

# **Enquiry in to Financial Products and Services in Australia**

**Submission by Interprac Ltd  
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### **About us**

Interprac Limited is a business that was initially set up by accountants for accountants as a hub to provide a place with expertise for accountancy practise client's to obtain financial services advice.

The focus was to have a professional that would act on behalf of the client without any bias towards a product supplier.

Interprac Limited provides accountants which are primarily those that are members of the NTAA (National Tax Accountants Association) access to 5 specialist business units that offer this referral resource.

The business units are:

1. Mortgage broking for an accountant and their clients
2. Vehicle and Equipment Finance Broking for an accountant and their clients
3. PI insurance scheme for accountants
4. Financial Planning License that offers the opportunity to license accountants that have the necessary training to be an authorised person.
5. A Corporate business that establishes companies, trusts and Super funds on behalf of an accountants clients

As a market participant in many of the areas we would welcome the opportunity to discuss our views in regards to the enquiry in more detail .

### **Summary**

As a participant in the industry and current holder of an Australian Financial services license (Interprac Financial Planning Pty Ltd AFSL 246638 ) we see the inquiry as providing a positive step towards improving the understanding of the role of a financial planner within the community.

We take this opportunity to provide our views to the committee from a position where we are well aware of the various needs of consumers seeking financial products and services and cognisant of the areas of primary concern.

At the coal face it is evident that the community is not proactive in seeking financial advice at the level we would consider appropriate and therefore necessary.

The latest Financial Planning Association (FPA) figures show that approximately 75% of Australian adults do not have a relationship or have sought a relationship with a financial adviser.

More disturbing 85% of advice that is given to a retail investor comes from advisers that represent an AFSL that is owned by a product provider.

In addition, in the case of Industry Superannuation funds the advice is given where there is clearly a lack of potential distinction and transparency to the customer between products available in the market place.

Interestingly, we are seeing industry funds offering a fee for service option to members that seek additional advice, the concern we have with this advice is that it generally does not allow any sale of product or entry to product other than to their own funds. This is an issue we will discuss in more detail within our submission.

On a positive note surveys undertaken by the regulator ASIC has shown that they have an overall confidence in the Financial advice industry, and in their opinion the current standard of advice that is given to clients is adequate.

It is also positive that industry bodies such as AIOFP recognise the need for the industry to continually improve its levels of education, services, scope of advice and transparency.

Our submission to the committee will support this stand.

### **Our position**

Our position is that the reforms undertaken in the Financial Services Reform (FSR) regime are generally working well, however we do see the need for some fine tuning to ensure a greater transparency for consumers who actively seek advice for their financial affairs.

We see this fine tuning that is required to be most important at the product manufacture, consistency of remuneration, licensee approval and in the area for providing a greater clarity of advice.

For those that give advice we see there is an absolute need to offer clients distinct payment options to have access to the said advice.

We see that remuneration on product sales via a commission, fees for service and the option for a salaried person of a single based product. as the 3 remunerations options that need to be available.

It is vital for both a commission or a fee for service option to be maintained to traditional authorised persons.

In our opinion all clients should be offered choice, and alternatives clearly described at the outset of the advice provided should be clearly disclosed in the Financial services guides of licenses.

In our opinion the greatest concerns that have resulted in the need for this enquiry seem to be centred on product failures or a misunderstanding of products sold that have caused loss or dissatisfaction with investors.

In the cases of Opes, Storm Financial, much of Great Southern and many of the failed Debenture issuers, the clients who suffered loss were primarily those made from sales of the license owners own products , salaried staff , or products manufactured that were exclusive to the licensee owned business.

Primarily and of importance to note this was not as a result of whether there was a commission paid on product sales or a fee for service being charged for the advice provided to clients.

In most cases it does not appear from our readings and research that these losses were as a result of the advice process being incorrect but more directly from the licensee acting as a retailer, and manufacturer of product that failed in the market place.

We see this as the greatest issue causing a loss of confidence in the advice process within the industry.

Prior to the changes of FSR, most advisers acted as an agent of the product manufacturer and both the adviser and manufacturer were responsible for the advice given.

