22 October 2010

Ms Kate Spargo
Accounting Professional & Ethical Standards Board Limited
Level 7, 600 Bourke St
MELBOURNE VIC 3000

By email: sub@apesb.org.au

Dear Kate

Proposed Standard: APES 230 Financial Advisory Services

CPA Australia, the Institute of Chartered Accountants, and the National Institute of Accountants (the Joint Accounting Bodies) have considered the Exposure Draft and our comments follow. The Joint Accounting Bodies represent over 180,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally.

We welcome the opportunity to comment on the Accounting Professional & Ethical Standards Board (APESB) Proposed Standard APES 230 Financial Advisory Services.

The Joint Accounting Bodies believe that any professional standard for members providing financial advice must meet the principal objective of assisting the availability of quality, affordable and understandable financial planning advice throughout Australia, including all regional areas. We also believe that generally while it is the client who should be empowered to make an informed choice about the terms on which they choose to receive financial advice there is a need to ensure there is both an obligation and guidance to protect clients from inappropriate remuneration structures.

The proposed standard and the Future of Financial Advice (FoFA) initiative

Before any standard for members is finalised, consideration should be given to potential changes to the current regulatory landscape such as the proposed Future of Financial Advice (FoFA) reforms.

The FoFA reforms announced by the Government earlier this year will potentially implement the most significant and extensive changes to the financial planning industry since the introduction of Financial Services Reform in 2001. While these reforms will be aimed at improving both the trust and confidence of the consumer in the financial planning industry and strengthening consumer protection, they will require financial planners to undertake considerable changes to their practices and systems.

As part of the FoFA consultation process, Treasury has established a peak consultation group to review the reforms including professional standards for the industry, conduct and competency standards. The Joint Accounting Bodies have two representatives on this peak consultation group to represent the accounting profession. Given the significance of these reforms, we believe it is imperative that the APESB is also actively engaged in the FoFA consultations to ensure that it can both contribute to the process and be fully familiar with all outcomes.

The Joint Accounting Bodies call on the APESB to defer issuing a standard to replace APS12 for financial advisory services that regulates members who provide licensed financial planning advice until the outcomes of the FoFA reforms are known. There are many benefits for deferring the issue of the standard including:

- Primarily, avoiding any unintended consequences of implementing a standard which may conflict with potential Government regulation.
- Avoiding duplication between APESB issued standards and government regulation;
- Enabling consistency across the financial services industry.
- Ensuring equity across all financial planners so that Members of the Joint Accounting Bodies are not unfairly placed at a competitive disadvantage to others in the market.
- The opportunity to facilitate a more efficient transition of members' business systems and practices into a new environment.

In the interim, APS 12 *Statement of Financial Advisory Service Standards* would continue to apply to Members. Once the outcomes of the FoFA reforms are known, we believe that the exposure draft of the proposed standard APES 230 should be redrafted and reissued for further comment.

Comments on proposed standard

Notwithstanding our comments above, we also make the following observations in respect of the current exposure draft:

- The scope of the proposed standard needs to be refined because the inclusion of non-licensed strategic and structural advice has the potential to make the scope of the standard so broad that it will affect the way in which traditional public accounting services are provided.

- The effective commencement date of 1 July 2011 is unrealistic. The earliest effective date should align with the Government's FoFA reforms with an appropriate transition period and/ or extension where the requirements of the proposed standard are at a higher level.

- Fee for service should be the preferred remuneration model to reduce conflicted remuneration structures.

- In recognition of the complexities that exist in insurance and the new legislation regulating consumer credit advice commissions should not be banned on risk insurance products and other non-financial planning products.

- Percentage asset based fees substantially fulfil the characteristics required to be considered Fee for Service where they are determined taking into consideration the relevant factors listed in the definition of Financial Advice and therefore should not be unilaterally banned at this time.

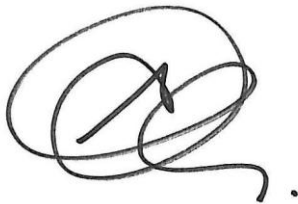
- The standard should be applicable to Members in public practice only, as employee members are not typically involved in the strategic and operational decision making of the business and therefore they are not in a position to influence the necessary changes to remuneration structures.

