionalism of the financial planning industry.

As part of the FOFA Peak Consultation Group and other discussions, the ABA has supported in principle an articulation of a best interests duty noting that many financial advisers (financial planners) have communicated and interacted with their clients on the basis that there is a common law obligation (fiduciary duty) owed to their clients. We have also supported in principle the banning of payments which are deemed to conflict the provision of personal advice to retail clients.

While the ABA recognises the changes contained in the FOFA legislative package are aimed at the business of financial planning, we are concerned about the breadth of the provisions and the prescriptive nature of the changes, especially with regards to the impacts on other parts of the industry, including retail banking and business banking. The FOFA legislative package will have significant implications and may result in adverse and unintended consequences across the banking and financial services industry, including undermining the policy intent of the FOFA reforms to broaden access to affordable financial advice.

The ABA believes that:

- Financial advice should be accessible and affordable;
- Financial advisers should be part of a trusted profession;
- Consumers should receive personal advice that is in their best interests;
- Financial services law should better accommodate the different advisory situations which relate to different types and classes of financial products; and
- Financial services law should not introduce price controls or interfere with remuneration structures within a banking business. Volume based and related performance payments between an employer and their employee should be permitted.

With these principles in mind, the ABA believes that it is important to ensure a balance between imposing additional regulation on banks and providing protections for consumers. Banks are already heavily regulated and there is significant additional regulation, both international and domestic, currently being progressed. There are numerous legal and regulatory obligations to ensure banks are managed prudently and to ensure banks provide their products and services in a transparent, accessible and responsible manner.

It is the ABA's view that a number of FOFA reforms could result in unnecessary regulatory burdens and additional compliance costs for banks and could therefore substantially increase the costs of banking for both banks and consumers. Additionally, certain FOFA reforms could conflict with one another – for example, banks are likely to have difficulty in implementing changes in a manner that does not adversely impact bank customers, bank staff and a bank's ability to improve the availability of different forms of financial advice, including 'simple' advice, general advice or 'scaled' advice (personal advice) on basic banking and financial products.

The ABA strongly advocates that the FOFA legislative package should not impact on the business of retail banking and business banking. With this in mind, we welcome the carve out for basic banking products as announced by the Government:

> 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 [*authorised*] Deposit-taking Institution (ADI) are advising on and selling their employer ADI basic banking products.[1]

However, the ABA does not believe that the FOFA legislative package is aligned with this stated policy intent. We consider that applying aspects of the best interests duty and conflicted remuneration provisions to basic banking products is inconsistent with Minister Shorten's policy announcement. It is essential for the legislative changes to target areas of concern without imposing unnecessary regulatory requirements and compliance burdens across the banking and financial services industry.

[1] Future of Financial Advice Information Pack. Section 2.8. 28 April 2011.

The ABA believes that the scope of the FOFA legislative package has extended significantly beyond the initial stated policy intent. The recommendations of the Parliamentary Joint Committee (PJC) Inquiry into financial products and services in Australia[2] were aimed at financial advisers (financial planners). However, the FOFA reforms have extended well beyond and consequently will result in a number of adverse and unintended consequences for banks and banking groups and their customers. Regulation should target identified market failures. However, we are not aware of any identified market failures, consumer detriment or systemic concerns regarding practices by banks in the offer of basic banking products or the provision of general advice by bank staff. We consider that the legal risks, regulatory burdens and compliance costs that will be imposed on banks as a result of the broad scope of the FOFA legislative package are unnecessary and inappropriate.

The ABA believes that the FOFA legislative package could have extensive implications for banks and banking groups where advice services are delivered via diverse corporate structures, internal licensee arrangements and business models. In the absence of clarifying and tightening the application of the proposed provisions, we consider that there could be significant adverse and unintended consequences for banking competition domestically and the contestability of the banking and financial services industry internationally. We are concerned that the FOFA reforms could result in banks having to substantially restructure their businesses in order to comply with the new law and/or significantly reduce choice for consumers and competition in the retail banking industry.

The ABA believes that the FOFA legislative package contains numerous drafting issues and anomalies which do not achieve the stated policy intent or result in impractical or costly compliance obligations. Additionally, the potential implications are exacerbated by the stated timing for compliance. In the absence of resolving and amending the application of the proposed provisions, addressing drafting anomalies and irregularities, reducing the logistical impediments and implementation costs, and adjusting the commencement date and transitional arrangements, we consider that there could be significant compliance and implementation issues for banks and banking groups. We are concerned that the FOFA reforms could significantly hinder innovation across the banking and financial industry and create substantial compliance and legal risks for banks, especially with regards to workplace, employee and remuneration arrangements.

The ABA recommends that the:

- Carve out for basic banking products must be clear and absolute. The law should reflect the stated policy intent and should not apply elements of the best interests duty or the conflicted remuneration provisions to basic banking products. (See sections 2 and 3 of this submission.)
- Scope of the FOFA reforms should target identified market failures. The law should not impose unnecessary and inappropriate obligations on banks and banking groups and should not apply to the provision of general advice. (See section 2 of this submission.)
- Timing for compliance should be adjusted to ensure the commencement date and transitional arrangements allow sufficient time for banks and banking groups to make the necessary and substantial changes required for compliance. (See sections 4 and 5 of this submission.)

[2] http://www.aph.gov.au/senate/committee/corporations_ctte/fps/report/report.pdf

2. FOFA and retail banking

The ABA notes there is no designation of a "financial planner" in the law. Therefore, applying the best interests duty and the conflicted remuneration provisions to all financial advisers arbitrarily will mean that a broad range of persons will be captured, including bank staff employed across the entire bank who provide financial advice on basic banking products. Importantly, this issue was recognised by ASIC:

> There is some misalignment between the common usage of the term 'financial adviser' and the legal concept of 'provider of financial product advice'. As a matter of law, a broad range of persons provide 'financial product advice'.[3]

Currently, some banks and other ADIs operate a 'no advice' model in their branches and call centres. Some banks operate by making use of the existing 'clerks and cashiers exemption' (section 766A(3) of the Corporations Act) to facilitate basic transactional services. Consequently, these banks do not provide customers with financial advice on basic banking products, but merely provide "factual information". While these banks meet their various legal obligations and their commitments under the Code of Banking Practice, these banks deemed that the FSR obligations attached to the financial advice regime were too onerous in a retail banking context and the compliance costs and systems required would unnecessarily increase the cost of banking for all customers.

Some other banks offer financial advice about retail banking products, including basic deposit products, general insurance, consumer credit insurance, non-cash payment facilities and first home saver accounts. These banks are required to meet the various FSR obligations attached to the financial advice regime, such as training requirements. Unfortunately, the FOFA legislative package could further exacerbate the compliance and legal risks for banks and the regulatory burden and costs imposed on banks. Ultimately, this could result in the expansion of 'no-advice' models across retail banking.

The ABA believes there is a need for certainty regarding the boundaries of the FOFA reforms. We do not consider that the policy intent was to capture all bank staff (including branches, call centres, etc). We are concerned that if bank staff are captured this could have significant ramifications for the business of retail banking and the availability of financial advice on retail banking products.

For example, imposing a best interests duty on bank staff would result in different rules applying to different staff and different financial institutions. Bank staff employed in banks that adopt a 'no advice' model will not have the duty. Whereas, bank staff employed in banks that offer financial advice will have the duty. Ultimately, this would result in administrative and regulatory complexity, compliance process and systems complications, employment arrangement consequences, inconsistency and inequality in the market, and overall, confusion for bank staff and bank customers. Additionally, a best interests duty seems to involve a much higher standard than what is required or expected in a retail banking context.

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[3] ASIC (2009). Submission to the PJC Inquiry into Financial Products and Services in Australia. Australian Securities and Investments Commission. August 2009. p108.
http://www.aph.gov.au/Senate/committee/corporations_ctte/fps/submissions/sub378.pdf

In practice, bank staff that provide bank customers with financial advice on basic banking products do so only on products and services offered by their bank. A bank teller or bank specialist can provide information about suitable deposit accounts offered by their bank to meet the bank customers' needs and provide current interest rate information associated with the deposit accounts offered by their bank. It is arguable that in doing so, the bank teller or bank specialist would be unable to meet the best interests duty. It would be nonsensical to assume that bank staff should be capable of providing advice on the myriad of accounts offered by other banks and ADIs or the myriad of interest rates which can change on a daily basis. Additionally, it would be nonsensical for bank staff to be expected to compare and provide advice on products offered by their banks' competitors.

Furthermore, in practice, bank customers do not expect retail banking staff to provide 'financial advice' and especially not advice on industry-wide products and services. (It should be noted that there are existing information repositories and websites that provide comparison data, e.g. information on the current deposit products and applicable market rates.)

Consequently, banks that provide bank customers with financial advice may be required to restructure their business and/or alter their distribution model – this could result in no financial advice being provided through bank branches and call centres, and possibly result in a reduction of products and providers in the market. We consider this an undesirable outcome and would be contrary to the policy intent of the FOFA legislative package to broaden the availability of simple advice for consumers or for financial advice to be scalable to the needs of consumers as well as contrary to the efforts of the Government to ensure competition within the banking industry.

The ABA is concerned that requiring bank staff to meet a best interests duty and the conflicted remuneration provisions is likely to have adverse and unintended consequences for banks and banking groups and result in:

- Complicated regulatory requirements and compliance processes and systems;
- Greater legal and operational risks for banks;
- Altered remuneration arrangements and business operations for banks and bank employees;
- Convoluted bank-customer relationships and poor customer experience; and/or
- Less information and 'simple' advice being made available through banks to Australian consumers.

The ABA believes that implementation of the FOFA reforms must exclude bank staff and bank specialists providing advice on basic banking products (similar to the exclusion of these products from the SOA disclosure requirements and consistent with the Government's policy announcement). If the FOFA reforms apply to bank staff offering or providing advice on banking products, the policy intent would be diluted and its efficacy reduced. Furthermore, the cost of providing banking products and services would be unnecessarily increased to the detriment of retail and business banking customers. For those banks that do not have a 'no advice' model, we consider it is vital to avoid introducing additional and unnecessary regulatory obligations. In fact, we consider that it is important to encourage banks to offer advice services so that more Australian consumers have access to simple, affordable financial advice.

2.1 Basic banking products

It is the ABA's view that the FOFA reforms should not apply to basic banking products, which is consistent with Minister Shorten's announcement on 28 April 2011. Specifically, we note the commentary about the carve out for 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.[4]

Despite this policy announcement, the Bill does not adequately carve out basic banking products or bank staff. The "carve out" as currently drafted is impractical and limited because retail banks operating in Australia offer basic products and provide basic advice services not merely relating to products defined as "basic banking products" and by staff not defined as "agents or employees of an ADI." For example, under section 961B(3) the carve out for basic banking products from the best interests duty will not apply unless the subject matter of the advice provided is solely on a basic banking product. Similarly, under section 963D the carve out for basic banking products from the conflicted remuneration provisions will not apply if advice is also given on a product that is not a basic banking product.

The ABA is concerned this would likely result in banks restructuring their retail banking service model where customers would be required to speak to different staff for different products. Ultimately, this would not deliver customers optimum streamlined services or products. Customers would no longer have access to a one-stop-shop retail banking service or access to convenient, bundled products – even organising direct debits from a transaction account to another financial or non-financial product would become more complicated for bank customers.

The ABA strongly advocates that the treatment of basic banking products in the law should reflect the fact that:

- These products are simple and well understood;
- The advice situations associated with the offer of these products is simple and straight forward;
- The banks and other financial institutions providing these products already have sophisticated compliance systems and appropriate consumer protection frameworks;
- The expectations of consumers when interacting with their bank and seeking to purchase or obtain advice on these products is they can do so with ease and in ways convenient to them; and
- There has not been any evidence of a market failure in the offer of banking products and services by bank staff.

[4] Future of Financial Advice Information Pack. Section 2.8. 28 April 2011.

The ABA is concerned that applying elements of the best interests duty and associated provisions and the conflicted remuneration provisions would impose additional and unnecessary legal obligations and restrictions on banks and other ADIs. This could result in banks and other ADIs adopting 'no advice' models to avoid having to introduce new and convoluted compliance systems and having to pass on additional costs to their customers. Ultimately, this would result in decreasing the availability of advice, rather than increasing access to affordable advice services.

2.1.1 Definition of basic banking product

The ABA notes that section 961F defines a "basic banking product" as a basic deposit product, non-cash payment facility, first home saver account, traveller's cheque, or other product prescribed by regulations. We welcome the ability to prescribe by regulations additional products as this provides flexibility for product innovation.

The ABA believes that the Explanatory Memorandum should be amended to define basic banking products as including:

- All types of at-call accounts – it should be clarified that the carve out specifically includes transaction accounts, savings accounts, and cash management accounts.
- All term deposit accounts – it should be clarified that the carve out specifically includes all term deposit products with a term less than 5 years[5].
- All basic banking products and non-financial products – it should be clarified that the carve out specifically includes the offer of basic banking products, other exempt products (e.g. general insurance), other exempt products made by regulations, and non-financial products (e.g. credit products). Additionally, it should be clarified that the carve out specifically includes deposit products bundled with a credit facility (e.g. a debit account with an overdraft facility)[6].

