FINANCIAL PLANNING
ASSOCIATION of AUSTRALIA

QUALITY OF ADVICE REVIEW
CONFLICTED REMUNERATION PAPER

Prepared for Treasury – Quality of Advice Review

14 November 2022

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Secretariat, Quality of Advice Review
Financial System Division
The Treasury
Langton Crescent
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Dear Ms Levy,

Re: Quality of Advice Review – Conflicted Remuneration Paper (November 2022)

The Financial Planning Association of Australia[1] (FPA) welcomes the opportunity to provide this response to the Quality of Advice Review – Conflicted Remuneration Paper, released 31 October 2022.

The FPA supports the Quality of Advice Review and has long been calling for a similar review of the legal and regulatory framework for financial planning to improve Australians' access to affordable, high quality, professional financial advice.

The Conflicted Remuneration Paper offers an opportunity to primarily consider the outcomes of the Life Insurance Framework Review, which included two ASIC life insurance advice file reviews and a life insurance data collection, which collected aggregate level data from a number of life insurers from 2017 to 2021.

The FPA is disappointed the outcomes of these reviews have not been provided for analysis and consideration in relation to the proposals made in this paper. The high-level analysis provided leaves more questions than answers and for this reason the FPA recommends a proper review of the outcomes is conducted. This should include a further round of file reviews to also consider the outcomes of the professional standard framework.

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[1]The Financial Planning Association (FPA) is a professional body with almost 12,000 individual members and affiliates of whom around 10,500 are practising financial planners and nearly 5,000 are CFP professionals. Since 1992, the FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
- In 2009 we announced a remuneration policy banning all commissions and conflicted remuneration on investments and superannuation for our members – years ahead of the Future of Financial Advice reforms.
- The FPA was the first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices.
- We have an independent Conduct Review Commission, chaired independently, dealing with investigations and complaints against our members for breaches of our professional rules.
- We built a curriculum with 18 Australian Universities for degrees in financial planning through the Financial Planning Education Council (FPEC) which we established in 2011. Since 1 July 2013 all new members of the FPA have been required to hold, or be working towards, as a minimum, an approved undergraduate degree.
- When the Financial Adviser Standards and Ethics Authority (FASEA) was established, the FPEC 'gifted' this financial planning curriculum and accreditation framework to FASEA to assist the Standards Body with its work.
- We are recognised as a professional body by the Tax Practitioners Board.

In relation to the proposals contained in this paper, the FPA is supportive of all proposals. The FPA remains concerned about the availability and accessibility of professional life insurance advice for younger clients and claims management support more broadly for the Australian community, given the current life insurance framework. The risk born by professional financial planners providing advice on life insurance strategies and implementation support for clients is of specific concern with the current remuneration structure.

The FPA would welcome the opportunity to discuss with the Review the issues raised in our submission. Please contact myself or Ben Marshan CFP® (Head of Policy), on 02 9220 4500 or policy@fpa.com.au to further discuss the suggestions raised.

Yours sincerely,

Sarah Abood
Chief Executive Officer
Financial Planning Association of Australia

Introduction

In considering our response to the proposals in this paper, the FPA has considered the role of professional financial advice in the context of the entire life insurance market. Life insurance plays an important role not for the individual policy holder but also serves as a community good for the entire nation. Both uninsured and underinsured individuals have the potential to create significant budgetary pressures on Government where support of that individual or their family turns to reliance on social services benefits and/or NDIS funding.

The life insurance market

The retail advised life insurance market in 2021 was made up of:

- the individual advised market made up 53% of premiums paid to the life insurers, and
- the group super market made up 37% (APRA Life insurance claims and disputes statistics).

Further, while the number of Australians who obtain cover through the group super market is higher, the levels of cover are substantially lower (on average $782k for retail advised Life (death) cover and $841k for TPD, versus $219k for Group death and $187k for Group TPD). Group super insurance plays an important role in ensuring that a greater proportion of the population have access to life insurance as a 'floor', however it is rarely enough for average Australians in the event of an insurable event. Ultimately the "best financial interests" test for superannuation trustees has a negative effect on the appropriate life insurance coverage for most Australians. The average cover shows the importance of a functional professional financial advice market for the benefit of the Australian population.

