February 2022

Quality of Advice Review - Draft Terms of Reference

ABOUT US

Super Consumers Australia
Super Consumers Australia (Super Consumers), is an independent, not-for-profit consumer organisation formed in 2013. Super Consumers was first funded in 2018. We work to advance and protect the interests of people on low and middle incomes in the Australian superannuation system.

CHOICE
CHOICE is the leading consumer advocacy group in Australia. CHOICE is independent, not-for-profit and member-funded. Our mission is simple: we work for fair, just and safe markets that meet the needs of Australian consumers. We do that through our independent testing, advocacy and journalism.

Financial Rights
Financial Rights is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Mob Strong Debt Help services which assist Aboriginal and Torres Strait Islander Peoples with credit, debt and insurance matters. Finally we operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies.

Introduction

High quality financial advice can improve financial security, give greater peace of mind and the freedom to pursue lifestyle goals. The Financial Services Royal Commission shone a light on how poor and conflicted financial advice can result in people being overcharged and being recommended poor financial products with disastrous impact. The causes of this behaviour, namely conflicts of interest, are now well understood and must be removed. It is also an opportunity to consider how regulation can better support the needs of average Australians in accessing affordable and independent advice they can trust.

This should be a review for the consumers of advice. The Terms of Reference need explicit direction to review the quality of advice being delivered to consumers today. Reviewing the quality of advice was not only the intention of the Royal Commission, but a sound evidence based place to start before proposing changes in regulation. The Review would fail to live up to its own name if it did not. The recent collapse of Dixon Advisory shows that problems with conflicts still exist. Without an examination of the current quality of advice, including specific examination of advice files, the review risks paying lip service to quality in the pursuit of affordability and access.

The Review must also provide solutions for all Australians, not just those who trust, can afford or seek out traditional financial advice. The cost of delivery and lack of trust remain significant issues in consumer access to advice. To an extent some of these problems are endemic to the traditional advice industry. For example, one on one advice by its nature is costly to deliver, while lack of trust in advice models with inherent conflicts will persist. The United Kingdom's advice market review terms of reference specifically looked at "the advice gap for those people who want to work hard, do the right thing and get on with life but do not have significant wealth." New solutions are needed here to address the needs of consumers, particularly Australians on low and middle incomes seeking requirement guidance. Getting the right advice about retirement savings can make a significant difference in someone's standard of living across the decades many spend in retirement. The new retirement income covenant is likely to drive super funds to develop better strategies and products for the retirement phase. However, these benefits may be lost if it is not accompanied by improved guidance for consumers to help them find the strategies and products that are appropriate to them.

The review needs to go beyond the financial advice sector and consider the role of independent organisations, Government and new business models in complementing and filling the gaps in traditional advice models. The United Kingdom government created a "guidance guarantee" to assist people approaching retirement. During consultation on a model to deliver on this guarantee the vast majority of respondents, including most of the financial services industry, agreed that consumers would not trust guidance given by a person or organisation with a vested interest in selling a financial product. Not building this current review on the same foundation risks repeating past mistakes in the regulations of Australia's financial advice system.

Australians who want it should have access to impartial, high quality advice that covers the ranges of options to help make sound decisions and equips them to take action.

Recommendations

Recommendation 1

That the following additional term of reference be included at 2.1: In particular, the Review should investigate, ● The quality of advice that is being provided to people and whether measures that have been implemented by government, regulators and financial services entities have improved the quality of financial advice.

Recommendation 2

The Review should determine if the remaining carve-outs, exceptions and safe harbour provisions, including addressing the remaining conflicts of interests, continue to be appropriate.

Recommendation 3

The Review should seek to understand the advice needs of cohorts of consumers across various levels of wealth and engagement. Specifically it should consider the needs of: ● Those who seek out experts to make financial decisions for them. ● Those who what to take a DIY approach to financial planning ● Those who are disengaged with their finances including those experiencing financial hardship.

Recommendation 4

The Review should investigate solutions to guarantee trusted guidance to all Australians who want it, that is impartial, conflict free, high quality, and covers the ranges of options to help people make sound decisions and equip them to take action.

Recommendation 5

The Review should examine the UK Money and Pensions Service as one of the options for an alternative model for the delivery of conflict-free, affordable advice in Australia.

