19 September, 2011

Sue Vroombout
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Email: *futureofadvice@treasury.gov.au*

Dear Ms Vroombout,

FUTURE OF FINANCIAL ADVICE – Tranche 1

The Financial Services Council (FSC) represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers and financial advisory networks. The FSC has 128 members who are responsible for investing $1.8 trillion on behalf of more than 11 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Stock Exchange and is the fourth largest pool of managed funds in the world. The FSC promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

The FSC makes this submission to The Treasury in response to the Exposure Draft of the Corporations Amendment (Future of Financial Advice) Bill 2011 (and accompanying Explanatory Memorandum ("**EM**")) issued on 29 August 2011 by the Minister of Financial Services and Superannuation, the Hon Bill Shorten MP.

The FSC thanks Treasury for the opportunity to comment on the Exposure Draft.

a. Best Interest Duty

In previous submissions to Treasury, the FSC has advocated the introduction of a 'best interests' duty for financial advisers to act in the best interests of their client and to give priority to the interests of the client in the event of a conflict of interest. However, it is critical that the 'best interests' obligation be clearly defined and its application outlined in the legislation and the EM to ensure that the obligation is not equated with the obligation imposed on trustees.

We have previously submitted that the drafting should define the duty so that it is clear and comprehensive to provide certainty for consumers and advisers as to the obligations owed by advisers when providing personal advice, including where there is a conflict of interest.

The exposure draft issued establishes a duty in s961C(1) but has not defined what "best interest' means. Our submission illustrates our interpretation of the duty(s) as drafted, comments on the difficulties the draft creates and makes a number of recommendations to address the concerns raised.

As stated above, given the significance of this change, the dimensions of the term "best interests" need to be explained in the EM. There is merit in, for example, if that is the intent, to indicate that relevant best interests are limited to "financial interests" as opposed to other interests e.g. physical, emotional etc.

Moreover, given that the term "best interests" appears in other legislative contexts e.g. section 52(2)(b) of the SIS Act and Section 181 of the Corporations Act there is also the potential for some degree of confusion or for incorrect assumptions to be made regarding its meaning in this context. On this basis, we have previously submitted that the drafting should define the obligation so that it is clear and comprehensive to provide certainty for consumers and advisers as to the obligations owed by advisers when providing personal advice, including where there is a conflict of interest.

c. Reasonable steps qualification

Both Government announcements in April 2010 and 2011 stipulate that the best interest duty would include "a reasonable steps qualification, so that advisers are only required to take reasonable steps to discharge the duty"[1] and "are not expected to base their recommendations on an assessment of every single product available in the market"[2].

Notwithstanding this, the draft legislation does not provide a reasonable steps defence. Further, the duty(s) as stipulated requires an adviser not only to consider all products available in the market, but to consider products in respect of which the adviser may not be licensed, authorised or competent to assess and or recommend. We do not believe that was the intention of the previous policy statements made by the Government. Our submission makes a number of recommendations to address these concerns.

d. Scalable advice

The FSC believes in the value that quality financial advice delivers to all Australians who receive it as well as to the Australian economy. KPMG Econtech research commissioned by the FSC showed individuals with a financial adviser saved an additional $1,590 each year (after the cost of the initial advice) when compared to a similar individual without a financial adviser. These savings equated to an additional $91,000 upon retirement for a 30 year old Australian.[3] The KPMG Econtech research also

[1] Future of Financial Advice, Information Pack 28 April 2011, page 12
[2] Future of Financial Advice, Information Pack 26 April 2010, page 5
[3] KPMG Econtech, Value Proposition of Financial Advisory Networks Update and Extension, 2011

found that if an additional five per cent of Australians received financial advice, national savings would increase by $4.2 billion (or 0.3 per cent of GDP) by 2016-17.

Given the significant value advice delivers, the FSC strongly supports a scalable advice framework that results in financial advice that is more accessible and more affordable for more Australians. However, to achieve this, a fundamental principle of the scalable advice framework must be regulatory certainty and clarity for both licensees and financial advice providers. The financial advice industry must be able to have confidence in the regulatory framework. Providers of advice and their clients should be able to limit the scope of the advice service to be provided by agreement. This clarity will enable clients to better select the advice level they desire and to better manage the cost which they will pay for advice.

Clear express statutory recognition of the ability to scale or scope advice and further guidance provided in the EM is needed as well as a revision of any " best obligation steps" which effectively limit or negate the ability to limit the subject matter of the advice. Moreover, both in the context of scalable advice and the best interest duty more generally the nature and scope of an obligation/duty can only be meaningfully and sensibly understood in the context of the relevant terms of engagement.

Moreover, the relevant statutory standard to be observed should be determined by reference to the tasks that the financial adviser is engaged to perform. In a statutory context, some judicial recognition of this principle is reflected in decisions such as Vines v ASIC [2007] NSWCA 75 in the context of director's duties.

However, given that this is a new statutory obligation, the EM will need to make specific reference to the relevance and impact of the terms of engagement.

This submission illustrates our interpretation of the duty(s) as drafted, comments on the difficulties the draft creates and makes a number of recommendations to address the concerns raised.

e. Intra-Fund Advice

We note the Government's announcement on 29 August 2011, which confirmed that tranche two of the Future of Financial Advice (FoFA) draft legislation will contain a definition of Intra-Fund Advice. Consultation on Intra-Fund Advice to date has been limited to the type of advice (subject matter) that can be provided by Intra_Fund Advice and therefore paid by a superannuation fund to an adviser from superannuation members' monies, and not on the policy principles generally.

As agreed by members of the FoFA Peak Consultation Group, we submit that Intra-Fund Advice providers must also be governed by the best interest duty regardless of how and by whom they are remunerated.

f. Opt-In

The FSC remains of the view that the consumer protection 'opt-in' aims to address (i.e. a consumer being charged for a service they are not receiving) is actually achieved through two other limbs in the FoFA reform package:

(a) The ban on conflicted remuneration structures– specifically, commissions; and

(b) The best interest duty which carries an explicit duty on an adviser to give priority to the interest of their client's above their own especially if there is a conflict such as remuneration.

As previously submitted, the FSC suggested that an Opt-out process be considered which could be coupled with additional fee disclosure. The obligation in the Exposure Draft is now an amalgam of the initial proposal announced by the Government (to require a consumer to opt-in to continue receiving a service the client agreed to pay), together with highly prescriptive additional annual disclosure requirements.

Whilst the FSC's members welcome the application of the obligation being limited to new client we are concerned that the highly prescriptive drafting of the new obligation means the obligation is administratively complex, costly and inflexible.

Our response comments on our members' concerns and makes recommendations to enhance the flexibility and therefore reduce the costs of compliance (and correspondingly, reduce the cost ultimately borne by consumers).

g. Transition

The FSC is concerned about the time pressures on the industry which are likely to flow from the introduction of the reforms proposed by the Government. Our members submit that significant systems, processes and procedural changes will be required to implement these major reforms. For example, the introduction of the best interest duty for advisers will require:

(a) systems and documentation changes to Financial Services Guides, Statements of Advice and other advice documents;

(b) fundamental changes to the training and compliance frameworks to include the general duty as well as specific duties;

(c) design and delivery of training programs for representatives and support staff; and

(d) updates to monitoring and supervision processes and systems to support these changes.

By the Government's own timetable, the final FoFA legislation will not be passed through Parliament until the end of the first quarter 2012 with the best interest duty and opt-in requirements due to

commence from 1 July 2012. This means that the industry will have somewhere between 3 to 6 months to ensure they are in a position to comply with the legislation.

Combined with many of the other elements of the reforms proposed both by FoFA and Stronger Super, it will be very difficult to comply with all of these new obligations by the proposed start date of 1 July 2012. For this reason, we request the Government consider either extending the proposed implementation date or providing a transitional period to give the industry and advisers sufficient time to make the necessary changes to ensure they are compliant with this legislation at the time of commencement.

If you have any questions regarding the FSC's submission, please do not hesitate to contact me on (02) 9299 3022.

Yours sincerely

CECILIA STORNIOLO
Senior Policy Manager

Best interests duties

1. **Executive Summary**

Key issues

1.1 We fully support the introduction of a legislative best interest duty as outlined by Minister Shorten in the "Future of Financial Advice Information Pack" released in April this year. However, the proposed provisions do not achieve many of the key policy objectives identified in that announcement, and in many cases will be counterproductive to the achievement of those objectives.

1.2 In the following table, we quote the key features of the duty as announced by the Minister in April, and then outline how the draft provisions do not reflect or achieve those objectives

Quotes from April 2011 Announcement	Our comments on the draft provisions
"Compliance with this duty will be measured according to what is reasonable in the circumstances in which the advice is provided. What is reasonable in the circumstances is commensurate and scalable to the client's needs. This means that if the client's needs indicate that only limited advice is necessary, the adviser is not obligated to provide holistic advice." (page 12)	Rather than clarifying the ability to provide scaled or scoped advice, the amendments make this less clear. Currently, as is made clear by the Explanatory Memorandum that accompanied the introduction of s945A, that section allows the adviser to proffer, and/or for the client to request, advice on a specific subject matter. The adviser and the client then agree on the subject matter for the advice, and the investigations are limited to that subject matter. However, the client is protected because the adviser must conduct a reasonable investigation of all relevant client circumstances and of the subject matter, and ensure that the advice given is appropriate having regard to that investigation. Unlike the current s945A, the draft provisions do not allow the adviser to specialise in particular areas of advice. Nor do they allow the adviser and the client to agree on the subject matter of the advice. The adviser must address the subject matter requested by the client, even if the adviser does not offer advice on all of those subject matters. Further, the adviser must consider all of the clients needs and objectives as are reasonably apparent, and must consider alternatives outside the agreed scope of advice even if neither the adviser nor the client want to do or pay for this. Advisers are also required to consider and assess alternative strategies – even those that do not involve financial products. Advisers must therefore be trained and competent in a far wider range of subject matters than is reasonable – in fact, the range is limitless because the universe of alternative strategies is limitless. The essential point is that scaled advice will require an ability to limit the subject matter of the advice. Consistent with the EM, the "steps" prescribed by the best interest obligation should not effectively negate the ability of the subject matter of the advice to be "scaled" or limited. The new provisions will drive advice businesses to a "one size fits all" holistic advice model. This will stifle innovation and specialisation (and therefore competition), and will make advice more difficult and expensive to for clients to obtain e.g. call centre advice.