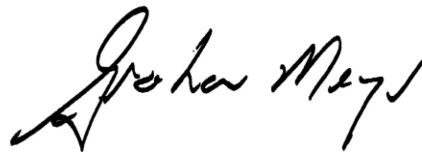
- Any implemented reforms should be on a prospective basis as there are considerable and often intractable issues when implementing retrospective standards (as demonstrated when legislative settings have tried to be implemented retrospectively).

We have attached in the Appendices both a summary of our recommendations (Appendix 1) and detailed comments outlining our concerns with the current exposure draft (Appendix 2). However we reiterate our principal recommendation which is to defer finalisation of the APES 230 until the outcomes of the FoFA reforms are known.

If you have any questions regarding this submission, please do not hesitate to contact Denis Pratt (CPA Australia) at denis.pratt@cpaaustralia.com.au, Hugh Elvy (the Institute) at hugh.elvy@charteredaccountants.com.au or Reece Agland (NIA) at reece.agland@nia.org.au.

Yours sincerely





Alex Malley
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Appendix 1
Summary of Recommendations

Principal Recommendations

- **Defer finalisation of APES 230 until the outcomes of the FoFA reforms are known.**

- **The APESB should become actively engaged and involved in the FoFA reforms consultation process.**

- **The proposed standard should be redrafted and reissued as an exposure draft for comment once the outcomes of the FoFA reforms are known. This will ensure consistency, avoid duplication and inequity, facilitate the transition of business systems and avoid any unintended consequences.**

Other Comments

While the Joint Accounting Bodies do not support issuing the standard at this time, we have reviewed the ED and make the following comments for consideration when that document is redrafted.

- Reforms which align with the proposed Government FoFA reforms should be identified and these reforms should have an implementation date no earlier than the date of these legislated reforms. All other reforms should have an operative of at least 12 months after this date.

- The scope of the proposed standard should be refined because including non-licensed strategic and structural advice has the potential to make the scope of the standard so broad that it will affect the way in which traditional public accounting services are provided. The scope's current definition may well also impact on the services provided by members and firms at a wholesale and corporate level.

- The ban on commissions should be prospective. Any implemented reforms should be on a prospective basis as there are considerable issues when implementing retrospective standards (as demonstrated when legislative settings have tried to be implemented retrospectively.

- Members should be encouraged to charge on a Fee for Service basis when providing risk advice. However in recognition of the complexities that exist in this area, the banning of commissions on risk products should be excluded from APES 230 and reviewed in due course.

- The definition of ***Commission*** be amended to remove reference to 'risk products'.

- Members who provide advice and services related to the procurement of loans and other borrowings provided pursuant to an Australian Credit Licence should be exempt from the requirement to only charge on a Fee for Service basis at this time. The following paragraph should be incorporated in Section 9.0 to reflect that Members are encouraged to charge on a Fee for Service basis where practical. However they can still be remunerated via commissions for the provision of risk advice and licensed credit activities:

  9.3 A Member who provides Financial Advice under either an Australian Financial Services Licence in relation to risk products or under an Australian Credit Licence in relation to credit activities should charge on a Fee for Service basis where practical.

- The scale of legacy products in the market combined with their complexities require appropriate provisions be included in APES 230, including a suitable definition, which should be based on the Government's description and be as follows:

  Legacy Product means a financial product that is closed to new Clients but remains in force due to existing client participation in the product.

- A new paragraph should be added to 9. Fee for Service to confirm Members who receive a commission from a Legacy Product will not be in breach of APES 230, provided they have met their recording obligations as follows:

  9.4 A Member whose Client holds a current interest in a Legacy Product is exempt from the provision of 9.2 provided the Member documents in a designated register the details of the Client and the legacy product in which they are invested in.

- Paragraph 9.2 be amended as follows to ensure it provides clear and concise guidance in regards to the charging of fees:

  9.2 A Member shall not charge nor receive Commissions for providing Financial Advisory Services.

- APES 230 provide principles based guidance for Members on how to charge on a Fee for Service basis for the Financial Advice they provide to their Clients and that this is achieved through deleting the second paragraph from the current definition of ***Fee for Service***.

- Should the Government elect not to prohibit percentage based asset fees on geared investments, this should be included in APES 230 when next reviewed.

