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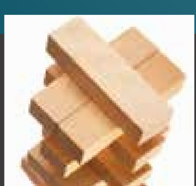
GET SET

IT'S BEEN A FOUR-YEAR SLOG JUST TO GET THE FOFA REFORMS TO THE START LINE. HAS ALL THE HARD WORK BEEN WORTHWHILE?

SIMON HOYLE AND ANDREW STARKE REPORT



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NOBODY SAID *THIS WOULD BE* EASY

It's been a four-year slog just to get the* Future of Financial Advice *reforms to the start line. Has all the hard work been worthwhile? Simon Hoyle and Andrew Starke report.

At the end of any significant legislative reform process, whether it's in financial services or any other sector, there is invariably a high level of fatigue among those whom the reforms affect.

Exhaustion is not too strong a term to use. Large-scale reform, however worthwhile, requires a lot of time and effort – physical and mental – and even if the overall thrust of the reform is broadly supported, the process itself can engender a lot of negativity.

It has been a long and arduous slog – four years, give or take – to get to where we are today: within days of the start of the *Future of Financial Advice* (FoFA) regime.

The Parliamentary Joint Committee (PJC) on Corporations and Financial Services began an inquiry into financial products and services in February 2009, and that inquiry was prompted by one of the most tumultuous periods in the industry's relatively short history.

FoFA: A LEGAL VIEW

The legal fraternity is divided on the benefits to financial advisers of the *Future of Financial Advice* (FoFA) reforms, although some are clearly prepared to consider a longer time frame than others.

Shaping the argument is Claire Wivell Plater, managing director of The Fold Legal, who believes no definitive answer can yet be given.

"If the FoFA reforms achieve their desired purpose, and that will only happen if they are fully embraced and effectively implemented, they will assist financial planners to move towards the holy grail of true professionalism," Wivell Plater says.

However, Astrid Raetze, a partner at Baker and McKenzie, is not convinced, reporting that she and her colleagues are struggling to see how the reforms have any benefits for financial planners.

"What we're seeing, in fact, is advisers giving less advice – everyone is trying to move to execution only (if they possibly can). If they can't do execution only, they're doing scaled or limited advice – and I've seen one or two of those, and to be honest that limited advice wasn't worth the paper it was written on. It was staggeringly inadequate," she says.

Even looking at the bigger picture, Raetze is unconvinced and believes the result will be:

- fewer independent financial planners;
- less comprehensive advice for the lower to mid end of the market;
- lots of execution only; and
- lots of limited or scaled advice, "which will be so disclaimed and say so little that it may as well not be advice at all".

However, Raetze adds the caveat that she is happy to be proved wrong.

