



Submission to the  
**Parliamentary Joint Committee on Corporations and  
Financial Services**

**Proposals to lift the professional,  
ethical and education standards in the  
financial services industry**

5 September 2014



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## About the Superannuation Consumers' Centre

In early 2012 the consumer organisation CHOICE convened an establishment committee for a Superannuation Consumers' Centre. The committee included former Macquarie Bank CEO Allan Moss, Former Vanguard CEO and Financial Services Council Chairman Jeremy Duffield, and former ASX and ASIC Chairman Tony D'Aloisio amongst others. In August 2012 the committee took a proposal to Government to provide a one off contribution to an investment fund to provide an endowment to fund the Centre for 20 years. The Government agreed to make a \$10million contribution, provided the industry matched that contribution. While a number of major funds agreed to contribute the committee did not raise the matching \$10million prior to the 2013 election.

Nonetheless the Superannuation Consumers' Centre has established itself as a legal entity, has received ACNC endorsement and is operating on a limited voluntary basis. The Centre aims to make a positive contribution to restoring trust and confidence in the superannuation industry. It will work to improve the operation of the superannuation and retirement income system so that it delivers the best possible retirement income for Australian consumers.

Given that the Centre is operating without funding, it is only able to provide limited input to Government policy processes, including this review.

The business case for the Centre remains relevant. Trust and confidence in the industry is lower than it should be. This is producing suboptimal outcomes for consumers, government and industry. No one policy response will solve this problem but **the establishment of a dedicated Superannuation Consumers' Centre is an important part of a suite of measures discussed in this submission.**

**We urge the committee to** support development of the Superannuation Consumers Centre via recommending that it receive:

- **specific listing in the Tax Act to enable the Centre to receive deductible gifts** from those in the community who support it; and/or
- **a tiny portion of the superannuation levy to support it, and/or**
- **Government seed funding.**

## Summary

<p>1. the adequacy of current qualifications required by financial advisers;</p>	<p>Education standards fall well short of consumer expectations and well short of the standards required to create an advice profession.</p> <p>Our preferred framework is:</p> <p>a) Minimum entry level standards in the form of a university degree combined with specialised learning assessed via a national capstone exam.</p> <p>b) Specialist accreditation standards for particular kinds of advice example for retirement income advice, structured products, hybrids etc</p> <p>c) Continuing professional development obligations.</p> <p>This framework could be oversighted by a self-regulatory body consistent with ASIC's regulatory guidance on governance of self-regulatory bodies set out in RG 183 (codes) and RG 139 (complaint schemes).</p>
<p>2. the implications, including implications for competition and the cost of regulation for industry participants of the financial advice sector being required to adopt:</p> <p>a) professional standards or rules of professional conduct which would govern the professional and ethical behaviour of financial advisers;</p> <p>b) professional regulation of such standards or rules;</p>	<p>Costs of regulation have to be weighed against the benefits. We have a crisis of confidence in the financial advice sector. At the same time we have an underdeveloped retirement incomes system that effectively forces consumers to obtain financial advice. Given the compulsory nature of the super system government has an obligation to ensure high standards of advice.</p> <p>Black letter regulation is generally regarded as more costly and less flexible than self-regulatory options or co-regulatory options. The financial services industry has a reasonable track record of self/co-regulation.</p> <p>Professional standards must deal with the key drivers of loss of trust and confidence in the sector - conflicts of interests, low education standards and the lack of a last resort compensation mechanism.</p> <p>Option A</p> <ul style="list-style-type: none"> <li>ASIC oversight of competency standards by way of national</li> </ul>

	<p>capstone exam and</p> <ul style="list-style-type: none"> <li>ASIC approval professional and ethical standards in accordance with RG183</li> </ul> <p>Option B</p> <p>The establishment of an <b>industry-based, professional and competency standards body</b>.</p> <p>Key elements include:</p> <ul style="list-style-type: none"> <li>Governance by an independent chair and equal numbers of consumer and industry representatives</li> <li>Three yearly independent reviews</li> <li>Adequate funding.</li> </ul>
3. the recognition of professional bodies by ASIC	<p>We support strong professional bodies. We do not support ASIC recognition or approval of industry bodies.</p> <p>It would be a form of endorsement of the regulated community by the regulator and would be confusing to consumers.</p> <p>There would be reputational contagion for the regulator if a “recognised” association subsequently fell short of community expectations.</p> <p>There would be an inherent perception of a conflict of interest in that the regulator would be oversighting both members of the association and the association itself.</p> <p>Such an approach would require the construction of new and very broad regulatory guidance which would ultimately be complex to administer due to the wide nature of activities undertaken by industry associations.</p>

## Towards an advice profession

The integrity of the super system depends on the emergence of a high quality advice profession.

