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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

CORPORATIONS AMENDMENT (STREAMLINING OF FUTURE OF FINANCIAL ADVICE) BILL 2014

DRAFT EXPLANATORY MEMORANDUM

Consultation Draft

Table of contents

Consultation Draft

Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

Abbreviation	***Definition***
ADI	Authorised Deposit-taking institution
ASIC	Australian Securities and Investments Commission
Bill	Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014
Corporations Act	*Corporations Act 2001*
Corporations Regulations	*Corporations Regulations 2001*
Dissenting Report	*Dissenting Report by Coalition members of the Parliamentary Joint Committee on Corporations and Financial Services inquiry into the FOFA Bills*
FOFA	Future of Financial Advice
FOFA Bills	Corporations Amendment (Future of Financial Advice) Bill 2012 and the Corporations Amendment (Further Future of Financial Advice Measures) Bill 2012
FOFA legislation	Part 7.7A of the *Corporations Act 2001*, as introduced by the *Corporations Amendment (Future of Financial Advice) Act 2012* and the *Corporations Amendment (Further Future of Financial Advice Measures) Act 2012*
Licence	Australian financial services license
Licensee	Holder of an Australian Financial Services License
Representative	Representative of an Australian financial services licensee
SIS Act	*Superannuation Industry (Supervision) Act 1993*

Consultation Draft

General outline and financial impact

Outline

The initial Future of Financial Advice (FOFA) reforms, which were aimed at providing better protection for consumers of financial products and services, were announced by the former Government in April 2010.

This was in response to the 2009 *Inquiry into Financial Products and Services in Australia by the Parliamentary Joint Committee on Corporations and Financial Services* (PJC Inquiry), which considered a variety of issues associated with corporate collapses, including Storm Financial and Opes Prime.

The underlying objective of the initial reforms was to improve the quality of financial advice while building trust and confidence in the financial advice industry.

When the FOFA Bills were introduced into Parliament, they were referred to the Parliamentary Joint Committee on Corporations and Financial Services.

The Committee delivered its report on the FOFA Bills in February 2012, which included a *Dissenting Report by Coalition members of the Parliamentary Joint Committee* (Dissenting Report)[1]. The Dissenting Report put forward 16 recommendations for changes to FOFA, reflecting the Coalition's concerns that the FOFA Bills were too complex, costly to implement and created unnecessary red tape.

Following passage of the FOFA legislation, the rules became optional for financial advisers from 1 July 2012, and mandatory from 1 July 2013.

In July 2013, the Coalition released its *Policy to Boost Productivity and Reduce Regulation*, in which it committed to reduce compliance costs for small business, financial advisers and consumers who access financial

1 http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Completed_inquiries/2010-13/future_fin_advice/report/index

Consultation Draft

advice, by implementing the recommendations from the Dissenting Report.

On 20 December 2013, the Assistant Treasurer, Senator the Hon Arthur Sinodinos AO, announced amendments to the FOFA legislation. The amendments implement the Government's election commitment to reduce compliance costs for the financial services industry. Specifically, the Government committed to implement the recommendations of its Dissenting Report, as well as make other changes to reduce compliance costs for the industry.

The Bill includes the following key amendments to the FOFA legislation:

- removing the need for clients to renew their ongoing fee arrangement with their adviser every two years (also known as the 'opt-in' requirement);
- making the requirement for advisers to provide a fee disclosure statement only applicable to clients who entered into their arrangement after 1 July 2013;
- removing paragraph 961B(2)(g), the 'catch-all' provision, from the list of steps an advice provider may take in order to satisfy the best interests obligation;
- better facilitating the provision of scaled advice; and
- exempting from the ban on conflicted remuneration, benefits relating to general advice.

The Government's approach is that time sensitive FOFA amendments will be dealt with through regulations, to the extent allowed under the relevant regulation-making powers, and then locked into legislation.

Consequently, the removal of the opt-in requirement, changes to fee disclosure statements, removal of the 'catch-all' provisions under the best interests obligation, the facilitation of the provision of scaled advice and the clarification of the meaning of 'intra-fund' advice will all be implemented via regulation, and subsequently repealed once this measure receives Royal Assent. The changes to the ban on conflicted remuneration will also be implemented via regulation; however some changes will not be subsequently locked into legislation, such as the stockbroking-related exemptions and the grandfathering arrangements for the ban.

Until the amendments are in place, and consistent with ASIC's stance during the introduction of other major policy reforms, ASIC announced

Consultation Draft

on 20 December 2013[2] that they are taking a facilitative approach to the FOFA reforms until mid-2014.

In light of this approach, ASIC will not take enforcement action in relation to the specific FOFA provisions that the Government is planning to repeal. For example, ASIC will not take action for breaches of the section which requires fee disclosure statements to be provided to retail clients with ongoing fee arrangements entered into before 1 July 2013.

However, ASIC's stance does not remove a client's right to take private action against a provider in the event they feel they are disadvantaged.

Date of effect: The amendments commence upon the day after this Act receives the Royal Assent.

The removal of the 'opt-in' requirement applies in relation to an ongoing fee arrangement for those renewal notice days for the arrangement that occur on or after the day after Royal Assent.

The changes to fee disclosure statements apply in relation to an ongoing fee arrangement for those disclosure days for the arrangement that occur on or after the day after Royal Assent.

The removal of the 'catch-all' provision, and the changes to the operation of scaled advice apply to personal advice provided on or after the day after Royal Assent.

The exemption of general advice from the ban on conflicted remuneration, and the changes to the ban on volume-based shelf-space fees apply to benefits given on or after the day after Royal Assent, that are not otherwise grandfathered.

Proposal announced: The amendments to FOFA were announced on 20 December 2013 by the Assistant Treasurer, Senator the Hon Arthur Sinodinos AO.

Financial impact: This Bill has no significant financial impact on Commonwealth expenditure or revenue.

Compliance cost impact: The amendments have no compliance cost impact; they are deregulatory in nature.

Consultation Draft

[2] ASIC 13-355MR

Regulation impact statement

An options-stage regulation impact statement (RIS) for the amendments to FOFA has been prepared. A summary of the RIS can be found in Chapter 4.

The options-stage RIS is largely used to inform the consultation process. The information gathered through consultations will be used to refine the RIS into a final details-stage RIS, which will be completed prior to the finalisation of legislation.