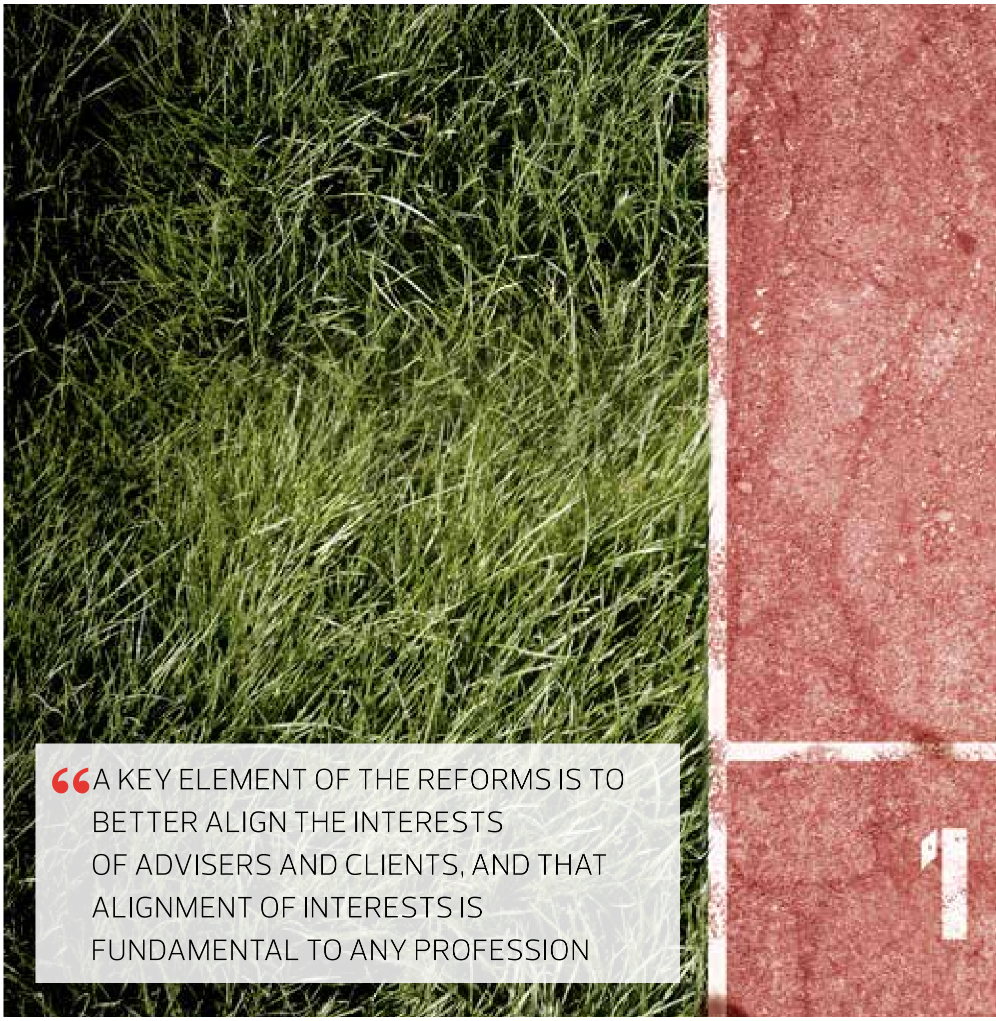
Tim Nethercote and Paul Derham, from Holley Nethercote, believe the benefits for financial planners will be that they will reconsider their overall service offering, because of the fee disclosure statement (FDS) requirements.

"We've already seen some great, streamlined service offerings built in to FDS templates," Derham says.

"Planners will also review their payment structures to comply with banned conflicted remuneration laws, which gives them an opportunity to optimise their revenue streams.

"Finally, they will be 'moving closer' to their clients by examining whether their motives are truly in the clients' best interests, and [ensuring] that those interests are prioritised over their own."

– Andrew Starke



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The PJC report (the "Ripoll Report") was released in November 2009. The government's response was released on Anzac Day in 2010. The first draft legislation followed in August 2011.

A 12-month extension to the original start date, from July 1, 2012, seems only to have prolonged the agony.

Whether the time, effort and expense will ultimately be worth it depends on who you ask.

"I have to remind people here," says the head of one major organisation.

"People go, 'My god, I'm exhausted'. And I go, 'Keep your eye on the prize. This is going to make a difference'."

He says it is issues that people disagree with and want changed or thrown out that inevitably absorb the greatest amounts of time and effort.

"There will always be elements that people will disagree with; there are elements that we would prefer to see done differently," he says.

