

AGENDA PAPER

Item Number: 4

Date of Meeting: 5 April 2013

Subject: APES 230 *Financial Planning Services*

Action Required

For Information Only

Purpose

The purpose of this paper is to provide APESB Board with:

- The proposed APES 230 *Financial Planning Services*; and
- The Basis for Conclusions for APES 230 *Financial Planning Services*.

Background

The professional bodies submitted a project proposal to develop a proposed pronouncement to replace the current APS 12 *Statement of Financial Advisory Services* in August 2007. The Board established the APES 230 *Financial Advisory Services* (subsequently renamed *Financial Planning Services*) Taskforce to develop the proposed standard.

Consultation Paper

In 2008 APESB engaged June Smith of Argyle Partners to prepare a Consultation Paper to inform the development of the proposed APES 230. APESB released the Consultation Paper *Review of Miscellaneous Professional Statement APS 12: Statement of Financial Advisory Services* in October 2008 for public comment for a period of 3 months. APESB received five submissions from professional bodies, Firms and Members. The respondents' comments were considered at the May 2009 Board meeting.

Submission to the PJC Inquiry

In February 2009 the Parliamentary Joint Committee (PJC) on Corporations and Financial Services initiated an inquiry into Financial Products and Services in Australia to inquire into the issues associated with financial product and services provider collapses that occurred in 2007-08. In August 2009 APESB made a submission to the PJC inquiry as well as appeared before the inquiry. The PJC inquiry issued its report in November 2009. On 26th April 2010 the federal government released an information pack on *The Future of Financial Advice* which was in effect the Government's response to the findings of the PJC inquiry.

Development process for ED1

In March 2010, the APESB Board approved the proposed principles to be addressed in APES 230. At its June 2010 Board meeting the Board approved the issue of ED 02/10 Proposed Standard APES 230 Financial Advisory Services (APES 230 ED1) for public comment.

APES 230 ED1 was closed for comment on the 15th October 2010. APESB received 67 submissions from Members, Firms, commercial organisations, professional organisations and the joint accounting bodies.

At the November 2010 Board meeting, the Board agreed to issue a media release to the public advising of the major issues identified by respondents and communicate that there will be an extension of the time frame.

The key issues identified were:

- Operative date of APES 230;
- Definition of Fee for Service;
- Fiduciary duties;
- Application to Members in Business
- Application to insurance and risk products; and
- The retrospective effect of the proposed standard in respect of trailing commissions.

APESB issued a Media Release in December 2010 to this effect.

The Board considered the issues identified by respondents in the Specific Comments Table 1, 2 and 5 at the January 2011 Board Meeting. The preliminary analysis of the Specific Comments Tables 3-4, 6-9 and the General Comments table were considered by the Board at its March 2011 Board Meeting. At this meeting the Board determined to invite key stakeholders/respondents to present on the key issues to the Board.

APESB engaged in an extensive stakeholder consultation process during 2011 including public consultations with key stakeholders. APESB considered the various matters that were raised by key stakeholders at the public Board meetings as well as the respondents' comments to APES 230 ED1, and developed a revised APES 230 *Financial Planning Services Exposure Draft* (APES 230 ED2).

Development process for ED2

Technical Staff prepared an *Explanatory Memorandum* for APES 230 ED2 which documented the background, key issues considered, and the Board's rationale for the key decisions.

The Board issued APES 230 ED2 along with the *Explanatory Memorandum* in July 2012 for public comment. APESB received 163 submissions from professional accounting bodies, other associations, Members, Dealer groups, financial institutions, consumer groups, the regulator and other stakeholders.

Technical Staff prepared a Technical Analysis Paper and mapping tables of respondents' key issues in respect of APES 230 ED2 for the Board's consideration at the November 2012 Board meeting. The Board considered the respondents' issues and the APES 230 Technical Analysis Paper. The Board endorsed the principles in ED2 and determined that there should be transitional arrangements to allow Members time to transition their financial planning practices to a Fee for Service business model. The Board issued a Media Release to this effect in November 2012.

Subsequent to the November 2012 Board meeting, APESB received additional representations from ICAA and CPA Australia. The Board determined to delay the commencement date of the standard from 1 July 2013 to 1 July 2014 to allow stakeholders additional time and also determined to introduce an alternative remuneration model in respect of Professional Fees and Third Party Payments.

Professional Fees

Subsequent to the November 2012 Board Meeting, APESB determined to redraft the *Professional Fees* section of the Standard. The proposed APES 230 now provides Members with two alternative remuneration methods to comply with APES 230. The first alternative is for a Member to be remunerated on a Fee for Service basis as proposed in APES 230 ED2. This is the most effective safeguard against threats to the fundamental principles of the Code arising from conflicted remuneration.

The second alternative provides that the Member may charge professional fees on the basis of the Client's assets or funds under management (FUM) as long as the Member adopts specified safeguards to address the threats from conflicted remuneration as follows:

- obtaining written Informed Consent from the Client prior to commencement of the Financial Planning Service;
- making an annual disclosure to the Client; and
- thereafter obtaining written consent from the Client on a biannual basis.