Consultation Draft

Chapter 1
Best interests obligation

Outline of chapter

1.1 Schedule 1 to the Bill amends the Corporations Act to remove the 'catch-all' provision from the list of steps an advice provider may take in order to satisfy the best interests duty, and to better facilitate the provision of scaled advice.

Context of amendments

1.2 The Government has committed to reduce compliance costs for small business, financial advisers and consumers who access financial advice. See Outline for further information.

Removal of the catch-all provision

1.3 The existing law requires advice providers to act in their client's best interests when providing personal advice. Subsection 961B(2) of Corporations Act lists a number of steps that an adviser may take in order to satisfy the best interests duty (commonly referred to as the 'safe harbour'). It consists of seven parts including a 'catch-all' provision, which states that a provider must prove that they have "taken any other step [in addition to the six preceding ones] that … would reasonably be regarded as being in the best interest of the client".

1.4 The Government has committed to removing the catch-all provision. This amendment addresses concerns that the catch-all provision creates significant legal uncertainty and renders the safe harbour unworkable for providers due to its open-ended nature.

Facilitating scaled advice

1.5 The existing best interests duty requires that advice providers make investigations into their client's broader objectives, financial situations and needs before providing scaled advice. Further, there is uncertainty on whether the client and provider can agree on the scope of the advice to be provided.

Consultation Draft

1.6 The Government has committed to amend the legislation to better facilitate the provision of scaled advice to reduce uncertainty and enable cost-effective scaled advice to be provided to consumers.

Reduced best interests obligation

1.7 The existing law allows some providers to satisfy a reduced best interests duty when a client has sought advice on a basic banking product or a general insurance product.

1.8 The Government has committed to reduce unnecessary complexity and will amend the obligations to reflect the intended, and current, operation of the law.

Summary of new law

1.9 The Bill amends the best interests duty in section 961B of the Corporations Act to:

- remove the catch-all provision, so that advisers need only satisfy the remaining six parts of the safe harbour;
- better facilitate scaled advice by limiting the scope of investigations and explicitly allowing clients and advisers to agree on the scope of any scaled advice provided; and
- clarify the circumstances when an agent or employee of an ADI may access the reduced best interests duty.

Comparison of key features of new law and current law

New law	*Current law*
There is no requirement for providers to satisfy the 'catch-all' provision in order to discharge their duty.	In order to satisfy the best interests duty, providers must be able to prove that they have "taken any other step [in addition to the six preceding ones in the safe harbour] that … would reasonably be regarded as being in the best interest of the client" (that is, the 'catch-all' provision).
Providers need only investigate the client's objectives, financial situation and needs that are relevant to the	Providers are required to undertake a fulsome investigation into the client's objectives, financial situation and

Consultation Draft

scaled advice to be provided. Clients and advisers are explicitly permitted to agree on the scope of any scaled advice provided.	needs before any scaled advice can be provided. Further, there is uncertainty on whether clients and advisers can agree on the scope of the advice to be provided.
An agent or employee of an ADI need not satisfy the steps in 961B(2)(d) to (f) in relation to personal advice on a basic banking or general insurance product when the subject matter sought by the client relates to a basic banking product, general insurance product, consumer credit insurance product, or a combination of these products. It remains the case that a provider need not satisfy paragraphs 961B(2)(d) to (f) to the extent that the subject matter of the advice relates to a general insurance product.	An agent or employee of an ADI is currently not required to satisfy the steps in paragraphs 961B(2)(d) to (g) when the subject matter of the advice sought by the client is solely in relation to a basic banking product. Further, a provider need not satisfy those steps when the subject matter of the advice sought by the client is solely in relation to a general insurance product. The Corporations Regulations provide that an agent or employee of an ADI need not satisfy the steps in 961B(2)(d) to (g) when the only personal advice provided is in relation to a basic banking product and a general insurance product. Further, that a provider need not satisfy paragraphs 961B(2)(d) to (g) to the extent that the subject matter of the advice relates to a general insurance product.

Detailed explanation of new law

Remove the 'catch-all' provision

1.10 Subsection 961B(2) of the Corporations Act provides seven steps that the provider may take to satisfy the best interests duty. This is commonly referred to as the 'safe harbour'.

1.11 Paragraph 961B(2)(g), the 'catch-all' provision, is the last of the seven steps. It states that a provider must be able to prove that they have "taken any other step [in addition to the six preceding ones] that, at the time the advice is provided, would reasonably be regarded as being in the best interest of the client, given the client's relevant circumstances".

1.12 The new law removes the catch-all provision. The new law also removes section 961E, which supplemented the catch-all provision.

Consultation Draft

1.13 Under the new law, providers will be required to satisfy the remaining six steps of the safe harbour in order to discharge their duty to their client. ***[Schedule 1, items 12, 13 and 17, section 961E and subsections 961B(2)(f) and 961B(2)(g)]***

1.14 Paragraph 1.20 below details how an adviser can use the safe harbour to satisfy the best interests duty under the new law.

Facilitating scaled advice

1.15 This measure will amend the best interests obligation to better facilitate the provision of low-cost scaled advice. Further, it will clarify that a provider of advice and a client may to agree on the scope of advice to be provided.

1.16 Scaled advice is advice about a specific area of a client's needs, such as insurance or superannuation. This contrasts 'holistic advice' which is another advice model offered by providers. Under the holistic model, a provider makes extensive enquiries about their client's circumstances, needs and objectives and provides advice to their client on all aspects of their financial circumstances in a full financial plan.

1.17 Given that scaled advice is about a specific issue or issues, it is often cheaper than traditional holistic advice and, as a result, enables many consumers to access advice that they could otherwise not afford.

1.18 It follows that, because the scope of advice is limited under a scaled advice model, the investigations required to be undertaken by an advice provider in order to provide scaled advice be also limited to what is relevant to providing advice that is in the client's best interests on the particular issue or issues.

1.19 A provider and their client will discuss the scope of any scaled advice to be sought by the client as part of their initial discussion. This discussion may occur at the same time the client discloses some preliminary information to the provider on their objectives, financial situation and needs, but before the provider commences their investigation into the client's relevant circumstances in order to formulate the advice.

