JOINT AIST AND ISA SUBMISSION

FoFA Post-Implementation Review

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ABOUT INDUSTRY SUPER AUSTRALIA (ISA)

Industry Super Australia is a research and advocacy body for Industry SuperFunds. ISA manages collective projects on behalf of a number of industry super funds with the objective of maximising the retirement savings of over five million industry super members. Please direct questions and comments to:

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ABOUT THE AUSTRALIAN INSTITUTE OF SUPERANNUATION TRUSTEES (AIST)

The Australian Institute of Superannuation Trustees is a national not-for-profit organisation whose membership consists of the trustee directors and staff of industry, corporate and public-sector funds.

As the principal advocate and peak representative body for the $700 billion profit-to-members superannuation sector, AIST plays a key role in policy development and is a leading provider of research.

AIST provides professional training and support for trustees and fund staff to help them meet the challenges of managing superannuation funds and advancing the interests of their fund members. Each year, AIST hosts the Conference of Major Superannuation Funds (CMSF), in addition to numerous other industry conferences and events.

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FOFA POST-IMPLEMENTATION REVIEW

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INTRODUCTION

Industry Super Australia (ISA) and the Australian Institute of Superannuation Trustees (AIST) appreciate the opportunity to provide comment to Treasury's Consultation Paper, as part of the Post Implementation Review (PIR) on the regulatory impact of Future of Financial Advice (FoFA) reforms. The Consultation Paper states that the aim of the review is "to help the delivery of efficient regulatory outcomes and prevent unnecessary red-tape".

The FoFA reforms were several years in the making and were developed in response to a series of high profile and distressing instances of financial collapse including Great Southern, Westpoint, Opes Prime, Trio and Storm Financial.

The detailed work of several Parliamentary Committees which examined in detail the causes and impact of these collapses, particularly the 2009 Report on the Storm and Opes Prime collapses, confirmed that conflicted remuneration structures coupled with the absence of a requirement for advisers to act in the best interests of their client were key contributing factors to the collapses, and unanimously and explicitly recommended that reform be undertaken to address these deficiencies in the law.

After several years of consultation the FoFA reforms were legislated, premised on two key pillars:

- The banning of the receipt of conflicted forms of payment for financial advice; and
- The imposition of a requirement for financial advisers to act in the best interests of their clients.

The PIR focused on 5 measures announced on 28 April 2011. It is important to remember that at that time there was a hung Parliament and a number of compromises were reached to secure the FoFA reforms.

There has now been sufficient time for industry to adapt to the changes and to consider whether the 5 measures announced in 2011 should continue to have a place in a system which has a key objective to end the placement of self-interests over client interests.

The evidence suggests that despite the FoFA reforms, the financial industry continues to be plagued with too many examples of individuals and firms behaving in ways that maximise their interests, but leave consumers worse off. The culture of sales-driven financial advice is not desirable or sustainable and will cost the economy, consumers and the industry much more in the medium to long term. So, while the FoFA reforms have had a significant impact in mitigating some of the risks in the industry, more needs to be done to ensure that consumers are being connected to high quality providers with products that deliver the appropriate benefits to them. To this end, any regulatory change must be considered through the premise that the FoFA objectives are paramount, and superior to the aims of the PIR (ensure efficient regulatory outcomes and prevent unnecessary red-tape).

It is crucial that as part of this PIR the industry does not take a backward step by re-permitting conflicted forms of remuneration and or lowering conduct requirements. If this were to occur, then the likelihood of future scandals are considerably increased, some would say a certainty. If anything, this PIR should encourage industry to further reduce the instances of any misalignment that exists between advisers and consumers.

To this end:

- The ban on up-front and trailing commissions and like payments for both individual and group risk insurance within superannuation needs to be extended to general insurance, and to all individual and group life insurance regardless of whether it is within superannuation or not, in order to:
  a) protect the integrity of the financial system;
  b) ensure consumers are being provided products they need; and
  c) financial advisers are acting in their clients' interests.