Continue .. "To facilitate scaled advice, the Government will amend the existing reasonable basis for advice obligation in the Corporations Act to make it clear that this obligation is commensurate and scalable to the client's needs when providing advice. This will help address some concerns identified by industry that the provision of scaled advice is not consistent with their obligations under the Corporations Act." (page 14).	Continue … Advisers will not have certainty over whether the considerations they have made will be sufficient to meet the duties. We believe that the new provisions amount to mandatory over-servicing. Advisers will be required to provide these additional services regardless of whether or not the client wants them or is prepared to pay for them.
The duty should not be interpreted as imposing trustee-style obligations on financial advisers given the differences in roles between a trustee and a financial adviser." (page 12)	The general best interests duty in s961C(1) is undefined. Neither the draft provisions, nor the Explanatory Memorandum, explain whether the cases on the meaning of "best interests" in a trustee context are relevant to interpreting the duty. Further, it is unclear what additional steps or outcomes an adviser is required to take or achieve to comply with the general best interests duty if the adviser has complied with the specific duties in s961C(2), the appropriateness duty in s961H, and the duties of priority in proposed Subdivision E. Also, the duty is not confined to the chosen subject matter of the advice, implying that the duty is much broader than the engagement for advice agreed with the client. The Explanatory Memorandum creates further uncertainty by describing the best interest obligation as being of a "broad nature".
"The focus of the duty should be on how a person has acted in providing advice rather than the outcome of that action." (page 12)	A product cannot be recommended from an APL unless the product "would" achieve the client's objectives or meet their needs. Not only should the duty not focus on the outcomes, but equally, advisers should not be responsible for the performance of products they do not issue. Further, the obligations to consider whether the client's needs and objectives could be better met by alternative means effectively create a duty of "best advice".
"The duty would include a reasonable steps qualification, so that advisers are only required to take reasonable steps to discharge the duty." (page 12)	Neither the general best interests duty in s961C(1), the prescriptive steps in s961C(2), nor the duties of priority in Subdivision E, include a reasonable steps qualification. Compliance with the specific steps set out in s961C(2) should operate as a defence or safe harbour for the best interests duty, rather than as a set of additional prescriptive obligations. Further, the prescriptive steps should be required to be complied with only if and to the extent that it reasonable in the circumstances and relevant to the subject matter of the advice.

"A person giving personal advice will not be required to broke the entire market or a subset of the market of all available financial products to find the best possible product for the client, unless this service is offered by the adviser or requested by the client and subsequently agreed to by both parties." (page 12)	While it is clear that the adviser is not required to consider **all** of the financial products on the market to comply with the requirement to conduct a "reasonable investigation" of products, there is nothing that makes it clear that the adviser is not required to investigate all of the products in a subset of the market (such as "all products that might meet the client's needs and objectives", or "all of products in the class identified for investigation by the client"). As drafted, the ability to limit investigation to the products on the APL can never apply. The adviser is required to consider alternatives outside the subject matter of the advice, and even outside the market for financial products, which goes beyond the expertise of the adviser. This is neither reasonable nor practical and again constrains the ability to offer scaled/limited advice. Finally, none of these limitations apply to the general best interests duty in s961C(1).
"Individual advisers will not be held financially liable for any breach of the duty." (page 13)	Individual advisers who are employed by authorised representatives and are authorised representatives in their own right will be liable for civil penalties under the current draft legislation. There is an inconsistency in the treatment of advisers who are employed by authorised representatives compared to advisers employed by licensees, as the former will frequently be authorised representatives themselves.

1.3 There are also a number of important issues raised by various aspects of the best interest duty. For example:

(a) how does an adviser deal with inconsistent or competing client needs and objectives? Clients want low risk and high return, or lower cost and better features, or may have objectives that are unlikely to be achieved in the timeframe required. How is it possible to identify a product on the APL that "would" meet the client's needs and objectives? The performance of the product is the responsibility of the product issuer. The adviser should be responsible for selecting a product that has the potential to meet particular needs because, at the point of recommendation, potential is all that can be known.

(b) the civil liability that could flow from a contravention of the specific duties represents a substantial and potentially disproportionate expansion of the types of losses that can be recovered from a licensee. Liability can arise in relation to areas that neither the client nor the adviser would contemplate as being within the adviser's sphere of responsibility. Managing this risk will effectively prohibit limited or scoped advice.

(c) As advisers will be subject to the best interest duty and the duty to give priority, in the interests of simplicity and certainty, they should not also be subject to a common law fiduciary duty.

1.4 At this stage it is not clear whether there will be any exemptions from the duty beyond those for basic banking products. In our view, apart from that exemption, the duty should apply to **all** personal advice to retail clients, regardless of whether the advice is intra fund advice, strategic advice or holistic advice.

1.5 The design and establishment of the processes, reprogramming of multiple systems, preparation of documentation and training necessary to comply (and demonstrate compliance) with the specific duties will involve a substantial commitment of time and resources, and is unlikely to be achievable between the date that the legislation is finalised and the currently proposed commencement date.

Best Interest Duty submission outline

1.6 To help illustrate the above and other issues, sections 3 to 8 of the Best Interest Duty submission looks at a simple, practical advice scenario (described in section 2) and attempts to apply the proposed drafting to that situation.

1.7 It is important to note that although the example relates to general insurance advice, the issues raised by the example are not confined to general insurance – these and other issues will apply to any type of personal advice. The example merely serves to illustrate some of the difficulties that will arise in the practical application of the proposed provisions as currently drafted – even in relatively simple cases.

1.8 We note concerns with the application of the Best Interest Duty to basic banking products including the need for greater clarity in application and refer you to the ABA's submission for specifics.

1.9 In section 9, we raise concerns about the ability to provide advice via a computer program in light of the best interest duty as drafted.

1.10 In section 10, we look at some additional suggestions to clarify the provisions.

Use of text boxes in this submission

The text boxes contain our recommendation for resolving the issues identified. However, even if Treasury disagrees with our recommended solution, we urge Treasury to consider alternative solutions to the issues identified. If Treasury does not consider that the issues identified are valid, we would ask that additional text be added to the Explanatory Memorandum to clarify the intended operation of the provisions.

2. Advice scenario (Sample fact situation)

2.1 Consider an adviser who is an employee of a business operating as an authorised representative. The business specialises in providing personal advice on general insurance products. The FSG discloses that the authorised representative only advises on general insurance products and only recommends insurance from a specified list of insurers. A client wants advice on building insurance for their home and their investment property. During the fact finding process, it emerges that both the client's home and their investment property are mortgaged (the mortgagee's interest must be noted on the policy).

2.2 Section 3 to 8 of this submission contains a detailed analysis of the difficulties that arise in applying the proposed duties to the above scenario:

(a) in section 3, we look at how the provisions in effect prohibit scoped advice, and suggest a solution;

(b) in section 4, we look at the specific steps set out in s961C(2);

(c) in section 5, we consider the appropriateness test in section 961H;

(d) in section 6, we look at the duties of priority in subdivision E;

(e) in section 7, we return to section 961C(1) to consider the general best interest duty; and

(f) in section 8, we look at the potential consequences of a breach for the adviser and the licensee.

3. Scoping the subject matter of the advice

3.1 In our example, the adviser is seeking to limit the scope of the advice to be provided, to general insurance only. From a policy perspective, this is appropriate given that the adviser can specialise in that area and give clients access to cheaper and/or better advice on that issue as a result. It also means that both planner and client can negotiate and will be clear about what services will be provided. Further, the opt-in provisions effectively require an adviser's terms of engagement to define the types of advice that the adviser and the client agree will be provided.

3.2 Currently, clients may go to different types of advisers to address different needs. For example, a client may go to an adviser or product issuer for general insurance needs, to another adviser for investment needs, and to a superannuation trustee for advice relating to their superannuation.

3.3 However, the best interests duties as drafted prevent advisers from focusing only on the specific subject matter (agreed between the client and the adviser) if the client also has broader objectives or needs in other areas. On current drafting of the best interest duty, the subject matter that the adviser must address is driven solely by the client's needs.

3.4 Later in this submission we explain our reasoning for these conclusions in more detail, but examples of the way in which the draft provisions prohibit scoped advice include:

(a) in sub-paragraph 961C(2)(c)(i), the adviser must consider whether the information supplied by the client is sufficiently complete to advise on the requested subject matter, even if the agreed subject matter is more expansive or more limited than that which was originally requested;

(b) paragraphs 961C(2)(d) and (f) require the adviser to consider other subject matters and alternatives beyond the scope of the requested advice,

(c) in paragraph 961C(2)(e), the adviser must decline to advise where the requested subject matter is outside the adviser's expertise, even where the adviser and the client have agreed to a more limited subject matter that is entirely within the adviser's expertise;

(d) in paragraph 961C(2)(g), the adviser must investigate products that might meet the clients needs and objectives, but this is not limited to those needs that the client and adviser agree are to be addressed;

(e) sub-section 961C(3) does not apply if the client requests advice on products that include non- basic banking products. It also does not apply if the client is not specific about the types of products that the client is requesting advice on; and

(f) section 961D defines "reasonably apparent" only by reference to what would be apparent to a reasonable adviser. It is not (but it should also be) limited to what is relevant to the subject matter of the advice. As a result, all needs and objective that are "reasonably apparent" to a reasonable adviser would need to be considered, even if they are irrelevant to the advice that the client has requested or the adviser has offered. Further, the "reasonably apparent" qualification is only expressed to apply to the obligations imposed on an adviser under sub-sections 961C(2)(c) and (d) – the provider does not have the benefit of this judgment rule in relation to the other elements of the duty. Finally, the "reasonably apparent" test is defined by reference to the subject matter of the advice

requested. This should instead refer to the subject matter agreed with the client, to foster scalable advice and ensure that the scope of the provider's authorisations and capability are recognised.

The FSC recommends that these provisions should be amended to make it clear that the client and adviser can agree to limit the scope of the subject matter of the advice. Further, the best interest duty should more broadly refer to the need to only provide advice on matters which are "reasonably apparent"

3.5 Accordingly, on current drafting, it is not permissible for the adviser to seek to have the client agree that the adviser need only consider a particular subject matter if the client also has needs in other areas.

3.6 Section 960A makes a provision of a contract void if the provision seeks to exclude any of the duties. In the case of the general insurance adviser, in our view, this would seem to apply to their offer to consider only general insurance. Accordingly, the provision setting out the agreed scope of the services to be provided is void. In turn, this means that the key provision of the contract which entitles the client to an adviser's services is void.