Third Party Payments

Subsequent to the November 2012 Board Meeting, APESB determined to redraft the *Third Party Payments* section of the Standard. The proposed APES 230 now provides Members with two alternative remuneration methods to comply with APES 230. The first alternative is for a Member to be remunerated on a Fee for Service basis as proposed in APES 230 ED2 and to rebate any Third Party Payments received back to the Client. This is the most effective safeguard against threats to the fundamental principles of the Code arising from conflicted remuneration.

The second alternative allows for a Member who provides a Financial Planning Service in respect of life insurance, other risk contracts and procurement of loans to receive Third Party Payments as long as the Member adopts specified safeguards to address the threats from conflicted remuneration as follows:

- obtaining written Informed Consent from the Client prior to commencement of the Financial Planning Service;
- disclosing three comparative quotes where available;
- making annual disclosures to the Client on the estimated and actual amount of Third Party Payments received; and
- where applicable, disclosing to the Client the impact of any proposed changes to existing life insurance and other risk contracts and loans.

ASIC's Regulatory Impact Statement and Regulatory Guides

ASIC has recently released a Regulatory Impact Statement and Regulatory Guides in respect of the administration of the *FoFA* legislation which is attached herewith for the Board's information.

A summary of these ASIC publications is provided below.

ASIC's Regulation Impact Statement – Future of Financial Advice: Best interests duty and related obligations

In December 2012 ASIC released Regulation Impact Statement on *FoFA* best interests duty and related obligations. This document outlines ASIC's assessment of the potential regulatory and financial impact of their administration of the new obligation for advice providers to act in the *best interests of the client* and related obligations in Div 2 of Pt 7.7A in the *Corporations Act 2001*. It outlines the consultation process that ASIC underwent in determining how best to assist those providing personal financial advice to comply with the best interests duty and related obligations.

APESB has determined that the best interest duty and related obligations from *FoFA* should apply to all Clients in respect of Financial Planning Services, notwithstanding that *FoFA* does not apply to wholesale Clients and advice provided outside of an Australian Financial Services License. All Clients are entitled to be accorded the same duty of care and diligence from Members who provide Financial Planning Services.

ASIC's RG 245 on Fee Disclosure Statements

At the end of January 2013 ASIC released RG 245 Regulatory Guide on Fee Disclosure Statements. This guide applies to new and existing retail clients, with a limited number of items for which ASIC will take no action positions in respect of existing retail clients. It will apply to all fee recipients, i.e. financial planners/advisers from 1 July 2013.

Some of the key requirements include:

- Financial planners/advisers will be obliged to disclose the amount (in Australian dollars) of each ongoing fee paid by the client under the ongoing fee arrangement in the previous year which means that the fees must be stated as dollar amounts, rather than as a percentage of funds under management; and
- Commissions constitute a commercial arrangement between the product issuer and the financial planner and generally need not be disclosed. However, if the commissions are not disclosed then care must be taken in the choice of wording in the fee disclosure statements so that the Fee Disclosure Statement (FDS) does not mislead clients that it is the only payment received by the financial planner. If it is too difficult to determine the breakdown of commissions and advice fees then everything must be disclosed; and
- For commissions that were entered into with the clear consent or at the direction of the client must be disclosed. The mere existence of disclosure in the Statement of Advice (SOA) does not amount to consent.

This guidance from ASIC creates further challenges for financial planners/advisers in receiving conflicted remuneration and strengthens the position of APES 230 by supporting requirements to disclose dollar amounts for professional fees.

ASIC's RG 246 on Conflicted Remuneration

ASIC issued Regulatory Guide 246 *Conflicted remuneration* (RG 246) on 4 March 2013. RG 246 provides ASIC's final guidance to help industry understand the practical operation of the ban on conflicted remuneration and how ASIC intends on administering it. This guidance includes ASIC's definition of what constitutes conflicted remuneration and covers:

- volume-based benefits;
- performance benefits for employees;
- volume-based shelf space fees;
- asset based fees on borrowed amounts;

- transitional provisions; and
- the anti-avoidance provision.

Some key points from RG 246 include:

- the presumption that volume-based benefits are conflicted remuneration;
- examples of benefits that are generally conflicted remuneration include: Commissions, volume-based benefits, and fee discounts; and
- exclusions to conflicted remuneration include: 'grandfathered' benefits; benefits for advice on general insurance and life risk insurance products; consumer credit insurance; and execution-only services.

Staff Recommendation

Subject to the Board's review comments and editorials, the Board approve the issue of APES 230 *Financial Planning Services* and the accompanying Basis for Conclusions for APES 230 *Financial Planning Services*.

Material Presented

- Proposed Standard APES 230 *Financial Planning Services*;
- Basis for Conclusions for APES 230 *Financial Planning Services* (in progress and to be released on or after 4 April 2013);
- ASIC's Regulation Impact Statement – *Future of Financial Advice: Best interests duty and related obligations*;
- ASIC's Regulatory Guidance RG 245 *Guide on Fee Disclosure Statements*; and
- ASIC's Regulatory Guidance RG 246 *Conflicted Remuneration*.

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Date: 28 March 2013