

14 September 2010

The Chairperson  
Accounting Professional & Ethical Standards Board Limited  
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Dear Sir/Madam

### **Proposed Standard: APES 230 Financial Advisory Services**

We welcome the opportunity to make a submission on the proposed APES 230 ED.

As the holder of an Australian Financial Services Licence, a Principal Member of the Financial Planning Association and a member of the Association of Financial Advisers we are already subject to an extensive range of strict and onerous standards in relation to the provision of financial services.

We have a particular interest in the proposed APES 230 ED in that our board comprises members of the ICAA, CPA Australia and NIA and a number of our employees and representatives are also members of those professional bodies.

We agree with the fundamental principles in the proposed APES 230 ED that Members who provide Financial Advisory Services act in a Fiduciary Relationship (putting their Clients' best interests ahead of their own interests) and that in so doing they must remove conflicts of interest.

However, we consider that the proposed standard goes a step too far in the prescription of the basis of remuneration and, if implemented, may even serve to frustrate some of the objectives of the standard.

Our principal concern with the proposed standard relates to the overarching requirement for financial advisory services to be provided solely on a fee for service basis (as defined).

#### **1. Personal Risk (Life) Insurance**

The requirement for pure fee for service has no regard for how the provision of personal risk (life) insurance services operates in practice. In fact, it is our view that a fee for service basis for such services is totally unworkable without significant detriment to Members and Clients alike, which would only serve to exacerbate Australia's massive underinsurance problem.

We offer the following comments in support of this position.



- 1.1. The stance adopted in the proposed standard is inconsistent with the position taken by other professional bodies and the Government. The Financial Planning Association, for example, has excluded risk products from its Financial Planner Remuneration Policy until further consideration is given to such products. The Federal Government, under its Future of Financial Advice reforms, has also deferred dealing with commissions from risk products, noting that:

*“Insurance has different features from investment products, including the fact that there are no investment funds which might be used to pay for advice. Therefore, concerns about affordability and the potential for under-insurance need to be explored in this context.”*

(The Future of Financial Advice Information Pack, p4)

- 1.2. The whole essence of life insurance is to pool risk. In a similar vein, the current commission-based fee model provides the opportunity to pool revenues, which allows us to provide services such as claims administration and underwriting fairly and efficiently. There is nothing to suggest that a fee for service model in this area would improve the delivery of such services to our clients.
- 1.3. Not every life insurer provides policies on a no-commission basis, meaning that we may fail in our obligations to act in the clients’ best interests. Alternatively, if the responsibility to rebate any commission received were to fall on us, we would need to employ additional human resources and incur significant IT costs to attend to that process manually.
- 1.4. For those policies that are available on a no-commission basis, the reduction in premium is not commensurate with the amount of commission waived/rebated. In fact, we understand that the average premium reduction is only 15%-20%, which is significantly lower than the cost of providing the services. This is clearly not in the best interests of our clients.
- 1.5. The proposed standard puts Members at a competitive disadvantage with other advisers who can continue to offer personal risk insurance services under a commission-based model.
- 1.6. To propose that the new standard apply to existing and new clients ignores the magnitude of any transition process and how commercially unrealistic and impractical such a guillotine approach would be. In fact, the consequences of the proposed standard on our personal risk insurance business are so dire we consider that we would be left with no choice but to surrender our memberships of the professional accounting bodies or divest ourselves of that part of our business altogether.

***For the reasons set out above, we submit that risk products should be expressly excluded from the proposed standard until there is greater certainty about the treatment of such products under the Future of Financial Advice reforms and/or how the life insurers propose to modify the premium structures in their policies in the future.***



## 2. Asset-based fees

We disagree that an asset-based fee structure (to be distinguished from commissions) presents a conflict of interest situation in relation to the provision of investment services.

- 2.1. On the contrary and by way of an example, we currently outsource our clients' portfolio administration to a third party provider, who charges us on a wholesale basis using a tiered, asset-based fee scale. We pass on those fees directly to our clients, adding a margin to cover our role in the provision of the services. Under this model, fees are capped so that portfolios whose values exceed a prescribed threshold are charged a maximum amount. This represents a clear benefit for clients from such a fee structure.
- 2.2. It is important to understand and appreciate that an asset-based fee is a fee for service arrangement (and not a commission). In exchange for the fee charged to the client, the following services are typically provided:
  - Regular portfolio reviews and meetings (monthly, quarterly or bi-annually depending on the client's requirements and portfolio size);
  - Regular economic and investment market updates via email newsletter;
  - Invitations to seminar presentations (typically quarterly);
  - Monthly or quarterly portfolio reporting;
  - Portfolio administration services; and
  - Access to advisers via telephone or face to face meetings outside regular review meetings as required by the client.
- 2.3. Note also that most, if not all, platform administration service arrangements are charged on an asset fee basis, typically on a sliding scale.
- 2.4. Delivery of the above services involves significant hours of document preparation, administration, meetings, other client liaison, product research, compliance, etc. A significant proportion of this time cannot be directly attributed to clients and the asset-based fee scale is a fair, efficient and transparent method of allocating those costs.
- 2.5. If asset-based fees are fully disclosed in a manner clients are able to understand (which is required by law), which includes a dollar based estimate, clients are able to make a sound value judgement and there is no mischief.

***Clearly the focus should be on the quality and value of advice rather than cost or the method of charging. Clients are the best source of referrals for advisers. Therefore it is in an adviser's best interests to give high quality, ongoing, value-for-money service to their clients in order to retain business and generate new work.***

## 3. Other matters

- 3.1. The obligations in paragraph 6.2 may also be met in whole or in part by the provision of a Financial Services Guide (FSG) and so reference to a FSG should be made in addition to Statement of Advice.
- 3.2. Paragraph 7.8 should include a similar deeming provision to paragraphs 6.4 and 10.4, where a compliant Statement of Advice is provided by an AFS Licensee.



Please contact us if you require any further information.

Yours faithfully

**Paul Bodimeade**  
Managing Director  
Representative