What might a professional look like?

A **highly educated** workforce— both at entry level and higher learning accreditation programs alongside life-long education through continuing professional development

**Strategy and analytical advice** would be the primary offering with product recommendations a secondary consideration and implementation a distant third – strategy and analysis will be what consumers will primarily pay for.

The **client's interests will be front and centre** –conflicts of interests would disappear including asset based charging, there would be **structural separation between product and advice**.

**Fees will be completely transparent** – not concealed by percentages or charges that change with market movements. They will be appropriate to the level of training, skill and expertise of the adviser and the complexity of the task, and **formal consent will be obtained**. Not two yearly under opt-in rules but annually if there is an ongoing advice relationship.

The quality of any profession depends on its **professional associations**. These would lead the profession in the attainment of high standards, actively helping members reach these standards and better manage the rump of the industry.

More must be done to facilitate the development of an independent trusted advice profession and the work of this Committee is an important step.

The foundations of a profession - a concept built up over centuries - generally encompasses three core elements:

1. High levels of technical proficiency; and
2. High standards of ethics - stemming from higher duties to clients – usually a fiduciary duty – which arises when one party is highly dependent on the other, a fiduciary duty requires to advice giver to act in the client's best interest
3. Client care from beginning to end of relationship ie fulfilment of promises

## 1. Competency standards - adequacy of current qualifications for advisers

### 1.2 Technical proficiency derived from significant body of learning

Professionals earn their status through a recognised standard of technical and ethical education and learning. This starts with entry level standards, specialist accreditation for higher learning, and lifelong learning.

In terms of the current framework the bar is too low at all steps of the way – both at entry level training and ongoing requirements – but critically it doesn't **consistently** deliver good outcomes – outcomes depend on the licensee and/or training provider.

We have is extreme diversity in practices – people entering the industry with quality finance, economics, business, accounting and/or auctorial university degrees, followed by high quality training provided by some licensees on one hand. Yet others enter following completion of a short course offered by RTOs with no prior learning. As some say five months to become a financial planner five years to be a hairdresser.

Five months is an improvement on the recent past when entry to the industry to the industry was possible via even shorter courses however a five or ten month course that has no prior educational or experience requirements falls well short of the body of technical proficiency and learning required of a profession or indeed for the sort of fees the industry charges consumers. Courses such as the one below<sup>1</sup> provided by the Registered Training Organisation Monarch are completed in around “five to eight months”<sup>2</sup> with no prior learning required. No high school completion, no prior relevant work experience. And they offer price matching! Assessment involves four multiple choice quizzes and four assignments. No exams.

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<sup>1</sup> Available at <http://www.monarch.edu.au/courses/financial-planning/diploma-financial-planning/>

<sup>2</sup> According to advice given over the phone on 18 March 2014

### Diploma in Financial Planning – Detailed Pricing

You can choose to enrol in the FULL Diploma of Financial Planning or alternatively you can enrol in just individual units (see prices below). There are substantial savings when enrolling in the Full Diploma of Financial Planning.

Diploma units	Distance (self paced) Education	Face to Face (workshops)^
DFP1 Foundations of Financial Planning	\$475	\$950 – 2 days
DFP2 Investments	\$475	\$950 – 2 days
DFP3 Superannuation & Retirement Planning	\$475	\$950 – 2 days
DFP4 Insurance & Risk Management	\$475	\$950 – 2 days
<b>FULL Diploma</b> Enrol in the FULL Diploma and save!!	<b>\$1,425 – we price match!</b>	<b>\$2,950 – 8 days – we price match!</b>
<b>HUGE SAVINGS</b>	<b>Quality education, now more affordable</b>	<b>Quality education, now more affordable</b>

**Entry to the industry falls well short of consumer expectations and well short of the standards required to create an advice profession.**

### 1.3 Competency/education standards

Professionals earn their status through a recognised standard of education and learning. This starts with entry level standards, followed by specialist accreditation for higher learning, followed by lifelong learning.

The current framework sets the bar is too low at all steps of the way – at entry level training and ongoing requirements.

What we have is extreme diversity in practices – people entering the industry with quality finance, economics, business, accounting and/or auctorial university degrees, followed by high quality training provided by some licensees at one end and short courses offered by RTOs with no prior learning at the other end.



There is a crisis of confidence in the community about financial advice. This is driving an appetite in the industry for reform as recent announcements by the CBA and AMP have shown. Last month the CBA announced<sup>3</sup> new minimum education standards for its financial planners, supervisors and managers of planners.

