



6 May 2013

General Manager
Retail Investor Division
The Treasury
PARKES ACT 2600

Submission by email: futureofadvice@treasury.gov.au

Dear Ms Sim,

Future of Financial Advice – Intra Fund Advice Regulations

The FSC thanks the government and The Treasury for the opportunity to provide comments on the proposed amendments to the Corporations Regulations (the **Principal Regulations**) pertaining to the convergence of intra-fund advice (**IFA**) and the FoFA adviser charging provisions of the Corporations Act.

The Financial Services Council represents Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks, trustee companies and Public Trustees. The Council has over 130 members who are responsible for investing more than \$1.9 trillion on behalf of 11 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world. The Financial Services Council promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

Principles of FoFA

The FSC, consistent with the government and regulator, is strongly of the view that financial advice is beneficial and indeed provides value for Australians who access it. The FSC contends that accessible and affordable financial advice is therefore critical for Australians and to this end we have supported measures by the government which deliver this policy objective.

However, the FSC submits that the Intra-Fund advice's charging regime is counter to the policy objectives of the FoFA reforms. This regulation, in addition to the MySuper Core Provisions Act codifies the cross-subsidisation and non-transparent payment of ongoing fees by consumers from their retirement savings for an advice service Australian superannuants may never access and may never know they are paying.

The FSC restates its position on Intra-Fund Advice in Item 1 of the Key Issues section following.

Further to the codification of Intra-Fund Advice within superannuation, we note that the government has made several announcements to exempt Intra-Fund Advice over other forms of personal advice to retail clients from certain provisions of FoFA. However, there are a number of legislative and regulatory instrument amendments which are required to enable Intra-Fund Advice to work without the providers breaching FoFA legislation. This submission makes recommendations to amend these specific proposed regulations to align with the government's intent. The submission also reminds Treasury that there remain further legislative gaps which need to be addressed to enable Intra-Fund Advice to be provided lawfully.

The FSC is happy to assist and discussing the contents of this submission and any drafting concerns Treasury may have with you. If you have any questions regarding the FSC's submission, please do not hesitate to contact me on (02) 9299 3022.

Yours sincerely



CECILIA STORNILO
SENIOR POLICY MANAGER



FSC SUBMISSION

Intra Fund Advice Regulations

MAY 2013

KEY ISSUES

1. Intra-fund advice is inconsistent with FoFA

A key element of the Government's FoFA announcements made in April 2010 was the consideration of the provision of "low cost simple advice (known as Intra-Fund Advice)".

The Government's commitment to low cost simple advice was warmly welcomed by the industry. The ability to provide simple advice (at a lower cost) would deliver significant benefits for Australian consumers namely in the form of increasing accessibility and affordability of advice.

Importantly, access to affordable and scaled or piece by piece advice¹ is increasingly preferred by Australians over more complex/holistic advice, which is legally required to be given by a financial advice licensee under section 945A of the Corporations Act.

Critically, the FSC has always advocated for a product and channel neutral approach to scaled advice: that is, scaled advice which should not be limited to superannuation. Additionally, scaled advice was always expected to be subject to FoFA requirements – namely the best interest duty, renewal and the conflicted remuneration provisions to name a few.

As a result, the FSC previously has submitted on numerous occasions to Treasury that the concept of Intra-Fund Advice – which includes limited personal financial advice provided by a superannuation product provider – should be extended beyond superannuation so that Australians who invest in savings, managed investments and insurance products can also be afforded this low cost type of advice.

We contend that the payment for Intra-Fund Advice on a hidden basis replicates product commissions which FoFA banned, directly contradicts the central objectives of the reforms including:

- Increased transparency of advice fees paid by consumers;
- Ensuring that consumers who do not access advice are not paying for advice;
- Banning conflicted remuneration including product commissions for advice; and
- Enhancing consumer trust in financial advice

These regulations, which deliver on the government's announcement of 8 December 2011², will exempt Intra-Fund Advice fees from superannuation members' monies being subject to the FoFA's "Opt-In" measure despite the Cooper panel's comments that "Opt-in" should also apply to superannuation:

¹ ASIC report *Access to financial advice in Australia (REP224)*, December 2010 paragraphs 53 and 62.

² Minister Shorten MR164 "Improving Access to Simple Financial Advice", 8 December 2011. "The Government has already accepted the recommendations of the independent Superannuation System Review (the Cooper Review) that intra-fund advice can be collectively charged by superannuation trustees to their members and not be subject to provisions such as opt-in."

