Compliance;
The Advisor in a Post RC Paradigm

March 2019 InterPrac Financial Planning Conference

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InterPrac

Helping accountants and financial planners deliver professional financial services for their practices

Agenda

- **Reflection**
- **The Royal Commission & Financial Planning**
  - Findings
  - Likely outcomes
- **InterPrac and ASIC**
  - Surveillance
  - Action against AR's
  - Complaints
  - Business Rules
- **Major Hot Spots**
  - FDS
    - Uploading of FDS and Renewal Notices (Opt Ins) for 2018
  - Best interest
  - FASEA and CPD

Agenda

- **Conflicted Renumeration / Commissions / Grandfathering**
- **AML / CTF**
- **AIOFP Lobbying – Pamela Anderson and the FSU**

Morning Tea

- **The Compliance Panel**
  - Shane, Richard & Tadeya
  - Kaplan
  - Talking FDS, CPD & Trips and Traps for Advice

Reflection

“It is easy to get lost in the long grass of negative sentiment and miss the opportunities to soar through blue sky.”

The Royal Commission

Summary of recommendations for financial advisers

1.	All fee arrangements to be renewed annually. Prior to opting in each year, the client must be provided with a clear statement of services and fees to be charged.
2.	Advisers must send the product provider the client's written authority before fees may be deducted from an account.
3.	Fees may not be deducted from a MySuper Account.
4.	If you are unable to say that you are independent, impartial or unbiased you must provide a clear written statement to the client as to why this is the case before making a recommendation.
5.	All Grandfathered remuneration will cease before 1 January 2021.
6.	Life insurance commissions will continue until the ASIC review in 2021 with the likelihood of the cap reducing, possibly to zero.
7.	Measures to improve the quality of advice will be reviewed by the government.

The Royal Commission

Summary of recommendations for financial advisers - Continued

8.	Advisers will need to register with a Professional Disciplinary Body.
9.	No unsolicited offering of superannuation or life insurance products.
10.	Greater reference checking and cooperation with AFCA.
11.	Quarterly compliance 'concerns' reporting to ASIC and the PDB.
12.	Fees for No Service – must stop; remediation is necessary.
13.	Systems and monitoring – licensees will need to improve their systems and processes for monitoring advisers.
14.	Regulation – ASIC to become more litigious and will prosecute in relation to more offences.

Ongoing Fee Arrangements

The Commissioner recommended that **fee arrangements become annual** as opposed to the biennial arrangements currently in place under the FOFA Scheme.

This **will apply to every client**, not just new clients and there will not be any grandfathered clients.

The Commissioner recommends that the **annual fee arrangement only commence after the client has been given a clear statement of the fees and services.**

Ongoing Fee Arrangements

Note the **services must be clearly defined and not be vague** in any way. The way some advisers have described their services to clients in the past was sternly criticized by the Commissioner.

Other recommendations in relation to ongoing fee arrangements include:

- A fee for the services may only be deducted from an account if the client has given their express written authority to the account provider.
- Only when the account provider has this authority will it be permitted to deduct fees and pay them to the adviser.
- These authorities will expire every year.
- Fees may not be deducted from a MySuper account.
- Fees may be deducted from a Choice account but only upon the written authority having been received by the account provider as referenced above.

Fees for No Service

In making the above recommendations, the Commissioner was attempting to deal with the Fees for No Service issue.

It is noted he has referred at least three entities to the regulatory authorities for further investigation, and it would seem prosecution, in relation to taking fees and not providing services.

The Commissioner repeated his statement in the interim report that "charging for what you do not do is dishonest" (p 133).

Among a series of critical observations of the industry regarding Fees for No Service, the Commissioner referred to problems with services being poorly described such that the adviser was under no real obligation to provide anything. In other words the promise was illusory which could amount to misleading conduct in itself. The Commissioner also referred to services that promised nothing of any real value to the client, and yet this was not reflected in fees which were of real value to the adviser. He raised the lack of transparency associated with taking fees from accounts and, in addition, the fact these fees were often still being deducted many years after the initial agreement with the adviser was struck. In such cases the client had naturally forgotten what had been promised, and often the adviser had as well.

Fees for No Service

A lot of the Commissioner's criticism in this area lay in the **fact that entities had not remediated clients or were slow in doing so**.