1.20 Subsection 961B(2) of the Corporations Act provides a number of steps a provider may take in order to satisfy the best interests obligation. The steps that a provider may take in order to satisfy the best interests obligation will now be:

- identify the subject matter of the advice sought by the client (the current subparagraph 961B(2)(b)(i));

Consultation Draft

- identify the objectives, financial situation and needs of the client that would reasonably be considered relevant in providing the advice sought by the client (the current subparagraph 961B(2)(b)(ii));

- identify the objectives, financial situation and needs of the client that the client discloses to the provider (the new paragraph 961B(2)(ba));

- make reasonable inquiries to obtain complete and accurate information where the information disclosed by the client does not satisfy the circumstances that the provider identified under subparagraph 961B(2)(ii) as relevant in providing the advice sought by the client (the current paragraph 961B(2)(c));

- assess whether the provider has the expertise required to provide the advice sought by the client, and if not, decline to provide the advice (the current paragraph 961B(2)(d);

- if it is reasonable to consider recommending a financial product in response to the advice sought, the provider must conduct reasonable investigations into the financial products that may achieve the client's objectives and meet their needs, and assess the information gathered in the investigation (the current paragraph 961B(2)(e)); and

- in providing the advice, base all judgements on the client's circumstances that are relevant to the advice sought (the current paragraph 961B(2)(f)).

[Schedule 1, items 10, 11 and 14, paragraphs 961B(2)(a) and (ba) and subsection 961B(2) (note)]

1.21 For the avoidance of doubt, a new subsection 961B(4A) is inserted to clarify that nothing in subsection 961B(2) prevents a client agreeing the subject matter of the advice sought with the provider. ***[Schedule 1, item 16, subsections 961B(4A)]***

Reduced best interests obligation

1.22 This measure will provide clarity on the operation of the law and broaden the circumstances in which an agent or employee of an ADI can access a reduced best interests obligation in relation to advice provided on a basic banking product or general insurance product.

Consultation Draft

1.23 Under subsection 961B(3), an agent or employee of an ADI is not required to satisfy the steps in paragraphs 961B(2)(d) to (g) when the subject matter of the advice sought by the client is solely in relation to a basic banking product. Subsection 961B(4) further provides that a provider need not satisfy those steps when the subject matter of the advice sought by the client is solely in relation to a general insurance product.

1.24 The Corporations Regulations provide that an agent or employee of an ADI need not satisfy the steps in 961B(2)(d) to (g) when the only personal advice provided is in relation to a basic banking product and a general insurance product. Further, that a provider need not satisfy paragraphs 961B(2)(d) to (g) to the extent that the subject matter of the advice relates to a general insurance product.

1.25 The new law provides that an agent or employee of an ADI need not satisfy the steps in 961B(2)(d) to (f) in relation to personal advice on a basic banking or general insurance product where the subject matter sought by the client relates to a basic banking product, general insurance product, consumer credit insurance product, or a combination of these products. ***[Schedule 1, item 15, subsection 961B(3)]***

1.26 Further, subsection 961B(4) is amended to clarify in the legislation that that a provider need not satisfy paragraphs 961B(2)(d) to (f) to the extent that the subject matter of the advice relates to a general insurance product. ***[Schedule 1, item 15, subsection 961B(4)]***

Application and transitional provisions

1.27 The amendments to the best interests obligation apply in relation to the provision of personal advice to a retail client on or after the commencement day. The amendments commence the day after Royal Assent. ***[Schedule 1, items 42, 43 and 44, sections 1531A and 1531B]***

1.28 The current requirements will continue to apply until the new law is in place or new regulations are made.

Consultation Draft

Chapter 2
Ongoing fee arrangements

Outline of chapter

2.1 Schedule 1 to this Bill reforms the requirements introduced under the FOFA reforms in Chapter 7 of the *Corporations Act 2001* to:

- remove the renewal notice obligation for fee recipients; and
- make the requirement for advisers to provide a fee disclosure statement only applicable to clients who entered into their arrangement after 1 July 2013.

Context of amendments

2.2 The Government has committed to reduce compliance costs for small business, financial advisers and consumers who access financial advice. See Outline for further information.

Removal of the 'opt-in' requirement

2.3 The current law provides that advisers who have an ongoing fee arrangement with a retail client must obtain their client's agreement at least every two years to continue the ongoing fee arrangement, for new clients whose ongoing fee arrangement commenced after 1 July 2013. If, after receiving the renewal notice, the client decides not to renew or fails to respond to the fee recipient's renewal notice, the ongoing fee arrangement terminates.

2.4 The Government has committed to remove the requirement for advisers to obtain their client's approval at least every two years in order to continue an ongoing fee arrangement (known as the 'opt-in' requirement) on the basis that it would unnecessarily increase costs, red tape and uncertainty for both consumers and businesses.

Changes to fee disclosure statements

2.5 The current law provides that advisers must give all retail clients who have an ongoing fee arrangement a fee disclosure statement which

Consultation Draft

shows the fees paid by the client, the services the client received, and the services the client was entitled to receive, in the previous 12 months.

2.6 The Government has committed to making the annual fee disclosure statements prospective only. In other words, a fee disclosure statement will only need to be sent to clients charged an ongoing fee during a period of 12 months or more who entered into the arrangement after 1 July 2013. It will not be required for arrangements entered into prior to 1 July 2013.

2.7 This is on the basis that retrospectively applying the annual fee disclosure statement imposes large costs on industry and the consumer, with minimal benefit.

Clarification of what is intrafund advice

2.8 The Government has committed to clarifying the treatment of advice provided within superannuation by clarifying the term ***intrafund advice*** in the FOFA legislation.

Summary of new law

2.9 Where an ongoing financial advice relationship exists between an adviser (the 'fee recipient') and a retail client which involves the charging of an ongoing advice fee (however described), the adviser will no longer be required to:

- provide a renewal notice for fee recipients; and
- provide a fee disclosure statement to clients who entered into their ongoing fee arrangement before 1 July 2013.

2.10 Advisers still need to provide an annual fee disclosure statement to all other clients (i.e. post-1 July 2013 clients).