“The Panel notes the Future of Financial Advice reform package requires that if an adviser is to provide an ongoing service, the adviser must send an annual renewal notice to the client. Although those reforms are intended to apply in relation to any financial services, including superannuation, the Panel is particularly of the view that an annual renewal regime would be necessary in MySuper³.”

The government announcement on 8 December 2011⁴ *only* permits superannuation funds to offer Intra-Fund Advice⁵ which will be able to provide ***any general and personal advice limited to the member’s beneficial interest in the superannuation fund (the sole purpose test)*** and:

“there will be new restrictions on the types of advice that can be provided under intra fund advice rules. Specifically, the following are excluded:

- Advice relating to whether the member should consolidate their existing superannuation accounts
- Advice to switch the member away from the superannuation fund into another superannuation fund except to the extent the advice relates to moving the member from an accumulation product into a retirement product offered by the same registrable superannuation entity
- Advice that contains recommendations in relation to financial products that the member holds outside of superannuation
- Advice in relation to investment choice outside of the trustee-prescribed investment options”

This means MySuper members, deemed to be investors requiring the greatest levels of protections, will pay for financial advice, regardless of whether they access this general and personal financial advice.

We note that the MySuper legislation allows superannuation trustees to charge advice fees bundled with the administration cost of the fund - exactly the same ‘conflicted remuneration’ the FoFA reforms now ban.

³ Cooper Review: Review into the Governance, Efficiency, Structure and Operation of Australia’s Superannuation System, *Superannuation System Review Final Report, Part Two, Recommendation Package*, 2010, page 21.

⁴ Intra-Fund Advice is today only permitted to be offered by superannuation funds under a Class Order exemption [CO09/210]. Under a Class Order exemption [CO09/210], trustees of regulated superannuation funds are currently permitted to provide personal financial product advice in respect of various matters relating to the superannuation fund, and are exempted from section 945A of the Corporations Act in doing so. (Other licensed advisors are required to comply with section 945A). Hence, superannuation trustees relying on the Class Order can provide personal financial product advice without determining the client’s relevant personal circumstances (“knowing your client” requirement), or considering and investigating the subject matter of the personal advice (“knowing your product” requirement). The superannuation trustee is also exempted by the Class Order from the section 945A requirement to provide appropriate advice. FoFA Best Interest Duty obligations replace s945A of the Corporations Act. Class Order 09/210 has not been repealed by ASIC at the time of writing this submission.

⁵ The MySuper Bill legislates the ability for a superannuation fund to charge superannuation fund members this fee collectively.

Indeed, Industry Super Network (**ISN**) has been very outspoken about these very types of fees and costs. A sample of ISN's comments on these matters follow:

"these members are not informed (advice fees are not disclosed but bundled as administration cost) of the service they are paying for but not necessarily receiving⁶"

ISN asserts that payments (namely commissions) of the following nature are conflicted and has on numerous occasions recommended they be banned:

"such fees are ongoing in nature and therefore not necessarily reflective of the advice received⁷";

"cause a conflict of interest because the adviser is paid by the product provider not the client, and so will only be paid for recommending a certain product⁸";

"are economically inefficient in the sense that they are not tied to the provision of quality of advice – commissions are paid irrespective of ongoing provision of advice services⁹"; and

"commissions are often justified as being a cost effective way for consumers to pay for advice, particularly for lower income consumers. ISN has long challenged this view due to the ongoing nature of commissions and the fact that commissions are paid irrespective of whether ongoing advice is provided¹⁰".

A superannuation trustee (or advice licensees to whom a superannuation trustee outsources the advice function) will continue to provide conflicted advice because the advice provider can only advise the client with regards to one related party product. As ISN has previously stated:

"Wherever a client is given advice, and that advice is skewed towards particular products due to related party interests... their financial outcomes are very likely to be diminished"¹¹.

To be clear, the FSC welcomes the removal of legislative barriers that prohibit (directly or indirectly) the financial advice industry from providing piece-by-piece (or scaled) advice or for a superannuation fund or other product provider to offer simple advice.

However, the FSC submits that the proposed framework supporting the provision of Intra-Fund Advice is entirely inconsistent with the policy rationale underpinning the FoFA and MySuper reforms.

The proposed framework permits an advice fee to be bundled with a product administration fee and to be charged to all members of a superannuation fund regardless of whether the member accesses any advice.