Recommendation 6

The Review should assess how to best address the advice needs of people in low and middle Australia as they grapple with the complexity of retirement planning.

Ensure the Quality of Advice review actually reviews and improves the quality of advice

The intention of Commissioner Hayne's recommendation 2.3, which this review is built upon, was to review, in consultation with ASIC, the effectiveness of measures that have been implemented by the Government, regulators and financial services entities. The purpose of this review was to see if the quality of advice being provided to people has improved and is no longer contributing to consumer harm. Consideration of access and affordability have since been added to the Review. This is important because quality, access and affordability all need to be considered in harmony if people are to be adequately supported through important financial decision-making. However, the starting point must be a review of the current quality of advice, without this, the review risks repeating past failures in advice regulation.

ASIC last reviewed the quality of advice provided in a specific sector - superannuation - in 2019. This predates many reforms to the sector to which Commissioner Hayne referred. This review of advice by super funds found that only 49% of the files demonstrated full compliance with the best interests duty and related obligations.[1] 15% of the files did not comply with the best interests duty and related obligations and there was an indication that the member was at risk of suffering financial or non-financial detriment as a result of following the advice provided.[2] Previous ASIC reviews of advice delivered by vertically integrated financial service providers (65% in breach of legal obligations) and SMSF advice (91% in breach of legal obligations) have shown even higher rates of non-compliance with the duty to act in the best interests of clients.[3] Before this Review moves to assessing areas where affordability and access can be improved it must first assess the extent to which recent reforms have addressed these high rates of misconduct.

A good starting point for the review would be an assessment of the quality of advice currently being delivered to Australians against the benchmarks set in these previous reviews. Only then can we move to a clear eyed review of the 'opportunities to streamline and simplify regulatory obligations' as stated in the draft terms of reference. As Commissioner Hayne stated, "if those changes have not – or have not sufficiently – improved the quality of advice given by financial advisers, consideration must be given to what further changes will be necessary".[4]

Reducing the regulatory obligations on advisers before determining quality, is particularly important in the context of current proposals to weaken the education standards for current financial advisers. Commissioner Hayne stated, "prevention of poor advice begins with

[1] REP 639 Financial advice by superannuation funds, p7
[2] REP 639 Financial advice by superannuation funds, p7
[3] REP 562: Financial advice: Vertically integrated institutions and conflicts of interest and REP 575 SMSFs: Improving the quality of advice and member experiences
[4] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report p178

education training”.[5] Current proposals may place at risk the hard-fought progress the industry is making towards professionalisation. Increasing professionalisation within the industry has been used as an argument for reducing regulation. If changes are made based on professional education measures that will be repealed and without a review of quality, there can be no guarantee that potential quality improvements will continue.

The Review will run for approximately a year. If properly resourced, this gives time for ASIC to source advice files and review them. This can be conducted with new files or files ASIC currently have using their current methodology. Additionally, the introduction of APRA superannuation heatmaps, provides a new basis for a benchmarking methodology. The most recent choice heatmap found 60% of products underperformed a long term benchmark. In many cases, people are advised into choice super funds. We encourage the reviewer and ASIC to use benchmarks as a performance test metric to determine if the advice people receive is resulting in materially better outcomes. Once this preliminary review of quality is conducted, focus should turn to the efficacy of the regulatory regime in delivering quality, accessible and affordable advice.

One of the four key questions of the Financial Services Royal Commission was “Should the approach to addressing conflicts of interest change from managing conflicts to removing them, either by banning all or some forms of conflicted remuneration and sales or profit-based remuneration and/or changing industry structures?”.[6] Conflicted remuneration is the root cause of many of the problems uncovered by the Royal Commission. Cases like that of Dixon Advisory show that the problems of conflicted remuneration and structures are still in play three years after the Royal Commission report. For the thousands of people who entrusted their retirement savings to a seemingly reputable brand like Dixon Advisory, their retirement plans are now at serious risk due to the Dixon Advisory collapse. This was exactly the type of evidence Commissioner Hayne said this Review should be considering to decide if the regulatory regime was adequately protecting consumers from conflicts. The Review needs to take a fulsome look at this case and the state of the industry generally to judge if more needs to be done to address conflicts. On the current evidence failure to do so will continue to put the savings of Australian retirees at risk.