- The standard be amended to be part of the APES 300 series that is applicable only to Members in public practice as employee members are not typically involved in the strategic and operational decision making of the business and therefore they are not in a position to influence the necessary changes to remuneration structures.

- The definition of ***Fiduciary Relationship*** and any other references be removed from the standard to avoid unintended consequences of introducing a fiduciary duty that is not clearly defined and may possibly conflict with Member's statutory fiduciary duty once implemented.

- The word 'Client' be removed from the definition of ***Commissions*** to avoid any confusion that a Member can receive payment from their Client for advice or services provided.

- The definition of ***Soft Dollar Benefits*** be reviewed to ensure that it does not have unintended consequences, such as preventing a third party from paying for advice where the Client is a Not-for-Profit company.

Appendix 2

Comments on Proposed Standard: APES 230 Financial Advisory Services

While the Joint Accounting Bodies do not support issuing the standard at this time, we have reviewed the ED and make the following comments for consideration when the ED is redrafted.

Proposed operative date – 1 July 2011

The effective commencement date and the lack of appropriate transitional provisions in APES 230 is a significant concern to the Joint Accounting Bodies. We believe that it poses a risk to the credibility of both the APESB and the accounting profession. Member feedback confirms that the majority of those affected will be unable to comply with the proposed standard in its current form within the short timeframe proposed. Further if they attempt to, it will impose an unreasonable burden of cost and time.

The APES 230 Exposure Draft requires Members to make fundamental changes to their business structures, review their current remuneration models and then consider how the firm will charge as a result of the proposed reforms to remuneration being proposed in APES 230.

For many public practitioners this may also include evaluating where future cash flows will come from given the proposed banning of receipt of all commission, which rightly or wrongly, may potentially threaten the profitability and possibly the viability of a Members' practice. The limited timeframe will not allow members to make the appropriate decisions for their businesses. Such revaluations may also affect covenants in place with lending institutions, impact the members' costs of servicing their obligations and access to ongoing finance in a tight credit market.

Of further importance is that Members are being compelled to make these significant changes not only in an extremely short timeframe but also following the Global Financial Crisis and its associated impact.

The 1 July 2011 operative date also fails to recognise that there will be existing Client arrangements in place, which cannot be amended during this timeframe or possibly at all in the case of Clients who have funds invested in legacy products.

Member feedback indicates a concern that the APESB is being unnecessarily hasty in pushing the new standard before the proposed Government reforms. Members are also concerned that it appears that the APESB have not taken into account the implications raised above when setting the proposed operative date for the standard. These same concerns were raised by the Joint Accounting Body representatives at the Taskforce during the drafting of the proposed standard.

It should also be noted that the review of APS 12 commenced in October 2008 and it has taken nearly 20 months of reviewing this standard before the release of the Exposure Draft of APES 230. This in itself is evidence of the extensive complexities that are embedded in this industry.

We strongly believe that the proposed start date of 1 July 2011 is both unrealistic and unachievable. It provides insufficient time for Members to make the necessary changes to their practices, market their new value proposition to their Clients and then transition to a Fee for Service remuneration model. Further time is required to allow Members to appropriately make this transition.

Recommendation:

- **Reforms which align with the proposed Government FoFA reforms should be identified and these reforms should have an implementation date no earlier than the date of these legislated reforms. All other reforms should have an operative of at least 12 months after this date.**

Scope of the proposed standard

The inclusion of strategic and structural advice that does not require a licence in the definition of ***Financial Advice*** has the potential to capture all advice provided by Members in public practice.

For example, Members in public practice regularly give advice on business matters including tax advice (as registered tax agents), appropriate business structures e.g. establishing, running, winding up companies, trusts, partnerships, buying and selling businesses, legal advice and underwriting share floats.

In addition, feedback from a wide range of members in practice and business indicates that there is a clarity issue in terms of the application of the proposed standard. An unintended consequence of this lack of clarity is its application to wholesale and corporate services and advice provided by members and their firms.

Recommendation:

- **The scope of the proposed standard should be refined as including non-licensed strategic and structural advice has the potential to make the scope of the standard so broad that it will affect the way in which traditional public accounting services are provided.**

Application of the proposed standard

The Joint Accounting Bodies are concerned at the inclusion of Members in business in the scope and application of proposed standard APES 230. Employee Members are not typically involved in the strategic and operational decision making of the business and therefore they are not in a position to influence the necessary changes to remuneration structures. These are the responsibility of senior management and the owners of the business. The inclusion of such Members in the final standard has the potential to force these Members to choose between their employment and maintaining their membership with their Professional Association.

