Strategy First Financial Planning Pty Ltd

submission to the

Inquiry into Financial Products and Services

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Mr Bernie Ripoll MP
Chair, Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Mr Ripoll,

Strategy First Financial Planning Pty Ltd is an independently owned financial planning business with its own Australian Financial Services Licence (AFSL 290771). This affords us complete autonomy from the constraints or influences of external affiliations.

The financial planners at Strategy First have worked together since 2000 and have the combined experience in the financial services industry of more than 40 years.

We specialise in servicing the wealth management needs of 'mum and dad investors', senior executives, professionals and business proprietors throughout Australia and abroad.

We are a **fee-only** firm where advisers are paid a salary. We do not accept commissions, brokerages or volume rebates from any product providers. We have intentionally structured the business in this way to ensure impartial advice and to protect clients from any conflict of interest.

I, David Price, the author of this submission, am the Director, the Responsible Officer and a Representative of Strategy First Financial Planning Pty Ltd. I have been operating as a licensed financial planner since June 2000. Prior to June 2000, I spent five years in the funds management industry.

I completed the Graduate Diploma in Financial Planning (from Deakin University) in 2002, have completed undergraduate studies in financial markets from the Securities Institute of Australia and postgraduate studies in applied finance from the University of Technology, Sydney.

Thank you, in advance, for taking the time to read and consider my submission.

Yours sincerely,
Strategy First Financial Planning Pty Ltd

David Price
Managing Director

Executive Summary

I welcome the opportunity to offer my input to the Inquiry into Financial Products and Services in Australia. I am confident this is the vehicle that will deliver the fundamental and comprehensive reform that is required to ensure the long-term viability of the financial services, particularly planning, industry.

I believe that the nature of remuneration through commissions and third-party payments has, regrettably, created an industry that is built on a structurally corrupt foundation.

This submission will address many of the inquiry's terms of reference, namely:

1. The role of financial advisers;
2. The role played by commission arrangements relating to product sales and advice, including the potential for conflicts of interest, the need for appropriate disclosure, and remuneration models for financial advisers;
3. The committee will investigate the involvement of the banking and finance industry in providing finance for investors in and through Storm Financial, Opes Prime and other similar businesses, and the practices of banks and other financial institutions in relation to margin lending associated with those businesses;
4. The need for any legislative or regulatory change.

It is my intention, in this submission, to outline the inherent problems that currently plague the industry and to offer recommendations that can pave the way to a more promising future for all stakeholders. In short, those solutions largely focus on the need to move financial advice to an industry-wide, fee-only model of remuneration and to ban all commissions and third-party payments.

My business partners (David Hardman and Patrick Anwandter) and I have the collective industry experience of more than 40 years, so as a team, we believe that we can speak with some authority. In addition, we have met with no less than 25 former Storm Financial clients over the past seven months to offer advice and support, pro bono. Through our extensive discussions with these clients, we have gleaned consistent evidence of the nature of the problems that ultimately led to the demise of Storm Financial, and more importantly their clients, in January 2009.

Let me say, from the outset, that I am proud of my role as a financial planner and the support and assistance that I can offer my clients; I am proud of the passion with which I run my business; I am proud of my highly qualified and dedicated team. Now, I want to be proud of the industry to which I belong. It is my firm opinion that only comprehensive reform will see the financial planning industry evolve into a respected profession.

This inquiry is the platform from which that comprehensive reform should, and I trust will, rise.

Introduction

I feel it prudent to reveal what I know of Storm Financial's demise as it puts into context my following concerns of the current structure of the industry and my recommendations for comprehensive change.

As mentioned in the executive summary, Strategy First has gathered consistent evidence of Storm Financial's operating and investment management methods through lengthy discussions with many former Storm Financial clients and two ex-Storm employees.

Storm Financial collapsed when the global financial crisis – a 1 in 50-year event - descended upon us all late in 2008. I acknowledge that this was beyond Storm Financial's control and that they should not be held accountable. That said, the foundation on which Storm Financial was operating, like many financial planning businesses, was fundamentally flawed. For this reason, there is much the financial planning industry can learn from Storm Financial's demise to ensure this disaster is not repeated.