Furthermore, the ABA believes that the proposed provisions duty should not impede the provision of basic banking products across different business and distribution models. Therefore, the Explanatory Memorandum should be amended to clarify that financial services (e.g. ATMs, facilities, devices and infrastructure) used to execute retail banking transactions and associated with the offer of basic banking products are exempt.

The ABA recommends that the Explanatory Memorandum should be amended to clarify that the exemption for basic banking products includes all types of at-call accounts, term deposit accounts, basic banking products offered along with other exempt products and non-financial products, and financial services associated with the offer of basic banking products.

[5] The ABA notes that this approach would ensure that banks are able to offer term deposits with a term less than 5 years via bank staff and bank specialists while obviously meeting their other legal obligations in respect of these accounts, including training and disclosure. Bank customers rarely require personal advice on these products, even though the offer of these products can trigger the legal definition of personal advice within the law. Clarifying the application of the carve out for term deposits would mean that if bank customers seek personal advice, this advice service remains available within the market. Importantly, this would mean that banks are able to continue to meet their business and prudential requirements, including managing their balance sheet, meeting their financial obligations, and implementing strategies to deal with business exposures, risk, liquidity and capital management. It is essential that banks have ready access to term deposits for the purposes of meeting the funding needs of the Australian economy (and the pending implementation of the Basel III standards).

[6] The ABA notes that this approach would ensure that bank staff and bank specialists would continue to be able to sell, or advice on, basic banking products. In the absence of clarification, it is likely that banks will have to entirely restructure their retail banking services. In practice, bank customers will no longer be able to readily access basic services at a branch or via a call centre and receive information and/or advice across their suite of retail banking products. Instead customers will have to speak to individual staff about individual products. This would result in convoluted compliance systems and procedures for banks and poor customer experience.

Definition of basic deposit product

The ABA notes that the definition of a basic deposit product is defined in section 761A of the Corporations Act. A basic deposit product is deemed to be a "basic banking product" (section 961F). However, the definition of a basic deposit product is uncertain due to new prudential standards (specifically, Basel III standards which have been developed in response to the global financial crisis and incorporate new standards for liquidity risk). We are concerned that a narrowing in the category of deposits deemed to be basic deposit products has significant implications for banks and other ADIs and consumers. (It should be noted that the ABA has provided comments on ASIC's Consultation Paper 169: *Term deposits that are only breakable on 31 days' notice: Proposals for relief*.)

The ABA recommends that section 761A should be amended to:

- Clarify that term deposits up to two (2) years, where early withdrawal is at the discretion of the bank or other ADI, are basic deposit products.
- Clarify that term deposits up to five (5) years, where early withdrawal is at the discretion of the depositor, with a notice of withdrawal period, are basic deposit products.

2.1.2 Carve out for basic banking products

The ABA notes that section 961B(3) exempts advice solely on basic banking products from the best interest duty where a provider satisfies the elements of the duty in subsections 961B(2)(a)-(c) and subsection 963D(b) exempts a benefit from the conflicted remuneration provisions where the benefit is solely dependent on recommending a basic banking product. While we welcome the carve out, we consider the exemptions in these sections are impractical in application.

Bank staff do not only provide advice on financial products regulated by the Corporations Act, but on a number of products across the bank's entire product range, including products regulated under the *National Consumer Credit Protection Act 2009*. We note that this approach provides customers with a better service in terms of discounts and lower prices as well as a one-stop-shop for all their banking and finance needs.

Bank staff may provide information or advice to a customer on a basic banking product (e.g. transaction account) and also on a credit product (e.g. home loan). As currently drafted, this situation would result in the full best interests duty obligations applying and the employee not being able to receive an annual performance bonus or a payment relating to the offer of the basic banking product.

Bank staff may provide information or advice to a customer on a basic banking product (e.g. savings account) and also on a non-basic banking product (e.g. general insurance product). Even though the general insurance product is carved out of the conflicted remuneration provisions, as currently drafted, the fact that the employee gave information or advice also on a non-basic banking product means this would result in the full best interests duty obligations applying and the employee not being able to receive an annual performance bonus or a payment relating to the offer of the basic banking product or the general insurance product.

Subject to comments in section 3.1.1 of this submission, the ABA believes that section 961B(3) should be amended to carve out basic banking products where the subject matter of the advice is 'in relation to' a basic banking product (but not solely in relation to a basic banking product). Similarly, subsection 963D(b) should be amended so that access to the benefit is dependent on the licensee or representative recommending a basic banking product (but not solely dependent).

Additionally, subsection 963D(c) should be amended so that the licensee or representative does not give financial product advice that does not relate to basic banking products, or products as defined in section 963B or prescribed by regulations, or non-financial products. We consider that this drafting anomaly should be corrected so that the payment of a benefit from a bank to their "employee" is permitted where the payment relates to the offer of a basic banking product or exempt product or non-financial product.

2.1.3 Definition of employee

The ABA notes that section 961B(3) exempts an "agent or employee of an Australian ADI" from the best interests duty and section 963D exempts benefits for work carried out by an "agent or employee of an Australian ADI" for recommending basic banking products from the conflicted remuneration provisions. We welcome the carve out and the ability for banks to adopt flexible workplace arrangements, including employee, agency and franchise arrangements. However, we consider that these sections do not provide sufficient clarity regarding these arrangements. All staff and representatives of an ADI, irrespective of their workplace arrangements, should be exempt. Additionally, these sections do not adequately address the consequences of banks which operate without a branch network or via a corporate structure with related bodies corporate or companies or wholly owned subsidiaries of the ADI offering retail banking services.

The ABA believes that section 961B(3) should be amended to carve out basic banking products from the best interests duty where the information or advice is provided by an agent, employee or representatives of an ADI or otherwise acting by arrangement with an ADI under the name of the ADI or employees of subsidiaries of an ADI. Similarly, section 963D should be amended to carve out benefits for recommending basic banking products where the benefit is paid by a licensee or representative to their "employee".

Additionally, the Explanatory Memorandum should be amended to take into account numerous employment arrangements, business models and corporate structures that may be applicable to the offer of basic banking products (i.e. franchisees, community banks, agents, contractors, intra-group arrangements, mobile banks, and other non-traditional distribution and channel arrangements). We submit that the Explanatory Memorandum should clarify that all staff and representatives which sell or recommend products on behalf of the bank are included in the carve out. Specifically, the carve out should include:

- employees, agents and representatives of the bank (including employee, agency and franchise arrangements);
- persons acting by arrangement (including contractors who work on behalf of the bank);
- employees of employment agencies who may be temporarily working for the bank;
- employees of a related body corporate or company to the ADI;
- employees of wholly owned subsidiaries which may not be an ADI; and
- employees of another company who work exclusively for the bank.

Furthermore, the ABA believes that the duty should not impede the provision of basic banking products via non face-to-face banking models. Therefore, the Explanatory Memorandum should be amended to clarify that banking distribution and channels arrangements (e.g. Internet banking, mobile bankers) associated with the offer of basic banking products are exempt.

The ABA believes that in the absence of these clarifications, some banks would not have the benefit of the carve out for basic banking products, which may cause distortions in the retail banking industry and may have adverse effects for banking competition.

The ABA recommends that section 961B(3) and section 963D should be amended so that the only qualifications on the carve out for basic banking products are:

- that the subject matter of the advice is 'in relation to' a basic banking product (but not solely in relation to a basic banking product);
- the advice is provided by, or the work is carried out by, an employee, agent or representative of an ADI, or a person or company otherwise acting by arrangement with an ADI under the name of the ADI, or an employee of a subsidiary of an ADI;
- in the case of s963D(b) – access to the benefit is dependent on the licensee or representative recommending a basic banking product... (but not solely dependent); and
- in the case of s963D(c) – licensee or representative does not, in the course of recommending a basic banking product, give financial product advice that does not relate to basic banking products, or risk insurance products (general and life insurance), or products as prescribed by regulations, or non-financial products.

2.2 General advice

The ABA notes that while the provisions on the best interests duty relate only to personal advice, the conflicted remuneration provisions apply to benefits relating to personal advice, general advice and the distribution of financial products.

While the Government announcement in April 2011[7] indicated that the conflicted remuneration provisions would capture personal advice and general advice, the original aim of the FOFA reforms, as based on the Parliamentary Joint Committee (PJC) Inquiry into financial products and services in Australia, was to target concerns with the provision of financial advice to retail investors (i.e. personal advice) where there was a risk of retail investors receiving conflicted advice. We are concerned that the scope of the FOFA reforms has extended significantly and this could have substantial implications for the provision of financial product advice across the spectrum of financial products, and in particular the provision of general advice.

The ABA believes that business models and remuneration structures should not be prohibited where they do not result in a negative outcome for the provision of personal advice to a retail investor, and therefore the FOFA reforms should not apply to general advice. By definition, general advice does not take into account a person's needs or objectives and must be accompanied by a warning indicating that the advice does not consider the client's individual personal circumstances, and hence the client should consider their personal circumstances and the accompanying disclosure documents before making a decision.

[7] Future of Financial Advice Information Pack, 28 April 2011.

Furthermore, the ABA believes that general advice may have an informative purpose, without including product specific advice, and is often available to the consumers through various channels, including websites, product brochures, media advertising, seminars, newsletters and market reports. Given the wide range of circumstances in which general advice is given, including for educational purposes, the opportunity for unintended consequences is increased, whereby situations are caught by the law when it is neither necessary, nor intended. We submit that general advice is given in a much broader set of circumstances than personal advice, and by its nature would not result in the issues and concerns outlined in the FOFA legislative package.

The ABA is advised by member banks that only around two in five Australians are seeking financial advice. Many Australians do not seek financial advice because of issues related to affordability and the limited availability of 'simple' advice. Additionally, some Australians living in rural and regional areas face additional difficulties in accessing advice services. Many do not have ready access to financial planners. Banks and banking groups with large distribution models, targeted advisory services, and various channel arrangements are well-positioned to fill this gap in the financial advice market. Australia's ageing population means it is vital that Australians have access to some form of financial advice. While we welcome the introduction of a 'scaled' advice model, we are concerned that the treatment of basic banking products, coupled with the breadth of the conflicted remuneration provisions, will restrict the ability for banks to offer innovative advice services.

The ABA recommends that the FOFA legislative package should not apply to general advice and should encourage the adaptation of the 'scaled' advice model, especially in circumstances where a bank customer contacts their bank via frontline bank staff or bank specialist or bank website to discuss or seek information about one or more of that bank's products.

3. Specific comments

3.1 Best interests duty

3.1.1 Elements of the best interests duty – basic banking products

The ABA welcomes the carve out for basic banking products in section 961B(3) (as well as the carve out for general insurance products in section 961B(4)). However, we are concerned that the carve out is not clear and absolute and would impose additional obligations on banks than what is currently contained in the law.

The ABA notes that the Bill repeals section 945A (requirement to have a reasonable basis for advice) and section 945B (requirement to warn a retail client if advice is based on incomplete and inaccurate information). For this reason, we assume that the elements contained in subsections 961B(2)(a)-(c) attempt to identify specific process steps and in doing so generally restate the current 'know your client', 'know your product', and 'appropriateness' requirements. Furthermore, while we welcome the commentary in the Explanatory Memorandum regarding the intended application of the elements of the best interests duty to basic banking products, we are concerned that the elements contained in subsections 961B(2)(a)-(c) could significantly extend the obligations for bank staff and bank specialists.

The ABA believes that the law should:

- Not impose unreasonable and unnecessary obligations on banks with regards to advice about basic banking products – this is both consistent with the Government's announcement in April 2011 and the Government's stated policy of making advice more accessible and affordable ('scaled' advice). These products are simple and well understood and associated with the provision of retail banking services. Consumers want access to low-cost, banking products and simple, low-cost financial services.

- Encourage banks to offer advice on these products, rather than create legal uncertainties, and ultimately restrict the possibility of 'scaled' advice or indeed result in the further expansion of 'no advice' models (factual information only). (It should be noted that deposit products already have a history of different regulatory treatment in financial services regulation and are subject to the guarantee (which banks will pay for via the Financial Claims Scheme)).

- Not result in a disjointed, haphazard or poor customer experience whereby unnecessary administrative complexity frustrates the provision of information or advice to bank customers. (It should be noted that, in practice, if bank staff and bank specialists are only able to provide advice via a personal advice model, this would require significant restructuring of existing retail banking businesses.)

Retain and clarify the reasonable basis for advice test in terms of basic banking products

The ABA believes that sections 945A and 945B should not be repealed. Instead the law should be amended so that the 'reasonable basis for advice test' applies only to basic banking products, general insurance products and products as prescribed by regulations. This would preserve the existing obligations and clarify the requirement for advice on basic banking products to be "reasonable" and "appropriate", and unless specified, apply the best interests duty to all other financial products. Furthermore, the law should not impose obligations that extend beyond the current requirements and should clarify that it is not reasonable or necessary for staff of banks or other ADIs to obtain additional information from their customer, to provide more than their customer has requested, or to consider other products that might also achieve the customer's needs and objectives. Banks and other ADIs have implemented compliance systems and procedures to reflect the existing provisions of the law, as required and as relevant to their business model and distribution arrangements.

