SUBMISSION IN RELATION TO THE PROPOSED FOFA CHANGES

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I wish to submit that the proposed changes to the *Corporations Regulations 2001* (the Principal Regulations), in particular the amendments which relate to the Future of Financial Advice (FOFA) provisions in Part 7.7A of the Act, are not in the public interest, destroy the trust between investors and financial advisers, are opposed by significant stakeholders and analysts, are contrary to research findings and leaves the government open to charges of being morally a contributor to investors' losses when advised by an adviser.

I will not call the proposed changes a reform because reform means an improvement or amendment of what is wrong, corrupt, unsatisfactory, etc, and these proposed changes are not an improvement.

I retired 10 years ago and actively manage the my wife and my pension fund held in an APRA approved and bank owned investment vehicle. Our combined pension is now in the top 10% of value of all investors in this very large platform which has millions of pensioner investors. I am well educated with a B.Ec and MBA as well us holding many other qualifications. I have a real interest in managing our finances as well as possible and take an active interest in the market. I have had the same financial adviser since 1998 – 16 years – but do not pay for his advice, as we feel capable of making all our own decisions. We recognise that we are very fortunate to be able to do this.

These are the five issues I wish the government to consider before making the proposed changes:

1) FOFA REFORMS BENEFIT SECTIONAL INTERESTS NOT THE PUBLIC INTEREST

The primary beneficiaries of the proposed FOFA "reforms" are Australia's banks and large financial institutions which dominate the financial services sector. The Explanatory Statement for the reforms issued by the authority of the Assistant Treasurer states that one of the benefits of these "reforms" will result in "direct ongoing cost savings of approximately $190 million per year; one-off implementation cost savings are approximately $90 million" for the financial services industry.

However these "reforms" will come at a major cost to investors, people who have superannuation accounts and pensioners. These are not reforms which will benefit the public interest. They only benefit financial advisers by making the client information collection and financial advice process simpler. It is highly unlikely that consumers will "gain access to more affordable and accessible financial advice as lower costs to industry are passed through to consumers" (Explanatory Statement, p.11). I believe banks and large financial institutions will maintain approximately the same fee structure and argue that other factors justify this. If the government is convinced that these institutions will lower their fees, where is the research to support this claim?

Ross Garnaut in his book *Dog Days: Australia After the Boom,* sets out the policy dangers in meeting only the demands of politically active vested interests at the expense of the public interest, and these changes fall fully into this category.

2) THE TRUST RELATIONSHIP BETWEEN INVESTORS AND FINANCIAL ADVISERS WILL BE BROKEN

The difference between holistic and scaled advice as set out in the Draft Explanatory Memorandum, page 14 is potentially very confusing for both investors and financial advisers. It should be remembered that the initial FOFA reforms were designed to improve the quality of financial advice while building trust and confidence in the financial advice industry. It is astounding that the Draft Explanatory Memorandum never addresses trust in its 37 pages.

A metaphor for these proposed changes is that if you wish to build an extension to your house and employ an architect to design it, then the architect has only to ensure the integrity of the extension itself but pay no attention to how the extension integrates with the rest of the house. In the financial advice framework, this could lead to impossible situations and total confusion.

3) OPPOSITION FROM MANY STAKEHOLDERS AND ANALYSTS

Peter Collins, former Liberal Premier of NSW, has been a Director of the leading Industry Superannuation fund HOSTPLUS since 2006 as well as having extensive experience in the financial sector has expressed astonishment at the proposed changes to FOFA.