Further, the Joint Accounting Bodies have no means to monitor or take practical action in relation to entities that are not Members. It would be a breach of the principles of natural justice to take professional action against a Member in relation to an issue they have no control over. Implementing a compulsory standard for Members that cannot be adequately monitored or enforced puts at risk both the credibility and effectiveness of the proposed standard.

Therefore to ensure the integrity of APES 230, the standard should be amended to be applicable to Members in public practice.

Further analysis is required to address the application of the proposed standard to the variety of entities and structures that members operate and the application to non-members within these entities. While the intent and principles are supported, there needs to be a detailed analysis of the practical application and monitoring of these different structures For example clear guidance must be issued to advise Members who will be required to adhere to the standard once issued where the Member does not provide Financial Advice but they do have an equity interest in a practice. This issue here is to identify at what stage would the proposed standard apply based on the equity holding of the entity.

Recommendation:

- **The standard be amended to be part of the APES 300 series that is applicable only to Members in public practice as employee members are not typically involved in the strategic and operational decision making of the business and therefore they are not in a position to influence the necessary changes to remuneration structures.**

- **Further analysis as to the application of the proposed standard to clarify its practical application to the various entity structures under which members operate.**

Remuneration - Fee for Service

The past two years have seen a shift in remuneration practices from what have been traditional charging methods to the financial adviser now setting a fee that is appropriate for the advice and reflects its value to the consumer. We believe this must be the underpinning principle of genuine fee-for-service remuneration and therefore support the intent of the remuneration reforms proposed in draft standard APES 230.

The Joint Accounting Bodies also strongly support principles based guidance. The implementation of a professional statement that is principles based ensures that it will be capable of being applied to a dynamic and evolving environment such as the financial services industry. It will also allow the Members of the Joint Accounting Bodies to use professional judgment on how they will comply with the provided guidance.

In setting any standard, it should be noted that the financial advisory services industry is highly regulated and Members already face a wide range of obligations from government, regulators and other associations.

Percentage based asset fees

The issue of fees and remuneration has been widely debated over the last couple of years and a key issue is to also ensure that clients are protected from conflicted remuneration structures.

The first paragraph of the definition ***Fee for Service*** which details the factors Members can consider when calculating their fee, has deliberately been broadly defined to allow Members the flexibility to determine the appropriate fee for the advice and service they will provide to each Client. This is consistent with the principles based guidance in APES 110, section 240.1 which states:

> *When entering into negotiations regarding services, a Member in Public Practice may quote whatever fee is deemed appropriate*

The factors listed in this paragraph include the level of training of the Member, the Member's staff, the degree of responsibility applicable to the work such as risk and time. Further factors that are not explicitly stated but will also be considered include costs to the business such as research, compliance and overheads. The final consideration will be the need for an inbuilt margin to ensure a profit is returned to preserve the viability of the business.

Our Members have indicated that they believe they can demonstrate that they use these same factors to determine their percentage based asset fees for their Clients. (With further clarification this may well align with APS 12 which states that 'A mere standardised percentage basis applied to all funds under management is not a fee for service.')

As the level of funds under management, or the degree of responsibility applicable to the work such as risk, is also considered to determine the level of fees that will be paid, these factors and costs are apportioned to each Client.

Therefore if ***Fee for Service*** did not explicitly exclude percentage based asset fees from its definition, percentage asset based fees would fulfil the requirements to be considered ***Fee for Service****.*

The ED states the fundamental reason why Members should only charge on a ***Fee for Service*** basis is to eliminate actual or perceived conflicts of interest. All methods of remuneration however have the potential to create actual or perceived conflicts of interest, even the proposed ***Fee for Service*** remuneration method proposed in APES 230 ED. It is therefore critical that a Professional Accountant use their own professional judgment to ensure that their objectivity and professional competence and due care is not compromised. This is consistent with the principles of APES 110.