Recommendation 1

[5] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, p171
[6] Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report p5

That the following additional term of reference be included at 2.1:

In particular, the Review should investigate,

- The quality of advice that is being provided to people and whether measures that have been implemented by government, regulators and financial services entities have improved the quality of financial advice.

Recommendation 2

The Review should determine if the remaining carve-outs, exceptions and safe harbour provisions, including addressing the remaining conflicts of interests, continue to be appropriate.

A review that provides solutions for all Australians, not just those who go to financial advisers

There are key times in people's lives including entering the workforce, starting a family and planning for retirement when access to quality advice and guidance is crucial to making good financial decisions. Getting the right guidance at the right time can transform someone's standard of living. For example, the Productivity Commission estimated there is a $500,000 retirement balance difference between someone staying with a good performing super fund throughout their working life compared to a poor performer.[7] Due to barriers, such as cost and lack of trust, many consumers can't access quality, conflict-free advice and guidance. The attention of this Review must be broadened to look at these barriers and develop solutions to address them. To achieve this it needs to go beyond the financial advice sector and consider the role of government, independent organisations and new business models in overcoming these barriers.

Currently, it is very difficult to get independent strategic and product advice outside of paying for individual financial advice. Individual advice will remain an important resource for some consumers to navigate the complexity of retirement planning, but it is not the solution for all. Super Consumers Australia research found that only a quarter of pre-retirees looked to experts (e.g. financial advisers) to help them with retirement planning.[8]

[7] Productivity Commission Inquiry report - Superannuation: Assessing Efficiency and Competitiveness, p13

[8] Retirement Planning Survey, February 2021, Super Consumers Australia and Fiftyfive5, N=1,541, https://superblog.netlify.app/2021/07/28/nationally-representative-retirement-survey-results/

A further 37% of pre-retirees rely on themselves to make these often complex and time-consuming financial decisions. Trust rather than cost was a key motivating factor in this group deciding to take a 'DIY' approach to planning. For this group access to quality, independent information and guidance is crucial.

The final 38% of pre-retirees in our survey are largely disengaged with retirement planning. This group was more likely to come from lower wealth households, where limited resources meant the group had limited savings to make financial decisions over. In general, financial advice and guidance is poorly adapted to this group's needs. They have relatively less to gain from advice and significant spending would be required to get this cohort to engage with retirement planning in the first place.

As currently drafted, the terms of reference will go some way in addressing the affordability of advice. So long as this is not done at the cost of quality this type of focus will especially help the 25% of people who look to financial advisers to address their needs. However, the affordability of advice will always be relative. Just as there is an affordability barrier to accessing other kinds of professional services, such as lawyers, the likely reality will be that the business model of paying for individual personal financial advice in a private market will always be out of reach for a significant proportion of people. According to research from the Financial Services Council (FSC), reducing consumer protections, such as removing the safe harbour steps and statements of advice, would lower the average cost of providing advice from around $5,300 to $3,500.[9] According to the industry lobby this would "allow advisers to provide advice to up to an additional 44 new clients each year".[10] For the 25% of the population who seek out financial advisers to help them with their retirement planning this cost saving may be of benefit, but as noted, cost is not the critical factor for many consumers looking to plan for retirement. If this approach is taken the Review also needs to carefully assess the impact on consumer outcomes if these protections are removed.

Charging $3,500 for advice is still seven times the $500 an average Australian is willing to pay for financial advice.[11] We agree that the cost savings of removing some compliance obligations should be assessed to see if they are actually delivering benefits to consumers. However, the changes proposed to date are unlikely to bridge the gap between the cost to deliver advice under current business models, versus what consumers are willing to pay. As such the Review should focus its attention on examining how new ways of delivering advice to low and middle Australia could address both the cost and trust requirements of consumers.

A one to one delivery model for financial advice is by its nature not scalable and as a result will always come at a significant cost beyond the means of the average Australian. The Review needs to recognise this fact and look at how other countries around the world have dealt with

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[9] FSC White Paper on Financial Advice, p3

[10] FSC, 2021, 'FSC launches White Paper on Financial Advice',

[11] Rice Warner, Future of Advice, p11

this challenge. The model also relies heavily on trust in the advice sector. Due to ongoing conflicts of interest consumers have concerns about the extent to which they can trust advisers and super funds to give them unbiased information. ASIC's MoneySmart and other government resources provide some good independent strategic guidance, but these are underused and do not provide product level recommendations that consumers require to act on their advice. This leaves a significant gap for low and middle income Australians looking for quality independent information to help them self-manage their retirement planning.

