

*The consumer under FSR*

*Address by Richard Gilbert*

*CEO IFSA to the FICS AGM*

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Thank you for the opportunity to address this AGM.

While thinking about today's topic, *The Consumer Under FSR*, my mind almost immediately went back to the 1990s.

It was in 1991 that I first encountered the industry as public servant working in the Australian Senate.

I dusted off a copy of the 1993 ALRC report *Collective Investments: Other People's Money*

- and thumbing through the introduction of what is a massive body of work, I reflected on how far we have come in terms of consumer protection in the 13 years since publication.

Back in the bad old days of the 1980's, there were investment schemes that promised fortunes, but did not deliver them – in fact we had losses in the late 80's which exceeded a billion dollars!

We had a barely regulated advice industry.

And financial planners could receive secret payments for advice.

Since the advent of the SGC system we have had a cascade of reforms in favour of consumers.

Legislation cannot – and should not- entirely eliminate investment risk. The risk return equation underpins a free market economy.

The FSR regime strives to offer maximum protection to consumers, while still allowing providers of financial services to devise innovative financial solutions.

We currently have a regulatory regime which has few peers amongst OECD countries. I would challenge the critics of FSR to find a regime which has the regulatory quintuplet of:

- A single product licensing regime;
- A single regime for regulating advice;
- A national disputes resolution system at no cost to customers;

- Disclosure of all fees charges and commissions across all financial products under the FSR umbrella; and
- Finally and most importantly – low levels of customer disputation and high levels of customer satisfaction.

This legislative protection, along with good industry conduct insulated our industry from the scandals that plagued and so damaged other markets over the last five years.

When the markets dipped by more than 20 percent at the beginning of the millennium, the Australian regulatory system within which we operate was 'stress-tested' and found to be robust.

In fact, regulators and industry both maintained a watchful eye on the governance of funds - and the principles of honesty and integrity that go with managing *'other people's money'* were, I believe, firmly upheld.

It would be remiss of me not to mention the fact that overall our twin peaks have worked.

APRA and ASIC need our support and confidence as they go about their sometimes difficult task of being the protector of the consumer interest.

Reform invariably imposes new obligations for the industry. It is important that there be a balancing of the true costs and benefits of the reform.

The industry jury and I also believe the consumer jury have returned a verdict that FSR has been for the overall public good.

In this regard, I would like to comment on the AFR Editorial earlier this week which said that the Government's 'red tape pledge cannot be trusted'. I'll say just two things.

The Clerp 9 reforms and the ASX Corporate Governance Council principles were infinitely better for our industry than the now widely discredited Sarbanes-Oxley reforms.

Second, the FSR Refinements packages Mark 1 and 2 will cut red tape for our industry.

We have every confidence that Parliament Secretary Chris Pearce and the Government will deliver on these reforms.

The regulatory success that we have had is no guarantee that in the future we will not experience failure in the delivery of the best in consumer outcomes.

Eternal vigilance and upholding the best of fiduciary conduct will.

Vigilance and being a good fiduciary go hand in hand with brand and reputation.

Repeatedly the customer research shows that "Good reputation counts most" in the minds of a customer.

It is trust which underpins consumer confidence

IFSA looks constantly at the drivers of confidence and the drivers of trust in the Australian financial services system.

Indeed, complaints about aspects of the industry are the most useful measure of our overall health and well-being.

Although the dispute resolution process is seen by some as being too harsh it is one of the critical underpinnings of FSR and it needs our support.

Touching briefly on complaints, I note that compared with overseas jurisdictions, Australians don't seem to be complaining about their investment experiences at

anywhere near the levels of those, for example, in the UK .

In fact, complaints to FICS in 2003 ranged from the high 500's - and by December 05, had dropped away to the high 400's, with complaints about financial planners dropping markedly.

The Australian Superannuation Complaints Tribunal that looks after the interests of more than 26 million superannuation account holders in this country had less than 1300 written complaints in 2003. By 2005, the figure had fallen to around 1100- or to put this into perspective- around 1 in 29,000- or if you like- 3 complaints per day.

This, to me, suggests that for consumers under FSR, the system in Australia is working.

Compare this with complaints to the British Financial Ombudsman Service between 2003 and 2005. It's like looking at the torque curve on a Ferrari.

The line goes pretty much straight up – and almost as fast as a Ferrari. While resisting the temptation to joke about whinging Poms, a leap from just over 40,000 complaints in 2003 to 100,000 per year in 2005 suggests that British consumers are not completely happy under their regulatory regime.