2.11 The new law also clarifies the term ***intrafund advice***.

Comparison of key features of new law and current law

New law	*Current law*
No requirement to obtain a client's agreement to charge an ongoing fee. Any ongoing fee arrangement	Advisers who have an ongoing fee arrangement with a retail client must obtain their client's agreement at least

Consultation Draft

continues to exist unless the arrangement is terminated by either the client or the adviser.	every two years to continue the ongoing fee arrangement, for new clients who enter into an ongoing fee arrangement from 1 July 2013.
Advisers who have an ongoing fee arrangement with a client must give retail clients who entered into the arrangement after 1 July 2013 a fee disclosure statement which shows the fees paid by the client, the services the client received, and the services the client was entitled to receive, in the previous 12 months.	Advisers who have an ongoing fee arrangement with a client must give *all* retail clients a fee disclosure statement which shows the fees paid by the client, the services the client received, and the services the client was entitled to receive, in the previous 12 months.
A note clarifies the link between the term 'intrafund advice' and the relevant subject rules under section 99F of the SIS Act.	The term 'intrafund advice' is not expressly referred to.

Detailed explanation of new law

Removal of the renewal notice 'opt-in' requirement

2.12 Under the current law, where an ongoing financial advice relationship exists between an adviser (the 'fee recipient') and a retail client which involves the charging of an ongoing advice fee, the fee recipient is required to obtain their client's agreement at least every two years to continue the ongoing fee arrangement by way of a renewal notice, for clients who entered into an ongoing fee arrangement after 1 July 2013.

2.13 An ongoing fee arrangement exists where a retail client is given personal advice and charged an ongoing fee during a period of more than 12 months.

2.14 The renewal notice is required to contain information indicating that the client may renew the ongoing fee arrangement, as well as information setting out what will happen if the client elects not to renew the arrangement, or if they do not respond to the renewal notice, in particular, that the arrangement (including the provision of advice and the ongoing fee) will terminate.

2.15 The renewal notice must to be sent to the client within 30 days of the end of the two-year period. The client then has 30 days to agree to renew the arrangement.

2.16 If, after receiving the renewal notice, the client decides not to renew or fails to respond to the fee recipient's renewal notice, the ongoing

Consultation Draft

fee arrangement terminates. This means that the fee recipient is not obligated to provide ongoing financial advice to the client, and the client is not obligated to continue paying the ongoing fee.

2.17 The current law provides that licensees or representatives may be exempted from the renewal notice obligation by ASIC if they are bound by an approved code of conduct.

2.18 The new law removes the obligation for an adviser to provide a renewal notice to a client. ***[Schedule 1, items 5-7 and 18-22, Subdivision B of Division 3 of Part 7.7A (heading), sections 960, 962CA, 962K, 962L, 962M and 962N and subsections 962F(1), (2) and (3)]***

2.19 Therefore, under the new law, an 'opt-out' system applies where any ongoing fee arrangement continues to exist unless the arrangement is terminated by either the client or the adviser.

Changes to fee disclosure statements

2.20 Under the current law, where an ongoing financial advice relationship exists between an adviser (the 'fee recipient') and a retail client which involves the charging of an ongoing advice fee (a fee for a period longer than 12 months), the fee recipient is required to give all retail clients a fee disclosure statement which shows the fees paid by the client, the services the client received, and the services the client was entitled to receive, in the previous 12 months.

2.21 The fee disclosure statement must be provided before the end of a period of 30 days beginning on the 12 month anniversary of the day the arrangement was entered into, or, if a fee disclosure statement has been given to the client since the arrangement was entered into, before the end of a period of 30 days beginning on the 12 month anniversary of the day immediately after final day of the year for which disclosure was provided in the last fee disclosure statement.

2.22 The new law removes the requirement to provide a yearly fee disclosure statement to clients who entered into their ongoing arrangement prior to 1 July 2013, restricting the requirement for advisers to provide a fee disclosure statement to clients who entered into their ongoing arrangement after 1 July 2013. ***[Schedule 1, items 23, 40 and 41, Subdivision C of Division 3 of Part 7.7A, table item 22 of subsection 1317E(1) and subparagraph 1317G(1E)(b)(v)]***

2.23 The obligations for providing a fee disclosure statement to post-1 July 2013 clients set out in Subdivision B of the *Corporations Act 2001* will remain unchanged.

Consultation Draft

2.24 The result is that the obligation to provide a fee disclosure statement applies to advisers ('fee recipients') in situations where they:

- provide personal advice to a retail client; and
- the client is charged an ongoing fee during a period of 12 months or more; and
- the arrangement was entered into after 1 July 2013.

2.25 Provisions in Chapter 7 of the Corporations Act which support the fee disclosure statements to post-July 2013 customers (such as those outlining what information must be included in the fee disclosure statement, and what happens when the fee recipient does not comply with the requirement to provide a fee disclosure statement within the specified time) will remain unchanged.

Definition of intrafund advice

2.26 The new law inserts a note clarifying the term ***intrafund advice*** into section 960, which defines the key terms used in Part 7.7A of the Corporations Act. ***[Schedule 1, item 9, section 960]***

2.27 Under the current law, the term intrafund advice is not expressly used.

2.28 The term intrafund advice is commonly used to describe financial product advice given by a trustee of a regulated superannuation fund to its members.

2.29 The note links the commonly used term with the rules under section 99F of the SIS Act, which deal with the subject area.

Application and transitional provisions

Removal of opt-in requirement

2.30 The removal of the 'opt-in' requirement applies in relation to ongoing fee arrangements with renewal notice days (the renewal notice day being either the second anniversary of the day on which the arrangement was entered into or, if the arrangement had previously been renewed, the second anniversary of the last day on which the arrangement was renewed) that occur on or after the day after Royal Assent. ***[Schedule 1, items 42, 43 and 44, sections 1531A and 1531C]***

Consultation Draft

2.31 The current renewal notice obligations compulsorily apply to clients who entered into an ongoing fee arrangement after 1 July 2013. Fee renewal notices will become due within 30 days of 1 July 2015. As such, no renewal notice days will occur prior to the removal of the 'opt-in' provision.

2.32 However, FOFA was optional from 1 July 2012. For those fee recipients who chose to comply with FOFA early, the renewal notice obligations apply to clients who entered into an ongoing fee arrangement after the fee recipient's opt-in date. As such, fee renewal notices could become due earlier than 1 July 2015 for these fee recipients.