  An ASIC report found that 96 per cent of the poor advice was given by advisers paid under commission models.[1] The evidence also suggests that the availability of commissions on individual risk policies in non-default super creates an incentive for advisers to recommend non-default products due to lucrative commissions attached to insurance that can be paid for out of those super products. The mis-selling of insurance is a serious problem and creates issues for not only the consumer but the industry as a whole. Additionally, mis-selling creates insufficient market outcomes as there is inadequate competition on the quality of the insurance. Stronger action is needed to tackle this problem.

- The requirement for advisers to renew client agreements for ongoing advice fees every two years (opt-in regime) needs to be an annual requirement. There continues to be a multitude of embarrassing examples of advisers deducting fees for services that have not been provided. One way to reduce the risk to consumers is to require advisers to have regular contact with their clients about fee arrangements. In fact no rational reason has been provided as to why advisers, who collect an annual fee, cannot annually confirm with their client the on-going fee arrangements for a further year. Once a year is a far from regular contact.

- Soft dollar benefits are conflicted remuneration and have no place in a system of integrity, trust and a system which purports to protect consumers by ensuring the availability, accessibility and affordability of high quality financial advice.

- The double standard that exists by carving-out segments of the financial industry from conflicted remuneration structures and best interests duty is unacceptable. This is more so when one considers the alarming regularity of related scandals. The banking industry has demonstrated that it should not be afforded special leniency, because unless it is specifically required to put its consumers first it will fail to do so.

However, one of the most successful aspects of the FoFA reforms has been the introduction of scaled advice. The view that there is uncertainty around whether ADIs can remain compliant with the best interests duty and still provide scaled advice appears to be an unfortunate pretext to lower conduct obligations. Scaled advice has provided consumers with access to advice they would not have ordinarily received and in the superannuation sector, one administrator reports increases in uptake averaging 46,000 additional statements of advice per year since 2012.

[1] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 42*.

The ban on up-front and trailing commissions and like payments for both individual and group risk insurance within superannuation

The FoFA reforms did not extend the ban on conflicted remuneration to all **individual** life insurance sales under personal advice nor does the ban extend to general insurance.

The ban on up-front and trailing commissions and like payments only applies to:

- a group life risk policy inside superannuation (regardless of whether it is for a default or another type of superannuation fund); and
- an individual life insurance policy for the benefit of a member of a default fund (MySuper products).

The ban on up-front and trailing commissions and like payments is limited. This limited scope reduces the prospects of:

1. removing conflicts of interest in the financial services industry;
2. advisers putting the needs of their clients first;
3. creating an efficient regulatory system.

The Government's stated objective for this regulation was to ensure that the remuneration structures of *life insurance advisers* were appropriately aligned with the interests of their clients.[2] It is difficult to see how this objective could be met under the current regulation, as the ban on up-front and trailing commissions and like payments for both individual and group risk insurance do not apply to all life insurance inside and outside superannuation (or for that matter general insurance). When an adviser provides a retail client with personal advice, the nature of the relationship, including the differences in knowledge and sophistication, establishes a relationship of trust and confidence between the parties. Clients deserve, and the law should require, advisers to act in a way that respects that trust: advisers should owe their clients unflinching loyalty. The best interest obligation, in concept, accomplishes this goal, however its limited application to a portion of the financial services industry is unsound.

The Consultation Paper also stated that a reason why the best interests duty did not extend the ban on conflicted remuneration to all individual life insurance sales under personal advice was because the "government did not want to eliminate a channel for distributing life insurance cover given this could increase levels of underinsurance in the Australian community."[3] This exemption, however, does not achieve the stated objectives. Underinsurance in Australia cannot be solved by sacrificing consumer interests. If consumers are being sold insurance they do not need or that is not in their interests, the issue of underinsurance is not solved, but a new problem is created. In fact there are a plethora of examples listed in ASIC's report 413: Review of retail life insurance, dated October 2014, which show that consumers are being sold insurance they do not need. ASIC found that some advisers recommended clients retain existing default insurance arrangements inside superannuation, while also recommending the client purchase new insurance outside superannuation. In many cases, ASIC found very little rationale as to why this was a suitable option for the client. In many of the other poorly rated files, the adviser did not even consider the existing product as an option.[4]

[2] *Post-Implementation Review Future of Financial Advice, Consultation Paper, p 6*

[3] *Post-Implementation Review Future of Financial Advice, Consultation Paper, p 6*

[4] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 59.*

By failing to extend the ban of up-front commissions and trail commissions to all life insurance (whether inside or outside superannuation) and general insurance, the industry has accepted that it will tolerate the provision of poor advice. This is akin to turning a blind eye to bad advice being provided.

