FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA

Sue Vroombout
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The Treasury
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19 October 2011

Dear Ms Vroombout,

Future of Financial Advice Bill 2011: Exposure Draft - Tranche 2

The Financial Planning Association of Australia (FPA)[1] welcomes the opportunity to provide comments and feedback into the Future of Financial Advice (FoFA) Exposure Draft Legislation (Tranche #2).

The FPA has broadly supported the reform package since they were announced in April 2010 and we continue to support the reforms as they are packaged in this second exposure draft.

In general, the FPA is pleased with the exposure draft and the purpose of our submission is to highlight areas of clarification and potential unintended consequences. In particular we have concerns with:

- The definition and application of group life within a superannuation fund;
- The application of banning asset based fees on geared funds;
- Unintended consequences for employed financial planners;
- Commencement date of each measure within the Bill; and
- Transition period for compliance with the Bill.

The FPA has also noted that several elements of the draft legislation are not included in Tranche 2, most notably the transitional and grandfathering provisions in respect to commissions and volume payments, which would have significant implications for the application of these provisions. We encourage Treasury to accept further comments on Tranche 2 once these important missing elements have been released.

If you have any questions regarding the FPA's submission, please contact me directly on 02 9220 4505 or dante.degori@fpa.asn.au.

Yours sincerely

Dante De Gori
General Manager Policy and Government Relations

[1] The FPA is the peak professional body for financial planning in Australia. The 8,000 individual professional members of the FPA have an enforceable Code of Professional Practice, including the Client First principle. 5,700 of our members have achieved CFP certification, which is the global standard of excellence in financial planning. FPA practitioner members manage the financial affairs of more than 5 million Australians whose investments are valued at $630 billion.

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Exposure Draft – Tranche #2

Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011

Exposure Draft – Tranche #2

A Bill for an Act to amend the law in relation to financial products, and for related purposes

FPA submission to:
The General Manager
Retail Investor Division
The Treasury

19 October 2011

FINANCIAL PLANNING
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Exposure Draft – Tranche #2

INTRODUCTION

As part of our analysis of the exposure draft, the FPA would like to specifically highlight with Treasury our concerns on the following key issues:

- Group life within a superannuation fund;
- Asset based fees on geared funds;
- Unintended consequences for employed financial planners;
- Commencement date; and
- Transition.

Further the FPA would request that consistency in language and terminology needs to be considered when reviewing between the exposure drafts, Tranche #1 and Tranche #2, before fnalising legislation.

Group life within a superannuation fund

The concept of 'group life' insurance' is well established within the financial services industry. It is commonly understood to mean the structural arrangement whereby insurance is purchased from a life company by a trustee of a superannuation fund on behalf of a 'group or class' of members and subsequently offered by that trustee to its members. The structuring of the policy in this way provides many administrative and cost benefits for trustees and their members.

It should be noted that a 'group life' insurance policy does not mean that insurance available under the 'group life' policy cannot be tailored for individual members or that an individual cannot seek financial advice specific to their needs. A 'group life' insurance policy is an insurance contract, which covers a group or class of members of a superannuation fund whereas an individual policy is an insurance contract, which covers an individual member only. Whether a policy is a 'group life' or 'individual' insurance policy does not prohibit a member of the superannuation fund from obtaining personal financial advice on their insurance needs.

The FPA understands that the reason for a ban on commissions for 'group life' is the assumption that members within a 'group life' insurance policy will not have received individual financial advice in respect of their insurance options. Therefore the Government's policy intent is to stop financial planners receiving commissions from insurance premiums paid by members of a 'group life' insurance policy (inside super) that they did not provide individual personal financial advice for. However, the draft legislation, from our perspective, is unclear in its application and appears to capture circumstances that were not intended.

Commissions paid in respect of individual life insurance policies are permitted whereas commissions paid in respect of 'group life' insurance policies (inside super) are prohibited, despite the fact individuals receiving life insurance cover under the 'group life' insurance policies may, like the individuals receiving cover under the individual life insurance policies, be the recipients of personal financial advice in respect of their life insurance cover.

