



7 May 2015

Financial Services Unit
Financial System and Services Division
The Treasury
Langton Crescent
PARKES, ACT 2600

Email: ProfessionalStandards@treasury.gov.au

Dear Treasury,

AFA Submission – Lifting the Professional, Ethical and Education Standards in the Financial Services Industry

The Association of Financial Advisers Limited (“**AFA**”) has served the financial advice industry for over 65 years. Our aim is to achieve *Great Advice for More* Australians and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

The Board of the AFA is elected by the Membership and all Directors are required to be practising financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting wealth.

Thank you for the opportunity to provide a submission in response to the consultation on lifting the professional, ethical and education standards in the financial services industry. The AFA is strongly supportive of the broad thrust of the PJC recommendations and in this submission we address the areas that we believe could be modified to achieve a better outcome.

Our goal at the AFA is to achieve Great Advice for More Australians and inherent in that is raising the public perceptions of advice through engaging and educating them, whilst at the same time, continuing to provide leadership to advisers on the standards and behaviours required of them to earn the public’s trust and support.

In this submission we address the following key considerations:

- The need to ensure that the critical role of Australian Financial Services Licensees in ensuring a high standard in the quality of advice is maintained.
- The critical importance of finding a practical solution for increasing the current education standard for existing advisers without causing a significant exodus of high quality financial advisers who might not already meet the new education standard.
- Consideration of alternative models of professional association approval that would not require the development of a professional standards scheme that would involve a limitation on the liability of financial advisers.
- Consideration of alternative models with respect to the employment of new/trainee financial advisers during the proposed professional year.

The PJC Model

Question 1.1 – What impact would the introduction of the PJC model have on the structure of the financial advice industry?

The impacts from the introduction of the PJC model would be particularly broad. It would impact virtually every key stakeholder including advisers, licensees, education and training institutions, professional associations, regulators and lead to the establishment of a new standards setting body (FPEC). Looking at each of these groups separately, the core impacts are expected to be as follows:

- **Financial Advisers.** Financial advisers will need to increase their education standards and ensure that they are members of an approved professional association. For new advisers the changes will be greater as the training before they can commence will be significantly longer and more expensive. Some existing advisers may decide that it is not worthwhile attaining the increased standard and may choose to exit the industry. Attaining the increased standard will incur substantial costs and time diversion away from servicing clients and providing financial advice, which is likely to reduce their income earning capacity. This will have a disproportionate impact on self-employed and small business owning financial advisers when compared to institutionally based advisers where the institution is likely to provide the capital for the training expense.
- **Licensees.** Licensees will have increased responsibility with respect to the supervision of new/trainee financial advisers during the Professional Year. There will be one-off costs to adjust their business models and ongoing staffing costs to provide for the increased supervision and monitoring of advisers. In addition salaried advisers are likely to be more expensive to recruit as education standards increase and all advisers will require a higher level of ongoing training. Licensees will need to develop better ways of working with professional associations, including how they share information with respect to training undertaken, compliance performance and client complaints. Many non-vertically integrated licensees will find it difficult to fund training from existing revenues and this could make it considerably more difficult for them to compete against vertically integrated licensees when recruiting, as advisers may need to fund their own development.
- **Education and Training Institutions.** The current education model, which is largely based upon the VET sector will need to change with a much greater level of reliance upon higher education institutions, who can deliver a bachelor degree program and other bridging courses.

This will require the building of new courses and the modification of existing courses. Higher education institutions will need to consider student capacity issues and break-even points in considering whether to build and deliver appropriate course content.

- **Professional Associations.** Associations will have a significantly increased role in monitoring the conduct of their members, including oversight of education, ongoing training, professional years and registration exams. Professional Associations will also incur significant expense in seeking approval from the Professional Standards Council including going through the process of obtaining approval of a professional standards scheme. To date the associations have had a reactive stance to enforcing member standards and it appears that this would change to include proactive supervision. Mandating of membership will also mean that the professional associations will now have a portion of “reluctant” members that have been forced to join. The “bad apples” will also be forced into the professional bodies, bringing with them a contingent risk to the reputation of the associations and their other members.
- **Regulators.** The role of ASIC will change as they transfer the role of setting education standards over to a new education standard setting entity (FPEC).
- **Consumers.** The impact on consumers is likely to be an improvement in advice quality, an increase in advice cost reflecting recovery of the higher costs of training advisers, and in the short to medium term, a reduction in the number of advisers available to provide advice. Maintaining the number of advisers to meet consumer demand for financial advice will be a key consideration in the effective management of this period of transformation. We think it will take some time before any clear indication of increased consumer trust will be achieved and that measures to drive an increase in financial literacy would be an essential ingredient to achieving that outcome.

Question 1.2 – What are the practical implications of the PJC model applying to advisers from all sizes and types of firms?

There is no question that the new regulatory model needs to apply to all segments of the financial advice marketplace. The implications at a high level would be broadly similar for each type of advice organisation, however we would see particular differences in smaller practices, particularly those that are regional or rural. In addition, licensees with a higher proportion of single person or smaller practices will have additional complexity with supervision and the issues involved with recruiting new advisers into existing practices.

Self-employed advisers (and most likely employed advisers within small practices) will personally incur increased training and development costs to reach the new minimum standards. The time invested in such training will also reduce their time available to service existing clients and advise new clients with a consequential reduction in income likely to result. These costs may be passed on to clients by way of higher fees. It is important to note research from Beddoes Institute in conjunction with Zurich that shows advice practice profitability has fallen by one third in the last two years, so the combination of increased training costs and reduced revenues would likely deepen this trend and may challenge the viability of many practices.

The extent to which a licensee applies fees to their advisers based on turnover may cause a significant reduction in licensee revenue in the short term as studies are completed and adviser revenue drops.

Institutionally employed advisers are likely to expect that their employer will pay for necessary training and this cost may be recouped through reduced benefits or greater productivity expectations being applied to the adviser.

Question 1.3 – Are the lines of responsibility clear under the PJC model?