For example, financial planners will typically consider their clients debt, requirements to support the education and living costs of young children to reduce stress on the surviving spouse, and the level of cover required to minimise the risk of financial hardship. Just in comparison to the average group death and TPD levels noted above, the average mortgages in Australia are now over $500k meaning group cover would not be sufficient to meet just this need of the surviving family.

Additionally, direct policies are underwritten and provide certainty for the insured, particularly given the work undertaken by the financial planner to pre-underwrite and manage the client through the underwriting process.

NMG Consulting research on the level of new business volumes shows that retail advised new business volumes have declined from $638 million in 2016, before the LIF reforms commenced, to just $317 million in 2021 (in contrast to the numbers quoted in the report). This number is expected to fall further over the next few years, driven largely by the following factors:

- The significant exit of financial planners from the profession and particularly those who are active in the life insurance advice market.
- The reduction in remuneration has made it economically unviable to provide life insurance advice to the bulk of the population.
- The APRA intervention in the Individual Disability Income Insurance market has led to substantial changes to Income Protection products, making it very difficult for generalist to come up to speed in terms of understanding these new products.

Overall, the number of financial planners who choose to provide life insurance advice has declined substantially and this has meant that it has become much more difficult for Australians to access.

Another consideration for the framework needs to be the size and quality of the insurance pool. The following table, based upon the APRA Claims and Disputes Statistics, highlights what has happened to individually advised clients in recent years. A combination of a decrease in the size of the pool and an increase in its average age has the effect of reducing the quality of the insured pool and creates risks for all policy holders.

Individual Advised Policy Holders – '000

Category	31-Dec-18	30-Jun-20	30-Jun-21	31-Dec-21	Cumulative % Change
Death Cover	1,994	1,717	1,653	1,621	-18.7%
TPD	1,177	996	968	972	-17.4%
Trauma	826	792	768	752	-9.0%
Disability Income	911	847	816	805	-11.6%

Financial planner remuneration

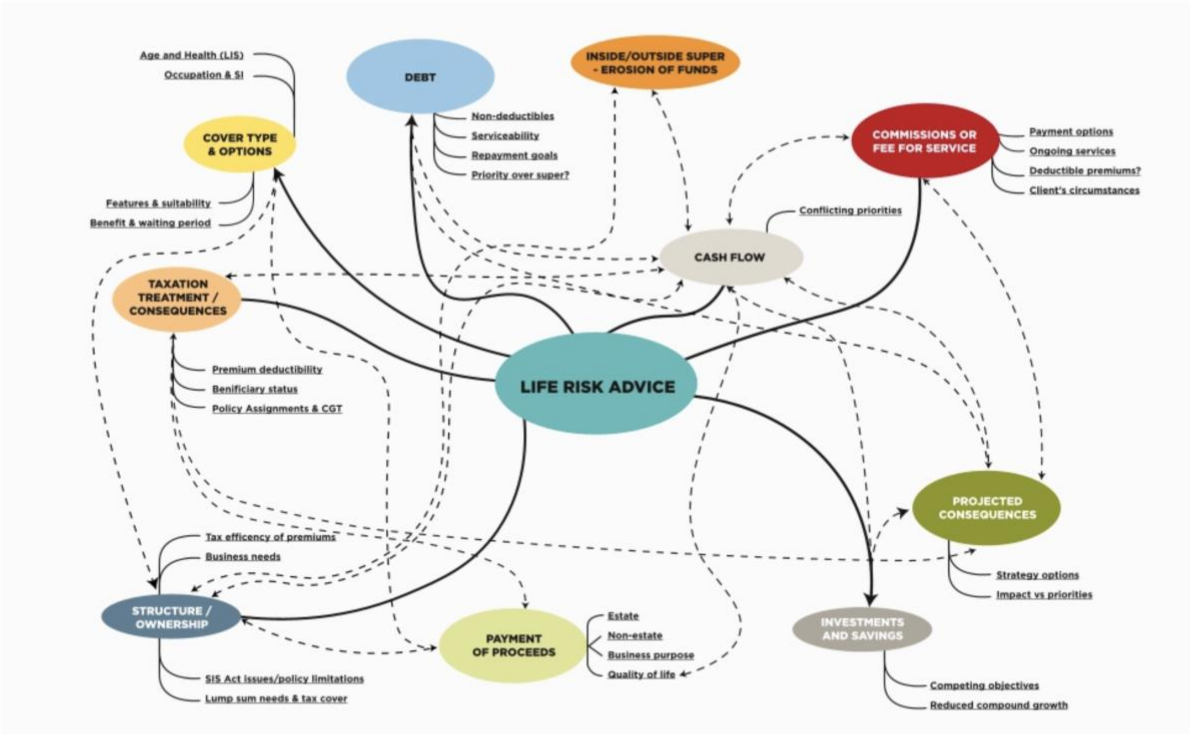
The FPA has long supported and required members to use charging models for professional financial advice which allow clients to understand how they are paying for advice, allow them to choose how to pay for advice and required clients to agree the fee with their financial planner. These obligations for FPA members were first developed in 2006 as the FPA Principles to Manage Conflicts of Interest and evolved into the FPA Financial Planner Remuneration Policy[2] released in 2010 and implemented from 1 July 2012. The Six Principles for financial planner remuneration developed by members were:

1. Clients must be able to understand the fees they are paying
2. Clients must be able to compare the fees they are paying
3. Clients must be presented with a fee structure that is true to label
4. Clients must be presented with fees that are separated between advice and product
5. Clients must agree the fee with their financial planner and can request that the fee is switched off if no on-going advice is required
6. Clients, rather than product providers, should pay for financial planning services, so as to remove potential for bias.

The exception to principle 6 related to life insurance commissions given the Remuneration Policy worked as part of the FPA Code of Ethics and FPA Code of Professional Practice to ensure advice was appropriate and in the best interests of the clients. Further, the challenges of the availability of commission free products at the time, the challenges in rebating commissions to clients, and finally the capability of all but a few life insurance clients to directly pay for advice could not be ignored. This was particularly in the context of the complexity that life insurance advice entails, as can be seen in the diagram below.

[2] https://fpa.com.au/wp-content/uploads/2017/01/2012_02_Financial-Planner-Remuneration-Policy.pdf

Example Mind Map of Life Risk Advice



FPA Life Risk Advice Guide (developed in collaboration with the AFA) – Example Mind Map of Life Risk Advice (page 21)[3]

With financial advice currently costing a minimum of $4,500 (without considering profit and business sustainability), there is little ability for financial planners to broaden the provision of advice to younger, lower premium clients, exacerbating the issues highlighted above. Member and consumer feedback has also consistently pointed to a preference (particularly among younger clients more in need of assistance with life insurance strategy) for paying for advice via commissions due to lower financial resources available to pay for advice up front.

[3] https://fpa.com.au/policy/policy-issues/life-risk-advise/

FPA response to consultation questions

General Insurance and consumer credit insurance (Proposal 1)

1. Do you support Proposal 1, which requires financial advisers or insurance brokers to obtain informed consent from their clients in order to be able to receive a commission from a product issuer for the sale of a general insurance product or consumer credit insurance?

a) If you do not support this proposal, please state your reasons

FPA position on proposed change:

The FPA supports the proposed recommendations.

This support is following the clarifications provided by the Review at meetings on 11 November 2022 in relation to the disclosure upfront of initial and trail commissions, the consent requirements from the client and in relation to ongoing service obligations.

Members have expressed concern (both publicly and privately) at the proposals in the paper in relation to what additional obligations would apply in relation to disclosure, consent and ongoing services given they already do this. We would encourage the final report to make clear that where these obligations are already complied with in relation to personal advice by a relevant provider, no additional obligations are required to be met.