Let me begin by discussing Storm Financial's approach to disclosure and how this clearly illustrates the limits of this protocol to truly protect all clients from acting on inappropriate and biased advice.

Storm Financial's process of disclosure, compliance and education of clients was of a very high standard, and arguably, industry best standard. Storm Financial ran many seminars and education sessions for prospective clients. This meant that when the clients received the Statement of Advice documents (again very compliant), they had received hours of 'education' (which was more like Evangelism) about risk and return, gearing, market volatility and the difference between short-term and long-term returns. Clients would have also known that they were paying a 7% up-front commission on the money invested and that Storm Financial was receiving a 0.3% p.a. volume rebate on all money invested with Challenger - and still signed off on it.

So despite all of this, why did many clients not understand the level of risk they were taking and why did the process fail to protect these clients?

This process failed because, despite the client education and disclosure, the advice given by Storm Financial which was completely inappropriate. That is, many of the ex-Storm Financial clients we met were not capable (due to the complexity of investment markets and their lack of investment experience) of making an informed decision. In that situation it was the professional, ethical and moral responsibility of the financial planner to make the decision. They did not.

Obviously, the up-front 7.0% commission the financial planner received and the 0.3% p.a. volume rebate that Storm Financial received, was a strong enough incentive for Storm Financial and its advisers to encourage clients to take on massive debt and unnecessary risks.

Storm Financial clients were fed spin and propaganda: the emphasis of all discussions and seminars was on the potential gains and robust nature of this solution, not on detailed risk analysis and unbiased advice. Meanwhile, the traditional 'selling triggers' of greed and fear were played upon by Storm's financial planners to ensure the client invested.

Worse still, Storm Financial's advice was completely inappropriate for many of its clients. It was not personal financial advice; they simply offered one solution, which was for clients to borrow heavily against their homes and to use this to leverage further into margin loan and invest 100% into Australian shares.

Storm Financial had a square hole and jammed people into it no matter their shape and size. For example, Storm Financial had clients on the Aged Pension and minimal other income signing up to borrow $1 million. Irrespective of market conditions, how is that appropriate financial advice?

This product, a margin loan, is not sophisticated. But by its nature, a margin loan should only be offered to people who meet certain criteria to ensure they can manage the inherit risks. In my opinion, a margin loan should only be recommended to people with:

- assets and cash flow, excluding the income from the investment portfolio, adequate enough to meet the cost of all interest;
- assets and cash flow, excluding the income from the investment portfolio, adequate enough to meet the contingencies of a margin call and;
- arguably an income high enough that they attract the top marginal tax rate ($180,000).

Storm Financial had many clients who were completely unsuited to its product. Some were at the end of their careers, some were earning very little income and paying minimal tax and, many that we met, had no way of ever making it back from the disaster that ensued.

In short, the problems of Storm were:

(1) Storm had a 'one size fits all' model of financial advice, which was inappropriate, not just for the majority of their clients, but arguably for most clients. Their processes meant clients maintained gearing at the maximum level at all times, so it was just a question of time before markets corrected and clients were margin called;
(2) The capacity [i.e. education, training, experience and independence] of the Storm 'Advisers' to provide appropriate advice [after all, they were all invested alongside clients] tells a lot about their understanding of markets and their ability advise others;
(3) Leading on from point two, Storm advisers followed the one size fits all model and directed all clients into it without considering whether the advice to do so was appropriate for that particular individual;
(4) The Storm fee model was biased towards clients investing the most they could, which maximised fees for Storm and its advisers and maximised risk for their clients;
(5) Greed. In the case of one particular Storm Financial office, we have consistent anecdotal evidence that suggests the financial planner there would say almost anything to clients get them to sign. One such example involved the financial planner telling a priest that "God brought you to me".

While eliminating commissions will not stop greed or such blatant untruths, surely it will lead to better business models that are designed with the clients' needs at front of mind.

