22 March 2019

Financial Services Reform Taskforce
The Treasury
Langton Crescent
PARKES ACT 2600

**Email**: FOFAGrandfathering@treasury.gov.au

Dear Sir/Madam,

**Re: Ending Grandfathered Conflicted Remuneration for Financial Advisers**

**In brief:**
AIST supports this exposure draft legislation which will see the end of grandfathered conflicted remuneration on financial products. We believe that the 2021 implementation date is too late, and this measure must be implemented as soon as possible. In the meantime, details of commissions must immediately be added to fee disclosure statements, and in the absence of compelling reasons for their continued exemption, risk insurance products must be included in this measure.

Recommendation 2.4 of the *Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* advised that conflicted remuneration in relation to retail clients should be removed as soon as is reasonably practicable. AIST welcomes the Government's decision to implement this recommendation and takes the opportunity to thank Treasury for the opportunity to consult on this exposure draft legislation (ED) which implements this. The ED proposes that grandfathering arrangements for conflicted remuneration and other banned remuneration in relation to financial advice are removed from 1 January 2021. The ED also provides for regulations which would see amounts which would have otherwise been paid as conflicted remuneration paid to affected consumers.

AIST supports these measures. However, we wish to make it clear in this submission that the implementation date of 1 January 2021 is too late. The Future of Financial Advice (FoFA) reforms which prohibited certain forms of conflicted remuneration from July 2013, were excluded from applying to existing arrangements that were in place prior to that date. This resulted in various clients of financial advisers continuing to have amounts of their investment remitted to their financial advisers with no oversight. In the case of certain providers, when the clients did not even have an assigned adviser, this amount would be pocketed by the provider with no disclosure, as the grandfathered commissions were never subject to the fee disclosure statement regime which was introduced as part of FoFA.

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The grandfathering provisions were introduced as part of the FoFA measures in order to ensure that contractual relationships between advice licensees and their representatives was able to stay in place for existing clients. Evidence provided by witnesses to the Royal Commission confirmed that the intention in relation to advice fees was that they would take over as clients were negotiated into new fee arrangements. It would appear that the retention of clients in commissioned arrangements is mainly caused by a lack of contact between advisers and we are not aware of evidence that would contradict this.

It defies belief that after this time there continues to be any clients of financial advisers, nearly six years after the implementation of FoFA, who are still in commissioned arrangements with arrangements unchanged. In the meantime, many retail clients – some of whom had started their existing arrangements prior to the commission disclosure requirements introduced by the Financial Services Reform (FSR) measures which were mandatory from March 2004 – may have never even seen the amount which they are paying their advisers.

The ED proposes that this situation ends on January 2021. This is nearly two years away, making it seven and a half years since the implementation of the FoFA reforms, with commissions still likely to make up a sizeable portion of income for advisers – many of whom may not even have been operating their practices prior to the FoFA reforms, and for whom an entitlement to grandfathered income from clients they had never advised is therefore highly questionable.

AIST recommends that commissions end as soon as reasonably practicable, as recommended by the Royal Commission. Two years is well outside this reasonableness test, and we would accept that the ban comes into force from July this year.

AIST additionally recommends that in the meantime, clients be provided with details of commissions in fee disclosure statements (FDS). ASIC's *Regulatory Guide 245 Fee Disclosure Statements* notes (in paragraphs RG 245.34-37) that commissions are not generally required to be disclosed in the FDS. Given that there is no functional difference between commissions and fees except for the degree of transparency, it is unacceptable that these continue to be obscured by a legal technicality between now and when they cease. Details should include amounts paid to advisers and/or licensees, as well as amounts retained by product providers which are not refunded to client accounts.

Additionally, AIST strongly urges that amounts which are currently being paid as grandfathered commissions – or equivalent amounts which are being retained by providers – be rebated in full to client accounts as soon as possible. We note that the proposed section 963N allows for regulations to be made to ensure that amounts that would otherwise have been paid are rebated to client accounts. We recommend that the regulations be consulted on at the earliest possible point in time to ensure that they can be implemented without delay.

We note that the ED is set to cover grandfathered commissions from investment products, but not risk insurance products. Recommendation 2.5 of the Royal Commission recommended that the cap on commissions for life risk insurance products be reduced to zero, unless a clear justification could be found to retain those commissions. We are not yet aware that such a justification has been found and would recommend that a deadline be given to the industry to provide one.

The continued exemption of risk insurance commissions highlights the existence of risk-only superannuation products which still pay large commissions to financial planners. The proceeds of rollovers from clients' other superannuation accounts at other funds to pay insurance premiums are routinely marketed to financial planners as an easy way to fund additional sales of these products and these recurring rollovers from members' main funds (via SuperStream) materially erodes members' retirement savings each year. Given the bans on conflicted remuneration that already apply to most insurance in superannuation in other places, practices such as these appear to be obvious attempts to circumvent such bans and arbitrage regulatory restrictions.

We see no reasons why risk insurance products should be exempted from this measure and note that further delays in the removal of commissions on all financial products will continue to unnecessarily complicate financial arrangements, cost consumers money, skew financial advice and distort pricing.

For further information regarding our submission, please contact Richard Webb, Policy & Regulatory Analyst at 03 8677 3835 or at rwebb@aist.asn.au .

Yours sincerely,

Eva Scheerlinck
**Chief Executive Officer**

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