Alan Kohler, ABC financial presenter and managing director of Business Spectator, has written an article in the Business Spectator on Monday 10 Feburary 2014, about the reforms. The article is titled, *The swinging pendulums of IR and financial advice.* He states:

> "… One of the regulations being repealed is known as 'little g' – the catch-all provision in the part of the FoFA (Future of Financial Advice) reforms that requires advisers to act in the best interests of their clients.
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> The section lists six things that a provider has to do to satisfy the requirement to act in the best of interests of the client, and then adds a seventh - s961B(2)(g), aka little g – that says: "(take) any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interests of the client, given the client's relevant circumstances".
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> Assistant Treasurer Arthur Sinodinos says that it is being removed because advisers say it leaves them "uncertain as to whether they have satisfied the best interests duty".
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> Well, in my view he would be better off getting rid of (a) through (f) and leaving (g). Any adviser who complains about (g) and not about the six other regulations doesn't really want to act in the best interests of their clients – they just want to have a paper trail that shows he or she ticked the right boxes."

Alan Kohler is correct in zeroing in on the problem of financial advisers no longer having to act in the client's best interests, should the repeal of the regulation take effect.

John Collett is an experienced financial writer for The Sydney Morning Herald. He has pointed out in a number of articles the faults with these proposed changes.

Lenore Taylor, political editor for The Guardian, Australia, wrote in an article on the 16th February 2014, "The Abbott government's strategy to avoid parliamentary scrutiny of its plan to unwind new protections for consumers receiving financial advice by implementing it through regulation could backfire because the regulations may be found to be invalid, leaving financial advisers open to legal class actions." This additional complication in the implementation of these changes would be extremely detrimental to certainty in the financial services industry.

4) THE PROPOSED CHANGES ARE CONTRARY TO RESEARCH FINDINGS OF THE AUSTRALIAN FINANCIAL SERVICES INDUSTRY

The excellent research by ASIC outlined the problems of ordinary investors dealing with the complexity of financial products. The proposed changes only increase the complexity in obscure and opaque ways. Please refer to this reference: Australian Securities and Investment Commission (ASIC). 2012. Shadow shopping study of retirement advice, Report 279, Sydney. http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/rep279-published-27-March-2012.pdf/$file/rep279-published-27-March-2012.pdf.

Recent research by Agnew, Bateman, Eckert, Ishhakov, Louviere and Thorp, *Individual Judgement and Trust Formation: An Experimental Investigation of Online Financial Advice*, Draft 5 January 2014, states:

> "Our experiment produced several interesting results. First, most individuals did well at separating good advice from bad advice. However, what was noteworthy was that respondents found that for some topics it was significantly more difficult to discriminate on advice quality than for others, particularly topics related to stock diversification and index fund fees. We referred to these topics as 'hard' topics, and paying down debt and consolidating retirement accounts as 'easy' topics. Categorizing our advice topics into these two groups proved valuable for our subsequent analysis of persistency and evaluation of advisers.
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> Second, we found individuals rely on extraneous signals to judge advice quality; for example, respondents preferred younger advisers. Advisers with certifications were also chosen more often. Respondent characteristics also mattered, specifically older, more numerate individuals, and those who had made good decisions in the past were more likely to choose 'good' advice.
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> Third, individuals demonstrated a degree of persistency in their choice of an adviser to follow, suggesting some clients may stay with advisers even when the quality of advice is not always good.
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> Fourth, as mentioned earlier, we found an important interplay between the quality of advice, the difficulty of the advice topic, and the order the advice topics were presented…. We found that advisers who could establish their trustworthiness early on an easy topic by providing good advice were still trusted after giving wrong advice on hard topics, and vice versa."

The implications of both of these pieces of research do not appear to have been considered by the government in proposing the changes to FOFA.

5) THE CHANGES WILL MAKE THE FEDERAL GOVERNMENT A CONTRIBUTING PARTY TO INVESTORS' LOSSES WHEN ADVISED TO MAKE INVESTMENT CHOICES BY A FINANCIAL ADVISER

The proposed changes will make the Federal Government morally a contributing party to investors' losses. This is caused by the government creating a framework of diminished responsibility for the financial adviser. No doubt in the next major financial collapse, eg. Storm Financial, these issues will be raised in courts and Senate Select Committee hearings.