The Future of Financial Advice: Reforming the reforms - the current state of play

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This paper considers the FOFA reforms that came into effect on 1 July 2013 against the amendments to the current FOFA legislation proposed in the exposure draft of the Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014 and the Corporations Amendment (Streamlining Future of Financial Advice) Regulation 2014 released by Treasury on 29 January 2014.

Part 1 of this paper sets out the legislative framework of the FOFA reforms that took effect on 1 July 2013 and highlights the key amendments proposed in the recently released exposure draft of the new reforms.

Part 2 of this paper considers some of the complexities and challenges faced by the industry in implementing aspects of the current FOFA regimes such as client directed payments, best interests duties and scaled advice, and discusses the ways in which the proposed reforms may alleviate these challenges.

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Background

FOFA reforms

On April 2010, the Minister of Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen MP, announced the Future of Financial Advice (**FOFA**) reforms. The FOFA reforms represent the Government's response to the 2009 *Inquiry into Financial Products and Services in Australia* by the Parliamentary Joint Committee on Corporations and Financial Services, that considered a variety of issues associated with corporate collapses, including Storm Financial and Opes Prime.

The FOFA reforms have been implemented by two Acts, namely, the *Corporations Amendment (Future of Financial Advice) Act 2012 (Cth)* and the *Corporations Amendment (Further Future of Financial Advice Measures) Act 2012 (Cth)*, which amended the *Corporations Act 2001 (Cth)* (the **Corporations Act**) and the *Corporations Regulations*. The reforms were voluntary from 1 July 2012 and mandatory from 1 July 2013.

The underlying objective of the reforms was to improve the quality of financial advice while building trust and confidence in the financial advice industry through enhanced standards which align the interests of the adviser with those of the client, reduce conflicts of interest and facilitate access to financial advice through the provision of simple or limited advice. Broadly, the reforms set up a framework with the following features:

- a 'best interests' obligation for financial advisers requiring them to act in the best interests of their clients and to place the interests of their clients ahead of their own when providing personal advice to retail clients;
- a ban on conflicted remuneration (including product commissions, volume payments and soft-dollar benefits), where licensees or their representatives provide financial product advice to retail clients;
- a ban on volume-based shelf space fees from asset managers or product issuers to platform operators;
- a ban on asset-based fees on borrowed amounts;
- a requirement for providers of financial advice to obtain client agreement to ongoing advice fees and enhanced disclosure of fees and services associated with ongoing fees, including a requirement for ongoing advice fees to be actively renewed by retail clients every two years; and
- enhanced ASIC powers to deal with licensing and banning orders.

Reforming the reforms

On 20 December 2013, the Assistant Treasurer, Senator the Hon Arthur Sinodinos AO, announced major reforms to the Labor Government's FOFA legislation. Senator Sinodinos has said that these reforms are designed to deliver affordable and accessible financial advice and reduce compliance costs for the financial services industry by removing some of the significant burdens and complexity that were present under the Labor Government's regime.

On Wednesday 29 January 2014, Treasury released exposure drafts of the Corporations Amendment (Streamlining of Future of Financial Advice) Bill 2014 (**Bill**) and the Corporations Amendment (Streamlining Future of Financial Advice) Regulation 2014 (**Draft Regulations**) (together, the **New FOFA Reforms**), to amend the FOFA provisions contained in Part 7.7A of the Corporations Act and the Corporations Regulations in accordance with the announcement by the Assistant Treasurer on 20 December 2013.

In summary, the New FOFA Reforms include the following key amendments to the Corporations Act and the Corporations Regulations:

- Opt-in: The removal of the opt-in requirement so that advisers no longer need to seek their client's agreement to the relevant fee arrangement every two years. An 'opt-out' system will apply so that any ongoing fee arrangement continues to exist unless the arrangement is terminated by either the client or the adviser.

