

26 September 2011

Ms. Sue Vroombout
General Manager
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Treasury
Canberra
ACT

by e-mail transmission sue.vroombout@treasury.gov.au

Dear Ms Vroombout

Re: Future of Financial Advice Reforms
Corporations Amendment (Futures of Financial Advice) Bill 2011

We refer to our letters of 27 June, 22 July and 5 August 2011 with regard to the FOFA reforms.

We thank you for the consideration that has been given to the submissions with regard to the Commission Sharing and Stamping Fee aspects of the proposed FOFA reforms.

Both Commission Sharing and Stamping Fees are long standing practices of or applicable to all sectors of the financial services industry. It is submitted that any potential conflict of interest is adequately managed by disclosure and as a result will not impact on the quality of advice being provided to the retail investor.

Prohibition of Third Party Commissions:

We support the prohibition of third party commissions [other than Stamping Fees associated with exchange listed (or to be listed) capital raisings], as we do not believe that the potential conflicts of interest can be managed by disclosure and consequently could potentially affect the quality of advice being provided to the retail investor.

The practice of third party commissions being paid by issuers of non-exchange listed managed funds to advisers whose clients subscribe to them has been a practice of all sectors of the financial services industry. The facts that it has been concentrated in the financial planning sector and has brought about the development of that sector's role as the distributor of manufactured non-exchange listed financial products, is largely irrelevant as it is a practice in which all sectors have participated to one degree or another.

The development of participants of the financial service industry as distributors of manufactured non-exchange listed managed funds to retail investors has given rise to a wide range of third party commissions offered by the issuers of those products in order to promote their distribution. The variety of these third party commissions has provided the opportunity for advisers to provide advice which may have had more regard for the differentials in such commission rates than what was in the best interests of the retail investor. Large fees have clearly enticed some providers of financial advice to recommend products which may not,

and in some circumstances were clearly not, appropriate for the adviser's retail client. If the commission rate is the same irrespective of the financial product recommended to the retail client then there is no benefit to the adviser in recommending one financial product over another.

This prohibition in itself will go a very long way in re-shaping those sectors of the financial services industry which have relied on high and differential commission rates and as a result will immediately improve the quality of advice provided to retail investors.

Types of Service within the Financial Services Sector:

There is a range of providers of advice to retail investors which include both generalists and specialists in relation to one or another of the financial products available for investment and consequently there is a range in the type of advice available to the retail investor. In some ways the structure of the financial service industry is analogous to the medical profession where there are general practitioners and specialists. Bell Potter regards itself as a specialist.

The fact that the Financial Planning sector has, in the main, taken on the distribution of unlisted managed funds on the basis of a questionable third party commission structure may well have arisen as a result of its generalist type financial advisory service provided by the generation of holistic financial plans, which purport to cover the whole of a client's assets and liabilities, income and expenses and relevant personal circumstances.

On the other hand, the sector in which Bell Potter operates has arisen from its direct participation in exchange traded securities markets through both their primary capital markets and the secondary markets in the entities listed on the exchange. Of course, there are other sectors of the financial services industry in addition to financial planners and stockbrokers, namely "white labeler" brokers, futures brokers, CFD brokers etc

Accordingly, it needs to be recognised that there is a distinction between the types of advisory service provided by the various participants in the financial service industry. Those services range from the provision of holistic advice by means of a complete financial plan to specialist advice in relation to only exchange listed Equities and Fixed Interest, or only Futures or only over-the-counter financial products like CFDs.

As a result Bell Potter's equity broking representatives are accredited in relation to Equities and Fixed Interest and are authorised to represent the Company in relation to these categories of financial products only. These advisers are not authorised to provide Financial Planning, Insurance, Futures or CFD advice. On the other hand Bell Commodities' Futures brokers are accredited and authorised to provide advice in relation to Futures only and are not authorised to provide advice in relation to Equities or Fixed Interest. Bell Potter operates a very small Financial Planning department and its advisers within that department are again specifically accredited and authorised to provide Financial Planning advice.

It is acknowledged that despite proper accreditation and authorisation retail investors can on occasions be provided with inappropriate advice; however, the Financial Ombudsman's Service and ASIC can provide redress in these situations.

Because the re-shaping of sectors of the financial services industry in order to improve the quality of advice to retail investors, is being effected by changes to the Corporations Act, which regulates the whole financial services industry, the proposed amendments may have unintended consequences for those parts of the financial services industry which are not subject to the quality of advice, trust and confidence shortcomings which have been identified by the Government.

To Act in the Best Interests of the Retail Client:

It is submitted that if the subject matter of the advice requested by the retail client is an exchange listed securities (or part of a portfolio which is substantially made up of exchange listed securities) and the provider is subject to ASIC's ASX Market Integrity Rules, the provider is deemed to have satisfied the obligation to act in the best interests of the retail client if the provider takes the steps mentioned in paragraphs 961 C (2) (a), (b) and (c).

