FSC FINANCIAL SERVICES COUNCIL

Financial Planners and Advisers Code of Ethics 2019 Guide

Submission

November 2020

FSC FINANCIAL SERVICES COUNCIL

Contents

1. About the Financial Services Council

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advice licensees and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

2. Executive Summary

The FSC welcomes the release of FASEA's *Draft Financial Planners and Advisers Guide* **("the Guide")**. In particular it welcomes a greater focus by FASEA on the intention behind the standards and the inclusion of reflective questions to guide advisers in using their professional judgement. The Guide is an improvement on the initial guidance released by FASEA last year[1][2].

The FSC locates its suggested improvements to three areas of focus:

- Conflicts of interest
    - Referrals
    - Remuneration
- Consent
    - Commission being categorised as a fee
    - Format of consent
    - transferring clients
- Scoped advice and the applicability of Standard 6
- Other remedial proposed changes

These improvements will ensure consistency with other regulatory tools and across the industry.

The FSC understands the Guide will supplement and not replace the first iteration of guidance FASEA issued last year. The FSC suggests the content of this Guide and all withstanding Guidance, scenarios and examples are consolidated into a single document. It would be significant aid to the adviser to have to only refer to one document.

[1] *FG002 – Financial Planners and Advisers Code of Ethics Guidance* (https://www.fasea.gov.au/wp-content/uploads/2019/10/FASEA-Financial-Planners-and-Advisers-Code-of-Ethics-2019-Guidance.pdf)
[2] *Preliminary Response to Submissions FG002 Financial Planners and Advisers Code of Ethics Guidance* (Source: https://www.fasea.gov.au/wp-content/uploads/2019/12/FASEA-Preliminary-COE-guidance-response-v1.0-Dec-2019.pdf)

3. Recommendations

Conflicts of interest - Referrals

1. Provide additional guidance and examples confirming that advisers who provide advice under a Corporate Authorised Representatives **(CARs)** structure and associated business structures can receive referral fees provided this is in the best interests of the client, meets the provisions of the Code of Ethics **("the Code")** and satisfies the disinterested persons test.
2. Clarification regarding referral fees paid to joint ventures.

Conflicts of interest – Remuneration

3. The Guide suggests there are some forms of remuneration that will always give rise to a conflict – what form this remuneration takes should be clearly articulated. Clearer language is needed in relation to the following:
    a. the process for requesting access to existing files
    b. amendments to Fundamental Question 2 of Standard 7

Consent – commission being categorised as a fee

4. Life Insurance commission is paid by insurer to an adviser. It should not be categorised as a fee for advice or service, unless there is an agreement between the adviser/CAR/licensee to provide advice and/or services to the client in acknowledgement of the receipt of the adviser of commission.

Consent – format

5. Clarification permitting electronic and other forms of consent as is consistent with current practices and advice document arrangements.
6. Confirmation that client consent obtained in the course of the transaction is sufficient to evidence the client's free and informed consent to the continuation of those arrangements with the new adviser, or to what extent this must be reobtained.
7. Clarification of what evidence can be retained on file to demonstrate that the client's consent was informed and given freely and what evidence is not acceptable.
8. Additional examples for Standard 5 and 6 for providing scoped advice to enable better interaction with tools such as *RG 244 Giving information, general advice and scaled advice* is needed.
9. The Intent Section of the Guide in relation to Standard 5 should be updated in respect of Approved Product Lists **(APLs)**, and the definitions of a "well-rated product" and "demonstrably appropriate product".

Scoped advice and other recommendations

10. Updated examples, language and better interaction with guidance from other regulators as well as the Corporations Act relating to scoped advice.
11. Further guidance in relation to wholesale clients.

4. Conflicts of interest

4.1. Conflicts of interest - referrals

Commentary under 'Applying the standard' for Standard 7 states that an adviser is prohibited from receiving referral fees directly from a third party for advice and services provided to their client. However, referral fees may be paid to a corporate entity that employs those advisers.

