



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

Inquiry into the disclosure of commissions on risk insurance products

My Industry Background

I have been a financial planner for nearly 14 years. During that time I have seen many changes in the industry. One prominent issue that receives my full support is the disclosure of commissions and other 'soft dollar' benefits.

Although I am an Authorised Representative of a national dealer, I make this submission as an individual, in my own right. I feel strongly that the principle of Disclosure should be applied consistently across our industry, in order to provide better information to our clients and reduce the incidence of criticism and confusion. I fully support the recommendations of the Financial Planning Association¹ in this regard.

As a consumer, I like to make informed decisions; I believe I am entitled to know the full cost of goods and services I procure. I believe our clients are entitled to the same consideration.

I am not aware of any other industry in Australia that is regulated in respect to disclosure of fees and commissions, to the same extent as the financial planning industry. In spite of this, the industry continues to receive criticism from bodies such as the Australian Consumers' Association² because advisers receive remuneration based on commission. In principle, I believe these criticisms are unjustified, particularly when we are required to make full disclosure of these commissions in both percentage and dollar amounts.

Our requirements are totally unlike those of the real estate and motor vehicle industries where remuneration is also based on commissions. While these industries are focused solely on selling products, the financial planning industry focuses on strategies to address the overall financial needs and objectives of our client(s), with products being the means of achieving the objectives.

I believe the most effective way of overcoming some of the criticism directed to our industry is for financial planners to provide full disclosure and to be consistent across all sectors of the industry.

Insurance

Commission on Risk Products

Item 6.30 *

Many financial planning practices offer their clients the choice of commissions or 'fee for service', to avoid the possible criticism that could be associated with 'commission based remuneration', e.g. an adviser recommends Product 'A' over Product 'B' because the provider/fund manager of Product 'A' offers a higher rate of commission.

The primary issue should be to match the strategy and product to the client's needs and objectives, within their Risk Profile. If a product with a higher fee structure is more suitable, and therefore in the best interest of the client, that product should be recommended to the client, with the appropriate explanation and disclosures.

* Chapter 6 of the Report on regulations and ASIC policy statements

There is no doubt that a commission payment, deducted from the client's investment, impacts on the rate of return of the investment. This is a cost to the client, the same as if the client paid a fee for the service provided by the financial adviser.

In either case, the cost – commission or fee - initial and ongoing - must be disclosed.

I do not see 'fee for service' being offered in the 'risk' section of the industry.

Cost and Service – not commission – were the primary influences on consumers of risk products

Item 6.33 1st dot *

While the rate of commission may not affect the payout to the insured party, the amount of commission paid to an adviser is clearly a cost to the insurer and the insured. The amount of commission and other benefits to advisers, such as extravagant overseas trips, must add to the cost of premiums – cost being one of the factors the Committee considered.

In some cases, initial commissions are in excess of 100%; ongoing commissions are in the region of 30% pa. I believe many clients would be shocked by this high number.

Insurance 'agents' claim that their work can be very time consuming – following up applications, medical reports, etc.

This is no more time consuming than checking on superannuation entitlements, Reasonable Benefit Limits, advice from the Australian Taxation office, liaising with client's tax advisers, etc.

The comment that incentives to participate in overseas trips, (loosely called conferences) etc do not influence agents is, in my opinion, incorrect. However, this is an opinion that is very difficult to either prove or disprove. It is interesting to note that these 'conferences' are hosted by life companies rather than non-life fund managers.

If these benefits are simply a bonus/reward for business written, why do the (life insurance) companies offer additional points/incentives for writing business, particularly risk business?

While an investor's decision to work with a particular adviser and place investments with him/her should not be based solely on fees/price, this is a consideration and the investor should be aware of the fee/price in order to make an informed decision. This applies equally to 'risk' products as much as any other.

If there is nothing to hide from clients, why is there an issue?

A disclosure requirement for risk products would be detrimental to small business operators

Item 6.33 2nd dot *

A significant portion of the financial planning industry is comprised of small businesses. While I am an Authorised Representative of a large, national dealer, I own and manage my own financial planning practice. I am a 'small business operator'.