The ABA suggests that section 945A(1) of the Corporations Act should be amended as follows:

(1) "For the subject matter of the advice, a providing entity must only provide the advice to the client if:" [and then proceed with the current wording].

The amendment should also be explained in the Explanatory Memorandum with the following:

> "The amendment is made to clarify that the subject matter of personal advice can be a single issue such as a particular objective or need, an aspect of a single financial product or a single topic. The scope of personal advice can be agreed between a customer and a providing entity or can be offered on a limited basis. Inquiries, under section 945A can be tailored to the scope of the advice to be provided."

The ABA also suggests that section 945A (as set out above) should be accompanied by an additional provision to subsection 945A(2) of the Corporations Act:

> "Where it is clear in the provision of the advice that only certain types of products or identified objectives are to be considered, the provider need only obtain personal and other information that is relevant to the subject matter of the advice under consideration."

The ABA recommends that the existing reasonable basis for advice test should be retained for basic banking products, rather than applying the elements subsections 961B(2)(a)-(c). The existing provisions should be clarified to apply to basic banking products, general insurance products and products as prescribed by regulations, and in doing so facilitate and promote access to 'scaled' advice.

3.1.2 Elements of the best interests duty – basic financial products, and simple advisory situations

The ABA notes that section 961B(5) provides a regulation making power to prescribe a class of financial products or sub-class of financial products as defined to meet certain elements of the statutory best interests duty, steps the provider must take in addition or in substitution or is not required to take, and circumstances where the duty does not apply. We welcome the inclusion of a regulation making power to ensure that the law can be amended to respond to innovation in the offer of basic financial products and the provision of 'simple' advice and limited advisory situations.

The ABA believes that it is important to ensure that other basic financial products can be exempt from the provisions where it is deemed appropriate. For example, we consider that with regards to less complex financial products (i.e. simple insurance, investment and superannuation products), which are typically distributed through bank branches and other bank distribution and channel arrangements, it is unreasonable and unnecessary for all the elements of the best interests duty to be applied, and therefore these products should be treated similarly to basic banking products and general insurance products. In these instances, clients' expectations could range from seeking only factual information or general advice from bank staff to receiving only limited advice or personal advice via readily available banking arrangements and distribution channels.

The ABA believes that the law should encourage the offer of basic financial products and the provision of 'simple' advice, especially in circumstances where the client contacts their bank via frontline bank staff, bank specialist, bank financial planner or their bank's website and simply wants to discuss (factual information or financial product advice) the appropriateness of one or more of that bank's products. Furthermore, the law should encourage innovation and specialisation in the offer of basic financial products.

The ABA supports a regulation making power as a mechanism to make appropriate adjustments to the best interests duty.

3.1.3 Elements of the best interests duty – financial products

The ABA supports a duty for advisers to act in the best interests when providing personal advice to retails clients and to give priority to the interests of those clients in the event of a conflict of interest. We consider that the duty should define the application of the duty and articulate the elements of the duty.

However, the ABA believes that the best interests duty as currently drafted is likely to create legal uncertainties and compliance risks for banks and banking groups, including:

- The duty is undefined and the terminology is unclear. This legal uncertainty will create significant compliance risks for banks and other financial service providers.
- The duty does not contain a reasonable steps defence. In practice, in the absence of a reasonable steps qualification an adviser is required to exercise all judgements and take all steps in order to comply with the duty.
- The duty does not allow a provider to scope the advice. In practice, in the absence of a clearly defined duty and conduct steps a provider is unable to offer 'scaled' advice.

Definition

The ABA believes that the statutory best interests duty should contain a comprehensive definition to provide certainty for advisers and consumers as to the obligations of advisers in providing personal advice to retail clients. Section 961B(1) has not defined what "best interests" means. We consider that the duty must be clearly defined in the law and its application clearly outlined in the Explanatory Memorandum to avoid confusion and incorrect assumptions or interpretations.

> The ABA recommends that section 961B(1) should be amended to define the best interests obligation so that a provider has reasonable certainty in relation to what they must do to comply with the duty. It is essential that the law offers certainty in relation to the interpretation and practical application of the duty by licensees and advisers.

Reasonable steps qualification

The ABA notes that the Government announcements in April 2010 and 2011 stated that the best interests duty would include "a reasonable steps qualification so that advisers are only required to take reasonable steps to discharge the duty"[8] and "are not expected to base their recommendations on an assessment of every single product available in the market"[9].

However, the Bill does not provide a "reasonable steps defence". Notwithstanding, under the current drafting a provider must take reasonable steps to ensure it complies with the best interests duty and associated provisions. Additionally, a provider is required to base "all judgements in advising the client on the client's relevant circumstances" (s961B(2)(f) and take "any other steps that would reasonably be regarded as being in the best interests of the client" (s961B(2)(g)). These obligations are non-exhaustive and involve interpretative professional judgement which may differ.

[8] Future of Financial Advice Information Pack. 28 April 2011. page 12.
[9] Future of Financial Advice Information Pack. 26 April 2010. page 5.

The ABA believes that subsections 961B(2)(f)-(g) as currently drafted places an unreasonable duty on a provider to establish that all judgements have been made and all steps have been taken. It is not reasonable for an adviser to be required to consider all products available in the market, including products for which the adviser may not be licensed, authorised or competent to assess and/or recommend. We consider that a reasonable steps qualification must be included in the Bill. The law should be clarified that if a provider acts reasonably in the circumstances and complies with the elements of the duty contained in section 961B(2) that they are taken to have complied with section 961B(1).

The ABA recommends that the best interests duty should explicitly contain a reasonable steps qualification where the adviser has acted reasonably based upon the information that is available at the time the advice is given and in the circumstances. Alternatively, the duties should be drafted conversely and identify what a provider must not do and thereby establish the grounds for a defence in relation to enforcement or court action.

Elements of the statutory best interests duty

The ABA believes that the statutory best interests duty is problematic. It is essential that banks and other financial service providers have certainty regarding their legal obligations. We note that the steps in section 961B(2) are additional to the duty an adviser owes their client under common law fiduciary obligations.

The ABA submits that subsections 961B(2)(a)-(c) must be amended (especially if these elements are to apply to basic banking products), so that a customer or client is able to agree the scope of the advice and so that a provider is not required to determine or verify information provided by the customer or client.

In practice, the absence of a defined duty and the way the duty is currently drafted prevents a consumer from seeking advice only on a product. The provider would have to provide advice where the scope of the advice is in the best interests of the consumer and the recommendation is in the best interests of the consumer. For example, a client wants advice on a savings product. However, a savings product may not be in the broader best interests of the client, instead it may be in the best interests of the client to reduce their home loan. The provider would be prevented from providing advice limited to the savings product. We consider that section 961B(2)(b) should be amended to clarify that a consumer is able to agree to the scope of the advice.

In practice, the uncertainty as a result of the current drafting of the duty implies a provider must validate the information provided to them by the client. For example, a client wants advice on a savings product attached to their credit facility (i.e. home loan). The client provides information about the value of their home along with other information about their personal circumstances and financial situation. It is unclear the extent to which a provider is expected to validate the information provided by the client. However, it may be interpreted that the provider would be required to verify the information provided by the client (i.e. the value of the home) by validating against external sources to establish whether the information is inaccurate and/or be required to conduct additional investigations into the objectives, financial situation and needs of the customer and into all products in order to establish whether the information is incomplete. This would require substantial resources and time and extends significantly the advice service offered by banks. We consider that section 961B(2) should be amended to clarify that a provider is not required to validate the information provided by the client.

The ABA recommends that section 961B(2) should be amended to clarify the scope and nature of the duty in terms of the ability to limit the scope and subject matter of the advice. Bank staff should not be required to verify information provided by the customer where the limited advice given is in relation to basic banking products. Bank staff should be able to meet the best interests duty by providing advice only on those products offered by their bank/banking group (including subsidiaries) and not be expected to compare products offered by other banks/banking groups, subject to appropriate warnings. Additionally, section 961E should be deleted.

Furthermore, the ABA recommends that section 961B should be amended to clarify that where a provider has complied with the best interests duty, it will be deemed that they have complied with their common law obligation (fiduciary duty).

The ABA notes the submission prepared by the Financial Services Council (FSC) and we support the specific recommendations and drafting suggestions to address the legal, technical and practical concerns associated with the best interests duty.

Scaled advice

The ABA supports the reform to expand the availability of simple, low-cost advice and improve the affordability of financial advice. The provision of accessible and affordable advice is important to ensure that the many Australians who do not have adequate knowledge/skills or information have greater opportunities to access the relevant knowledge/skills or information to assist them make informed decisions about their savings and investment options.

Currently, a number of banks are:

- *Providing personal advice to bank customers*: Personal advice might be the consequence of information provided by a bank teller or bank specialist to the customer or vice versa. However, we consider that consumers do not expect their interactions with bank staff in branches and call centres to be administered or regulated in the same way as financial advice provided by a financial planner. For example, member banks advise that a common frustration for bank customers is when a bank teller is unable to complete a transaction, such as open a bank account, because depending on the situation, the personal advice regime may be triggered. In this instance, the bank customer is required to complete the transaction with a bank specialist or bank customer relations manager.

- *Providing free consumer education and general advice*: Financial information and general advice might be provided via a number of different distribution channels, including via banks' websites, seminars and workshops, information and materials, etc. Recently announced ASIC policy regarding online disclosure should allow further opportunities for banks to develop innovative ways of distributing financial information and simple advice. However, we consider there are a number of further changes required to facilitate the greater availability of advice on basic, retail banking products and non-product specific advice.

The ABA believes that better identification of the stratification of financial advice is necessary. In the short-term the focus of reforms should be initially to provide legal certainty around the provision of limited personal advice. In the medium to longer-term, we continue to advocate a change to the definition of personal advice.

It is the ABA's view that the FOFA reforms should explicitly allow 'scaled' advice, which is consistent with Minister Shorten's statement on 8 December 2011. Specifically, we note the commentary about the importance of 'scaled' advice:

> The delivery of scaled advice is critical to achieving the Government's objectives of promoting greater access to financial advice. This Government is committed to providing advisers with certainty of how to provide this form of advice in a way that meets their regulatory obligations[10].

The ABA believes that the law should recognise the provision of 'scaled' advice and that it is not reasonable or necessary for an adviser to obtain additional information from their client, or provide more than their client has requested, or to consider other products that might also achieve the client's needs and objectives. Furthermore, the law should recognise the provision of advice via non face-to-face models. The implementation of a new 'scaled' advice framework is likely to provide opportunities for industry to tailor and target their advice offerings to the needs of their retail customers and clients. However, the best interests duty is intrinsically linked to the ability for advisers to offer 'scaled' advice and comply with the law. The duty as currently drafted does not permit an adviser to act on the client's instructions or permit the client and the adviser to agree on the scope and subject matter of the advice while still acting in the best interests.

The ABA believes that the inability to scope the advice will impede the ability for banks and other financial service providers to offer 'scaled' advice and discourage innovation and specialisation in the provision of simple, low-cost advice. Ultimately, the ability for advisers to provide clients with cheaper and/or better access to advice services will be hindered. In the absence of the ability for an adviser and their client to limit the scope of the advice, including agreeing the subject matter of the advice, clients would be unable to select the advice service they want and advisers would face greater difficulty in managing costs of the advice service provided. (It should be noted that the ABA has provided separate comments on ASIC's Consultation Paper 164: Additional guidance on how to scale advice.)

Furthermore, the duty as currently drafted creates an uneven playing field (regulatory arbitrage) between financial advisers regulated under the FOFA reforms and superannuation fund trustees and related service providers under the "intra-fund advice" regime. (See section 6 of this submission.)

The ABA recommends a number of initiatives to improve access to 'limited personal advice' and refine the FSR regime to better accommodate, and treat more consistently, basic financial products and simple advisory situations. Specifically, we consider that section 961B(2) must be amended to explicitly provide the ability to offer 'scaled' advice. Furthermore, we consider that amendment of the *Corporations Act 2001* is necessary if certainty is to be provided and barriers to the availability and accessibility of limited personal advice are to be reduced. Law reform must facilitate limited personal advice and start to address the inherent supply and demand issues associated with the delivery of advice across the spectrum of advisory situations and different types and classes of financial products.

[10] Minister Shorten MR164 "Improving Access to Simple Financial Advice", 8 December 2011.

Calculators and computer programs

The ABA believes that the law should not hinder the ability for banks and other financial service providers to offer advice services via technology solutions, including through Internet banking or mobile banking, and via tools and calculators on bank's websites, computer programs and applications on mobile phones, tablet computers, etc. We welcome that the Bill (s961(6)) and the Explanatory Memorandum contemplate facilitating the provision of personal advice via a calculator or computer program. We consider that non face-to-face models of advice will be an important way to provide simple, low-cost advice and fill the gap in the financial advice market.