The manufacturer in this case was responsible for both the advice and the product, and provided tighter compliance and training regimes for those agents of their own.

Under FSR the licensee is now responsible for the advice of the authorised representatives and as such, each license should, and must determine a reasonable process for the accreditation of products on an approved product list for the agents of the licensee (Authorised representatives) to be able to recommend.

In the case of Product Manufacturer owned licensees we believe this process is outside the spirit of the reforms and many of these licenses are a sales force of products or in many cases a single product seller and the imbalance between sales , remuneration , product research and an advice capacity is very difficult to determine .

On this basis we believe that product manufacturer owned licensees should be required to provide greater disclosure in regards to their ownership and be required to follow a more consistent research process for owned and non owned products.

This greater transparency should include that the licensee should carry the product name in their AFSL name.

The sales commission on their products should also be exactly the same for their own license as it is for others and no special incentives for selling “own product” should exist.

If “own product” is paid preferentially to an authorised representative it is outside the reform requirement for a licensee to be seen to representing the client.

On this basis the consumer will have a greater understanding that the advice being given from authorised persons is being provided consistently across the industry.

Undoubtedly there will be times when the house product is the most appropriate for the client, but if the process is the same for all licenses it is less likely that there is a home product sale being made because of remuneration advantage opposed to what is best for the client in an equal playing field.

In the case where ONLY products of the manufacturer are able to be recommended within a license, our opinion is that these advisers should be salaried employees much like industry fund employees and not be paid on a commission scale basis.

It should also be clear in statements of advice to clients that the advice they provide is that of an employee of the product provider, and restricted to such advice so clients do not misunderstand that the recommendation being made is any different from that of any other product that is sold by an owner of the product. (i.e. a Holden dealership sells Holden's.)

At present we believe that the current Legislation where a licensee is not owned by a product provider but products that are on a recommended list come from a researched viewpoint, we believe the advice process does provide consumers a value added service.

The process to be placed on any recommended list of licensees is an onerous one and in the spirit of the Legislation provides a process that most retail investors could never undertake in a cost effective manner.

This process to why an adviser recommends one product or strategy over another could be better expressed in part of the statement of advice and we would like to see the regulator therefore create a standard template for licensees to include that they are satisfied, provides transparent disclosure in this regard.

We feel product choice or selection of product the planner makes from this list of choices should also be included in the statement of advice, but in a limited form as too much information confuses rather than informs the majority of retail clients. .

It should where appropriate also clearly state if an adviser has restricted choice of product options to disclose this.

The fact that the independently owned license looks at product by product to determine a list is vital for inclusion however to include this actual process in every advice recommendation with a consumer would create even greater confusion in the mind of the individual

All of this is undertaken in our opinion in a market that requires competition, disclosure, suitability, and transparency between the product manufacturers.

We believe there is some merit to say that licenses who try to act in both capacities ie offer products out to market yet also have single product sales forces on higher remuneration levels with the only function to have advisers who act on their behalf should be terminated.

The Great Southern plantations AFSL license was a prime example of this.

## **Advisers Role.**

The role of the financial adviser has never been more important than ever in the history of financial services advice.

Our population is aging; the compulsory superannuation Legislation has seen more Australians than ever before have large investment balances that they need to understand. Less than 75% of consumers have an adviser and international investment markets are experiencing volatility that only the more experienced participants tend to comprehend or understand.

In looking at the role of the adviser, our belief is the consumer wants and needs a trusted professional who is able to assist them in managing and understanding those affairs relating to their financial situation.

Someone who understands the client's situation, acts with honesty and fairness, and has high levels of competence in the area of advice is the answer that the client seeks.

It is someone who also understands the investment market, can make recommendation/s on a range of products, and can partner with the client from the introductory meeting throughout the lifetime of the clients needs.

In looking at the inquiry we strongly stress that clients be able to continue to be able to seek the alternative method of paying for advice either by a fee for service or by the adviser receiving a commission on products recommended and completed by an adviser.

In our view most retail clients want to avoid paying fees for service but will however accept that there is a commission payable on product sales to financial planners.