Another reason for not extending the ban to all life insurance products was the concern that financial advisers will exit the market because of the loss of business and or revenue and this will lead to lessening of competition.[5] This concern is unsupported. The evidence shows that in fact since the FoFA introduction there are more financial advisers. In May 2009, there were "just over" 18,000 financial advisers in Australia.[6] As at 31 December 2016, there were "over 25,300" financial advisers recorded on the ASIC financial advisers register.[7]

Therefore the rationale for the not extending the ban to all life insurance products does not withstand scrutiny.

However, even if the argument that financial advisers will exit the market because of the loss of business and or revenue and this will lead to lessening of competition was accepted, which it is not, there is a fundamental concern with the view that competition is needed at all costs, i.e. at the costs of consumers being sold products that are not in their best interests.

This carve-out, along with the scandals involving conflicts of interests and failures to put the clients' interests first continue to undermine the credibility of the financial services system. Increasing distrust and a lack of confidence in financial advisers and the financial system persists.

The Government should remove the exemption in relation to the ban on commissions for all life insurance products and general insurance to ensure the availability, accessibility and affordability of high quality financial advice. The distinction between insurance purchased within or outside superannuation is arbitrary and irrelevant to the need for regulation across all life insurance. Efficient regulatory outcomes should not expose certain consumers to the heightened risks of being sold products by persons who have no duty to put their client's interests ahead of their own interests merely because the insurance is being purchased outside the realms of superannuation.

The ban of commissions in retail life insurance is demonstrably overdue.

In October 2014 ASIC released its review of retail life insurance[8] dispelling the myth that there were no problems in insurance advice and providing a damning report card on Australia's retail life insurance advice industry.

According to ASIC:

> *"… surveillance results indicate that many advisers giving post-FoFA advice may prioritise their own interests in earning commission income ahead of the interests of the client in getting good quality advice"*.[9]

The ASIC report raised a number of examples of scandalous advice being provided to consumers. ASIC observed that:

- more than a third of advice (37 per cent) did not meet the laws relating to appropriate advice, a result that ASIC describes as an 'unacceptable level of failure[10]'

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[5] *Post-Implementation Review Future of Financial Advice, Consultation Paper, p8*

[6] *Ripoll Report, 2.41 referencing IBIS World Industry Report, Financial Planning and Investment Advice in Australia, May 2009, p 7*

[7] *ASIC Report 515 "Financial advice: Review of how large institutions oversee their advisers", dated March 2017, p 17.*

[8] *ASIC Report 413 "Review of retail life insurance advice', October 2014*

[9] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 41.*

[10] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 6.*

- 96 per cent of the poor advice was given by advisers paid under commission models[11]
- where an adviser is paid under an upfront commission model it has a statistically significant bearing on the likelihood of that adviser giving advice that did not comply with the law.[12]

These findings demand a change. The industry cannot regain the confidence of consumers until commissions are banned from all insurance arrangements.

ASIC stated that:

> "…….*surveillance suggest that dependence on upfront commission remuneration arrangements has a material effect on the type of advice an AFS licensee's business will give, and increases the possibility that the business may give advice that does not comply with the law*".

Commission structures result in excessive churn of life insurance policies, with clients often recommended to change cover to attract the more generous level of commissions in the first year of cover. ASIC found that high upfront commissions give advisers an incentive to write new business. The more premiums they write, the more they earn. There is no incentive to provide advice that does not result in a product sale or to provide advice to a client that they retain an existing policy unless the advice is to purchase additional covers or increase the sum insured. ASIC's findings illustrate just how vulnerable consumers are. The availability of commissions on individual risk policies in non-default super creates an incentive for advisers to recommend non-default products due to lucrative commissions attached to insurance that can be paid for out of those super products. ASIC noted in many cases, consumers had the option to increase their life insurance cover in their default superannuation fund at a low cost and obtain additional insurance cover inside that fund, but found that such advice was rarely given to clients.[13]