- Annual fee disclosure: The removal of the retrospective application of the fee disclosure requirement, so that advisers will not need to provide fee disclosure statements to clients who entered into a fee arrangement before the mandatory 1 July 2013 commencement date of FOFA.

- Best interests duty catch-all: The removal of the catch-all provision (section 961B(2)(g)) so that advisers can be certain they have satisfied their obligations under the best interests duty.

- Scaled advice: Clients and advisers will be explicitly allowed to agree on the subject matter of advice to be provided.

- Life insurance inside super: The ban on conflicted remuneration will only apply to commissions on risk (life) insurance products inside superannuation in relation to MySuper or in circumstances where no personal financial advice has been provided to the member regarding life insurance.

- General advice: Benefits relating to the provision of general advice will be exempt from the ban on conflicted remuneration.

- Execution-only exemption: A causal link will be introduced into the exemption so that benefits are permitted where no advice has been provided to the client by the individual or licensee receiving the benefit (as opposed to the licensee or authorised representative more broadly) in the previous 12 months.

- Training exemption: The existing training exemption is broadened to include forms of education and training that are relevant to the operation of a financial services business as opposed to just the provision of financial product advice.

- Volume-based shelf-space fees: The drafting of the ban on volume-based shelf-space fees has been amended to clarify that incentive payments between fund managers and platform operators for preferential treatment of certain products on the platform 'shelf' are banned.

- Intra-fund advice: A note has been inserted which will clarify the term 'intra-fund advice'. The note provides that intra-fund advice is commonly used to describe financial product advice given by a trustee of a regulated superannuation fund to its members and links the commonly used term with the rules under section 99F of the *Superannuation Industry (Supervision) Act 1993 (Cth)* (**SIS Act**).

- Client paid exemption (**CPE**): A clarificatory note has been inserted to the effect that a reference to giving a benefit includes a reference to causing or authorising it to be given. The Draft Explanatory Memorandum to the New FOFA Reforms states that the benefit may be paid directly by the client or by another party where the benefit is given at the direction of the client with the client's clear consent.

- Grandfathering: The existing grandfathering provisions will be amended to, among other things, allow advisers to move between licensees and to continue to access grandfathered benefits in certain circumstances.

- Conflicted remuneration: The conflicted remuneration provisions will allow for the payment of benefits under 'balanced' remuneration structures.

- Minor technical amendments: What the Government describes as a number of minor amendments will be made to address technical issues including in relation to:

    - the stamping fee exemption - to include capital raising activities and broaden its application to include investment entities;

- brokerage fee exemption - to include brokerage fees paid in relation to financial products traded on the ASX24;
- ensuring that the wholesale/retail client distinction that currently applies in other parts of the Corporations Act also applies in respect of the FOFA provisions; and
- clarifying the operation of the mixed benefits provisions.

A question arises as to whether these are truly 'technical' and 'minor' amendments or are part of a much more significant set of changes.

The recent debate about whether and how the Government will get its package of the New FOFA Reforms through Parliament raises more fundamental issues of the rationale for the changes.

At its heart there is a strong tension between consumer groups and funds managers about what the appropriate balance should be between incentivisation and protectionism.

It is also not surprising that much of the tension involves different views on Government paternalism. Certain types of incentivisation would appear more universally acceptable than others. For example, the new package acknowledges the legitimacy of the so-called balanced scorecard regulations whereby, subject to controls, employees can be paid low amounts of volume related remuneration.

There are also issues of certainty and efficiency. For example, the changes to the best interests duty where the procedural defence available to advisers has been simplified. This is primarily a certainty measure as the previous test did not give clarity, or at least not sufficient clarity, to advisers about how they needed to satisfy the duty.

Restructuring the adviser-client relationship?