Due to the 'marketing spin' promoted by the financial services industry, the complexity of investment markets and the lack of investment experience in general, many Storm Financial clients didn't have the capacity to understand the advice given. These are, unfortunately, the factors that affect many retail clients in the general community and, as such, these clients are very reliant on their financial adviser to give them appropriate advice.

This means that if the industry does not move to accept this responsibility, regulators must, by eliminating all conflicts of interest and any impediments to unbiased advice and trust. In addition, advisers must be independent in the true sense of the word and have the necessary education, training and experience to give appropriate advice.

Case Study 1

My case in point is illustrated by Sydney couple Peter and Lisa. Peter was aged 52 and a senior executive when he and Lisa were courted – for at least 12 months – by their financial adviser to sign up to Storm Financial's product.

"The financial adviser that I had used for the previous 12 years had suddenly formed an alliance with Storm. In fact, I think she had sold her business to them," says Peter.

"The Storm Financial seminar had a very positive spin. You could see the potential risks in it, but the financial adviser was quick to point out that if you went back through history, even to the Great Depression, their model was robust enough to survive that.

"My regret is that we were dragged into it because we were in a position of trust with our financial adviser. She glossed over it and I relied on her too much and trusted her too much."

When the couple took their financial planner's advice, they only had a debt of $245,000 (their home mortgage). After signing on the dotted line, their total debt jumped to $1,925,000: more adventurous than Peter had ever contemplated.

Had Peter and Lisa known then how Storm Financial and the Commonwealth Bank Australia (CBA) would later manage theirs - and other clients' - investments when the market did plummet, they would never have entered the agreement.

"Our biggest issue is how poorly Storm and CBA managed it during the downturn. I was contacting people constantly but there were never any answers," says Peter.

"Our particular investment had been allowed to decline to a point where it was actually less than our loan. When we got to an LVR (loan to valuation ratio) of around 80% we gave permission to turn our investment into cash as a holding position, but that action wasn't followed and it wasn't turned into cash until six weeks later when the loan was 115% of the investment."

Peter and Lisa now accept they will have to work longer and push back any plans for retirement, and they have no cash flow to allow them to make bigger purchases such as cars or holidays. They expect that when the Storm Financial debacle is wrapped up they will be in debt for $1 million.

Case Study 2

Policeman Ray was on duty in October 2000 when he lost control of his motorbike on the Sydney Harbour Bridge. He was so badly injured, mentally and physically, that he would never again be able to hold down regular, full-time employment. As a result, the NSW Government granted him a pension - about $1000 per week indexed to CPI - that was guaranteed for life.

In 2007, Ray was given a choice: continue drawing the weekly pension or take a $606,000 payout. It was at that point that he, and wife Jane, sought out financial advice, which came from Storm Financial. "We wanted to know what our best option was, to take the payout or stay on the pension?" says Jane. In short, they wanted advice, not products.

The couple attended seminars organised by Storm Financial; they asked questions, voiced their concerns. But the spin was always the same. "They told us, over and over, 'don't worry about it, that's what we are here for, you go and enjoy your life'," recalls Jane.

Ray and Jane trusted Storm Financial. They wanted to believe with all their hearts that Storm Financial would, in fact, meet its promise and look after them. So they pulled their money out of superannuation, paid the tax and invested their money – along with a margin loan from Macquarie Bank – into the Storm/Challenger Managed Investments.

But they were in over their heads and they were unsure of their financial investment, especially when Storm Financial urged they take out another loan with the Bank of Queensland. "There were certain things we didn't like about it, like borrowing extra money," recalls Jane. "We kept saying 'we don't want to do this because we don't want to lose our home'. Ray was so strong about that, but they said to us, 'there is no way you will ever lose your home, ever'."

In October last year, Ray and Jane became very nervous as they watched the financial markets plummet. Jane called Storm Financial for more advice. "Don't worry," they repeated. Despite Jane and Ray asking Storm to cash out their investment, it didn't happen until late November when Macquarie sold their investments. Jane and Ray paid off the Macquarie Bank loan, but had nothing left to pay out the Bank of Queensland for $550,000. That bank now holds the mortgage papers to their home.