The new education standards include:

- All new CFP financial planners, direct supervisors or managers must hold a degree in finance, business, commerce or a related field;
- Existing financial planners and their supervisors will be required to hold either an Advanced Diploma in Financial Planning (or equivalent) or a degree in finance, business, commerce or a related field by 30 June 2017;
- Existing Senior Financial Planners will be required to obtain the CERTIFIED FINANCIAL PLANNER® certification with the Financial Planning Association of Australia; and
- CFP commits to making membership of a relevant financial services industry association a minimum standard required of all CFP financial planners by 30 June 2015.

In August AMP announced<sup>4</sup> all existing and new advisers must hold a Certified Financial Planner® (CFP), a Fellow Chartered Financial Practitioner (FChFP), or Masters in Financial Planning (MoFP) qualification with a five year transition timeframe.

These are welcome initiatives and suggest the industry may be capable of managing transition to higher standards without a black letter law approach.

Our preferred framework is the establishment of:

- a) Entry level standards that include a capstone exam: a university degree combined with specialised learning assessed via a national capstone exam. This would allow multiple pathways to entry to the industry.
- b) Specialist accreditation standards for example for retirement income advice, complex products (structured products, hybrids etc)
- c) Continuing professional development obligations.

This framework could be oversighted by either ASIC or an appropriately constituted and adequately funded industry based body. (see 3.4 below for details).

However whichever model is chosen we support a stakeholder governance model that **shares governance of the scheme equally with consumer representatives and industry stakeholders,**

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<sup>3</sup> CBA media release 18 July 2014

<sup>4</sup> <http://media.amp.com.au/phoenix.zhtml?c=219073&p=RssLanding&cat=news&id=1959641>

**oversighted by an independent Chair.** We note that ASIC's guidance documents on industry self-regulatory schemes<sup>5</sup> require governance to be shared amongst industry and consumer stakeholders in equal numbers. This model has proven its effectiveness over the last 20 years in the various financial industry complaint schemes and over the last 15 years in a number of financial services codes of practice<sup>6</sup>. It has not only driven increased community and trust in industry initiatives it has ensure schemes have kept pace with community expectations.

## 2. Professional standards

Professional standards are a key part of the development of a profession. Development and adherence to professional standards are a central way professional gain community trust. Development of professional and ethical standards must focus on the key drivers of loss of community trust in the sector, namely conflicts and the lack of compensation arrangements.

### 2.1 Conflicts

The crisis of confidence in the advice industry has number of causes but top of the list is conflicted remuneration models which have tainted advice and seen consumers lose their life savings.

#### Asset fees

FoFA did not remove all forms of conflicted remuneration and new forms of conflicted remuneration have replaced older models.

The dominant form of remuneration post FoFA is asset based fees or percentage fees.

Asset based fees incentivise advice towards assets from which a fee can be deducted. They work against the provision of strategic advice.

Percentage fees obscure the full cost of advice. They result in consumers paying too much and they erode savings as costs escalate over time.

Percentage based so called "fees" will stand in the way of professionalism because they are effectively commissions by another name.

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<sup>5</sup> See RG 183 and RG 139 discussed in more detail below

<sup>6</sup> Particularly the Banking Code of Practice and the (general) Insurance Code of Practice

While ever asset based charges are the dominant forms of charging the reputation of the whole industry will suffer and confidence will remain low.

### Aligned advice and cost

Alignments between advice and product makers create conflicts inconsistent with professional advice giving. Post FoFa new forms of conflicted remuneration have arisen, such as the balanced scorecard and very low platform licensing fees.

Banks have been subsidising advice for a very long time. Effectively general bank customers have been subsidising advice, which is predominantly sought by those with higher net worth.

Post FoFa new forms of subsidisation have emerged including very low licensing fees for platform access.

Any form of subsidisation by product makers of advice is conflicted remuneration.

It occurs for one reason. Product makers find it a profitable way to sell their products. Banks are willing to subsidise advice because it is a good way of selling their products.

While ever the banks, with 80% market share, subsidise advice conflicted remuneration models remain.

However the operation a white label platform or other preferred arrangements between advisers and product makers also create conflicts.

**Disclosure is not a policy solution to this problem.** Disclosure of conflicts has the perverse effect of increasing consumer trust<sup>7</sup>. Disclosure makes this worse! Therefore disclosure is not an appropriate tool for managing conflicts.