We should also be mindful that the financial advisory services industry is now highly regulated and Members already face a wide range of obligations from Government, regulators and other associations. The Government will also be implementing further reforms through their Future of Financial Advice initiative, which will is likely to see the introduction of a statutory fiduciary duty to act in the Client's 'best interests' and the banning of percentage based asset fees on geared investments.

The Joint Accounting Bodies supports both of these proposed reforms and believe these initiatives will further mitigate any actual or perceived conflicts of interest in respect of remuneration.

We also believe that consistent with APES 110, APES 230 should provide principles based guidance for Members on how to charge for Financial Advice and the definition of ***Fee for Service*** should be amended by removing the second paragraph:

> ***Fee for Service*** means fees determined by taking into consideration factors such as the complexity of the Financial Advisory Service, the required skills and knowledge, the level of training
> and experience of the Member and the Member's staff, the degree of responsibility applicable to
> the work such as risk and the time spent on the Financial Advisory Service.
>
> ~~Fee for Service does not include Commissions, percentage based asset fees, production bonuses,~~
> ~~or other forms of fees or remuneration that are calculated by reference to product sales or the~~
> ~~accumulation of funds under management, whether paid by the Client or a third party such as a~~
> ~~product manufacturer.~~

This amendment will ensure the standard will be capable of being applied to a dynamic environment such as the financial services industry and that the Member, as a Professional Accountant, can use their own professional judgment, within the bounds of the law, to comply with the issued guidance.

(It should be noted that under the proposed FoFA reforms asset based fees for geared investments are to be banned. Should this not proceed it should be addressed when APES 230 is next reviewed.)

Recommendations:

- **APES 230 provide principles based guidance for Members on how to charge on a Fee for Service basis for the Financial Advice they provide to their Clients and that this is achieved through deleting the second paragraph from the current definition of *Fee for Service*.**
- **Should the Government elect not to prohibit percentage based asset fees on geared investments, this should be included in APES 230 when next reviewed.**

Proposed banning of commissions

It is widely accepted that commissions can create a conflict of interest. The financial planning industry for the most part has now accepted this, evidenced by many of the large financial planning dealer groups moving to a form of fee-for-service remuneration models prior to the Government announcing its intention to ban commission payments from 1 July 2012.

The proposed Government ban however currently both excludes commissions received on risk products, and will also be prospective in application. Both of these decisions are in acknowledgement of the complexities within the financial planning industry and the need for further consideration before making any final decisions. The Joint Accounting Bodies also support this approach.

APES 230 will also regulate advice and services related to the procurement of loans and other borrowings, including credit activities under an Australian Credit Licence (ACL). This proposed reform also warrants further consideration before final implementation as the impact of APES 230 should be considered in light of the legislation now implemented in this area.

Risk Products

The transition by the financial planning industry to move away from commission based remuneration has arguably been triggered by the Inquiry into financial products and services in Australia, which has resulted in the FoFA reforms and the Financial Planning Association (FPA) releasing its remuneration policy in 2009. Both of these currently exclude risk insurance.

The Government acknowledges that risk products have structural issues that differentiate them from investment products. Unlike investing, there are no investment funds which may be used to pay for this advice. It also acknowledges industry concerns regarding affordability of personal risk advice under a fee for service arrangement and fear that it may fuel the current under-insurance problem in Australia. Therefore the Government has proposed to delay the banning of Commissions on risk products until there is further industry consultation.

Risk advice, like all financial planning advice, requires both time and expertise to provide. Risk advice for an average consumer may require approximately ten hours to complete the needs analysis, prepare the statement of advice and organise the insurance cover to be underwritten with the insurer. Under a Fee-for-Service model this may cost $1500-$2000. The commission may however only be $500. Where the Client is a key partner in business, the process involved is much more complex and will also include analysing how the cover should be structured and held, as well as other key considerations to ensure the ongoing viability of the business. It is likely that this type of complex risk advice may cost the Client $10,000 to $15,000 under a fee for service remuneration model. Given that underinsurance remains a problem in Australia, the potential impact of banning of commissions on affordability warrants further consideration.