ASIC ultimately concluded that there was a clear link between conflicted remuneration and the quality of advice:

- "Our findings confirm that adviser incentives affect the quality of advice consumers receive."[14]
- "A remuneration arrangement tied to a product sale creates an incentive for the adviser to make a sale, rather than provide non-product-specific advice or strategic advice for which the adviser may not be paid."[15]

There are serious risks of further mis-selling erupting in the financial services industry and stronger action is needed to tackle this problem. The issues unearthed by ASIC validate the view that commissions have no place in a financial services system which purportedly operates on integrity and trust and in the best interests of the consumers. We cannot become desensitised to the magnitude of the damage that is been caused to consumers and the financial services industry due to the endless examples of poor, self-interest based behaviour by advisers. It is no accident that remuneration structures have been created in a way which supports business interests and adviser interests above consumer interests.

ASIC's finding are compelling

> *"…commission incentives for advisers are operating in such a way as to distort and/or influence the behaviour of advisers. This has real commercial effects on insurers, on the price of life insurance products and on the quality of advice consumers receive."*[16]

Not only are the exemptions to the ban on conflicted remuneration unsupportable, the three alternatives outlined in the Consultation Paper also are unsatisfactory:

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[11] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 42.*

[12] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 42.*

[13] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 59.*

[14] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 42.*

[15] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 43.*

[16] *ASIC Report 413 "Review of retail life insurance advice', October 2014, p 39.*

1. Ban insurance commissions in relation to MySuper only
2. Ban insurance commissions in relation to group policies in superannuation only
3. Ban commissions in relation to all life insurance policies in superannuation and commissions in relation to all other all life insurance products.

All the alternatives are not feasible in achieving the objectives of FoFA. The first and second alternatives leaves advisers free to put self-interests ahead of client interests in a significant portion of the financial services sector, which clearly undermines the FoFA reforms. Alternative 3 does not go far enough because it does not cover general insurance.

One of the fundamental goals of the FoFA reforms has been to produce a uniform approach to the provision of high quality advice. This cannot be achieved if we are unevenly applying the rules by allowing carve outs to exist. If the objectives of FoFA (which are primary) are to be met then the regulation needs to be expanded to ban all up-front and trailing commissions and like payments for both individual and group risk insurance in and outside superannuation as well as in general insurance.

The requirement for advisers to renew client agreement to ongoing advice fees every two years (opt-in regime)

ISA and AIST have consistently advocated for an annual requirement for advisers to renew their agreement with their clients to deduct ongoing advice fees.

Purchases of advice by retail consumers in other industries, such as legal, medical, accounting, architectural or engineering services, are charged on a one-off time or service-based fee model. Proper fee-for-service arrangements, which are one-off or paid by instalment and which relate to a particular piece or quantity of advice, are more likely to generate a professional and product-neutral advice industry.

Given the potential for ongoing fees to replicate the ill effects of commissions and other conflicted forms of remuneration, the renewal requirement is critically important to the FoFA reforms. The renewal requirement is a key safeguard which enables consumers to understand the fees they are paying for ongoing financial advice and to make a further assessment about whether they are receiving value for the fees paid. It is vitally important that the industry puts in place a structure that further:

- minimises the potential for fees to be passively earned by advisers; and
- protects against the unnecessary erosion of the client's superannuation and other assets.

An annual opt-in regime is one way in which the government can strengthen the protection for consumers from the "forgotten" fees eroding retirement benefits. Whilst the measure of bi-annual opt-in arrangements aim to minimise the risk, the risk of two years' worth of unnecessary fees being deducted from member benefits is unacceptable. It is not acceptable or plausible to suggest that an annual opt in requirement would place a significant burden on advisers to contact their clients. Surely if the adviser is being paid an annual fee, it is reasonable for that adviser to make annual contact with the client, in fact they are required to provide annual fee disclosure. The rationale that an annual opt-in arrangement would place a significant burden on industry, as advisers would have been required to contact their clients annually does not hold up to scrutiny.