1. The 'best interests' obligations

The New FOFA Reforms make the following key amendments to the best interests obligations:

- The removal of the 'catch all' provision of the best-interests duty safe-harbour, which requires advisers to prove that they have 'taken any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interest of the client, given the client's relevant circumstances.' Advisers will still be required to satisfy the remaining six steps of the safe-harbour specified in section 961B(2). This reform will be welcomed by businesses who will now have greater certainty on their ability to meet the best interests duty obligations.
- Clients and advisers are now explicitly permitted to agree on the scope of any scaled advice provided. Providers will only need to investigate the client's objectives, financial situation and needs that are relevant to the scaled advice to be provided in discharging their best interests obligations.

  Although ASIC and the Government had previously indicated that they were in favour of financial planners providing low cost scaled advice, the scaled advice model did not sit neatly with the best interests duty requirements, especially those in relation to obtaining details of the objectives, financial situation and needs of the client disclosed by the client through instructions.

  The drafting of the legislation indicated that it was the client that needed to give instructions even though as a matter of practice it is the client and the adviser who will together determine the scope of instructions. Although it is still possible to provide scaled advice under the current drafting of the legislation, the processes that the adviser needs to go through to get to that position are burdensome on advisers and involve a level of risk because they rely on advisers strictly following set procedures and scripts. Clarification that advisers and clients can agree on the scope of advice and the removal of the 'catch-all' provision is certainly helpful in this regard and provides certainty as to the scope of adviser's duties.

- The clarification of the circumstances in which an agent or employee of an ADI may access the reduced best interests duty safe-harbour. The New FOFA Reforms provide that an agent or employee of an ADI can satisfy the reduced best interests duty when the subject matter sought by the client relates to a basic banking product, general insurance product, consumer insurance product or a combination of these products.

2. Ongoing fee arrangements

2.1 Removal of the renewal notice 'opt-in' requirement

An ongoing fee arrangement exists where a retail client is given personal advice and charged an ongoing fee during a period of more than 12 months. The current law provides that advisers who have an ongoing fee arrangement with a retail client must obtain their client's agreement at least every two years to continue the ongoing fee arrangement. If after receiving the renewal notice, the client decides not to renew or fails to respond to the fee recipient's renewal notice, the ongoing arrangement terminates – i.e., the fee recipient is not obligated to provide ongoing financial advice to the client and the client is not obliged to continue paying the ongoing fee. The New FOFA Reforms remove the obligation for an adviser to provide a renewal notice to a client, and accordingly, an opt-out system will apply where any ongoing fee arrangement continues to exist unless the arrangement is terminated by either the client or the adviser. The 'opt-in' requirement has been removed on the basis that it would unnecessarily increase costs, red tape and uncertainty for both consumers and businesses. While this represents a win for businesses, many of whom were displeased with the administrative burden of the approach, it is unlikely to please consumer groups who saw the 'opt-in' requirement as important in ensuring that consumers were not paying ongoing fees in scenarios where they may not have even been aware that the fees were being deducted.

This is arguably the most controversial of the New FOFA Reforms. Importantly, a client can still terminate an ongoing fee arrangement under section 962E.

2.2 Fee disclosure statements

Under the current law, where an ongoing financial advice relationship exists between an adviser and a retail client which involves the charging of an ongoing advice fee, the adviser or fee recipient is required to give the retail client a fee disclosure statement which shows the fees paid by the client, the services the client received and the services the client was entitled to receive in the previous 12 months. The current drafting also means that fee disclosure statements are required to be provided by advisers in respect of arrangements that were entered into prior to 1 July 2013. The New FOFA Reforms amend the fee disclosure statement requirements, so that a fee disclosure statement is no longer required to be provided to clients who had entered into their ongoing fee arrangement before 1 July 2013. Ongoing fee recipients will still be required to provide annual fee disclosure statements to post-1 July 2013 clients.

The basis for the change is the large cost to industry and consumers, for minimal benefit. Given the difficulties that many organisations faced with identifying appropriate disclosure dates for legacy customers, this change is likely to be welcomed by the business community.

3. Curbing the scope of the ban on conflicted remuneration

3.1 General advice exemption

Under the current law, any benefit (monetary and non-monetary) received in relation to the provision of personal advice and general advice is captured by the ban on conflicted remuneration.