In our view the responsibilities are clear for most stakeholders, however we believe that the PJC recommendations have caused confusion with respect to the role of licensees and whether they would need to transfer or share some responsibilities with the professional associations. In our opinion reducing the responsibilities of licensee would be a mistake. Licensees are currently responsible for the conduct and education of their advisers and this should remain the case. The challenge is to find an effective way for both licensees and professional associations to play a coordinated role in overseeing the conduct of advisers. Licensees will continue to be the entity closest to advisers and most capable of identifying and resolving any issues.

Current Regulatory Framework

Question 2.1 – What are the practical implications of this overlapping of responsibility? Would this shift have flow-on implications for other provisions in the Corporations Act, or any other parts of the licensing regime?

At present the licensee is responsible for the conduct and the education & training standards of the advisers that they license/authorise. This model is appropriate and it works. Licensees hold individual advisers responsible for their conduct and compliance with the necessary qualifications required to practice. This includes their obligations to the licensee in terms of ongoing or Continuing Professional Development (CPD). The over-lap between the licensee and the adviser is sensible and aligned.

The picture gets more complicated when we introduce the role of professional associations. In reality professional associations are already a participant in this process, in that they have set standards and placed obligations on advisers to complete the necessary CPD. A clearer and more central role for professional associations on education and CPD is sensible, however it should not be expected that professional associations would take over from licensees. It is more appropriate that they would work with licensees on ensuring that the necessary standards are achieved.

The professional associations would need clear communication from licensees with regard to disciplinary matters against a member. The associations should have a primary role with respect to breaches of the ethical code of conduct, whereas breaches of the law/regulations should sit primarily with the licensee as the AFSL.

Question 2.2 – Should licensees maintain a legal obligation to ensure advisers meet relevant training and competency standards?

We support a strong continuing role for licensees to remain responsible for ensuring that their advisers meet the relevant training and competency standards. There is no reason or justification to change this model.

We would not envisage that the obligations of licensees should change at all as a result of the implementation of the PJC recommendations. Licensees play a critical role in assessing education, training and professional standards at the time of appointment of an adviser and they continue to play a critical role in ensuring that the adviser retains the necessary level of training and knowledge and that they continue to comply with all their obligations and maintain the necessary standards.

The role of the licensee is critical and central to ensuring the standards for advisers are maintained. They have frequent interaction with the adviser and ready access to client files. Other parties, such as professional associations and the regulators have significantly reduced visibility and access to relevant information. Licensees should be the primarily responsible party, but work in cooperation with other relevant stakeholders.

Education and Training Standards of Financial Advisers

As baby boomers approach retirement in increasing numbers over the next few years, there is no question that we need to ensure that there is an adequate number of competent financial advisers to meet this demand for financial advice. It will be critical to ensure that we have an adequate volume of new advisers entering the profession as existing advisers depart. Thus any fundamental change to the education standards needs to be done in a manner where transition arrangements will ensure that clients can still access the financial advice that they so clearly need within the timeframe that is relevant to their life stage.

We strongly believe that financial advice education needs to contain a balance of technical knowledge and also emotional intelligence skills. Client relationship skills are essential in financial advice. Financial advisers who have strong technical skills, but poor client relationship skills struggle and don't succeed in driving the behavioural changes that provide the emotional outcomes that clients seek, like peace of mind, confidence and security. These are things that clients really value in their relationship with a financial adviser and have been proven through client research (AFA Research with Zurich and the Beddoes Institute – Pathways to Excellence – October 2012 and the Trusted Adviser – May 2013). Ensuring these skills are incorporated into University/Higher Education based financial advice degrees is essential. It is important to remember that much of the benefit from financial advice comes from the client successfully adopting better money and risk related behaviours and it is the adviser relationship and coaching element that creates the environment for this to happen and be maintained. It takes unique skills to create behavioural change with clients.

Raising the education and qualification standards for financial advisers will undoubtedly have an impact upon competition and cost in the financial advice marketplace. The changes proposed by the PJC and those already announced by a number of large licensees will have significant implications for the profession and the marketplace for financial advice. We are concerned that if these changes are pushed too quickly that we will see a significant reduction in the number of practicing advisers. Achieving the right outcome of moving the entire profession in the right direction and also maintaining the capacity to meet the consumer need for financial advice will mean that the transition needs to be measured and pragmatic.

As a result of this proposed change, older advisers will leave the profession at a faster rate than they otherwise would have and new advisers will join at a slower rate (at least initially) than would otherwise have been the case. This means that there is likely to be a reduction in financial adviser numbers for a period of time, compounding the 13% reduction in adviser numbers already experienced over the last five years. In addition financial advisers who have to complete additional education requirements are likely to have less time available to advise clients. These are all key factors that will impact upon access and affordability of financial advice. We believe that an appropriate transition period will mean that the short to medium term implications are in aggregate a reasonable price to pay for the achievement of the longer term objective which will see increased consumer trust in financial advice and hopefully a strong flow of new and highly educated financial advisers.

The point should be made that the profession already has many outstanding individuals and practices. These are people from a range of different backgrounds with outstanding educational standards who

really believe in financial advice as a profession. The real impact of this transformation is going to be in raising the standard right across the profession, and particularly with respect to new entrants. The outcome will be an increase in the average education level, which over time as part of a broader package of reforms will have a significant impact upon both the quality of advice and the public's perception of financial advice.

We have defined professionalism as the combined outcome of knowledge + attitude + behaviour + accountability. Education and training applies mostly to knowledge within this equation. The other three elements are equally important and the package of recommendations must speak to those elements as well.

Question 3.1 – How would the PJC model interact with existing regulatory regimes for specific types of advisers, for example stockbrokers and tax advisers?

We support an integrated education and training standard for all financial advisers.

In our opinion the model should be a comprehensive model and therefore address all the training and education requirements for advisers across both the AFSL and the Tax Agent Services Act (TASA) regimes (along with other regimes that may apply to certain groups), with respect to their performance as a financial adviser. At present the education requirements for the AFSL regime under ASIC is separate to the TASA regime under the Tax Practitioner Board (TPB). Ideally we would have one education and training standard that incorporated the requirements of both regimes. This would be beneficial in terms of simplicity, cost and certainty for both licensees and advisers.

