

20th Dec 2011

Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra

Regarding the Joint parliamentary inquiry into the future of financial advice reforms

Dear Mr Bryant,

Thank you for the invitation to make a further submission to your inquiry.

I understand the Federal Government sees the importance of this profession being effective in helping Australians become more financially self-sufficient to provide for their own retirement and aged care.

Financial advice has a major role helping their clients to achieve this self-sufficiency, which is becoming more important now a greater proportion of Australians will be moving into retirement.

I have therefore addressed my comments to what I believe some of the long term effects to Australians becoming more self-sufficient in retirement will be should the proposed amendments become law in their current form.

In regard to the (Further Future of Financial Advice Measure Bill)

Submission on proposed amendments to the Corporations Act

PROPOSED AMENDMENT

In regard to : *require financial advisers to provide fee disclosure when charging fee longer than 12 months.*

Regarding an annual ongoing advice fee disclosure to retail clients.

Currently this is being done annually with the June 30th financial statements sent direct to clients from the product providers including administrative platforms.

These annual statements include adviser fees shown as separate amounts as part of the financial year statement.

EFFECT of this Amendment.

To have financial advisers duplicate fee disclosure is adding further administration costs and does not give clients any more information than they already are receiving.

Suggested change to ensure an efficient continual fee disclosure to clients.

Have all investment, superannuation and pension providers show the Advisers fee clearly on the annual financial year statements.

PROPOSED AMENDMENT

In regard to: *require financial advisers to provide fee disclosure statement and a renewal notice to a client when charging advice fees for longer than 24 months.*

Benefits of Current Fee practise :

The reasons why financial advisers structure advice fees as an ongoing service charge against a client investment which is paid monthly by the product provider.

1. Ongoing service fees are far more cost effective without the administrative costs of billing and eliminating fee loss through bad debts.
The savings help our industry to be more cost competitive with benefits flowing through to clients.
- 2 This ongoing service fee structure amortizes the true cost of advice over time so it's much more affordable especially to lower and middle income clients.
- 3 A further benefit of an ongoing fee charged against the client's investment is it aligns advisers interests more with our client's financial interests.
Both client and adviser benefit as clients savings and total financial strength increase.
- 4 The ongoing fee encourages the continued contact with clients for advice and education to address the many ongoing aspects that affect them financially such as,
 - A Regular Legislative changes to tax, super and pensions
 - B Stages of working life in managing mortgages and income changes
 - C Pre retirement planning
 - D Post retirement planning and income management to ensure superannuation pension income will continue much longer.
 - E Helping clients not make wrong decisions during financially volatile periods.
 - F Continual changes to products and platforms
 - G Ensuring any changes of address are notified to product providers to reduce lost accounts.
- 5 The use of ongoing service charge is making ongoing advice affordable for the client with a reduction of dependence on government support in later years.

EFFECT of this Proposed Amendment.

- 1 The impact of this proposed amendment will be far greater on independently owned financial practices and advisers, as opposed to Bank and Insurance company owned financial advice practices with employees or tied agents.
This is because independently owned financial practices cannot offset advice costs against the income generated through owning the investment or insurance products that clients will use.

Banks will also have the added advantage under the proposed amendments to recoup any bad debts given that clients will also be bank customers with bank accounts that can be billed.

- 2 Costs of advice will have to increase with the full cost being charged as an initial fee.
Should advisers attempt to use the asset service charge to offset part of the initial fee they can only count on this being in place for two years as it's expected many clients will not sign up to the renewal notice in 2 years' time.

Therefore it will not be possible to use an asset service charge to cover the advice costs as it takes more than two years to recover advice costs.

As an illustration.

A client invests \$10,000 and is charged a trail of 0.6% on this investment. This will pay the adviser \$60 per year or for two years \$120, assuming no change in value.

- 3 Large upfront fees will obviously be a disincentive for middle and lower income people to take advice.
- 4 There is also the increased risk of their specific financial plans and strategies that have been recommended being abandoned.
- 5 Financial planning is not a 2 year sprint.
Should this be a trend then it can be expected that greater government assistance will be needed in the future for the 2 year clients.
- 6 Long term effects will be fewer middle and low income Australians receiving financial advice.

Amortizing advice costs using an ongoing asset fee is the opposite of the large initial planning fee and upfront commissions.