Under the New FOFA Reforms, the definition of conflicted remuneration has been amended so that benefits relating to the provision of general advice will be exempt from the ban on conflicted remuneration. The ban will continue to apply to benefits given to a licensee or a representative that could reasonably be expected to influence the personal advice provided or the financial products recommended to a retail client in the course of providing personal advice.

If this amendment is passed as law, it will significantly reduce the scope of benefits that are banned. The Government has stated that it has proposed the change because it considers that the application of the ban on conflicted remuneration risks limiting the availability of general advice and unnecessarily burdens the industry by capturing staff not directly involved in providing advice to clients. An example of the risk of limiting the availability of general advice is evident when one considers general advice placed on websites which are intended to assist and educate consumers. A number of licensees were preparing to or had removed general advice from their websites in order to ensure that they were not captured by the conflicted remuneration ban.

It is noted that the ban on volume-based shelf-space fees and asset-based fees on borrowed amounts will continue to apply in circumstances where personal advice is not provided.

3.2 Life risk policies

Under the current law, monetary benefits paid to licensees or representatives in relation to life risk insurance offered outside of superannuation are exempt from the ban on conflicted remuneration. However, benefits paid in relation to life risk insurance offered inside superannuation are generally banned, including in circumstances where advice has been provided in respect of a group life policy for members of a superannuation entity or a life policy for a member of a default superannuation fund.

Under the New FOFA Reforms, benefits paid to licensees or representatives in relation to life risk insurance offered outside of superannuation continue to be exempt. However, the exemption provided for monetary benefits paid in relation to life risk insurance policies offered inside superannuation will be broadened such that the ban on conflicted remuneration will only apply in relation to monetary benefits paid with respect to:

- life risk insurance products for MySuper members; or
- life risk insurance products offered inside other (non MySuper) superannuation products in circumstances where no personal financial advice (i.e. only general advice or no advice) has been provided to the member regarding life risk insurance.

The practical effect of this would be that commission can be paid on risk (life) insurance products provided within superannuation funds, where personal advice has been provided to the client. The Government has stated that the purpose of the change is to minimise market distortions and cost impacts that may result from the differing treatments of these benefits inside and outside of superannuation.

MySuper products are simple superannuation products that replace the existing default superannuation products. MySuper members are those members of a superannuation fund that hold an interest in a MySuper product. The New FOFA Reforms also provide that a life risk insurance product is considered to be provided for a MySuper member if the product is issued to the licensee (or custodian) of a superannuation fund for the benefit of the MySuper Members of that fund.

3.3 Execution-only exemption

Under the current law, benefits paid for execution-only services in respect of the issue or sale of a financial product are exempt from the ban on conflicted remuneration provided that financial product advice about the product, or class of product to which the product belongs, has not been given to the client as a retail client by the licensee or representative in the 12 months immediately before the benefit is given.

The New FOFA Reforms attempt to clarify this exemption so that execution-only benefits are exempt from the ban on conflicted remuneration except where advice on that product or products in that class has been provided to the client in the previous 12 months by the same licensee or representative (e.g. employee) receiving the benefits.

3.4 Education and training exemption

Under the current law, the education and training exemption provides an exemption from the ban on conflicted remuneration for education and training relating to the provision of financial product advice. The New FOFA Reforms are amended to broaden the existing training exemption provisions (section 963C(c)) to include other forms of education and training that are relevant to the operation of 'a financial services business', which includes the provision of financial product advice. The Draft Explanatory Memorandum provides that this could include training in relation to client administration services. The broadening of this exemption appears to be a sensible approach and seems unlikely to be controversial.

3.5 Basic banking exemption

Under the current law, a benefit is exempt from the ban on conflicted remuneration if the benefit relates to a basic banking product and the agent or employee of an ADI, at the same time as providing advice on the basic banking product does not provide financial product advice on any other financial product except a general insurance product.

