



Australian Government
The Treasury

TSY/AU

Quality of Advice Review

Submission by



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Consultation template

Name/Organisation: The Conexus Institute

Questions

Intended outcomes

1. Do you agree that advisers and product issuers should be able to provide to personal advice to their customers without having to comply with all of the obligations that currently apply to the provision of personal advice?

The present collection of obligations appears unworkable and is not resulting in outcomes which work for all parties involved:

1. Consumers are receiving lengthy, templated, difficult to understand SOA's. They are incurring the negative cost impacts of these activities. The time required reduces the supply of advice available to the broader population. The cost involved creates a barrier to entry for some cohorts of the population and reduces the value-for-money equation for all consumers. We have no informed view on whether the present collection of obligations is reducing the quality of recommendations being made by advisers and product issuers. We do note however that the present set of obligations hasn't eliminated poor outcomes for consumers, most notably the recent case of Dixon Advisory. This is an important example as it was a large mainstream case of the potential poor outcomes associated with vertical integration. We note that the term 'vertical integration' wasn't referenced at all in the Consultation Paper.
2. Advisers are encumbered with the time, cost and frustration of significant compliance-related activities. This impacts business finances and adviser morale.
3. We consider product providers on a category-by-category basis as a healthy test of the proposals. Here it is interesting to reflect on the spectrum of activities from pure product provider through to a fiduciary relationship with the member / client, the corresponding relationship between strategic advice and product advice, and the possible degree of poor outcomes (ranging from incrementally poor to versus catastrophically poor).
 - a) Super funds are arguably a special case due to the additional duties placed on trustees, the level of entity and product-level regulation in this sector, and especially in the MySuper default space, the low risk of catastrophic consumer harm. In practice this 'special case' argument weakens as the non-MySuper investment choice menu expands in size.

Further, 250,000 people retire each year and the retirement financial planning decision is arguably the most complex financial decision most people will face. There are some alarming dynamics at play here: financial advisers have scale challengers and, in many cases, don't have the technology in place to account for the stochastic nature of the problem nor the range of product being made available. The scalable solution for retirement support is an important challenge and super funds are a strong candidate to provide greater support.

Overall I consider the benefits of strategic advice outweigh the lack of product advice, but this argument weakens as you get further away from default products.

Further, there is an important question of whether retirement advice, given its complexity and breadth of considerations, should be comprehensive advice. If the view is yes, then we consider the proposals outlined in the Consultation Paper will unlikely achieve this aim – we anticipate they will most encourage provision of limited advice.

- b) Insurance providers are arguably a special case because consumer benefit arises when insurance contracts are highly personalised. We have no insight into general insurance so our comments focus on life insurance. Here, we observe two features: (1) Idiosyncratic requirements amongst consumers, and (2) Differences in product features and cost.

Anecdotally, it appears that the advice process to determine appropriate insurance arrangements is costly and that advisers are stepping away from this service provision because restrictions on commissions make insurance advice financially unattractive.

While life insurance can be purchased directly, it is also available via a super fund. This creates a conflict to the direct provision of insurance advice by insurers.

The inferred trade-off presented in the Consultation Paper, greater provision of limited advice and little in the way of product advice, is challenging for this case study. The limited advice may assist to tailor insurance arrangements, but the opportunity cost of the least optimal product solution may be more than a reasonable definition of incremental.

- c) Investment managers, ignoring super funds, are very much product providers. It is hard to identify the benefits of strategic financial advice beyond distribution benefits to the investment management firm. My concern here is that we view the value of product advice as significant, and there is the potential for poor outcomes that exceed an interpretation of incremental. Further we think the breadth of strategic advice offered by investment

managers is likely to be limited. The trade-off is a concerning one and we have some reservations. Unfortunately it is hard to distinguish between investment managers: for instance low cost passive funds compared with more nuanced higher cost funds.