"In hindsight, we weren't good candidates for a margin loan. We kept saying to them, 'aren't we a bad risk?' They kept saying 'it's okay, don't worry, that's what we are here for'," says Jane. "We have nothing now. We have gone back to what we were when we were first married, and we may still lose the house. It's really, really hard."

These tales from both clients are tales of financial woe that, unfortunately, mirror that of thousands of other ex-Storm Financial clients.

1. THE ROLE OF FINANCIAL ADVISERS

Discussion

The goal for all financial advisers must be to provide independent, impartial and appropriate advice that is tailored to a client's personal objectives.

Clients, generally-speaking, will put their faith into their financial adviser, believing that the adviser has their best interests at heart. Because clients are often not savvy to the intricate dealings of the financial products industry, they trust their financial adviser to advise them on how to manage what usually amounts to their life savings.

For this reason, it is the responsibility of the financial adviser to understand financial markets, to know, intricately, the nature of all the financial products and to keep abreast of changing legislation. Only then can a financial adviser know what advice, including financial products if appropriate, best suit the needs of the individual and to tailor the advice accordingly.

Please note that the best advice is often to not purchase a financial product.

Recommendation

The problem I see with the industry in its current format is that there are financial planners throughout Australia who don't meet the aims mentioned above. This stems from the fact that the majority of financial planners are not financial advisers, but are merely financial product advisers (sellers). The sole motivation of these financial product advisers is not to give independent advice tailored to the individual client, but to simply sell the product to which they are aligned or that maximises their remuneration.

I will discuss the nature of product aligning arrangements (and the problems with this) in more detail throughout this submission. Here, I would just like to offer my recommendation with regards to the definition of the financial adviser.

We have an industry where approximately 80% of financial advisers are owned by, or aligned to, product manufacturers, including administration platforms. This means that the majority of clients seeking financial advice throughout Australia are not getting independent advice, but solutions built around products and their distribution.

In an ideal world, there would be no product alignment in the financial planning industry. The first step towards this is the complete removal of all commissions on all financial products. I say this because I am realistic enough to know that, in the short-term at least, we will not be able to separate financial planning businesses from financial institutions and product manufacturers like MLC, AMP and the big four banks. Doing so, considering the current business model, would send many financial planners into insolvency and this would result in many Australians having no access at all to any kind of financial advice. This is a result that is obviously not ideal during such trying times.

Another feasible solution is to create a clear distinction between 'financial product advisers' and 'financial advisers'.

Financial product advisers would be able to continue their role of simply selling one or more financial solutions to which they are aligned. Disclosure rules and regulations must be followed stringently by these advisers so that the nature of their business is completely transparent to the client.

In fact, we would recommend new legislation that limits financial product advisers to providing advice only on the products manufactured or managed by the institution to which they are licensed: A bit like going to a Holden Dealer to buy a Holden Commodore – the consumer knows that they are going to be sold a Holden.

There would also need to be a widespread public awareness campaign to educate the public on the differences between these two categories of financial planners so that clients can make an informed choice from the outset.

The second group in this industry, financial advisers, would have to meet stringent criteria of experience, education and business structure to be able to call themselves financial advisers. For example, they would have to hold their own Australian Financial Services (AFS) licence and have no ownership links to product manufacturers or administration platforms. They must also meet ongoing compliance regulations with a peak industry body or ASIC to ensure that they do not form alliances with any product manufacturers to take advantage of any third-party payments, bonuses, discounts or incentives.

Financial advisers must operate solely on a fee-only basis and not accept any commissions, brokerages or volume rebates from any product issuers.

Summary of recommendation

The creation of two distinct professional titles to improve transparency between those advisers who provide financial products and those who provide independent advice.

