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Advice and Investment Branch
Retirement, Advice and Investment Division
Treasury
Langton Crescent
Parkes ACT 2600

AdviceReview@treasury.gov.au

ClearView Submission – Quality of Advice Review terms of reference

ClearView Wealth Limited is an ASX-listed diversified financial services company that partners with financial advisers to help Australians achieve their financial and wellbeing goals by protecting and growing their wealth.

Proudly Australian, we are focused on two business segments, Life Insurance and Wealth Management. As at 30 June 2021, ClearView had \$289 million of in-force premiums and \$3.39 billion in funds under management. Our life insurance products appear on almost 800 approved product lists across Australia's financial advice community¹.

ClearView participates in financial advice through its 24.5 per cent shareholding in Centrepoint Alliance, one of the top 10 financial advice businesses in Australia.²

Introduction

We thank you for the opportunity to provide feedback on the terms of reference for the Quality of Advice Review, which was a key recommendation of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. We recognise this forms part of the Government's broader commitment to ensure Australians have the benefit of quality, affordable and accessible financial advice.

The financial advice sector has been subject to a series of major inquiries and reform packages over the last 15 years aimed at improving the quality of advice, the consequences of which have severely impacted the affordability and accessibility of advice. Modelling conducted by KPMG for the Financial Services Council (FSC) last year indicated the cost to service a single client within the existing advice regulatory regime is now almost \$5,500. At the same time, research conducted by ASIC indicates cost is the number one barrier to more consumers seeking financial advice.³

¹ As of 30 June 2021

² Licensee Owners List 2021, Professional Planner, June 2021

³ 'How to get financial advice without forking out \$3000', The Australian Financial Review, 20 April 2021

Evidence suggests the focus on improving advice quality and consumer protection in recent years has been successful, with just 2 per cent of complaints received by the Australian Financial Complaints Authority in FY20 relating to the financial advice industry⁴. ClearView believes it is now critical that the Government's review turn its sights to addressing both advice affordability and accessibility. Advice affordability and accessibility form two of the three key pillars to a properly functioning and effective advice ecosystem – the third being quality.

Summary of feedback to terms of reference

We have put forward a series of recommendations concerning where the review should focus its efforts and data collection in order to pinpoint areas for improvement on both accessibility and affordability of advice. These include the following:

- A focus on the benefits versus costs of repealing the safe harbour provisions in the best interests duty, which is one of the key drivers of increased regulatory burden for advisers;
- How scaled advice can be better used within a financial advice practice to mitigate licensee concerns regarding legal liability associated with this type of advice;
- Reforming advice documents from the perspective of the consumer and rejecting the provision of excessive disclosure as a solution to advice misconduct;
- Modernising sophisticated investor definitions to bring them better in line with current household wealth levels in Australia;
- Creating clarity and certainty for financial services organisations in relation to general and personal advice definitions;
- Retaining choice in relation to payment and remuneration for insurance advice clients;
- Financial and compliance impacts of the Design and Distribution Obligations legislation on advice businesses, which is likely to further drive up the cost of advice; and
- Interaction between APRA's IDII reforms and servicing requirements for insurance advisers, which will also significantly increase the cost of ongoing insurance advice for consumers.

Impact of the safe harbour provisions on regulatory burden

The draft terms of reference to the Quality of Advice review rightly identify the safe harbour provisions demonstrating compliance with an adviser's best interest duty as a key target for reform within the current advice legislative framework. Commissioner Hayne identified the

⁴ 'Advice complaints fall to 2% in FY20', IFA, July 2020



provisions as overly prescriptive in his final report and recommended they be repealed if no clear justification could be found for retaining them.⁵

ClearView supports the views of the FSC in its 2021 white paper on financial advice, where it argued that such prescriptions had no place in a move to principles-based regulation for the advice industry, which is what Commissioner Hayne envisioned and what more recent reforms such as the FASEA Code of Ethics have focused on.

The safe harbour provisions in their current form make simple advice unviable and are contributing to licensee reluctance to implement scaled advice for consumers, as adhering to these provisions requires the same amount of paperwork and research for both simple and comprehensive advice in order for the adviser to prove compliance with the best interests duty, and are the key driver of increased compliance costs in advice⁶. KPMG estimates the removal of the provisions would immediately reduce the cost of advice between 9 and 11 per cent.⁷

Recommendation: ClearView recommends the review investigate how the safe harbour provisions can be repealed and replaced with principles-based guidance, with minimal compliance disruption for financial advice practices.

