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Advice and Investment Branch  
Retirement, Advice and Investment Division  
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### **AFA Submission: Review of the quality of financial advice - Draft Terms of Reference**

The Association of Financial Advisers Limited (**AFA**) has served the financial advice industry for over 75 years. Our objective is to achieve *Great Advice for More Australians* and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

With the exception of Independent Directors, the Board of the AFA is elected by the Membership and Directors are currently practicing financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting their wealth.

#### **Introduction**

The AFA welcomes the opportunity to provide feedback on the Draft Terms of Reference for the Quality of Advice Review (QAR).

The AFA is very supportive of the Government's pursuit of this review and the objective of ensuring accessibility and affordability of quality advice. This review is happening at the right time, and is a critical review that must seek to address the continuing problems confronting the advice profession. Importantly this review needs to identify solutions to address the existing and emerging challenges that could threaten continued access to advice for the many clients who already have an advice relationship and the many more potential clients who would benefit greatly from access to personal financial advice.

In our view, the Terms of Reference are well drafted, and with the exception of a few recommendations that we have set out below, should largely address the objectives.

## Key Recommendations

We have identified a limited number of key themes that we would like to ensure that the review addresses, including the following:

- **Voice of Existing Clients.** It is critically important to hear the voice of existing clients. In recent years the Parliament has introduced additional layers of bureaucracy with little consideration of the impact on clients and whether they value these measures and whether they were willing to pay for them. We believe that this existing client perspective is critical to incorporate in order to make sure advice is affordable and valued by clients. Some recent examples that are worthy of detailed consideration include:
  - The annual renewal requirement and client consent forms. Clients now need to renew their arrangement with their adviser each year, and to also sign consent forms that are provided to each of the product providers that are involved. For a couple, this could involve signing six or seven fee related forms every year.
  - Clients no longer have the flexibility to decide the timing of the renewal of their ongoing fee arrangement. This is set by when they first became a client and cannot be changed. The advice process and regulations should support the needs of clients, not make things more difficult for them.
- **Process Re-engineering.** Financial advice is a complex process that is heavily defined by regulation, and needs to be carefully analysed. Each step in the process needs to be assessed for efficiency and value to the end consumer. Following so much change over recent years, the balancing of the benefits of each new regulatory requirement, as well as the unintended consequences, needs to be carefully scrutinised. Non-value adding steps need to be removed and inefficient steps need to be made more efficient. The QAR should involve a process re-engineering review to carefully analyse each step in the process and what can be done to reduce the cost without the removal of activity that is value adding to clients. An example of such a regulatory requirement is the Financial Services Guide (FSG), which may have been more important in the past, given conflicted remuneration and a market typified by significant vertical integration, however, the market has changed, and conflicted remuneration has largely been banned. It is appropriate to ask what is the utility of an FSG for advised clients now, especially given other disclosure documents which are provided to clients. This is worthy of consideration, including with respect to alternative options.
- **Centralised Systems and Standardised Processes/Forms.** In recent years, regulatory change has been introduced without adequate consideration of leveraging cross industry standardised systems and processes. Most things are built on a licensee basis or a specific product provider basis, which means that advisers have to comply with the different systems and processes of each product provider they work with. Classic examples are the client consent form solutions and Design and Distribution Obligation reporting. There must be much greater opportunity to use centralised system solutions (i.e. Blockchain style) and standardised processes and forms. One contributing factor to the lack of industry standardisation might be the restricted implementation and transition timeframes that have applied with recent reforms. This might suggest that there is a minimum implementation timeframe that should be defined and greater consideration of implementation in an industry wide efficient manner.
- **Regulatory Uncertainty.** Regulatory uncertainty is a well recognised issue and one that has been discussed in the course of parliamentary hearings in recent times. Licensees have been blamed for processes and rules that are considered unnecessarily risk averse. Licensees are uncertain, with respect to what the regulators may expect and whether their processes will meet, not only the standards that apply now, but also the standards that may exist in the future, when the actions of today might be assessed. The obvious example of this is with respect to “fees for no service”, where licensees and advisers are being assessed in terms of record keeping on the basis of standards that apply now and not what was in existence 10 years ago. Efficient processes are often based upon a clear, sector-wide understanding of regulatory requirements that can be relied upon. We would encourage the QAR to consider how to deal with regulatory uncertainty. One suggestion that arises from time to time is that

of binding rulings that apply with respect to other regulators. Another option to consider with this issue is the development of a publicly available consolidated register of compliance obligations.

- **Risk-Based Compliance Regime.** Whilst we strongly advocate for a complete overhaul of the regulatory and legislative frameworks that govern the provision of financial advice in Australia, to ensure meaningful change, we concede that the QAR will ultimately need to be limited in its scope, timeframe, and deliverables. Notwithstanding these limitations, we recommend that any changes to the legislative and regulatory framework, because of the QAR, consider a risk based regulatory and legislative response. The services and advice that a financial adviser may provide ought to be listed, alongside the various risks and consumer detriment that may arise from each activity, ensuring that the compliance framework that governs the activity is proportionate to the risks that may ensue. This approach will ensure that compliance is targeted at high-risk advice and services, which may cause significant consumer detriment. This ought to reduce the red tape that may apply to other lower risk services and advice which struggle under the weight of the regime that sits across the entire spectrum of advice and services.
- **Encouraging New Entrants.** One of the greatest challenges confronting the financial advice profession is the lack of new entrants. There are a range of factors including the perceived reputation of the financial advice profession, the education standard, the availability of courses and the appetite of practices to employ new entrants and put them through the Professional Year. We would like to see this issue carefully analysed to assess what more could be done, including potentially through rationalisation of the Professional Year requirements or through Government support of new advisers (akin to apprenticeship programs).
- **Individual Licensing.** The ongoing debate of licensees versus individual licensing is worthy of consideration by the QAR. It is understood that this is a complex and broad issue, however the advice profession needs to have some certainty on whether this is an issue that might be pursued in the future.