Life risk insurance product (Proposal 2)

2. Do you support Proposal 2, which requires financial advisers to obtain informed consent from their clients in order to be able to receive a commission from a product issuer for the sale of a life risk insurance product?

a) If you do not support this proposal, please state your reasons

FPA position on proposed change:

Quality of Advice Review proposals

The FPA supports the proposed recommendations.

This support is following the clarifications provided by the Review at meetings on 11 November 2022 in relation to the disclosure upfront of initial and trail commissions, the consent requirements from the client and in relation to ongoing service obligations.

Members have expressed concern (both publicly and privately) at the proposals in the paper in relation to what additional obligations would apply in relation to disclosure, consent and ongoing services given they already do this. We would encourage the final report to make clear that where these obligations are already complied with in relation to personal advice by a relevant provider, no additional obligations are required to be met.

Ongoing Concerns with Life Insurance Market

Australians want financial advice to help them when they select life, TPD, income protection and trauma insurance. These products involve complicated application processes, have complicated contractual terms and complicated and varied tax treatments both in relation to premiums and benefits. Australians generally have little understanding of how to calculate an appropriate level of cover particularly when cashflow may be impacted. As shown in the example in the introduction, there are a lot of elements in the client's objectives, financial and personal position required to be considered to ensure appropriate cover is implemented for a client. The cost of this advice is often an obstacle and contributes to the dichotomy where insurance advice is often most needed at a time of life when people do not have capacity to pay for it.

The Life Insurance Framework (LIF) provides an opportunity for consumers to pay for financial advice indirectly, through commissions paid to financial planners by insurers. Many Australians would not be able to afford to pay for financial advice on life insurance by paying an upfront fee given the cost of providing advice.

As upfront and trail commission rates are closely regulated under the LIF, commissions no longer provide an incentive for a financial planner to recommend one insurance policy over another. The combination of clawbacks, the Financial Planners and Advisers Code of Ethics 2019, best interest duty and conduct oversight by the ASIC Financial Services and Credit Panel provide considerable consumer protection benefits from inappropriate life insurance policy sales. These measures have collectively disincentivised inappropriate cover recommendations, churning of policies and improved life cover outcomes for the clients of financial planners. This is evidenced by improvements in EDR claims through AFCA, conduct investigations by ASIC and the outcomes of ASIC's review of life insurance advice (seen in significant reductions in both instances of advice failing the best interest duty and leading to significant consumer detriment) and the limited number of regulatory enforcements taken off the back of this review.

Importantly, the LIF has allowed consumers to choose how to pay for their life insurance advice in a manner which provides them with choice and flexibility. Further, the professional standards framework has ensured there is clear disclosure and client acceptance of the remuneration model.

There are significant issues with just relying on the group super market (including the best financial interests test super trustees must comply with) in terms of appropriate life cover for individuals and there has been a significant decrease in the advised life market over the period LIF has been in operation. A combination of policy measures (LIF and 'Protecting Your Super') has led to an increase in underinsurance which decreased the global level of cover of everyday Australians. This creates significant social hazard and a notable risk to the government in needing to fund lifestyle shortfalls through the NDIS and social security systems.

The FPA believes life insurance companies should provide consumers with flexibility in how financial advice is paid for by creating new fee collection options and new products that offer transparent and commission-free options.

Additionally, given the challenges in supporting clients in the recommendation and implementation of life insurance policies, we would encourage the life insurance industry to consider standardising terminology, definitions and terms. At present, life insurers compete on the complexity of policy definitions, creating a knowledge asymmetry for consumers of their products and all but the most skilled financial planners. Documentation between insurance products is not easily comparable as insurance contracts and PDSs all have differing formats and different section ordering. This all adds to a perception that life insurance companies are hard to deal with by consumers and adds to the financial disengagement and underinsurance epidemic in this country.

The FPA therefore recommends that consideration be given to:

- defining a standard for describing product features;
- use of standard definitions in product contracts and descriptions; and
- a requirement that insurance policy documentation should have a standard ordering.