The PJC model addresses financial advisers who provide personal financial advice on tier 1 products. It does not address advisers providing advice on tier 2 products or general advice. This is a separate consideration, that might result in the application of different frameworks for different groups.

Question 3.2 – Is holding a relevant Bachelor Degree the appropriate minimum education requirement? What is a relevant Bachelor Degree? Would this requirement limit the ability of other degree-qualified individuals to become financial advisers?

We support the introduction of a relevant bachelor degree requirement for new advisers, however we also believe that it is essential for a pragmatic solution to be developed that would allow graduates of other degrees to transition to a financial advice career through the completion of an appropriate bridging course.

We support the introduction of a relevant bachelor degree for new advisers, that would take effect from a sensible commencement date over the next few years.

The AFA supports the goal of a relevant university degree as the entry criteria for new financial advisers entering the financial advice profession, however we do not believe that this goal can be achieved in the short term. The reasons for this are as follows:

- The education marketplace for financial planning degrees is currently immature. Some dedicated financial planning courses exist, however they are not well supported and typically the entry level is reasonably low. There simply isn't currently a high level of demand or throughput for financial planning degrees.

- Many of the graduates of current degrees do not have the necessary depth of knowledge in specific areas relevant to financial advice and graduates find themselves needing to complete additional vocational courses to meet the current standards. Altering courses and allowing time for graduates to come through the new coursework is necessarily a four to six year proposition.
- Whilst life experience isn't mandatory for someone operating in the financial advice profession, it is often considered by clients to be desirable as it better enables an adviser to have the empathy, understanding and emotional intelligence integral to helping clients develop new behaviours to improve their financial position.
- The recent avalanche of negative media coverage about financial advice will invariably impact upon the interest in pursuing a career in financial advice, or enrolling in a financial planning degree.
- The current adviser market place is skewed with a number of older advisers who are expected to leave the profession over the next few years before a sufficient supply of University graduates will be qualified.

In this context it is clear that the number of graduates from financial planning degrees is insufficient to meet the level of supply needed to address the expected consumer demand for financial advice. It is likely to be some time before the marketplace can place a high level of reliance upon the pure financial planning degree courses.

For this reason we believe that the eligible degrees that would be considered relevant would need to be broader and include a range of business related degrees that might already include a number of the necessary subjects. The Tax Agent Services Regulation defines a relevant degree as including finance, financial planning, commerce, economics, business, tax, accountancy and law. We would support this as a sensible definition for the purposes of the financial advice profession, however we note that the completion of these degrees does not equip a graduate with all the necessary education and training to work as a financial adviser. Therefore it is most likely that there would need to be some form of bridging course to ensure that new entrants had met the requirements of all the necessary knowledge areas and at a suitable level.

We consider it quite likely that a reasonable proportion of new advisers over the foreseeable future will not come directly to financial advice. They might have completed another form of degree and they may also have worked in other areas before deciding that they would like to be a financial adviser. This avenue is likely to remain critical as we seek a steady flow of new advisers. We therefore recommend that bridging courses are made available for university graduates with a broader range of alternative degrees.

Question 3.3 – What are the practical implications of requiring advisers to hold a relevant Bachelor Degree?

We support the introduction of a relevant bachelor degree requirement for new advisers, however recommend that the solution for existing advisers needs to provide for a new increased standard, but provide a pragmatic solution to avoid excessive interruption to the market place and reduced consumer access to advice.

We support the proposal with respect to a relevant degree for new advisers, however in addition to recognising the need for a higher level of flexibility with respect to what is a relevant degree and the availability of bridging arrangements, we also point out that the required standard for existing advisers must be set in a pragmatic context.

We strongly support raising the current education standard for existing advisers and recommend that raising it to the advanced diploma level (AQF6) is the most appropriate step at this stage. Our own analysis of the adviser community indicates that the percentage of existing advisers with a degree qualification would be in the range of 25 – 30%. The percentage of advisers that have what might be classified as a relevant degree would be significantly less than this. We have also done further analysis of our own membership that indicates 46% of advisers are 50 years and older and 23% are 60 years and older. We expect this to be similar to the overall population of financial advisers.

Completion of a 24 subject undergraduate degree takes three years full time study or significantly longer for those studying part-time. We do not believe that it is appropriate to require existing advisers to go back to full time study to complete a degree. Whatever the final requirement is for existing advisers it is most likely that it would be completed on a distance learning basis. This will ensure that these advisers are going to remain in the industry and available to their clients for the provision of advice.

With an estimated 50% of the adviser community currently holding the base level education requirement of a four subject Diploma of Financial Planning or equivalent, we believe that it is appropriate to set a new requirement of an Advanced Diploma of Financial Planning (AQF6) or equivalent. This is an existing course that is readily available. If advisers were informed of such an obligation then they could commence this study in the short term and it would then be reasonable to expect the completion of this additional training by the end of 2019. Each licensee will need to develop a specific training plan for each adviser in terms of the gap that needs to be addressed.

For this reason we believe that this standard should be set by the Government, rather than needing to wait until the establishment of the Financial Professionals Education Council (FPEC) to set the standard. This increased certainty would enable advisers to commence their study earlier and therefore would increase the percentage of advisers who might be expected to complete the training by the necessary deadline.

We would expect that in the context of the age demographics of financial advisers that any increase in education standards will result in a number of advisers choosing to leave the industry. For this reason we believe that setting the new standard at the advanced diploma level will provide the most sensible compromise between raising the standard and retaining experienced existing advisers in the marketplace.

It is important that existing advisers will get value from undertaking additional education and therefore there should be some flexibility to develop training programs that facilitate a specialisation in an area that is most relevant to them (i.e. risk specialists, SMSF specialists or aged care).

The AFA also strongly encourages financial advisers to pursue professional association designations such as our Fellow Charter Financial Practitioner (FChFP) and further higher education, such as the Master of Financial Planning. This is exactly the approach that a number of large licensees have committed to. We support the approach that they have taken and believe that the industry taking the lead is an important message about the profession's commitment to address this important issue.