Bell Potter believes that every participant in the financial service industry would accept a **general** obligation to act in the best interests of the retail client at any given point in time.

However, where the retail client pays a uniform rate of commission regardless of the exchange listed financial product, which is the subject matter of the advice, Bell Potter believes a general obligation to act in the best interests of the retail client is no different from the current obligation under s 945 A of the Corporations Act.

Bell Potter has an issue with the nature and prescription of the steps that need to be taken to satisfy the '*best interests of the client*' obligation under the draft legislation. It appears to us that these prescriptive steps are intended for the financial planning sector or, at least, those providing holistic advice and are not intended for those providing specialist advice.

This is evident to us from the Outline to the Explanatory Memorandum (3rd paragraph) and the Context of Amendments section (1st paragraph). In the latter case, the quoted structure is not a structure of the stockbroking sector; it is a common structure applicable to the distribution of non-exchange listed manufactured managed funds, which are in the main distributed by the financial planning sector.

Also, while the 2nd paragraph of the section headed "*Act in the best interests of the client*" makes reference to the fact that the prescriptive steps of the proposed legislation are based on conditions under which advisers currently operate, in fact, they are the specific conditions under which an adviser providing a holistic advisory service, by means of the preparation of a financial plan, might operate, but certainly not the way advisers dealing specifically in exchange traded financial products operate.

Finally, the Explanatory Memorandum acknowledges that the proposed "*best interests of the client*" obligation implements Recommendation 1 of the Parliamentary Joint Committee's (PJC) Inquiry into the collapse of Storm Financial etc. However, this was very much an enquiry into financial planning, which the PJC found originated as a sales force for financial product manufacturers and which from the outset involved a sales-advice conflict of interest. Advice in relation to exchange listed financial products was not considered by the PJC and all the issues considered by the Inquiry as outlined in Chapter 5 of the Inquiry's Report were related to financial planning advisory issues.

From the point of view of a provider of advice in relation to exchange listed financial products, Bell Potter believes an obligation to assess whether the retail client needs are better met other than through the acquisition of exchange listed financial products, when the client has come to Bell Potter with the intention of dealing in such financial products, is going too far. In fact, we think it is impractical to expect those accredited in, and authorized to provide advice on, exchange listed financial products be required to advise on the suitability of another category of financial product for which they are neither accredited nor authorised.

The Opt-In Provisions:

With regard to the Opt-In provisions it is recommended that where the on-going fee is primarily related to an administrative service entailing direct documentary reporting to the client it should be excluded from the Opt-In obligation.

Bell Potter's on-going fee arrangements in the main, relate to its Portfolio Administration Service (PAS) and its Superannuation Solution Service (SSS). The former can be terminated at any time on 2 weeks notice and the latter can also be terminated at any time with a pro rata fee charged for the year of termination, except for the first year, when the annual fee is payable on termination within the first year.

PAS provides transaction, valuation, sector analysis, income and capital gains reporting and entails acting as the client shareholder's mail box enabling the receipt and reconciliation of dividends and the processing of corporate actions.

This service is based on all the retail client's exchange listed securities being Brokers Sponsored by Bell Potter and all non-exchange listed securities being registered to Bell Potter's address. Failure to Opt-In by the specified date would oblige us to immediately change the registered address of all securities and for the retail client to assume complete responsibility for all the aforementioned matters, which unless purposely intended by the retail client, would result in considerable inconvenience and risk of loss of entitlements under corporate actions.

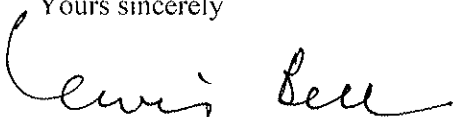
SSS is even more complicated in that it manages contributions, taxation, pension payments, and reporting etc in accordance with the requirements of the ATO, the regulator of self managed superannuation funds. Although clients can easily withdraw from the SSS they need to have organized alternative administration arrangements well in advance of the withdrawal and an inadvertent failure to Opt-In could result in ATO penalties.

Conclusion:

The proposed amendments to the Corporations Act will apply to all providers of financial advice to retail clients and because of the different types of advisory service provided within the financial service industry the proposed amendments may have some unintended consequences, which rather than improve the quality of advice in some sectors of the industry will unnecessarily increase the cost of providing advice and may as a result decrease the availability of such advice. Not all types of financial advisory services are suffering from the lack of quality of advice, trust and confidence that has been identified by the Government.

The solution is to limit the regulatory obligation of specialist financial service providers who are subject to the Market Integrity Rules to the proposed s 961 C (2) (a), (b) and (c) and to exclude administrative services from the Opt-In provisions.

Yours sincerely



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