## 2.2 Compensation for loss

Professionals look after their clients from the beginning of the relationship to the end. Hence professions such as doctors and lawyers have developed various last resort funds to enable professionals to fulfil promises to customers when things go wrong.

The Financial Claims Scheme cover losses of banks and insurers, Part 23 of the SIS Act covers superannuation losses but consumers of investments and advice are on their own.

Professional standards must extend to caring for customers across the totality of the relationship.

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<sup>7</sup> The dirt on coming clean: The Perverse effects of Disclosing Conflicts of Interest  
<http://www.cmu.edu/dietrich/sds/docs/loewenstein/dirtclean.pdf>

We would support development of a last resort compensation scheme within a co-regulatory framework.

### 3. Regulatory options

Costs of regulation have to be weighed against the benefits. We have a crisis of confidence in the financial advice sector. At the same time we have an underdeveloped retirement incomes system that effectively forces consumers to obtain financial advice. Given the compulsory nature of the super system government has an obligation to ensure high standards of advice.

Black letter regulation is generally regarded as more costly and less flexible than self-regulatory options or co-regulatory options. The financial services industry has a reasonable track record of self/co-regulation as we set out below.

We note the industry is showing signs of coming to terms with the need to raise standards as shown by recent announcements by AMP and some of the major banks.

It may be that the climate is right for a co-regulatory approach rather than a legislative approach on these matters.

#### 3.1 History of co-regulation in financial services

Codes of practice, complaints and disciplinary schemes are the two main tools of self-regulation and the more mature parts of the financial services industry have a good track record in self-regulatory initiatives.

The Financial Ombudsman began its life as seven sector-specific industry-based disputes scheme, each created by the respective industry associations. Similarly the banking and insurance codes of practice have operated for some time with increasing success.

In the time since Wallis there have been three drivers of successful self-regulatory initiatives.

- 1) Governance arrangements that involve equal numbers of consumer and industry representatives with an independent chair
- 2) Periodic external review (usually every three to five years)
- 3) Approval of arrangements against agreed standards

Shared governance increases independence and consumer confidence. In practice it has proved highly effective, delivering a strong sense of stakeholder ownership and confidence in the impartiality of the scheme. Strong cultures of co-operation, respect and achievement have characterised these boards and difficult issues have been worked through together in a collegiate and timely fashion.

Periodic external reviews have provided an opportunity for users of the scheme to contribute very directly to its development. They have provided a strong accountability mechanism and ensured schemes continue to develop to meet the needs of their users. They have provided useful strategic guidance to Boards and management.

ASIC has developed regulatory guidance for both industry-based complaint schemes and industry based codes. Both RG 139<sup>8</sup> and RG 183<sup>9</sup> set out standards against which ASIC would assess and approve codes and complaint schemes. Importantly both require shared governance arrangements and periodic reviews.

RG 139 has proved particularly effective, largely because post Wallis financial services providers have been required to belong to an ASIC approved complaint scheme. This means operators of complaint schemes have been required to meet all the RG139 benchmarks.

However RG 183 which sets out guidance for developers of codes of practice has not delivered to the same level. While the content is more or less equal to RG139 no industry body has applied it to the same degree as complaint scheme operators have, probably because compliance is a choice rather than an obligation.

That said the banking code, general insurance, mutuals and insurance broking codes broadly meet its criteria even if they are bit slow with conducting and implementing the results of reviews. The biggest gap has been in the advice space, where no code has sought to meet the standards set out in RG 183, the biggest stumbling block has been the willingness to resource proper administration.

In summary RG 183<sup>10</sup> sets out important standards for effective codes. It builds on years of evidence and experience with self-regulatory codes and was updated as recently as March 2013 as part of the FoFA process.

It sets out criteria for five key features of successful codes:

- Processes used to develop codes (consultation especially of end users)
- The sort of content that should be included (eg not merely restate the law)
- Compliance and enforcement approaches
- Administration (independent, properly resourced)
- Periodic independent review.

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<sup>8</sup> [https://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/rg139-published-13-June-2013.pdf/\\$file/rg139-published-13-June-2013.pdf](https://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/rg139-published-13-June-2013.pdf/$file/rg139-published-13-June-2013.pdf)

<sup>9</sup> [http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/rg183-published-1-March-2013.pdf/\\$file/rg183-published-1-March-2013.pdf](http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/rg183-published-1-March-2013.pdf/$file/rg183-published-1-March-2013.pdf)

<sup>10</sup> *ibid*

RG 183 largely mirrors the ACCC's Guidelines for developing effective voluntary industry codes of conduct even though it predates the ACCC guideline. The ASIC document is clearer and consequently we have found it more useful to apply that the more generic ACCC document.<sup>11</sup>

We agree that self-regulatory initiatives have greater flexibility than the law to respond to emerging problems and this has been amply borne out by the various jurisdictional changes to the complaint schemes, most of which have occurred over 6 – 12 months periods. By comparison regulatory or legislative change can take years.

