3 June 2022

Quality of Advice Review Submission

About Adviser Ratings

Adviser Ratings launched in October 2014, in the wake of the Future of Financial Advice reforms (FOFA), and the scandals of the time. Adviser Ratings' vision is to improve the penetration of advice among Australian consumers. There are more than 16,000 financial advisers on the Adviser Ratings independent platform, enabling consumers to browse and search for an advice solution suited to their needs, with advisers rated and reviewed by other consumers.

Adviser Ratings is also a unique data and insights company, built on Australia's only financial ratings platform. We help financial services businesses make data-driven decisions in engaging their ideal audience, by supplying leading industry insights, data services and research. Our clients are key players in the wealth management industry including advice licensees, super funds, life insurers, fund managers, investment platforms and software providers.

Recommendations

1. Embed an Adviser Quality Score (AQS) to help measure the improvements of advice and adviser quality using external qualitative and quantitative data sources.

2. Differentiating advice dispensed by social influencers or other media commentators from approved financial advisers through a unique symbol / trademark.

3. Tax deductibility for all financial advice by an approved financial adviser of up to $3,000 per year.

4. Redefining the "sophisticated investor" definition to help with consumer protections, to $300k annual income for two years and/or $5 million in assets as the first of a two-stage process in establishing a new definition and requirements test in the future.

Recommendation 1 – Adviser Quality Score

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Over the past three years Adviser Ratings, along with industry and academic experts (UNSW, WSU), have created the Adviser Quality Score (AQS). The AQS represents insights gained through roundtable discussions with industry participants, academic research, and qualitative and quantitative analysis. The score rates every adviser/broker in Australia on a scale of 300-1200. It is akin to a credit score when assessing credit quality of consumers – assessing the likelihood of that consumer going into default.

The predictive nature of these scores will allow the industry to determine quality of each adviser. Quality can be defined as:

- Quality of financial advice dispensed
- Likelihood or not of misconduct or other negative risk factors, such as director history
- Satisfaction of clients.

Data has been analysed from multiple sources and a proprietary scoring framework overlayed and mapped against different advisers. These data sources have initially been sourced from: Australian Bureau of Statistics, Adviser Ratings, ASIC, Equifax, FASEA, and the Australian Financial Complaints Authority.

For licensees, the AQS helps provide a benchmark to complement its own internal reporting of where any potential risk resides under their licence.

For industry providers, the AQS helps them evaluate counterparty risk with advisers or licensees, and how their solutions may help reduce risk and increase the AQS of particular licensees and advisers.

For advisers, the AQS helps them understand what constitutes advice quality, or the risk of an adverse event among their peers, practice, or licensee.

Since the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, the AQS has improved, with a few organisations, such as licensees, asset managers and superannuation funds embedding it in their assessment criteria when partnering with advisers for both distribution and compliance purposes.

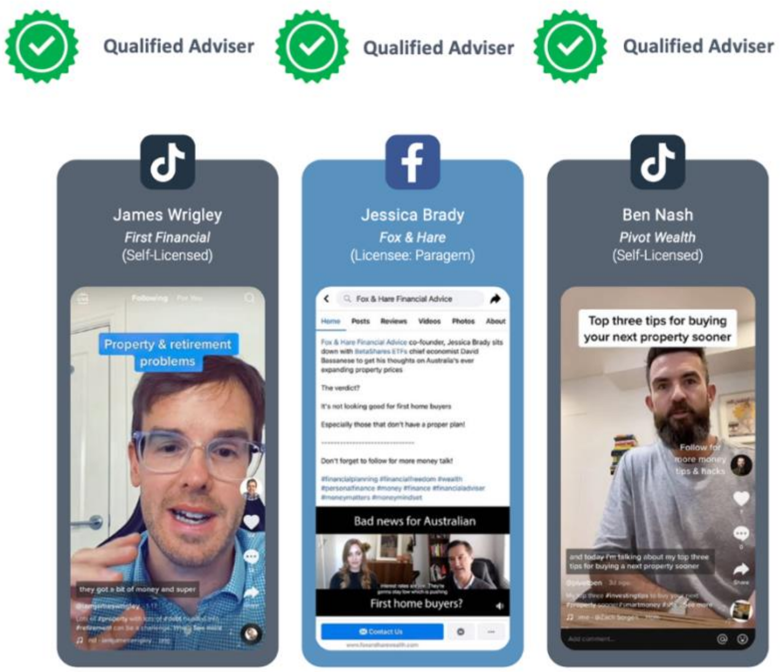
> The recommendation is to support an industry-wide quality metric score such as the AQS and an index, the Adviser Quality Score Index (AQSI), so the industry can independently assess whether certain legislative changes and instruments are being effective. The score is intended to be refined over time as more data is made available and / or contributed by the industry into a central repository pool.
>
> Individual AQS should be tested over a period of 6-12 months and then assessed on whether they become available to clients or consumers.