As a business that works very closely with accountants, who almost exclusively charge their clients a fee for the service or in time increments, we recognise the consumer does not want to do this.

If it was compulsory to see a financial advisor before investing just like it is compulsory to lodge a tax return with a fee for service model pertaining to each respective business operation it would be possible but it is not in the current operande.

Already too many Australians do not seek out available advice largely because of the perceived cost to get advice, and by restricting the options for all parties to get advice to fee for service, only those with larger investment amounts or greater net wealth will seek out the service.

As such it is vital choice of how the advice is paid for continues.

The changes made under FSR have been excellent in this regard.

The fact that advisers must disclose the cost of the products recommended and the commission that is payable to the license and then the advisers share is not broken.

The FSG and statement of advice requirements for all retail clients offers transparency and provides clarity

We do however believe that the inconsistency of commission amounts needs to be further investigated and propose a more level means of product commission be introduced.

We believe the model of the general insurance industry is more transparent in that generally speaking a license receives the same commission percentage irrespective of the insurer they recommend.

On Life insurance products such as Term Life, Income Protection, and Trauma Insurance we would recommend this be initiated in 2 forms.

An upfront commission with a low renewal component or

A level commission amount payable each year.

In this regard we would propose a reasonable level to be

Up front 100% of 1<sup>st</sup> years premium  
Renewal 10% of annual premium paid or

Level 25% of every premium paid

Currently there is a variety of commission's payable between 80% up front to 120% up front plus incentives and there is scope for the advice to be perceived as being influenced by the level of one company's commission rate over another's.

In the case of the Life Company owned licenses there is clearly a benefit for sale of owned products in adviser's commissions' packages that are not consistent with other products on their lists.

The average Life insurance premium is approximately \$600 per year, and the requirement on the adviser is to

1. Meet the client and conduct a fact finding interview
2. Prepare a strategy and provide a client a statement of advice recommendation
3. If agreed upon complete an authority to proceed and complete all paperwork of the life office and lodge the application
4. Follow up doctors with medical information, to see the application is accepted
5. Establish an annual review of the client's affairs to continue to ensure the cover is appropriate for the clients needs.

On average this process takes around 8-10 hours per application.

In regards to Managed funds, Wrap accounts and Master funds there could be some consideration to having a fixed capped component of commission on the funds under advice, as well, as an option for an adviser to charge an adviser service fee from the account.

What is appropriate to be an amount to fix trail at is very difficult to determine but a starting point may be

UP to 100,000	0.6%
100,000 to 1,000,000	0.5%
Over 1,000,000	0.25%

In the case where clients do seek a fee for service only, this fixed commission component can then be refunded to the client.

Generally speaking the time required to see a client with \$50,000 to invest compared to a client with \$1m to invest is not that much different, which makes the fee for service option tend to be only cost effective for larger clients but ineffective for smaller clients who arguably need the advice far more.

Again generally speaking a typical standard financial plan, including gathering of information, researching funds, preparing strategy, providing statement of advice and then providing a reasonable service level per annum is at a minimum at least 20 hours per annum.

To charge a client with a \$50,000 account balance or wanting to look to take out an insurance policy to protect their income on an up front basis for 20 Hours of time is not efficient for the market.



As a result planners have tended to recover smaller client acquisitions as a loss leader component of their business, and receiving the trail income over the life of the advice is the only real way to provide a high level of service to clients with small portfolios.

In getting back to supporting the offering fees of for service , in conjunction with commission payable under a capped fixed amount , an adviser in conjunction with a client can always agree to provide the full service by allowing an adviser to dial up a adviser service fee payable from the product provider works most efficiently and is very transparent.

The cost of the product with all products paying the exact same amount, and then separately the cost of the advice is very clear in this proposal.

Under this proposal the commission component will be consistent amongst every fund, and the cost of the product differentiation will be easier for licensees, the regulators and the consumers to identify.

In respect to up front fees payable to advisers on managed funds wrap accounts etc we believe the current system is efficient and the requirement for full disclosure to say what this amount is operating well.

