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Professor Ian Ramsay
EDR Review Panel
C/o: Department of Treasury

By email: EDRreview@treasury.gov.au

Dear Professor Ramsay

COMPENSATION SCHEME OF LAST RESORT – SUPPLEMENTARY ISSUES PAPER

Thank you for the opportunity to comment on the EDR Reviews Supplementary Issues Paper regarding a potential compensation scheme of last resort (CSOLR).

While AMP is sympathetic to the customers who have unpaid FOS determinations, AMP does not support the establishment of a CSOLR. In our view, a CSOLR represents poor public policy for many reasons which were outlined in our previous two submissions to the Panel.

We strongly support the FSC's submission to the Panel on this issue. Unfortunately the ABA's submission does not represent AMP's views notwithstanding that we have the largest advice network within the ABA's membership.

AMP supports the urgent implantation of the Richard St John 2010 recommendations following his extensive examination of compensation arrangements. That is, that there are appropriate PI insurance and capital requirements to ensure that a licensee is in a position to pay compensation determinations to customers (as a result of IDR, EDR or other actions).

This addresses the policies from the front end of the regulatory system and will assist in customers having trust and confidence in the willingness and ability of a licensee to take responsibility for the financial advice they provide.

We do not propose to duplicate our previous submissions on this issue – and assume the Panel will review these as part of their consideration of a potential CSOLR. In summary, AMP is opposed to a CSOLR for reasons including:

- It is considering the problem from the wrong end. Arrangements should be put in place to ensure, as far as possible, that licensees have the proper capital and insurance before they commence providing financial advice to customers
- Compensation schemes of last result could result in significant moral hazard, and

- The cost burden is being imposed on those companies who have invested in capital and PI insurance and have done the right thing by their customers who have received improper advice.

We consider that capital and insurance requirements should be developed as a means of protecting consumers from ever needing to look towards a scheme of last resort. This is because there will be adequate availability of funds to pay any determinations.

In addition to our previous submissions, we have the following comments on the supplementary issues paper.

Principles Guiding the Review

We agree with the principles set out in the paper that underpin the policy assessment undertaken by the Panel. We have the following comments:

- Efficiency – we consider that appropriate PI insurance and capital requirements are more efficient than a CSOLR given that they provide consumers with protection upfront rather than at the end of the process. A CSOLR will be less efficient and will require considerable resources to administer.
- Equity – PI insurance and capital requirements will provide customers with trust and confidence that they will be treated fairly. It also removes any cross-subsidisation from firms who ‘do the right thing’ to firms which are unwilling to be responsible for their advice. It also reduces any ‘moral hazard’ whereby firms and consumers may take risky decisions with a belief that a public safety net will provide compensation.
- Complexity – a CSOLR is more complex than requiring upfront license conditions.
- Transparency – consumers should receive financial advice confident that the licensee will have adequate resources to pay any compensation for poor advice
- Accountability – requiring licensees to have adequate PI insurance and capital arrangements enforces accountability to each licensee. Maintaining appropriate PI insurance also has the added benefit of reinforcing the need for strong compliance frameworks in order to minimise claims on PI insurance and reduce premiums. Capital requirements also provide some assurance against licensee insolvency.
- Comparability of outcomes – all customers should be able to expect that licensees will compensate them for poor advice, whether as an outcome of IDR or EDR processes.
- Regulatory costs – a CSOLR will create moral hazard. There may be an incentive for some advisers to leave licensees that have strong compliance frameworks, including prohibitions on risky products or strategies.

Redress for Past Disputes

While we sympathise with the customers who have unpaid determinations, we do not support a scheme that would retrospectively address unpaid determinations. We question whether it would legally be possible to levy participants for past issues. Asking shareholders of licensees to pay for previous actions by firms who we have had no control over is not a good public policy outcome. We

suggest that any retrospective compensation should be funded more broadly through some form of Government assistance.

Compensation arrangements – PI insurance

While we understand ASIC's concerns that PI insurance is not available to directly compensate customers, we respectfully consider that the outcome in achieving the public policy intention is what should be considered.

PI insurance provides customers with trust and confidence that the licensee will have adequate resources to pay any determinations. It does not directly compensate the customer but it does significantly increase the likelihood of appropriate compensation. A licensee may choose to pay out of capital in some instances and not draw on PI insurance. However that does not negate the need for appropriate PI insurance unless the licensee has effectively 'self-insured' through capital requirements.

We also note that PI insurance will not provide cover for certain situations such as fraud. No general insurer, as far as we are aware, is willing to underwrite fraudulent activity in the industry. This is obviously a practical and prudent approach. That is why, in most cases, a mixture of both PI insurance and capital is required to provide assurances that a licensee can pay appropriate compensation.

It is also unreasonable to expect shareholders of licensees who do the right thing to underwrite fraud elsewhere in the industry.

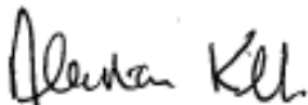
We also understand that PI insurance is working well in other sectors, eg the National Insurance Brokers and the various state-based Law societies.

Conclusion

Thank you again for the opportunity to contribute to this important discussion. We would be pleased to discuss our views with the Panel at your convenience.

Should you have any questions, please contact Jenifer Wells, Head of Public Policy on 0402 111 044.

Yours sincerely



Alastair Kinloch
Director, Government Affairs