⁶ *Industry Super Network Submission* to the Parliamentary Joint Committee on Corporations and Financial Services, August 2009.

⁷ Ob Cit, pg 18.

⁸ Ibid, page 9.

⁹ Ob Cit.

¹⁰ Ibid, page 13.

¹¹ Ibid, page 12.

In our view, this framework is at odds with the Minister's second reading of Bill 2 in Parliament, where he said:

"It is only by ensuring that advisers' only source of income is from their clients that clients can be sure that the adviser is working for *them*, rather than a product provider.

For the most part, advisers will not be able to receive remuneration (from product issuers or from anyone else) which could reasonably be expected to influence financial advice provided to a retail client."

Cost of intra-fund advice

Proponents of Intra-Fund Advice often argue that it is relatively inexpensive, especially when assessed at a member, rather than whole of fund, level.

Indeed, the submission of the Association of Superannuation Funds of Australia Limited (**ASFA**) to the Parliamentary Joint Committee on Corporations and Financial Services' 2012 inquiry into FoFA argues that given the costs are relatively low on a per member basis, the benefits of this form of advice merit its provision on a collective basis. That is, the argument for non-transparent, non-FoFA compliant advice fees to be bundled in the product administration fee of a superannuant's monies is that the cost of the service is low.

The FSC does not share this view. For the reasons outlined above, we believe a preferable approach would be to adhere to the principles underpinning the FoFA and MySuper reforms and facilitate scaled advice on a product and channel neutral basis.

Importantly, the FSC has always supported the provision of general advice (factual information) from a superannuation fund about a member's interest in that superannuation fund. Allowing this form of general advice to be provided, while at the same time developing a product and channel neutral scaled advice framework, would better achieve the policy objective of increasing the availability of simple and cost-effective advice without creating an uneven playing field and compromising the underlying principles behind these reforms – including transparency for consumers.

The FSC has conservatively estimated that the provision of Intra-Fund Advice by all superannuation providers would result in approximately **\$405 million** per annum being deducted from all superannuation fund member accounts.

Significantly, the Cooper Review found that 80% of members are disengaged. On this basis, it is reasonable to conclude that up to **\$324 million** (80% of **\$405 million**) is being paid by disengaged members who are not receiving any advice – but who are nevertheless cross-subsidising personal advice being received by the remaining 20% of fund members

COST OF INTRA-FUND ADVICE**Methodology**

1. Compulsory provision of Intra-Fund Advice.
2. Cost of IFA: ASFA's submission to the Parliamentary Joint Committee, 25 November 2011, page 3 states that "expenditure on financial planning services varied from \$0.65 a year per member to \$26.25". Selecting the mid-point, approximately \$13.50 per year is paid by members for IFA.

An IFA cost of \$13.50 per year equates to \$0.26 per week, per account. FSC believes this is a conservative estimate on the basis that increasing amounts of personal advice will be provided in the future – driven by retention motives and an aging member base – resulting in higher overall IFA costs.
3. Account numbers: Approximately 30,000,000.
4. IFA is charged as part of the administration fee which is levied on every account (as opposed to a unique member).

Total cost to superannuation fund members is approximately \$405 million per annum – regardless of whether the superannuation member accesses the advice.

2. Intra fund advice regulation should relate to the advice permissible by s99F of the SIS Act

On the basis that the government has enacted Intra-Fund Advice and is now making amendments to FoFA to exempt Intra-Fund Advice from certain FoFA elements, we note the following amendments are required to consistently align these regulatory changes with the conditions enacted in recent MySuper Acts (namely the Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Act 2012).

As stated in the Minister's 8 December 2011 media release No.164, Intra-Fund Advice is not "personal advice" but:

"Intra-fund advice will cover any general advice or personal advice provided within the sole-purpose test. However, there will be new restrictions on the types of advice that can be provided under intra fund advice rules. Specifically, the following are excluded:

- *Advice relating to whether the member should consolidate their existing superannuation accounts*
- *Advice to switch the member away from the superannuation fund into another superannuation fund except to the extent the advice relates to moving the member from an accumulation product into a retirement product offered by the same registrable superannuation entity*
- *Advice that contains recommendations in relation to financial products that the member holds outside of superannuation*
- *Advice in relation to investment choice outside of the trustee-prescribed investment options."*

Therefore, the "product fee" definition proposed by subregulation 7.7A.10(3) needs amendment to amend the definition of a product fee and secondly to define or be specific about the type of advice which will be exempted from the Opt-in measure.