Therefore the FPA believes there are some circumstances where commissions paid from a 'group life' insurance policy (inside super) should be permitted, as they are not the scenarios that the policy measure was designed to capture. For example:

- if a client who actively seeks individual personal advice and acts on financial advice to purchase an insurance policy through a 'group life' arrangement (inside super) in order to access the advantages of group life policy rates as an individual, commissions should be permitted. In this scenario the financial planner is only eligible to receive commission on the 'group life' insurance policy that they have provided individual personal advice on – not commission from all members of the 'group life' arrangement.

- Where a client seeks individual personal financial advice to review and top up their insurance needs, which happens to be within a 'group life' arrangement (inside super), commission for the financial advice relating to that individual's increase of insurance cover should be permitted. Again the financial planner is only eligible for the commission payable on the increase of life insurance cover and not from all members of the 'group life' arrangement.

Asset based fees on geared funds

It is the FPA's understanding that the proposed banning of asset-based fees on geared funds aims to target conflicts of interest where a financial planner is incentivised to recommend leverage (gearing) to increase funds under management and hence their fee income. The FPA notes this measure directly correlates to a recommendation from the Parliamentary Joint Committee on Corporations and Financial Services (PJC) Inquiry into Storm Financial to stop financial planners recommending gearing to clients to increase their fee.

While the FPA supports the intent of this policy measure, we believe the policy design is practically flawed and the issue of 'conflicts' will be addressed by the best interest duty obligations as proposed under s961C (Tranche #1).

The FPA submits that asset-based fees have not been deemed or defined by Government (or any existing or proposed legislation) as conflicted. Further we believe that the banning of asset-based fees on geared funds is being disingenuous to the benefit that a statutory best interest duty obligation will provide. Government and industry must support that through legislation requiring that gearing advice (indeed any advice) is to be in the best interest of the client will assist in driving the behavioural change needed to address this issue for consumers.

Therefore, the FPA suggests the draft legislation under Subdivision C is unnecessary and, due to its inconsistent application in relation to banning asset based fees only in certain scenarios, will create significant confusion and overwhelming complexity for both consumers and financial planners. It is particularly unclear and complex from a practical application, especially in relation to how it applies to existing clients.

Unintended consequences for employed financial planners

The FPA understands the intention of the policy measure is to remove all conflicted remuneration including Bonus payments structured around and depended on the volume and sales targets of financial products. As outlined in the information pack released on 28 April 2011:

> "volume based payments from licensees to their employee advisors for distribution of retail financial products, contingent or based on meeting sales targets".

However, there is some uncertainty from the current draft whether performance based payments would be permitted. In particular the FPA is concerned with those payments that have no link to a particular financial advice outcome or a particular kind or class of product, which based on the announcements by the respective Ministers in April 2010 and April 2011 would be assumed permissible.

There has already been a significant shift away from having all bonus style arrangements dependent on volume and sale targets of financial products. Many employers are requiring financial planners to demonstrate the quality of their financial advice through performance in technical training and examination, continuing development requirements and compliance scores.

However, rewarding financial planners on the amount of fee-for-service revenue that they generate such as through flat dollar fees, hourly based fees and asset-based fees should remain permissible, provided there is no link to a particular financial advice outcome or a particular kind or class of product.

Commencement date

The FPA notes paragraph 2(2) states that information in column 3 of the Commencement information table is not part of the Act and can be edited at any time. However, in his media release (dated 29/08/2011) for Exposure Draft – Tranche #1, the Minister for Financial Services and Superannuation, Bill Shorten MP, confirmed *1 July 2013* as the commencement date of the ban on life insurance commissions in default superannuation and group risk policies within superannuation.

The exposure draft does not confirm the date as 1 July 2013 as per policy measure and Minister Shorten's media release. Rather the exposure draft has 1 July 2012 as the commencement date for all measures within the exposure draft.

The FPA recommends Tranche #2 be amended to ensure it is clear that the provisions relating to the ban on life insurance commissions in default superannuation and 'group life' policies within superannuation do not commence until 1 July 2013.