These considerations would make it significantly easier for consumers and their advisers to compare products to allow the selection of the most appropriate product to provide risk cover for the consumer. Under the current regulatory settings, it is difficult and costly for financial planners to comply with the product comparison requirements under the best interest duties, to the detriment of consumers.

It has also been raised in the past that the medical profession have significant issues with assisting consumers in providing medical reports to insurance companies. Each insurance company has its own medical questionnaire, so where a consumer is applying for multiple life insurance products from multiple providers, a doctor may need to complete a number of different medical reports just for the purposes of underwriting. This again adds significantly to the complexity and cost of obtaining insurance cover. The FPA would therefore also recommend that a single medical request form be developed which can be shared across insurers to better assist consumers in getting medical exams and obtaining cover.

Life Insurance Framework Review Outcomes

We are disappointed with the lack of transparency in relation to the results of ASIC's life insurance advice review and are unable to comment at this point on whether the existing remuneration limits are appropriate or not.

Many FPA members have ceased providing life insurance advice to their clients at current commission rates as they do not remunerate the financial planner sufficiently. Current commission rates fail to adequately compensate planners for either the work required to advise and implement insurance recommendations. There is additionally ongoing risk in relation to providing continuing service and support for the client given the risk of complaints and legal action in the event of an issue occurring at the time of claim (i.e. the cover having lapsed, the cover no longer being at an appropriate level, or the claim occurring in a policy exclusion areas) through no fault of the planner. Given these risks, many members of the FPA have chosen to cease offering life insurance advice services to their clients and instead refer them to others or scope out risk from their advice. This can be seen in the APRA and NMG data on cover levels and new policies written.

For these reasons, the FPA recommends a proper review of both the outcomes of the ASIC file review project and the APRA data collection project be undertaken as a separate review on the outcomes of the life insurance framework. This should include a further round of file reviews following the full conclusion of the Financial Planner and Adviser Professional Standards transition. Additionally, the review should consider the economic risks for the planner, the AFSL and the economy more broadly in relation to the current state of the life insurance market, distribution options for consumers, and professional support from financial planners.

Recommendation

The FPA supports the continuation of the existing exemption on life insurance commissions under the life insurance framework.

Time-sharing schemes (Proposal 3)

3. **Do you support Proposal 3, which recommends that the Government conduct a separate holistic review of time-sharing schemes and the way they are promoted?**

    a) **If you do not support this proposal, please state your reasons**

FPA position on proposed change:

The FPA remains concerned by the selling tactics and remuneration models in relation to time-sharing schemes but supports the proposal for a separate review to be conducted given the limitations of the Quality of Advice Review terms of reference.

Other Conflicted Remuneration exemptions (Proposals 4-7)

4. **Do you support Proposals 4 -7, which remove or modify the existing exemptions to the ban on conflicted remuneration?**

a) **If you do not support any of these proposals, please state your reasons**

b) **Do you consider there to be any unintended consequences related to the implementation of Proposals 4 -7?**

FPA position on proposed change:

Proposal 4

The FPA supports proposal 4 and welcomes the intent to align the Corporations Act with the EM and ASIC guidance.

Proposal 5

The FPA supports proposal 5. Remuneration for financial advice should be directly linked to advice services and provided with client consent. This exemption is counter to outcome and should be removed.

Proposal 6

The FPA supports proposal 6. This ensures all financial products including Tier 2 products operate under the same conflicted remuneration laws.

Proposal 7

The FPA supports proposal 7. There is no benefit in retaining redundant exceptions to the law.

General

5. **Do you have any other comments or feedback on the Quality of Advice Review Conflicted Remuneration Consultation Paper?**

The FPA does not believe enough time has been allowed to consider the outcomes of the ASIC file review or ASIC/APRA data gathering outcomes to properly assess the outcomes of the Life Insurance Framework review. Additionally given the other regulatory changes which have taken place during this period, more research and consideration of consumer outcomes in relation to life insurance cover is required. The FPA therefore recommends a standalone review is conducted, including more file reviews.

6. **Do you have any other comments on the regulation of conflicted remuneration under Chapter 7 of the Corporations Act?**

The FPA does not have any further comments.