The AFA built the FChFP as a specific education pathway for existing advisers, which is set at the AQF9 level and delivers the additional benefit as an entry point into the Masters of Financial Planning. The FChFP designation is an education framework for financial advisers that balances the academic rigour and technical quality of advice with the practical delivery of advice. AFA research shows that clients highly value the interpersonal communication skills of an adviser. It is the adviser's ability to demonstrate care, understanding and empathy that often results in the change of consumer behaviour required to make better financial decisions.

Question 3.4 – What are the practical implications of requiring new advisers to undertake a structured professional year at the outset of their careers as financial advisers as a way to develop on-the-job skills?

We support a structured professional year, however to avoid the potential negative economic consequences of such an arrangement, we recommend that they can seek provisional registration early in the professional year, and provide advice on a supervised basis.

Access to structured on-the-job training is essential for all new professionals. We support this objective.

Whilst we support the proposal with respect to a professional year, we also recognise that the effective utilisation of trainee advisers during their professional year will be an important consideration. Currently more than half of the financial advice community work within small self-employed businesses. Adding additional non-income producing staff involves significant cost, particularly when there will be limits on the activities that they can undertake. This will be most relevant when consideration is given to the issues with the employment of trainee advisers in rural and regional practices, which are quite often one person operations. For these reasons we support the concept of a professional year, however to make it more economically viable we would suggest that the trainee advisers could complete their registration exam in the first three months of their professional year and then obtain provisional registration in order for them to work with clients in a supervised context before they complete their professional year.

The supervised context may mean that they can conduct client interviews on their own once they have passed the exam, however Statements of Advice would require the approval of a senior adviser or supervisor (perhaps from the licensee).

Should the requirement be that trainee advisers completing their professional year cannot provide advice on a supervised basis then we would expect to see a much reduced level of employment of these trainees in the self-employed sector. This is likely to mean that most recruitment and training is completed within the salaried business channels, where they have access to greater scales of economy and resources.

During the professional year we would expect there to be a structured program of supervision and monitoring. One key component of this is the development of soft skills, which are unlikely to be taught at a higher education institution. Learning client relationship skills from an experienced adviser is an effective way of preparing them for the provision of financial advice to clients. We see the need for some flexibility around the requirements of the professional year to allow for a combination of face to face contact, phone based mentoring and formal training sessions. There could also be a structured process of file reviews for trainee advisers during a provisional authorisation period.

Structure and Role of a Standard-Setting Body

Question 4.1 – What are the practical implications of FPEC performing this role?

The introduction of FPEC does significantly change the way that the industry is structured, however there is no reason why it can't work effectively. As a self-regulatory body, FPEC would need to work with a range of stakeholders in order to achieve the set objectives.

There are a range of options on how FPEC could be formally constituted. One option would be to recognise FPEC through legislation. Another option would be to enable ASIC to provide the authorisation behind the outcomes of the FPEC processes. There would be some sense in this in that ASIC would remain the regulator responsible for oversight of the industry and the education and training standards would need some form of formal recognition.

Mandatory membership of professional associations, would also enable the authority for the application of FPEC standards to come from the professional associations, in that they could be the party that endorses the standards set by FPEC and enforces them as a requirement on all members.

The membership of the FPEC Board is an issue that will be subject to significant debate. In consideration of this, thought needs to be given to the broader structures that an entity like FPEC will employ and the core objective of such an entity. It is likely that the Board of the FPEC will play a role in approving what is developed from within the entity and most likely as a result of working groups that operate in consultation with a broader group of industry stakeholders. For this reason we do not believe that the Board will be the point in the organisation that develops the frameworks, however it will be the body that provides approval.

We also question the concerns that appear to be emerging about the necessity for the FPEC to be demonstrably independent of all influences. From our perspective this concern seems misplaced as the financial advice profession is equally interested in getting a significant leap in standards. A self-regulatory body necessarily needs to include representation from the bodies that represent the parties being regulated.

In our view the Board of the FPEC needs to have people with the right skills, rather than an allocation of people across what is considered to be a range of interested stakeholders. The role of this Board should be to ensure that the overall entity is driving out the right results and that the right decisions are being made.

It also should be noted that the key outcomes of the new model, such as the relevant degree requirement, professional year and registration exam will be set by Government, not FPEC, but will be subject to detailed development and implementation by FPEC.

The issue of the funding of FPEC is an important matter to resolve. It is important to ensure that it is adequately funded, but in a manner that avoids the risk of there being any perception of undue influence. We believe that a user pays model would be the most appropriate means for the ongoing funding of such an organisation. A solution also needs to be found for the initial funding to get it established.

Question 4.2 – Are there alternative arrangements that would be more appropriate or effective?

In our opinion the only alternative is the current arrangement, where ASIC has been responsible for the education standards for financial advisers via RG 146. There have been many efforts to make fundamental change to these requirements, all of which have not proceeded to implementation. At this point, it is expected that Government will take a role and set the new requirements. This will enable a new model to be developed and implemented. The establishment of FPEC will enable the new model to be refined and improved over time without the need for the Government to step in again. The model proposed provides a sound basis for the ongoing management of education standards.

Registration

The PJC recommendations have used registration as a key driver of a range of important factors such as the use of the terms “financial advisers” and “financial planner” and the implementation of mandatory membership.

Question 5.1 – What are the practical implications of requiring individuals to be registered in order to provide financial advice?

At present, with the new ASIC adviser register, all advisers are required to be registered. This requirement will not change, although the vehicle under which they get registered will be changed, in that it is proposed that the professional associations need to nominate an adviser for inclusion on the register. At present it is the licensee who notifies ASIC of the authorisation of the adviser. Introducing the professional association into this process is, by the look of it, part of the model that seems to be designed to introduce mandatory membership of professional associations, which is also apparently part of the model to ensure that the new obligations can be enforced.

As a basic concept it is absolutely essential that only registered (and therefore licensed or authorised) advisers can provide financial advice to consumers. It is also appropriate that registration is seen as an important step and should come with a range of clearly set out obligations.

Question 5.2 – Should it be the role of professional associations to notify ASIC that all requirements have been met for an adviser’s registration, and of factors which affect their subsequent fitness for registration?