Transition

The FoFA reforms are the most significant changes to the financial planning industry since the introduction of the Corporations Act in 2001. While the policy objectives of the FoFA reforms have been known and hotly debated over the past two years, the detailed legal obligations required by financial planners, authorised representatives and licensees which dictate the business practices needed to comply with the obligations,

will not be known until the legislation successfully passes through Parliament. Given the pending adjournment of Parliament over the Christmas period, and the level of stakeholder interest in the FoFA reforms, it is foreseeable that this could take some time with the potential of legislation receiving Royal Assent as late as the autumn sitting in 2012. This would leave only a short period of time for industry to ensure business processes, systems and practices meet the detailed obligations of the new law by the commencement day of 1 July 2012.

Given the significant change in industry practice, business models, systems and operations for licensees and providers, the FPA recommends an appropriate transition period be provided to ensure compliance with the new obligations can be achieved with as little disruption as possible to the provision of quality advice to consumers.

Similar to the implementation of the Consumer Credit Act, the FPA recommends allowing a 3 to 6 month assisted compliance period in ASIC's regulatory action in relation to potential breaches of the provisions in Corporations Amendment (Future of Financial Advice) Act 2011. During this assisted compliance period, the focus of ASIC action should be to assist industry to comply, except in the case of serious and deliberate breaches, which cause consumer detriment.

Division 4 – Conflicted Remuneration

Subdivision A - What is conflicted remuneration?

Section 963 Conflicted remuneration

Paragraph 963(1) ***Conflicted remuneration*** *means any benefit, whether monetary or non-monetary, given to a financial services licensee, or a representative of a financial services licensee, who provides financial product advice to persons as retail clients that, because of the nature of the benefit or the circumstances in which it is given:*

(a) might influence the choice of financial product recommended by the licensee or representative to retail clients; or

(b) might otherwise influence the financial product advice given to retail clients by the licensee or representative.

The FPA understands that legislation cannot and should not define (or prescribe) the meaning of every specific word within legislation. However the definition of '**might**' seems very broad and will become the subject to interpretation reducing certainty for this provision. Further the FPA is concerned that it introduces language, which is inconsistent with that used in Tranche #1.

The FPA recommends either a definition of 'might' be included in the legislation, or the term "likely to" be used to make the language consistent with Tranche #1, with either the Explanatory Memorandum and/or the Regulations to detail an objective test ASIC would have to meet to show cause for the Regulator to believe a licensee or representative is "likely to contravene" its obligations.

The FPA understands this policy measure is designed to specifically ban commissions payable as a result of funds under management or the number of products sold. However, the provisions as drafted will capture anything that 'might' be deemed as conflicted.

The FPA seeks clarity around what other forms of remuneration (excluding soft-dollar and volume payments specifically referred to in the draft legislation) that 'might' be deemed as conflicted. Should there be other valid conflicted forms of remuneration, the FPA recommends these be clearly described in either the Explanatory Memorandum or the Regulations.

The FPA recommends either a definition of 'might' be included in the legislation, or the term "likely to" be used to make the language consistent with Tranche #1.

Paragraph 963(2) *Without limiting subsection (1), each of the following is conflicted remuneration:*

*a) a benefit access to which, or the value of which, is dependent on the **total value of financial products** of a particular kind, or particular kinds, recommended by the licensee or representative to retail clients, or a class of retail clients;*

*b) a benefit access to which, or the value of which, is dependent on the **number of financial products** of a particular kind, or particular kinds, recommended by the licensee or representative to retail clients, or a class of retail clients;*

*c) a benefit access to which, or the value of which, is dependent on **the total value of investments** of a particular kind, or particular kinds, made by retail clients, or a class of retail clients, to whom the licensee or representative provides financial product advice.*

***Please note** that the following comments refer to and include comments on Section* **963(a)**

The Information Pack April 2010 states that performance or outcome-based fees are permitted. However, it is unclear as to whether or not s963(2) allows this to occur. In particular the meaning of 'total value of investments' could impact on the ability for a financial planner to be rewarded on performance as was intended in the policy measure.

Further the definition and intent of 'a particular kind' or 'particular kinds' is very much ambiguous and again introduces new language inconsistent with Tranche #1.