FASEA explicitly states that for any business structure set up for the sole purpose of receiving referral fees, the adviser would otherwise not be entitled to receive this as to do so might be considered to circumvent the intent of the Code. The FSC appreciates FASEA's intention on this issue, but note business structures are established for multiple reasons, including legal requirements, estate planning, tax arrangements and diversified streams of revenue.

Providing clarity to this rationale will better assist advisers in understanding the intent of the Code clearly in relation to referrals and conflicts. There are several areas for which clarification is needed:

- The Intent Section of Standard 1[3] explains that the standard discourages practitioners from setting up structures to circumvent ethical obligations that would apply to individuals. However the Guide also explains the Code prohibits advisers from receiving referral fees.[4] On that same page it then states if you are set up as a CAR with a sole purpose of receiving fees it "may" circumvent the Code.
- The response given to Fundamental Question 2 of Standard 1[5] indicates that:
  - Referral fees cannot be received directly from a third party for advice and services provided to an advisers client, regardless of the nature of those services;
  - Advisers cannot use a CAR/business structure as a mechanism for directly passing through a referral fee received from a third party, as this would circumvent the intent of the Code;
  - Where part of an advisers revenue is related to the referral revenue received by the CAR/business structure the adviser will need to demonstrate that receipt of referral revenue does not inappropriately influence the advice given by the relevant provider and is in the best interests of the client, meets the other provisions of the Code, and passes the disinterested person test.
- FASEA should include a fundamental question or further guidance confirming:
  - advisers that are sole practitioners that and are either the single authorised representative of a licensee (i.e. no CAR) or
  - a single/the only authorised representative of a CAR

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[3] Page 13 – *"Standard 1 discourages advisers from setting up business structures merely to circumvent ethical obligations that would otherwise apply to them as individuals."*
[4] Page 14 – *"The Corporations Act permits referral fees to be paid directly to an adviser, however the Code prohibits an adviser from receiving referral fees"*
[5] Page 14

are also able to receive referral fees (either directly in (a), or via the CAR in (b)), provided that the fee did not inappropriately influence the advice given by the relevant provider and is in the best interests of the client, meets the other provisions of the Code, and passes the disinterested person test.

4.2. Conflicts of interest - remuneration

On Page 17 it says:

> *"the Code does not seek to ban particular forms of remuneration, nor does it determine that particular forms of remuneration will always give rise to an actual conflict of interest or duty. That said, you should remain open to the possibility that certain forms of remuneration will always fail to meet the requirements of the Code of Ethics."*

It would be preferred if some remuneration types (that by FASEA's estimate will *always* fail to meet the Code) be explicitly called out.

Joint ventures

Advisers or CARs can be party to joint ventures with other financial services professionals, such as accountants or mortgage brokers. It would be beneficial if the Guide could clarify whether it would be permissible under the Code for an adviser to set up a joint venture, with an accountant, for example, and for both the adviser and accountant to receive revenue under that arrangement.

Confirmation that arrangements where a fee is shared between two parties (e.g. Mortgage broker and adviser) are not conflicted should be clearer because the amount paid is not an additional cost to the client, it is a split between parties (e.g. the Authorised Representative does not get paid a referral fee, they share a fee with the referrer i.e. there is no difference in the cost to the client).

4.3. Ordinary person

On Page 18 it says:

> "*In making this assessment the adviser is to imagine standing in the shoes of an ordinary person – not the client, not a consumer advocate, not another adviser, not a regulator, just an ordinary person in the street with ordinary intelligence and good judgement.*

This language differs from the requirements of the Best Interest Duty set out in the Corporations Act.

A Code of Ethics that applies to a profession would normally call out an ordinary person in that profession, not someone from the community without those professional skills and knowledge. It is not uncommon for Codes to apply standards above the law, and as such it an example of how the ordinary person test might work in practice would be welcomed.