However, the ABA believes that the best interests duty does not permit the scope of the advice to be determined by the provider and only allows advice to be scaled by the client, which is not possible where the client is accessing advice online via a calculator or computer program. The current drafting presents a number of practical difficulties in matching a technology solution to the application of the duty. For example:

- A computer program cannot comply with a broad undefined duty to act in the best interests of the client. A computer program needs parameters by which to operate and given it is not clear what this duty means, a computer program will have no ability to comply with it.
- A computer program is unlikely to be able to determine whether information entered by a client is inaccurate.
- A computer program will not always be able to determine whether it is reasonable to consider recommending a financial product.
- A computer program cannot take any other step that would reasonably be regarded as being in the best interests of the client.

The ABA believes that where technology programs and applications are used to provide advice, the provider must be able to limit the scope of the advice. We consider that the law should be clarified so that the duty can apply to the scope of the advice as agreed and to an approved product list.

The ABA recommends that:

- The duty must explicitly enable 'scaled' advice and its operation clearly outlined in the Explanatory Memorandum to avoid confusion and incorrect assumptions or interpretations.
- The duty must explicitly accommodate the provision of advice being scoped by a person providing advice via a calculator or computer program.

3.1.4 Clarify in terms of "reasonable investigation"

The ABA notes that the Bill imposes an obligation on the provider to conduct a "reasonable investigation" into financial products that might achieve relevant client objectives and that also might meet relevant client needs. We note that section 961D defines "reasonable investigation". We welcome that the Bill and the Explanatory Memorandum clarify that a provider would not be required to conduct an investigation into all products available in the market.

However, the ABA believes that section 961D should be clarified. The duty should only require an adviser to assess products that might "meet" the needs and objectives relevant to the subject matter of the advice, and only where recommendations are to be made, and by reference to the client's personal circumstances. We consider that the law should be clarified to ensure that an adviser is not required to investigate all products that might "achieve" the client's needs and objectives.

The ABA recommends that section 961D should be amended to clarify that a provider is required to conduct a reasonable investigation into the financial products that might meet the client's needs and objectives.

3.1.5 Clarify in terms of an additional appropriateness test

The ABA believes section 961G should be clarified. The law should not require a bank or other ADI in practice to only provide holistic financial advice – that is, it would be unreasonable and impractical for bank staff (branch tellers, call centre staff, bank specialists or bank financial planners) to be required to investigate all products available in the market or to recommend products offered by their banks' competitors. Furthermore, the law should be clarified to ensure that the adviser provides advice exercising care and with regard to the client's instructions.

Currently, section 945A of the Corporations Act explicitly relates appropriateness of the advice to the investigation of the subject matter which is reasonable in the circumstances. We consider that the appropriateness test should be clarified to reflect other provisions which do not apply to banks and other ADIs in relation to basic banking products. Furthermore, the law should be clarified for other financial products having regard to the information that the bank or other financial services provider knows, or would have known, to satisfy the best interests duty.

The ABA recommends that section 961G should be amended to explicitly relate the provision of advice by a person with relevant expertise exercising care and having regard to the client's instructions.

Furthermore, the ABA recommends that the law should be clarified so that an employee, agent, or representative of a bank or other ADI satisfies section 961G if they satisfy the test/duty.

3.2 Opt-in obligation

The ABA supports transparency of fees and disclosure of fees paid by consumers for financial products and services. However, we consider that the opt-in obligation as currently drafted is problematic – the Renewal Notice provisions are inflexible and the Fee Disclosure Statement is highly prescriptive. We are concerned that the proposed opt-in obligation is likely to result in increased administrative complexities and costs for advisers. Therefore, we believe that the opt-in obligation provisions should be amended.

3.2.1 Apply only to new clients of the adviser

The law is inconsistent with the Government's announcement and the exposure draft legislation released on 29 August 2011. We consider that the law should clarify the grandfathering provisions and the definition of client. The opt-in obligation, including the Fee Disclosure Statement, should apply prospectively to new clients. Additionally, the opt-in obligation (Renewal and Fee Disclosure Statement) should carve out 'legacy products', including products that are no longer open or issued to new members/investors.

3.2.2 Allow the sale or transfer of business

The law should allow for the sale or transfer of all or part of an "advice business" without triggering a new "ongoing fee arrangement". Specifically, we consider that section 962 should be amended to apply to an ongoing fee arrangement which moves between authorised representatives/representatives within the same licensee or moves between licensees upon sale or transfer or where there is a continuation of the contractual terms of the original arrangement.

3.2.3 Apply to fees relating to the provision of personal advice to retail clients and ongoing fee arrangements

The law should clarify that the opt-in obligation should apply to an "ongoing fee arrangement" where a fee is to be paid ongoing for a period longer than twelve (12) months and which is provided to the licensee or representative for the provision of personal advice. For example, the opt-in obligation should explicitly exempt ongoing account keeping or service fees applicable to the provision of basic banking products, retail banking services, and other financial products. These product fees and charges or transactional fees can relate to financial services and non-financial services as well as execution-only services, and not limited to advice services. Additionally, the opt-in obligation should not apply to insurance premiums and insurance commissions included in premium for risk insurance products (general and life insurance) (s962A(4)).

3.2.4 Allow an adviser to implement the opt-in process in a way that suits the manner in which the adviser, and their client, currently communicate and interact

The law should allow for a Fee Disclosure Statement and Renewal Notice to be provided by an adviser to their client in flexible manner and suitable time (i.e. at least annually or every two years from the commencement or establishment of the ongoing fee arrangement or the last renewal notice, respectively). Specifically, we consider that section 962G should be amended to remove "must, within a period of 30 days beginning on the disclosure day" and insert "at least annually" and section 962K should be amended to remove "must, within a period of 30 days beginning on the renewal notice day" and insert "at least once every two years".

3.2.5 Allow a client to advise instructions

The law should permit a client to advise their adviser of instructions using a range of methods, including in-writing and via electronic methods and technologies (i.e. email, facsimile, SMS, online facility, etc). Specifically, section 962M and section 962N should be amended to ensure that any client instruction can be captured and accepted, including in-writing, technologies or recordable methods.

3.2.6 Clarify "give" and "send"

The law is inconsistent in the use of the terms "give" and "send" with regards to the Fee Disclosure Statement and the Renewal Notice. Document(s) may be given to a client at a face-to-face meeting or sent to a client via electronic methods and technologies. Advisers should have the ability to give their client these document(s) in a flexible manner and to adopt circumstances appropriate in discharging their opt-in obligation. We consider that the term "give" defined in section 940C should be extended to apply to section 962G and section 962K. Any requirement should be clear that it refers to contact being made on a best endeavours basis (e.g. mailed to the client's postal address or emailed to the client's email address).

3.2.7 Consequences if a client notifies they do not want to opt-in (renew)

The law should allow sufficient time for the fee recipient to terminate arrangements upon request. Section 962M should be amended to provide that the arrangement terminates 30 days after the day on which the notification is received. We consider that this would be more consistent with section 962N and provide the fee recipient time to calculate outstanding fees and terminate the arrangement. It should be clarified that the 30 day period commences when the notification is received by the fee recipient as opposed to the day when it is "given" by the client (as the fee recipient will not always be able to determine when the notice was "given" by the client (e.g. mailed by the client to the adviser's postal address)).

3.2.8 Consequences if a client fails to opt-in

The law should provide a 30 day 'grace period'. Specifically, section 962P should be amended to provide an adviser a 30 day administrative 'grace period' from civil penalty provisions.

3.2.9 Allow an adviser to adequately administer upon the death of a client

It is unclear how an adviser would continue to manage arrangements dealing with advice and estate planning for the client and their family in the event that the client dies. Section 962 should be amended so that if a client (who is a natural person) dies, the estate of the client, and any dependents of the client, is taken to be the client during a reasonable period following the death of the client. We suggest a reasonable period would be six (6) months during which time the client's spouse and/or dependents would be treated as the client for the purposes of the ongoing fee arrangement.

3.2.10 Allow non-product fees to be "other prescribed arrangements"

The regulation making power in section 962A(5) should not be limited to fees related to prescribed product fees. The ability to carve out certain arrangements from the definition of an "ongoing fee arrangement" should enable the regulations to prescribe any types of arrangements whether or not they relate to a prescribed product fee.

3.2.11 Carve out instalment plans where the fee is agreed before advice is provided

It is unclear the treatment for instalment plans and instalment fee arrangements. Currently for a payment plan to be captured as an "instalment plan" and therefore carved out from the definition of an "ongoing fee arrangement", the arrangement must be entered into after the advice is given. In practice, this is nonsensical and would rarely happen. Furthermore, it is contrary to the policy objective of disclosing and agreeing fees upfront and before advice and services are provided to the client. Subsection 962A(3)(d) should be amended to remove the requirement for personal advice to be provided before the arrangement has been entered into. Furthermore, we consider fee arrangements based on assets under advice should be permitted subject to the fee being a set sum, agreed upfront, and not ongoing.

3.2.12 Allow licensees and representatives to consolidate numerous ongoing fee arrangements

The law and Explanatory Memorandum should clarify where a client has numerous ongoing fee arrangements with the one fee recipient that the document(s) can be consolidated for the purposes of complying with the opt-in obligation. We consider providing clients with multiple Fee Disclosure Statements and multiple Renewal Notices at different times will be confusing and frustrating for clients as well as difficult to administer for fee recipients.

3.2.13 Allow additional information to be provided

The law should clarify that the Fee Disclosure Statement and the Renewal Notice can include other information to that which is required subject to the required information being provided in a manner that is clear, concise and effective.

3.2.14 Clarify "past fees"

The law should not require disclosure of past fees (previous 12 months) on the Fee Disclosure Statement. We consider that clients already receive adequate ongoing fee disclosure.

The ABA recommends that the opt-in obligation must be amended to clarify the scope and application, explicitly apply prospectively to new clients, and better accommodate a flexible approach for advisers and their clients.

3.3 Conflicted remuneration

The ABA supports the banning of adviser remuneration that is conflicted. However, we are concerned that the conflicted remuneration provisions are much broader than necessary to ensure that retail clients have access to unbiased advice and capture legitimate payments made between banks and their employees, agents and representatives and legitimate business-to-business payments. Furthermore, the FOFA legislative package as currently drafted introduces a significant degree of legal uncertainties and compliance risks.

3.3.1 Definition of conflicted remuneration

The ABA notes that the proposed ban on 'incentives' in connection with financial product advice to retail clients relies on the definition of "conflicted remuneration" contained in section 963A, which includes both monetary and non-monetary benefits, and has only limited carve outs (contained in sections 963B, 963C and 963D). We are concerned that the definition of conflicted remuneration remains too broad, especially as it is not limited to personal advice and the Explanatory Memorandum states "any flat payment received by a licensee would on its face be conflicted remuneration"[11].

The ABA notes the changes to section 963A(1) and 963A(2) in relation to the threshold test for the capacity of benefits to "influence". The exposure draft previously applied the ban on conflicted remuneration to any benefit, whether monetary or non-monetary, which because of the nature of the benefit, or the circumstances in which it is given, "might influence" the choice of financial products recommended to retail clients or might otherwise influence the financial product advice provided to retail clients. We previously submitted to Treasury that such an evidentiary standard was not only too low, but also exceptionally vague and incredibly ambiguous. Therefore, we welcome the changes in the Bill to establish in section 963A the ban on the receipt by licensees and their representatives, and on the payment by product issuers or sellers, of remuneration that could "reasonably be expected to influence" the financial product advice given, or choice of financial product recommended, to retail clients.

[11] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.20, p28.

Nevertheless, in practice, we note that any payment "could" influence behaviour and be prohibited. Therefore, the evidentiary standard remains too subjective resulting in both legal uncertainties and compliance risks for banks and banking groups. We are concerned that these practical complexities could result in 'no-advice' models being extended by banks which would be contrary to the policy intent of the FOFA legislative package, namely to improve the availability of, and accessibility to, financial advice. Additionally, we are concerned that the legal complexities could result in banks being forced to revise their existing workplace, employee and remuneration arrangements, and in particular remove incentive structures and performance bonus payments for all staff.

It is the ABA's view that the FOFA reforms should ban payments that result in a conflict or misalignment of interests, which is consistent with Minister Shorten's announcement on 28 April 2010. Specifically, we note the commentary about conflicted remuneration:

> ... distortions to remuneration, which misalign the best interests of the client and the adviser, should be minimised[12].

Therefore, while the definition of conflicted remuneration contained in the Bill is an improvement to that contained in the exposure draft, the cornerstone principle of the FOFA reforms – to prevent retail clients receiving conflicted advice that is motivated by inappropriate incentives – has been lost. Appropriate incentive structures are used across many industries to promote productivity and innovation. Therefore, it should not be assumed that all incentive structures results in negative outcomes for retail clients. However, the proposed definition has the effect of capturing many of the existing incentive structures in the banking and financial services industry, which could "reasonably be expected to influence", even where these payments have not been problematic or resulted in negative outcomes for retail clients.