Based on the above framing:

1. There is a shortage of quality, affordable financial assistance for all Australians and consumers would benefit from greater service provision of strategic advice. However, we have concerns here that in many cases product advice remains an important determinant of outcomes and so should not be cast adrift.
2. We view the likely outcome of the framework being an increase in limited advice, not comprehensive advice. The specific concern we have is whether limited advice is sufficient when it comes to developing a retirement financial plan. If so
3. Advisers would benefit from a review / refinement of existing obligations. Here we note two caveats:
 - a) The review / refinement of obligations need not be as extreme as the changes proposed in the Consultation Paper.
 - b) There is a real risk that any reduction in obligations is applied to improving advice business margins at the expense of improved affordability.
4. Super funds could be viewed as a special case and structural changes could be made to position these groups as benevolent fiduciaries which would make their circumstances even more special. Some of the changes required go well beyond the scope of this Review as they pertain to business structure, legislated purpose etc.
5. Insurance providers could contribute quality specialised strategic advice. How to ensure good product choices is difficult, while for life insurers there is a natural conflict with the products provided by super funds.
6. Allowing investment managers to provide advice creates a direct trade-off between strategic advice and product choice considerations. Here, we believe that product choice is significantly important.

What should be regulated?

2. In your view, are the proposed changes to the definition of 'personal advice' likely to:

- a) reduce regulatory uncertainty?
- b) facilitate the provision of more personal advice to consumers?
- c) improve the ability of financial institutions to help their clients?

Proposed definition from Consultation Paper: *The financial services regime should regulate the provision of 'personal advice'. 'Personal advice' is a recommendation or opinion provided to a client about a financial product (or class of financial product) and, at the time the advice is provided, the provider has or holds information about the client's objectives, needs or any aspect of the client's financial situation.*

We think the proposed changes make good sense.

1. We agree that the stated intention of reducing regulatory uncertainty would likely be achieved.
2. We are not sure the proposed definitional changes would facilitate the provision of more personal advice to consumers. It is hard to form a view on the impact of the definitional changes on a standalone basis compared to the impact of all the proposed changes in aggregate. We note the risk that the narrowing of general advice means that some groups may withdraw their services (that may or may not be a good thing).
3. We are not sure the proposed definitional changes would improve the ability of financial institutions to help their clients. While improved clarity is beneficial it is likely other changes in the Consultation Paper which will be the significant determinants of whether financial institutions can more readily help their clients.

3. **In relation to the proposed de-regulation of 'general advice' - are the general consumer protections (such as the prohibition against engaging in misleading or deceptive conduct) a sufficient safeguard for consumers?**
 - a) **If not, what additional safeguards do you think would be required?**

We have no informed view on this issue.

How should personal advice be regulated?

4. In your view, what impact does the replacement of the best interest obligations with the obligation to provide 'good advice' have on:

- a) the quality of financial advice provided to consumers?
- b) the time and cost required to produce advice?

We make two comments on the proposal to replace the best interest obligations with the obligation to provide 'good advice':

1. This proposal has had a healthily disruptive impact on how personal advice should be regulated. The switch from a "regulate conduct of the adviser" to "regulate content of advice" will promote significant reflection. Our additional observation here is whether this framing needs to be an either / or debate or whether there is the opportunity for elements of both framings to shape an improved regulatory framework for advice. We think there is a spectrum between these two extremes that warrant exploration. Our working view is that some regulatory requirements for relevant providers could provide useful consumer protections, especially in a setting where it may be hard to prosecute non-provision of good advice given its subjectivity.
2. We think the practically that the framing of 'good advice', once taken inside by financial service institutions, will be "sufficiently good advice". This isn't intended to be sceptical, just pragmatic. Anecdotes constantly suggest that legal / compliance departments have a strong say in determining advice processes. Further, for many financial services groups, anything beyond sufficiently good advice represents additional cost without unsure direct marginal revenue impact (which is different to benefit to client). We think it would be a healthy exercise for the Quality of Advice Review to work through the outcomes on the basis of "sufficiently good advice".