The financial services industry is riddled with scandals related to advisers charging ongoing fees when no ongoing advice is being received by the client.

In October 2016 ASIC released a report[17] about the systemic 'fee-for-service failures'— which related to instances where customers were being charged a fee to receive an ongoing advice service, but had not been provided with this service because:

1. the customer did not have an adviser allocated to them; or
2. the adviser allocated to the customer failed to deliver on their obligation to provide the ongoing advice service, and the advice licensee failed to ensure that the service was provided.

At the time, ASIC identified that AMP, ANZ, CBA and NAB have all identified systemic issues in relation to the charging of ongoing advice fees for no service.[18]

In May 2017 ASIC reported that AMP, ANZ, CBA, NAB and Westpac have so far repaid more than $60 million of an expected $200 million-plus total in refunds and interest for failing to provide general or personal financial advice to customers while charging them ongoing advice fees.[19] Whilst the report notes most of the breaches related to pre-FoFA reforms, it demonstrates an extraordinary failure by these institutions to consumers. Perhaps if none of the breaches related to post FoFA matters, we could be more confident that the existing FoFA reforms would stop these disasters occurring. However, this is not the case. The evidence is clear, further reform is needed to reduce the risk of fees unnecessary eating into retirement benefits.

An annual requirement for advisers to renew their agreement with their clients to deduct ongoing advice fees is a simple and informative measure to assist members if required, in preserving their retirement benefits from being unnecessarily eroded.

The rationale for not having an annual opt in arrangement has not been substantiated. The regulatory standards, in an environment when systematic breaches continue to occur, need to be lifted. Additional consumer protection is crucial and an annual requirement is far from burdensome.

The ban on soft dollar benefits over $300 per benefit

Conflicted remuneration is any benefit given to an AFS licensee, or its representative, that provides financial product advice to retail clients that, because of the nature of the benefit or the circumstances in which it is given, could reasonably be expected to influence:

1. the choice of financial product recommended to clients by the AFS licensee or representative; or
2. the financial product advice given to clients by the AFS licensee or representative.

It is accepted that non-monetary benefits (or commonly known as "soft dollar" benefits) are a form of conflicted remuneration, and for this reason many (but not all) forms of soft dollar benefits have been banned. The following soft dollar benefits are not banned:

1. benefits given or authorised by the client
2. benefits in relation to general insurance benefits
3. benefits of a small value $300
4. benefits for the provision of information technology software or support
5. benefits with an educational or training requirement.

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17 *ASIC Report 499: Financial advice: Fees for no service, dated October 2016*

18 *ASIC Report 499: Financial advice: Fees for no service, dated October 2016 p 5*

19 *17-145MR Compensation update: major financial advisory institutions continue refund programs for fees-for-no-service, 19 May 2017.*

As a matter of principle all carve outs should be removed because by their very nature they reasonably could be expected to influence an adviser on the choice of financial product recommended to clients; or the financial product advice given to clients. For example, it is illogical to somehow conclude that because a benefit is authorised by the client that this somehow changes what influences the adviser.

Soft dollar benefits have no place in a financial system which has stated objectives of creating a system of trust and unbiased advice. To this end, if the soft dollar benefits are not banned in their entirety then at the very least regulations should be introduced to further tighten the use of the exemptions. For example, regulations can be further strengthened by making it explicit that the education and training carve out cannot be relied upon if the education or training is not genuine or linked to sales volume hurdles as this would go against the spirit of the FoFA reforms.

The regulation in its current form does not meet its objectives to:

- minimise or eliminate the use of remuneration practices that distort the quality of advice and adversely affect consumer outcomes;
- encourage the provision of professional unbiased financial advice;
- enable consumers to understand the fees they are paying for advice and the services that they are paying for; and
- facilitate better market outcomes.

The Sedgwick Report[20] specifically recommended that soft dollar benefits be ceased.[21] The reason for this was that "[soft dollar benefits are] unrelated to the effort required by the broker to service a potential borrower's needs".[22] This recommendation has also been backed by ASIC.[23] The same rationale for banning soft dollar benefits in superannuation applies.