The FSC recommends that the provisions should only make a condition of a contract or arrangement void to the extent that the provision seeks to exclude the duties. The provision should clearly allow the adviser and the client to agree the scope of the advice.

3.7 To help address these issues, the various obligations/duties should apply only to the extent relevant to the agreed subject matter of the advice. In particular, the adviser should only have to consider the client's needs, objectives, financial circumstances and interests if and to the extent that it is reasonably apparent that they are relevant to that subject matter. This should be a general principle that applies across all of the obligations/duties for the reasons detailed in this submission.

The FSC recommends that a new section should be added that applies across all of the obligations/duties in Division 2 of Part 7.7A that explicitly recognises that those obligations/duties apply only to the extent that it is reasonably apparent that they are relevant to the subject matter of the advice, and require the adviser to investigate and consider only those client needs, objectives, financial circumstances and interests as are relevant to that subject matter.

3.8 The current drafting appears to reflect a concern that allowing advisers and clients to agree on the scope of the subject matter will result in clients not receiving the advice they need, or in clients receiving advice that is inappropriate or not in their interests. We believe this fear is unfounded, because advisers would still have to consider all of the client's circumstances as are relevant to determining whether the recommendation ultimately given is appropriate and in the client's interests. This is currently the case under s945A of the Corporations Act 2001, as expanded upon in the Explanatory Memorandum relevant to that section.

The FSC submits that importantly, the adviser would still be required to investigate and consider all of the client's financial situation, needs and objectives as are relevant to the agreed subject matter and to ensure that the advice given is appropriate for the client.

Because the adviser must consider all the relevant personal circumstances of the client, it would not be permissible for an adviser to narrow the scope of the advice in such a way as to produce a compliant, yet unsuitable, recommendation.

Even if the scope of the advice is on a single product, the adviser must investigate and consider all client circumstances that are relevant to determining whether that product is suitable (including, if relevant, products already held) and must place the client's interests first when they do so. If those investigations lead to the conclusion that the product is unsuitable, the adviser would be prohibited from recommending the product.

In this way, the provisions would provide an appropriate level of flexibility to enable limited advice models, yet still provide the highest level of consumer protection by not allowing recommendations that are not in a client's best interest.

3.9 In fact, forcing advisers to go beyond the agreed subject matter means that clients will not be able to address any specific needs without addressing all needs – meaning that specific needs will be left unaddressed until the client has the time and money necessary to seek and obtain holistic advice.

The FSC submits that allowing the subject matter to be agreed between the client and the adviser better serves the interests of consumers. It will also result in greater accessibility to the type of advice clients want and for which they are prepared to pay.

4. **Specific steps in s961C(2)**

Paragraphs (a) and (b)

4.1 In this example, paragraphs (a) and (b) of s961C(2) raise the following concerns:

(a) should be limited to relevant personal circumstances; and

(b) is quite unclear as a separate obligation - what does it actually require an adviser to do? Really this should act as a qualifier for all the steps.

That is (1) and (2) should be limited by reference to the subject matter or agreed scope of the advice.

Paragraph (c)

4.2 In order to comply with s961C(2)(c), the adviser must (among other things) obtain instructions from the client as to the replacement value of the buildings. However, the replacement value of the buildings is not accurately known by the client. The adviser collects information from the client about the building's construction, size, and any site specific issues such as whether the block is steeply sloping. From this information, the adviser estimates the likely cost of replacing the building.

4.3 However, the adviser's obligation is to make reasonable enquiries **to obtain complete and accurate information** – not just to make reasonable enquiries to obtain information that is sufficiently accurate and complete for the purposes of giving the advice. In this case, the steps taken would only ever produce an estimate, and is based on the client's description of the premises, which may be incomplete. Strictly speaking, then, the adviser has not met their obligation to take reasonable steps to ensure accuracy and completeness. The adviser would seem to be obligated to go to the time and expense of arranging a formal building valuation, which is unreasonable in the circumstances. In addition, the adviser should only be required to make reasonable inquiries of the client and to not make inquiries of other people or verify the client's information.

The FSC recommends that s961C(2)(c) should only require the adviser to make reasonable enquiries of the client to obtain information that is sufficiently complete and accurate for the purposes of providing advice on the subject matter.

Paragraphs (d) and (f)

4.4 Under paragraph s961C(2)(d), the adviser must consider whether it is reasonably apparent that the client's needs and objectives could be better achieved by obtaining advice on a different subject matter.

4.5 The FSC submits it is not clear what needs and objectives are relevant here, nor how far afield the adviser must go in exploring potential alternative subject matters. Unlike the existing provisions of

s945A, s961C(2)(d) is not qualified by reference to the subject matter of the advice, so it seems that (at least) **any** needs and objectives that are "reasonably apparent" must be considered, and a determination made as to whether it is "reasonably apparent" that those needs or objectives "could" be better met by obtaining advice on a different subject matter.

4.6 The adviser appears obligated to give considerations outside of the requested subject matter, and potentially beyond the adviser's expertise or authorisation.

4.7 In the present case, for example, does the adviser need to consider:

(a) whether the client should consider life insurance to help pay off the mortgages if the client dies or cannot work, even though this was not requested by the client?

(b) whether the client "could" be better off selling the investment property and instead investing in a diversified portfolio of investments, say through superannuation?

4.8 Does the adviser need to tailor the advice about other potential subject matters to the client's specific needs and objectives, or is it enough to provide pro-forma disclosure about what will not be covered by the advice, with a recommendation that the client consider whether they should obtain advice in those areas?

4.9 How is the adviser to determine what other subject matters could better achieve the client's needs and objectives without fully exploring those other subject matters?

4.10 How likely does it need to be that the client's needs or objectives would be better achieved in order for the adviser to need alert the client that they "could" be better met? Is a mere possibility that the client could be better off sufficient to trigger the requirement?

4.11 If there are two or more other subject matters that could better achieve client objectives, does the adviser need to identify all of them, or only the best one? Does this paragraph therefore effectively require the adviser to identify the best possible subject matter for the client to obtain advice on? Does this include subject matters that go beyond the adviser's authorisation, expertise or APL?

4.12 We submit this paragraph effectively prevent scalability of advice because of the requirement to consider these alternatives.

4.13 In effect, we submit this paragraph requires the adviser to provide holistic advice to the client and identify the best advice for the client.

4.14 Similar questions arise in s961C(2)(f) as arise for paragraph (d). For example, in our general insurance example, does the adviser have to consider whether the client would be better off:

(a) selling the investment property to pay off the mortgage on the client's home?

(b) selling the investment property or home and buy another one in a safer location?

(c) buying a different type of investment, such as art or commodities?

4.15 In addition, unlike paragraph (d), paragraph (f) is not qualified by reference to a "reasonably apparent" test.

4.16 Further, paragraph (f) does not merely require the adviser to consider whether the client should obtain advice on the alternative means of satisfying the client's needs and objectives, it actually requires the adviser to assess any alternative strategy that "could" meet the client's needs and objectives.

4.17 In effect, this will require advisers to become experts in areas that they are not currently required or able to advise on, such as real property, and also require advisers to speculate as to whether non-financial product alternatives "could" meet the client's needs and objectives.

The FSC submits that in their practical application, s961C(2) paragraphs (d) and (f):

- **prevent advisers and clients from agreeing to limit the subject matter of the advice to a particular scope;**
- **require advisers to develop expertise in areas outside their authorisations and business models;**
- **have no boundaries as to what other subject matters have to be considered;**
- **require advisers to identify the best possible scope of advice rather than an agreed scope, in effect the best advice;**
- **require advisers to consider subject matter that the client has not asked them to consider; and**
- **require clients to pay for advice and adviser time for matters they have not requested.**

For these reasons, recommend that s961C(2) paragraphs (d) and (f) should be deleted.

S961C(2) Paragraph (g)

4.18 Paragraph (g) is also too broad in that it is not limited to the needs and objectives relevant to the subject matter of the advice. In our general insurance example, this means that the adviser must consider what financial products might meet the client's investment needs – the adviser is aware that the client has investment needs and objectives because they are aware of the investment property.

4.19 Personal advice does not always involve product recommendations. In some cases, advisers will advise on broad strategies, or (for example) about the type and amount of superannuation contributions or life insurance required, but without making a specific product recommendation. Paragraph (g) requires an investigation of products in every case, and so is inappropriate in such cases.

The FSC recommends that s961C(2) paragraph (g) should be amended so that it only requires the adviser to assess products that might meet the needs and objectives relevant to the subject matter of the advice, and then only where product recommendations are to be made.

s961C(2)(g) Reasonable reliance on research

4.20 Sub-paragraph (ii) of s961C(2)(g) imposes an undefined and potentially onerous and inefficient obligation on authorized representatives and employee representatives. The current law requires the provider (currently the licensee or authorized representative) to conduct such investigation of the subject matter (including product research) as is reasonable in all of the circumstances. Authorised representatives have the defence of reasonable reliance on information or instructions provided by their licensee. Employees do not have this defence as they do not have the obligation, and are not exposed to a penalty. Under s912C(2)(g), the provider (now the individual authorized representative or employee representative) must personally "assess" any information gathered by a third party in the investigation of products. This third party includes any other person employed or engaged by the licensee, including the licensee's own specialist research team..

4.21 This proposition raises a number of questions:

(a) Does it require an authorised representative or employee representative to second guess the licensee's APL?

(b) Does it require an authorized representative or employee representative to second guess every element of research into products, model portfolios and strategies, including research conducted by the licensee's own internal specialist research analysts?

(c) What kind and extent of assessment is required?

(d) How will a provider prove that he/she has carried out the assessment in each case?

(e) Provision of approved lists and research is a critical element of any licensee's compliance procedures and risk management. How can a licensee supervise, monitor and generally ensure compliance by individual advisers if those advisers are not permitted to rely on the licensee's research, and are required to review it?

(f) What effect will this obligation have on the cost of providing advice?

4.22 We acknowledge the policy objective that responsibility should not be shrugged off to external research houses who have no direct obligation or legal exposure to the client. However the proposed framing of the obligation creates significant inefficiencies, and the potentially greater risk of ad hoc decisions by individual advisers.

4.23 There is a limited form of protection for individual employee representatives under the proposed provisions, in that they are not subject (or at least not intended to be subject) to the civil penalty regime. This remains problematic, because

(a) It still imposes a substantial and undefined burden on each individual employed adviser;

(b) It still requires the licensee to devise a compliance and monitoring regime to ensure that each of its employees has individually assessed every element of the licensee's own research; and

(c) The employee is still exposed to the possibility of a banning order arising from breach of the obligation, with no statutory defence of reasonable reliance on the licensee's instructions

The FSC recommends that s961C(2)(g) (ii) should be amended so that the obligation can be satisfied by reasonable reliance on information or instructions provided by the licensee.