The ABA recommends that remuneration structures should only be prohibited where there is a negative outcome for the retail client, i.e. the ban should only apply to circumstances where a monetary or non-monetary benefit has a reasonable likelihood of inappropriately influencing the financial product recommended or financial advice given, thereby resulting in biased or conflicted advice. Furthermore, the definition should be limited to a negative influence to ensure that any influence which results in a positive outcome for the client is not captured.

The ABA notes that a critical provision related to conflicted remuneration is not contained in the FOFA legislative package, namely the arrangements to ensure that brokerage and fees connected to capital raising are clearly and comprehensively excluded. We are advised by Treasury that the details of the proposed exemption will be contained in regulations. The banking and financial services industry continues to eagerly await details of the exemption.

3.3.2 Treatment of benefits from employers to employees—volume-related payments

The ABA notes that section 963L establishes a statutory presumption that certain volume-related payments are 'conflicted remuneration' (as defined in section 963A), unless the contrary is proved. Volume based incentives include benefits "access to which" or the "value of which" is wholly or partly dependent on the total value or number of financial products recommended or acquired of a particular class or classes.

[12] Future of Financial Advice Information Pack. 28 April 2010. p2.

Where a volume based payment of a kind described in subsection 963L(a) or subsection 963L(b) is made, the party alleged to have paid or accepted the benefit, must prove that, in the circumstances, the benefit was not conflicted remuneration (as defined in section 963A). Therefore, the statutory presumptions in section 963L are linked to the potential for the payment to influence the advice. Placing the onus of proof on the parties to demonstrate that certain volume based benefit structures are not 'conflicted remuneration' under the definition in section 963A, is considered by the Explanatory Memorandum to be appropriate: "as this will peculiarly be within the knowledge of those paying and receiving the benefits"[13].

The ABA welcomes a number of changes made to the exposure draft, including:

- Section 963A – definition of conflicted remuneration.
- Section 963D – inclusion of the concept of sales incentives not being conflicted when paid by an ADI employer to an "employee" where they advice on, or sell, basic banking products[14].
- Section 963L – replacement of a complete prohibition on volume based benefits with a statutory presumption that there is the ability to prove that a volume based benefit is not 'conflicted' and linking the section to the definition of conflicted remuneration in section 963A (specifically, the potential for the payment to influence the advice).

The ABA also welcomes the confirmation in the Explanatory Memorandum that "performance pay can be an important part of any remuneration arrangement" and that the intention of section 963L is to provide the industry "with the flexibility to maintain broadly based performance-based remuneration arrangements without compromising the advice provided to retail clients"[15].

However, the current drafting of the conflicted remuneration provisions does not support this intention. If an employee is remunerated based on a range of performance criteria, one of which is the volume of financial product(s) recommended, the part of the remuneration that is linked to volume is presumed to be conflicted by virtue of section 963L. However, if it can be proved that, in the circumstances, the remuneration could not "reasonably be expected to influence" the choice of financial product recommended, or the financial product advice given, to retail clients (section 963A), the remuneration is not conflicted and is not banned. This will depend on all of the circumstances at the time the benefit is given or received[16].

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[13] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.18, p27

[14] Despite the Bill not being explicit, the Explanatory Memorandum confirms that arrangements where an employee or an agent of an ADI advise on, and sell, basic banking products are exempt from the ban on conflicted remuneration. "This entitles an employee to receive sales incentives from their ADI employer, even if it is volume based". *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.41, p33.

[15] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.19, p28

[16] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.19, p28

The ABA believes that the law could be interpreted that any payment of a benefit – or in other words a "financial reward" – could influence a recommendation. Therefore, it may be interpreted that: (1) the payment of a performance bonus to potentially all bank staff is prohibited; and (2) the carve out for basic banking products is unworkable, due to this interpretation. For example, a payment that rewards a bank teller or bank specialist for the overall performance of the business could be assumed to be conflicted remuneration simply because it relates to "volume" (number and/or value of financial products). Similarly, a payment that rewards a bank financial planner for an aggregate net improvement in their clients' position would be assumed to be conflicted remuneration (even though this may influence advice positively) because part of the payment would be based on "volume".

Given that the onus is on licensee to prove that a payment is not conflicted remuneration, it is unclear how banks and other financial service providers are expected to demonstrate compliance. Furthermore, other paragraphs in the Explanatory Memorandum are unclear as to the ability of a licensee to prove that a payment is not conflicted remuneration. For example, "volume based payments of the kind described in section 963L appear on the face of it to be inherently conflicted, since the financial adviser will have a financial incentive to maximise the value of payments irrespective of the suitability of the products or investments for the client"[17]. Therefore, the Explanatory Memorandum implies that recipients directly involved in the advice process are less likely to be able to accept any volume based benefits without those benefits being conflicted.

Bonus pool arrangements for bank employees

The ABA submits that performance pay for bank employees is beyond the policy intent of the FOFA reforms. Furthermore, it does not automatically follow that a client is at risk of receiving advice which is conflicted merely because an adviser may receive part of their remuneration in the form of a performance bonus payment from their employer based on their overall activities for the year and the overall service provided to retail clients. We believe there are a number of important factors to keep in mind with reforms that contemplate intervention in employment arrangements, including:

- *Productivity, innovation and efficiency:* Performance based remuneration structures can be designed to:
    - Result in improved bank-customer relationships, including a one-stop-shop retail banking service and better, more holistic financial advice outcomes for clients (in this regard because incentive structures can encourage advisers to give advice on a client's entire portfolio which provides increased visibility of a client's overall financial position and improved ability to identify any gaps and opportunities in savings and investment strategies);
    - Ensure business sustainability by enabling a remuneration framework to protect the underlying business from operational risks (in this regard because incentive structures can assist banks manage earnings volatility and exposures due to the transactional nature of the industry and reliance on market sentiment);
    - Ensure pay is commensurate with productivity by aligning performance, risk and efficiency measures based on the company's performance;

[17] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.18, p27

- Align the interests stakeholders, including shareholders; and
- Attract and retain high quality staff by offering competitive performance-driven remuneration structures and salary packages which promote superior performance and long-term commitment to the business.

- *Industry competitiveness*: Performance based remuneration structures are also common across many forms of employment in Australia and overseas. Banks and other financial service providers compete with other industries for high quality staff. It should be noted that many private sector organisations and professions and public sector agencies, including accountancy, law, compliance (i.e. global regulatory authorities, such as ASIC, APRA, Financial Services Authority (UK), Financial Stability Board (USA), etc), use performance indicators and performance based remuneration restructures to retain staff and increasingly to align employee reward with organisational performance. Additionally, listed companies are implementing various measures and incentives to retain staff and increasingly to align employee remuneration and company performance as directed by shareholders.

- *Global competitiveness:* Performance based remuneration structures are an important part of the ability for Australian banks and financial institutions to compete with offshore markets and remain able to attract and retain high quality staff and talented advisers. This is critical to supporting the Government's efforts to promote Australia as a financial services centre. We consider that one of the prerequisites to that aim is that Australian-based employees and offshore employees are on a level playing field. The service available to clients and, ultimately, the industry's success, is dependent upon the skills of specific individuals. Remuneration is a major factor in motivating staff to relocate offshore or leave the Australian banking and financial services industry. Loss of talent overseas may impact the quality or cost of advice as well as the efficiency of the operation of our financial markets.

The ABA notes that some banks and banking groups are progressively transitioning from commission payment models and sales related incentive models for their employees towards other payment structures, such as a fee-for-service. However, these employees may also have access to a bonus pool arrangement based on revenue generated from alternative payment structures and overall revenue targets. Additionally, some banks' salary models are based on volume based payments and commissions to their employees working in a community bank, bank agency, franchise network or mobile bank.

Revenue generated from the sale of products may not be specifically volume based or directly linked to specific sales targets. The ABA is advised by member banks that incentive arrangements for bank staff are generally funded via a bonus pool arrangement. Incentive plans or variable rewards schemes can be based on a balanced scorecard approach where performance outcomes and behaviours are measured, such as customer satisfaction and quality (based on proxies used to ensure product sales meet customer needs and the product is used), community engagement, culture and employee management, self-development, financial and risk management, strategic process and quality, and revenue (based on individual or overall team performance). Measures are both financial and non-financial. The actual percentage of a scorecard relatable to a revenue measure varies from bank to bank, function to function, and individual to individual.

Measures relating to the sale of products are generally calculated against a broad portfolio of products or overall revenue generated, rather than directly linked to specific product targets of a class of products. Payments from the bonus pool are generally discretionary, although performance payments are included in workplace agreements, contracts and awards. The ABA is advised by member banks that incentive plans do not typically encourage products to be sold in the same way as could be the case with conflicted remuneration structures. Furthermore, individuals must achieve a minimum scorecard outcome to be eligible for a performance bonus payment and/or eligible to a component of the incentive calculation (depending on the incentive plan). Remuneration policies, performance management systems and criteria assessment ensure that individual behaviour assessment impacts on the incentive outcome and deferral, or adjustment, of a bonus payment can be made depending on performance or compliance issues. Internal controls ensure performance pay is not conflicted.

The ABA notes that employment agreements vary from bank to bank depending on the operating structure and business model. The following provides some indications of existing workplace arrangements used across banks:

- *Employment agreements*: These agreements are generally ongoing and tend to include provisions for employees to be eligible to participate in a reward program with outcomes based on key performance indicators. Some of these reward programs can be varied or cancelled at any time. (We note that there are also legacy agreements in place across banks.)

- *Enterprise agreements*: These agreements are negotiated and approved by Fair Work Australia and can contain provisions for employees to receive discretionary payments. Incentive plans and variable reward schemes (including the details of scorecard methodology and the nature of targets) are typically contained in separate policy documents, but are generally subject to provisions contained in the enterprise agreement. Enterprise agreements are usually negotiated to be in place for a fixed term (i.e. 2-5 years) until the expiry date, unless there are significant and material changes. Consultation and amendment arrangements, including with employee and union representatives, varies from bank to bank.

- *Contractual agreements*: These agreements are generally based on fixed terms and tend to include detailed provisions on remuneration structures, including commission payments or performance bonus payments. Contracts can be individual or business related. Termination clauses tend to be strict with little ability for unilateral variation. (We note that termination or variation of these agreements would need to comply with various laws, for example, for business contracts the Franchising Code of Conduct which has effect under the *Competition and Consumer Act*. We also note that commission payments and interests are clearly detailed in the Financial Service Guide (FSG) of banks operating an agency or franchise network.)

The ABA believes that the ban on conflicted remuneration should explicitly not apply to bonus pool arrangements for bank staff where incentive plans and variable reward schemes contain revenue measures that are not specifically volume based, or wholly and directly linked to specific sales targets of a class of products, or where individual sales volume does not solely determine the incentive payment. This approach would ensure that employees are not prejudiced by the FOFA reforms which are only intended to restrict volume based payments which create perverse incentives for financial advisers (financial planners) to select and recommend certain products/providers over others. Additionally, this approach would ensure that the existing bonus arrangements are not interrogated based on granularity of measures, especially where attribution of bonus to explicit sales targets or individual product revenue streams is unknown.

The ABA highlights that if bonus pool arrangements were required to be restructured for bank staff then workplace arrangements, contracts, agreements (including legacy employment contracts and agreements) and awards would need to be revised or renegotiated. Consequently, banks and banking groups would need to give careful consideration to a number of factors, such as the:

- Legal implications of having to modify agreements;
- Operational implications, including risk of losing employees, reduction in productivity, risk of confusing customers, or reduction in availability of products and services;
- Practical implications and change management, including modelling of new arrangements, redesign of incentive plans and reward programs, redevelopment of remuneration policies, and modifications to systems used to calculate bonus pool arrangements;
- Employee expectations with regards to access to bonus payments (which supplement base salaries), communications with employees, and negotiations with employee and union representatives on proposed changes; and
- Shareholder expectations with regards to bank staff performance and contribution to company value and communications with shareholders, stakeholders and other interested parties in banks' financial performance.

The ABA believes that the statutory presumption contained in the Bill and the Explanatory Memorandum is not aligned, and therefore the law is ambiguous as to the treatment of bonus pool arrangements. Even though the Explanatory Memorandum generally accepts that not all volume based payments (including performance bonus payments) are conflicted, section 963L appears to prohibit any payment which relates to the revenue generated from the sale of financial products (value or number of financial products) and deems such payments as inherently conflicted[18]. Therefore, the ability of a licensee to prove, contrary to the statutory presumption, that the benefit is not conflicted remuneration would appear impractical in application.

Given the legal risks and compliance difficulties associated with section 963L, the divergence between the Bill and the Explanatory Memorandum in relation to the assumed efficacy of the statutory presumption and the ability of a party to prove that a benefit was not conflicted remuneration, we suggest that section 963B should be amended to exempt payments that are not "wholly or directly" related to the value or number of financial products, and thereby permit the payment of performance bonuses. Furthermore, we consider that section 963L should be amended to include a materiality threshold. (However, it is likely that ASIC guidance would be required to address concerns regarding interpretation.) In the absence of amendment and clarification, this could result in all bank staff not being rewarded and the removal of certain discretionary incentive structures, including performance bonus payments based on balanced scorecard methodology.