The FPA recommends that legislation be amended to clarify the intention of the policy measure as well as amend the language to be consistent and provide definitions and/or examples for certainty.

Employed Financial Planners

Current practice for rewarding employed financial planners can include a bonus based on the fee-for-service advice fee revenue (ie. flat dollar fees, hourly based fees and asset-based fees) that the financial planner generates for the business. This bonus is not related to or dependent on the value or number of products or investments recommended to the client. It is unclear whether this type of incentive program would be permitted under s963(2) and therefore s963C(a).

The FPA believes a fee-for-service advice fee based bonus is a legitimate incentive program, as it does not influence the financial advice outcome and the product recommendations made to the client, and therefore it is not conflicted remuneration. As this type of bonus is not connected to products, the FPA also believes they fall outside the intent of the Government's policy on conflicted remuneration.

The FPA recommends Treasury amend s963(2) and s963C(a) to clarify that bonuses dependent on the total fee-for-service advice fees are permitted, provided there is no link to a particular financial advice outcome or a particular kind or class of product. The Explanatory Memorandum should also be amended to confirm that such incentive programs are allowed.

963A Monetary benefit given in certain circumstances not *conflicted remuneration*

Paragraph 963A(1)(c) *each of the following is satisfied:*

(i) the benefit is given to the licensee or representative in relation to the issue or sale of a financial product to a person;

(ii) financial product advice in relation to the product, or products of that class, has not been given to the person as a retail client by the licensee, the representative or an associate of the licensee or the representative;

The FPA understands the intent of these provisions is to capture execution only services provided to non-retail clients. In relation to these provisions, we note the EM paragraph 1.22 describes payments received as a result of execution only sale of a financial product to a retail client is not conflicted remuneration. However, this is unclear under s963A(c)(i).

The FPA recommends 963A(a)(c) be tightened to close potential loopholes in this provision which could allow representatives to rely on the Life Insurance Code which permits a 'give no advice' for premiums under $500, and ensure it is clear in the legislation that 963A(c) relates specifically to execution only services provided to non-retail clients.

Paragraph 963A(1)(e) *the benefit is a prescribed benefit or is given in prescribed circumstances.*

The FPA notes EM paragraph 1.25 states that this provision is intended to permit stockbrokers to continue to receive conflicted remuneration for execution only stockbroking services provided to retail clients.

The FPA recommends this stockbroker's exemption be clearly described in the regulations under the terms 'prescribed benefit' or 'prescribed circumstances' and confirm the application is available for financial planners who are eligible to provide stockbroking services.

Paragraph 963A(2) *A life risk insurance product is a **group life policy for members of a superannuation entity** if the product is issued to an RSE licensee of a registrable superannuation entity, or a custodian in relation to a registrable superannuation entity, for the benefit of a class of members of the entity.*

The policy intent of this provision is to stop financial planners receiving commissions from every member of a group life policy (inside super), especially if they did not provide individual personal financial advice to each member of that policy. The FPA is concerned that the draft legislation is unclear in its application and therefore goes further than the intended policy.

In particular the drafting does not take into consideration that under the choice environment within superannuation many super funds are offering 'group life' style arrangements for individual retail clients for administrative convenience and to be able to provide retail clients with access to group style premium rates.

The FPA believes there are some genuine circumstances where personal financial advice has been provided to an individual member of a group life policy within a superannuation fund – therefore commissions should be permitted. For example:

- if a client who actively seeks individual personal advice and acts on financial advice to purchase an insurance policy through a group life arrangement (inside super) in order to access the advantages of group life policy rates as an individual, commissions should be permitted. In this scenario the financial planner is only eligible to receive commission on the group life insurance policy that they have provided individual personal advice on – not commission from all members of the 'group life' arrangement.

- Where a client seeks individual personal financial advice to review and top up their insurance needs, which happens to be within a group life arrangement (inside super), commission for the financial advice relating to that individual's increase of insurance cover should be permitted. Again the financial planner is only eligible for the commission payable on the increase of life insurance cover and not from all members of the 'group life' arrangement.

The FPA believe that the current inclusion and definition of 'group life' policies in sections 963A(1)(b) and 963A(2) respectively has the unintended consequence of capturing insurance within superannuation choice environment, which was not intended.