In addition, clarification should be provided in the Explanatory Memorandum of the extent to which an individual adviser must go in "assessing" information gathered by third parties.

Section 961E

4.24 The requirements under paragraph (g) are affected by s961E.

4.25 While subsection s961E clearly states that a reasonable investigation of financial products does not require an investigation into every available financial product, it does not clarify that the adviser is not required to investigate every financial product that might meet the client's needs and objectives.

4.26 For example, while our general insurance adviser is clearly not required to investigate, for example, car insurance, it is not clear that the adviser is not required to look at all building insurance products on the market.

The FSC recommends that s961E(1) should be amended to clarify that the adviser is not required to investigate all products that might meet the client's needs and objectives.

4.27 If the client asks the adviser to consider "building insurance products" as a class (which is by implication almost necessarily the case), s961E(2) applies. The word "However" in subsection (2) seems to suggest that subsection (2) is a qualification or exception to subsection (1) – which arguably means that the client's request means that the adviser must consider all building insurance products.

The FSC recommends that s961E(2) should be amended to clarify that the adviser is not required to investigate all products in the class requested by the client.

4.28 As the best interest obligations in section 961C are not an exhaustive list of obligations, s961E does not achieve what is intended in any event, which is to modify the best interest duty to an investigation of products on an APL. This needs to be remedied.

Section 961G(3)

4.29 Paragraphs 961C(2)(g) and s961E are also affected by s961G(3).

4.30 If our general insurance adviser has an APL and the APL contains a product that would meet the needs of the client, s961G(3) does not apply. This is because s961G(1)(c) or s961G(2)(c) (whichever applies) is not satisfied. This means that there is nothing in the provisions that makes clear that the adviser's reasonable investigation of products can be limited to the APL.

The FSC recommends that the drafting should clarify that s961G(3) applies regardless of whether 961G(1)(c) or 961G(2)(c) apply. It is suggested that the substance of paragraphs 961G(1)(c) and 961G(2)(c) should be moved into s961G(4) – subject to the amendments recommended later in this submission.

Paragraph (h)

4.31 The Explanatory Memorandum says that paragraph (h) is intended to apply where the adviser is recommending the substitution of a product or the acquisition of a product that is substantially similar to a product already held. The draft provisions do not fully reflect the "substantially similar" qualification.

4.32 In our general insurance example, paragraph (h) would apply even if the client had no existing building insurance. This is because the client almost certainly has another financial product, such as a bank account.

The FSC recommends that s961C(2) paragraph (h) should be amended so that it only applies to a recommendation to substitute a financial product or acquire a product in cases where the provider knows or ought reasonably to know that a product already held by the client could meet the client's needs and objectives relevant to the subject matter of the advice.

4.33 If the client did have existing building insurance and the adviser is considering whether to replace the insurance, paragraph (h) requires the adviser to weigh the disadvantages of replacing the insurance against the advantages of using the existing insurance. In other words, the adviser seems to be required to weigh the disadvantages of acquiring the product against each other. What seems to be missing is a consideration of the advantages of acquiring the product and of the disadvantages of not acquiring the product.

The FSC recommends that s961C(2) paragraph (h) should be amended to require the adviser to weigh the advantages of acquiring the product against the disadvantages of acquiring the product.

Paragraph (i)

4.34 The Explanatory Memorandum states that the duties of priority do not prohibit the adviser from pursuing the adviser's (or another person's) interests where they do not conflict with the client's interests. However, paragraph (i) requires all judgements to be based on the needs and objectives of the client. Accordingly, even if the cost and features of two alternative products are identical, the adviser will not be able to choose one product over the other on the basis of the adviser's own interests (or the interests of the licensee or other third party).

The FSC recommends that s961C(2) paragraph (i) should be deleted as it seems to override the intended operation and limitations of the duties of priority.

Section 961G

4.35 If the general insurance adviser has an APL, then section 961G applies. The effect of the section is that the adviser cannot recommend a product on the APL unless the product "would" meet the needs and achieve the objectives of the client.

4.36 Clients typically have needs and objectives that conflict with each other. For example, our general insurance client would have the objective of obtaining maximum coverage for their properties, but would also have the objective of not paying more than a specified limit. However, more coverage typically means higher premiums. This being the case, how is the adviser going to be able to find a product that "would" achieve both those objectives? In reality, the adviser will need to exercise a judgement in balancing competing client objectives – the provisions should be drafted to reflect this.

4.37 Advisers also meet client needs by combining products. For example, an investment client would want to diversify their investments to reduce risk – but the adviser should not be restricted to having to satisfy that need through one product only.

4.38 Clients needs and objectives may also be subjective or unachievable. For example, if our general insurance client's property was in a flood-prone area where no insurers provide flood coverage, can the adviser recommend any products? What if there is an specialist insurer that does provide flood coverage for a very high premium? What if that specialist insurer is not on the APL – is the adviser required to investigate insurers outside the APL in order to determine whether any insurers offer flood cover?

4.39 Finally, even if there is a need or objective that is not in conflict with another need or objective, the "would achieve" test inappropriately focuses the test on the outcome of the advice rather than on the reasonableness of the process and the requirement to give priority to the client's interests. Whether an objective "would" be achieved is usually subject to future contingencies beyond the control of the adviser (or anyone).

4.40 For all of these reasons, we submit that the requirement that a product cannot be recommended unless it "would" achieve the client's needs and objectives is inappropriate.

The FSC recommends that paragraphs 961G(1)(c) and 961G(2)(c) (as moved into s961G(4)) should be amended so that the test is whether it would be reasonable to conclude that a product on the APL would be appropriate for the client, within the meaning of section 961H. If not, the adviser must not recommend a product on the APL. This recognises that client's needs and objectives are not always all achievable.

4.41 We also note that (on current drafting) s961G(4) applies where the adviser concludes that no product on the APL "would" meet the clients needs and objectives, but then requires the adviser to tell the client that there is no product on the APL that "might" meet their needs and objectives.

4.42 More importantly, if the adviser refrains from recommending a product on the list as required by s961G(4)(b), what is the purpose of requiring the adviser to make the disclosure in s961G(4)(a)?

The FSC recommends that Paragraph 961G(4)(a) should be deleted.

5. The appropriateness test in s961H

5.1 The general insurance adviser would then need to ensure that the advice meets the appropriateness test in section 961H.

5.2 Currently, section 945A explicitly ties the appropriateness of the advice to the investigation of the subject matter or the client's circumstances. It does so by requiring the advice to be appropriate "having regard to" those enquiries and investigations. This element is missing from 961H.

The FSC recommends that s961H should be amended to ensure that appropriateness is tested "having regard to the information that the provider knows, or would have known if the provider had satisfied the duty under s961C".

6. The duties of priority in Subdivision E

6.1 The adviser then needs to satisfy the duties of priority in Subdivision E.

6.2 It is not clear whether the duties of priority would be breached if the adviser fails to give priority to an interest of the client of which the adviser was unaware. Does the duty extend to interests that the adviser should have been aware of had the adviser complied with their other duties? Does the duty extend to client interests that are not "reasonably apparent"?

The FSC recommends that the duties of priority should only apply to interests of the client that the adviser either was aware of, or interests which the adviser would have been aware of had they complied with the other statutory duties.

7. The general duty to act in the client's best interests in s961C(1)

7.1 We return now to s961C(1), the general duty to act in the client's best interests. This duty is not qualified by reference to s961C(2), nor by the appropriateness test, nor by duties of priority, nor is there a safe harbour or reasonable steps defence as previously announced.

7.2 Further, because the general best interests duty in section 961C(1) is not defined or qualified, in our view its meaning is very uncertain. In particular:

(a) If the specific steps in section 961C(2) have been complied with (including that all judgements have been based on client needs and objectives), and the advice is appropriate for the client (s961H), and the adviser has given priority to the client's interests (Subdivision E), what additional steps or outcomes does the adviser need to take or achieve to satisfy the general duty? The rules of statutory interpretation will require a court to find additional content in the general duty, over and above the requirements in the other sections. What is that additional content intended to be?

(b) A number of the other requirements have been carefully qualified or limited to avoid unintended consequences. Given that those other requirements do not qualify or limit the general duty, do those limitations also apply in relation to the general duty? For example, in complying with the general duty:

(i) Is it enough if only “reasonably apparent” inaccuracies or gaps in information are investigated?

(ii) Is it enough if only “reasonably apparent” alternative subject matters are considered?

(iii) Is it enough to merely advise the client of potentially better subject matters for the advice, or does the adviser actually have to investigate those other subject matters?

(iv) Does the investigation of products need to involve investigation of every product available, and can this be limited by reference to the APL?

(v) Must the advice only be “appropriate”, or does the advice have to be “best advice”?

(vi) Does the general duty allow the adviser to pursue their own interests where they do not conflict with the client’s interests, as per the duty of priority?

(c) Does the general duty require "best advice"? What does the word "best" mean in "best interests"?

(d) Does it include a duty of care, or is it enough that the adviser genuinely acts with only the client's interests in mind, even though their advice was inappropriate?

(e) Can the adviser pursue its own or another person's interests if they are not inconsistent with the client's interests? The Explanatory Memorandum says that this is not prohibited by the duty of priority, but does not say that this not prohibited by the general best interests duty.

(f) To what extent must the adviser challenge or revisit client objectives that the adviser does not agree with?

(g) Does the adviser satisfy the duty if they advise in accordance with a client’s wish to take a high risk? For example, to obtain only minimal insurance cover and risk that the property will not be fully covered for the key risks, or to take a non-insurance example, to advise in accordance with a client’s wish to invest aggressively in high risk investments in order to pursue high returns? Or must the adviser only recommend a conservative and prudent approach, giving priority to protecting the client’s existing position, as is typically done by trustees?

(h) Is the best interests duty limited in scope to the subject matter of the advice and/or to the needs and objectives relevant to that subject matter? For example, if our general insurance adviser considers direct property to be a poor or risky investment, can the adviser recommend any insurance to the client without also recommending that the client sell their property?

(i) To what extent is the case law on “best interests” in the life insurance company and trustee contexts actually relevant and applicable to the general duty in s961C(1)? Advisers are in a very different position to trustees and life insurance companies – advisers have a personal relationship with the client and must take into account individual needs and objectives, whereas a trustee or life company typically needs to consider the interests of the beneficiaries and policyholders only to the extent that those interests arise in their capacity as beneficiaries or policyholders.

