

28 June 2017

The Chairman
Accounting Professional and Ethical Standards Board
Level 11, 99 William Street,
Melbourne, VIC, 3000.

Dear Ms Roxon,

Submission on APES230

We are pleased to have the opportunity to make this submission on APES230 (Financial Planning Services) in response to the APESB's Consultation Paper CP 01/17 of April 2017.

Background

The undersigned were the two member representatives in the Working Party which assisted the APESB throughout the development of the original version of APES230. The principles of that version were announced by the APESB in November 2012 after a comprehensive and unprecedented public consultation process of four years.

Those principles mandated a **genuine fee for service** approach to the provision of financial planning services by our members who are in public practice. The principles excluded all forms of conflicted remuneration. That is, they excluded commissions paid by third parties, commissions paid by clients (referred to in the industry as asset fees and often misleadingly labelled as "fees for service"), volume or production bonuses and all other forms of incentive payments designed to achieve or incentivise the accumulation of funds under management and the sale of financial products, including managed investments, direct real estate and shares, insurance, credit/loans and derivatives thereof.

The current version of APES230, which was published in April 2013, after an intense public and private campaign against the **original conflict removal/disclosure version** of the standard, introduced a diluted version of the standard that allows members to choose whether or not to receive conflicted remuneration. That is, members may choose the highest level of ethics, based on **conflict removal/avoidance** (thus precluding them from receiving any form of conflicted remuneration). Alternatively, members may choose the lowest level of ethics, based on **conflict disclosure** (thus allowing them to receive conflicted remuneration).

This unique approach to ethics in financial planning has become irreverently known in the industry as “optional ethics”. It has been the subject of ridicule amongst those who would suggest that the accounting profession is not the pinnacle of ethical practice that it often claims to be. Sadly, we must agree with these critics’ analysis.

Of course, from the point of view of those who campaigned against the original version of APES230, the “optional ethics” approach was commercially ideal. It achieved exactly what was intended, namely the continuation of conflicted remuneration and, as a result, an unchanged culture and “business as usual” for product selling.

In essence (with some additional disclosures), the current version of APES230 replicates the flawed and ethically-compromised regulatory regime in the Future of Financial Advice legislation. The words are different, but the consumer-unfriendly outcomes are much the same.

Recommended Action

As a profession which claims to serve the public interest and which seeks unqualified trust between ourselves and our clients, we respectfully submit that the only satisfactory way to resolve this problem is to amend APES230 so as to adopt the original principles publicly announced by the APESB in November 2012. That is, we must remove all forms of conflicted remuneration for our members and we must mandate a genuine fee for service approach to the discipline of financial planning.

If we don’t do that, the accounting profession’s reputation and the value of our designations will continue to suffer. No amount of spin and marketing of our professional “brands” will make any difference to that result because we will be seen as hypocrites, failing to practise what we preach. The public perception of much of the Australian banking/financial services industry is a good example of what may happen to our profession’s reputation if we don’t act decisively and clearly, as proposed above.

Objections to Change – “It can’t be done”

The principal objection to the change we propose is **“genuine fee for service can’t be done”**. This was also the principal objection between 2007 and 2013. Nevertheless, during the development phase of the current version of APES230, a large amount of written and verbal evidence was presented to the contrary, especially from successful practitioners, demonstrating that a genuine fee for service approach is possible, practical, desirable and even inevitable.

Since that time, much more evidence has accrued. Many stakeholders and commentators have reinforced the professional imperative and the commercial common sense of transitioning the financial advice industry to a genuine fee for service basis. Examples of this since 2014 are outlined below:

1) Financial Services Industry Associations

Industry associations report a growing interest in a genuine fee for service approach and an acceptance of its inevitability. For example, in 2016, the President of the Independent Financial Advisers Association of Australia (IFAAA) said: **“Financial planners approach us all the time to talk about what steps are necessary to achieve genuine independence as an adviser.....asset-based fees and commissions on all products, including risk and life insurance....(are) banned for IFAAA (members). Our members are the early adopters of something that is inevitable. It has its own momentum now.... these members aren’t just advocates.....they’re really inspiring and it’s a reminder of why we do what we do”**;

2) Financial Institutions

Financial institutions accept the inevitability of a fee for service environment. For example, in 2015, Craig Meller, the CEO of AMP, said: **“the life insurance advice industry is on a journey to implement a fee-for-service remuneration model. I think in the long term, it is going to be a fee-for-service world.....I think you’ll look at financial advice and say it is an entirely fee-for-service world.”** Only a few short years ago, a statement of this nature by the CEO of AMP would have been commercially inconceivable;