Under the New FOFA Reforms, section 963D will be amended to exempt a benefit from the ban on conflicted remuneration where it relates to a basic banking product, and the agent or employee does not, at the time of providing advice on the basic banking product, provide financial product advice on any other financial product except a general insurance product or a consumer credit insurance product.

The Draft Explanatory Memorandum provides as an example that in order to have access to this exemption, the agent or employee, at the time of providing advice on the basic banking product, must not provide advice on financial products other than a general insurance or a consumer credit insurance product.

The practical consequence of this amendment is that an agent or employee will be able to advise on products that are not financial products for the purposes of the Corporations Act such as a credit card or home loan while advising on a basic banking, or a general insurance, or a consumer credit insurance product. However, an adviser will not be able to provide financial product advice in relation to a non-exempt product such as superannuation in the course of recommending a basic banking, general insurance or a consumer credit insurance product. In this case, the benefit (and arguably) the whole benefit would be caught as conflicted remuneration.

It is noted that the existing Regulation 7.7.A.12H which exempts benefits given in relation to basic banking and general insurance products has not been proposed to be removed in light of the above amendments. This appears to be an oversight and is expected to be repealed.

3.6 Stamping fees

The draft regulation introduces a significant expansion to the operation of the current exemption which will allow stamping fees to be paid in relation to capital raising activities in respect of investment entities.

An investment entity is currently defined under sub-Regulation 7.7A.12B(3) as an entity which provides a return to its shareholders (members) mainly from either an investment in financial products or in owning real property (other than for the purposes of developing the property), but does not include an 'infrastructure entity' (as defined under sub-Regulation 7.7A.12B(3). This definition is proposed to be removed under the New FOFA Reforms.

The effect of this amendment is that 'stamping fees' will be able to be paid in relation to capital raising activities in respect of investment entities.

The proposed changes also clarify that the exemption applies where the benefit is given to a provider in relation to an 'initial issue or sale' of an 'approved financial product'.

3.7 Stockbroking related exemptions

The Draft Regulations amend the application of the brokerage-related exemptions to ensure the ban on conflicted remuneration does not apply to brokerage fees which relate to transactions undertaken on the ASX24 or products traded on the ASX24.

3.8 Balanced scorecard remuneration arrangements

The Draft Regulations introduce a new performance bonus Regulation 7.7A.12EB which exempts monetary benefits provided to employees paid under a 'balanced scorecard arrangement' if certain specified criteria are met. A balanced scorecard remuneration arrangement exists where an employee receives remuneration that is calculated by reference to both volume-based and non-volume-based factors. The following criteria must all be met in order for the exemption to apply:

- the benefit is given to or for a provider who is an employee;
- the benefit is an element of the employee's remuneration;
- access to or the value of the benefit (or both) is partly dependent on the total value of financial products of a particular class, or particular classes, that are recommended by the employee or acquired by clients to whom the employee has provided financial product advice;
- the financial products are not already exempt from the ban on conflicted remuneration under specified sections of the legislation, including general insurance products under section 963B(1)(a), life insurance products (section 963B(1)(b), basic banking products (section 963D) and as prescribed under Corporations Regulations made for section 963B(1)(e);
- the benefit is ***low in proportion to the employee's total remuneration***;
- in calculating the benefit, the weighting attributed to the total value of the financial product is outweighed or balanced by the weighting attributed to other matters; and
- if the benefit or part of the benefit relates to personal advice provided to a retail client, that part of the benefit that relates to personal advice is given in circumstances that are likely to encourage the giving of personal advice that is in the client's best interests.

The Draft Explanatory Memorandum provides that a benefit is likely to be considered low if it comprises less than 10% of the employee's total remuneration. This new provision will provide greater flexibility and certainty for licensees in determining the remuneration structures for employees. While the term 'total remuneration' is not defined, in the writer's view it would clearly include fixed pay and any other monetary benefit. There is also a strong argument that non-monetary benefits would also be included in any calculation of 'total remuneration'.