2.33 The removal of the 'opt-in' provisions will apply from the earlier of the day after the regulations are registered, or the time outlined in paragraph 2.30 above.

Limitation of fee disclosure statement

2.34 The removal of the requirement to provide a fee disclosure statement to clients who entered into their ongoing fee arrangement before 1 July 2013 applies in relation to an ongoing fee arrangement for those disclosure days for the arrangement that occur on or after the day after Royal Assent. ***[Schedule 1, items 42, 43 and 44, sections 1531A and 1531D]***

2.35 The current requirement to provide clients with a fee disclosure statement will continue to apply until the new law is in place or new regulations are made.

Consultation Draft

Chapter 3
Conflicted remuneration and other banned remuneration

Outline of chapter

3.1 Schedule 1 to the Bill amends the Corporations Act to provide exemptions in relation to the payment and receipt of remuneration that is banned under the current law.

Context of amendments

3.2 The Government has committed to reduce compliance costs for small business, financial advisers and consumers who access financial advice. See Outline for further information.

General advice

3.3 Under the current law, remuneration (both monetary and non-monetary) received in relation to the provision of personal (financial product advice that takes into account the client's objectives, financial situation and needs) and general advice (financial product advice that does not take into account the client's objectives, financial situation and needs) is captured by the ban on conflicted remuneration.

3.4 The Government has committed to exempt general advice from the ban on conflicted remuneration. The Government considers that the application of the ban on conflicted remuneration risks limiting the availability of general advice and unnecessarily burdens industry by capturing staff not directly involved in providing advice to clients.

Exemption for life risk insurance benefits

3.5 Under the current law, monetary benefits paid to licensees, or representatives, in relation to life risk insurance offered outside of superannuation are exempt from the ban on conflicted remuneration. However, benefits paid in relation to life risk insurance offered inside superannuation are predominantly banned, including in circumstances

Consultation Draft

where advice has been provided to members on their life risk insurance coverage.

3.6 The Government has committed to minimise the market distortions and cost impacts that may result from the differing treatments of these benefits inside and outside of superannuation by broadening the exemptions provided for benefits paid in relation to life risk insurance offered inside superannuation.

Execution-only exemption

3.7 Under the current law, benefits paid for execution-only services (in respect of the issue or sale of a financial product) are exempt from the ban on conflicted remuneration except where a person within the licensee group (of the person receiving the benefit) has provided advice on that product, or class of product to the client in the previous 12 months.

3.8 The Government has committed to clarify the exemption so that execution-only benefits are exempted except in circumstances where advice on that class of product has been provided to the client in the previous 12 months by the individual receiving the benefit. The Government considers that this will reduce unnecessary administrative complexity and ensure that legitimate execution-only services can be provided.

Education and training exemption

3.9 Under the current law, the education and training exemption provides an exemption from the ban on conflicted remuneration for education and training relating to the provision of financial product advice.

3.10 In order to facilitate industry attempts to up-skill, the Government has committed to broaden the exemption to include training that relates to conducting a financial services business more broadly.

Basic banking exemption

3.11 Under the current law, a benefit is exempt from the ban on conflicted remuneration if the benefit relates to a basic banking product and the agent or employee of an ADI, at the time of providing advice on the basic banking product, does not provide financial product advice on any other financial product except a general insurance product.

3.12 The Government has committed to broaden the circumstances when an agent or employee of an ADI can access the basic banking

Consultation Draft

exemption to where the agent or employee also provides financial product advice on other simple ('Tier 2') financial products at the same time as advice on a basic banking product. The objective is to provide an exemption from the ban on conflicted remuneration for simple, well understood products where consumers generally understands that employees selling these products are not financial advisers, therefore reducing the risk of detriment to consumers.

Ban on volume-based shelf space fees

3.13 Under the current law, a platform operator is prohibited from receiving volume-based shelf-space fees from a funds manager where the fee is for 'purchasing' shelf space or preferential treatment by the platform operator.

3.14 In order to clarify the scope of the ban and provide certainty to industry, the Government has committed to amend the ban on volume-based shelf space fees to clearly identify the benefits the ban is intended to capture.

Client-pays exemption

3.15 Under the current law, certain benefits paid by a client to a licensee or representative are exempt from the ban on conflicted remuneration.

3.16 The Government has committed to reduce unnecessary complexity by clarifying that the exemption applies in circumstances where the benefit is paid directly by the client or by another party where the benefit is given at the direction of the client and with the client's clear consent.

'Mixed' benefits

3.17 Under the current provision of the Corporations Act, certain benefits may not relate to more than one of the products or circumstances that are exempt from the ban on conflicted remuneration. While the Corporations Regulations addressed this problem, this is not currently reflected in the Act.

3.18 The Government has committed to reduce unnecessary complexity and will amend the exemptions to reflect the intended operation of the law.

Consultation Draft

Summary of new law

3.19 The Bill amends the Corporations Act to broaden and clarify exemptions from the ban on conflicted remuneration. Specifically, the amendments provide that:

- general advice is exempt from the ban on conflicted remuneration;
- the ban on conflicted remuneration will only apply to monetary benefits paid in relation to life risk insurance products inside superannuation in circumstances where no personal financial advice about life risk insurance has been provided, or where coverage is provided in relation to MySuper;
- the execution-only exemption is expanded so that it applies where no advice has been provided to the client by the individual performing the execution service in the previous 12 months;
- the exemption from the ban on conflicted remuneration for the provision of training is expanded to include broader forms of training relevant to a financial services business;
- the exemption from the ban on conflicted remuneration for basic banking products can be accessed in a broader range of circumstances, that is, when advice on other simple ('Tier 2') financial products is provided at the same time as advice on a basic banking product;
- clearly define the benefits the ban on volume-based shelf-space fees is intended to capture, including incentive payments between fund managers and platform operators for the preferential treatment of products;
- clarify that, in relation to the ban on conflicted remuneration, the giving of a benefit includes causing or authorising it to be given, for example, a client causing or authorising a fee to be paid to their adviser out of an investment account; and
- clarify the exemptions from the ban on conflicted remuneration to allow a benefit to relate to more than one exemption.

