



CHARTERED ACCOUNTANTS™
AUSTRALIA + NEW ZEALAND

29 March 2019

The Treasury
Financial Services Reform Implementation Taskforce
Langton Crescent
Parkes ACT 2600
Email: FOFAGrandfathering@treasury.gov.au

Attention – Taskforce Lead James Kelly

Dear Mr Kelly

Re: Ending Grandfathered Conflicted Remuneration for Financial Advisers

Chartered Accountants Australia and New Zealand (Chartered Accountants) welcomes the opportunity to comment on the Exposure Draft Treasury Laws Amendment (Ending Grandfathered Conflicted Remuneration) Bill 2019.

Chartered Accountants is a professional body comprised of over 120,000 members, including more than 25,000 members in public practice in Australia. Our members work in a wide range of roles in the financial services industry, as individual advisers as well as in small businesses, small and medium-sized accounting practices, the corporate sector, major financial institutions and financial product manufacturers.

As a professional body we advocate in the interests of our members and the accounting profession and in the public interest. In preparing this submission we have consulted with our members and other professional associations.

Chartered Accountants has long supported ending conflicted remuneration for financial advisers, with appropriate transitional timeframes. It is time for the industry to work together to change conflicted remuneration and incentive structures, including grandfathered commissions and commissions on life insurance products.

Chartered Accountants supports removing grandfathering arrangements for conflicted remuneration and other banned remuneration. In principle we support 1 January 2021 as the effective date for this new law. We also support the regulations providing for a scheme under which amounts that would otherwise have been paid as conflicted remuneration are rebated to affected consumers. However, there are issues which will need to be carefully considered and managed to ensure that the provisions operate as intended and to avoid any detriment to consumers.

Our detailed submission accompanies this letter. Further information about us in **Annexure A**.

If you would like to discuss our submission, please do not hesitate to contact Bronny Speed FCA, Leader - Financial Advice on (02) 8078 5442 or at bronny.speed@charteredaccountantsanz.com.

Yours sincerely,

Simon Grant FCA
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Ending Grandfathered Conflicted Remuneration for Financial Advisers

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Support for ending conflicted remuneration

Chartered Accountants has long supported ending conflicted remuneration for financial advisers, with appropriate transitional timeframes, and raising the standards of ethics and professionalism in the financial advice industry to better serve and protect consumers. This is vital to help restore public trust and confidence.

Improving trust and confidence in the financial advice industry was a key objective of the Future of Financial Advice (FOFA) reforms. During consultations on the FOFA reforms we did not support the carve-out of different forms of conflicted remuneration, due to concerns that this would add to complexity and administration costs and decrease the accessibility of affordable, quality to advice to consumers. We advocated that all payments deemed to be conflicted remuneration should be regulated consistently.

As noted in our submission on the interim report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Chartered Accountants believes it is time for the industry to work together to address poor institutional cultures and change conflicted remuneration and incentive structures, including grandfathered commissions and commissions on life insurance products.

Removing grandfathering arrangements

Enacting retrospective laws

Chartered Accountants has in previous submissions raised concerns about the enactment of laws with retrospective application. Care needs to be taken to ensure that any retrospective ban on conflicted remuneration does not create liability for persons who have sought in good faith to comply with the prevailing laws at the time.

Transitional timeframes need to be considered

Chartered Accountants supports removing grandfathering arrangements for conflicted remuneration and other banned remuneration in relation to financial advice to retail clients.

Whilst we support 1 January 2021 as the effective date for this new law in principle, careful consideration should be given to the appropriateness of this timeframe in circumstances where ending grandfathered remuneration may not be in the best interests of the client. It is critical that care is taken to avoid any detriment to consumers and any liability to advisers for breach of the best interests duty. Consideration should also be given to whether the 1 January 2021 deadline will provide a long enough lead time for product providers to change systems.

If laws can be enacted in the best interests of the client and product provider systems enabled to rebate existing ongoing commissions to clients prior to 1 January 2021, then Chartered Accountants would support this timeframe.

Chartered Accountants is pleased to note that on Thursday 28th March 2019, the Treasurer, The Hon Josh Frydenberg MP, released Draft Regulations to remove grandfathering arrangements for conflicted remuneration which will require product manufacturers to pass on to the client any benefits of previously grandfathered conflicted remuneration remaining in contracts after 1 January 2021 (Draft Regulations).

Acting in the best interests of the client

Chartered Accountants has concerns that a complete ban on conflicted remuneration may in some circumstances result in greater risk or harm to consumers than that which already flows from the conflicted remuneration, such as where a complete ban on commissions in respect of life insurance products leads to significant underinsurance if the client cannot afford to pay the upfront fee. The client's advisers may also be in breach of their best interests obligation.

We support Commissioner Hayne's view that if ASIC's post-implementation review in 2021 indicates that the cap on life insurance commissions has not contributed (or at least not significantly contributed) to underinsurance, then ASIC should continue reducing the cap, ultimately to zero.