2. THE ROLE PLAYED BY COMMISSION ARRANGEMENTS RELATING TO PRODUCT SALES AND ADVICE, INCLUDING THE POTENTIAL FOR CONFLICTS OF INTEREST, THE NEED FOR APPROPRIATE DISCLOSURE, AND REMUNERATION MODELS FOR FINANCIAL ADVISERS

The premise under which this industry was formed is fundamentally flawed and has left a legacy that undermines the financial planning industry's ability to provide independent advice and become a profession.

The financial planning industry was established in the early to mid-1980s on the back of services provided by large life insurance companies such as MLC, AMP, Zurich and AXA. These companies created savings products, which they took to the market through sales agents, who received 10% to 12% commissions.

The one positive element to come from the work these product agents performed was the recognition of the need for an industry that offered personal financial advice and tailored solutions and products. Hence, the evolution of the financial planning industry.

Since then, there have been attempts to regulate the industry, as it moved towards a profession. The most notable of these attempts was the establishment of the Financial Services Reform Act in 2001. This legislation was incorporated into the federal Corporations Act and introduced a uniform licensing system, disclosure regulations and a standard code of conduct for financial service providers.

While an improvement, this has only been a ‘bandaid solution’, because it has failed to address the industry structure. It did establish the disclosure regulations that are now common practice and provided a code of conduct that all advisers should abide by. That said, and as proven by the number of accountants who were caught up in the Timbercorp collapse, an industry code of ethics does not always protect against the ‘easy money’ of commissions. Timbercorp gave limited authority to accountants to ‘sell’ Timbercorp investments to their clients and, as a result, received 10% commissions.

Many industry participants suggest that it is not commissions, but rather disclosure that is required to protect clients. Surely the example of Storm Financial and others over the last 18 months suggest that disclosure is not working or not being adhered to.

There are at least three basic steps a financial adviser must go through when dealing with a new client:

1. provide a Financial Services Guide (FSG) which outlines how the adviser will be paid;
2. provide a Statement of Advice (SOA) document that clearly outline the fees paid in dollars;
3. and, of course, explain to the client every element of the recommendations being made, the clients’ rights and responsibilities plus the risks, benefits and costs of any advice.

The problem is that FSGs are often so complicated (due to all third party arrangements), that clients don’t understand the implications for themselves or what they are actually paying for advice. Then they receive an SOA - and this can be 70 pages long and very involved – but, again, the key points and the implications may be lost within in the lengthy document.

Just because an adviser has met these requirements on paper doesn’t mean they have focused on it explicitly and ensured the client has understood the terms. More to point, just because a client knows what the adviser is getting paid doesn’t mean that the advice they are getting for that fee is appropriate.

Again Storm Financial and their advice to have aged pensioners borrow in excess of $1M and invest in the Australian sharemarket is an example of this.

Recommendation

The separation of advice and financial product is an absolute precondition for quality, independent and appropriate advice. This separation must pertain to both ownership of financial products and remuneration structures.

It is my recommendation that all commissions, volume rebates and brokerages be banned and that a fee-only structure become mandatory for financial advisers. Financial advisers should not receive remuneration of any sort (salary, bonus, stock options/shares, incentive trips, subsidised training, research or rent) based on the volume of client money they 'direct' into any one financial product, including loans or administration platform. The practice of receiving trail commissions from the financial products sold to 'legacy clients' must also be stopped.

In addition, AFS licence holders should not be able to 'badge' administration platforms, or have preferred product lists that result in them being paid volume rebates.

Instead, all financial advisers should only be paid by clients, with the amount, method of calculation and collection agreed to by mutual consent between the client and financial adviser. The client must also have the ability to turn this payment method off if they are not receiving the level of service they were promised.

With respect to the ownership requirements of financial products, my recommendation is that all institutional groups like (but not limited to) AMP, Westpac, Commonwealth Bank Australia and the National Australian Bank that manufacture products, should be restricted from owning financial planning businesses. I realise this is not a short-term solution, so I would envisage that a five-year moratorium be established to allow for this to occur. During this time, their advisers would fall into the 'product advisers' group.