However in our experience self-regulatory initiatives work best when they sit within a co-regulatory framework such as currently exists with RG 183 (codes) and RG139 (complaint schemes).

They also work best when sponsoring organisations:

- have good coverage of the market and
- apply resources to monitor, publicise and enforce requirements.

### 3.2 Possible co-regulatory approach for education and competency standards

Within financial services there are a number of areas where industry codes could help improve consumer outcomes, **provided they sit within the RG 183 framework**. These include:

- life insurance commissions;
- management of conflicts of interest such as asset-based fees
- entry level, accreditation and continuing professional development standards
- other professional and ethical standards.

There is nothing inherent about these areas that lend themselves to improvement through industry codes. Rather we see self-regulatory initiatives as part of the evolution of the industry towards a profession. Ownership of standards that meet community expectations is fundamental to professional development.

However meeting the standards set out in RG183 is critical to success of any codes in these areas. A critical feature is the composition of the governing and administration bodies and the requirement for periodic review. Not only does this provide a structural way of ensuring community needs and concerns remain an ongoing part of the dialogue, but 25 years of experience with the industry based dispute schemes have shown their involvement is critical to community confidence in self-regulatory initiatives.

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<sup>11</sup>

<http://www.accc.gov.au/system/files/Guidelines%20for%20developing%20effective%20voluntary%20industry%20codes%20of%20conduct.pdf>

### 3.3 Professional associations

The quality of any profession depends on its **professional associations**. Ideally these would lead the profession in the attainment of high standards, actively helping members reach these standards and better manage the rump of the industry.

Professions typically have high industry association membership and we support incentives to encourage professional association membership, but fall short of supporting compulsory membership or ASIC endorsement of professional associations.

The financial planning industry is a long way from a mature profession and the community is not ready to trust it with oversight of its own standards process. Indeed it is the crisis of confidence in the industry that is driving moves to increase professional standards.

We note in recent years there has been a trend away from community trust in professions, including mature professions, to set and administer their own standards.

In the early 1990s the legal profession lost the right to full self-regulation. In 2006 the APES board was set up in response to concerns about the accounting profession's capacity to administer its own standards.

In addition we do not think it appropriate that the regulator accredit industry associations.

- It would be a form of endorsement of the regulated community by the regulator and would be confusing to consumers eg it would be difficult to explain that the regulatory endorsement extended to structures and processes rather than any particularly content or advocacy by an association.
- There would be reputational contagion for the regulator if an approved association subsequently fell short of community expectations or for example mounted an advocacy campaign that was at odds with community expectations or indeed the regulator's experience such as the recent opt-in debate
- There would be an inherent perception of a conflict of interest in that the regulator would be oversighting both members of the association and the association itself.

In addition such an approach would require the construction of new and very broad regulatory guidance which would ultimately be complex to administer due to the wide nature of activities undertaken by industry associations.

### 3.4 Our preferred path for raising competency (including at entry level) and professional standards

#### Option A

This option builds on existing infrastructure and follows a proven route.

This includes:

- ASIC oversight of competency standards by way of national capstone exam and
- ASIC approval professional and ethical standards in accordance with RG183

ASIC already has done considerable work to frame a **national exam (CP 153)** and has a framework in place for **approving codes of practice in RG183**.

The Financial Ombudsman currently provides **independent administration services** for four financial services code of practice and this could be easily be extended to oversight financial planning codes of conduct. Indeed the current code administrator has considerable expertise in the advice sector.

#### Option B

The establishment of an **industry-based professional and competency standards body** that complies with the governance and administration parts of RG183 and RG 139, namely that the Board is governed by a Board comprised of an independent Chair and equal number of consumer and industry representatives.

The Board should be responsible for both competency standards and professional and ethical standards.

This means it would have oversight over standards for entry to the industry, specialist accreditation continuing education, and the capstone exam.

It would also set professional and ethical standards and would have responsibility for ensuring they were appropriately administered and promoted by code owners.

The financial services industry has a reasonable track record with industry-based initiatives. Industry based initiatives have greater flexibility over legislated options in that they can flexibly respond to emerging problems.

Key elements of a new professional standards body must be:



- Governance by an independent chair and equal numbers of consumer and industry representatives
- Three yearly independent reviews
- Adequate funding.

End