We believe that there are two key stakeholders in the addition of an adviser to the register, being the licensee and the professional association. It is the licensee who is appointing the adviser, rather than the professional association. It is therefore questionable as to whether the professional association should manage the registration process with the support of the licensee or for the licensee to manage the registration process on the basis of the endorsement of the adviser by the professional association. In our view it would make better sense for the licensee to remain responsible for the registration process, but subject to confirmation of formal endorsement by the professional association.

With respect to ongoing fitness to be on the adviser register, it is appropriate that the licensee and the professional association work closely together with respect to the investigation of any conduct that might result in a decision to remove them from the register. Such an action would have significant consequences and would therefore need to provide natural justice to the financial adviser. Given the disparity in access to information, it would be essential that this was done in a cooperative and consultative manner.

We would envisage that the licensee would remain principally responsible for this investigation however mechanisms may be required in regulation or law that provide for the licensee to share relevant information with the professional body to allow assessment of cases.

Question 5.3 – What are the practical implications of having these criteria listed on a public adviser register?

The inclusion of all the proposed additional elements on the register appears reasonable. The inclusion of all professional association censure actions will require alignment between the rules of the professional association and the rules with respect to the register to ensure that there is no breach of privacy provisions and no likelihood of any defamation action.

Question 5.4 – Are there alternative or additional criteria that should be listed on the Register?

One consideration for the register is additional information on the reasons for an advisers departure from a licensee that can be used by a recruiting licensee as a further source of information to assess as part of the recruitment process.

Ensuring that “Bad Apples” are removed from the financial advice industry is a key factor in ensuring that financial advice can successfully continue the move towards professionalism and to avoid further negative media coverage. Improved management of bad apples is an important policy area and something that the register might make an important contribution towards.

Question 5.5 – What are the practical implications of having professional associations perform this role? For example, are professional associations sufficiently resourced and how would they interact with ASIC in relation to these requirements? Does this approach dilute the responsibility of licensees?

We believe that the responsibility for arranging registration should remain with the licensee, who are the entity authorising the adviser.

Placing this responsibility on professional associations would involve considerable cost and a requirement around information retention that is beyond the current requirements and capability. As an example professional associations would not retain information on historical details of previous licensee appointments. Neither would it be efficient for professional associations to have to verify the adviser’s data every time an existing adviser was appointed to a new licensee.

If this was required of professional bodies then substantial capital costs would be incurred and an appropriate time frame for acquisition and implementation of software and systems would be required. It would also need to be supported by legislation/regulation/licence conditions being applied to licensees to ensure they facilitate appropriate information flows to enable the association to perform the task.

Question 5.6 – Is legislative protection of the titles ‘financial adviser’ and ‘financial planner’ necessary?

We support the legislative restriction on the use of the terms “financial adviser” and “financial planner”.

There are already laws that prevent people from holding themselves out to provide advice on financial products if they are not licensed or authorised to do so. The value of this measure is that it will serve to prevent people from using the terms when they are not eligible to do so and it will serve to limit the use of these terms by the media and other parties when they are referring to people who may have done the wrong thing, but are not financial advisers. At present a lot of media stories about people caught doing the wrong thing (i.e. property spruikers) are wrongly described as financial advisers. There seems to be a tendency to describe anyone working in the area of finance or investment as a financial adviser or financial planner. This contributes to the issue of the reputational damage that negative media coverage has on the financial advice industry.

Exam

A registration exam for new and existing advisers is one important mechanism of ensuring that all advisers have reached a certain standard, which we believe will be beneficial in providing greater confidence to consumers.

Question 6.1 – Do you consider a registration exam should be a component of a framework to improve professional standard? Should the exam apply to both existing and new advisers?

We support the introduction of a once off registration exam for both new and existing advisers.

The introduction of a registration exam will ensure that clients have the confidence that their adviser has passed a standard national test and has met the minimum standard. This will enable a higher level of confidence for new clients.

The introduction of a national exam will also provide a mechanism for existing advisers to demonstrate their capability, which is an important part of the process in seeking to repair the trust and confidence of the Australian community.

Question 6.2 – What are the practical implications of the use of a registration exam?

To be effective, the registration exam would need to be standardised and apply to all advisers.

As discussed previously in Question 3.4, there is concern about the timing of the exam within the professional year. We propose that a new adviser be allowed to sit the registration exam during their professional year rather than at the end of the professional year. This would allow them to obtain provisional registration and to be allowed to provide advice to clients on a supervised basis. This modification would better ensure that trainee advisers could be effectively employed during the professional year, which would make the appointment of a trainee adviser more economically achievable for advice practices and licensees.

Question 6.3 – What content should be covered in the exam?

There has been some debate on this matter over recent years. It is broadly agreed that the most effective and efficient solution is to have a single exam that would apply to all advisers.

There is however some level of concern about the value of a single exam that is applied across all adviser groups. We appreciate that this is an issue, however believe that the exam can be focussed upon the core obligations of financial advice that apply across all groups. We would see this exam covering things like the core FoFA obligations, an understanding of the advice process, high level concepts relevant to core advice strategies, behavioural factors and ethical issues.

Question 6.4 – Is FPEC the appropriate body to set the exam? Who should be responsible for invigilating the exam? Who should be responsible for marking the exam?

FPEC is the right body to set the exam. They have responsibility for curriculum and would be best positioned to prepare and update the exam. There would be better efficiency achieved by having the FPEC play a role in setting curriculum across the relevant degree, the professional year, the CPD and the registration exam.

The party running the exam should be a group who have expertise in this field and the resources necessary to operate such a program. The resources will vary depending upon the delivery mechanism for the exam, however it would be expected that it would be in an on-line format to ensure that it was delivered as efficiently as possible. It would be expected that the same party could also mark the exam.

Ongoing Professional Development

A commitment to ongoing professional development is a critical element of a profession. Professionals need to maintain their competency and should be looking to continuously develop their skills. In this regard we currently require our members to complete a minimum of 30 hours per year, which can be achieved through a variety of learning situations, including conferences, workshops and on-line learning/assessment. It is important that there are clear guidelines to ensure that CPD is gained across all relevant knowledge areas and through a balanced range of sources, rather than a predominance of on-line activity. As an outcome of this process we would expect to see greater standardisation in the accreditation of CPD material. The AFA is committed to implementing a program of random sampling of CPD compliance for members.