7.3 In our view, these and other questions mean that the application of the general duty is extremely uncertain in practice. It will be some time before court decisions emerge to give clarity to industry

and regulators on these issues. In the meantime, the costs of providing advice will have increased as advisers seek to manage their risks. Professional indemnity insurers are also likely to raise premiums to offset the increased risk and uncertainty.

The FSC recommends that the best interests duty should:

- **be exhaustively defined in the legislation, along the lines described in the Explanatory Memorandum, namely that acting in the best interests of the client means "making the interests, objectives, financial situation and needs of the client in relation to the subject matter of the advice paramount"; and**
- **expressly state that the duty is focussed on the process and considerations that the adviser must follow and focus on, rather than on the quality or outcome of the advice. The quality of the advice should be left to be tested under s961H.**
- **be qualified by a reasonable steps defence or safe harbour as previously announced by both Minister Bowen and Minister Shorten. The defence or safe harbour should apply if subsection (2) is complied with; and**
- **expressly clarify that the adviser and the client can agree a subject matter of the advice and that the consideration of the client's financial situation, needs, objectives, interests, products and alternative strategies (including the specific steps in subsection (2)) are limited so that the adviser need only consider them to the extent that they are relevant to that agreed subject matter.**

The FSC submits that these measures will provide industry, regulators and consumers with the required high level of protection and certainty.

8. What if there is a breach?

8.1 Because our general insurance adviser is an employee of an authorised representative of a licensee, the adviser must also be an authorised representative of that licensee (see s911B). Because the proposed duties apply to the provider (being the employee in this case), and because s769B(7) does not apply, the effect of s769B is that if there is a breach, both the adviser, the adviser's employer and the licensee will have committed the breach. This in turn means that both the employee and the employer both contravene s961S, which in turns means that both the employer and the employee are liable for the civil penalties that may be imposed.

8.2 However, if the adviser had instead been employed by a licensee, the effect of s961M(2) is that only the licensee is subject to the civil penalty.

The FSC recommends that the treatment of employed advisers should be consistent regardless of whether the adviser is employed by an authorised representative or by a licensee. In both cases, it is the employer that should be liable for the penalty. Section 961S should be amended accordingly.

Subsection 769B(7) should also be amended to include reference to the new Division 2 of Part 7.7A to ensure that licensees are not deemed to have done what their authorised representatives have done for the purposes of the new Division 2 of Part 7.7A.

8.3 Authorised representatives have a defence to the civil penalties if they act in reasonable reliance on the directions or guidance of the licensee. There is no defence for employees of licensees or authorised representatives in relation to their contraventions. Even though employees are not (intended to be) liable for civil penalties, they will still be subject to regulatory action against them as individuals.

The FSC recommends that employees of licensees and authorised representatives should have a defence if their contravention was a result of reliance on the directions or guidance of their employer. The defence should not be limited to "reasonable" reliance, as it would be unreasonable to require employees to "second guess" the legality of their employer's instructions.

8.4 The existing civil penalty provisions provide that a court may order a pecuniary penalty only if (broadly speaking), the contravention materially prejudices a person that the relevant provision is designed to protect, or is otherwise a serious contravention. However, the civil penalty provisions for the proposed duties do not include this requirement.

The FSC recommends that the proposed section 1317G(1E) should include a requirement that the Court can only order payment of a pecuniary penalty if there is a substantial number of similar previous breaches and the breaches are serious.

8.5 Section 961P provides for civil liability to compensate clients for loss or damage caused by a contravention of the duties. In determining whether the duties are drafted appropriately, it is necessary to closely consider the civil liability consequences of a breach.

8.6 In our example, what if the general insurance adviser fails to:

(a) Advise the client to consider obtaining advice on life insurance to cover the client's mortgage (which would appear to be a breach of s961C(2)(d) on current drafting), and the client later dies without life insurance?

(b) Advise the client to consider obtaining advice on investing in something other than direct real property (which would appear to be a breach of s961C(2)(d) on current drafting), and the client subsequently loses money because they weren't sufficiently diversified?

(c) Assess whether the client should sell their investment property to pay off their home mortgage, or to instead invest in an alternative non-financial product investment (which would appear to be a breach of s961C(2)(f) on current drafting), and the client later realises that the return would have been better had the client done so?

(d) Ensure that the product recommended from the APL "would" meet the client's needs and objectives (which would appear to be a breach of s961G(4) on current drafting), and the product does not cover flood because no insurer on the APL offered this, and the property floods?

8.7 What is the measure of damages that the licensee would have to pay the client? Is this level of liability fair and reasonable given that the client was only seeking, and the adviser was only offering, advice on building insurance?

The FSC recommends that the civil liability consequences of a contravention should be closely reviewed. On current drafting, some aspects of the new duties could impose a disproportionate level of civil liability on the licensee, for losses that are outside the scope of advice agreed between the client and the adviser.

Appropriate amendment of the duty as outlined above will go some way to remedying this concern.

8.8 The Corporations Act will not override an adviser's common law duty of care or an adviser's general law fiduciary duty (which provides that the adviser must not obtain a benefit for themselves or a third party, and must not act in a conflict situation, unless they have the prior informed consent of the client). This means that there will be two regimes dealing with conflicts of interest that will both need to be complied with – one that requires that you obtain informed consent from the client and one that

requires that you give priority to client interests. Why is it necessary to obtain informed consent when you are obliged to give priority to client interests in any event? This just adds to the regulatory burden and does not provide a clear and simple rule for planners to follow and to explain to clients on conflicts.

The FSC recommends that an An **amendment should be made to section 961B to make it clear that a provider (and their authorised representative and responsible licensee) who complies with their best interests obligations in the Division will be deemed to have complied with their general law fiduciary obligations.**

8.9 Where a breach of the best interests obligation does occur, in determining the quantum of/liability attaching to any relevant loss, it will be important to take into account whether, and to what extent, a client has reasonably relied on the advice (such as for departing or delaying implementation of all or any part of the advice) and/or should share responsibility for the loss (such as for failure to mitigate a loss). Additional guidance and clarification in the EM and legislation is clearly required in this context.

Warnings and disclaimers

8.10 It is important in settling the legislation to establish the best interest duty that the quality of advice to clients is improved but in a manner that does not add unduly to the costs of giving advice. As stated elsewhere in this submission, if the costs associated with providing advice are excessive, then fewer advisers will be able to afford to remain in the industry, those in the industry will resist providing personal advice and consumers' accessibility to advice will be reduced.

8.11 For that reason, it is important to consider those sections in Sub-Division B of Division 2 which require a provider to give additional disclosures or warnings which are not within the scope of existing disclosure requirements (in particular, the FSG or SoA framework).

The FSC recommends that if additional disclosure is required, it should be included within the existing financial services disclosure framework as much as possible.

8.12 Take the disclosure required by Section 961C (2)(d)[4]. If it is "reasonably apparent" that the client's objectives could be better achieved or the client's needs better met if the client obtained advice on another subject matter, either in addition to or in substitution for the advice requested, there must be advice given to the client in writing of that fact. An FSG must already disclose information about the kinds of financial services that the providing entity is authorised to provide and the kind of financial products to which those services relate. Accordingly the client will already have been informed that advice on subject matters outside of those in the FSG cannot be given, where those subject matters fall outside the scope of the provider's authorisations. To the extent that a provider is not able to give advice on subject matters outside of the scope of the provider's authorisations and expertise, then the client could be provided with a standard form disclaimer in the SoA which indicates the scope of the provider's advice.

The FSC requests that the explanatory memorandum be amended to recognise that the disclosures in the FSG will meet this additional disclosure requirement imposed by the best interests obligation.

8.13 The next warning or disclaimer is that in Section 961G (4), which concerns a circumstance where a licensee or authorised representative maintains an approved product list and it is reasonably apparent that there is no product on the list that would achieve the objectives and meet the needs of

4 For the reasons set out above, we are concerned that this requirement will create difficulty in settling a scope of advice to be provided with a client. It also impacts on scalable advice as it suggests that advice cannot be restricted to particular subject matters as agreed with the client. The FSC looks forward to seeing the proposed drafting for provisions which support scalable advice.

the client.[5] To satisfy the duty to act in the best interests of the clients, the provider must advise the client in writing that the provider cannot recommend a product from the list that might achieve the objectives and meet the needs of the client and must not advise the client to acquire a product that is on the list. The concern is that the provider not advise on an inappropriate product. This can readily be met by requiring that the provider not give advice recommending a product from the APL. We therefore submit that paragraph 961G(4)(a) should be deleted and that paragraph 961G(4)(b) is sufficient.

The FSC recommends that paragraph 961G(4)(a) should be deleted and that paragraph 961G(4)(b) is sufficient. If the Government decides to keep the requirement in 961G(4)(a), which we believe should be deleted, it should at least be amended to provide for the client to be notified at the same time and by the same means as the advice is provided, consistent with the warning requirement in section 961J.

9. Providing personal advice through a computer program

9.1 It is crucial that advice be able to be provided through various mediums (including electronic) in order for more people to be able to access quality advice and it is clear that the current drafting of s961(6) recognises this. However, the current best interest duty only allows advice to be scaled by the client. This is incompatible with the situation where the client is accessing advice online through a computer program.

9.2 Where advice is being provided through a computer program, it must be possible for the person who is providing advice through the computer program to be able to scope the advice. Division 2 of Part 7.7A needs to recognise this.

9.3 There are other problems with a computer program trying to comply with the following provisions when providing personal advice:

(a) 961C(1)

(b) 961C(2)(b)

(c) 961C(2)(c)

(d) 961C(2)(d)

(e) 961C(2)(f)

(f) 961C(2)(h)

(g) 961C(2)(i)

(h) 961D

(i) 961H

(j) 961J

[5] As a matter of drafting, the term "would achieve" should be altered. There will never be a product which is guaranteed to achieve the objectives and meet the needs of the client. We suggest words such as "which a reasonable person would expect could achieve the objectives and meet the needs of the client."

9.4 The problems with the draft legislation as they apply to a computer program mostly result from the following:

(a) the inability for a computer program to have to provide advice based on any subject matter requested by the client;

(b) a computer program can't necessarily agree the scope of advice with a client;

(c) a computer program can't necessarily identify inaccuracies in accuracies in client-inputted data or necessarily determine if data entered by a client is incomplete;

(d) the difficulties in clearly limiting the application of the draft provisions to an agreed scope of advice;

(e) a computer program needs limits around what it can consider;

(f) a computer program can't comply with broad undefined obligations; and

(g) a computer program cannot make unlimited assessments and judgements about client-inputted data.