This was evidenced in the hearings and the Commissioner inferred this was because of two main reasons:

1. A lack of systems and processes capable of monitoring and managing the receipt of Fees for No Service and which ensure that services, as promised, are provided.
2. The poor culture existing in many financial services businesses, if not across the industry generally. Culture is something the Commissioner spent particular time on and addressed by way of separate inquiry.

The impression one takes from the Final Report is that Fees for No Service is one of the most egregious issues raised at the Commission. It is widespread and it raises questions of honesty.

As a result, we can expect an ongoing priority for ASIC in the future will be the receipt of fees for no service.

Conflicts

In the Commissioner's view, the poor quality of advice that was exposed in the Royal Commission hearings is partly due to the conflicts of interest and duty that exist in the industry, that is the conflict between duty to client and interests of the adviser. To address this, he made several recommendations, including:

Grandfathered commissions should cease to be paid.

The Government agrees. As a result, all remaining remuneration for financial products (other than life insurance) that has been paid to date as grandfathered commissions (including, it would seem, bonuses and such payments) will cease before the end of 2020. The Government will monitor the industry's progress to the cessation date by requiring ASIC to report to it on this over the period 1 July 2019 to 1 January 2021.

Conflicts

ASIC should continue with its foreshadowed review of life insurance advice due in 2021.

Life insurance commissions were also subject to the Commissioner's recommendations. The Commissioner agreed that ASIC should continue with its foreshadowed review of life insurance advice due in 2021. He said this should result in a reduction to the caps on life insurance commission and in his view, he said, they should be reduced to zero, unless there is clear justification to do otherwise.

On the subject of commissions, the Commissioner recommended general insurance commissions and commissions paid in respect of credit insurance should be reviewed before 31 December 2022.

Conflicts

Disclosure around using the term independent, unbiased or impartial.

Another recommendation of the Commissioner was in relation to disclosure. Presently the law prohibits an adviser from using the term independent, unbiased or impartial. The Commissioner recommends that if this prohibition applies to you and you cannot use one of those terms, then before you make a recommendation to a client you must provide them with a clear written explanation as to why. If this applies to you, this would normally be because at least some of your income is commission of some kind.

Quality of Advice

The Commissioner was concerned with the general quality of advice presented at the hearings. He said the **new FASEA requirements will be of some assistance**, but he also recommended that the requirements which regulate and try to improve financial **advice should be reviewed by Government** by 30 June 2022 and no later than 21 December that year.

Commissioner Hayne queried the **effectiveness of the safe harbour provisions** of the Corporations Act. He said that there is nothing in the safe harbour checklist which really requires the client to be given a recommendation which is best for the client, even if it is not in the interests of the adviser.

The safe harbour provisions reduce the obligation to act in the best interests of the client to a checklist of processes which may or may not result in the adviser acting in the client's best interests. He said the review referred to in the preceding paragraph should consider the relevance of the safe harbour provisions. It may be this is replaced with a fiduciary duty or something like that, as was argued during the FOFA debate.

A Profession

The Commissioner says: ***"One hallmark of a profession is the existence of a credible and coherent system of professional discipline where the ultimate sanction is expulsion from the profession." (p.198).***

The Commissioner recommended that **advisers be individually registered with a professional disciplinary body (PDB).** This would not replace ASIC and it would not replace the role of the licensee. ASIC would still be the statutory regulator with powers to investigate and refer to the Director of Public Prosecutions for prosecution. Advisers would still be required to operate under the supervision of a licensee. But in addition, advisers would have to register individually with a professional body.

A Profession

The PDB would be able to impose additional standards on the industry by way of de-registration or non-renewal of registration. It would be able to impose sanctions on advisers when licensees fail to and its disciplinary powers would travel with the adviser from licensee to licensee.

Why not continue to rely on ASIC?

Apart from its investigation powers, ASIC has a power to ban advisers, but this is usually reserved for matters at the more serious end of the range. The PDB would be able to impose sanctions and make requirements of advisers in relation to lower grade matters and because of this be able to act quicker than ASIC or where ASIC is unable to because of the burden of the law or lack of resources.

The Commissioner also recommended **stronger reference checking and information sharing along the lines of the ABA's protocol**. He suggested a breach of the protocol by an AFSL should amount to a breach of their license conditions.

Compliance

The Commissioner recognised that licensees have different compliance and audit systems and ways of dealing with breaches. He encourages ASIC to continue its on-site supervisory approach, the **Close and Continuous Monitoring Program** and suggested that further guidance be issued on best practice audit and consequence management.