4.4. Examples – couples

On Page 19 states:

> *I am the existing adviser of a couple who have advised they are going through a separation or divorce. Is it appropriate for me to continue to advise both clients in this circumstance?*

Advising both members of the couple would place the adviser in a position of actual conflict. Clarification as to how that conflict could be dealt with appropriately through more examples beyond the requirement to exercise professional judgment in a given situation would be welcomed.

5. Consent

5.1. Consent – insurance commission being categorised as a fee

The FSC disagrees with the implication that an insurance commission can be categorised as a fee, and thus that the consent obligations apply in respect of clients for whom advisers receive commission only. Where a client has been provided with advice in relation to insurance, and the adviser receives a commission as a result of an arrangement with the issuer of that insurance policy, this cannot be grounds for implying, without further basis, that an ongoing advice relationship exists between the parties.

Where an adviser receives commission in respect of a life insurance policy, but does not provide any further advice or ongoing service to that person, that person is not a client, and thus the adviser is not subject to consent-related obligations under the Code (unless and until the adviser and client agree for advice and/or services to be provided by the adviser to the client).

Recommended approach

FASEA should specify when someone is not a client. This will best illustrate when obligations will apply, and when they will not. For example, obligations will not apply in respect of a person who holds a life insurance policy (and for which the adviser is receiving commission), unless the adviser has agreed to act for, or otherwise interact with that person, for that commission.

Additionally, it should be clarified as to the grounds in which it would be proper to assume that a contractual arrangement between an insurer and a licensee should be voided, in whole or in part, in respect of a particular adviser, because that adviser has not obtained consent to act from the insured, in circumstances where they are not currently acting, and may not be required to act in future, for the insured.

FASEA should include guidance that a person/entity is no longer a client when:

- the adviser stops acting for (or interacting with) the client and the client is no longer paying the adviser a fee, or the period to which a fee relates has ended; or
- the contract has terminated.

This would exclude persons in respect of whom the adviser receives commission only, and to whom the adviser has not agreed to provide a service. Conversely, if the adviser agreed to provide the person a service in respect of that commission, that person would be a client for as long as the commission is being paid.

Consistent with this, we propose that Fundamental Questions 1 and 2 of Standard 4 are amended as follows:

1. How do I determine which existing clients I need to contact to obtain consent?

Answer: You need to obtain consent from any retail client who you have provided and implemented a personal advice recommendation, which includes retail financial products, and you continue to receive an ongoing fee (including commissions) in return for advice and/or services you agreed to provide to them and from whom you have not received free, prior and informed consent.

2. I have a number of existing insurance only clients who I have irregular contact with. These clients received an advice document and signed an authority to proceed when I presented the original advice a number of years ago. Do I need to contact them to obtain consent?

   Answer: If you did not agree to provide the client with any advice and/or service beyond your original advice, you do not need to obtain consent, as you are not receiving commission because you agreed to act for that person. Consent to act is only required where you agreed to provide advice and/or services for the commission you are receiving from the insurer.

In situations where the adviser's only connection to the insured is insurance commissions, time should be given for the Life Insurance Framework **(LIF)** to be embedded, the LIF Review to be conducted by the regulator, and changes brought about with appropriate industry consultation. Changes premature of this run the risk of being impractical and conflicting with the LIF Review. For example, insurance only clients may not be readily trackable on advisers' systems which makes the consent requirements proposed by FASEA difficult to comply with. Furthermore, if the client does not provide the consent, while the adviser can remove themselves from the policy this does not typically result in any reduction in premiums paid by the client. We note that insurance commissions are payable by the provider to the adviser.

5.2. Consent - format

The Code requires advisers to seek consent to:

- services offered, and fees charged (standards 4 and 7); and
- implementation of the advice provided (standard 4).