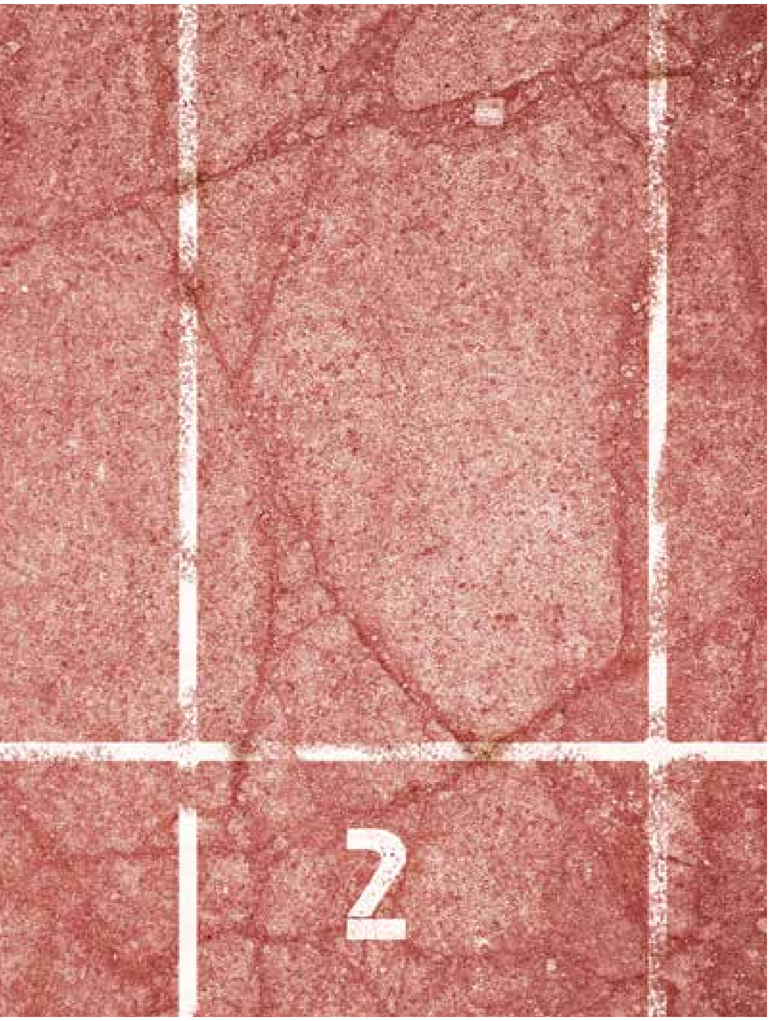
"But that's the nature of major reforms."

Peter Kell, Commissioner and recently appointed deputy chairman of the Australian Securities and Investments Commission (ASIC), says the overwhelming benefit for financial planners from FoFA will be "greater professionalism".

"The holy grail for the financial planning industry for some time now has been to become a profession, with all that the term implies," Kell says.

"The FoFA reforms will make a significant contribution to that objective, which is an objective we all support. A key element of the reforms is to better align the interests of advisers and clients, and that alignment of interests is fundamental to any profession.

"For too long we've seen business models and structural features of this industry produce misalignments between the advisers and financial services firms on the one hand, and customers on the other hand. The reforms will help provide a structural basis for better alignment between planners and advisers, and consumers.



"Part of that is removing some of the conflicts of interest from the industry. Part of it is ensuring that the best interests of a client are prioritised. Ultimately, it's also going to improve trust. And professions are all about trust.

"This isn't going to happen overnight. It will be a transition. But FoFA will contribute to this objective in significant ways.

"It's also going to rely on a lot of work from industry participants themselves and through their industry associations. I'm not suggesting that FoFA alone is going to deliver this outcome, but it does provide that structural basis for better aligning the interests of the client and the adviser, and putting in place some of the core elements of what it means to be a profession."

Mark Rantall, chief executive officer of the Financial Planning Association (FPA), says that "whilst these reforms have been arduous for many, for others that have been early adopters, they've been ahead of the change curve and have experienced better client engagement as a result of some of the changes that have been made".

Rantall says the most significant change to how planners "operate and engage with clients is uncoupling of the payment for advice from the product that might result from advice – the removal of commissions from being embedded in products".

"The most significant change that empowers consumers makes fees and services transparent and changes the relationship between a financial planner to be more embedded with the client and less embedded with product manufacturers," he says.

"The bigger picture impact of that change is firstly, consumers are empowered to have control over the transaction. By that, I mean that they have ultimate control over whether or not they continue to receive advice or they don't; and if they choose not to continue to receive advice then they can terminate that relationship and arrangement and the subsequent fees that go with that.