Further the risk insurance industry is largely based on commission based remuneration. The likelihood of the industry transitioning to fee for service remuneration must therefore also be considered. This issue has been discussed with a senior actuary within the risk industry who has advised they are aware of a number of insurers who are currently exploring how the commission can be separated from the cost of the premium so that these products can be sold on a genuine fee for service basis. This transition however will take some time. We also believe that those limited number of policies currently available on a no-commissions basis have only reduced their premiums by approximately 15-20%, which is not commensurate with the amount of commission being waived, significantly lower than the cost of providing this advice and therefore arguable not in the client's best interests.

Member feedback has also noted that should they be compelled to charge for Fee for Service for risk advice, while being placed at a competitive disadvantage they would also be required to employ additional staff and incur further IT costs to refund any commission they received manually to the Client. Some Members noted they would have no choice but to discontinue providing risk advice to their Clients. This is of concern to the Joint Accounting Bodies as potentially this may place the consumer at risk, especially in regional communities where there are limited licensed advisers.

A further consideration is that the trail income that the financial adviser is currently receiving is in fact their remuneration for the risk advice and services that they have previously provided to their Client, which they have elected to collect over a period of time. Given that each life insurance policy constitutes a separate contract between the consumer and the insurer, the financial adviser is now unable to ask the insurer to stop the payment of the trail commission and rather now have the balance of their fee paid so that they are paid for the advice they have provided and will comply with the proposed requirements of APES 230.

As previously stated, the Joint Accounting Bodies support the principles of APES 230 and the banning of commissions. We believe however that the banning of commissions on risk products should be excluded from the proposed reforms in APES 230 at this time, in line with the FoFA reforms.

There are complexities in this area that must be considered and insurers should be allowed further time to explore how they enable a smooth transition to fee for service, rather than simply electing to impose such an uncompromising reform on the Members of the Joint Accounting Bodies who provide risk product advice. To enable this recommendation, reference to 'risk products' should be removed from the definition of ***Commissions*** in the draft standard.

We believe that this position should be reviewed in due course to assess what developments have been made by industry during this time and what, if any further guidance may be necessary. Members

who provide risk product advice should still be encouraged to charge on a Fee for Service basis where practical.

Recommendations:

- **A prospective ban on commissions from 1 July 2012 as per the FoFA reforms**
- **Members should be encouraged to charge on a Fee for Service basis when providing risk advice. However in recognition of the complexities that exist in this area, the banning of commissions on risk products should be excluded from APES 230 and reviewed in due course.**
- **The definition of Commission to be amended to remove reference to 'risk products'.**

Procurement of loans and other borrowing arrangements

While some lenders do not pay commissions and a brokerage fee is charged to the Client, it is more common that mortgage brokers and other providers of credit advice are paid by way of an upfront and trail commission. Traditionally this has been largely unregulated. However this has changed with the implementation of the National Consumer Credit Protection Act 2009 (National Credit Act) regulated by ASIC.

Australian Credit Licensees and their representatives must now meet initial and ongoing requirements, including:

- A general conduct obligation to ensure that adequate arrangements are implemented so Clients are not disadvantaged by any conflict of interest that may arise either wholly or partly in relation to credit activities that the licensees or their representatives may engage in
- A well researched and comprehensive product list representative of the products on the market (being the market available to the Client)
- A credit guide that must be provided to the consumer which includes details any commissions that are likely to be received either directly or indirectly, including a reasonable estimate of the amounts and methods for working out those amounts; and
- They cannot provide credit assistance unless the consumer has been provided with a quote detailing any amount that will be payable by the consumer, which the consumer must also sign and date.

Commissions remain the dominant method of remuneration for credit brokers and intermediaries and there are no planned reforms to change this practice. However threats to independence and conflicts of interest that may have previously existed must now be addressed and adequately managed to ensure that the consumer will not be disadvantaged.

Given the implementation of this new and extensive regulation, the Joint Accounting Bodies do not believe requiring Members who provide licensed credit advice to charge purely on a Fee for Service basis is warranted at this time. The new disclosure requirements and the mandatory requirement to ensure all conflicts of interest are adequately managed largely mitigate any mischief that may have been an issue prior to the new regulation.

Recommendation:

- **Members who provide advice and services related to the procurement of loans and other borrowings provided pursuant to an Australian Credit Licence should be exempt from the requirement to only charge on a Fee for Service basis at this time. The following paragraph should be incorporated in Section 9.0 to reflect that Members are encouraged to charge on a Fee for Service basis where practical. However they can still be remunerated via commissions for the provision of risk advice and licensed credit activities:**

9.3 A Member who provides Financial Advice under either an Australian Financial Services Licence in relation to risk products or under an Australian Credit Licence in relation to credit activities should charge on a Fee for Service basis where practical.