## Detailed Feedback

Our further, more detailed feedback, is as follows:

- Paragraphs 1 and 2 refer to “high quality affordable and accessible financial advice”. We suggest that “high quality” needs to be defined as there is a risk that the difference between “quality” and “high quality”, may make the advice unaffordable. There is an inevitable trade-off between quality and cost, and it is necessary to carefully choose the point at which the marginal cost of additional quality starts to significantly exceed any marginal benefit.
- We would like to see paragraph 3.1.1 also focus upon “strategic advice”, which is advice that does not involve a recommendation with respect to a specific financial product, and the barriers that prevent the efficient provision of strategic advice. We support increased use of strategic advice, which should be possible to deliver in a simpler form.
- With respect to paragraph 3.1.5, we appreciate that this is connected to Royal Commission Recommendation 2.5 and the issue of underinsurance. We believe that it is important to make the point that underinsurance has been impacted by a range of reforms other than just the LIF reforms. We are referring to other life insurance reforms such as Protecting Your Super Package, Putting Members Interests First and the APRA Intervention into the IDII market. We recommend that paragraph 3.1.5 be amended to “The life insurance remuneration reforms, and other life insurance reforms, and the impact of these reforms on the levels of insurance coverage”. Another important factor influencing access to advice on life insurance and therefore underinsurance, is the decline in the number of financial advisers, and particularly the substantial decline in the number of life insurance advisers. This has been influenced by a range of issues and is another factor that should be considered in the context of underinsurance and the implications of any further changes to life insurance advice remuneration.
- Paragraph 3.3 refers to the actions of ASIC, who are particularly important in the financial advice sector. ASIC is the most significant regulator for the financial advice sector. More

recently, APRA have also emerged as an important regulator in a number of ways, including their intervention in the Individual Disability Income Insurance market and their issuing of a joint letter with ASIC to the trustees of super funds on the oversight of fees charged by financial advisers. In this letter they have gone as far as to require that trustees review a sample of Statements of Advice, which in our view is inconsistent with the Privacy Obligations and inappropriate for a super fund trustee to have visibility of a clients non super assets, or investments in other super funds. We also note that APRA are responsible for the Sole Purpose Test and their guidance on this was issued in 2001, more than 20 years ago, and in a very different era. This is a key issue impacting regulatory uncertainty.

- Paragraph 4.2 rightly refers to best practice developments internationally, which we strongly support, however we would also suggest consideration of the operating models of other advice-based professions in Australia. As an example, how does the financial advice process compare with the medical profession? It is wrong to simply dismiss this type of analysis on the grounds of the conflicts of interest that exist in financial advice. Conflicts exist in medicine, where doctors can recommend medical procedures, that they will administer, that involve high levels of risk and significant costs.
- We acknowledge that the Government is separately dealing with the issue of the education standard for financial advisers, which we consider to be appropriate. Another consideration with education is the issue of specialisation and the need for education and experience to support practice in that area. This is an issue that FASEA never addressed, but one that is important to ensure that consumers get high quality advice and services. We recommend that this is included in the scope of the QAR.

## Process

We note that the Government proposes that this review be undertaken by a single independent reviewer. The utilisation of a single person to undertake the review increases the importance of the selection of the reviewer. We would also argue that it is essential that the reviewer has access to quality knowledgeable people from the advice profession, who can assist with the investigation of issues and the development of solutions. Given that it is the Quality of Advice review, and as one of the main financial advice professional associations, the AFA wishes to play a leading role and seeks to be meaningfully engaged in the review. We expect to be directly consulted on an ongoing basis along with the other major associations that represent the sector, to prevent the handing down of recommendations and changes that are either ineffective or inappropriate.

The appointment of a single reviewer serves to highlight the importance of selecting a person who has a deep understanding of financial advice and the best interests of consumers. More than likely, they will be a person who has previously been employed in a senior role in the financial services industry.

We would firmly favour an approach that involves the release of discussion or issues papers as the review progresses, and the release of an interim report for consultation. We would like to ensure that the financial advice sector has the opportunity to contribute to the understanding of the current issues and the identification of solutions. It would be profoundly disappointing for the reviewer to make final recommendations that do not align with the underlying reality of the sector or that lack the support of the financial advice profession. This is not to say that the reviewer should not canvas and recommend controversial ideas or to challenge conventional thinking, however this should happen as part of the process and not at the conclusion.

We would also like to see that the QAR identifies a range of quick wins, during the review, that they can immediately transfer to the most appropriate party to implement. This might be issues that can be fixed by regulatory change or industry practices that can be referred to the financial services industry to address. The problems facing the financial advice sector are substantial and we would favour any obvious wins being implemented as soon as practical.

## Concluding Comments

We support the Draft Terms of Reference, although we believe that it can be enhanced by the addition of a few extra focus areas and by some refinement of what has already been proposed.

We would be happy to discuss this matter further, or to provide additional information if required. Please contact us on (02) 9267 4003.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'PA Anderson'.

**Phil Anderson**  
Chief Executive Officer  
Association of Financial Advisers Ltd