The FPA recommends the definition in the legislation clearly articulate that where a client actively chooses to access and act on personal individual advice and chooses a particular insurance cover as a result of that advice, either through a group life arrangement or individual risk insurance policies inside superannuation, commission-based remuneration should be permitted.

The FPA recommends examples are included in the EM to illustrate the application of the definition and show allowable versus banned commissions such as those provided above.

963B Non-monetary benefit given in certain circumstances not *conflicted remuneration*

Paragraph 963B(c) and (f)

> ***(c)*** *the benefit satisfies each of the following:*
> *(i) the benefit has a genuine education or training purpose;*
> *(ii) the benefit is relevant to the provision of financial product advice to persons as retail clients;*
> *(iii) the benefit complies with regulations made for the purposes of this subparagraph;*
> *(f) the benefit is a prescribed benefit or is given in prescribed circumstances.*

***Please note* that the following comments refer to and include comments on Section 964(2)(e)**

In order to meet Corporation Act requirements to ensure the competency of representatives in providing advice, licensees provide professional development opportunities for representatives. It is common practice for product providers to sponsor licensee conferences and professional development activity either by providing educational speakers, venues or funding for the venue.

The FPA seeks clarity as to the intended treatment of such sponsorship arrangements under sections 963B and 964 and recommends the sponsorship of licensee professional development activity be permitted by specifically including it in the Regulations under 963B(c) and/or (f), and 964(e) and/or (g).

Paragraph 963B(d) *the benefit satisfies each of the following:*

> *(i) the benefit is the provision of information technology software or support;*
> *(ii) the benefit is related to the provision of financial product advice to persons as retail clients in relation to the financial products issued or sold by the benefit provider;*
> *(iii) the benefit complies with regulations made for the purposes of this subparagraph;*

Support services provided to a financial services licensee, or a representative of a licensee, by a 'benefit provider' (for example, a product provider) can include information technology software or support such as financial planning software (intended to be covered by s963B(d)).

However it can also include non-technological support such as technical support services and paraplanning services offered as part of a 'financial advice' service offering. Hence, technical support services are different to information technology (IT) services. For example technical services delivered to financial planners include support and advice in the areas of taxation, superannuation (including SMSF), estate planning, life insurance and social security legislation. Effectively it is the provision of technical strategies and legislative analysis to financial planners.

While such technical support services relate to the provision of financial advice, they have no influence on the advice provided or product recommended and therefore should be separately defined as 'not conflicted remuneration' under s963B and explained in the Explanatory Memorandum.

The FPA recommends additional provisions be included under s963B(g) to clearly define technical support services provided by 'benefit providers' to licensees and/or their representatives, as 'not conflicted remuneration'. These additional provisions should be appropriately explained in the Explanatory Memorandum

963B Non-monetary benefit given in certain circumstances not *conflicted remuneration*

Explanatory Memorandum paragraph 1.34 *Professional development*

- *Domestic requirement – the professional development must be conducted in Australia or New Zealand.*
- *Majority time requirement – where 75 per cent of the time (during standard day of 8 hours or equivalent time) is spent on professional development. In a standard 8 hour day, this takes into account a one hour lunch break, as well as another hour that might be applied to other activities such as networking.*
- *Expenses – any travel costs, accommodation and entertainment outside of the professional development activity must be paid for by participants or its employer or licensee.*

The FPA notes the request for comments on the professional development definition in paragraph 1.34 of the EM and provides the following comments and suggested amendments.

The FPA does not support the limitation of the definition that restricts professional development to Australia and New Zealand. If a representative attends a professional development conference where the costs associated with the professional development activity (only) are covered by the licensee or employer as a benefit for work performance, and the benefit is open to all representatives, this should be permitted as long as the selection criteria for the benefit is not connected with conflicted remuneration. Professional development activity in overseas destinations should be permitted as long as the criteria for a representative to attend is not based on conflicted remuneration such as the value or number of products or investments recommended to clients.