The FSC believes that many of the difficulties identified with providing personal advice through a computer program under the draft legislation should be addressed if the other issues identified in this submission are remedied. In particular it will be critical to ensure the provisions only apply to an agreed scope and to permit a restricted approved product list to be used. In addition, the legislation must permit a computer program to delineate the scope of advice.

10. Other suggestions

Exclusion of fiduciary duty (or even other general law duties), including analogy with s55 of SIS

10.1 Section 55(5) of the Superannuation Industry (Supervision Act) 1993 ("SIS Act") (Cth) provides a defence to a claim, whether brought under the statutory cause of action at s 55(3) of the SIS Act, or under general law, for loss or damage suffered as a result of the making of an investment by or on behalf of a superannuation trustee. It applies if the defendant establishes that the investment was made in accordance with the investment strategy required under the covenant at s 52(2)(f) of the SIS Act. A like defence should be available for any person subject to a claim for loss or damage suffered as a result of the making of an investment in connection with personal advice provided by an adviser regulated under Division 2 of Part 7.7A.

10.2 Where the defendant can establish that the advice satisfied the requirements of ss 961C, 961H, 961J, 961K and 961L, he or she should have a complete defence to such a claim, whether the claim is brought pursuant to s 961P or is otherwise made (noting, particularly, that a representative is not subject to claims under s 961P, but may be exposed to claims brought under other statutory provisions or under the general law).

10.3 Provision of such a defence would reflect the fact that the new legislation has raised the general standard of care required of a reasonable adviser, so that compliance with the legislation is sufficient to comply with the general law standard. It would also ensure that the general professional standard required of an adviser is to ensure that reasonably appropriate recommendations are made following a reasonable investigation of the subject matter of the advice agreed with the client.

The FSC recommend that a defence would require amendment to s961B, and the replacement of s 961P(3) of the draft legislation with a provision of the type suggested.

Opt-In

1. **Executive Summary**

1.1 **T**he FSC remains of the view that the consumer protection 'opt-in' aims to address (i.e. a consumer being charged for a service they are not receiving) is actually achieved through two other limbs in the FoFA reform package:

(a) The ban on conflicted remuneration structures– specifically, commissions; and

(b) The best interest duty which carries an explicit duty on an adviser to give priority to the interest of their client's above their own especially if there is a conflict such as remuneration.

1.2 In addition, the majority of new advice fees administered via platforms are already operating on a fee for service basis, generally giving clients the ability to opt-out at any time. We believe the introduction of a provision requiring a fee arrangement to include the ability to opt out at any time would achieve the same level of consumer protection while reducing the cost burden on advisers and administrative burden which is effectively placed with the client.

1.3 As previously submitted, we believe that an inflexible renewal requirement is also contrary to the best interests of consumers. It will give rise to an unnecessary administrative burden on consumers (and the advice industry) and will shift the risks associated with a changing regulatory, economic and investment environment onto consumers should they inadvertently fail to respond to the opt-in requirements or renew.

1.4 We have previously submitted that where an advice service relationship exists between the client and the adviser, the adviser charging regime should be sufficiently flexible so that the client and adviser can agree:

(a) on the advice service/s to be delivered;

(b) the cost of that service; and

(c) the payment mechanism and term for that service.

1.5 In an opt-in environment we strongly advocate a renewal mechanism that aligns with the contractual term and nature of the client / adviser relationship. However, a number of provisions of the draft legislation in fact, create inflexibility and are far more prescriptive than discussed during the Government's consultation process during the previous twelve months.

1.6 We consider that the proposed provisions will fail to achieve some of the key policy objectives identified in the Government's previous FoFA announcements in April 2010 and April 2011 including increasing access to and affordability of advice and in many cases will in fact be counterproductive to the achievement of those objectives. The following table summarises our concerns:

Quotes from April 2011 Announcement	Our comments on the draft provisions
A requirement for advisers to obtain client agreement to ongoing advice fees every two years. Page 4	The proposed drafting of s962A(1) is very broad and would potentially capture fee scenarios broader than those paid to a financial adviser/provider **for personal advice.**
A two year opt-in means advisers are in regular contact with clients, but provides some flexibility regarding implementation. Page 8	The proposed drafting of the entire Opt-In Division is extremely prescriptive. For example, prescribing new disclosure statements (which cannot be provided to a member at an annual review meeting) and requesting highly prescribed disclosure content.
Only those advisers intending to charge an ongoing advice fee to retails clients need to send the notice. Page 9	The proposed drafting does not adequately exclude arrangements for one-off advice.
The April package distinguishes between commissions (particularly relating to risk insurance) and ongoing fees. Page 7 and 8.	As s962A (1)(a) defines an ongoing fee as "...a fee (however described or structured), we seek clarification from Treasury as to whether the draft provision is intended to capture permissible insurance commissions as an ongoing fee thus bringing them into the opt-in framework. We are aware of commentary by the minister and Treasury stating that this is not the intention. However the current drafting does not preclude it nor carve it out.

1.7 While the opt-in arrangements will not be triggered until 2014, the systems, processes, documentation and training necessary to comply (and demonstrate compliance) will need to be developed as of 1 July 2012. This is unlikely to be achievable between the date that the legislation is finalised and the currently proposed commencement date.

1.8 The FSC therefore strongly submits that further consultation should seek to determine which elements of the opt-in arrangements could be deferred a further 12 months in order to provide licensees and advisers sufficient time to comply with these requirements.

Outline of this part of the submission

Use of text boxes in this submission

The text boxes contain our recommendations for resolving the issues identified. However, even if Treasury disagree with our recommendation, we urge Treasury to consider alternative solutions to the issues identified.

If Treasury does not consider that the issues identified are valid to amend the legislation, we would ask that additional text be added to the Explanatory Memorandum to clarify the intended operation of the provisions.

2. **Application of the Opt-In Division**

Grandfathering

2.1 The following is intended to reflect contractual practices that occur today so that the provision is clear in it practical application and not intended to expand the grandfathering intentions as announced by the Government.

2.2 The FSC submits that the grandfathering provision (s962) should allow for the sale or transfer of all or part of an "advice business" without triggering a 'new ongoing arrangement' and without disruption or alteration to the key disclosure obligations or renewal dates.

2.3 The FSC considers that where this Division applies the above principle should also apply where:

(a) the client's ongoing fee arrangement moves between representatives within the same licensee; or

(b) where the arrangement moves when a representative or an authorised representative moves from one licensee to another; or

(c) where the arrangement moves between different licensees and or authorised representatives through

(i) the sale; or

(ii) other transfer of a licensee's business to another licensee.

(d) Further, and for the avoidance of doubt, it should also apply where both the licensee and authorised representative are different but there is a continuation of the contractual terms of the original arrangement.

2.4 This position is supported by the Minister's confirmation of the contractual rights advisers (licensees) have to receive ongoing remuneration as follows:

"Following legal advice from the Australian Government Solicitor, the Government has determined that the ban on conflicted remuneration (including the ban on commissions) will not apply to existing contractual rights of an adviser to receive ongoing product commissions."[6].

2.5 From a practical perspective, where a 'grandfathered' ongoing fee arrangement is arranged on, or after the commencing day via a platform (superannuation or non-superannuation), the platform will be required to administer the grandfathering arrangements based on assurances from the adviser and/or investor in question that the opt-in requirements do not apply to the ongoing fee arrangement.

2.6 Further, the purchase of an authorised representative's register by the authorised representative's licensee under Buyer of last Resort arrangement ("BOLR") (e.g. adviser retires), no services are provided by the licensee and then, that licensee sells the register to another of its authorised representatives, the situation should be considered 2 "rollover events" similar to CGT so that if grandfathering applied in the original arrangement before BOLR purchase, it should apply to the continued operation of that arrangement with a new authorised representative of the licensee. This should be subject to the arrangements being "substantially similar" and should apply even if the register is divided up and sold to more than 1 authorised representative of that licensee.

[6] The Hon Bill Shorten MP, Press Release 127, 29 August 2011

2.7 Given the liability for these arrangements sits with the licensee/adviser it would be helpful for the Division, or alternatively the EM, to clearly state that the liability for the provision of false information to a third party (e.g. - a platform) by a fee recipient in relation to the application of the grandfathering provisions for ongoing fee arrangements rests with the fee recipient/licensee only.

The FSC recommends the following amendment to s962(3)(a) to capture the spirit of the grandfathering arrangements announced by the Government:

"Where the client has not been provided with [personal – see above comments] financial product advice as a retail client by either the financial service licensee or the provider before the commencing day"; and to

s962(5) For the purposes of this Division, the word "provider" has the same meaning as in Division 1.

We also recommend the following amendment to s962A to provide for continuity of ongoing fee arrangement.

962A (4) Where an ongoing fee arrangement has been entered into between a client and either a financial services licensee and/or an authorised representative of a licensee (Original Arrangement) and:

(a) **the financial services licensee or the authorised representative of the licensee sells or otherwise transfers its business to another provider (Transferee), and a new ongoing fee arrangement is entered into between the Transferee and the client which is on substantially the same terms as those which applied under the Original Arrangement;**

(b) **the provider then changes; or**

(c) **the provider commences to provide financial services to the client as a representative of a different financial services licensee (New Provider) to the financial services licensee which was a party to the Original Arrangement, and the client enters into a new ongoing fee arrangement with the New Provider on substantially the same terms as those which applied under the Original Arrangement, for the purpose of determining when a Transferee or a New Provider is required to give the client a fee disclosure statement or a renewal notice, any new ongoing fee arrangement is taken to be a continuation of the Original Arrangement, notwithstanding that the Original Arrangement may have been terminated.**

Definition of client – multiple capacities

2.8 Some clients might seek advice in a range of different capacities. For example, a person might seek advice in their personal capacity and also in their capacity as trustee of an estate. The law should be clarified to ensure that a client can be treated as the same client, irrespective of the different capacities in which advice may be sought.