Further in respect to advisers we propose the following

1. The education level outlined in RG 146 continue
2. That adviser must complete 36 hours per annum of approved training
3. That each adviser of a licensee is audited by an external compliance provider on behalf of the licensee and this audit is available to the regulator.
4. That every adviser must come under a Licensee.
5. That a single adviser cannot also be the Licensee
6. That each adviser has or is named on the licensees PI insurance
7. That every adviser belongs to an industry body such as the FPA, AIOFP, CPA, AFA etc.

## **Role of Licensee.**

We see the changes that the FSR enacted to have been overall very successful and the role of the licensee to act on behalf of the client to be one of the most important and effective changes the industry has undertaken.

This function though has tended to have been broken down a little with so many licenses now owned by product manufacturers.

As we view the roles we see the role of the licensee to encapsulate all of the expectations of the regulator in respect to improving the access of advice for retail investors and ensuring that the quality of advice is forever looking to be improved.

The licensee has under the changes the lead role in providing advice on products and services to the industry.

This role needs to remain clear in the process of a clients understanding of what all parties roles are, and is instrumental in the important role of seeing more and more Australians having access to advice in a cost effective and professional manner.

Our submission to the committee is that there needs to be greater clarity in respect to the following roles

1. The product manufacturers should be differentiated on the value their product provides to the end consumer. As such our earlier submission that all commissions payable to authorised representatives via a license is the same irrespective of which license or which Life insurers or fund managers are recommended.
2. Advisers are accountable to a licensee that has the sole role of being a licensee.
3. ASIC and any other of the regulators assist licensees with surveillance of authorised representatives of licenses.
4. A license holder must not be a single adviser business, and there is a distinct level of regulation between the licensee and the authorised reps that represent the licensee in the advice process.
5. A licensee that has “House Product “have greater disclosure requirements .advice.

In addition to the above submission we feel there is a swing towards advisers taking out their own licenses because they do not enjoy being subject to a licensee compliance regime.

The need for a Licensee and the adviser to be separated is vital, so that all representatives have a clear minimum level of support and surveillance.

As the licensee provides the advice and support of its agents, then it is important that the level of minimum support be provided to every authorised representative under their license, and these need to include

1. Research and a clear process for advisers to have access to on all products on a recommended product list
2. Be provided regular education to achieve a minimum of 36 hours of education per annum

3. Have a compliance and procedures manual for advisers to follow
4. Have an external audit of all advisers to ensure that the advisers are following the licensee's compliance program.
5. Have a Regular surveillance process in addition to external audits conducted by the license to ensure an adviser is following the stated guidelines
6. Ensure that all advisers have adequate PI cover in addition to the cover the license provides.
7. Ensure there is a minimum of 1 full time responsible person employed by the license at all times.
7. Ensure that all documentation that is given to clients is clear and concise. (FSG, business card templates etc.)
8. Be a member of FOS and one of the industry organisations like FPA or AFA.
9. To ensure there is a distinction between an adviser and a license have minimum of ten authorised representatives requirement for each licensee.

## **Role of regulator**

We believe the current regulator ASIC has provided the industry a very clear path on the requirements it has so that the public has greater confidence in the seeking of sound financial advice.

Unfortunately the international environment has seen many quality businesses particularly in the US suffer and in the wake of this many products that in a bull market should have performed well have failed.

These losses have highlighted all parties in the industry with product providers, advisers and the regulator all being the brunt of much of the Medias criticism of the industry.

In our view the role of the regulator is at this time in the right balance between that of a law enforcer and that of assisting the industry reach benchmarks it aspires to in the provision of financial advice and product sales

In respect to the functions of the regulator we would like to make the following comments.

### **1 The role of licensing**

We believe there are too many licenses and generally speaking that profitability of licenses is low.

As such we believe that a greater compliance and disclosure requirement be implemented for licenses that are owned and subsidized by their product owners.

We also believe that a license should have the function of being a license and as such have a minimum of 10 authorised steps it is responsible for in regards to education, compliance and giving its authority to act as agent for.

### **2 The role of compliance.**

As ASIC is the watchdog, and licensees are in fear of losing their license to operate, there can be a reluctance to seek aid and assistance in best practise and the understanding of the ASIC view on various areas regarding maintaining total compliance.