According to the intent of the proposed regulations, a product fee is not an ongoing fee and may be passed onto other members (cross-subsidised) where it relates to a restricted type of personal advice.

Intra-Fund Advice is narrower than "personal advice"

Section 99F of Further MySuper and Transparency Measures) Act 2012 and s99F of the Superannuation Industry (Supervision) Act (SIS), defines Intra-Fund Advice narrower, as announced by the government, than broadly "personal advice" to a retail client as contained in proposed sub-regulations 7.7A.10(3)(b), by stating that the Trustee must not directly or indirectly pass on the cost of providing advice onto other member to the extent the advice is personal advice and provided in the circumstances in Section 99F(1)(c):

“S99F(1) (c) the advice is provided in any of the following circumstances:

(i) the subject member has not yet acquired a beneficial interest in the fund when the advice is given, and the advice relates to whether the subject member should acquire such an interest;

(ii) the advice relates to a financial product that is not a beneficial interest in the fund, a related pension fund for the member and the fund, a related insurance product for the member and the fund or a cash management facility within the fund;

(iii) the advice relates to whether the subject member should consolidate that member's beneficial interests in 2 or more superannuation entities into a beneficial interest in a single superannuation entity;

(iv) at the time the advice is provided, the subject member reasonably expects that a person mentioned in subparagraph (a)(i) or (ii) will periodically review the advice, provide further personal advice or monitor whether recommendations in the original or any later advice are implemented and the results of that implementation;

(v) other prescribed circumstances.”

Paragraph 1.42 of the revised Explanatory Memorandum to the Further MySuper and Transparency Measures) Act says:

*“In recognition of the importance of retirement savings not being eroded through excessive fees, **the amendments place specific restrictions on the types of personal advice that superannuation trustees can charge across their membership as intrafund advice.**”*

Recommendation

The FSC submits that sub-regulation 7.7A.10(3)(b)(i) used of “personal advice” is too broad and not in accordance with the government’s policy as announced by Minister Shorten media release 164 “Improving Access to Simple Financial Advice”, 8 December 2011 and with the Law and SIS.

Sub-regulation 7.7A.10(3)(b)(i) could be amended to use “intra-fund advice” in place of “personal advice”. Intra-Fund Advice may need to be defined.

Alternatively, the sub-regulation could mirror 99F of Further MySuper and Transparency Measures) Act 2012 and s99F of SIS by narrowing “personal advice” to exclude the following types of advice from being provided in a collective manner:

S99F(1)(c) the advice is provided in any of the following circumstances:

- (i) the subject member has not yet acquired a beneficial interest in the fund when the advice is given, and the advice relates to whether the subject member should acquire such an interest;*
- (ii) the advice relates to a financial product that is not a beneficial interest in the fund, a related pension fund for the member and the fund, a related insurance product for the member and the fund or a cash management facility within the fund;*
- (iii) the advice relates to whether the subject member should consolidate that member's beneficial interests in 2 or more superannuation entities into a beneficial interest in a single superannuation entity;*
- (iv) at the time the advice is provided, the subject member reasonably expects that a person mentioned in subparagraph (a)(i) or (ii) will periodically review the advice, provide further personal advice or monitor whether recommendations in the original or any later advice are implemented and the results of that implementation;*
- (v) other prescribed circumstances.”*

3. Ability to pass on the 'fee' under section 99F

The FSC submits that sub-regulation 7.7A.10(3)(b) is also narrowing the government's intent as evidenced by the enacted amendment to SIS at section 99F(1) and section 99F(1) of the Superannuation Legislation Amendment (*Further MySuper and Transparency Measures*) Act 2012. We submit that the proposed regulations be redrafted to replicate or incorporate s99F(1)(ii) (from both the Law and SIS, both quoted below).

Both the Further MySuper and Transparency Measures Act 2012 and SIS (quoted following) do not permit the "passing on" directly or indirectly the cost of providing intra fund advice to another member of the fund under certain conditions. In Section 2 previously, we noted what type of advice needed to be provided. In this section we highlight that s99F of SIS and *Further MySuper and Transparency Measures*) Act 2012: 99F Cost of financial product advice also permits the advice to be provided by 'another person acting as an employee of, or under an arrangement with, a trustee or trustees of the fund'.