We also believe that ethics should become a mandatory component of the annual CPD obligation, with the introduction of a minimum of 4 hours per year.

Question 7.1 – What are the practical implications of the proposed ongoing professional development requirements?

Whilst mandatory CPD requirements are already enforced by licensees and professional associations, we support a more direct legislative means of stipulating this obligation.

Licensees already have responsibility for ensuring that their advisers remain competent. Whilst neither the law, nor ASIC stipulates a minimum requirement for CPD, this is typically set and actively monitored by licensees. Commonly licensees will set a minimum overall requirement of 30 or 40 hours and will also stipulate the number of hours that need to be completed in each of the relevant knowledge areas. Licensees strongly enforce these requirements and will take disciplinary and remedial action against any adviser who fails to meet the required standard. Licensees, in setting these requirements, are leveraging the standards set by professional associations. Typically, where the professional associations are monitoring the actual CPD completed by individual advisers, this is being done on a random sampling basis.

In terms of the implications for financial advisers as a result of the PJC proposal, the extent of the change will depend upon the exact rules that are developed. We believe that it continues to make

sense for licensees to monitor the completion of CPD activity. Should it prove necessary for professional associations to maintain a record of all training completed by advisers, then we believe that this would be best achieved by the professional associations working closely with licensees, rather than individual advisers.

Question 7.2 – Are professional associations well-placed to administer ongoing professional development requirements?

We believe that it continues to make sense for licensees to maintain records and monitor the completion of CPD activity.

Should it prove desirable for professional associations to maintain a record of all training completed by advisers, then we believe that this would be best achieved by the professional associations leveraging the systems and processes of licensees. It is not practical to take this responsibility away from licensees and it would also be particularly costly for this to be managed by professional associations. Such a requirement would likely involve a significant system project and for the purposes of necessary efficiency, this would need to be completed on-line by each adviser. These systems would duplicate what licensees already have.

Professional and Ethical Standards

It is our experience that education standards, whilst particularly important, will not on their own achieve all the outcomes intended. Cultural change, as proven through behaviour, is the ultimate goal and professional association membership, peer-to-peer learning experiences and practical training and supervision are needed to be successful.

Ensuring that trust and confidence returns to the financial advice profession is also dependent upon proof that financial advisers operate within boundaries of behaviour that would be expected of a professional. Therefore the establishment and maintenance of high standards of professional and ethical conduct is critical.

There is no question that the vast majority of advisers operate with integrity and demonstrate the required ethics. Nonetheless we believe that the importance of integrity and ethics can be reinforced by the provision of specific and focused training.

Codes of conduct, for professional associations, also play an essential role. This is a set of standards that members can hold themselves and their colleagues accountable to that sit above the minimum legal standards expected of a Practitioner. Working as a professional, ensuring that everyone lives up to the standards expected of them, is something that financial advisers can take collective responsibility for through self-regulation via professional bodies. Codes of conduct focus upon behaviour and ethical conduct that sits above compliance with the law.

We believe that the core role of professional associations are as follows:

- Through a code of conduct setting the minimum standards of behaviour and conduct,
- Promoting and encouraging education and professional development,
- Certification of advisers at a higher standard than is required by the law,
- Supervision and monitoring of financial adviser conduct and responding to complaints,
- Playing an active role to ensure that bad apples are appropriately dealt with,
- Advocating for the best interests of financial advisers and their clients, and

- Fostering community trust in the members of the association.

The PJC model is a highly integrated model with many different elements that are inter-connected. The model includes a focus upon the importance of codes of conduct and seeking to ensure that all advisers are subject to an approved code. It is equally understandable that the professional associations and their codes should be subject to some approval process. This all leads to the proposals around mandatory membership and approval of professional associations by the Professional Standards Council (PSC).

Question 8.1 – What are the practical implications of having each professional association create its own code of ethics? For example what are the implications of having multiple codes as opposed to a single code?

The professional associations in the financial advice marketplace already have separate codes of conduct. This is not a problem and even those members who belong to more than one association accept this as a reality. Each association has already invested significant effort into developing their code of conduct and it would seem to be a significant task to consolidate each of these codes into a single code that could be applied across each association. In other professions it is not uncommon for different groups to have different codes of conduct. Accountants or mortgage brokers who also operate as a financial advisers will have multiple codes of conduct to comply with.

It should also be noted that financial advisers are also subject to the Tax Practitioners Board Code of Conduct.

Question 8.2 – What are the practical implications of requiring that a code of ethics be approved by the PSC? Are there alternative approaches that would be more appropriate or effective?

We support the requirement for professional associations to be required to be approved by some approval organisation and consider the PSC as a viable solution.

As stated above we support the proposal with respect to approving professional associations. In the context of mandatory membership of a professional association, professional associations should be subject to some form of approval or recognition process. As part of this it would be expected that their code of conduct would need to be reviewed, along with other key processes such as member review and monitoring arrangements.

There is no simple solution for this proposal. The PSC is one government entity that exists for this specific purpose and it has experience in the review and approval of professional bodies and the ongoing development of their control and risk management arrangements. It is however acknowledged that there is one major outcome of the PSC process that might not have been envisaged as a central objective of the financial advice reform agenda. This is the limited liability capability that the PSC can deliver. Whilst the purpose of this is more realistically described as assurance that participants have the capacity to meet their financial commitments, it is recognised that the optics of something that puts a cap on payouts to clients is challenging in the current environment.

In order to put a scheme in place there is a significant amount of work involved with the compilation and assessment of loss or claims data which is all used by the PSC to consider the most suitable arrangements that they can then implement for the professional body.

We recognise that the limited liability element of this proposal has significant implications, and would therefore welcome consideration of a PSC approval model that excludes the establishment of a scheme, but retains all other elements of the PSC approval process and the ongoing focus upon the improvement of professional standards. It is recognised that a variation of this nature could involve significant issues of a legislative nature.

The only alternative model is to build a form of ASIC approval process. Through Regulatory Guide 183 there is already an ASIC code approval process, however we consider code approval to be significantly different from the approval or recognition of professional associations. In our view the PSC solution presents the best alternative.