Legacy Products

It is common in the managed investment industry for products to be closed to new investors due to changes in commercial practices. Legislative, regulatory and tax developments also result in financial products becoming outdated. These products are then known as 'legacy products'.

The Financial Services Council (FSC) has estimated that the total amount of funds under management in legacy products may amount to $221 billion or approximately 25% of all funds under management.

The Government is working to establish a product rationalisation framework. This is because Clients invested in legacy products cannot simply be moved into a new product due to the structural, legal and institutional environment in which these products exist, coupled with the need to balance the interests and rights of the beneficiaries. For instance, in the case of life insurance each policy constitutes a separate contract between the consumer and the product provider.

Given the scale of these products and the complexities involved, appropriate recognition and provisions should be included in the final APES 230 standard.

The Joint Accounting Bodies recommends that a legacy product should be defined in the standard and provisions inserted to ensure a Member will not unintentionally breach the new standard where their Client is invested in a legacy product that pays a commission. The onus will be on the Member to demonstrate that where they are receiving a commission from a Legacy Product, that they have recorded both the details of the Client and the product in a separate register. This register must then be made available for review upon request of the Members' respective Joint Accounting Body.

The definition of a legacy product should be based on the Government's description of these types of products[1] and be as follows:

> ***Legacy Product*** means a financial product that is closed to new Clients but remains in force due to existing client participation in the product.

The following paragraph should then be included in 9. Fees to confirm that Members will not be in breach provided they have met their recording obligations for such products:

> **9.4** A Member whose Client holds a current interest in a Legacy Product is exempt from the provision of 9.2, provided the Member documents in a designated register the details of the Client and the legacy product in which the Client is invested in.

Recommendations:

- **The scale of legacy products in the market combined with their complexities require appropriate provisions be included in APES 230, including a suitable definition, which should be based on the Government's description and be as follows:**

  Legacy Product **means a financial product that is closed to new Clients but remains in force due to existing client participation in the product.**

- **A new paragraph should be added to 9. Fee for Service to confirm Members who receive a commission from a Legacy Product will not be in breach of APES 230, provided they have met their recording obligations as follows:**

9.4 A Member whose Client holds a current interest in a Legacy Product is exempt from the provision of 9.2 provided the Member documents in a designated register the details of the Client and the legacy product in which they are invested in.

Further amendments to Paragraph 9. Fee for Service

Feedback from both Members and the industry has suggested that the requirements detailed in Paragraph 9. Fee for Service require further clarification. There is a view that a Commission could still

[1] *Product Rationalisation Issues Paper*, The Treasury 2007 p. 11

be accepted by a financial adviser depending on whether the Commission is charged by the financial adviser as opposed to the financial adviser receiving a Commission paid by the product provider. To provide clarity on this point we recommend paragraph 9.2 is amended to the following:

9.2 A Member shall not charge nor receive Commissions for providing Financial Advisory Services.

This amendment in conjunction with our previous recommendations will ensure that there is no confusion in regard to acceptable remuneration practices and will ensure that Members are not in breach of the standard due to circumstances beyond their control.

Recommendation:

- **Paragraph 9.2 is amended as follows to ensure it provides clear and concise guidance in regards to the charging of fees:**

9.2 A Member shall not charge nor receive Commissions for providing Financial Advisory Services.

Consistency in APESB issued guidance

The Joint Accounting Bodies are concerned that the principles and guidance being proposed in the APES 230 ED may not be consistent with other guidance that has been issued by the APESB.

The APESB has proposed the banning of commissions in the APES 230 ED on the basis that they cause a conflict of interest. We note that the APES 110 Code of Ethics for Professional Accountants ED has been amended to remove the specific reference allowing a Member who is a financial adviser from receiving a commission. We raise the issue that other Members in Public Practice who do not provide ***Financial Advice*** and therefore will not be subject to the proposed requirements of APES 230 will still be allowed to receive a commission from the sale of goods or services to Clients.