Suggested change to ensure financial planning is affordable to all.

Remove the requirement for planners to have clients resign a renewal notice every two years to continue the charging of fees on their investments.

In place of this proposed amendment I suggest that all Adviser fees cease once clients funds become lost accounts.

PROPOSED AMENDMENT

In regard to : *extend the Australian Securities and Investments Commission licensing and banning powers used to supervise the financial services industry.*

My only comments on this amendment is that if it results in placing even more compliance requirements on the financial advisers then it will be a backward step.

No amount of further legislation to protect the public and clients will help if action cannot be taken prior to an offence being committed. We all know the good guys will just try to comply with whatever additional burden of compliance you put on them and for the bad guys they still bend the rules to the detriment of clients.

One of the main reasons for these proposed legislative changes was actions of Storm Financial which lead to the Ripoll inquiry.

In casual discussions with Advisers from other groups it seems a number of Advisers were aware of the extreme risks the investment strategy Storm was exposing their clients to long before the collapse.

Suggested change to enable ASIC to investigate prior to bad practice leading to a formal complaint.

I suggest that any change include the ability for ASIC to be able to check on organisations before things go wrong and an offense is committed. I suggest that should an organisation be found to be out of order and endangering clients financially then ASIC should allow to immediately step in and organise an ongoing rectification program to be allowed over a period of time to ensure correct practice.

PROPOSED AMENDMENT

In regard to : *require persons providing personal financial advice to retail clients to act in the best interests of the clients.*

It's important to define more closely what aspects advisers are expected to consider to properly act in the best interests of a client.

This will help removed much of the risk of varied interpretations making for operational difficulties.

My only comment is this proposed amendment confirms that advice must be thorough to comply and I cannot see it being cheap.

PROPOSED AMENDMENT

In regard to : *ban conflicted remuneration (including product commission), where licensees or their representatives provide financial product advice to retail consumers*

I don't see a problem with this as it applies at the adviser level.

Aspect of conflict of interests

However I see an aspect that could be overlooked that applies to the major companies (Banks and Insurance Companies) that have financial planning organisations with employed advisers or tied agents, giving financial advice.

These same major companies are developing an increasing number of investment products that can be recommended to retail clients.

Financial planning organisations all select a range of products for an "approved product list" which their advisers and agents must select from when recommending any investments to retail clients.

For major companies it is simple to bias this "approved product list" to include a greater proportion of their own products.

As investment products are profitable to their owners this advantage to increase the amount of investments in their products is attractive.

It also increases their ability to offset the costs of financial advice thus attracting more retail client investments.

There is a real conflict of interests for these major companies.

There is a second level in the conflict of interests,

With these major companies owning the retail investment products that invest into the Australian stock market, product investment managers could be directed to buy the shares of the parent company to influence the market prices of the parent company shares.

Independently owned financial advice practises don't own any of the products on their "approved products list" so do not have this conflict of interest.

Recommendation

Ensure it remains possible for independently owned financial practises to be viable so there is an alternative choice to bank employed advisers and insurance company tied agents for retail advice.

Independently owned financial practises cannot offset planning costs from profit owning the investment products recommended or used by retail clients.

Keeping efficient fee structures that are cost efficient with the cost of advice being able to be amortised over a period longer than two years is vital.

Suggested Change to proposed legislation

Remove the following requirement

: require financial advisers to provide fee disclosure statement and a renewal notice to a client when charging advice fees for longer than 24 months.

PROPOSED AMENDMENT

In regard to : *ban volume-base shelf-space fees from asset managers or product issuers to platform operators*

I have no problem with this proposed amendment.

Recommendation

No change to this proposed legislation

PROPOSED AMENDMENT

In regard to : *ban asset-based fees on borrowed amounts*

Not a bad proposal however being a response to the financial losses by retails clients of Storm advice it should be noted that banks were equally party to this risky arrangement.

Recommendation

No change to this proposed legislation

SUMMARY

Current proposed amendments will,

- 1 Significantly increase the cost of providing advice being a disincentive to middle and lower income Australians seeking financial advice.
- 2 Clients becoming 2 year clients dropping out of long term advice benefits.

The long term effect of these proposed amendments will be a reduction of Australians receiving advice to become financially more self-sufficient with more becoming Government dependent.

Please consider carefully

Yours faithfully

Rod Longmire