For example, some licensees reward representatives with professional development activity related to advice based on the technical and compliance performance of the representative. The FPA believes professional development activity rewards are a legitimate incentive for encouraging representatives to improve their performance, as long as the incentives are not in any way dependent on or connected to the value or number of products or investments recommended to clients. Incentivising representatives to improve their technical and compliance performance, for example, can assist in raising the quality of advice provided to consumers.

Further if the Government is committed in developing Australia into becoming a financial services hub it needs to effectively compete with other jurisdictions. To limit professional development to only Australia and New Zealand unnecessarily limits our opportunities as a profession.

The FPA recommends the removal of the 'domestic requirement' provision in paragraph 1.34 of the EM for professional development activity.

963C Certain benefits given by an employer to an employee not *conflicted remuneration*

Paragraph 963C(b) *the benefit is remuneration for work carried out, or to be carried out, by the licensee or representative as an employee of that employer and:*

(i) the employer is an Australian ADI; and
(ii) access to the benefit, or the amount of the benefit, is dependent on the licensee or representative recommending a basic banking product; and
(iii) the licensee or representative does not, in the course of recommending that basic banking product, give other financial product advice that does not relate to a basic banking product.

The FPA accepts the intention to permit bank tellers to provide advice to retail clients under existing remuneration sales targets. Given the high degree of media attention surrounding the removal of commissions on financial advice, the FPA recommends existing remuneration and advice disclosures must continue, or even be strengthened, in relation to this service provided by banks and ADIs to ensure retail clients clearly understand that these particular conflicted remuneration structures are being received.

The FPA is also concerned that to 963C(b)(iii) provides a loophole and could result in advice provided by a bank or ADI to a retail client being split into two separate pieces of advice – one on basic banking products; and one on other financial product advice.

The FPA suggests this would be counter to the intent of the provision and of the FoFA reforms and therefore recommends restricting the splitting of a client's advice based on access to remuneration structures.

Subdivision B – Ban on conflicted remuneration

963D Licensee must not accept conflicted remuneration

Paragraph 963D(2)(a) *A financial services licensee contravenes this section if:*

(a) a representative, other than an authorised representative, of the licensee accepts conflicted remuneration; and

The FPA queries why Authorised Representatives are excluded from paragraph 963D(2)(a).

The exclusion of authorised representatives from this provision significantly reduces the ban on conflicted remuneration obligations on licensees, who are the authorising license holder and greatly influence the ability of the provider to meet these obligations when providing advice.

The FPA recommends clarification as to why authorised representatives are excluded from paragraph (2)(a) and/or request that the words 'other than an authorised representative' be removed from this paragraph.

Division 5 – Other banned remuneration

Subdivision A – Benefits from financial product issuers

Section 964 Product issuer must not give monetary or non-monetary benefit to financial services licensee or representative

Paragraph 964(2)(b) *Subsection (1) does not apply to a monetary or non-monetary benefit given to a financial services licensee, or a representative of a financial services licensee, who provides financial product advice to persons as retail clients in the circumstances set out in any of the following paragraphs:*

(b) the benefit is the purchase price for property and the benefit reasonably represents the market value of the property;

The term 'property' is not defined in relation to the intended meaning of provision 964(2)(b). The term property can have many different meanings and most commonly takes the meaning of residential or commercial buildings. Property under this definition is not a regulated financial product and hence, the FPA questions the inclusion of this provision.

The FPA understands that the inclusion of the term 'property' may relate to the provision of a sale or purchase of a licensee business, however this is unclear and not clarified in the EM.

The FPA recommends the term property be clearly defined in legislation and/or the EM or replaced with 'a term more appropriate for s 964(2)(b).

Subdivision B – Volume-based shelf-space fees

964B What is a *volume-based shelf-space fee*?

Paragraph 964B(1) and (2)

*(1) The benefit is a **volume-based shelf-space fee** if:*

(a) access to the benefit, or the value of benefit, is dependent on the total number or value of the funds manager's financial products of a particular kind, or particular kinds, about which information is included on the facility or which are issued through the facility; and

(b) the benefit is not a discount on an amount payable, or a rebate of an amount paid, by the platform operator to the funds manager for services provided by the funds manager to the platform operator (see subsection (2)).