Unfortunately, the Westpoint failure will see FICS numbers spike.

In fact, over 60%\* of the investors in Westpoint appear to be self-managed super funds.

If I can just hark back to 'reputation' again for a minute.

IFSA research to date has revealed that no IFSA members had Westpoint on their platform.

Also, IFSA members with approved product lists for their financial planners did not have Westpoint as an offering.

It is reasonable to ask therefore, was this outcome an accident or did it happen by design?

I rather suspect the latter – overwhelmingly, our industry goes to great lengths to evaluate investment opportunities.

We are very serious about due diligence - some would say to the point of *obsession*- if you look at IFSA's conference topics and speakers and 60 odd issues sessions that we offer our members the focus is on good regulatory outcomes and quality compliance procedures.

The recent ASIC report on breach reporting confirms this. There are systems in place to identify and report breaches. Breaches are being rectified and investors are being compensated where losses occur.

Still our industry has its critics.

We welcome the robust and free ranging debate as it focuses the competitive mind.

Recently, there was a somewhat heroic assertion that the industry operates as some sort of cartel- the 'big end of town' - who always gets what it wants. Not surprisingly, we don't quite see ourselves this way.

To suggest that we need the ACCC to swoop down and have a good look at the possibility of cartel-like behaviour in the Australian wealth management industry is an absurd proposition.

We are in the midst of a price and value war to win the hearts and minds of superannuation customers.

Under choice suddenly the public offer big end of town has had 30 or 40 not for profit competitors unleashed in the market.

A number of these new players have breath taking scale, and are rapidly developing scope, as they too seek the holy grail of providing affordable advice to their customers.

Self managed super presents another opportunity for consumers and this segment has had meteoric growth for the last ten years.

Within this three way tug o war for customers there is a multiplicity of mechanisms for the payment of advice.

Provided that there is transparent disclosure it is good for consumers to be able to choose between a range of options to pay for advice.

Currently, advice can be obtained via 5 different mechanisms, viz:

- Fee for service via separate payment (a less than optimal tax outcome);
- Fee for service by way of deduction from fund based on an annual agreement;
- Free but paid by the fund as a whole;
- On going advice via a dial down commission; and
- On going advice via a dial up commission.

Some say that one or a number of these methods should be banned.

We say let consumers decide.

The very strength of our industry is that it has been able to innovate and operate in a free market system.

But the industry still has strong regulation.

I would venture to suggest that we are perhaps the most regulated industry in Australia, with the cost of compliance now comprising some 15% of total costs to our members.

Returning to the cartel assertion, the Macquarie Dictionary states - *a cartel is a collusive syndicate, combine or trust, generally formed to regulate prices and output in some field of business*".

To the contrary, my members spend most of their waking hours, plotting and scheming against each other in a never-ending battle to build their customer base.

I'd just like to close by sharing a couple of quotes with you from a book by Jack Bogle- given to all of my board members as a Christmas gift by Jeremy Duffield, Head of Vanguard Investments Australia.

Jack Bogle founded Vanguard in the US in 1974 and last year he published *"The Battle for the Soul of Capitalism"*.

Jack Bogle quoted Alan Greenspan, former Chair of the US Federal Reserve who said: *"Recent transgressions in financial markets have underscored the fact that one can hardly overstate the importance of reputation in a market economy..... rules cannot substitute for character"*.

Henry Kaufman the eminent financier, economist and historian provides us with one of my favourite quotes from Bogle's book.

*"Breaking the rules is not merely a breach of ethics and the law- it is poor business. Trust is the cornerstone of most relationships in life. Financial institutions and markets must rest on a foundation of trust as well. When financial buccaneers and negligent executives step over that line, the damage is inflicted on all market participants and the notion of financial trusteeship too frequently is lost in the shuffle. That is why the large majority of ethical and responsible market participants must not tolerate the transgressions of the few abusers. And regulators and leaders of financial institutions must be the most diligent of all".*

Hear, hear.

It is my firm belief that our consumers are well protected and well served - and you can be assured that IFSA will, continue- along with regulators, to be as Mr Kaufman urges, among the most diligent of all.

Thank you very much.

*\*60% figure comes from a report called "Super Disaster" on page 22, BRW, Thursday 16<sup>th</sup> March*

*2006. This estimate comes from Slater & Gordon,  
solicitor for more than 2000 of the investors affected  
by Westpoint.*