On the basis that the performance bonus regulation does not apply to benefits which are automatically exempt from the conflicted remuneration under sections 963B(1)(a), 963B1(b) and 963D (i.e. general insurance products, life insurance products, employee benefits relating to recommendation of basic banking products, general insurance products and consumer credit insurance products) it appears there are two readings that could apply to the interpretation of this new regulation.

On a narrow reading the performance bonus regulation cannot be used in respect of advice provided in relation to basic banking, general insurance and consumer credit insurance (or a combination of these) products only as the regulation cannot be accessed for benefits that are potentially already exempt from conflicted remuneration. On this view, the performance bonus regulation can be accessed in respect of non-exempt benefits such as superannuation or managed investment products provided that they satisfy the 'low proportion' criteria along with the other requirements.

However, on a broader technical reading if a benefit relates to say basic banking products in circumstances where mixed advice has been provided on other products such that s 963D does not apply, then that benefit could be paid under the performance bonus regulation provided that the other requirements are also satisfied.

In the writer's view, the latter interpretation is the better interpretation of the performance bonus regulation. However, it is not clear that this is what was intended by the Government. In addition, it is also arguable that if the scorecard is appropriately segmented, a 10% benefit could be given in relation to each financial product the subject of the scorecard.

In light of the above, it is expected that the Government will need to provide further details on what was intended to be covered by this regulation to give licensees and advisers certainty as to the payments which will be exempt from the ban on conflicted remuneration under this performance bonus regulation.

3.9 Permissible revenue exemption

The Draft Regulations introduce a new Regulation 7.7A.12HA which provides that a benefit will not be conflicted remuneration where the amount or value of the benefit is calculated by reference to another benefit:

- that is not conflicted remuneration; or
- to which Division 4 of Part 7.7A does not apply.

A question arises as to whether the practical effect of this provision is that it would expand the operation of the CPE in that it would allow advisers to pass on all or part of the benefit that is subject to the CPE.

The scope of this provision is unclear. Clearly there will be circumstances where the calculation of a benefit on the value of an exempt or grandfathered benefit will be appropriate.

However, the exemption on its face is broad and some delineation seems desirable. For example, it could be expressed to apply to benefits which are exempt under relevant provisions up to the value of those benefits.

4. Refreshing the grandfathering provisions

The Draft Regulations make amendments to the grandfathering arrangements so that when a business is sold, the purchaser of a 'grandfathered' book of business has the same right to rely on the grandfathering provisions as the person that sold the business. This allows continuity of the grandfathering of commissions and other remuneration within a book of business notwithstanding a change of ownership.

The Draft Regulations also amend the grandfathering of 'pass through' benefits so that the pass through exemption also applies where:

- an authorised representative of one licensee becomes an authorised representative of another licensee after date of application of the ban on conflicted remuneration;
- a representative (for example, an employee) of a financial services licensee becomes an authorised representative of the same licensee.

These changes are intended to allow advisers to move between licensees without losing the benefit of grandfathering.

In addition, a person that has a superannuation interest in 'growth' phase prior to 1 July 2014 and switches to pension within the same superannuation interest will not be taken to have made an acquisition of a new financial product. This will allow grandfathered benefits to continue to accrue where the client held the superannuation interests prior to 1 July 2014 and made the election to take a pension after this date.

5. Technical changes and clarification of interpretation

5.1 Volume-based shelf-space fees

Under the current law a platform operator is prohibited from receiving volume-based shelf-space fees from a funds manager. The existing law presumes that benefits that are wholly or partly dependent on the total number or value of the funds manager's financial products which relate to platform arrangements are volume based shelf-space fees. There are specific exemptions from the presumption where the benefit relates to scale efficiencies or is paid as a fee for services provided by the platform operator.