The Review must look for new solutions to address the needs of consumers, particularly low and middle Australians seeking retirement guidance. Getting the right advice over retirement savings can make a significant difference in someone's standard of living across the decades many spend in retirement. In 2015, the United Kingdom Government conducted the Financial Advice Market Review (FAMR). This review's Terms of Reference specifically looked at "the advice gap for those people who want to work hard, do the right thing and get on with life but do not have significant wealth".[12] The Australian review could benefit from a similar approach by starting with an assessment of what this demographic needs to help them plan for retirement.

Specifically, it should focus on the needs of the cohort (37%) of people in our research who currently prefer to take on retirement planning themselves, primarily due to this lack of trust in advisers and super funds to give them unbiased information.[13]

Many individuals may find themselves in poor products due to a lack of guidance and complexity. This can have dire consequences for their retirement savings. For example, we identified a MySuper fund where the pension account is comparable to the MySuper option. The fund's option performs 142 basis points below the benchmark portfolio over a six year rolling net return as of June 2020.[14] There are over 500,000 fund members in the default option who may be exposed to this underperformance if they did not select a different option at retirement. The UK Financial Conduct Authority found: "the majority of consumers (60%) do not switch providers when they buy an annuity, despite the fact that 80% of these consumers could get a better deal on the open market, many significantly so.[15] Australia is likely to be similar. On a system wide-scale, this may mean Australians stick with a poor fund and end up increasingly relying on

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[12] https://www.gov.uk/government/publications/financial-advice-market-review-terms-of-reference/financial-advice-market-review-terms-of-reference

[13] Retirement Planning Survey, February 2021, Super Consumers Australia and Fiftyfive5, N=1,541, https://superblog.netlify.app/2021/07/28/nationally-representative-retirement-survey-results/

[14] We are using the December 2020 APRA MySuper Heatmap which has investment performance over six years to June 2020. We can derive whether the performance of the MySuper option is more than 50 basis points below the benchmark portfolio after accounting for current administration fees (we deduct the median 50K industry fee from benchmark portfolio and the 50K admin fee from the funds 6 year net return). Our approach is a close approximation of the APRA performance test.

[15] Financial Conduct Authority, February 2014. At http://www.fca.org.uk/static/documents/thematic-reviews/tr14-02.pdf

the pension as people run out of money earlier than they should have. A new model has the potential to provide individual and system wide savings that no other model can solve for.

Consideration should be given to the benefits of establishing a model in Australia similar to the UK Money and Pensions Service. The UK model integrated a range of services into a one-stop-shop. Their Pension Wise service gives people access to free, impartial, specialised guidance - delivered face to face or over the phone - about their pension options. It also provides a free, online tool to help people choose how to access their pension money, including a product comparison tool.

This model was a result of an industry-wide consultation process following the introduction of new 'pension freedoms' which provided people with more flexibility in accessing their pension pots. The government deemed it necessary for everyone in the UK approaching retirement to be offered guidance that was impartial, good quality and covered the options in the market. The majority of respondents to the consultation highlighted the need for guidance to be trusted by consumers, and the vast majority, including most of the financial services industry, agreed that consumers would not trust guidance given by a person or organisation with a vested interest in selling a financial product.[16] The government decided that this guidance should be provided by organsations that are independent and have no actual (or potential) conflict of interest.

The pensions guidance part of the service had a budget of £36.9m (AUD$72m) in 2019/20.[17] Feedback from users on the Pension Wise guidance service has been very positive, with a 94% satisfaction rate.[18] In the words of a recent departmental review of the service: "Debt advice charities, banks, investment companies and pension providers are all unequivocally supportive of the role MaPS plays in the UK; as one interviewee for this review put it 'if MaPS didn't exist, we'd have to invent it'."[19]

In Australia, responsibility for these types of services fall between different government bodies and private service providers. ASIC MoneySmart is responsible for providing web based tools and information. The Financial Information Service and Centrelink provide some direct financial advice and pension related information. Not-for-profits like financial counselling and community legal services linked with the National Debt Helpline cover direct advice to people in financial

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[16] Freedom and choice in pensions: government response to the consultation https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/332714/pensions_response_online.pdf, p21