The FSC agrees that an adviser should ensure their client agrees with the advice provided, and consents to the adviser implementing that advice on their behalf. However, it is important that the *format* of that consent is not limited to signed consent only as indicated in the Guide.

The Guide includes a question regarding what format is required when obtaining consent from clients and the answers state an adviser will need to ensure they receive signed consent from their clients. This means written consent from the client prior to providing them with personal advice. Intrafund advice is often simple advice over the phone and provided at no additional cost to the superfund member. We question the necessity and practicality of obtaining client consents in writing if verbal informed consent can be obtained during the appointment booking or meeting which is recorded.

Fundamental Question 7 of Standard 4 indicates that advisers should obtain signed consent from their clients (including via signed file notes). The practical effect of this is:

- to no longer permit clients to provide verbal consent for an adviser to implement further advice that may have been provided verbally, in accordance with the law (and then prepared a Record of Advice, which is not required to be given to the client). In other words, an adviser is permitted to provide verbal advice, but the Code would then require the adviser to change the mode of their communication with the client and obtain consent in writing from that client. This is at odds with current legislation and poses significant deviation from current recognised operating procedures. Communicating in writing might not be the means by which the client has chosen to engage with their adviser.
- that clients who have elected to receive advice electronically, for example, via email, would not be able to consent to the implementation of that advice by confirming via return email, unless they had software that enabled the addition of a digital signature.
- Necessitates an advice process in each case. More guidance is therefore required in cases where the customer does not want to undergo an advice process but wants to retain adviser support.
- With intrafund advice which is often simple advice over the phone and provided at no additional cost to the superfund member. The FSC questions the necessity and practicality of obtaining client consents in writing if verbal informed consent can be obtained during the appointment booking or meeting which is recorded.

To remedy the issues outlined in above, the following revisions to the Guide are needed:

- The draft guide should make it clear that the following forms of client consent are also permissible, and that it is for the adviser to use their professional judgement to determine which format of consent is appropriate in the circumstances:
    - verbal consent to the provision of, and implementation of, further advice;
    - written consent via electronic means, without a signature, responding to written advice or to an advice services agreement, that is delivered via electronic means.
- Addition of a Fundamental Question to confirm that client consent obtained in the course of the transfer (Purchase or change of adviser) transaction is sufficient to evidence the client's free and informed consent to the continuation of those arrangements with the new adviser, or to what extent this must be reobtained (e.g. original advice documentation for previous informed consent).[6]
- Clarification of what evidence can be retained on file to demonstrate that the client's consent was informed and given freely and what evidence is not acceptable.

Practicality of Fundamental Question 2 of Standard 4

[6] In situations where a client has changed adviser (for example, due to an adviser transferring their book of clients to another adviser), it is common practice to obtain the client's consent to the transfer of any ongoing service agreement, including ongoing fees, as well as the transfer of their files, including any personal information held in them.

Fundamental Question 2 of Standard 4 should be more practical. Insurers cannot facilitate not having a linked adviser (in many cases) and doing so would not necessarily reduce costs for the consumer. However, the consumer would be detrimentally impacted as they would have to deal directly with the insurer at claim time or if they need to make an ad hoc policy adjustment. This is not a good consumer outcome. This is also impractical for Australian Financial Service License **(AFSL)** holders - where they have been providing advice for many years there are likely high numbers of consumers where there is an adviser code on a policy.

In addition, most insurers cannot simply "switch off" trail commission, therefore the only way an adviser can cease receiving this revenue is to orphan the client back to the insurer. In essence, the consumer would still be paying the same premium and the insurer would be keeping the trail commission.

The requirement an adviser must obtain a client's 'ongoing consent to act'[7] in order to continue to earn trail commission could contradict LIF reforms, which allow product issuers to pay (and advisers to continue to receive) LIF compliant life insurance remuneration from the product issuer without the additional requirement that the client must consent to the product issuer's ongoing payment of LIF compliant trail commission.