[18] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.18, p27

The ABA believes that the current drafting also unfairly benefits those advisers who are individual licensees or authorised representatives and not employed by another licensee. These advisers may accept the types of remuneration which are carved out of the 'conflicted remuneration' definition in sections 963B, 963C and 963D (such as income generated from wholesale clients, execution-only services, fee-for-service and asset-based advice fees), but advisers who are employed may not be able to accept these types of remuneration because they are wholly or partly dependent on volume, and therefore presumed to be conflicted. We consider that there should be a level playing field between advisers who are employed and advisers who are not employed.

The ABA recommends that:

- The conflicted remuneration provisions should not apply to general advice.
- Section 963L should be amended so that the law does not prevent "access to" a benefit related to value or number. The phrase "wholly or partly" should be replaced with "wholly and directly". Specifically, the law should be redrafted as follows: "a benefit, the value of which is wholly and directly dependant on ..."
- Section 963B should be amended to clarify that a benefit may paid to an "employee" if the benefit is not specifically volume based, or wholly and directly linked to specific sales targets of a class of products, or where individual sales volume does not solely determine the benefit. Additionally, the Explanatory Memorandum should be amended to confirm in these circumstances that incentive structures and performance bonus payments are not conflicted.
- The law should be clarified so that the exemptions in sections 963B, 963C and 963D apply despite sections 963A and 963L. (It should be noted that this amendment would clarify that the carve outs from the conflicted remuneration provisions apply whether or not they are volume based benefits. For example, the statutory presumption in section 963L that certain volume benefits are presumed to be conflicted should be subject to (i.e. limited by) sections 963B, 963C and 963D, which carve out certain benefits from the definition of conflicted remuneration (income generated from wholesale clients, execution-only services, fee-for-service and asset-based advice fees).
- Section 963J should be amended to clarify that an employer may pass on benefits to their "employees" where those benefits are set out in sections 963B, 963C and 963D.
- Section 963B(1)(d) should be amended so that the law allows a benefit to be given by a licensee or representative to their "employees" based on total revenue generated (and gross income pool) where the benefit could not reasonably be expected to influence the choice of financial product recommended or the financial product advice provided to a retail client (consistent with section 963A), even where the benefit is wholly or partly dependent on volume (value or number of financial products).
- The law should be clarified so that the definition of "employee" applies to all bank staff (employees, agents, and representatives), persons otherwise acting by arrangement with an ADI under the name of the ADI, or employees of subsidiaries of ADIs. (The concept of employee should be consistent with the best interests duty.)

3.3.3 Carve out for basic banking products—benefits for recommending basic banking products not *conflicted remuneration*

The ABA previously submitted to Treasury that the carve out of basic banking products from the ban on conflicted remuneration was unclear and ambiguous. Specifically, we suggested that the ban on conflicted remuneration should explicitly not apply to volume based payments or commissions related to advice on, or the distribution of, basic banking products. Therefore, we welcome the introduction of section 963D into the legislation as a separate exemption. Unfortunately, as currently drafted the carve out for basic banking products is still not sufficient.

In order for a monetary or non-monetary benefit given to a financial services licensee, or a representative of a financial services licensee not to be deemed "conflicted remuneration" (for recommending basic banking products)*:*

- The benefit must be "remuneration for work carried out", or to be carried out, by the licensee or representative as an agent or an employee of an Australian ADI, or in otherwise acting by arrangement with an Australian ADI under the name of the Australian ADI;
- Access to the benefit, or amount of the benefit, must be solely dependent on the licensee or representative recommending a basic banking product; and
- The licensee or representative cannot, in the course of recommending that basic banking product, give other financial product advice that does not relate to a basic banking product.

The ABA is concerned that this provision would result in substantial legal risks and compliance issues for banks. There are several outstanding issues. Therefore, we believe that the conflicted remuneration provisions should be amended.

'Employee'

It is still unclear in the Bill and the Explanatory Memorandum whether the exemption is intended to apply to all bank staff, including staff not "employees of an ADI", employees of subsidiaries and related bodies corporate or companies, franchisee, community and mobile banking models. We suggest that the carve out should be the same as the carve out for basic banking products from the best interests duty as we have redrafted. Additionally, the Explanatory Memorandum should be amended to clarify the application of the carve out for basic banking products from the conflicted remuneration provisions to all bank staff arrangements. This will ensure that all bank staff employed or otherwise working for a bank or other ADI via standard and other workplace arrangements will be included in the exemption. In the absence of amendment and clarification, this could result in distortions in the retail banking industry and may have adverse effects for banking competition.

Benefit paid to an 'employee'

The Bill and the Explanatory Memorandum infer that the benefit is given to a financial services licensee or representative for "work carried out" as an agent or employee of an ADI ('the employer'), rather than the benefit being given to an employee or agent by a licensee or representative. We suggest that the carve out should apply to the benefit given by a licensee/representative to the "employee".

The law should also have regard to "referrals".

'Work carried out'

It is unclear in the Bill and the Explanatory Memorandum what constitutes "work carried out". Even though the Explanatory Memorandum states that this benefit could include an "employee's salary", it is unclear how this relates to different bank staff paid via different remuneration structures and subject to different workplace arrangements. For example, does the exemption include base, award or non-award salary only, or 'annualised salary', including wages and other certain entitlements (i.e. overtime, penalty rates, annual leave loading), or 'salary package', including flex-time payments, day-in-lieu payments, allowances and reimbursements, etc, or 'salary package', including salary sacrifice or benefit entitlements, incentive structures, etc? We suggest that the Explanatory Memorandum be amended to clarify that "work carried out" relates to all forms of salary including wages and other entitlements, either non-discretionary or discretionary, as paid by the employer to their "employee" (noting the concept of employee must take into account all bank staff arrangements).

Performance bonus payments – basic banking products and other products

The Bill and the Explanatory Memorandum state that a benefit paid relating to advice on basic banking products and other financial products is deemed to be conflicted. If financial product advice is given on financial products other than basic banking products, either in combination with, or in addition to, the advice provided on basic banking products, the receipt of the benefits will be considered conflicted remuneration, and not permitted. This means that an "employee" of an ADI is unable to participate in a bonus pool arrangement and receive a performance bonus payment if they provide advice on products in addition to basic banking products, including risk insurance products (general and life insurance) even though these products are specifically exempt from the conflicted remuneration provisions.

While we recognise that the intention is to eliminate the possibility that bank employees are able to receive a benefit for the offer of financial products that are not basic banking products, unfortunately the proposed provisions means the carve out for basic banking products would be significantly limited in practical application, given that bank staff do not only provide information and advice on basic banking products. In practice, bank staff could offer customers the choice of a range of products across the bank's entire product suite, which can include basic banking products, other 'Tier 2 products' (i.e. general insurance products), other financial products, and credit products.

The ABA notes that a bank employee might provide advice in relation to a basic banking product (i.e. savings account) and then also provide advice on an exempted non-basic banking product (i.e. general insurance product) or a non-financial product (i.e. credit product). We consider that it should be explicitly clear that despite the employee giving advice on a basic banking product 'in combination with or in addition to' advice on a non-basic banking product, the staff member could be paid a benefit. We believe that the law should not prevent the payment of a performance bonus if bank staff also advice on, or sell, other banking products, including financial and non-financial products. Additionally, subsection 963D(c) should be amended so that payments given by an employer related to advice on, or distribution of, financial products deemed not to be conflicted (i.e. general insurance product) are also not conflicted.

The ABA recommends that:

- Section 963D should be amended to clarify that the carve out relates to a benefit paid by a licensee or representative to their "employee". Additionally, the Explanatory Memorandum should be amended to clarify that "work carried out" relates to all forms of salary including wages and entitlements, either non-discretionary or discretionary, as stipulated in the contract or agreement of the "employee".
- Section 963D should be amended to clarify "agent and employee". (It should be noted that the carve out should be the same as the carve out for basic banking products from the best interests duty as we have redrafted.) Additionally, the Explanatory Memorandum should be amended to clarify the application of the carve out for basic banking products from the conflicted remuneration provisions to all bank staff arrangements.
- Subsection 963D(c) should be amended to clarify that payments given by an ADI employer related to advice on, or distribution of, other financial products deemed not to be conflicted are also not conflicted. (It should be noted that the carve out for basic banking products does not prevent bank staff from advising on other 'Tier 2' products.)
- Subsection 963D(b) should be amended to clarify that the carve out relates to a benefit paid relating to basic banking products and/or other exempt products. Specifically, the law should be redrafted as follows: "the benefit is dependent on the licensee or representative recommending a basic banking product or other product in relation to which benefits are not conflicted remuneration pursuant to section 963B or 963C or as prescribed by regulations".
- Subsection 963D(b) should be amended to clarify that an ADI employer is able to reward their "employees" for the offer of basic banking products where they also offer financial products to which the conflicted remuneration provisions apply (and other financial products specifically exempted) provided no reward is paid wholly or directly for the offer of the non-exempted financial product.

3.3.4 Execution-only services

The ABA notes that subsection 963B(1)(c) exempts monetary benefits given in relation to an issue or sale of a financial product where no financial product advice in relation to the product, or class of products, has been given to the person as a retail client. We welcome the exemption for execution-only services. However, we submit that the provision is not sufficient.

According to the Explanatory Memorandum, the carve out is intended to exempt commissions and incentive payments in relation to execution-only sales or issues of financial products, i.e. "where the product is sold with no advice provided to a retail client"[19]. Therefore, if a bank planner advises retail clients in relation to a particular class of product, it seems that a licensee can never pay commission to the planner in relation to a product of that class where the product is to be sold to retail clients because even if the product is to be sold on an execution-only/no advice basis, there is no way of ensuring that the planner has not previously provided advice in relation to that product or class of product.

[19] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.25, p29.

In practice, the exemption seems impractical and limited. Accordingly, it should be clarified that the financial product advice referred to in this section is in relation to the issue or sale for which the benefit is given.

> The ABA recommends that section 963B(c)(ii) be amended to "financial product advice in relation to that issue or sale of the financial product has not been given to the person as a retail client by the licensee or representative."

The ABA believes that the exemption may be impractical and limited for large financial institutions. It may be interpreted that the execution only exception will not apply if the licensee or representative has previously provided advice to the client, including general advice, as "financial product advice in relation to the product, or products of that class" must "not have been given to the person as a retail client by the licensee or representative". For example, if a bank planner provided advice to a retail client in relation to a managed investment scheme as part of a financial plan, say, 5 years ago. Presumably, it is not the intention of the law to prevent payments where a retail client may have received advice from the bank or banking group in the past.

> The ABA recommends that section 963B(c) should be amended to clarify that the exemption for execution-only services relates to advice provided previously by the adviser. (It should be noted that this amendment would clarify that the advice would be provided by the relevant representative (and not by any representative of the licensee)).

3.3.5 'Sophisticated businesses'

The ABA notes that the FOFA reforms do not apply solely to individuals, as businesses are included in the definition of "retail client". According to the law, a "retail client" includes a small business with less than 100 employees (for a manufacturing business) or 20 employees (non manufacturing business)[20]. Additionally, where the transaction size is less than $500,000, the business will be considered a "retail client". Unlike the classification of individuals as retail or wholesale investors, there is no current mechanism for a business to be classified as wholesale other than the employee number or transaction value tests. As a result, the Bill is likely to impact the provision of products to a large portion of Australian businesses which meet the legal definition of "retail client".

Many businesses which meet the requirements to be considered as a "retail client" often require products in order to facilitate day-to-day business operations (i.e. foreign exchange contracts, derivatives and commodity products within the agricultural industry and manufacturing industry). Therefore, these products are not investment products, and are not used for speculative purposes. Instead, these products are used by business customers for risk management and hedging purposes, e.g. managing a financial risk to their business which they may be exposed to as a result of undertaking the business (i.e. fluctuations in prices and interest rates). We are concerned that these types of transactions and hedging products are beyond the policy intent of the FOFA reforms, and therefore without amendment could restrict the availability of such products. Non-availability of a range of risk mitigation/management tools to Australian businesses would have a substantial impact on Australian businesses' capacity to manage cash flows and other financial, business and operational risks (with potential implications more broadly for the Australian economy).

[20] *Corporations Act 2001,* section 761G.

The ABA believes that prohibiting payments that relate to the distribution of products and/or services to business customers for products used for hedging purposes is likely to result in these services becoming less efficient and more costly for businesses, and in particular small-to-medium sized business clients and corporate clients which do not operate their own trading desks. Unnecessary transaction costs are likely to make products and services offered by domestic banks and other financial service providers less attractive to corporations and other end-users. Therefore, we consider that the law should explicitly allow payments in relation to these transactions (for the purposes of hedging). (It should be noted that such financial products when sold to business customers, are similar in nature to insurance products, which have been provided with a carve out from the conflicted remuneration provisions.)