[17] https://www.ftadviser.com/pensions/2019/04/10/industry-to-pay-36-9m-for-pension-guidance/

[18] Pension Wise service evaluation, https://moneyandpensionsservice.org.uk/wp-content/uploads/2020/10/Pension-Wise-Service-Evaluation-report-2019-2020.pdf

[19] Department of Work and Pensions, 2021, 'Departmental Review of the Money and Pensions Service (MaPS)' available at: https://www.gov.uk/government/publications/departmental-review-of-the-money-and-pensions-service-maps/departmental-review-of-the-money-and-pensions-service-maps

hardship dealing with credit, debt and some insurance issues. However, unlike the UK, these services are not connected up or advertised through a single portal. Our consumer research on engagement with financial decision making has highlighted the need for consumers to have access to a 'one stop shop'.[20] Currently these services are spread out over multiple locations meaning some consumers aren't aware of the different service offerings that may assist them. In the words of one respondent to our survey on retirement planning:

> *"I am a reasonably well educated, reasonably intelligent person who is overwhelmed by the process of retirement. I have not dared to go to Centrelink to find out about options going forward as I hear so many horror stories. I had no idea of several of the options in your survey of places to find out about retirement and I wish I had made a screen shot of that page of the survey!" - Michele (65-74, retired)*

Recommendation 3

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- Those who seek out experts to make financial decisions for them.
- Those who what to take a DIY approach to financial planning.
- Those who are disengaged with their finances including those experiencing financial hardship.

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The Review should investigate solutions to guarantee trusted guidance to all Australians who want it, that is impartial, conflict free, high quality, and covers the ranges of options to help people make sound decisions and equip them to take action.

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The Review should examine the UK Money and Pensions Service as one of the options for an alternative model for the delivery of conflict-free, affordable advice in Australia.

Have more than 'regard' for the Retirement Income Covenant and Retirement Income Review

The Retirement Income Covenant is likely to lead to a large expansion of the range of retirement products available to people. The Retirement Income Review found that people already face significant complexity in retirement planning.[21] While the covenant is likely to drive super funds to develop better strategies and products for the retirement phase these benefits

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[20] CHOICE, 2016, 'Project Superpower' available at: https://www.choice.com.au/-/media/39a3a46234d64be398df0ebaba25c65d.ashx?la=en

[21] Retirement Income Review, p17

may be lost if it is not accompanied by improved guidance for consumers. Funds will be reluctant to spend resources developing more appropriate offers and consumers are unlikely to take them up without improvements in the current advice offering. As already raised, the lack of affordable, independent guidance to low and middle Australia is a significant barrier to people taking up more appropriate products. Some of the decisions consumers need to make about these products will be one off and have repercussions for their standard of living throughout retirement, so it is important that they get these decisions right.

While there are protections at the market level in the form of design and distribution obligations and member outcomes assessments, these are not designed to assist an individual make a decision about the best product for them. Likewise, existing individual focused protections, like product disclosure, have consistently been found to be poor consumer protections.[22]

The Review should look at the role super funds can play in helping to guide people to more appropriate products. It should also set a bright line to help funds avoid directing their members in situations where the fund has an inherent conflict of interest. For example, it may be appropriate for a fund to give a holistic view of the types of products available to retirees that would address the various needs a retiree is likely to have across the remainder of their life. However, it would be inappropriate for a fund to confine this guidance to only products that the super fund offered, or recommend a specific product that the fund offered. To fill the gap this creates, people need access to a quality independent advice service.

A review of advice will be quickly out of date if it doesn't consider the central impact the covenant will have on Australians who are retiring and need help. As we have highlighted the UK, implemented 'a right to financial guidance at retirement'. Australia's review on advice must determine how our framework will complement the Retirement Income Covenant and findings of the Retirement Income Review.

Recommendation 6

The Review should assess how to best address the advice needs of people in low and middle Australia as they grapple with the complexity of retirement planning.

Consumer Action Law Centre's submission

Separate from the issues in this submission, we have had the opportunity to review the submission authored by Consumer Action Law Centre and we endorse those recommendations.

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[22] ASIC, 2019, 'REP 632 Disclosure: Why it shouldn't be the default', available at: https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-632-disclosure-why-it-shouldn-t-be-the-default/