Application to personal advice

The Guide implies the obligation should apply to advisers earning LIF compliant insurance commission in providing personal advice in recommending life insurance products, in circumstances where it appears to be perfectly fine to continue to receive LIF compliant trail commission for a non-relevant provider (i.e. a general advice model or a non-advice model, including comparison services). It is difficult to sustain scenario where an adviser who provides personal life insurance advice to a client is worse off than a person/company that does not provide any advice and does not take into account the client's personal circumstances.

5.3. Consent – transferring clients

The answer provided for Fundamental Question 1 of Standard 4 states[8]:

> *"You need to obtain consent from any retail client who you have provided and implemented a personal advice recommendation, which includes retail financial products, and you continue to receive an ongoing fee (including commissions) from whom you have not received free, prior and informed consent"*

Where an adviser has purchased a book of clients, and the previous adviser obtained the clients' fee prior and informed consent, we believe the acquiring adviser should not have to repeat that process where the client's consent has been given to the transfer of their file, data etc as part of the purchase transaction.

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[7] Page 21
[8] Page 21

Applicability of consent regarding product advice

Fundamental Question 2 for Standard 4[9] and its answers should be clarified with regard to a 'product advice recommendation'. If the adviser in question is not providing advice it should be clearer as to what extent consent is needed.

As worded, the Guide appears contradictory when it states if the clients in question have not been seen for several years the adviser should confirm that there are no changes to their personal circumstances and to confirm the client's ongoing consent to act.

However, if the adviser is not providing ongoing advice to the client what is this consent regarding (i.e. the adviser is not currently 'acting' for the client and the client is not currently paying a fee to receive advice. We recommend FASEA review the guidance for this question in light of our earlier comments regarding the upcoming LIF Review.

Request for access to existing files

The answer to Fundamental Question 2[10] for Standard 8 reads:

"…If clients are transferring the adviser will need to request access to existing files."

The FSC requests what is meant by 'requesting access to existing files' be clarified.

[9] Page 21
[10] Page 30

6. Best Interest Duty and scoped advice

FASEA should provide additional examples for both Standards 5 and 6 for the provision of scoped advice as well as meeting the BID. The longer-term interests need to be understood and considered in the advice development process, this should not inhibit advice provision where the consequences and implications are clear and outlined (particularly in cases where there is uncertainty or trade off conversations occur particularly). Providing more examples of where advice is scoped and complies with the Code would be welcome beyond the requirement of exercising professional judgement.

Standard 6 states that advice should "actively consider the clients broader, long term interests and likely circumstances.[11] The Guide then expressly states that limited scope and/or scaled advice can be "highly effective".[12] This appears contradictory and we would suggest a working example of limited scoped advice in the scenarios listed in the guidance to address broader, long term client interests.

6.1. Interaction with ASIC Regulatory Guidance on scaled advice

Clarification of the Guide to ensure it better interacts with existing Regulatory Guidance on scaled advice or scoped advice regarding what advice is permitted to be scaled advice will incentivise is take up, likely reduce costs and risks associated with its provision. Revisions of FASEA's Guide could be timed with updates ASIC makes to its Regulatory Guides for example a forthcoming consultation on RG 244. *RG175: Licensing: Financial product advisers – Conduct and disclosure* has not been updated since the Code took effect and should be updated to include the Code and Best Interest Duty interactions. Insofar as its remit permits, FASEA should work with ASIC on remedying discrepancies between its Guide and ASIC's regulatory guidance.

6.2. Interaction with AFCA: Fairness and Scoped advice

Consistency with the Australian Financial Complaints Authority's (AFCA) process for assessing complaints should also be reflected in the Guide.