We feel there is room for the regulator to support licenses wanting to continually improve their understanding of the ASIC view on a range of issues so that best practise can be undertaken on an ongoing basis in an ever changing environment

The current perception of inviting ASIC out to a license for fear of increased surveillance / enforcement capacity needs to be better communicated.

### **3. Complaints**

The introduction of FOS and continuation of ASIC has made it very easy for a client to make complaints in the market of obtaining financial advice or product recommendation.

We do not believe the process is broken and the requirement for every license to have a dedicated complaints handling process is very efficient.

The requirement for minimum PI cover and the disciplinary measures available from FOS and ASIC are effective on seeing that licenses do everything within their power to have their agents acting in a honest, and efficient manner at all times.

## **Role of product providers**

As previously discussed we believe that by allowing the product providers to own 85% + of the adviser market, the industry has suffered a significant loss in credibility.

In our submission and again in this area we reiterate that this ownership bias is by far the most single reason why the public has lost confidence in seeking advice on their financial affairs.

The ability of a product manufacturer to dictate the cost of the product, the amount of remuneration an adviser generates and then places a restriction of what products are able to be recommended needs to be changed if we are going to have an efficient market place.

Without repeating our comments we propose

1. A Greater disclosure requirement for a licensee that owns product to include that name in the license name, this could be where the product manufacturer holds in excess of 50% equity of the license. ( e.g. All National Australia Bank owned licenses be called National Bank Financial Planning )
2. All Insurance companies pay the same level of up front and trail commission on their products.
3. All managed funds, Platforms; Wrap accounts have the same in built trail commission on a capped basis. This would ensure that there was no perception an adviser was making one recommendation over another because of the level of commission paid.
4. That no marketing income or override is payable to or passed on to any authorised reps of a license. This income however is important and should be shared with Licensees as it reduces the cost of product to market. As discussed earlier the function of the licensee should be to provide training, education and compliance support to its entire license. This allowance is primarily in the area of platform business and we propose that these marketing fees be a consistent formula across the industry. As the savings is a savings to the platform provider as the function of growing Funds under management is reduced through distribution support this ultimately allows the fees of platform providers to be lower than they would normally have to be. The important component however is that all of the marketing fees should be the same and this formula are disclosed in the PDS, within every SOA, and FSG of each licensee. By sharing the saving a product manufacture enjoys on achieving greater funds under advice it supports the competitive needs of the market place allowing product providers to reward volume, but without an ownership requirement to do so. It also allows all platforms to be equal and then licensees

and their advisers to receive remuneration at the same level irrespective of any special deals or relationships one platform may have over another.

### **Remuneration of Advisers**

As discussed previously we believe it is vital that the industry maintains the options of commission and fees for service when offering clients a service or placement of a product.

Already too many Australians do not seek advice from a planner because of many reasons, but one being a factor of cost.

The fee for service only model will make the cost of advice prohibitive for most working class Australians. It will also play in to the hands of the product providers who look to sell direct product to clients without the education or lack of bias an adviser brings to the role.

The examples where advice was provided on a specific product such as that of the leveraged equity strategy for Storm Financial clients is a classic example of this.

As previously discussed the need for a more transparent remuneration structure is vital, and achievable if the industry implemented a set benchmark for commission of products that was the same across the industry.

There is no doubt the industry would implode if commissions were banned , and that the cost of obtaining advice would increase and only be available to the highest net wealth earners.

Further more the need for the licensee to be separate from the adviser is paramount in the remuneration equation

The licensee needs to fulfil one role, and that is of a licensee, not a product provider, not a single adviser, and a role that is very transparent and provides the adviser industry with the support, education, compliance, and home that is best suited to their needs.

### **Pi Insurance**

**Our submission is to ensure that all Licensees have PI insurance, are members of FOS, have at least 10 advisers, and have sufficient capital on deposit to cover the PI policy excess on up to 10 claims at any one time.**

**The PI Insurance covers the Licensee and separately ensures that all of the authorised reps are named on the policy for cover up to an amount equal to \$5m any one claim or the gross turnover of the licensee whichever is the greater.**

### **Summary**