I feel that moving to a fee-only structure will achieve numerous wide-ranging benefits such as increased trust in the profession by the community. This will have the two-fold effect of encouraging more people to seek financial advice and, thereby, create a more financially savvy public. This, in turn, will provide greater financial protection to clients and ensure the viability of the industry well into the future.

Secondly, this will ultimately reduce the cost of financial advice to clients and reduce the burden of disclosure compliance for financial advisers. By negating the need for detailed FSGs and lengthy SOAs, when not required for simple advice, financial advisers do not need to spend as much time on each client's case, thereby reducing their fees. Secondly, as there will be no commissions (up front and especially ongoing) paid to financial advisers, the cost of financial products will also fall significantly.

Summary of recommendation

All commissions, volume rebates and brokerages on financial products to be banned and replaced by a mandatory fee-only structure for financial advisers. Secondly, all institutional groups that manufacture products must not be permitted to own financial planning businesses long-term. In the interim, they must meet separate requirements as 'product advisers'.

3. THE COMMITTEE WILL INVESTIGATE THE INVOLVEMENT OF THE BANKING AND FINANCE INDUSTRY IN PROVIDING FINANCE FOR INVESTORS IN AND THROUGH STORM FINANCIAL, OPES PRIME AND OTHER SIMILAR BUSINESSES, AND THE PRACTICES OF BANKS AND OTHER FINANCIAL INSTITUTIONS IN RELATION TO MARGIN LENDING ASSOCIATED WITH THOSE BUSINESSES.

As mentioned, my knowledge of the Storm Financial situation is based on anecdotal evidence collected through discussions with former Storm Financial clients. As such, following is an account that I feel confident is accurate given the consistency of the nature of those conversations.

Storm Financial had negotiated special deals with the banks with which it was aligned. These included the CBA, Bank of Queensland, ANZ, National Australia Bank and Westpac.

The average loan-to-valuation (LVR) on margin loans is 70%. Storm Financial, however, negotiated an LVR of 80-90%, meaning the clients were operating under a structure of greater risk than normal.

The standard protocol is that once an LVR is triggered, the margin lender contacts the adviser, who, in turn, is to contact the client within a three-day period to manage the situation. Storm Financial had negotiated a five-day period, so by the time Storm Financial advisers had contacted clients, the market had dropped so significantly that some clients had negative equity.

The banking sector must take some responsibility in failing to protect clients by not enforcing better constraints on its lending practices. Evidence that has come to light recently has shown that the banks have failed not only in protecting Storm Financial clients, but clients of numerous other failed ventures also.

For example, *The Australian* newspaper reported in an article on June 18 this year that:

> *In 2004, NAB lost its chief executive and chairman and initiated a sweeping review of its risk management operations and internal culture after rogue traders lost $360m betting on currency markets.*
>
> *Last year, ANZ chief executive Mike Smith launched a "warts and all" review of the bank's involvement in so-called stock lending after being caught up in the collapse of broker Opes Prime.*
>
> *ANZ, which has been forced to book provisions for hundreds of millions of dollars of losses relating to the Opes debacle, has sacked several executives even though the review found no wrongdoing.*
>
> *The big four Australian banks are carrying provisions for up to $14bn in bad loans to companies that foundered during the global financial crisis, including Opes, ABC Learning Centres and Babcock & Brown.*

Meanwhile, in the same article, it was apparent that the CBA recognises it is not blameless in the Storm Financial disaster.

> *CBA chief executive Ralph Norris, who initially played down the bank's role in the collapse of Storm in January, said yesterday it had identified "shortcomings" concerning loans it made to Storm clients.*

The issue is understood to involve some customers being granted loans they were unable to repay.

The bulk of money lent to Storm clients was in the form of margin loans - often secured against the homes of mum and dad investors - which was then ploughed into the stockmarket ahead of the crash.

In the fallout of the Storm collapse there have been widespread claims of mortgage application "irregularities" from investors, with some claiming loan forms were completed without their knowledge. The CBA would not elaborate on the "shortcomings" it had identified in its lending procedures.