The New FOFA Reforms clarify that this ban is intended to capture benefits such as incentive payments between fund managers and platform operators for the preferential treatment of products. The current provisions relating to the volume-based shelf-space fees are amended to provide that a volume-based shelf-space fee is a benefit that, because of the nature of the benefit, or the circumstances in which it is given, could reasonably be expected to influence the platform operator to:

- increase the total number or value of the funds manager's financial products in which the platform operator is prepared to provide under the custodial arrangement; or
- give ***preferential treatment*** to the funds manager's financial products in providing the custodial arrangement.

A benefit will therefore only be a volume-based shelf-space fee if it influences the platform operator's behaviour, much in the same way that the ban on conflicted remuneration only applies to benefits that influence an adviser's behaviour. In addition:

- specific exemptions remain for a reasonable fee for services provided to the funds manager;
- the drafting of the exemption for scale of efficiencies is clarified to mean *a discount on an amount payable or a rebate of an amount paid, to the funds manager by the platform operator, that can reasonably be attributed to economies of scale gained because of the number or value of the funds manager's financial products in relation to which the platform operator provides custodial arrangements*;
- a new exemption from the ban will apply for fees that relate to a general insurance product or a life risk insurance product offered under the custodial arrangement.

5.2 Client paid exemption

There are various possible interpretations of the current wording of the CPE set out in section 963B(1)(d) of the Corporations Act:

- a narrow view that it only operates in circumstances where payments are made from client money or amounts held on behalf of the client;
- another view that it also operates in circumstances where payments are made from the amounts paid by (or on behalf of) the client into a product where the client has approved or authorised the payment;
- a wide view that the exemption allows amounts to be paid from the product provider's own resources where the client has approved or authorised the payment to the banker, at least where the payment could not be made without the consent of the client.
- At the time of writing this paper, a view (cf the narrow view mentioned above) has been circulating which may well be reflected in a subsequent draft of the Explanatory Memorandum or the legislation itself, to the effect that the client can only authorise a payment from monies to which he or she is beneficially entitled. This seems an unnecessarily narrow view as:
    - for client consent to be effective in the superannuation context, the client does not have a beneficial interest in his or her account balance except to the extent of an amount held which is an unrestricted non-preserved amount;

- the necessary lynchpin to client authorisation seems to be whether the authorisation by the client is a necessary prerequisite to the payer being able to make the payment;

- for certain types of financial products, such as an investment life policy, the client does not have a beneficial interest in the value of his or her policy (it is rather a chose in action) but it is suggested legally that the client should have the ability to give his or her consent to a payment from the value of his or her policy.

In the writer's view, the CPE is capable of a wider interpretation set out above on the following basis:

- section 52 of the Corporations Act provides that a reference to doing an act (such as giving a benefit) includes a reference to authorising the act to be done;

- the client has no entitlement to money held in a super account and so is only authorising the payment in this context;

- the Explanatory Memorandum to the FOFA Act which extends the operation of the CPE by virtue of the application of section 52 of the Corporations Act; and

- ASIC Regulatory Guide 246 which states that benefits given by the client may include benefits that have been authorised by the client and that ASIC will interpret a benefit as having been paid by the client where it is paid by the licensee at the direction, or with the clear consent, of the client. In ASIC's view, consent is 'clear' if it is genuine, express and specific.

However, there has nonetheless been some confusion in the industry in relation to the extent to which the CPE can be used.

The New FOFA Reforms insert a note to the definition of conflicted remuneration that 'giving a benefit includes a reference to causing or authorising it to be given' as per section 52 of the Corporations Act. This is intended to clarify that the CPE (section 963B(1)(d)) extends to a benefit given at the direction of the client or with the client's clear consent. However, the Draft Explanatory Memorandum provides that the mere fact that a client consents to a benefit being paid does not mean that the benefit is caused or authorised by the client. In the writer's view the position would be better dealt with by a change to the drafting of the legislation rather than simply by the use of an explanatory note which does not form part of the legislation.