In the early 1990s, there was a similar concern among financial advisers that disclosure of commissions would force them out of business. Despite these concerns, the industry has continued to grow strongly.

* Chapter 6 of the Report on regulations and ASIC policy statements

I believe disclosure has

- Reduced entry fees and ongoing management fees on a wide range of products;
- Produced a more informed and questioning public;
- Provided a more competitive industry in which advisers provide clients with explanations of the benefits and suitability of the strategy and products recommended; and
- Encouraged advisers to provide a higher level of service to their clients.

I see no reason why the same should not apply in the risk sector of the industry.

Inconsistency in Disclosure Requirement

As an Authorised Representative of a Dealer Group, I am required to disclose any commission I receive from risk business.

Under the Insurance (Agents and Brokers) Act 1984, if I had a direct Agency Agreement with a life company and recommended exactly the same product to a client, I would not be required to disclose commission.

Where is the logic in this? It is a classic example of the inconsistency that has existed between financial planners who have not come from a 'risk' background and those who have.

Financial Planning Association (FPA)

The FPA is the pre-eminent professional body in the Australian financial planning industry. It "is committed to the universal disclosure of commissions and benefits for all financial products including investments, life, super, risk, borrowings and real property".¹

Practice Guideline No. 3 addresses the issue of disclosure of financial adviser fees and commissions. For many years, the FPA has promoted full disclosure of commission, fees and benefits in our industry in percentage and dollar terms. This information helps the client to make an informed decision about the effective cost of the product, be it superannuation, managed investments or risk products.

A contrarian view, proposed by the Association of Financial Advisers (AFA) and others, does not support disclosure where commission has no effect.³

I acknowledge that the end benefit for a trauma or income protection policy will be the same, regardless of the commission paid, because the client applies for a dollar nominated amount of cover. However, given that the commission is a cost to the insurer, and a significant cost as stated previously, I contend that the premium is influenced by the amount of commission.

In the current financial environment, where the public is encouraged to question and enquire about all forms of fees and charges by banks and other financial institutions, I believe clients are entitled to know the composition of the cost of their insurance and also the percentage and dollar amount payable to their agent/adviser.

Why does the 'risk' section of the industry want to be treated differently?

I strongly support the view in the Money Management editorial⁴, which states in part "if there is nothing wrong with commissions, why are they not being disclosed?"

Conclusion

In my opinion, the sole reason for 'non disclosure' of commission and other benefits is that the agents want to hide the amount of their 'total' remuneration – they do not want their clients and the public at large to know the extent of the benefits they are receiving.

I believe the Association of Financial Advisers **** may be acting more in the interest of 'insurance agents' than in the best interest of the public** and the financial advisory industry, providing the opportunity for more criticism. If this association wants to be part of the financial planning industry, it should accept the uniformity that is being promoted by the Financial Planning Association.

*** This association was originally the Life Underwriters' Association of Australia & New Zealand, then the Life Underwriters of Australia, then the Australian Lifewriters Association, until 1997 when it became the Association of Financial Advisers.*

Non-disclosure does nothing to benefit our industry and everything to harm it. I do not agree that remuneration based on commission is bad, but the details must be disclosed. This principle should be consistent and applied right across our industry and all industries where remuneration is earned in this way.

The FPA has issued a comprehensive Practice Guideline covering 'Disclosure of Financial Adviser Benefits & Other Charges Incurred by Clients' ¹. Item 1.5 is particularly worthy of note and states **"This commitment to full transparent disclosure enhances financial adviser's positioning as professionals because it puts beyond doubt that the financial adviser is acting in the client's interests and is not motivated by hidden rewards or incentives."**

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References:

1. FPA Practice Guideline – Disclosure of Financial Adviser Benefits & Other Charges Incurred By Clients - Practice Guideline No. 3 - 1 July 2000.
2. Address to the Funds Management World Conference (December 2002) by Louise Sylvan, Chief Executive, Australian Consumers' Association.
3. Para 6.32 - Report on regulations and ASIC policy statements made under the Financial Services Reform Act 2001.
4. "If you can't show the money, then change the system" - Editorial of Money Management, November 28, 2002