Consultation Draft

Comparison of key features of new law and current law

New law	*Current law*
The ban on conflicted remuneration will not apply to the extent that the benefit relates to general advice provided to a retail client. The ban will continue to apply to benefits given to a licensee or a representative that could reasonably be expected to influence the personal advice provided or the financial products recommended to a retail client in the course of providing personal advice.	The ban on conflicted remuneration applies to benefits given to a licensee or a representative that could reasonably be expected to influence the financial product advice provided or the financial products recommended to a retail client (that is, includes both personal and general advice).
Monetary benefits paid to licensees, or representatives, in relation to life risk insurance offered outside of superannuation continue to be exempt from the ban on conflicted remuneration. Monetary benefits paid to licensees, or representatives, in relation to (group or individual) life risk insurance offered inside superannuation are exempt from the ban on conflicted remuneration except: in relation to MySuper; or in circumstances where no personal financial advice has been provided to the member regarding life risk insurance.	Monetary benefits paid to licensees, or representatives, in relation to life risk insurance offered outside of superannuation are exempt from the ban on conflicted remuneration. Monetary benefits paid to licensees, or representatives, in relation to life risk insurance offered inside of superannuation are exempt from the ban on conflicted except: in relation to group life risk insurance offered inside any type of superannuation fund; or individual life risk insurance offered inside a default superannuation fund.
The execution-only exemption will now apply if a monetary benefit is given in relation to the issue or sale of a financial product and the licensee or representative receiving the benefit (for example, an employee) has not provided personal advice to the client in relation to the product, or products of that class, in the previous 12 months.	A monetary benefit is exempt from the ban on conflicted remuneration if it is given in relation to the issue or sale of a financial product (i.e. execution-only), and the licensee or representative has not provided financial product advice to the client in relation to the product, or products of that class, in the previous 12 months.
The education and training exemption will now apply if it is relevant to the operation of a financial services business, which includes the provision of financial product advice.	A non-monetary benefit is exempt from the ban on conflicted remuneration if it relates to education and training that is relevant to the provision of financial product advice.

Consultation Draft

The basic banking product exemption in the Corporations Act will now apply if, at the time of providing advice on a basic banking product, the agent or employee of an ADI also provides financial product advice on a general insurance or a consumer credit insurance product. Therefore, in order to have access to the exemption, the agent or employee, at the time of providing advice on the basic banking product, must not provide advice on financial products other than a general insurance or a consumer credit insurance product.	A monetary or non-monetary benefit is exempt from the ban on conflicted remuneration if it is given to an agent or employee of an ADI and the benefit relates to a basic banking product. At the time of providing advice on the basic banking product, advice must not be provided on financial products other than a basic banking product. The Corporations Regulations provide that financial product advice on a general insurance product may also be provided at the same time.
A definition of a 'volume-based shelf-space' fee is provided as a fee which could reasonably be expected to influence the platform operator to increase the number or value of the funds manager's products that the platform operator is prepared to offer, or influence the platform operator to give preferential treatment to the funds manager's financial products under the custodial arrangement. Specific exemptions remain for a reasonable fee for service. The drafting of the exemption for scale efficiencies is clarified. A further exemption is provided for fees that relate to a general insurance product or a life risk insurance product offered under the custodial arrangement.	Volume-based shelf-space fees paid by a funds manager to a platform operator are banned. No specific definition of a 'volume-based shelf-space fee' is provided. A benefit is presumed to be a volume-based shelf-space fee if it is based on the total number or value of the funds manager's products to which the custodial arrangement relates. Specific exemptions are provided for a reasonable fee for service and a discount or rebate which does not exceed the scale efficiencies gained by the platform operator.
The existing exemption remains but is clarified that the benefit must be given at the direction of the client with the client's clear consent.	A benefit given by a retail client to a licensee or representative is exempt from the ban on conflicted remuneration if it relates to the issue or sale of a financial product or financial product advice provided by the licensee or representative.
The exemptions in Division 4 of the Corporations Act will apply *to the extent* that the benefit relates to an exemption. This means that one benefit may relate to several different exemptions.	The exemptions relating to general insurance, life risk insurance and basic banking products provide that the benefit must 'solely' relate to one of these products, meaning that a benefit cannot be given if it relates to

Consultation Draft

	one or more exemptions in Division 4 of the Corporations Act. This was rectified through the Corporations Regulations, however it is not reflected in the Corporations Act.

Detailed explanation of new law

General advice

3.20 This measure will exempt benefits that relate to general advice from the ban on conflicted remuneration. The objective of this measure is to properly target the advice that has the greatest ability to influence a retail client's financial decisions and to ensure that parties not directly involved in providing advice are not unintentionally captured.

3.21 Currently, section 963A of the Act defines 'conflicted remuneration' as a benefit given to a licensee or representative that could reasonably be expected to influence the choice of financial product recommended or the financial product advice provided to a client. 'Financial product advice' is defined in subsection 766B of the Act to include both personal and general advice.

3.22 The new law will amend the definition of 'conflicted remuneration' in section 963A of the Act to provide that a benefit given to a licensee or a representative will be banned if it could reasonably be expected to influence the personal advice provided or the financial products recommended to a retail client in the course of providing personal advice. ***[Schedule 1, items 24 and 25, paragraphs 963A(a) and (b)]***

3.23 The effect of the new law is that any benefits that relate to the provision of general advice to a retail client will not be subject to the ban on conflicted remuneration.

Exemption for life risk insurance benefits

3.24 This measure will limit the application of the ban on conflicted remuneration in relation to monetary benefits paid to licensees, or representatives, in relation to life risk insurance policies offered inside superannuation in order to minimise any distortions that may result from the differing treatment of these types of benefits inside and outside of superannuation.

Consultation Draft

3.25 Under the current law, monetary benefits paid in relation to life risk insurance offered outside of superannuation are exempt from the ban on conflicted remuneration.

3.26 Monetary benefits paid in relation to life risk insurance offered inside superannuation are predominantly banned, except in relation to individual policies offered under a non-default superannuation fund i.e. a life risk insurance policy offered for the benefit of an individual member (rather than a class of members i.e. a group policy) who has given written notice that the fund is their chosen fund.

3.27 Under the new law, the treatment of monetary benefits paid in relation to life risk insurance offered outside of superannuation is not altered, that is, benefits paid in relation to these offerings will continue to be exempt from the ban on conflicted remuneration.