To achieve this, the FSC recommends the inclusion of a new interpretation provision in s962 along the following lines:

> **"(5) For the purposes of this Division, a client who seeks advice in different capacities is taken to be the same client, notwithstanding the different capacities in which advice is being sought."**

3. **Issues relating to Ongoing Fee Arrangement definition**

Commencement of the arrangement

3.1 The use of the term "arrangement" suggests a broader concept than a legally binding contract. This creates uncertainty as to when the arrangement commences. While the concept appears to be designed to capture arrangements which may not be recorded in writing, we consider that for administrative simplicity, and as a mechanism to encourage advisers to enter into an agreement with their clients, a rule should be introduced which provides that where the arrangement is set out in a written agreement by the client, the arrangement is deemed to commence on the date the client agrees to the fee arrangement commencing. The will enable the relevant arrangement to capture multiple and ongoing advice scenarios whilst provide a clearer demarcation between potentially overlapping arrangements.

3.2 There are also a number of important issues raised by various aspects of the Ongoing Fee Arrangement definition including for example:

(a) Payment plan/deferred payment for one-off advice

(b) "Ongoing fee arrangements" captures fees and arrangements that are not intended to be caught

(c) Most financial services likely to be caught as "ongoing fee arrangements"

(d) Uncertain application within the advice sector – mixed services

These are examined below:

(a) Payment plans/deferred payment for one off advice

3.3 The FSC understands that section 962A(1)(b) is intended to permit genuine "advice fee payment" arrangements over a specified term (eg payment plan), and is concerned that it fails to meet that objective.

3.4 It is possible that the current drafting of section 962A may pick up fee arrangements for initial and ongoing advice, despite the Explanatory Memorandum explaining at paragraph 2.10 that payment plans for advice or services already provided are not intended to be captured. The lack of clarity results because it is likely that ongoing fee arrangements will often be agreed before any advice, whether initial or ongoing, is given.

3.5 The current drafting assumes the advice process is simplistic – that a client would agree to pay a fee (however described or structured) reasonably characterised as unrelated to any corresponding advice.

3.6 However, the advice process, which is a process of discussions between a client and their adviser, is more intricate that the drafting scenario. In almost all circumstances, the fee for advisory services will be discussed and agreed before the service (the advice) is provided. Even if a genuine deferred payment arrangement is negotiated as opposed to an ongoing arrangement (for example a retainer service), the "advice arrangement" will commence before the advice is provided because it has been agreed to in advance of the adviser conducting the relevant investigations etc.

3.7 This means that initial advice may be brought in to the opt-in regime, despite clause 962A(1)(b) seeking to exclude it from the regime. For example, the Financial Planning Association of Australia rules require that [providing entities] enter into a Terms of Engagement agreement with their clients, which will often be agreed before any advice is provided. Alternatively, ongoing fee arrangements may be documented in a Statement of Advice, which is then signed and agreed to by the client. Again, the advice would not be provided before the ongoing fee arrangement is entered into. Rather than the commencement date being linked to the date a financial service is provided, or a financial product issued, the drafting may need to carve out deferred fees in a way that accommodates the timing of the ongoing fee.

The FSC does not believe that the current drafting reflects the drafting intention. We suggest that the draft be amended to clarify this by inserting a new sentence at the end of S 962A(1) as follows:

"For the avoidance of doubt, an arrangement under which a financial services licensee agrees to provide advice to a retail client once only, with no ongoing arrangement for the provision of advice in the future, is not an ongoing fee arrangement, irrespective of when the client pays for the advice".

Alternative to above: s962A(1) An ongoing fee arrangement is an arrangement in respect of personal advice under which:

(a) **a person to whom a financial services licensee, or a representative of a financial services licensee, provides personal advice as a retail client, agrees to pay a fee for that advice (however described or structured); and**

(b) **the arrangement does not fall within s962A(4).**

s962A(4) An ongoing fee arrangement does not include an arrangement under which a person agrees to pay a single fee (whether or not paid in instalments or by lump sum) (one-off fee) in respect of discrete personal advice where:

(a) **the one-off fee relates solely to that discrete personal advice;**

(b) **the arrangement does not include an agreement to provide ongoing personal advice; and**

(c) **the arrangement does not include an obligation to pay additional or ongoing fees (other than the one-off fee).**

(b) "Ongoing fee arrangements" captures fees and arrangements that are not intended to be caught

3.8 A further significant issue is that an "ongoing fee arrangement" will capture arrangements having nothing to do with the financial advisory sector that is sought to be regulated. In fact, it is likely to capture practically all paid services provided by financial services licensees.

3.9 As drafted, an "ongoing fee arrangement" may apply in any situation where a retail client receives financial product advice - whether or not the advice is personal advice. Treasury will be aware that "financial product advice" is defined in extremely broad terms in the Corporations Act, and includes a broad range of statements and publications outside the realm of traditional financial advice.

The FSC recommends that specifically, the reference in this section to providing "financial product advice" should be amended to refer to "personal financial product advice". If not, the opt-in regime may apply to relationships between a "product manufacturer" (such as a superannuation trustee) and its clients (such as the members of the fund), which would be unworkable.

Similarly, we recommend that the reference in section 962(3) to a client not having been provided with "financial product advice" should be amended to refer to the client not having been provided with "personal financial product advice".

Simple Bank account example

3.10 To select one example, assume that a retail client enters a bank branch, seeking to open a savings account. If the branch is displaying any posters relating to specific financial products or kinds of financial products (including, but not limited to, savings accounts), financial product advice will have been provided to the client by the bank, satisfying the first limb of section 962A(1). When the client accepts the terms of the account, they will usually agree to pay one or more fees. Those fees will relate to a range of matters, including the ongoing provision and management of the account, and perhaps specific fees for service. At least part of the fee will relate indirectly to the provision of regular account statements, which in all probability will include occasional fliers that are likely to contain "financial product advice". The second limb of section 962A(1)(a) is satisfied.

3.11 Even if the fee does not relate in any way to the advice, it is our understanding that section 962A would be satisfied. There is no express requirement for any linkage.

Bank account an "ongoing fee arrangement"

3.12 Based on the description of fees above, these fees cannot reasonably be characterised as relating to advice that has already been given. In this example, the fees relate to all financial (and potentially non-financial) services, including but not limited to advice, to be provided in future.

(c) Most financial services likely to be caught as "ongoing fee arrangements"

3.13 From this example, it will be seen that "ongoing fees" as defined, includes substantially any fee (however described or structured), paid to any financial services licensee by a client that has received "financial product advice" of any kind which are payable after agreement has been reached with the client, whether or not they are truly "ongoing" fees of the kind that are sought to be regulated.

3.14 It will be seen that the definition as drafted (and therefore Division 3) will actually apply to substantially all remunerated services provided by any licensee or authorised representative to a retail client, whether or not primarily concerned with advice, provided that some 'financial product advice" is provided, at any time.

The FSC does not believe that the opt-in requirement is intended to capture all agreed fees relating to financial product advice but rather those which are paid to a financial advice provider for personal financial product advice over a future period.

Our recommended amendments seek to clarify this intended operation.

(d) Uncertain application within the advice sector – mixed services

3.15 Even within the sector that is intended to be regulated, the application may be uncertain. Assume that an adviser agrees a fee arrangement with a client involving some ongoing payment for advisory services, together with specific fees for separate defined future services (such as execution of trades or negotiation of recurrent insurance). Under the draft legislation as it currently stands, the whole of that fee arrangement will be an "ongoing fee arrangement" for the purpose of Division 3 (as the fees do not relate solely to past advice). If, at the second anniversary, the client fails to give a renewal notice, the whole of the arrangement must come to an end. The adviser would also be required to

switch off all record keeping and account information access. The consequence could be that the client seeks to engage the adviser to execute a transaction, however the adviser would be unable to charge fees for providing such services because even though the fee relates to a separate service requested by the client, the charging of fees for these services after the 30 day grace period will be a civil penalty offence.

3.16 The amendments we have suggested would address this situation by clarifying that the ongoing fee arrangement is limited to the fees payable in relation to personal financial product advice.

4. Fee Disclosure Statement

4.1 2.11 of the EM expresses that the Opt-in obligations are imposed on fee recipients only when the ongoing fee is to be charged for a period longer than 12 months in the case of the disclosure obligations. However, there is nothing in the drafting that supports this statement. S962D(1) as drafted will trigger the disclosure requirement. This is presumably just a drafting anomaly.

The FSC recommends that the fee disclosure statement obligations in s962D be amended to clarify that a fee disclosure statement is not required to be provided if the ongoing fee is not charged for a period longer than 12 months

4.2 The current drafting requires that the fee disclosure statement be provided 'at least 30 days before' the first anniversary of the arrangement. In our view the drafting should provide reasonable flexibility to align the provision of the fee disclosure statements with advice/client practices such as an annual review meeting. This is not currently achieved, as the disclosure notice must be given after 10 months.

The FSC seeks an amendment to s962D and s962G to remove "at least 30 days before" and insert "at least annually" and "no less frequently than once in every period of two consecutive years", respectively, at the end of the sentence in those sections. We note that there will need to be some adjustment to S962J and K as a result to recognise that the key dates related to an anniversary of an ongoing fee arrangement being established.

Section 962G Disclosure

4.3 We consider that there are a number of practical challenges with the prescriptive requirements for the content of the fee disclosure statement. This includes:

(a) where ongoing fees are based on a percentage of assets under management, it will be impossible to calculate the actual amount of fees paid for the preceding 12 months as the notice will be sent in month 10 or earlier;

(b) in the same way, it will not be possible to specify services that the client has actually received over the relevant period (12 months) as the first notice will be sent in month 10 or earlier;

(c) with regards to s962E(2)(c)-(f) it is unclear what level of "details" are intended to be provided to a client regarding the service agreed to be provided and those actually provided. Given the details of the service agreement will have been articulated at the commencement of the arrangement of ongoing fees, it is likely that the service promised will have been delivered as agreed. If Treasury intended to proceed with requiring information about the actual services provided, it should be made clear that details are not required and that it is only information or a high level description of the types of services which were actually received (as opposed to, for examples, itemised phone calls, emails and attendances with details about when they were received, what was discussed etc); and

(d) it is onerous and unlikely to be useful to specify in the notice, the services that the fee recipient anticipates that the client will receive during the next 12 months.

We recommend that:

- **The word 'details' appearing in s962E(2)(c) – (f) be amended to 'information'.**
- **s962E(2)(f) be deleted on the basis that the services to be provided as agreed in the ongoing fee arrangement will be the services the client is entitled to receive (as per s962E(2)(e).)**

5. Renewal mechanics

S962F and s962G: Fee Disclosure Statement and Renewal Notice provision

5.1 The current drafting requires that renewal notices be provided 'at least 30 days before' the second anniversary of the arrangement. In our view the drafting should provide reasonable flexibility to align the provision of renewal notices with fee disclosure statements. This is not currently achieved, as the trigger for renewal notices is tied to the date the arrangement was entered into, whereas the disclosure notice could be given after 10 months, which would then mean the 2nd year disclosure notice would be due 1 year and 10 months after the ongoing fee arrangement was entered into, but the renewal notice would be due 24 months after the ongoing fee arrangement was entered into.