The proposed blanket ban of commissions in APES 230 would infer the APESB believe Members who are Financial Advisers are unable to use their own professional judgment to ensure their objectivity and professional competence and due care is not compromised.

The Joint Accounting Bodies suggest that this apparent inconsistency be addressed to ensure that all guidance issued by the APESB is fair and equitable for all Members.

Recommendation:

- **All guidance issued by the APESB for Members in Public Practice should be consistent across all APESB provisions and equitable between all Member groups, as currently there appears to be inconsistencies between the APES 110 Exposure Draft and the APES 230 Exposure Draft in respect of commissions.**

Fiduciary responsibilities of Members

A fiduciary relationship gives rise to a higher standard of care and duty than one based in statute or contract. The Joint Accounting Bodies support the concept that Members providing financial advice have a fiduciary responsibility to their Clients. However we are concerned this inclusion may have unintended consequences.

There is evidence that the duties of a financial planner already include certain fiduciary obligations, evidenced by both case law and the fact the Financial Ombudsman Service (FOS) often refers 'to the investor relationship as in financial planning as fiduciary' in their determinations. The elements of a fiduciary relationship however are not currently articulated in legislation, but rather are embedded in common law.

APES 230 ED does not provide sufficient discussion or detail on the actual expectations of this requirement. For example, what constitutes the 'Client's best interests' is ambiguous and open to interpretation. Further, whilst paragraph 4.5 demonstrates that the level of action required by the Member to discharge their fiduciary duty varies depending on the circumstances, it fails to provide any guidance on what this may entail. This is of concern given that FOS and the courts may look to this standard for guidance and make their own interpretation as to what this may mean.

The Joint Accounting Bodies raise the issue as to whether it is appropriate to directly link fiduciary responsibilities to a specific remuneration model. For example, it is possible that in certain circumstances fee for service remuneration may not be in the client's best interests.

The Government's *Future of Financial Advice* reforms also include a proposal to introduce a statutory fiduciary duty on all Australian Financial Services Licensees and their authorised representatives to act in the best interests of their Clients. The Government has advised that this will include a 'reasonable steps' qualification that must be undertaken to discharge this duty. While what will constitute 'best interests' and 'reasonable steps' is still to be developed in consultation with industry, we understand that it will be detailed and provide licensed financial planners with a clear message of what will be expected. It is also possible that the Australian Securities and Investments Commission (ASIC) will provide further guidance to demonstrate what will be expected from both licensees and their representatives. Even without this detail, the Government has advised it will not expect a financial adviser to make an assessment of every product available in the market in order to act in the 'Client's best interests'.

There is also a risk that the fiduciary duty being proposed for Members in APES 230 may conflict with what will become their statutory fiduciary duty once it is defined and implemented by Government.

Taking into consideration these concerns the Joint Accounting Bodies recommend that the definition of **Fiduciary Relationship** and any other references be removed from the standard in order to avoid any unintended consequences.

Recommendation:

- **The definition of Fiduciary Relationship and any other references be removed from the standard to avoid unintended consequences of introducing a fiduciary duty that is not clearly defined and may possibly conflict with Member's statutory fiduciary duty once implemented.**

Definitions

Commissions

The definition of ***Commissions*** in the APES 230 ED prohibits a Member from receiving a monetary amount from a Client. This may be an oversight and should be amended as follows to ensure that a Member can receive payment from their Client for advice or services provided:

> ***Commissions*** means all monetary amounts received by a Member from an Australian Financial Services Licensee, ~~Client,~~ or other party, in respect of placement or retention of the Client's funds, or purchases or sales of financial or risk products, and includes trailing commissions and income.

Recommendation:

- **The word 'Client' be removed from the definition of 'Commissions' to avoid any confusion that a Member can receive payment from their Client for advice or services provided.**

Soft Dollar Benefits

Member feedback has suggested that the definition of ***Soft Dollar Benefits*** may potentially capture circumstances where a third party may pay for the advice of a Client where the client is for example a Not-for-Profit company. Whilst it may not be the intention of the proposed standard to capture these situations, we believe that it warrants further consideration to avoid any unintended consequences.

Recommendation:

- **The definition of *Soft Dollar Benefits* be reviewed to ensure that it does not have unintended consequences, such as preventing a third party from paying for advice where the Client is a Not-for-Profit company.**