Rebating conflicted remuneration

Insurance contract issues

Chartered Accountants supports a ban on all bulk (volume) commissions to the extent this can be achieved without causing disadvantage to consumers.

As part of these reforms, as soon as is practicably possible, but certainly by 2021, where the client to whom the conflicted remuneration relates can be identified, insurance companies should be required to rebate to the client the quantum of existing upfront commissions against first year premiums, and no less, as is the case in many current circumstances, and to keep a record of all conflicted remuneration rebated to the client. Where conflicted remuneration can only be attributed to a group of clients it should be rebated equitably amongst the group.

Where it is *inappropriate* to move an existing policy to a new insurance contract (for example in many instances where the client has been in the policy for a period of time and/or there is a level premium policy and/or the client is insured, has an injury, and is unable to obtain new insurances) all ongoing commission should be rebated against future ongoing premiums and, in these circumstances, this *should not* be deemed to be conflicted remuneration as the commission does not pass through the Australian Financial Services Licence.

Insurance companies should be required to offer all new contracts from 1 January 2021 at reduced premiums, upfront and ongoing, as they will no longer be paying commissions on those new contracts. Insurance companies should be encouraged to introduce non-commission premium rates as soon as possible, many offer this already.

Chartered Accountants recommends that where advisers take on a new client and are bound by the best interests duty to look into existing policies (and hence the policy is under the adviser's name and a commission is received as a legacy issue), at the new adviser's request, insurance companies should be required to rebate any ongoing trail commissions to that client at the same quantum as the current commission was paid to the previous adviser. In this way, advisers can review existing policies and observe their best interests obligations without being held liable for receiving commissions.

It appears as if this is the intention in the Government's Draft Regulations.

Investment product issues

Consideration should be given to the various issues that may impact on an adviser's ability to sell and/or move an investment that contains an ongoing commission without disadvantaging the client, such as:

- Cost of a Statement of Advice (SoA) to advise a client to move from a commission related investment;
- Inability to do a Record of Advice (RoA) if the adviser didn't recommend the product in the first place;
- Cost of realising unrealised capital gains;
- Buy/sell spreads;
- Cost of researching as part of an overall assessment of the client's situation – under the best interests duty;
- Uniqueness of investment and its ability to be replaced;
- Illiquidity of the investment;
- Transaction fees;
- Legacy products that are in the best interests of the client;
- Early redemption costs;
- Exit costs;
- Deferred bonuses foregone on life insurance products; and
- Practicality of doing so for a whole of life policy.

Chartered Accountants recommends that where a client has an investment product, and it contains an ongoing commission, and it cannot/ should not be sold or moved, the investment manager should be required to rebate the quantum of that ongoing commission back to the client's investment with no adverse tax and/or regulatory consequences.

We note that this appears to be reflected in the Government's Draft Regulations.

Superannuation fund issues

As with investment products, consideration should be given to the numerous issues that may impact an adviser's ability to move a superannuation investment that contains an ongoing commission without detriment to the client, such as:

- Cost of an SoA to advise a client to move from a commission related super product;
- Inability to do an RoA if the adviser didn't recommend the product in the first place;
- Cost of realising unrealised capital gains on rollover;
- Buy/sell spreads;
- Cost of researching as part of an overall assessment of the client's situation – under best interests' duty;
- Inability to rollover the fund due to insurances;

- Illiquidity of investments within the super fund;
- Being part of a corporate super plan whereby the fees are at a cheaper rate than can be obtained by individual advisers;
- Transaction fees;
- Legacy products that are in the best interests of the client;
- Early redemption costs;
- Exit costs;
- Deferred bonuses foregone on life insurance products; and
- Other life insurance issues.

Chartered Accountants recommends that where a client has a superannuation fund, and it contains an ongoing commission, and it cannot/should not be rolled over, the super provider should be required to rebate the quantum of that ongoing commission back to the client's super fund without any adverse tax and/or regulatory consequences.

The Government's Draft Regulations appear to support this position.

Appendix A

Chartered Accountants Australia and New Zealand

Chartered Accountants Australia and New Zealand is a professional body comprised of over 120,000 diverse, talented and financially astute members who utilise their skills every day to make a difference for businesses the world over.

Members are known for their professional integrity, principled judgment, financial discipline and a forward- looking approach to business which contributes to the prosperity of our nations.

We focus on the education and lifelong learning of our members and engage in advocacy and thought leadership in areas of public interest that impact the economy and domestic and international capital markets.

We are a member of the International Federation of Accountants and are connected globally through the 800,000-strong Global Accounting Alliance and Chartered Accountants Worldwide which brings together leading Institutes in Australia, England and Wales, Ireland, New Zealand, Scotland and South Africa to support and promote over 320,000 Chartered Accountants in more than 180 countries.