The ABA notes that the carve out in section 963B(c)(ii) is intended to exempt payments where advice is provided to an individual in their capacity as a wholesale client only. However, while the ABA is advised by member banks that the new policy regarding the 'retail/wholesale client distinction' test may address the anomaly regarding 'sophisticated businesses' and hedging transactions, the timing of implementing any changes means there could be a difference between the commencement of the new law and the implementation of new statutory tests. It is unacceptable for industry (including product providers and their advisers) and customers to face uncertainty or unnecessary compliance costs in the interim. (It should be noted that the timing for making changes to the retail/ wholesale client distinction test' has still not been made clear to industry.)

The ABA recommends that for certainty a subsection should be inserted into section 963B to deem that a payment made in relation to a transaction for the purposes of hedging/risk management is not conflicted.

3.3.6 White labelling arrangements

The ABA notes that white labelling, as a commercial arrangement, tends to relate to agreements that a bank may have with other providers – typically other banks or subsidiaries of other banks – to provide the system or infrastructure that underpins the provision of a financial product or financial service.

In this banking context "white labelling arrangements" are intended to leverage commercial arrangements, support services and experience and take advantage of economies of scale so that a bank does not need to invest in building their own IT system and can utilise existing technologies and infrastructure. The white labelling partner can then provide the service to their end-clients under their own brand. These systems and facilities are bank branded (not provider branded) and available to bank customers to use to facilitate a transaction or payment (e.g. ATMs to access deposits or an online trading facility to access shares). The bank simply provides access to these products and services via a "branded" facility (execution only).

Depending on the system or facility, a bank may only be merely providing a service, offering a product (e.g. non-cash payment facility, debit card), or providing factual information. In the case of online trading, in the limited circumstances where advice is provided to the retail client, neither the service provider[21] nor partner provides personal advice, only general advice (e.g. market data, market reports, and company information sourced from independent third party providers, including the ASX or research houses, i.e. Morning Star or Thomson Reuters). Nevertheless, such payments are deemed conflicted remuneration by virtue of the fact that the conflicted remuneration provisions apply to general advice.

The ABA submits that prohibiting legitimate business-2-business payments that relate to the distribution of products and/or services via white labelling arrangements (internally within a conglomerate banking group and externally) is unnecessary. We note that the key principle of the FOFA reforms is to reduce the risk of a retail client receiving "conflicted" or "biased" advice. In the instances of these white labelling arrangements, such advice is unlikely to occur because the customer does not receive personal advice, the payment of fees is not related to the provision of personal advice[22], and the customer has a choice to use the system or facility, or not.

The ABA is concerned this would likely result these important services being remodelled or withdrawn because of the restriction on such business-2-business payments to the detriment of consumers. This would result in increasing the cost of general advice (as general market data and market reports would be removed from websites forcing retail clients to make their own arrangements to receive and pay for such information) and reducing the availability of products and services for consumers.

The ABA recommends that the conflicted remuneration provisions should not apply to general advice. Alternatively, the provisions should be drafted to exempt general advice given by way of general market information, such as marketing material, market reports and market data.

3.3.7 Benefit provided by retail client

The ABA notes that subsection 963B(1)(d) aims to exempt payments agreed directly between a client and the adviser. Monetary benefits given by a retail client in relation to the issue or sale of a financial product, or in relation to financial product advice given by the licensee or representative to the client are not conflicted remuneration. Therefore, 'fee-for-service' arrangements, including, volume based charges for advice are permitted, except to the extent that geared funds are involved.

The ABA welcomes the clarification in the Explanatory Memorandum that the provision intends to exclude benefits "given" by:

- A retail client directly;
- By another party at the direction of the retail client; or
- With the clear consent of the retail client.

[21] The ABA notes that provider will be an AFSL holder, governed by their licence authorisations, required to provide the appropriate disclosures and are regulated by ASIC.

[22] For example, in relation to outsourced/white-labelled share trading facilities, revenue is generally calculated by the service provider and a portion is paid to the bank on a monthly basis as a distribution fee/volume based commission. Such payments should not be considered 'conflicted' because the benefit is calculated based on the revenue as a whole and not in relation to the promotion of any particular product or class of products.

However, the ABA submits that the expanded interpretation of "given" contained in the Explanatory Memorandum should be contained in the Bill. Additionally, where the "adviser" is employed by a bank, the payments will be made to the bank, not directly to the adviser. Therefore, the Bill should recognise that the benefits may be given by the client to the employee indirectly.

The ABA recommends that:

- Subsection 963B(1)(d) should be amended to clarify that the benefits may be given by the client to the employee indirectly so that asset based fees are not conflicted remuneration even where the fees are paid through an investment facility. Specifically, the law should be redrafted as follows: "the benefit is given to the licensee or representative by, at the direction or with the clear consent of, a retail client..."
- Subsection 963B(1)(d) should be amended to clarify that the benefits may be given directly or indirectly to an "employee". Specifically, the law should be redrafted as follows: "the benefit is given to the licensee or representative by, at the direction or with the clear consent of, a retail client in relation to: the issue or sale of a financial product by the licensee or representative to the client; or financial product advice given, whether directly or indirectly, by the licensee or representative to the client."

3.3.8 Regulation making power

The ABA notes that subparagraph 963B(1)(e) provides a regulation making power to prescribe a benefit, or circumstances in which a benefit is given, is excluded from the definition of conflicted remuneration. We welcome the inclusion of a regulation making power to ensure that the law can be amended to respond to innovation in the offer of simple financial products and additional exemptions can be included.

According to the Explanatory Memorandum, the proposal is to "exclude certain stockbroking activities from being considered conflicted remuneration"[23]. The proposed stockbroker carve out is intended to allow "persons undertaking stockbroking activities to receive third party 'commission' payments from companies where those payments relate to capital raising". We note that the precise breadth of the carve out is subject to further consultation. However, it is proposed that "'stamping fees' from companies for raising capital on those companies' behalf not be considered 'conflicted remuneration' where the broker is advising on/or selling certain capital-raising products to the extent that they are (or will be) traded on a financial market".

The ABA submits that the scope of the carve out should be broad enough to cover financial planners, bankers and stockbrokers equally. Like stockbrokers, financial planners and bankers are a major source of capital for capital raising activities. We consider there is no reason to differentiate between different types of advisers as their functional role is the same on the relevant transactions.

[23] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph2.28, p30.

The ABA recommends that the proposed carve out for stockbrokers should permit the payment of commission, brokerage and stamping fees on all capital raisings and should apply equally to financial planners, bankers and stockbrokers. A practical carve out is necessary for financial institutions to raise the required amount of capital from retail investors domestically.

3.3.9 Non-monetary benefit given in certain circumstances not *conflicted remuneration*

The ABA notes that the Bill prohibits non-monetary (soft dollar) benefits that could reasonably be expected to influence financial product advice (section 963A). However, section 963C prescribes a number of soft dollar benefits which are not to be regarded as conflicted remuneration, including:

- Benefits given in relation to a general insurance product;
- Benefits under the amount prescribed by regulations, so long as the benefits are not identical or similar and provided on a frequent or regular basis;
- Benefits with a genuine education or training purpose that are relevant to the provision of financial advice to retail clients (professional development exemption);
- Benefits that are the provision of IT software or support that are related to the provision of financial product advice; and
- Benefits provided by a retail client in relation to the sale of a financial product or provision of financial advice.

The Explanatory Memorandum confirms that "the ban on non-monetary benefits is not generally intended to cover the services provided by a licensee to its authorised representatives for the purposes of the authorised representative providing financial services on behalf of the licensee"[24]. The Explanatory Memorandum also states that these services would only be captured by the ban if the services were provided in such circumstances where it "could reasonably be expected to influence" financial product advice (section 963A).

The ABA believes that the operation of section 963A (containing the definition of conflicted remuneration which includes non-monetary soft dollar benefits) and section 963C which provides a number of carve outs from the general proposition that soft dollar benefits are conflicted remuneration, does not adequately fulfil the intention as contained in the Explanatory Memorandum.

The ABA recommends that section 963C(c) should be redrafted to ensure that a non-monetary benefit relevant to the provision of financial services or the conduct of a financial services business is exempt. (It should be noted that this amendment should clarify that licensees are permitted to provide non-monetary benefits to representatives for the purposes of providing financial services.) Additionally, the Explanatory Memorandum should be expanded to refer to "representatives" and not only "authorised representatives" in order to clarify that a licensee can provide professional development to all of its representatives without breaching the conflicted remuneration provisions.

[24] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.39 p 32.

3.3.10 Dollar limit

The ABA notes that section 963C(b) exempts the benefit where it is less than the amount prescribed by regulations and "identical or similar benefits are not provided on a frequent or regular basis". It is expected that, consistent with existing industry practice and the 'FSC/FPA Code on Alternative Remuneration', this amount will initially be set at $300, as proposed in the Explanatory Memorandum[25].

The ABA submits that a reference to similar benefits being provided "on a frequent or regular basis" is not adequately clear in the Bill. While it is not appropriate for these terms to be defined in the law, we suggest that the proposed provisions should be amended to include a test for what ought to be reasonably perceived to be designed to circumvent. Additionally, the Explanatory Memorandum should be amended to provide some examples of what does and does not constitute "frequent or regular basis".

Furthermore, the ABA believes that it is not sufficiently clear in the Bill that the exception is intended to apply to the licensee and to each representative separately. We suggest that the Explanatory Memorandum should be amended to clarify this intention.

3.3.11 Professional development

The ABA notes that section 963C(c) exempts the provision of genuine education or training events. We welcome this exemption as recognising these types of events are an important mechanism for licensees to achieve and maintain their necessary licence obligations with respect to ensuring their staff and representatives are appropriately trained and competent.

The Explanatory Memorandum confirms that the regulations will prescribe further requirements for professional development events. The following criteria is intended to be prescribed:

- Domestic venue (Australia or New Zealand);
- Minimum amount of time spent on educational content (six hours out of a standard 8 hour day); and
- Expenses outside of the professional development activity must be paid for by participants or its employer or licensee[26].

The ABA is concerned about the inclusion of subsection 963C(c)(ii) in relation to the professional development being "relevant to the provision of financial product advice". We submit that the relevance test should be removed, as it may lead to uncertainty about the range of topics that could be covered at these events. Financial advisers engage in activities beyond simply 'giving financial product advice', such as dealing and administrative activities. Therefore, there may be other topics relevant to the business of a financial adviser without being obviously "relevant to the provision of financial product advice", such as marketing, accounting, business strategy, OH&S, etc. These types of courses and events would be for a genuine educational or training purpose, but could be inconsistent with subsection 963C(c)(ii).

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[25] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.31, p30.
[26] *Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011,* Explanatory Memorandum, Paragraph 2.33, p31.

Furthermore, the ABA submits that the location restriction should be removed. Professional development events should not be limited to a venue in Australia or New Zealand, as this implies that conferences and events in other jurisdictions are not genuine professional development events. There may be reputational issues for Australia if this domestic location restriction was to proceed. Additionally, imposing a domestic location restriction would be contrary to the Government's efforts to promote Australia as a financial services centre. We note that part of being a financial services centre is not just about creating onshore opportunities, but promoting offshore opportunities and demonstrating the knowledge and expertise of the Australian banking and financial services industry in other countries. Therefore, instead, we suggest that the content of the event itself should determine whether it is a genuine educational or training event.

The ABA recommends that subsection 963C(c) should be deleted.

3.3.12 Basic financial products

The ABA submits that the provisions on conflicted remuneration should not apply to employees of a bank or financial institution who advise on, or sell, their bank/banking group's basic financial products.

While addressing the issue of ensuring that the FOFA reforms apply only to personal advice (not general advice) will go some way to addressing concerns with the accessibility and availability of basic financial products, we consider that an explicit carve out should be provided for simple superannuation products, simple wealth products (as that term may be defined), and retirement savings accounts. These products are widely available through bank branches and call centres with bank staff and bank specialists providing factual information and general advice. Importantly, we do not propose that the carve out be extended to personal advice on superannuation products or strategies, nor should it be extended to all superannuation products. An exemption for basic superannuation products should be defined commensurately with the features of the "MySuper" concept, namely around 'no frills/universal' funds. This approach would ensure that banks are able to continue to provide basic advisory services on simple super products.

In the absence of a carve out, it is likely that there will be fewer simple, low-cost advice options available to consumers on simple super products and other basic financial products which help grow and protect a consumers' wealth. Importantly, it is not viable for each bank branch to have a bank financial planner, nor is it necessary for a bank financial planner to perform this function due to existing compliance practices, such as training, scripting and disclosure, which are adopted by those banks with a 'general advice' model in order to manage consumer protection risk.

The ABA is advised by some member banks that current innovative advisory services and basic superannuation product offerings may be adversely impacted. Other member banks indicate that current implementation plans for new products and services may be thwarted. We consider that an additional limited carve out would support the Government's stated policy of making simple superannuation advice more readily accessible for Australians.