Addressing the specific questions:

1. Anticipated impact on the quality of financial advice provided to consumers: this is a difficult question to answer in aggregate. So we attempt to break it down by provider, accounting for strategic advice and product advice considerations, and the likelihood to offer financial advice:
 - a) Financial advisers: we are not sure it would lead to wholesale changes to the advice process, but rather lead to changes in the way that advice is delivered (e.g. less focus on SOA's etc.). We consider that the "good advice" framing has a more impact on small pieces of advice. It is easier to see how "good advice" interacts with simple, one-off pieces of advice, but it feels at odds with the concept of comprehensive advice. There may be greater provision of limited advice, but we are not convinced limited advice is a natural part of most advisers' service offering.

- b) Super funds: the potential to provide improved strategic advice, predominantly limited advice. The lack of product advice is arguably modest due to other regulatory protections in place. There is a risk that super funds do not have the right entity / capital / regulatory structure to be large providers of advice. Finally, we do not see super funds providing a comprehensive household retirement financial plan due to complexities like partner's financial affairs, other assets outside of super.
- c) Insurance providers: greater likelihood to provide useful strategic limited advice. The concerns are (1) the importance of product choice combined with the likely absence of product advice – this applies to both general and life insurance, and (2) life insurance arrangements provided by super funds. Overall we think general insurance providers will improve the strategic advice they provide but product advice will be absent. It is difficult to predict the advice provision activities of life insurers as we would envisage “good advice” to account for super fund arrangements, which may reduce the cost effectiveness of providing financial advice.
- d) Investment managers: we anticipate provision of strategic limited advice but effectively no product advice. Here we consider product dispersion to be sufficiently large to consider this a concerning prospect. We envisage that the provision of low cost strategic advice is an attractive business proposition for investment managers as it likely strengthens sales and retention. There are special cases, such as passive providers, but it is difficult to see how they can be catered for.

Overall it is unclear to what degree the provision of advice will be increased, and to what degree this will be benefit consumers. We think the biggest potential benefit would be the provision of smaller pieces of limited advice by financial advisers and provision of strategic limited advice by super funds, especially at the point of retirement (noting our previous noted concerns around whether a comprehensive household financial plan is necessary at retirement). In other areas it is difficult to weigh up the benefits of strategic advice provision versus the likely absence of product advice (in areas where the impact can be more than incremental).

The fundamental question we have is whether the concept of “good advice” can be safely self-administered to account for the situations where product advice (i.e. product comparisons) should be accounted for. We are concerned at the prospect of this form of product advice being put aside as strategic advice is sufficient to meet the obligation of “good advice”.

2. Anticipated impact on time and cost required to produce advice: again this is difficult. We consider positively the prospect of new entrants, compared against established providers with legacy processes and mindsets. We are also concerned that the concept of good advice is highly subjective and there will be little precedent. The realities of this in a compliance driven environment may be that costs do not fall significantly.

5. Does the replacement of the best interest obligations with the obligation to provide 'good advice' make it easier for advisers and institutions to:

- a) provide limited advice to consumers?
- b) provide advice to consumers using technological solutions (e.g. digital advice)?

1. Estimated ease to provide limited advice to consumers: we believe this is where the greatest provision uplift resides. Our expectation is that this comes with very little product advice.
2. Estimated ease to provide digital advice: our general answer is yes for two reasons, which generate a degree of caution / concern. (1) The absence of zero product advice. Our research into digital advice is that it has never done product advice well. The proposed "good advice" obligation is likely to place product advice to the side. (2) From our research we view digital advice as a collection of limited advice modules. We see very little in the way of true comprehensive advice. Digital advice is not set up to ask "is there anything else I need to know" – this doesn't fit the program.

We have a specific query about digital advice in settings (e.g. super funds) which may hold significant information: would the digital platform be required to make use of all this information, if it was all relevant? Under the concept of "sufficiently good advice" it may not need to. Would this meet consumer expectations and be consistent with the definition of personal advice?

6. What else (if anything) is required to better facilitate the provision of:

- a) limited advice?
- b) digital advice?

No comment on either, except for clarification on the question raised in part (2) of our response to question 5.