The current and future role of scaled advice

The terms of reference identify that the current role and bounds of scaled, intra-fund or limited scope advice should be considered as part of the review. In line with the point above, despite attempted progress from ASIC in 2021 to examine the barriers to further scaled advice take-up, overly complex rules around what constitutes personal advice are still preventing the vast majority of licensees from allowing their representatives to offer scaled advice.

ClearView recommends the review focus on the degree to which limited or scaled advice is currently being used in advice practices and the concerns of licensees in allowing their authorised representatives to provide scaled advice. The aim of this section of the review should be to establish some clear and workable principles for a scaled advice framework that is likely to generate mass take-up by advice businesses and can be practically implemented and enforced by regulators.

Recommendation: ClearView recommends the review focus on how a workable scaled advice framework can be established so that the majority of licensees would be comfortable to adopt from a liability perspective.

Reforming advice documents

The review proposes to consider how to improve the clarity of advice documents to present consumers with more concise information, and to examine current advice disclosure requirements including statements of advice (SOAs). ClearView believes the current disclosure regime, which has been heavily influenced by successive layers of regulation in

⁵ Final Report of the Royal Commission into Misconduct in Banking, Superannuation and Financial Services, P26

⁶ FSC White Paper on Financial Advice 2021

⁷ FSC White Paper on Financial Advice 2021

the industry, needs to be urgently addressed from the point of view of relevance and legibility to the consumer.

Current SOAs can be up to 100 pages in length, with a focus on excessive disclosure to mitigate compliance risks rather than information that is useful to the client⁸. In support of this, consumer research commissioned by the FSC also indicated almost two thirds of advice customers wanted less paperwork from their adviser⁹.

Recommendation: ClearView believes that in reviewing advice disclosure documents, Treasury should start from the point of view of the consumer, what information they find meaningful and what means of communication they would most engage with.

The sophisticated investor loophole

The draft terms of reference state that the review will consider whether current processes for determining whether an investor is wholesale are working effectively. ClearView supports reviewing the current sophisticated investor tests under the Corporations Act 2001 as a matter of urgency. These tests are out of step with current household wealth levels among middle class Australians and are restricting many from access to the consumer protections that come with retail financial advice.

The threshold tests to determine if an investor is 'wholesale' or sophisticated, and therefore excluded from retail advice protections, as outlined in the Corporations Act currently include clients with \$2.5 million in net assets, \$250,000 in gross income over two financial years, or a minimum investment of \$500,000 in a financial product. These thresholds have not been updated since 1991¹⁰ and have previously been flagged by Treasury in its Future of Financial Advice consultations as requiring reform.

As the cost of giving retail advice has increased enormously, the gap between wholesale and retail investor compliance requirements is shifting the dynamics of the industry, with large institutions exiting retail advice and doubling down on the wholesale market¹¹. The FSC estimates an increase in the net assets threshold test for wholesale clients to \$5 million would see more than 275,000 current wholesale investors be reclassified as retail¹².

Recommendation: ClearView believes the review should focus on establishing an industry consensus on adequate threshold tests for today's client, as well as mechanisms to ensure the thresholds are regularly updated (eg indexing to the Consumer Price Index). There should also be consideration to bringing consistency between the legal definition of a wholesale investor, and the FASEA Code of Ethics which states advisers may not rely on these definitions if they do not believe their client is financially literate enough to understand the advice being given.¹³

⁸ 'Digital SOA in works due to 'absurd and obscene' current system, IFA, 30 July 2021

⁹ FSC White Paper on Advice 2021

¹⁰ AXA and Charter Financial Planning submission to Treasury's FOFA Options Paper, January 2011

¹¹ 'NAB eyes HNW expansion with global banking buy', IFA, 10 August 2021

¹² FSC White Paper on Advice 2021

¹³ FASEA Financial Planners and Advisers Code of Ethics Guidance 2019, p11



Clarity and efficiency in advice definitions

The terms of reference have flagged the current definitions of 'financial product advice', 'general advice' and 'personal advice' as important parts of the Quality of Advice review in terms of how they are used by licensees and whether they need simplification.