Recommendation

While not in a position to provide input into the internal compliance and risk practices of banks, as a financial adviser I understand the link between the loans (home loan and margin loan) provided by banks and the way they remunerate the financial advisers and mortgage brokers that distribute them.

Not surprisingly, large commissions paid on the amount of loans written have played a role in the billions of dollars lost by investors and the collapse of associated businesses over the last two years.

When an adviser is incentivised to earn more money when their client takes more risk, the model is broken. Opes Prime, Lift and Storm Financial are all examples of where the remuneration model drove advisers to 'gear-up their clients' during a time when that was not the most appropriate advice.

It is my recommendation that all commissions and remuneration models that are based on a percentage of assets or loans be banned.

Summary of recommendation

Ban all percentage based remuneration and commissions associated with the distribution of loans of all types.

4. THE NEED FOR ANY LEGISLATIVE OR REGULATORY CHANGE

The financial planning industry will never regulate itself, so unfortunately, legislation and motivation must be put in place that is greater than the current incentives offered by the industry that is stalling change.

I have already spoken about legislative change that involves:

1. banning all commissions, brokerages and third party payments paid to financial advisers;
2. having two clearly defined categories of financial planners, so that one gives product advice on a limited list of products only and one provides personal advice;
3. putting in restrictions regarding the ability to or how financial institutions can own and operate financial planning businesses.

We note that in relation to point two, ASIC is already suggesting similar change for Superannuation Funds and related advice, which is outlined in Regulatory Guide 200.

http://asic.gov.au/asic/pdflib.nsf/LookupByFileName/RG200.pdf/$file/RG200.pdf

This can solve the problem of conflicted advice provided by product manufacturer owned salespeople by limiting their scope of advice to their products.

Recommendation

In addition to the above mentioned legislative changes and to counter the common industry argument that banning commissions would make financial advice too expensive for low income clients (which we believe is incorrect), we recommend that associated with the two categories of financial planners, legislation is introduced to make the fees charged for genuinely independent financial advice:

1. tax deductible for high income earners, and;
2. rebatable against tax payable for low income earners.

In addition to this, and only applicable to low income earners, the government could consider a form of Medicare Rebate for fees paid for genuinely independent advice from financial planners that meet a very strict list of criteria.

While this may seem like an expensive option, it is my belief that the money saved through cheaper financial products and a reduction in the number of financial disasters and ensuing inquiries would be more than enough to cover such a cost.

Summary of recommendation

Make the fees for independent financial advice tax effective and consider a Medicare-style rebate for low income earners.

In conclusion

I believe the quality and appropriateness of advice to all clients starts with the industry becoming a profession that puts the client first and focuses on duty of care, ethics, independence and ongoing education and training.

For this to occur there must be clear and distinct separation between product, distribution and advice.

I welcome the new direction the Financial Planning Association of Australia (FPA) is taking in its discussion paper that recommends fee-based remuneration be adopted as the standard model of payment for financial advisers from 2012.

The FPA has avoided taking this course of action in the past and I can only assume that is because the majority of its members run businesses that are wholly subsidised through commissions, volume rebates and brokerages.

I also support the IFSA’s call for change to a more transparent fee-based model in its new charter announced on June 17, 2009.

I feel that it is poignant that the peak industry bodies have finally realised that they can no longer avoid the need for widespread, comprehensive change.

Australia needs to only look to the UK to see that reform is long overdue. On June 25, it was reported in the *Financial Times* online edition that the Financial Services Authority would outlaw payments from fund managers and life assurers to advisers in three years.

The article continued:

> *Commission payments have been blamed for mis-selling scandals over the past 20 years involving mortgage endowment policies, personal pensions and stock market-linked bonds.*
>
> *The watchdog said it would ban product providers from offering commission to secure sales and ban advisers from recommending products that automatically paid commissions.*
>
> *Instead, investors will be told up front how much advice would cost and will be able to choose whether to pay a fee or have the cost deducted from their investment. Crucially, the amount the adviser receives for recommending a product will be negotiated with the investor and not determined by the provider.*

Now is the time to advocate for change and to set in motion the job of reforming the financial planning sector.