

Royal Commission Series | Financial Advice

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This section of the Report seeks to support the enforcement of existing law and provide clear principles and expectations of conduct for professionals working in financial services. Commissioner Hayne noted that there was too often a promotion of self-interest, and, in light of this, Commissioner Hayne dedicated this section of the report toward shifting the priority to that of the interests of the client. In particular, the Recommendations in this section focused on four key areas:

- fees for no service
- inappropriate advice
- conflicted remuneration
- professional discipline

Summary of Recommendations for Financial Advice

Category	Recommendation	Impact
Fees for no service	<p>Recommendation 2.1 – Annual renewal and payment</p> <p>The law should be amended to provide that ongoing fee arrangements (whenever made):</p> <ul style="list-style-type: none"> • must be renewed annually by the client; • must record in writing each year the services that the client will be entitled to receive and the total of the fees that are to be charged; and • may neither permit nor require payment of fees from any account held for or on behalf of the client except on the client’s express written authority to the entity that conducts that account given at, or immediately after, the latest renewal of the ongoing fee arrangement 	<ul style="list-style-type: none"> • This will increase the obligations of advisors to be more transparent with all of the clients, and to ensure that there is consent to the services and the payments made in respect of them. • Although some advisors that already annually renew/fully disclose their fees to their clients may be burdened by more paperwork or enhancement of fee processes and systems, this will place all advisors on equal footing, which, ultimately, will be beneficial to the customers.
Inappropriate advice	<p>Recommendation 2.2 – Disclosure of lack of independence</p> <p>The law should be amended to require that a financial adviser who would contravene section 923A of the Corporations Act by assuming or using any of the restricted words or expressions identified in section 923A(5) (including independent’, ‘impartial’ and ‘unbiased’) must, before providing personal advice to a retail client, give to the client a written statement (in or to the effect of a form to be prescribed) explaining simply and concisely why the adviser is not independent, impartial and unbiased.</p>	<ul style="list-style-type: none"> • Where the advice given may be influenced by considerations other than the client’s best interests, Advisors will have to provide a written statement to the client detailing why they are not independent. Relevant disclosure documentation will need to be reviewed and amended to include this disclosure, where applicable. • Whilst there are requirements to disclose some matters regarding conflicts of interest to the FSG, Commissioner Hayne was of the view that these are insufficient for personal advice to a retail client. • Such a move will again promote a greater level of transparency that consumers have been looking for in this Report.

	<p>Recommendation 2.3 – Review of measures to improve the quality of advice</p> <p>In three years’ time, there should be a review by Government in consultation with ASIC of the effectiveness of measures that have been implemented by the Government, regulators and financial services entities to improve the quality of financial advice. The review should preferably be completed by 30 June 2022, but no later than 31 December 2022.</p> <p>Among other things, that review should consider whether it is necessary to retain the ‘safe harbour’ provision in section 961B(2) of the Corporations Act. Unless there is a clear justification for retaining that provision, it should be repealed.</p>	<ul style="list-style-type: none"> • There is no change in this area, however, in three years, it is recommended that there be a review the best interest duty of advisers at statute. • Commissioner Hayne considered whether the best interest duty should be amended, however he noted that it is unclear what effect the Recommendations will have on the quality of advice provided, and that this should inform any amendment.
<p>Conflicted remuneration</p>	<p>Recommendation 2.4 – Grandfathered commissions</p> <p>Grandfathering provisions for conflicted remuneration should be repealed as soon as is reasonably practicable.</p>	<ul style="list-style-type: none"> • This Recommendation will end grandfathered commissions effective from 1 January 2021. • This move was unsurprising, and is expected to lead to savings for clients, either through direct rebates or otherwise. • During the transition period from 1 July 2019 to 1 January 2021, ASIC will be tasked with monitoring and reporting on the benefits passed on to clients. As a result, arrangements will need to be made to reflect this change during the transition period. • The amendment will obviously have an impact on those advisers currently receiving revenue from grandfathered conflicted remuneration arrangements.
	<p>Recommendation 2.5 – Life risk insurance commissions</p> <p>When ASIC conducts its review of conflicted remuneration relating to life risk insurance products and the operation of the ASIC Corporations (Life Insurance Commissions) Instrument 2017/510, ASIC should consider further reducing the cap on commissions in respect of life risk insurance products. Unless there is a clear justification for retaining those commissions, the cap should ultimately be reduced to zero.</p>	<ul style="list-style-type: none"> • There is no change here. Commissioner Hayne is of the view that there is no reason to allow such conflicted remuneration, it is not likely to result in underinsurance. • Accordingly, this Recommendation would add the reduction in the cap of these commissions to the 2021 ASIC review of recent changes.
	<p>Recommendation 2.6 – General insurance and consumer credit insurance commissions</p> <p>The review referred to in Recommendation 2.3 should also consider whether each remaining exemption to the ban on conflicted remuneration remains justified, including:</p> <ul style="list-style-type: none"> • the exemptions for general insurance products and consumer credit insurance products; and • the exemptions for non-monetary benefits set out in section 963C of the Corporations Act. 	<ul style="list-style-type: none"> • This Recommendation that the review referred to above (Recommendation 2.3) to improve the quality of advice should also examine the remaining exemptions to the ban on conflicted remuneration.