Therefore, the FSC seeks an amendment to s962D and s962G to remove "at least 30 days before" and insert "at least annually" and "no less frequently than once in every period of two consecutive years", respectively, at the end of the sentence in those sections. We note that there will need to be some adjustment to S962J and K as a result to recognise that the key dates related to an anniversary of an ongoing fee arrangement being established.

5.2 The current drafting also creates a difficulty in that the renewal and notification period operate on a "hard" anniversary date (without reference to weekends or public holidays), while the disclosure statement must be sent at a different period (at least 30 days before that anniversary).

5.3 However, the disclosure statement is required to include information that covers the whole period up to the anniversary date (that is, the total fees paid in relation to the year leading up to that anniversary - 962E(2)(a)). We note that in many cases, the total to be paid for a year may not be certain 30 days before the year ends. The client might request an additional specifically remunerated service. Where the fees depend on the value of assets under management, that value could be subject to change. As drafted, it will not always be possible to prepare an accurate statement.

The FSC submits that Treasury either:

Require that the fee disclosure statement specify the amount paid to the date of the statement and a reasonable estimate of any further amount to become paid or payable in relation to the year; or

Require that the fee disclosure estimate specify the amount paid for the whole year, to be based on statutory assumptions about events between the statement date and the anniversary date (similar to the tolerances and assumptions under section 180 of the National Credit Code); or

Require that the fee disclosure statement specify the amount paid in relation to the 12 months immediately before the date that the statement is prepared.

If the first or second option is selected, Treasury might consider clarifying in the EM that at any annual review meeting, actual fees against the estimates previously provided could be disclosed.

"Give" or "Send"

5.4 The fee recipient must 'give' a fee disclosure statement (s962D) and must 'send' a renewal notice and fee disclosure statement (s962G). It is not clear why these are different and how the fee recipient is to discharge the obligation. Given the inability to charge fees if you have not given or sent the relevant notices, these obligations should be clarified so that fee recipients can easily discharge their obligations under the legislation. As the intention is to provide flexibility (and therefore lower the cost of this legal requirement for consumers) documents may be provided at a face to face meeting 'give' is appropriate, although fee recipients will not want to be unable to charge fees if a client has not notified of a change of address, and so it should also be appropriate to discharge the obligation by "sending" the notice to the last known address. A provision like s940C should be included in Pt7.7A or should also apply to that Part.

Opt-in in "writing"

5.5 The Minister, Treasury and ASIC have at numerous times stated that the client ought to be able to opt-in using a variety of 'recordable' means. Indeed the EM at paragraph 2.31 highlights that the opt-in 'can be administered flexibly' by a number of means and this objective is supported by the FSC.

5.6 However, to avoid any doubt in the mean of "writing".

The FSC submits that Treasury confirm that the current definition of "writing" in the Corporations Act is congruent with and enables opt-In to be facilitated by the methods of communication documented in EM paragraph 2.31. This should not preclude the use of any means, so long as the renewal can be recorded and verified (For example – a renewal obtained via a recorded telephone conversation should be permissible as this occurs in a range of client/adviser/product provider interactions at present.

5.7 Further, the opt-in obligation is an obligation to be borne by the fee recipient, that is the adviser, to enable an adviser to be remunerated as agreed in the "ongoing fee arrangement". The ability for an adviser to leverage a product provider's website to discharge the fee recipient's legal obligations should not transfer the obligation to the product provider.

5.8 The responsibility for ensuring that the adviser ceases charging the client a fee ultimately rests with the adviser's authorising licensee under section 1317E(jaaf). To recognise that the adviser and their authorising licensee are responsible for discharging the opt-in obligation it is important that the opt-out notification be provided to the fee recipient and not a financial product provider.

The FSC submits that paragraph 2.31 of the EM be revised so that the reference to the applicable website is that of the advice 'provider", that is, the 'fee recipient' and not the product provider and that the law reflect this obligation requirement.

'Grace period' for opting-in

5.9 We note that the current draft legislation affords the consumer a "grace period" for 'non-response'.

5.10 However, s962Keffectively 'opts-in' the client out of the advice arrangement by the end of the renewal period.

5.11 The duty as drafted also affords the consumer no 'continuation' provision should they have missed notifying the adviser of their intentions even by one day. Is it the intention that the adviser will have to proceed with the full termination administration and the full establishment of a new arrangement?

5.12 In previous discussions and as provided to Treasury in December 2010, the FSC recommended that consumers should be afforded one month following the anniversary date of the service agreement to respond to an opt-in request. The basis for this recommendation is that some consumers leave matters to the last minute, in fact beyond expiry dates (for example renewing their driver's license, updating their car insurance etc.), without consequences (for example, they are not required to re-sit a driver's test unless the lapse is significant).

The FSC recommends that if the client fails to respond within a consumer grace period of 30 days post the second anniversary date or renewal period, the client would be deemed to have not opted-in to continue the advice relationship.

This recommendation presents a reasonable and efficient consumer experience whilst still affording the greatest consumer protection, given the adviser is still required to provide services and is still bound by the best interest duty.

6. Termination

6.1 To provide greater clarity as to the ways in which an ongoing fee arrangement can be terminated, the FSC submits that the draft legislation be amended to refer specifically to termination which occurs when all services required to be provided under the arrangement have been provided.

The FSC recommends that in s 962 (1)(b) and (2)(b), the following words be added to the provision, immediately after "terminated for any reason".

"including as a consequence of the client having been provided with all of the services required to be provided to the client under the arrangement"

Optional Termination by Client

Under s962B and s962J the client has an immediate right to terminate an ongoing fee arrangement at any time. We have previously requested that at least a 30 day grace period be built into the termination (or such shorter notice period as agreed to by the client and fee recipient). This is to recognise that the fee recipient will need some period of notice to arrange the practical aspects of terminating the arrangement (e.g. notifying product providers to terminate payments).

We submit the following draft may address this concern.

962B(1) and s962J It is a condition of the ongoing fee arrangement that the client may terminate the arrangement at any time on the provision of at least 30 days notice, or such shorter notice period as agreed between the client and fee recipient.

Adviser 'grace' period (non-penalty period) to affect the termination of an ongoing fee arrangement

6.2 As previously submitted, we have also requested that the adviser should have one month from the date of the lapse of the client's grace period to affect the cessation of the collection of any fees in respect of that client.

6.3 Irrespective of whether the client opts-out of an ongoing fee arrangement through the operation of s962B, s962J or s962K, the adviser may be required to liaise with multiple product providers to ensure that ongoing fees deducted from financial products on behalf of the client cease.

6.4 This is likely to involve a degree of time and administration on behalf of both the product provider and the adviser and it is therefore highly unlikely that even the most diligent of advisers would be able to instantaneously "switch-off" an ongoing fee arrangement for a client.

6.5 An additional consideration is that product providers will often calculate and pay those fees on a monthly basis and existing systems and business processes may not today readily accommodate an ongoing fee arrangement that ceases intra-month.

Therefore we seek an amendment to s962K (or the inclusion of an additional provision) to clarify that the current fee recipient must take all reasonable steps to ensure that any fees payable pursuant to an ongoing fee arrangement that will be terminated pursuant to s962K cease to be paid as soon as reasonably practicable, and in any event, within 30 days of the termination of the arrangement in accordance with s962K.

7. Cure

7.1 The consequences are different under the regime if you fail to give a notice (can't charge fees), terminate pursuant to the express statutory right (obligation to repay fees charged after termination if client requests and cap on termination fees) or if you fail to opt-in or opt-out during the renewal period (can't charge fees and liable to pay pecuniary penalty). It is not clear why the consequences are different.

7.2 It is not clear under the draft legislation how you cure a breach. For example, if there has been a failure to provide a notice, it is not clear how you then reset the relationship so that you can start charging fees and providing services again. We request that the process to cure a breach is clarified.

8. Other suggestions

Transitional arrangements on the death of a client

8.1 It is not unusual for a single family member to enter into an advice relationship and for that adviser to address estate planning issues. The client may well indicate to family members that on the client's death, the family should contact the adviser for assistance. To avoid disruption to those arrangements when the client dies, we submit that the law should allow a short term transitional period, during which time the estate of the deceased client and other family members, such as the spouse and any dependants, can be treated as falling within the ongoing fee arrangement established by the deceased client. Otherwise, an adviser may be prevented from assisting family members on the death of the client unless those family members enter into a new ongoing fee arrangement. This seems harsh in the circumstances and is likely to be contrary to the wishes of the client. A period of six months is recommended in the following as this is consistent with the processing of estates (to probate for example).

To address this, the FSC recommends the inclusion of a new interpretation provision in s962 along the following lines:

"(6) For the purposes of this Division, if a client who is a natural person dies, the client's estate and any dependants of the client are taken to be the client during a period of [6] months following the death of the client."

ASIC Powers

1.1 This new draft provision gives ASIC a significantly expanded power to vary or suspend an existing AFS licence, which is of concern due to its extreme breadth. It is arguable that every AFSL holder is likely to contravene a financial services law or the other obligations imposed under section 912A at some point.

1.2 In addition, individuals and licensees may from time to time be in non-compliance with their obligations under the financial services law and the general licensee obligations. The current scheme relating to breach reporting attaches a materiality test and similar principles ought to apply in relation to the extensions to ASIC's banning and licensing powers, ensuring that licensees in particular are not subject to licence revocations if ASIC is not of the view that the licensee will be in material or continuing breach of its obligations. ASIC is also required to have regard to certain matters when it is considering whether a person is not of good fame or character.

The FSC submits that some objective criteria apply to the exercise of ASIC's discretion when it is considering the cancellation or suspension of an AFSL.

These criteria should require ASIC to consider factors such seriousness of past or likely breaches, the number of clients likely to be affected, likely financial loss to clients arising from such a contravention, the impact on the person's ability to provide financial services, and whether the person took or is taking all reasonable steps to avoid the breach.

Given the widening of ASIC's powers, the legislative scheme should ensure that all decisions involving the exercise of those powers should be made after affording affected individuals or licensees an opportunity to appear at a hearing and to make submissions to ASIC, and all decisions should be reviewable by the AAT and Federal Court.