"Whereas before, where payment was embedded into the product, the client had no control over that transaction. I would argue the financial planner had no control over that transaction, either, so I think this change not only empowers the consumer but empowers the financial planner to have control over their business [and to] have control over the income flow of the business."

Phil Anderson, chief operating officer for the Association of Financial Advisers, says the FoFA regime "will in some ways force them, in other ways encourage them, but what will be the outcome will be a better quality of relationship with clients".

"That will be beneficial for both the clients and advisers," Anderson says.

"We've done some research recently that suggests that the more frequently you're in contact with your clients, the more profitable it is for the adviser. So I think that's a win-win.

Hugh Humphrey, managing director of Hillross, acknowledges that the *Future of Financial Advice* (FoFA) reforms have "many moving parts" but, aside from a few clarifications, says the regulator has declared the AMP dealer group ready for the July 1 start.

"There is still a bit more information to come, particularly around final clarity on conflicted remuneration, implications of grandfathering and details on annual fee disclosure statements," Humphrey says.

"We've got a lot of information, we understand where things are, we've been communicating all the way through and now, at the beginning of this year, we've swung into training and development with our advisers."

Humphrey says specific state-based FoFA courses are assessing Hillross advisers, determining any holes in their knowledge and delivering training to close these gaps.

"Clearly FoFA is a big deal with a lot of moving parts to it but we've put a whole lot of resources against it and some big budgets to make sure that it's all happening and trucking along in line with our expectations," he says.

"Our objective is that everything will be 100 per cent by July 1."

Being "consumed" by the FoFA changes is as dangerous as being underprepared, according to **Matthew Fogarty**, national practice development manager for The Encore Group.

"It is now about a new horizon and where we go to from here in terms of FoFA readiness," Fogarty says.

"For many, FoFA has been all-consuming and it is wearing a lot of people down, but the point is that we haven't even hit the start line."

Fogarty says the notion of best interest is already at the heart of what most advisers do, but added that the industry's "perception problem" would be addressed by the reforms.

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"That's probably the key thing that I expect to see that's good for all parties – that improvement in the quality of relationship, the better understanding of the client's needs and being more responsive to it.

"I guess that's probably one of the things that the government intended to see."

Anderson says that value is a two-way proposition, and "there must be value in that contact for the client as well".

"Some of the things that do come up is better understanding the client's circumstances and therefore needs, and potentially discovering needs that they may not have been ready to act upon, but through the regular contact they do.

"For example, if they have taken on more debt, or they've got another child, then it's responding to make sure their life insurance matches those needs, and so that then brings further business opportunities for the adviser."

That is not necessarily behaviour driven by FoFA, per se, but "what FoFA will do is, through the need to provide fee disclosure statements – and we'll see where we end up on opt in – but the fee disclosure statement, best interests duty, they will all encourage advisers to make sure they are keeping in contact with clients, and more clearly demonstrating the value that they are providing for those clients", Anderson says.

Ultimately, FoFA makes it easier for the regulator to do its job and to achieve the aim of raising the quality of advice generally.

Says Kell: "There's no doubt there's a big implementation task that we all face in the short term, and we're working closely with all parts of the industry on that issue.

"FoFA is going to enable us to take a tougher line on some of the conflict of interest issues that have raised problems in the past.

"It clarifies and improves some of the key elements around acting in the interests of the client. In an area that has received less attention, it has given ASIC some additional

HAS THE FOUR-YEAR SLOG TO GET TO THE START LINE BEEN WORTH IT?

"It's a bit of a hypothetical question, because we certainly haven't had the choice," says tbe chief operating officer of the Association of Financial Advisers (AFA), Phil Anderson.

"There are some positives that have come out of FoFA; there are some positives that have come out of the experience of the last five years for the industry.

"There has obviously a lot of unfortunate outcomes as well.

"Has it been worth it? Not really something that we had a choice about; it was something that we had to do and I am hoping in the longer term that some of those positives will start to shine. But certainly the process has been a difficult process.

"If you look at issues about the relationship with the client, the influence that FoFA has had on that will end up being positive; raising the bar as far as the best interests duty is certainly positive. We can argue about the detail of that, but the net effect is positive.