AFCA appears to focus strongly on the concept of fairness in their decision-making process. When considering a complaint, AFCA will identify the relevant legal principles and take these into account. However, AFCA will depart from legal principles where they consider that it is fair in all the circumstances to do so.[13]

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[11] Standard 6 – *"You must take into account the broad effects arising from the client acting on your advice and actively consider the client's broader, long-term interests and likely circumstances."*
[12] Page 25 – *"Limited scope engagement and/or scaled advice can be highly effective in meeting a client's immediate needs. Such limited advice scenarios may include: SMSF, insurance, stockbroking, investment and intra-fund advice. The Code is not seeking to prohibit this type of advice – only to ensure that it is only provided where appropriate."*
[13] https://www.afca.org.au/what-to-expect/how-we-make-decisions

The Guide offers a considerably broad definition of fairness and the difficulty that the subjectivity of this requirement imposes when determining that someone should have considered this in the broader client situation and other areas is of concern.

The FSC recommends the Guide is updated in several ways:

- Insertion of more examples illustrating the extent an adviser should take into account a client's circumstances if it is limited scope. Page 16 of the Guide states a client's *express wishes* [14]should be accounted for, but that these do not override duty to give advice in their best interests. For example, if a client asks for a planner not to look at their debt and the planners does not it is unclear what the standard of practice is in this situation. An example better illustrating what is intended should be provided by FASEA.
- Consistency with Example 2 in RG 244 - this example covers advice scaled to super but should consider others. This is particularly relevant as ASIC updates regulatory guidance in relation to scaled advice provision.

6.3. Intent section of Standard 5

The Intent Section for Standard 5 says:

> *"Advisers have a duty to be aware of available products in the market and it may be necessary for product recommendations to go beyond what is currently on a Licensees' approved product list (APL) if the adviser is aware of a product that would be in the client's best interests"*

The FSC seeks FASEA's clarity that the following process is appropriate:

1. Advisers must know the products on their APL,
2. The adviser must understand any products the client currently holds or expresses an interest in, and
3. The adviser assesses products under 1 and 2 and only if none are appropriate broaden the product assessment to other products that are appropriate to the needs of the client.

It should be clear that the expectation to go beyond an APL arises where the consumer requests consideration of a particular product, and does not generally require advisers to be aware of all products within the marketplace

Well rated product

The FSC recommends that FASEA remove reference to 'a well rated product' given an appropriate product will be unique to the client's circumstances which such a definition cannot capture.

Demonstrably appropriate product

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[14] *"You should take into account your client's express wishes, but these do not override your duty to give advice that is in the client's best interests".*

We recommend FASEA remove reference to a demonstrably more appropriate product. A product may appear more favourable in one respect but there may be reasons why the Licensee will not support the use which are equally as valid.

7. Other comments

7.1. Wholesale clients

The Guide raises the ethical question of whether a client who meets the Corporations law definition of a wholesale client should be treated as a wholesale client. The guidance to date has focused on a client with no experience or understanding of financial matters. It is unclear as to clients with some level of knowledge, experience and confidence how much is sufficient.

The FSC recommends FASEA provide further guidance on how an adviser might go about making such an assessment.

7.2. The interaction between the Code and the Corporations Act

The FSC acknowledges that while the Code and the Corporations Act differ in both form and authority, how they interact can be improved as well as ensure consistency across industry.

The Code expressly prohibits activity otherwise permissible under the Corporations Act. Where additional requirements are introduced in this draft guide by way of new or updated guidance and/or examples, there needs to be an acknowledgment that transitioning away from established, legally permissible practices might take time and that a facilitative approach to non-compliance with the Code in relation to acts or omissions that are otherwise permissible under the Corporations Act is appropriate.

7.3. Values

Language in relation to the values attached to the standard of the Code should be clarified in the following ways:

- Inclusion of the value of fairness should be included in Standard 12 with regards to the necessary actions to take when questionable advice is identified. For example, fairness should be applied in giving the previous adviser the opportunity to respond (where relevant) to explain their advice, particularly where there are developments they might not be aware of.
- Clarification regarding the values associated with each standard and their applicability that FASEA ranked should be clarified in light of the revisions to the Guide.