3) Banking Industry

The banking industry accepts that reform is necessary and possible. For example, in 2016, Brian Hartzler, the CEO of Westpac, said: **“We need to recognise, that as an industry, we have a trust gap. We need to recognise that we have not met the expectations of the community. People are saying things need to change. Things do need to change. The good news is they are changing.....from next month, we’re planning to remove all product related incentives across our 2,000 tellers in the Westpac branch network”**. Until recently, such a statement and practical action by a “big four” bank CEO would not have been possible, nor even considered necessary;

4) Superannuation Industry

Leaders of the superannuation industry have recommended that the financial services industry should be free of remuneration conflicts. For example, in 2016, David Whiteley, CEO of the Industry Superannuation Network, said: **“To restore public confidence, by 2020 the banking system should be free of all conflicted remuneration. What is required is a comprehensive ban on all incentives and commissions paid to all employees by all banks, including cashiers, business bankers and financial advisers.....A decision by the banks to cease paying all incentives by 1 Jan 2020, including all grandfathered commissions, is the circuit breaker needed to send a clear signal to the Australian community, parliament and regulators that the banks will stop cross-selling and up-selling superannuation and other products to consumers when it is not in their best interests”**;

5) Media

Reports in the mainstream media suggest that a move to a genuine fee for service approach is necessary and impossible to avoid if the accounting profession is to be trusted to deliver financial planning services in the public interest. For example, Andrew Robertson, senior reporter on the ABC's The Business said in 2015: **“The gold standard for financial planning was the original version of APES 230.....The saga of APES 230 is a story I have covered from the beginning, and in a nutshell, in its original form, it basically said that remuneration conflicts can't be managed, they need to be got rid of. Subsequently, the original 'gold standard' version was watered-down by the accounting bodies to establish a curious regime of optional ethics.....After successfully lobbying hard to have APES 230 watered down, it was encouraging to see CPA Australia, without acknowledging its mistakes of the past, announce.....that conflict-free advice makes good commercial sense”** and **“is in the public interest”**;

6) Parliamentary Inquiries/Regulator

There have been numerous parliamentary and other public inquiries into the practices and behaviour of the industry, all of which have concluded that conflicted remuneration has been responsible for much of the poor behaviour in the industry, including (uncomfortably for our profession), poor behaviour by practising accountants involved in selling managed investment schemes and self-managed superannuation funds. Evidence that has been recorded in those inquiries includes commentary from the Australian Securities and Investments Commission in 2014 that **“remuneration structures used in the financial advice industry create real and potential conflicts of interest that can distort the quality of advice”**. ASIC appears to conclude that not only are conflicts of interest inconsistent with providing quality advice but they are often not evident to consumers. Furthermore, ASIC appears to believe the most effective way to deal with this problem is to remove the remuneration structures that give rise to these conflicts;

7) Large Employers

A number of large employers have made arrangements with financial planners to provide remuneration conflict-free financial planning services to their employees/superannuants. For example, the Australian Defence Force, one of Australia's largest employers, established in 2014 a Financial Advice Referral Program. The Program consists exclusively of genuine "fee for service" financial planners. It has proved to be very popular with ADF members who are seeking to consult a financial adviser whom they can trust to offer advice in their best interests, not products. The Program seeks to overcome an increasingly observed phenomenon of financial advisers inappropriately recommending the commutation of a government-guaranteed indexed pension entitlement in order to "create" funds under management on which commissions or asset fees can be levied. There are 25 planners in the Program at present, while 15 more are being considered with a view to limiting the Program to 40 advisers;

8) Accounting Profession

The CEO of CAANZ, Lee White, wrote in 2016 (signalling a change of heart from the ICAA position in 2012): **"Now is the time to call a halt to the discussion that has taken place since the early 1990s and require planners and advisers to operate under stronger standards if they want to be viewed as putting the interest of their clients first. Progress needs to move from disclosure to removal of conflicts of interest. The industry already has a template for that goal in the independent Accounting Professional and Ethical Standards (APES) Board's ethical standard APES 230. When first proposed, the Board saw commissions and percentage-based asset fees as creating 'threats of self-interest for which no safeguards exist that can reduce the threats to an acceptable level'. Given the recent scandals, progress needs to pick up speed and remove the various forms of remuneration that lead to conflicts and replace them with hourly rates or fixed fees. Such a fiduciary rule could apply to all providers of financial advice, save investors millions of dollars and improve the nation's overall prosperity, as financial advisers would no longer be tempted to steer them to inappropriate products with higher fees and lower returns. Who knows, it might even restore investor trust in the nation's financial institutions?"** A similar change of position by CPAA is noted in item 5 above.