Professional discipline of financial advisers

Recommendation 2.7 – Reference checking and information sharing

All AFSL holders should be required, as a condition of their license, to give effect to reference checking and information-sharing protocols for financial advisers, to the same effect as now provided by the ABA in its 'Financial Advice – Recruitment and Termination Reference Checking and Information Sharing Protocol'.

Recommendation 2.8 – Reporting compliance concerns

All AFSL holders should be required, as a condition of their license, to report 'serious compliance concerns' about individual financial advisers to ASIC on a quarterly basis.

Recommendation 2.9 – Misconduct by financial advisers

All AFSL holders should be required, as a condition of their license, to take the following steps when they detect that a financial adviser has engaged in misconduct in respect of financial advice given to a retail client (whether by giving inappropriate advice or otherwise):

- make whatever inquiries are reasonably necessary to determine the nature and full extent of the adviser's misconduct; and
- where there is sufficient information to suggest that an adviser has engaged in misconduct, tell affected clients and remediate those clients promptly.

- Commissioner Hayne here continues to recommend disciplinary reforms, as he has in other sections.
- These Recommendations will ensure that there is increased communication between license holders, as well as with ASIC, regarding misconduct.
- This will, ultimately improve the ability for disciplinary action to be taken in cases of misconduct.
- The mandatory reporting of misconduct to various parties will form an important basis for the new disciplinary system (Recommendation 2.10 below) and will require entities to take steps to implement new policies to ensure that these requirements are complied with.
- The Recommendations will require both on-boarding and incident management and breach reporting processes to be reviewed and amended to implement the changes.

Recommendation 2.10 – A new disciplinary system

The law should be amended to establish a new disciplinary system for financial advisers that:

- requires all financial advisers who provide personal financial advice to retail clients to be registered;
- provides for a single, central, disciplinary body;
- requires AFSL holders to report 'serious compliance concerns' to the disciplinary body; and
- allows clients and other stakeholders to report information about the conduct of financial advisers to the disciplinary body.

- ASFL holders will be required to be individually registered, with new responsibilities being tied to the license as conditions.
- Disciplinary action will be tied these conditions, with deregistration as the harshest disciplinary action
- The creation of a new disciplinary system will help to build professionalism and public confidence in the industry, and bring financial advisers in line with other professions.

What can you do now to prepare?

Company policies will need to be updated to ensure compliance with the reforms. All participants should review their policies with regards to conflicts of interest and further develop them to ensure that the disclosure obligations are met where there is a lack of independence. Protocols will need to be developed for communication of disciplinary matters with the rest of the industry and ASIC. Stronger compliance systems will need to be put in place to ensure that 'fees for no payment' no longer occur. There will also need to be changes to remuneration models to ensure that grandfathered commissions are phased out before 1 July 2021. Dealers and advisers will need to consider the impact that any changes will have on their business during this period, and how to affect the best value for their clients.

Closing Comments

Rather than make wholesale changes in this section, Commissioner Hayne focused on rebuilding the independence and professionalism of the financial services sector. Whilst it surprised some that vertical integration models remains untouched, there will be a greater pressure on firms to minimise conflicts. Additionally, the reforms should improve the manner in which conflicts of interest are managed by advisers. Conflicts should be further reduced by the changes to remuneration models and the upcoming reviews of the current laws. The assessment of exemptions and safe harbour provisions will seek to ensure that the quality of advice is raised of the coming years.

Whilst advisers will believe the changes to remuneration are the most irksome, the most significant change will be in the creation of the new disciplinary system, which will go at least a ways towards restoring some public confidence in the sector, and provide similar standards to advisers as are applied to other professions. The introduction of individual registration will provide a level of personal professional responsibility that should increase the quality of advice and reduce disciplinary breaches.

These change will help to reshape the financial services industry and raise the standards of advice and foster a culture of professionalism that will ultimately benefit the client.

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We view the Royal Commission recommendations as an opportunity for industries to strengthen their compliance frameworks and apply independent practices to their respective businesses.

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