3.28 Under the new law, the exemption provided for monetary benefits paid in relation to life risk insurance policies offered inside superannuation will be broadened such that the ban on conflicted remuneration will only apply in relation to monetary benefits paid with respect to:

- life risk insurance products for ***MySuper members***; and
- life risk insurance products offered inside other (non-MySuper) superannuation products in circumstances where no personal financial advice has been provided to the member regarding life risk insurance.

[Schedule 1, item 29, paragraph 963B(1)(b)]

3.29 MySuper products are simple superannuation products that replace existing default superannuation products. The term MySuper is given meaning by the SIS Act.

3.30 The new law defines 'MySuper members' as having the same meaning as in the SIS Act. This will mean that those members of a superannuation fund that hold an interest in a MySuper product will be considered 'MySuper members'. ***[Schedule 1, item 4, section 960]***

3.31 The new law also provides that a life risk insurance product is considered to be provided for a 'MySuper member' if the product is issued to the licensee (or custodian) of a superannuation fund for the benefit of the 'MySuper members' of that fund.

3.32 The law also removes the existing terms 'group life policy for members of a superannuation entity' and a 'life policy for a member of

Consultation Draft

default superannuation fund', as these terms are no longer used. ***[Schedule 1, items 2, 3, 31 and 32, section 960 , and subsections 963B(2), (3) and (4)]***

3.33 The effect of the new law is that benefits paid in relation to life risk insurance offered inside superannuation will be permitted under a broader range of arrangements than under the current law.

Execution-only exemption

3.34 This measure will amend the existing execution-only exemption in paragraph 963B(1)(c) to provide a nexus between the party receiving the benefit and the requirement that financial product advice must not have been provided to the retail client in the previous 12 months.

3.35 The current law provides that a monetary benefit is exempt from the ban on conflicted remuneration if it is given in relation to the issue or sale of a financial product, and the licensee or representative has not provided financial product advice to the client in relation to the product, or products of that class, in the previous 12 months. This is commonly referred to as the 'execution-only' exemption.

3.36 Under the new law, the execution-only exemption will apply if a monetary benefit is given in relation to the issue or sale of a financial product and the licensee or representative receiving the benefit (for example, an employee) has not provided personal advice to the client in relation to the product, or products of that class, in the previous 12 months. ***[Schedule 1, items 30 and 32, subsections 963B(3) and (4) and paragraph 963B(1)(c)]***

Training exemption

3.37 The measure will broaden the existing exemption from the ban on conflicted remuneration for non-monetary benefits for education or training in paragraph 963C(c) to include education and training that relates to the carrying on of a financial services business.

3.38 The current law provides an exemption for a non-monetary benefit that is genuine education or training relating to the provision of financial product advice to retail clients and where the benefit complies with regulations made for the purposes of the exemption.

3.39 Under the new law, a licensee or representative may receive a benefit of education or training that relates to the carrying on of a financial services business (for example, training in relation to client administrative services). The term 'carrying on of a financial services

Consultation Draft

business' includes the provision of financial product advice. ***[Schedule 1, item 35, subparagraph 963C(c)(ii)]***

Basic banking exemption

3.40 This measure will broaden the existing exemption from the ban on conflicted remuneration for basic banking products to allow an agent or employee of an ADI to access the exemption if, at the time of providing advice on a basic banking product, the agent or employee also provides financial product advice on other simple, 'Tier 2' financial products.

3.41 For the purposes of ASIC's training guidelines, ASIC makes a distinction between 'Tier 1' and 'Tier 2' products. Tier 2 products are generally considered simpler in nature and therefore require less onerous training requirements in order to give advice on those products compared to Tier 1 products. Tier 2 products include basic banking products, general insurance products and consumer credit insurance products. Tier one includes all other financial products not listed in Tier 2 (for example, managed investment schemes and superannuation).

3.42 Section 963D currently provides that a benefit is exempt from the ban on conflicted remuneration if the benefit relates to a basic banking product and the agent or employee of an ADI, at the time of providing advice on the basic banking product, does not provide financial product advice on any other financial product. Regulation 7.7A.12H of the Corporations Regulations allows access to the exemption where the agent or employee also provides financial product advice on a general insurance product.

3.43 Under the new law, section 963D will be amended to exempt a benefit from the ban on conflicted remuneration where it relates to a basic banking product, and the agent or employee does not, at the time of providing advice on the basic banking product, provide financial product advice on any other financial product except a general insurance product or a consumer credit insurance product. ***[Schedule 1, item 36, section 963D]***

3.44 A definition of 'consumer credit insurance' is inserted into section 960 as having the same meaning as in the *Insurance Contracts Act 1984*. ***[Schedule 1, item 1, section 960]***

3.45 In the course of providing financial product advice on a basic banking product, an agent or employee is not precluded from providing advice on products that are not financial products for the purposes of the Corporations Act (for example, a credit card or home loan). The new measure restricts the financial product advice able to be provided in relation to financial products to basic banking, general insurance and consumer credit insurance products.

Consultation Draft

Ban on volume-based shelf-space fees

3.46 This measure will amend the ban on volume-based shelf-space fees in order to clarify the scope of the ban and provide certainty in relation to the benefits in which the ban is intended to capture.

3.47 Currently, section 964 of the Corporations Act provides that the ban applies where a benefit is given by a funds manager to a platform operator and the funds manager deals in a financial product to which the custodial arrangement (provided by the platform operator) relates.

3.48 Existing section 964A presumes that benefits that are wholly or partly dependent on the total number or value of the funds manager's financial products which relate to the custodial arrangements are volume-based shelf-space fees. Subsection 964A(3) provides specific exemptions from the presumption.

3.49 The new law will amend section 964 to provide a definition of a 'funds manager' as a financial services licensee or a responsible superannuation entity licensee who issues or sells a financial product to which a custodial arrangement relates. ***[Schedule 1, items 37 and 38, subsections 964(1) and (2)]***

3.50 The new law clarifies the operation of the provisions that prescribe that platform operators must not accept volume-based shelf-space fees. ***[Schedule 1, item 39, section 964A]***

3.51 The new law will amend section 964A to define a volume-based shelf-space fee and amend the exemptions. A volume-based shelf-space fee will be defined as a benefit that, because of the nature of the benefit, or the circumstances in which it is given, could reasonably be expected to influence the platform operator to:

- increase the total number or value of the funds manager's financial products in which the platform operator is prepared to provide under the custodial arrangement; or
- given preferential treatment to the funds manager's financial products in providing the custodial arrangement.