Further MySuper and Transparency Measures) Act 2012: 99F Cost of financial product advice

*(1) The trustee or the trustees of a regulated superannuation fund must not directly or indirectly pass the cost of providing financial product advice in relation to a member of the fund (the **subject member**) on to any other member of the fund, to the extent that:*

(a) the advice is provided by:

(i) a trustee of the fund; or

(ii) another person acting as an employee of, or under an arrangement with, a trustee or trustees of the fund; and

Superannuation Industry (Supervision) Act: Section 99 Cost of financial product advice

*(1) The trustee or the trustees of a regulated superannuation fund must not directly or indirectly pass the cost of providing financial product advice in relation to a member of the fund (the **subject member**) on to any other member of the fund, to the extent that:*

(a) the advice is provided by:

(i) a trustee of the fund; or

(ii) another person acting as an employee of, or under an arrangement with, a trustee or trustees of the fund; and

However, the proposed sub-regulations in 7.7A.10 (3) refers to “cost that may be passed”. It remains unclear what cost/fee may be passed on, from whom and to whom?

It is assumed that the “passing on” provided in the proposed sub-regulation 7.7A.10(3)(b) refers to the ability to cross subsidise the intra-fund advice cost across all members of the superannuation fund.

Recommendation

We submit that the proposed regulations should clearly state what product fee may be “passed on” to be exempted from the Opt-in provisions.

However, s99F(1) also refers to passing on and in light of s99F(1)(i) and (ii), we submit that there needs to be clarity regarding the ability of a Trustee to pass on the fee to “*another person acting as an employee of, or under an arrangement with, a trustee or trustees of the fund*”.

Whilst these proposed regulations will align if adjusted with the Further MySuper and Transparency Measures Act 2012 and SIS – we submit that “passing on” the product fee defined in these proposed regulations falls foul of the Conflicted Remuneration provisions of FoFA and as such makes Intra-Fund Advice unworkable where the payment of the product fee in part or whole to another person acting under an arrangement with, a trustee or trustees of the superannuation fund.

That is, there is currently NO legal provision or exemption which enables a trustee or trustees of a regulated superannuation fund paying or enabling the party under an arrangement with trustee(s) to be paid for the provision of the intra-fund advice services. The respective laws only permit a superannuation trustee to collectively charge members for the provision of the services and to exempt the product fee collected from the “Opt-In” measure.

Recommendation

The FSC submits that there remains a legislative gap between the MySuper Acts and FOFA to allow for a regulated superannuation trustee(s) to pay and for third parties under an arrangement with the regulated superannuation trustee(s) for the provision of intra-fund advice without breaching Division 4 of Part 7.7a of FoFA. The FSC submits this may be remedied by way of regulation by providing an exemption to parties in s963B of the Corporations Act. The FSC is happy to provide drafting to enable this amendment to be made.

TECHNICAL ISSUE

Note to sub-regulation 7.7A.10(3)(a)

The FSC submits the example provided to illustrate a product fee for the management and operation of a financial product should be one relevant to regulations. That is, a basic deposit product is not relevant to these regulations and should be replaced with a superannuation fund or managed investment scheme.

Further, the FSC queries the use of different and undefined terminology used in sub-regulation 7.7A.10(3)(a), namely “management and operation”.

Division 5 of the *Superannuation Legislation Amendment (MySuper Core Provisions) Act 2012 No. 162, 2012 section 29V (1)-(3)* defines and uses “administration fee¹²” and “investment fee¹³”. We submit the same terminology should be used in these regulations.

Recommendation

The FSC submits the Example included to illustrate sub-regulation 7.7A.10(3)(a) should be deleted and replaced with the following:

“A monthly administration and/or investment fee charged by a superannuation fund or a managed investment scheme”.

¹² S29V(2) defines an administration fee as “An **administration fee** is a fee that relates to the administration or operation of the fund and includes costs incurred by the trustee, or the trustees, of the fund (that are not otherwise charged as an investment fee, a buy-sell spread, a switching fee, an exit fee or an activity fee).”

¹³ S29V(3) defines an investment fee as “An **investment fee** is a fee that relates to the investment of the assets of the fund and includes:

(a) fees in payment for the exercise of care and expertise in the investment of those assets (including performance fees); and

(b) costs incurred by the trustee, or the trustees, of the fund (that are not otherwise charged as an administration fee, a buy-sell spread, a switching fee, an exit fee or an activity fee).”