Question 8.3 – Is the PSC the appropriate body to drive improvements in professional standards in this industry? Are there alternative arrangements that would be appropriate or effective?

The responsibility to drive an increase in professional standards is one that has to be shared across the industry, however the lead needs to be taken by the professional associations with the support of licensees. In terms of a body that can play a role in holding the professional associations accountable for driving and delivering this lift in professional standards, it would be reasonable to conclude that the PSC could play a significant role. It is equally the case that ASIC will play a critical role in holding the financial advice industry accountable. ASIC is the only other body that could play a significant role in driving improvements in professional standards, however as the regulator they have an existing role to ensure that licensees and advisers comply with the existing standards.

Question 8.4 – What are the practical implications of having the PSC perform this role? For example, how would the PSC interact with ASIC?

ASIC as the regulator for the industry already has a clearly defined role around supervision of the industry and working to ensure an effective marketplace that promotes consumer confidence. Often this places a significant focus upon those parts of the industry that are not performing to the required standard. The role envisaged for the PSC is quite separate in that it would play a role in working with the entire industry to facilitate the ongoing increase in standards. In effect, their influence will be a key part of ensuring that the financial advice profession accepts and delivers on the promise of moving towards broad recognition as a profession.

Question 8.5 – What are the practical implications of requiring professional associations to hold a PSC approved scheme?

We have addressed above our views on the implications of professional associations applying for and holding a PSC approved scheme. It is clear that this will involve a significant effort and investment to meet the requirements of a scheme. This will result in increased costs and the need for professional associations to raise additional income. This may come as a result of increased membership that flows from mandatory membership, however the timing of the additional expenditure and the additional revenue would need to be considered. We do not believe that the immediate objective is the establishment of a PSC approved scheme, but recognise that this is a core to the role that the PSC currently performs in approving professional associations.

Question 8.6 – Is it appropriate that liability in relation to financial advice/services be limited at this time? Is limitation of liability a necessary element for the operation of the PJC model?

We appreciate that a limitation on the liability for financial advisers is problematic in the context of the current media focus upon the industry. It also should be stated that this was never an objective of the AFA. We also recognise that the workload in achieving approval for a PSC scheme is significantly influenced by the steps required to prepare the necessary information for the establishment of a scheme. These factors are influential in considering this matter. Other factors are also important including how the External Dispute Resolution (EDR) arrangements, through the corporations Act, might fit with a limited liability scheme.

In reality we suspect that the concerns with respect to limited liability schemes may be overstated. Firstly these schemes are designed to ensure that people will get the benefit of the improved claims management capability. Secondly applicants to EDR schemes already need to work within caps, and the cap identified by a PSC scheme is certainly not going to be less than the EDR cap. Nonetheless we fear that this issue may derail the consideration of a PSC solution and we would therefore like to propose that consideration be given to PSC approval of professional associations without the need for the approval of professional standards schemes.

Question 8.7 – What are the practical implications of capping liability? For example, what changes to Commonwealth and/or state and territory legislation would be required?

We cannot speak with certainty about this matter, however we make the point that the PSC has significant experience with implementation of liability capping schemes. Since the Corporations Act does not refer to the caps that are employed within EDR schemes, it may be possible to implement such a scheme without the need for any legislative change to the Corporations Act.

As we understand it, limited liability schemes are enacted in each state and at the national level by means of regulation.

Question 8.8 – Would an alternative arrangement, under which a scheme’s approval would not limit liability, be practical?

As discussed above we would like to see this possibility investigated.

Question 8.9 – What are the practical implications of mandating membership of a professional association? Are there implications arising from the increased responsibility on professional associations rather than on the licensee?

We support mandatory membership of professional associations as a means of driving increased standards through the application of codes of conduct to all financial advisers.

At present, we estimate that less than 50% of financial advisers belong to a professional association. Mandating membership of professional associations would have a significant impact upon the

industry. This would lead to a significant influx of new members and a significant increase in responsibility for professional associations. It will also have a fundamental impact upon professional associations as they move from members who choose to belong, to a combination of those who choose and those who feel forced into being a member.

It is possible that some of those who have previously chosen to not belong are happy to operate at a lower level, without adherence to a code of conduct. This will change the attributes of professional associations and probably introduce a group of members who are more intolerant to change and less supportive of the journey towards full recognition as a profession.

The other side of mandatory membership is the additional responsibility that is placed on professional associations. Members who are expelled from a professional association are unlikely to find another association to support them and are therefore likely to no longer be able to operate. This places a greater onus upon the association to ensure that each of these decisions are in fact correct and of course opens the association up to legal challenge from expelled and/or disciplined members.

We think it would be important to recognise that the code of conduct obligations would be principle-based and seek to drive the right behaviours within the spirit of the law. They would govern ethical behaviour first and foremost with legal compliance remaining primarily the responsibility of the licensee as the AFSL holder. As we have pointed out earlier, a regulatory mechanism may be required to enforce licensees to share all relevant information with the professional bodies for the purposes of investigating a member's behaviour. This is not currently the case.

Other Issues for Consideration

Question 9.1 – How could the PJC model interact with the existing Tier 2 adviser training and competency requirements?

We envisage that the extension of FPEC to include Tier 2 product advisers and those who provide general advice is a prospect, however we suggest that this might be delayed until after the FPEC has addressed the agenda that has been established by the PJC recommendations.

Question 9.2 – Do you consider FPEC to be the best entity to determine transitional arrangements for existing advisers and advisers wishing to move within the industry?

We believe that FPEC, constituted as proposed, would be an appropriate entity to address transitional arrangements for existing advisers. We are, however, concerned about the timeframe to resolve this matter and consider that earlier resolution of the requirements for existing advisers might be preferential to a delay and consideration by FPEC.

We have set out what we consider to be the most appropriate requirements for existing advisers and feel that this is something that could be stipulated by the government in order to provide existing advisers greater clarity and to allow them to commence work on the additional study that will be required.

Question 9.3 – Do you consider Recognised Prior Learning a suitable transitional arrangement for existing advisers?

The answer to this question depends upon what standard is set for existing advisers, and what options

are made available for existing advisers to demonstrate their capability.