[Schedule 1, items 8 and 39, section 960 and subsection 964A(2)]

3.52 Specific exemptions are provided for:

- a reasonable fee for service provided to the funds manager by the platform operator or another person;

Consultation Draft

- a discount on an amount payable, or a rebate of an amount paid to the funds manager by the platform operator, than can reasonably be attributed to economies of scale gained because of the number or value of the funds manager's financial products provided by the custodial arrangement; and

- a benefit that relates to a general insurance product or a life risk insurance product provided by the custodial arrangement.

[Schedule 1, item 39, subsection 964A(3)]

Client-pays exemption

3.53 This measure will, for the avoidance of doubt, clarify that a reference to the giving of a benefit includes a reference to causing or authorising it to be given.

3.54 Existing section 52 of the Corporations Act provides that 'a reference to doing an act or thing includes a reference to causing or authorising the act or thing to be done'.

3.55 Under the new law, a note will be inserted under section 963A to clarify the operation of section 52 in relation to the ban on conflicted remuneration. ***[Schedule 1, item 26, section 963A (note)]***

3.56 The new note is particularly relevant to the exemption from the ban on conflicted remuneration for benefits given to a licensee or representative by a retail client (paragraph 963B(1)(d)). In order to satisfy the exemption, the client must cause or authorise the benefit to be given. The benefit may be given directly by the client or given by another party, for example, by a trustee of a superannuation fund or a platform operator. Where the benefit is given by another party, it must be given at the direction of the client, with the client's clear consent. However, the mere fact that a client consents to a benefit to be paid, does not mean that the benefit is caused or authorised by the client.

'Mixed' benefits

3.57 This measure will allow a benefit to relate to more than one exemption from the ban on conflicted remuneration.

3.58 The exemptions relating to general insurance, life risk insurance and basic banking products under Division 4 of Part 7.7A of the Corporations Act provide that the benefit must 'solely' relate to one of

Consultation Draft

these products, meaning that a benefit cannot be given if it relates to one or more exemptions in Division 4. This was rectified through the Corporations Regulations; however it is not currently reflected in the Corporations Act.

3.59 The new law provides that a benefit will be exempt from the ban on conflicted remuneration to the extent that it relates to one or more of the products or circumstances described in sections 963B, 963C and 963D. This will allow a benefit to relate to one or more exemptions as well as circumstances which do not fall within the definition of conflicted remuneration under section 963A. ***[Schedule 1, items 27, 28, 29, 33, 34 and 36, sections 963C and 963D, subsection 963B(1), paragraphs 963B(1)(a), 963B(1)(b) and 963C(a)]***

Application and transitional provisions

3.60 These provisions commence the day after Royal Assent.

Ban on conflicted remuneration

3.61 The amendments made in relation to the ban on conflicted remuneration apply to a benefit if:

- the benefit is one to which Division 4 of Part 7.7A applies under section 1528, that is, the benefit is not grandfathered; and
- the benefit is given on or after the commencement day.

[Schedule 1, Schedule 1, items 42, 43 and 44, sections 1531A and 1531E]

3.62 Certain benefits given under an arrangement entered into prior to the application day of the ban on conflicted remuneration, as defined in subsection 1528(4), are not be subject to the ban as a result of subsection 1528(1) and regulations made for subsection 1528(2). These benefits will not be impacted by the new law.

3.63 Benefits given under an arrangement entered into after the application day of the ban on conflicted remuneration and certain benefits given under arrangements entered into prior to the application day are subject to the ban. Under the current law, such a benefit could not be given or received if it is conflicted remuneration. The new law serves to exempt certain benefits that are subject to the current law. As such, the amendments are not likely to give rise to the risk of acquisition of property (within the meaning of paragraph 51(xxxi) of the *Australian Constitution*). In any case, subsection 1528(3) provides that Division 4 of

Consultation Draft

Part 7.7A of the Corporations Act will not apply to the extent it would result in an acquisition of property from a person otherwise than on just terms (within the meaning of paragraph 51(xxxi) of the *Australian Constitution*).

3.64 The current requirements will continue to apply until the new law is in place or new regulations are made.

Ban on volume-based shelf-space fees

3.65 The amendments made in relation to the ban on volume-based shelf-space fees apply to a benefit if:

- the benefit is one to which Subdivision A of Division 5 of Part 7.7A applies under section 1529, that is, the benefit is not grandfathered; and

- the benefit is given on or after the commencement day.

[Schedule 1, items 42, 43 and 44, sections 1531A and 1531F]

3.66 Under subsection 1529(1), the ban on volume-based shelf-space fees applies where the benefit is given under an arrangement entered into prior to the application day, as defined in subsection 1529(3).

3.67 The current requirements will continue to apply until the new law is in place or new regulations are made.

Consultation Draft

Chapter 4
Summary of regulation impact statement

An options-stage regulation impact statement (RIS) has been prepared in accordance with the Office of Best Practice Regulation (OBPR) guidelines. The RIS has been published on the website of OBPR and can be accessed here: http://ris.finance.gov.au/2014/01/13/future-of-financial-advice-amendments-options-stage-regulation-impact-statement-department-of-the-treasury/

Impact: The amendments to FOFA will affect businesses and consumers within the financial services industry.

Main points:

- The amendments to the FOFA legislation seek to fulfil the Government's election commitment, so no alternative policy options have been considered as a part of the RIS.
- The proposed FOFA amendments are deregulatory and have been designed to reduce the compliance burden on the financial advice industry. Firms within the industry are expected to benefit through a reduction in red tape and compliance costs.
- Preliminary estimates, based on industry consultation, of the direct ongoing cost savings are approximately $190 million per year; one-off implementation cost savings are approximately $90 million.
- Consumers are expected to gain access to more affordable and accessible financial advice as lower costs to industry are passed through to consumers.
- The options-stage RIS is largely used to inform the consultation process. The information gathered through consultations will be used to refine the RIS into a final details-stage RIS, which will be completed prior to the finalisation of legislation.

Consultation Draft