The reality is, in order to achieve the abovementioned objectives soft dollar commissions should be banned in their entirety because like commissions, soft dollar benefits distort the quality of advice and adversely affect consumer outcomes. An efficient regulatory system does not create fictitious differences which are inconsistent the broader policy objectives of the FoFA regime.

Two alternatives were outlined in the Consultation Paper:

1. Keep the status quo – manage potential conflict of interest via disclosure
2. Co-regulations.

Neither of these options satisfactorily meet the objectives of the regulation because soft dollar benefits by their nature put advisers in a conflicted position and impair an adviser's ability to provide unbiased advice (whether it is intentional or not, is irrelevant). Co-regulation is not a reasonable alternative because the industry has not demonstrated it can be counted upon to take sufficient, uniform action with enforceable remedies.

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[20] *Retail Banking Remuneration Review Report, Stephen Sedgwick, 19 April 2017*

[21] *Retail Banking Remuneration Review Report, Stephen Sedgwick, 19 April 2017, p 34*

[22] *Retail Banking Remuneration Review Report, Stephen Sedgwick, 19 April 2017, p 34*

[23] *Retail Banking Remuneration Review Report, Stephen Sedgwick, 19 April 2017, p 34*

The limited carve-out for basic products from the ban on certain conflicted remuneration structure and best interests duty

The ban on conflicted remuneration and payments that is part of the FoFA regime does not extend to most retail banking products as these are specifically exempt. The exemptions apply to basic banking products, general insurance products and consumer credit insurance.

The rationale for exempting basic banking products from the conflicted remuneration provisions was that the products are relatively homogenous and low risk.[24] Put another way, it is assumed these products are more easily understood, and consumers generally understand that employees of banks sell their employer's product. This assumption is flawed and goes against one of the fundamental goals of the FoFA reforms that is to produce a uniform approach to the provision of high quality advice.

ISA and AIST have consistently opposed carve-outs from the prohibition of conflicted remuneration and best interests duty. The exemptions provided where advice is given on basic banking products, general insurance, consumer credit insurance or a combination of these essentially motivates sub-optimal outcomes by allowing conflicted advice.

Under the current arrangements, in certain circumstances, bank employees will be required to act in the best interests (based on a modified version of the best interest duty) of their client and place the interests of their client ahead of their own. These obligations apply where a bank employee is dealing with a retail client and where they provide personal advice (advice provided where the employee has, or in the circumstances a reasonable person might expect them to have, considered one or more of a retail client's objectives, financial situation or needs). The notion that something less than the full best interests duty applies to personal advice provided solely in relation to basic banking products is absurd.

It is inconceivable that consumers are expected to be somehow knowledgeable about the legal distinctions between product information, and general and personal advice under the Corporations Act; it is even more ludicrous to assume that somehow the consumer is meant to understand that a modified best interests test applies in certain circumstances. The best interests test aims to ensure the consumer is receiving advice that is in their interest, and that advice provided is not influenced in some way by the personal benefits being offered to the adviser. The carve outs to this fundamental duty attempts to shift responsibility to the consumer, by somehow, creating the expectation that the consumer ought to be aware of the motives that exist behind the recommendations being made, instead of creating a framework which provides confidence to consumers that the advice is in the consumer's interest.

The Retail Remuneration Issues Report, dated 17 January 2017, by Stephen Sedgwick (Sedgwick report) demonstrates how the lack of a best interest duty applying to the ADIs exposes customers to poor outcomes fundamentally because sales targets are central to the work of bank employees at all levels. The existence of a deep entrenched sales culture was reinforced by Andrew Thorburn of NAB, where he admitted in Senate Estimates that 78 per cent of customer-facing staff at the NAB have sales targets. Customers of banks continue to be exposed to the downsides of a sales-based culture.