*(2) The benefit is also a **volume-based shelf-space fee** if:*

(a) the benefit is a discount on an amount payable, or a rebate of an amount paid, by the platform operator to the funds manager for services provided by the funds manager to the platform operator; and

(b) the value of the benefit exceeds the reasonable value of scale efficiencies obtained by the funds manager because of the number or value of financial products in relation to which the funds manager provides those services.

It is reasonable for a product provider to be charged an administration fee to cover the platform provider's costs of maintaining the product on the platform system. The legislation on the banning of volume-based shelf-space fees must allow for the appropriate recovery of costs associated with providing platform services. However, the FPA supports the removal of bias associated with payment for the placement of products on platforms.

The FPA recommends where there is a genuine value of costs that need to be recovered, this should be permitted.

Subdivision C – Ban on asset based fees on geared funds

964F Financial services licensees must not charge asset based fees on geared funds
Paragraph 964F(1)

(1) The financial services licensee must not charge an asset-based fee on geared funds used or to be used to acquire financial products by or on behalf of the client to which the advice relates.

***Please note* that the following comments refer to and include comments on Section 964H**

The FPA seeks clarity on the application of this definition and the definition of asset based fees under 964H, and therefore the application of the broader obligations under Subsection C, to brokerage fees if a client used geared funds to purchase shares through a stockbroker.

Paragraph 964F(1) and (3)

(1) The financial services licensee must not charge an asset-based fee on geared funds used or to be used to acquire financial products by or on behalf of the client to which the advice relates.
(2) The regulations may provide that subsection (1) does not apply in prescribed circumstances.

***Please note* that the following comments refer to and include comments on Section 964G**

The policy intent of this provision is to remove the incentive for financial planners to unnecessarily gear clients to maximise their fee potential. The FPA notes this provision directly correlates to a recommendation from the Parliamentary Joint Committee on Corporations and Financial Services (PJC) Inquiry into Storm Financial to remove the incentive for financial planners recommending gearing to clients to increase their fee income.

While the FPA supports the intent of this provision, we believe that this concern will be addressed by the introduction of a best interest duty obligation as proposed under 961C (Tranche #1). Requiring the gearing advice to be in the best interest of the client will assist in driving any behavioural change to address this issue for consumers.

Therefore, the FPA suggests the draft legislation under Subdivision C is unnecessary and, due to its inconsistent application in relation to banning asset based fee in certain scenarios, will be enormously complex to comply with and administer.

Should provisions 964F and 964G be included in the final draft of this Bill, the FPA recommends they be simplified to apply only in circumstances where the financial planner recommends the client borrow funds to invest.

Further, the following circumstances should be explicitly excluded from the provision in the regulations under 964F(3) and 964G(3):

- Where the financial planner is not responsible for and has not recommended the client borrow to invest (the gearing). For example, the client already has geared funds and requests an investment strategy from the financial planner.

- An existing client has a geared portfolio prior to the commencement of the Bill, and 'tops up' the gearing for further investment opportunities following the commencement of the Bill.

Paragraph 964F(4) *Nothing in this section affects the duty of the financial services licensee, or the representative of the financial service licensee, under section 961C to make reasonable inquiries to obtain complete and accurate information (see paragraph 961C(2)(c)).*

The FPA does not support the assumption in 964F(4) that provision 961C creates a duty on the financial services licensee. 961C only applies to the actual 'providers' of the financial advice. Licensees can only breach the best interest duty obligations under 961C indirectly if their representatives breach their obligations (see 961N Licensee must ensure compliance).

Under the draft legislation Tranche #1, licensees cannot breach the best interest obligations directly or in their own right as there is no best interest duty that applies to the behavior and actions of the licensee.

However, the FPA supports the need for a clear positive obligation on licensees to avoid a conflict, give priority to clients, or act in the clients' best interest.

As stated in a number of submissions, with the most recent being Tranche #1 draft legislation, the FPA recommends a positive obligation on licensees to give priority to their clients (considered as a whole) to be included in the legislation, similar to provider obligations under provision s961K.

The FPA recommends 964F be corrected by removing the reference that 961C creates a best interest duty on the financial services licensee.