- 7. In your view, what impact will the proposed changes to the application of the professional standards (the requirement to be a relevant provider) have on:**
- a) the quality of financial advice?**
 - b) the affordability and accessibility of financial advice?**

We have no comments on this issue.

- 8. In the absence of the professional standards, are the licensing obligations which require licensees to ensure that their representatives are adequately trained and competent to provide financial services sufficient to ensure the quality of advice provided to consumers?**
- a) If not, what additional requirements should apply to providers of personal advice who are not required to be relevant providers?**

We have no comments on this issue.

Superannuation funds and intra-fund advice

- 9. Will the proposed changes to superannuation trustee obligations (including the removal of the restriction on collective charging):**
- a) make it easier for superannuation trustees to provide personal advice to their members?**
 - b) make it easier for members to access the advice they need at the time they need it?**

Our working view is that the proposed changes remove the intra-fund advice 'safety blanket', whether or not this was identified correctly as such.

- 1. Fundamentally the proposed changes clarify the decision-making considerations (around whether to provide advice). Further, the removal of the intrafund advice 'safety blanket' sharpens the focus of trustees on whether to take on the risk of providing advice. However, it would not surprise me if many funds turn out to be quite hesitant to provide advice services as they question whether they have the appropriate business structure, capital structure and business processes to provide such services. Nonetheless our working view is that, influenced by competitive peer pressures, funds will offer advice services.

2. Our research as part of the Conexus Institute’s Transforming Financial ‘Advice’ project reveals that consumers have moderate awareness of the assistance provided by super funds and reasonably high trust levels. So funds would need to better communicate their services to ensure good take-up. We would also question whether, consistent with our comments in Q15, whether the emphasis is on limited advice. Our concerns are outlined below:
- a) Many issues traditionally considered to be limited advice, such as additional contributions (see (5) in Q15), are in fact quite complex pieces of advice.
 - b) Some decisions, like establishing a retirement financial plan are complex and arguably require comprehensive financial advice. Comprehensive advice would be better quality and consumers would be more confident to spend as recommended (an important focus of the Retirement Income Review).
 - c) The scope of advice will be limited to the extent it cannot easily recommend on interests outside the super fund. This makes it difficult to provide household-level recommendations.

Disclosure documents

10. Do the streamlined disclosure requirements for ongoing fee arrangements:

- a) reduce regulatory burden and the cost of providing advice, and if so, to what extent?
- b) negatively impact consumers, and if so, how and to what extent?

We have no significant insight, though appear to make sense.

11. Will removing the requirement to give clients a statement of advice:

- a) reduce the cost of providing advice, and if so, to what extent?
- b) negatively impact consumers, and if so, to what extent?

1. Cost of providing advice: we will be interested to learn of insights from financial advisers and licensees on this issue – their data will be valuable. Our general concerns are that (1) processes will need to be developed for record keeping (at a minimum) (2) much of the lengthy SOA was product PDS’s, a lot of which

could be constructed by software. True insights of the 'delta' between quality record keeping and the existing SOA process, and any necessary templates required etc., will be highly valuable.

2. We are of the view that customers should receive some recording of the advice they receive from their adviser. This could be written or a recording and could be agreed between adviser and client. We think this has multiple benefits:
 - a) It provides a reference point, record and set of actions for clients
 - b) It removes the risk of client misinterpretation
 - c) It creates accountability in the relationship between the service provider and the client

Additionally we believe recordkeeping should be formalised into a regulatory requirement. Given this we can't see it being difficult to require some formal recording of advice be shared with clients.

12. In your view, will the proposed change for giving a financial services guide:

- a) **reduce regulatory burden for advisers and licensees, and if so, to what extent?**
- b) **negatively impact consumers, and if so, to what extent?**

We have no comments on this issue.

Design and distribution obligations

13. What impact are the proposed amendments to the reporting requirements under the design and distribution obligations likely to have on:

- a) **the design and development of financial products?**
- b) **target market determinations?**

We have no comments on these issues.

Transition and enforcement

14. What transitional arrangements are necessary to implement these reforms?

We have no comments on this issue.