Recommendation 2: Distinguishing qualified financial advisers through a unique mark

Many social media finance influencers and financial commentators provide an accessible service to inform consumers on how to better manage their money. Whilst debate currently resides around consumer protections and risks around those who dispense product advice, in the absence of the regulators' ability to monitor and manage every publication and social media platform, we think a more effective, efficient, and less costly solution is to promote real financial advisers. An industry-wide trademark / logo / tick unique to the advice profession could be a way for consumers to immediately identify an approved financial adviser.

Like the national Heart Foundation Tick implemented 26 years ago, it would provide consumers a quick check on whether they are seeing a approved adviser or reading / reviewing content from an approved adviser. Pursuant to Recommendation 4 below, we would also recommend a distinction between a wholesale adviser and a retail adviser, so consumers are aware of which protections they are afforded.

Figure 1 – Example of distinguishing types of advice dispensed



The recommendation is to implement a symbol / tick or logo for every approved financial adviser, which they can use as distinguishing mark in social media and on other channels.

Recommendation 3: Tax deductibility for all financial advice

Advice costs have increased by more than 40% in three years, and the number of Australians with an adviser are at all-time lows, with only 10.1% of adult Australians seeing a financial adviser, or 1.9 million people (*Adviser Ratings Advice Landscape Report*, Adviser Ratings, 2022). To offset this cost, Adviser Ratings recommends tax deductibility for the full gamut of financial advice, including costs incurred to establish a plan, or for advice that does not relate to assets or investments that presently generate taxable income. Currently these parts of advice are not tax deductible.

Referencing the 2019 Australian per capita GDP, the potential increase to Australians if everyone was able to access properly implemented professional advice would be equivalent to $24,716 per person, per year – or an aggregate annual contribution equivalent to $630.26 billion (*The Value of Advice Research Report*, CPA Australia, 2021). As such, by allowing for tax deductibility across the full spectrum of advice, the benefits to the economy more than outweigh the tax effects. With median fees of advice at $3,526, we believe a sensible rate of $2,000-$3,000 in tax deductible expenses for every Australian who sees an approved financial adviser.

The recommendation is tax deductibility of up to $3,000 per annum per person from a qualified financial adviser, as defined by the definition of financial adviser in the *Corporations Act*.

Recommendation 4 – Sophisticated investor limits to be redefined

The sophisticated advice definition of $250,000 in salary for two consecutive years or $2,500,000 in assets has not been updated in 20 years. In that time, property prices have increased 6.8% annually, or more than 400% (CoreLogic, 2021).

Consumer impacts on this definition are far reaching, with schemes such as Mayfair 101 leaving many "sophisticated" Australians without consumer protections. There is a significant disconnect between financial knowledge and awareness, and the definition of sophisticated.

We believe the definition needs to be considered in a far more holistic way. This could be the removal of one's own house from the sophisticated investor definition, a basic fact find or knowledge test when assessing which product to invest in, or investment limits based on asset size.

In the interim, we believe a two-phased approach can be adopted, by immediately implementing an increase in the wholesale definition limits, before a phase two approach of working through other mechanisms that are more meaningful to the term "sophisticated investor" and hence wholesale advice. As part of the increase in the limits, we would expect wholesale advisers who are advising clients under the proposed limits would be reclassified as retail advisers and be subject to the same legislation requirements that exist today.

The recommendation is to increase the sophisticated limit definition to $300,000 salary for two consecutive years or $5million in assets, before adopting a 2nd phase evaluation of the definition. Current wholesale advisers advising within these new limits would be reclassified as retail advisers.

We welcome any feedback or dialogue on this submission. It represents a snapshot of further detailed work undertaken by Adviser Ratings and it partners.

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