We believe that consideration of RPLs may become an important factor, however we consider that some level of further training such as completion of the Advance Diploma of Financial Planning or something equivalent would be an appropriate target for existing advisers. As discussed below in Question 9.5 we consider that possible cases for an extension of RPL provisions may arise through the implementation stage.

Question 9.4 – What is an appropriate timeframe over which existing advisers should transition to the new system?

The answer to this question also depends upon the standard that is set for existing advisers. We have previously spoken in terms of a timeframe through to the end of 2019 in order to get all existing advisers up to the new standard. We continue to believe that this is appropriate.

We suspect that some of the timeframes set by the PJC might be overly optimistic. It is important to take the right amount of time to achieve such an important change as is necessarily required. It is in fact the quality of the journey and the value of the additional education that is undertaken that is the most important consideration in this major change initiative.

Question 9.5 – Are there any alternative transitional arrangements that would be more appropriate or effective, for either new or existing advisers?

We have spoken above about the importance of some level of flexibility, particularly in the early years, when the flow of graduates from FPEC approved courses will be relatively small. Certainly during this phase there should be ready access to bridging courses for existing graduates of relevant degrees and other graduates of courses that might otherwise be considered to be “non relevant”.

Existing advisers should be required to complete the registration exam and also to undertake sensible and pragmatic further education and training. This additional education and training should be structured to deliver business and personal benefits for those impacted. As this matter progresses it may become apparent that additional transitional arrangements might be appropriate for certain groups, such as those nearing retirement. It is always difficult managing significant change of this nature and it is problematic to establish alternative arrangements for particular groups. It may be appropriate to provide FPEC with certain exemption powers.

Question 9.6 – Are there any particular elements of the PJC model that present timing challenges?

As stated above, we consider some of the PJC timetable overly optimistic. It seems likely that it will take longer to constitute the FPEC and longer for some of the work of the FPEC to be completed. In addition, we suspect that it might take the universities and higher education institutions significantly longer to prepare FPEC compliant courses than has been stipulated by the PJC. We expect that the issue of timing considerations will be addressed further by training and education providers through this consultation process.

Question 9.7 – What timing or phasing would most effectively balance the recognised need to raise standards and competency in the short-term against practicalities of implementing a new model to raise standards of new and existing advisers over the longer term?

The introduction of new standards for new advisers may be possible to be implemented sooner, however there needs to be some equity with respect to students who are already committed in courses that they are undertaking in order to be eligible to work as a financial adviser.

As stated above we believe that the cut-off date for existing advisers should be 31 December 2019.

Regulation Impact

Question 1 – How many/what proportion of financial advisers are likely to be affected by the introduction of a new professional standard framework (such as that proposed by the PJC)?

We do not have access to the relevant statistics on the whole financial advice market, however based upon what we know from public data and our own members, we derive the following:

- Approximately 50% of advisers would need to join a professional association.
- Based upon our knowledge of existing adviser education levels and a new standard of the Advanced Diploma of Financial Planning, at least 50% of existing advisers would need to complete additional education.
- Based upon what we have proposed, 100% of existing advisers would need to complete the National Exam.

Question 2 – What proportion of financial advisers working in the industry are typically new entrants (for example, graduates and those coming from other professions) versus existing advisers who have been in the industry for a number of years?

We do not have access to research on this question with respect to the entire market, however the AFA has a special membership category for New Advisers, who are in their first three years of practice, and this group represents approximately 15% of our practitioner membership.

Question 3 – What is the typical education level of financial advisers?

Our analysis of financial advisers who attend our events, through surveys that we have undertaken, suggests the following:

- Approximately 25% – 35% have degrees or higher level designations.
- Approximately 20% of advisers have completed the eight subjects involved in both the Diploma of Financial Planning and the Advanced Diploma of Financial Planning.
- Approximately 45% - 55% have only completed the Diploma of Financial Planning

Question 4 – What proportion of advisers are currently members of a professional association(s)?

On the basis of our estimates, approximately 50% of financial advisers belong to a professional association.

This is not an easy assessment for the following reasons:

- Until the establishment of the Financial Adviser Register, the total number of financial advisers was less precisely known. The industry still needs to make sense of the most recent number of approximately 22,000 to be certain that it does not include a significant number of non-practicing advisers.
- There are a range of professional associations that financial advisers could belong to including the accounting bodies. Data is not readily available from some of these entities.
- Membership of multiple associations is not uncommon, however exact statistics are unknown.

Question 5 – What are the likely costs (labour and non-labour costs) associated with the various elements of the PJC model? Are costs likely to vary between different size advice firms, different professional associations etc? If so how?

The costs are expected to be significant across the entire industry and will depend upon the final solution and the exact implications for specific licensees and advisers. Licensees who already have mandatory membership of professional associations and higher education standards will have less requirements for change than those with advisers who are predominantly not members of professional associations and for whom most advisers are currently qualified at the existing four subject Diploma of Financial Planning level.

The cost for professional associations will be significant across the following areas:

- Preparation for the influx of new members that will flow from mandatory membership.
- Development of new courses that might be required to meet the needs of existing advisers.
- Further refinement of codes of conduct and development of additional controls and supervision arrangements.
- Preparation and submission of applications for approval by the PSC.
- New system and software (IT) requirements and associated recruitment and training of staff.

At this stage we are not in a position to quantify these costs, however we believe that they would be particularly significant. There will be scale of economy advantages in this exercise, so the effort and cost will be more manageable for the larger licensees and the larger professional associations.

Question 6 – Are there alternative options (other than the PJC model) which would provide an enhanced cost-benefit outcome?

The model proposed by the PJC is very comprehensive and as best as is possible it works with the existing infrastructure and entities.

In our opinion if the PJC proposal is broken down into sub-components then the outcome will be much less effective. We therefore do not believe that there is an alternative model that would deliver a better cost-benefit outcome.

Conclusion

We thank you for the opportunity to provide feedback on the PJC recommendations. The development of final solutions for implementation is critically important and there is no question that these changes will have a quantum impact on raising the standards across the financial advice profession to better ensure that consumers receive a higher quality of financial advice.

Should you have any questions, please do not hesitate to contact me on 02 - 9267 4003.

Yours sincerely,

Phil Anderson
Chief Operating Officer