The Commissioner also recommended that **Licensees report to ASIC on a quarterly basis**, not just in relation to breaches that may have been identified but also in relation to 'compliance concerns'. These would also be reported to the PDB. Licensees would be required to cooperate with AFCA under a legislated obligation and, for 12 months, AFCA's jurisdiction would extend to complaints that have not been previously heard and which are up to 10 year's old - longer than the existing six-year period under the statute of limitations.

Entities, not just licensees, operating in financial services would be required to **take steps to assess culture and governance**, deal with them and assess the effectiveness of this treatment. This is likely to require an objective review, possibly an independent review, of the systems, culture and record of every business in the industry, in respect of compliance, risk management and related matters.

InterPrac, ASIC and AFCA

Learning outcomes from Banning of Tai Nguyen

- Dates of documents and MetaData
- Signing Binding Death Benefit Nomination Forms

Learning outcomes from other Bannings, ASIC action

- Previous 12 month Ban is now 10 years and Permanent Bans are the new norm.
- ASIC still working through Advisers identified by institutions.
- EU's are becoming rarer and being replaced with licence conditions, prosecutions and cancellations for AFSL's and Banning action for AR's

Surveillance is on-going against most Mid and Large AFSL's

AFCA (Australian Financial Complaints Authority)

- The Good News is that we have no complaints against existing advisers.
- The Bad News is that AFCA see themselves even more so than FOS as a means to compensation for consumers.
- Recent activity includes a “Potential Systemic Issue Notice”.
- We are currently fighting 6 complaints that involve an adviser that left InterPrac in January 2013.

Business Rules

- To be launched over the next month
- The Business Rules are to replace the current Compliance Manual which is outdated and primarily directed at the AFSL not the AR
- Currently working on 12 Business Rule documents that will provide guidance on our expectations for AR's in regard to topics such as:
  - SMSF Advice
  - Advice Process
  - TPB
  - CPD
  - AML/CTF
  - Best Interest Duty
  - Breaches and Incidents
  - FDS/Renewal Notice requirements

Fee Disclosure and Renewal Notices

- Major focus of ASIC
- Richard will cover in some detail during the panel
- AFSL requirement to hold data on FDS
- Need to upload all FDS and Renewal Notices for 2018
  - Actual FDS provided
  - Completed and Signed/Returned Renewal Notice
  - Base document establishing the Ongoing Service Agreement

Best Interest

A fundamental principle of Advice is that be <u>Appropriate</u>

- it must not mislead or deceive
- it should not recommend, or result in, unconscionable conduct
- it must align with the what you reasonably know of the client's situation
- any recommended, enabling products must be fit for purpose

Fundamental principles in the provision of Advice Services include:

- the law must be obeyed (e.g. corporations law & regulations, common law & equity, contract law, consumer law, tax law, social security law … to name just a few)
- the adviser must act fairly
- the adviser must comply with industry codes

Additionally, both Advice and the provision of Advice Services must be demonstrably seen to be in the Best Interest of the client.

- the Best Interest duty is encapsulated in the Safe Harbour steps

Step	To Satisfy the Steps for Safe Harbour s961B(2) Description	Advice Process
1	Identify the objectives, financial situation and needs of the client that were disclosed by the client through instructions	Fact Finding File Notes
2	Identify the subject matter of the advice sought by the client (whether explicitly or implicitly)	Fact Finding File Notes
3	Identify the objectives, financial situation and needs of the client that would reasonably be considered relevant to the advice sought on that subject matter (client's relevant circumstances)	Fact Finding File Notes
4	If it is reasonably apparent that information relating to the client's relevant circumstances is incomplete or inaccurate, make reasonable inquiries to obtain complete and accurate information	Research File Notes
5	Assess whether the advice provider has the expertise required to provide the client with advice on the subject matter sought and, if not, decline to provide the advice	Adviser competence
6	If it would be reasonable to consider recommending a financial product: conduct a reasonable investigation into the financial products that might achieve the objectives and meet the needs of the client that would reasonably be considered relevant to advice on that subject matter; and assess the information gathered in the investigation	Research Risk Profiling File Notes
7	Base all judgements in advising the client on the client's relevant circumstances	Statement of Advice Record of Advice
8	Take any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interests of the client, given the client's relevant circumstances	'Catch all'

FASEA and CPD

- Shane and Brian Luke from Kaplan will present later on this topic
- Importance of completing CPD or suffer issues with ASIC

All new entrants from 1/1/2019 will need to complete a PY when entering the industry and will have the title Provisional Financial Adviser.