"The removal of conflicted remuneration is also going to be positive. It was a reality that the industry had accepted a long time ago, but it will have that positive impact of, as we talked about before, raising the perception of the professionalism of the industry. For too long it's been seen as one that is overwhelmed by conflicts, and that will make a difference there.

"There's other things that FoFA has pushed that have probably been more problematic, and I think that if FoFA had been more focused and more targeted it would have been an easier process to actually have achieved, and we would probably have got more out of it."

The chief executive officer of the Financial Planning Association of Australia (FPA), Mark Rantall, believes the effort has "absolutely" been worthwhile.

"Anything worthwhile is not going to be easy," Rantall says.

"When you're in a position of bringing about change and raising standards, winning the hearts and minds of people and bringing them along with you on that journey, then clearly everybody is going to evolve with you at a different pace."

He says that at a basic level "no one likes change".

"There is absolutely no doubt that the regulation pendulum has swung a little bit too far – I cite the examples of fee disclosure statements and opt in – and the size of the change brought in by FoFA has been underestimated by some, and the costs involved in doing that have been underestimated by many," he says.

"Having said that, there are still plenty of financial planners who have been early adopters and moved pretty quickly to a new environment, and come the first of July, FoFA will be the new reality, and people will adapt and get on with it."

Andrew Chan is a partner and senior financial adviser at Henderson Maxwell, specialising in self-managed superannuation funds (SMSFs).

"There has been a lot of talk about establishing a code of conduct… and I believe establishing a benchmark for standards in financial planning is vital and for us to be seen as a profession. A fiduciary responsibility to our clients seems essential, if not natural," he says.

"A code of conduct established for the reasons of excellence and professional standing for the sole reason of providing a better outcome for everyday Australians should be reason alone. To take advice and remove conflicts to the point where planning firms must offer either an independent (whole of market) or limited advice fee-based service, this would definitely be a standard worth aligning oneself to."

powers when it comes to removing bad apples from the industry through banning or preventing people from getting a licence in the first place if we think they have got a very poor track record. That will also help ASIC police the industry.

"Another element of FoFA that goes less to the actual legislative provisions is that it has provided the basis for ASIC to have an ongoing discussion with the industry around issues such as scaled advice and how we can increase the accessibility of advice; ongoing discussions around how technology might be incorporated into advice going forward; and around how business models in this sector can support a more sustainable approach to managing clients in an ongoing way.

"The process itself has helped ASIC get a better understanding of developments in the industry, and the sort of issues that practitioners are facing. That can only improve the way we communicate with the industry over time."

Rantall says the result of the FoFA reforms will be a raised level of trust and respect for financial planning as a profession. In a recent survey by the Roy Morgan Research group, financial planning was rated as the 18th most trusted profession in Australia – ahead of car salesmen, but a long way behind the most respected professions.

(Nurses, doctors, pharmacists, engineers and school teachers topped the list. The bottom five were insurance brokers, state members of parliament, real estate agents, advertising people and – last of all – car salesmen.)

"There will be more of a level playing field and every financial planner will have to operate on that basis, on fees versus commissions," he says.

"Whereas before, the more progressive financial planners had moved more along that continuum anyway, that level playing field will assist that trust measure because all consumers will be dealt with on the same basis in relation to payment. So I think that, going forward, [that] will be a positive, and of course the benefit for a financial planner when financial planning as a profession goes up the trust scale is clearly that more people will use financial planners, because they will have trust in the profession broadly.

> "THE FoFA REGIME WILL IN SOME WAYS FORCE THEM, IN OTHER WAYS ENCOURAGE THEM, BUT WHAT WILL BE THE OUTCOME WILL BE A BETTER QUALITY OF RELATIONSHIP

"That doesn't mean there are not going to be mistakes made. There will still be mistakes that continue to be made, just as in every profession there are some who do not operate in an appropriate manner.

"But in other professions those people are seen as rogues, and in the financial planning profession the number is probably no greater and yet the problem is seen as systemic." ■