9) Industry Consultants

Many consultants in the financial planning industry are actively promoting a move by their clients to a genuine fee for service. For example, Jim Stackpool, who was commissioned by the APESB during the development of APES230 to provide evidence about best practice in the industry, wrote in 2017: **"I support the original APES230 strongly. I believe the industry status quo has actively contributed to less Australians seeking quality financial advice due in the main to the systemic dysfunction of a product-based and remunerated industry portraying itself as providing impartial financial advice. Through our programs I'm meeting**

increasing number of advice firms that not only thrive and prosper abiding by the original APES230 standards, but they can't meet the demand for their professional advice.....these are the best of times to build great professional advice brands”.

Objections to Change – “We should wait until.....”

We are expecting that the APESB will be lobbied by some in the industry to wait until the new government standards body, the Financial Adviser Standards and Ethics Authority (FASEA), has issued its mandatory code of ethics. The APESB will be urged to simply replicate that code for the accounting profession.

This is the same disingenuous delaying tactic that was successfully employed in 2012. At that time, the financial services industry demanded that the APESB should wait until the FOFA reforms became law and just reflect those in APES230. Ultimately, this was the position of the accounting bodies and with a few additional disclosure requirements is what the current version of APES230 actually does.

Given the political nature of FASEA, it is most unlikely that a “government-mandated” ethics code will go so far as to require universal across-the-industry adoption of a genuine fee for service approach. In addition, whatever unfolds with FASEA, we can be sure it will be highly controversial in the development phase and is likely to be some considerable time away before implementation (the earliest date proposed is 1 January 2020).

Therefore, we believe that as a profession, we have an urgent duty to show leadership in the public interest, to go beyond the minimum level required by the law and to mandate a “no remuneration conflict” principle for our members. The need for this reform is best summarised in the following question:

Is it reasonable for the public to trust qualified and licensed members of the accounting profession to offer financial planning advice that is in their client’s best interests?

Sadly, the answer must be ‘No’ (or at best, ‘maybe’). This is an unacceptable position for a group of people who claim to be professionals. It is what is driving our proposal for this reform of APES230.

Transitional Arrangements

We acknowledge that some accountants who are currently receiving conflicted remuneration may need time to make the transition to a genuine fee for service approach to the provision of financial planning services. Therefore, we recommend that members be given a reasonable period in which to do so. We suggest up to 3 years.

We also recommend that arrangements with clients entered into prior to the date of the commencement of the amended standard be “grandfathered”. In an ideal world, we would not allow “grandfathering”, however, we believe that this concession will mitigate any commercial impediments to the implementation of the principles in the standard.

Required Amendments to the Standard

The changes to the current standard required to achieve a genuine fee for service approach are neither extensive, nor complex. That’s because the current standard contains the Board’s original genuine fee for service principles announced in November 2012, after which certain clauses were added in April 2013 to reflect the dilution of the standard. Clearly, certain clauses and dates would have to changed or refined, along with a clause to reflect “grandfathering” (noted above). We would be more than happy to work with the Board to redraft the current standard.

Conclusion

Thank you for the opportunity to make a submission on this important topic. Adoption of the reforms to APES230 that we are proposing will:

- 1) **Show** significant ethical leadership by the accounting profession in the discipline of financial planning;
- 2) **Restore** the ambiguous reputation of the accounting profession, especially given our involvement in a number of high profile scandals and dubious activities, including managed investment schemes and self-managed superannuation funds;
- 3) **Convince** those accountants who are not involved in financial planning (due to their negative view of it as an unprofessional “product flogging” activity) that our members should be enthusiastically involved in this emerging professional activity;
- 4) **Encourage** more members of the accounting profession, especially younger people who want to make a difference in the community, to choose financial planning as a legitimate professional activity of which they can be proud;
- 5) **Create** a substantial and profitable new client base for accountants and an increasing source of client referrals, especially from Australians whose financial affairs have been poorly served by the conventional financial planning industry;
- 6) **Establish** the accounting profession as the natural leader in the profession of financial planning due to the combination of our ethical approach and our technical and educational training;

- 7) **Align** the interests of clients with the interests of their financial advisers, thereby offering an unqualified assurance to the community that members of the accounting profession can be trusted to act in their clients' best interests;
- 8) **Prove** that the accounting profession acts in accordance with the highest professional and ethical standards, rather than simply saying we do and failing to deliver;
- 9) **Demonstrate** that the accounting profession unreservedly acts in the public interest which must be the overarching objective of any true profession; and
- 10) **Influence** much needed ethical reform in the wider financial services industry.

If you have any questions, please contact us.

Yours sincerely,



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