The ABA recommends that the Government should commit to prescribing by regulations an exemption for general advice provided in relation to basic financial products, including simple super products (commensurate to the "MySuper" product), simple wealth products, and retirement savings accounts. In the absence of provisions that provide an explicit statutory exemption, it is important for industry to have some certainty about the application of the future legal obligations, and as soon as possible.

3.4 ASIC powers

The ABA broadly supports enhancing ASIC's powers to refuse and revoke licences and to ban individual advisers from the financial services industry. We welcome the clarifications made to the Bill in terms of "likely to contravene" and the Explanatory Memorandum in terms of the due diligence and evidentiary processes that would be undertaken by ASIC. However, we remain concerned about the breadth of the new measures and the application of administrative penalties to individuals and civil penalties to licensees or authorised representatives, and in particular in the absence of a reasonable steps defence.

The ABA believes that to ensure procedural fairness all decisions involving the exercise of these powers should provide individuals and licensees and authorised representatives the opportunity to appeal to ASIC and review decisions by the Administrative Appeals Tribunal and the courts. We note that regulations will be required.

4. Grandfathering arrangements

The ABA strongly argues the need for the FOFA legislative package to include grandfathering provisions. It is essential that existing workplace arrangements and current contracts and agreements are not unreasonably and unfairly impacted by the new law.

Despite previous announcements from Minister Shorten[27], in relation to the grandfathering of existing payment arrangements entered into before 1 July 2012 and platform volume arrangements, the relevant provisions allowing for grandfathering arrangements are absent from the Bill. It is essential that banks are provided with appropriate time to replace existing contractual and other arrangements without disadvantaging parties to the existing arrangements. Given that grandfathering arrangements are a key exception, and the new law is currently due to take effect on 1 July 2012, the banking and financial services industry continues to eagerly await details of these provisions.

Firstly, banks and other financial service providers have varying employment and workplace arrangements as well as contracts and service agreements. In the absence of clear grandfathering arrangements, it is uncertain whether the Government is able to intervene in these arrangements, contracts and agreements legally or whether banks and other financial service providers are able to cease or alter these arrangements unilaterally or within imposed timeframes. We note that some arrangements have years to run before they expire or are due to be renegotiated. Typically these arrangements permit third parties (i.e. employee and union representatives) to decide negotiation circumstances. Therefore, it would be unreasonable and unrealistic to impose legal obligations on banks and other financial service providers to alter these arrangements within designated timeframes that are arbitrary and unrelated to the employment arrangements governed by laws outside the obligations contained in Chapter 7 of the *Corporations Act 2001*.

Secondly, the issue of 'crystallisation' must be taken into account during the drafting of the grandfathering provisions. This issue was noted in Minister Shorten's announcement[28], which indicated that the ban on conflicted remuneration would prohibit future payments to, for example, licensees/representatives in respect of new investments through a platform but will grandfather payments to licensees/representatives in respect of investments in a platform accumulated prior to 1 July 2012. This means the level of volume payments from platform providers to dealer groups will 'crystallise' and result in the need for major reconfigurations to support crystallisation of overrides, such as trail commissions, as at the commencement date.

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[27] Minister Shorten, Press Release, 29 August 2011.
[28] Minister Shorten, Press Release, 29 August 2011.

The ABA recommends that grandfathering provisions should be specifically incorporated in the law to allow current employment and workplace arrangements, contracts, service agreements and other arrangements to continue for existing employees, agents, representatives and other arrangements or to expire before new obligations consistent with the FOFA legislative package are required to be implemented. Importantly, ordinary cessation provisions should continue to operate and new arrangements should be entered into as required and consistent with the provisions under the new law.

5. Transitional arrangements

The ABA strongly argues the need for transitional arrangements. We believe that the FOFA reforms are at least as significant as those introduced by the *Financial Services Reform Act 2001*. We note that those reforms commenced on 10 March 2002 and included a two year transition period, ending on 10 March 2004. We are concerned that the final FOFA legislative package will not likely be passed through Parliament until at least towards the end of the first quarter of 2012, with many obligations due to commence from 1 July 2012. In addition, it is unlikely that the final regulations will be in place until at least potentially second quarter 2012. This means that the financial services industry will have at best only around 3 months[29] to understand the new regime, determine how it will impact across their businesses, undertake any necessary changes to systems, processes, and procedures, and comply with the new law. We consider this is unreasonable and insufficient time for industry to comply with their new obligations.

The ABA believes that the changes to systems, processes and procedures required to implement and comply with the FOFA legislative package will be substantial and comprehensive and impose significant costs on banks and other financial service providers – for example, changes will need to be made across all operational areas, i.e. technology systems, disclosure documentation, training (competency), compliance procedures, business processes, monitoring and supervision arrangements, etc. Furthermore, it is important to recognise that the FOFA reforms are being introduced at or around the same time as a number of other significant financial services regulatory changes, including the Basel III reforms, G-20 reforms (financial services and markets regulation), superannuation ("MySuper") reforms, consumer credit reforms, banking competition reforms, insurance capital regime changes, tax agent services reforms, personal property securities law, the US foreign account tax compliance law (FATCA) and ongoing AML/CTF requirements.

The ABA remains significantly concerned about the implementation pressures associated with the FOFA reforms – this is particularly concerning for retail banking and business banking where the impact of the reforms is still uncertain and where substantive provisions are still yet to be seen. Furthermore, the divergence between the Government's stated policy intent and previous announcements and the legislation as it currently stands has consequences for the legislative timeframes, implementation and compliance.

[29] The ABA notes that depending on date of passage of the legislation and introduction of regulations it is likely that banks and other financial services providers will have considerably less time to comply unless the commencement date and transitional arrangements are adjusted and confirmed.

Therefore, the ABA believes that transitional arrangements should be implemented given the significance of the changes and the wide ranging impact of the reforms across the banking and financial services industry. We consider a staggered approach to implementation is appropriate to ensure that:

- Industry is afforded sufficient time to make the necessary changes to comply with the new law – this is particularly important for retail banking and business banking;
- New entrants are afforded the flexibility to comply with the new regime and avoid having to implement unnecessary compliance systems;
- The FOFA and MySuper reforms can be better aligned – this is particularly important to ensure industry avoids having to administer multiple product, system and documentation changes; and
- The enhanced ASIC powers are introduced with immediate effect.

In addition, in the absence of amendments to ensure the remuneration systems, salary packages and performance bonus payments of employees of banks and other financial service providers are not adversely impacted, it will be necessary for grandfathering provisions to be introduced so that arrangements can be adjusted in an orderly and legal manner.

The ABA recommends that the Government implement the following transitional arrangements:

1. Enhanced ASIC powers commence from the commencement date (i.e. 1 July 2012);
2. Existing law continues to apply until 30 June 2013, yet providers are permitted to opt-in to the new regime prior to 1 July 2013 at their own discretion; and
3. New law commences from 1 July 2013.

6. Other FOFA reforms

The ABA notes that there are a number of other key parts of the FOFA reforms which remain outstanding and which may have significant impacts on the operations of measures contained in the FOFA legsilative package.

6.1 Retail/wholesale client distinction

This reform is central to the operation of the FSR regime. The 'retail/wholesale client distinction' tests may have a substantial impact on industry and its ability to comply with the new law. (It should be noted that the ABA has provided comments on the consultation paper.)

6.2 Accountants' exemption

The removal of the accountants' exemption will result in significant changes in how accountants provide financial advice. (It should be noted that the ABA has only provided preliminary comments during FOFA PCG meetings.)

6.3 Training requirements

The implementation of a new assessment and professional development framework is likely to result in significant changes to the training and competency requirements for financial advisers and the ability for advisers to demonstrate compliance with various legal obligations. The proposed new framework contemplates capturing general advice within the full competency requirements which would result in substantially more onerous and costly training requirements. The best interests duty relies on the competencies of an adviser and changes will impact on the advisers' ability to comply with the law. (It should be noted that the ABA has provided comments on ASIC's Consultation Paper 164: Additional guidance on how to scale advice. However, we are not a participant on the "Advisory Panel on Standards and Ethics for Financial Advisers".)

6.4 Compensation arrangements

The introduction of a statutory compensation scheme may result in significant additional and unnecessary costs for banks depending on how a scheme is implemented, if indeed it is deemed appropriate for a scheme to be implemented for financial advisers. (It should be noted that the ABA has provided comments on the consultation paper.)

6.5 Disclosure requirements

The implementation of new disclosure requirements for Financial Services Guides (FSGs) as announced in April 2010 as part of the FOFA reforms could have implications for banks' compliance systems. It is important for banks and banking groups to have clarity on any new disclosure obligations to ensure sufficient time and resources can be allocated to make the necessary changes required. Any new disclosure requirements should be harmonised with implementation of the FOFA legsilation to avoid unnecessary legal and compliance costs. (It should be noted that the disclosure document is still in consultation.)

6.6 Intra-fund advice

The implementation of the "intra-fund advice" model through the "MySuper" legislation could result in disparate duties and an unlevel playing field (regulatory arbitrage) for different types of advice providers. (It should be noted that consultation on this matter has been limited despite attempts to provide comments during FOFA PCG meetings. However, elements of the "intra-fund advice" regime have been inserted into the *Superannuation Legislation Amendment (MySuper Core Provisions) Bill 2011* and accompanying Explanatory Memorandum.)

Importantly, the ABA believes that providers of "intra-fund advice" must comply with the best interests duty where personal advice is given. With the exception of the carve out for basic banking products and general insurance products (and the inclusion of a regulation making provision), we consider the duty should apply to all personal advice provided to retail clients, regardless of whether the advice is intra-fund advice, strategic advice or holistic advice. Furthermore, we consider that intra-fund advice providers must comply with advice charging mechanisms that are consistent with the FOFA legislative package.

7. Concluding remarks

The ABA believes that the policy intent of the FOFA reforms is directed at the business of financial planning and the provision of personal advice by financial planners to retail consumers, not banks and the business of banking and finance. Bank customers regularly shop around for basic banking products and assess money management and account options, payment facilities, interest rates, loan and finance options, etc. Consumers understand that each bank will only provide information or advice on, or sell, the bank or banking group's own products. Consumers do not expect to receive independent advice on basic banking products available across the entire retail banking market. Importantly, banks have adopted distribution strategies for basic banking products and other financial products seeking to exploit different distribution channels and business models to ensure that customers can access products and services with ease and in ways convenient to them.

The ABA supports the introduction of the FOFA reforms as confirmed by Minister Shorten's announcement in April 2011[30]. However, we are concerned that the proposed provisions in the FOFA legislative package do not reflect the policy intent outlined in this announcement, and in fact, could be counterproductive to improving the quality of financial advice and the professionalism of the financial planning industry. Furthermore, we are concerned that the FOFA legislative package could inappropriately stifle product and service innovation in retail banking and business banking and unnecessarily hinder the availability of financial advice to many Australians.

Specifically, the FOFA legislative package could:

- Inappropriately stifle product and service innovation in retail banking – this will increase the costs of banking and decrease the availability of simple, low-cost advice on basic banking and financial products, thereby impeding competition within the banking industry. Extending the reforms to the business of banking and finance would provide little incremental value to consumers, but would increase administrative complexity and compliance costs for banks. Eventually, these costs will be passed on to bank customers. Therefore, we consider that the law should be targeted to the business of financial planning.

- Unnecessarily hinder the availability of financial advice to many Australians – the cumulative effect of the additional compliance costs and regulatory burdens as well as the uncertain liabilities on advisers is likely to result in banks and other financial service providers implementing conservative compliance systems (which would increase the cost of financial advice) and/or restructuring business models (which would decrease the availability of financial advice). Therefore, we consider that the law should explicitly exempt basic banking products, all bank staff whether employees, agents, representatives or other staff that work for a bank, and performance management systems that include key performance indicators which are related, but not wholly and directly, to revenue derived from the distribution of, or advice on, financial products.

[30] Minister Shorten, Press Release, 29 August 2011.

The ABA believes that a number of the FOFA reforms could have a significant impact on banks and banking groups and their staff and customers. We consider that it is important to take a balanced view on the implementation of the FOFA reforms, which are intended to address concerns with the professionalism of financial advice and the services provided by financial planners to retail clients. With amendment and clarification in how the proposed law reforms apply to banks and banking groups, bank staff and bank specialists, and retail banking products, we envisage that banks will take opportunities to expand their offerings of products and services, and thereby contribute to filling the gap in the financial advice market. It is essential that banks are able to continue to provide low-cost, basic banking products and simple, low-cost financial services to their customers via different business models and distribution channels.

The ABA is pleased to continue to work with the Federal Government on implementing changes to the financial services laws in a way that minimises adverse and unintended consequences for banks and their staff and customers.

If you have any queries regarding the issues raised in our letter, please contact me or Diane Tate, Policy Director, on (02) 8298 0410: dtate@bankers.asn.au or Jade Clarke, Senior Policy Analyst, on (02) 8298 0404: jclarke@bankers.asn.au.

Yours sincerely

Steven Münchenberg