AXIS FINANCIAL GROUP

Informer

Investors Bulletin

No. 150 November 2011

The Future of Financial Advice Reforms - What will they mean for you?

Australian investors can breathe a collective sigh of relief, thanks to new measures that will overhaul the financial services industry – particularly the financial advisory sector. Due to kick in next year, the Future of Financial Advice (FOFA) legislation will offer investors greater protection when dealing with financial advisers and tighten the responsibilities of those in the industry. So, what will the reforms mean for you? We've summarised them in this Informer and given more detail on those that will directly impact you.

FOFA's no furphy!

It's been two years in the making, but the draft legislation for FOFA is finally here. FOFA is the Government's response to some very bad seeds in the financial services industry. Individuals who focused on boosting their own financial futures instead of their clients. The fallout saw thousands of investors lose millions of dollars and a major loss of confidence towards the financial advisory industry. FOFA aims to prevent events like this from recurring.

From 1 July 2012, these new measures will give investors more protection. They will also ensure that the duties of financial advisers, how they're paid and the products they can recommend are more defined and stringent, with significant penalties applying for breaches.

Research shows that people who obtain personal financial advice are more likely to retire with higher account balances than those who don't. Therefore, restoring confidence in the industry is crucial. AXIS is pleased about these reforms. If implemented correctly, they will be an important step forward for investors and the industry. So, let's take a look at what the 5 main reforms mean for you.

I. Best Interests Obligations

This reform is all about protecting you and legislates the ethical code by which any good financial adviser should operate. Before your adviser can give you personal financial advice, they must have confirmed your personal financial objectives, needs and situation. In other words, the adviser must place your interests first at all times.

Only then can they recommend a product or course of action to you. This reform removes any potential conflicts of interest between an adviser's own interests and yours.

What does this mean for you?

This is a necessary and welcome reform. Traditionally, financial advisers have operated under a fiduciary and ethical code to "know their client, know their product and provide appropriate advice". This assumed code will now be law.

As an AXIS client we trust you're fully aware that we already adopt a best interest approach. All employees have personal risk profiles conducted prior to us providing advice. Remember that your dedicated Corporate Adviser, along with our Advisory and Technical Services team are always available to help.

So, under this proposal, you'll see no change in our servicing levels or processes.

II. Opting in for financial advice

This reform only applies to new clients. So it won't apply to existing AXIS clients and, you might actually be relieved about this! This reform is about improving disclosure on fees and services and works like this.

If your adviser's fees are to be ongoing for more than two years, they must issue you with a Renewal Notice. For the services to continue, you must sign the Notice, thereby "opting in" for the services. If, for some reason you don't sign the Notice, the adviser can no longer charge you fees and, naturally, can stop providing you with any service.

Where ongoing fee arrangements are in place, you can opt out at any time. This may be through the Renewal Notice, not completing the Renewal Notice or by other written means (eg email, text message, fax or an online facility, such as your adviser's website). If your adviser continues to charge a fee after you've opted out, they could be subject to financial penalties.

What does this mean for you?

This reform makes us nervous, for the simple reason that, if you inadvertently fail to sign the Renewal Notice, the servicing of your super and financial affairs will be terminated.

III. Ban on conflicted remuneration

This reform is tied in with the Best Interests Obligations and focuses on payment of commission to advisers. The Government found that the payment of commission upon the sale of a product can sometimes influence the integrity of advice given and lead to inappropriate investment strategies or excessive fees for clients.

From 1 July 2013 commission on group life insurance within super is banned, as is commission on personal life insurance attached to the default super fund (and MySuper products).

What does this mean for you?

This proposal won't make any difference to AXIS clients, as our Servicing Agreements are based on a fee-for-service model with agreed Key Performance Indicators. However, members of non-AXIS super funds may not be so lucky.

Further underinsurance problems

If commissions are banned on group insurance policies within super, many advisers might not be willing to provide insurance as part of their service offering. This could exacerbate Australia's massive underinsurance problem and leave many super fund members without a financial safety-net in the event of death, disablement or illness.

Higher costs

Individual insurance policies are generally more expensive than group insurance policies, as there is less bargaining power to negotiate premiums. Although personal policies within super are usually cheaper than those outside of super, employees will still be slugged with higher premiums.

However, there may also be a positive to this reform.

Improved servicing levels

If advisers can receive commissions on individual policies for members exercising super choice, we could see more advisers actively servicing their clients. This would be good news for super fund members and the industry. In our experience, underservicing is usually the main cause of low member account balances and why many Employers switch to utilising the services of AXIS Financial Group.

What does this mean for you?

Naturally, we should remember that any potential negative outcomes of this reform are just that – potential. Particularly given that financial advisers will be expected to adhere to the Best Interests Obligations at all times!

IV. Ban on volume-based shelf space fees

This reform bans commissions being paid to platform operators based on the total number or value of financial products (the "volume-based" part) that are listed on an administrative platform (the "shelf space" part). By banning commissions to platform operators, this proposal aims to improve transparency of fees.

What does this mean for you?

Again, AXIS clients won't be affected by this proposal as, importantly, we are not tied to any product provider. Our advice to you is based on the products which offer you the best solution. Ultimately, as our client, you receive non-aligned advice at all times.

V. Ban on asset-based fees on geared funds

Geared funds are borrowed monies. This reform bans commissions being paid on the amount of assets used to purchase a financial product, if those assets are borrowed. Naturally, financial advisers would be expected to make all necessary enquiries as to the source of the funds.

What does this mean for you?

This proposal is unlikely to have any impact on you as we do not use gearing strategies for your superannuation.

Contact us

As you can see, the reforms will go some way to protecting you, your fund and general investors from potential misconduct. They will also give the financial advisory industry greater clarity and support.

If you'd like to know more about the reforms, you can download the draft legislation, which is in two parts, at www.futureofadvice.treasury.gov.au

Alternatively, please contact our friendly Advisory Group or Technical Services team on (08) 9426 5800, 1800 111 299 or at super@axisfg.com.au

References:

- Australian Government, The Treasury, Future of Financial Advice, Corporations Amendment (Future of Financial Advice Measures) Bill 2011, Explanatory Memorandum, August 2011.
- Australian Government, The Treasury, Future of Financial Advice, Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011, Explanatory Memorandum, September 2011.
- Australian Government, The Treasury, Future of Financial Advice, Corporations Amendment (Further Future of Financial Advice Measures) Bill 2011, Explanatory Draft, September 2011.
- Corporate Super Specialist Alliance, Response to FOFA Draft Legislation Tranche 1, September 2011.
- Financial Planning Association of Australia, FPA Submission on Exposure Draft 1, September 2011.
- EBIX, Brokers caught up in FOFA volume payments ban, September 2011.
- Holly Nethercote, Mapping out Tranche 2 of the FOFA Reforms, September 2011.
- HWL Ebsworth Lawyers, Future of Financial Advice (FOFA) tranche two released for public comment, October 2011.
- IOOF, Adviser News, FOFA and MySuper: draft Bills get released and we still wait..., October 2011

www.axisfg.com.au

Feel free to contact your advisor with any questions about this bulletin

Phone 08 9426 5800 Fax 08 9426 5850
Freecall 1800 111 299 Email super@axisfg.com.au