- 1600 hours (100 hours structured training and 1500 hours work)
- Supervisor must have 2 years of experience
- PY plan will need to be prepared and define key direct and indirect supervision activities
- PY not required if the provider is returning after a career break

Conflicted Remuneration, Commissions & Grandfathering

- The change is that effectively the requirement is to demonstrate that remuneration received is not conflicted
- FUA fees
- Commissions on Life Insurance policies
- Grandfathered books of business need to be reviewed over the next 12 months to ensure that the clients are able to be serviced if Grandfathering is removed by 2021

AML/CTF & Cyber Breach Policy

- Austrac are not happy with the financial planning industry because compared to Banking and other areas we provide few reports.
- We must be aware of our obligations to:
  - Identify the people we are receiving Instruction from (Includes Companies and Trusts)
  - Identify and report suspicious matters

- The other issue in this space are the changes to Identifying and reporting Privacy Breaches.

Maintain information governance and security — APP 1 and 11

Entities have an ongoing obligation to take reasonable steps to handle personal information in accordance with the APPs. This includes protecting personal information from misuse, interference and loss, and from unauthorised access, modification or disclosure.

Suspected or known data breach

A data breach is unauthorised access to or unauthorised disclosure of personal information, or a loss of personal information, that an entity holds.

Contain

An entity's first step should be to **contain** a suspected or known breach where possible. This means taking immediate steps to limit any further access or distribution of the affected personal information, or the possible compromise of other information.

Assess

Entities will need to consider **whether the data breach is likely to result in serious harm** to any of the individuals whose information was involved. If the entity has reasonable grounds to believe this is the case, then it must notify. If it only has grounds to suspect that this is the case, then it must conduct an **assessment** process. As part of the assessment, entities should consider whether **remedial action** is possible.

Organisations can develop their own procedures for conducting an assessment. OAIC suggests a three-stage process:

- **Initiate:** plan the assessment and assign a team or person
- **Investigate:** gather relevant information about the incident to determine what has occurred
- **Evaluate:** make an evidence-based decision about whether serious harm is likely. OAIC recommends that this be documented.

Entities should conduct this assessment expeditiously and, where possible, within 30 days.

If it can't be done within 30 days, document why this is the case.

Take remedial action

Where possible, an entity should take steps to reduce any potential harm to individuals.

This might involve taking action to recover lost information before it is accessed or changing access controls on compromised customer accounts before unauthorised transactions can occur.

If remedial action is successful in making serious harm no longer likely, then notification is not required and entities can progress to the review stage.

NO — **Is serious harm still likely?** — **YES**

Notify

Where **serious harm is likely**, an entity must prepare a statement for the Commissioner (a form is available on the Commissioner's website) that contains:

- the entity's identity and contact details
- a description of the breach
- the kind/s of information concerned
- recommended steps for individuals

Entities must also notify affected individuals, and inform them of the contents of this statement. There are three options for notifying:

- **Option 1:** Notify all individuals
- **Option 2:** Notify only those individuals at risk of serious harm

If neither of these options are practicable:

- **Option 3:** publish the statement on the entity's website and publicise it

Entities can provide further information in their notification, such as an apology and an explanation of what they are doing about the breach.

In some limited circumstances, an exception to the obligation to notify the Commissioner or individuals may apply.

Review

Review the incident and take action to prevent future breaches. This may include:

- Fully investigating the cause of the breach
- Developing a prevention plan
- Conducting audits to ensure the plan is implemented
- Updating security/response plan
- Considering changes to policies and procedures
- Revising staff training practices

Entities should also consider reporting the incident to other relevant bodies, such as:

- police or law enforcement
- ASIC, APRA or the ATO
- The Australian Cyber Security Centre
- professional bodies
- your financial services provider

Entities that operate in multiple jurisdictions may have notification obligations under other breach notification schemes, such as the EU General Data Protection Regulation.

AIOFP & the FSU – Our lobbying partners

- The Mortgage Broker campaign was the best example that I have seen in getting legislation changed.
- Pamela Anderson is representing the AIOFP and the Industry in lobbying to Canberra with the help of the FSU.

Questions?