ClearView believes the review should consider the possibility of repealing the definition of 'general advice', which can effectively no longer be used by financial institutions who have an existing relationship with a consumer following the decision of the High Court in *Westpac Securities Administration & BT Funds Management v ASIC* last year. The case found despite representatives of Westpac giving a general advice warning and providing generic information to customers, the existence of a previous relationship between Westpac and the customers meant it was likely customers believed their circumstances were taken into account, and therefore the advice was considered to be personal, as per the Corporations Act definition of personal advice.¹⁴

As a result of this, any review may question the need for a distinction between 'general' and 'personal' advice as sub-categories within the overarching 'financial product advice' definition, given that all advice provided by institutions who know their customers could be considered effectively personal. The FSC has suggested the term 'general advice' be replaced with the legal term 'general information' to remove these layers of complexity in advice definitions and clearly delineate that any information given is not specific to the person's circumstances.

The review could also consider whether 'financial product advice' as a term needs to be updated or eliminated, as per the suggestions of both the FSC and Financial Planning Association that the process of giving advice needs to be clearly separated from the sale of financial products as the advice profession modernises.¹⁵

ClearView suggests the review also explore the impact of personal advice obligations on insurance advice as a specialty, which has already been heavily restricted in terms of consumer access by other pieces of insurance advice reform detailed in the point below. Recent legal precedents in this area including *Commonwealth Financial Planning vs Couper* and *Swansson vs Harrison* suggest limited scope advice on insurance may still trigger broader obligations in light of the definition of personal advice, and that personal advice obligations may also include the obligation to investigate changes in clients' medical conditions that could affect their policy eligibility over time.

Recommendation: ClearView suggests the review consider the implications of removing the sub-categories of 'general' and 'personal' advice as legal definitions and updating the current overarching definition of 'financial product advice'.

Impact of advice reform on life insurance

The terms of reference propose the Quality of Advice review will examine two elements related to life insurance advice – the impact of the life insurance framework on levels of

¹⁴ 'Court dismisses Westpac advice appeal', IFA, 3 February 2021

¹⁵ FSC 2021 White Paper on Advice; 'Affordable Advice, Sustainable Profession': FPA Policy Platform 2020



insurance coverage in Australia, and whether the conflicted remuneration exemption for insurance advice should be removed, as per Commissioner Hayne's suggestion in his final report.

Financial services research consultancy NMG's Australian Life Insurance Market Research Report in June 2020 stated that as a result of the previous five years of regulatory reform to insurance advice, including FOFA and the LIF, Australia is now ranked toward the bottom of the top 10 insurance markets in the world when it came to access to information and choice of products. This is particularly for middle-market consumers at key life stages where they required access to insurance, such as buying a home.

At the same time, the increase in lapse rates that the LIF was partially introduced to address, has continued with sustainability issues in the insurance market causing more clients, rather than advisers, to initiate product replacement or cancellation.¹⁶

Most corners of the financial services industry are now unanimous in calling for the retention of some form of commission structure to prevent further degradation of access to insurance advice, assistance and information for consumers,¹⁷ According to a 2019 ClearView survey of over 600 self-employed advisers, over half said they would stop providing insurance advice if commissions were removed or further reduced as a payment option.

ClearView believes it will be important for the review to consider any future changes to the structure of risk advice commissions and whether improvements can be made that lead to better consumer outcomes. Allowing more innovation in product payment structures could provide insurers the opportunity to design products that are more commercially viable for advisers while removing inappropriate incentives, carrying less additional costs for consumers.

The focus of any investigation should be on facilitating choice in payment models for consumers seeking advice structures that allow consumers to spread the cost of advice and retain the ability for advisers to advocate for their clients at claim time in a way that makes their time commercially viable.

Another important point to consider is the degree of support received by the consumer when making a claim through an adviser, and whether further restricting consumer access to insurance advice could lead to lower payout ratios for the client at claim time. The latest APRA statistics show that claims on advised life products are paid up to 20 per cent more often over the course of a year depending on the type of cover.¹⁸

A 2019 ClearView adviser survey also saw advisers nominate claim advocacy and administration as one of the top services funded through their clients' ongoing commission payments. This ensures advised insurance products provide better value for consumers and reduces the need for the policyholder to enter a costly and drawn-out litigation process when pursuing a claim.