There are a plethora of examples demonstrating how mis-selling and cross-selling area regular feature of consumer interactions with financial institutions including:

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[24] *Post-Implementation Review Future of Financial Advice, Consultation Paper, p16*

- **Opening extra bank accounts**.
  - a bank teller encouraged a customer to open nine separate bank accounts. This helped the branch to meet its targets for new accounts opened. The teller's colleague closed the unnecessary accounts on the client's instructions. The colleague was reprimanded for this.[25]
  - it is common practice for bank staff to talk a customer into opening two bank accounts and adding on internet banking whether or not the customer needs it. Bank staff report serving customers that did not know they had internet banking or an extra account.[26]
- **Mis-selling simple banking products**
  - Bank staff working in call centres report being required by their management to offer an increase in credit limit to all credit card customers. They had to do this even if it was apparent that such an increase would be unsuitable for the customer.[27]
  - One woman telephoned her bank to transfer funds between her two banks accounts. She was offered an increase in credit card limit which she accepted. The bank employee did not make reasonable enquiries about whether she could afford the increase. She was also sold credit card insurance. She was not aware of the insurance and did not agree to it. Over the course of two years, she had spent $3000 in credit card insurance and was in financial hardship.[28]

The best interest test is a key component in ushering in a culture focused on consumer benefits.

With this background, it is disturbing that the majority of banks provide incentives, commissions or bonus payments to at least some of their retail staff that are directly or indirectly related to product sales. The reality is that such incentives have led to behaviours or practices that result in poor outcomes for customers.

The Sedgwick Report found there are documented instances in retail banking and across the financial services sector more broadly, both in Australia and abroad, in which incentives have at least appeared to drive behaviour that was not in the best interests of customers and, on occasion, scandalously so.[29]

In many banks the cultural orientation towards sales is deep seated. For that reason the pendulum needs to move more towards consumer protection. Consumers continue to be exposed to unnecessary risk and the costs are high for consumers, institutions and the industry as a whole both financially and reputationally.

One of the reasons put forward in support of not extending the ban to basic banking products was that this would require significant changes to remuneration and workplace arrangements.[30] The Sedgwick Report makes it clear that significant change is required to the remuneration structures. Therefore, the rationale for not extending the ban to basic banking products because it would be overly onerous is significantly reduced and cannot be accepted as a strong basis for the ban not applying.

However, the recommendations in the Sedgwick Report, are just that, recommendations, they are not law and only capture conflicted remuneration. These recommendations should not be optional and need to be reflected in the law. The most efficient way to do this is to remove the carve outs that exist in relation to the best interest duty and conflicted remuneration.

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[25] *Retail Remuneration Review, Issues Paper, Stephen Sedgwick, 17 January 2017, p 35.*

[26] *Financial Services Union to ABA Retail Banking Remuneration Review, 9 September 2016, p 6.*

[27] *Financial Services Union to ABA Retail Banking Remuneration Review, 9 September 2016, p 10.*

[28] *Consumer Action Law Centre, Financial Rights Legal Centre and Good Shepherd Microfinance submission to independent review of product sale commissions and product based payments, 13 September 2016, p 7.*

[29] *Retail Banking Remuneration Review Report, Stephen Sedgwick, 19 April 2017, Executive Summary, i.*

[30] *Post-Implementation Review, Consultation paper, p 15*

In light of all the banking issues, it is clear consumers are being left vulnerably exposed to predatory practices.

The clarification provided in relation to access to scaled financial advice

A key objective of the FoFA reforms was to facilitate access for retail clients to financial product advice, including 'scaled' advice; that is, personal advice that is limited in scope. At the time of its introduction it was widely accepted that one of the main reasons more people do not seek financial advice, is that too often it does not seem worth the costs to see a planner about a single, relatively simple financial issue.

The Consultation Paper states that there is considerable uncertainty around whether ADIs can remain compliant with the best interests duty and still provide scaled advice. This appears to be a poor attempt to water down conduct requirements. It is vitally important that as an industry we do not lower conduct requirements, merely because it is seen as "inconvenient" by some quarters. This is more so, when some major financial institutions have been the subject of significant condemnation for poor consumer practices. One of the fundamental goals of the FoFA reforms has been to produce a uniform approach to the provision of high quality advice. As such, scaled advice is subject to the same legal requirements as advice that is fully comprehensive and this should not change.

As far as we are aware scaled advice has been a success in the superannuation industry, and some funds are reporting an increase in up take by up to 33 per cent since its introduction.

The chosen option of inserting a note into the Corporations Act stating that the best interests duty anticipates the use of scaled advice has met its objective.

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