General

15. Do you have any other comments or feedback?

(1) We view the proposals as increasing the provision of limited advice and having modest impact on comprehensive advice. Through the lens of the financial assistance needs of Australians we are not sure if this is the solution to the problem (we are not saying it isn't, we are saying we are unsure). For example, we think many households would benefit from comprehensive financial advice, particularly with respect to a household financial retirement plan.

(2) In our view the proposals outlined in the Consultation Paper implicitly encourage increased provision of limited advice via the non-requirement of product advice. The Consultation Paper doesn't state this explicitly, but we believe this to be a clear difference between "good advice" and a reasonable application of "best interests' duty". For some areas, like superannuation, we consider the potential opportunity cost to be modest. For other areas such as insurance and investment management the potential cost could be significant. This is an outcome of the uniform application of "good advice".

(3) We think the Consultation Paper would have been better balanced if it acknowledged the likelihood for, and considered the consequences of vertical integration. This would have allowed consideration of mechanisms to control potential adverse consequences. Applying (2), we believe the cost / benefit equation varies significantly across different areas of financial services. If reform effectively encouraged vertical integration, we think it would be very difficult to unwind e.g. some one major financial services firm had a three-year program to unwind its vertically integrated structure.

(4) Through our working project, Transforming Financial 'Advice', we consider that a range of solutions may be required to create a spectrum of financial assistance sources which provide access to quality advice and guidance services at a range of price points. Candidate solutions include government services like ASIC MoneySmart and Centrelink, online calculators, digital advice, and a re-defined role / structure for super funds (the benevolent fiduciary concept mentioned

in our response to question 1). We ask the Quality of Review panel to consider, if some of these other solutions were implemented, would that lead to a different set of recommendations, particularly the degree to which scaled provision of limited advice is traded off against the lack of product advice / risks of vertical integration.

(5) We are concerned by the example of simple advice, additional contributions to super, used on page 22 of the Consultation Paper. The decision around additional contributions is complex for many reasons including that it is an intertemporal decision (exchanges possible expenditure today and expenditure in retirement), and involves tax and liquidity considerations. We think this decision requires more consideration than what some intrafund advice processes may provide. This is an example where it would be hard to define “good advice”.

(6) Cameo 2, which considers retirement advice is interesting. Nobel Prize winner William Sharpe considers retirement to be the “nastiest, hardest problem in finance”. In our view the advice provided is beneath what is encouraged under the Retirement Income Covenant. We would only be comfortable with the advice provided based on some additional assumptions (which we call out, rather than assume): Ms Hughes is single and has no other superannuation accounts, and that the super fund does not offer any other retirement income stream products.

(7) Cameo 2 serves to highlight the awkward transition from Mr Ram to a relevant provider based on a fee. The self-directing filter on “good advice” is the complexity of the advice, while the payment element is captured in the definition. We can’t see an easy solution to this challenge but forecast a potentially undesirable outcome: funds are tempted to provide more complex advice free of charge because this preserves the fund’s optionality to not use a relevant provider.

(8) We are concerned that the complexity of the decision for super funds to provide advice will result in mixed decisions around whether to provide, and potentially worse, a decision to provide advice services based on peer pressure. It has long been questioned whether super funds have the appropriate business structures and capital structures to carry the risk of advice provision.

(9) Oftentimes we think the ability of the industry to innovate and self-regulate is wildly overstated. We think most parts of the financial services sector seek clear direction. Creating subjectivity and relying on judgement and innovation may not derive the benefits anticipated (in good faith) in the Consultation Paper.

(10) Our working view is that we would like to see appropriate regulatory requirements placed on designers / owners of digital advice models. This may mean that appropriate people signing off on algorithms need to be relevant providers. It is hard to envisage in-person / digital neutrality without such a requirement.

(11) Note that our comments in questions (1) and (4), particularly across market segments (superannuation, insurance and investment management), is through the lens of “good advice” (as defined). Through the lens of different requirements (e.g. express statutory duties applied to providers) the segment-based opinions would be updated and potentially different.