¹⁶ 'Challenges confronting the Australian Life Insurance Market', Choice and Access to Life Insurance, June 2020

¹⁷ Challenges confronting the Life Insurance Market, the Association of Financial Advisers, November 2020. <https://www.afa.asn.au/news/challenges-confronting-the-life-insurance-market>

¹⁸ Life insurance claims statistics and disputes, APRA, June 2021

Recommendation: ClearView recommends the review take serious consideration of whether choice and access to life insurance advice and support would be further restricted by the removal of the conflicted remuneration exemption for life insurance. The review could also consider potential future changes to the structure of commissions to create better consumer outcomes.

Impact of DDO on advice costs

The terms of reference state that the review should have regard to 'other key regulatory developments' in the advice space, including the design and distribution obligations (DDO). While DDO has been touted by ASIC as a "game changer" in putting the onus on product manufacturers to adequately target their products to the right market¹⁹, it also puts a considerable reporting obligation on financial advisers, many of whom effectively run a small business.

Advice industry bodies have suggested the new reporting obligations on licensees around product dealings and complaints will add further costs and compliance hours to already stretched advice businesses.²⁰ The FPA has argued for the strengthening of carve-outs within the obligations for providers of personal advice, as well as bringing complaints reporting requirements in line with other obligations for advice licensees under ASIC's new internal dispute resolution guidance.²¹

ClearView believes the Quality of Advice review needs to look at the year-one impact that DDO requirements are having on advice businesses in terms of resourcing, administration time and increased costs to the consumer. It should also examine how carve-outs for personal advice providers may be able to work more effectively without creating duplicate paperwork for licensees.

Furthermore, the current DDO obligations may restrict future product innovation and consumer access to choice of financial products, given the prescriptiveness of target market determination rules. ClearView suggests the review look at the impact of the new rules on the range of product types advisers are able to offer consumers, and whether this could be better balanced with consumer protections under future ASIC guidance around DDO.

Recommendation: ClearView recommends the review investigate the financial impact of the DDO requirements to financial advice businesses and whether improvements could be made to personal advice carve-outs, as well as the impact of the legislation on consumer access to financial products.

Interaction between APRA IDII changes and insurance advice

APRA has recently introduced a raft of changes to the way life insurance providers must structure their income protection products, in response to sustainability issues within the

¹⁹ Media release: ASIC releases regulatory guide on product design and distribution obligations, 11 December 2020

²⁰ 'ASIC called out on 'unnecessary and unworkable' DDO requirement', IFA, 16 September 2021; 'Industry body launches petition to delay DDO', IFA, 30 September 2021

²¹ FPA submission to ASIC on updated DDO requirements, 21 September 2021



individual disability income insurance (IDII) market.²² ClearView believes it's important for the review to consider the flow-on impacts of these changes to the adviser market and consumer access to insurance, which has already been heavily restricted by previous regulatory changes.

From 1 October 2022, it is proposed that insurance providers are only able to offer a policy contract term of up to five years for clients that purchase income protection insurance. The FSC has pointed out that this measure is likely to lead to further significant growth in lapse rates, particularly under the opt-in model favoured by APRA, as consumers opt not to renew after five years for affordability reasons or because they have left an adviser relationship during that time. It will also add significantly to the cost of advice and to adviser servicing times per client, as it may be considered consumers need a full advice review after the expiry of each five-year policy term under the current personal advice regulatory regime.²³

Recommendation: ClearView suggests the review include in its terms of reference the impact of APRA's IDII obligations on insurance advice, as part of its broader investigation into newly introduced key regulatory developments.

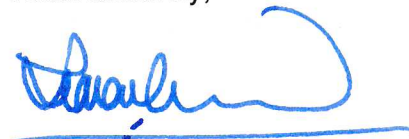
Concluding remarks

We welcome the opportunity for the industry to provide input on the many overlapping issues of concern from a regulatory perspective that are impacting both cost and accessibility in the advice space. These issues should be thoroughly investigated and addressed by Treasury as part of any wide-ranging review into the effectiveness of the advice model in Australia.

ClearView fully supports the Quality of Advice review as a critical opportunity to get the regulatory settings right for financial advice and balance consumer protection with choice and access to advice. This is particularly so given over a decade of significant regulatory reform to financial services. We look forward to making further contributions to the review process.

We would also welcome an opportunity to further discuss or clarify any of the points raised in this submission if deemed necessary.

Yours sincerely,



Simon Swanson
Managing Director

²² Letter to insurers: Final individual disability income insurance sustainability measures, APRA, 30 September 2021

²³ FSC Letter to ASIC and APRA, Opt-in approach for policy contract term measure, 20 December 2021