5.3 Definition of intra-fund advice

The New FOFA Reforms inserts a note to define the term 'intra-fund advice' into section 960. The note provides that intra-fund advice is commonly used to describe financial product advice given by a trustee of a regulated superannuation fund to its members and links the commonly used term with the rules under section 99F of the SIS Act.

It is noted that the term "intra-fund advice" is not used in the Corporations Act.

5.4 Mixed benefits

Under the current law, certain benefits may not relate to more than one of the products or circumstances that are exempt from the ban on conflicted remuneration. For example, the exemptions relating to general insurance, life risk insurance and basic banking products under the current law provide that the benefit must 'solely' relate to one of those products only and cannot be given in respect of a combination of them. On this basis a benefit cannot be given if it relates to one or more exemptions contained in Division 4 of the Corporations Act. Although the current Corporations Regulations attempt to rectify this restriction, the proposed amendments are intended to clarify that a benefit will be exempt from the ban on conflicted remuneration to the extent that it relates to one or more of the products or circumstances described in sections 963B, 963C and 963D as well as circumstances which do not fall

within the definition of conflicted remuneration under section 963A. This means that one benefit may relate to several different exemptions.

It is noted that the Draft Regulations provide a further clarification that a benefit does not become conflicted remuneration purely because it is paid together with another benefit or it is a mixed benefit.

5.5 Wholesale/retail client distinction

The Draft Regulations introduce amendments that will enable a person to be treated as wholesale client for the purposes of Part 7.7A of the Corporations Act if they meet certain criteria as set out in the Corporations Act and the current Corporations Regulation.

6. Timing

The amendments in the Bill will apply from the day they are given Royal Assent. However, the Government has announced that time sensitive FOFA amendments will be dealt with through interim regulations and then locked into legislation. The interim regulations will be repealed once the legislative amendments have been passed, while those amendments best addressed via regulations will remain in place.

Following the consultation process, the Government anticipates that regulations will be made at the end of March 2014 and that a Bill will be introduced into Parliament in the 2014 autumn sitting period with passage scheduled for the winter sitting period.

In the meantime, ASIC indicated in a media release on 20 December 2013 that it will take a 'no action' position in relation to those matters that are the subject of legislative amendment. During the reform period until mid-2014 ASIC will take a facilitative approach to the new reforms.

7. Summary of the new changes against the current law

Table 1: This table provides a comparison of the current law against the proposed reforms.

Subject matter	Current law	New FOFA Reforms	Application date for New FOFA Reforms
'Opt-in' requirement	Advisers who have an ongoing fee arrangement with a retail client must obtain their client's agreement at least every two years to continue the ongoing fee arrangement, for new clients who enter into an ongoing fee arrangement from 1 July 2013.	Removing the opt-in requirements so that advisers no longer need to seek their client's agreement every two years. An 'opt-out' system will apply so that any ongoing fee arrangement continues to exist unless the arrangement is terminated by either the client or the adviser.	The removal of the 'opt-in' provisions will apply in relation to ongoing fee arrangements with renewal notice days that occur on or after the day after Royal Assent, or earlier if implemented through earlier

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			regulations.
Annual fee disclosure	Advisers who have an ongoing fee arrangement with a client must give all retail clients a fee disclosure statement which shows the fees paid by the client, the services the client received, and the services the client was entitled to receive, in the previous 12 months.	Removing the retrospective application of the fee disclosure requirement, so that advisers will not need to provide fee disclosure statements to clients who entered into a fee arrangement before the mandatory 1 July 2013 commencement date of FOFA.	The removal of the requirement to provide a fee disclosure statement to clients who entered into their ongoing fee arrangement before 1 July 2013 applies in relation to an ongoing fee arrangement for those disclosures days in respect of the arrangement that occur on or after the day after the Royal Assent, or earlier if implemented through earlier regulations.
Best interests duty	• Catch-all: In order to satisfy the best interests duty, providers must be able to prove that they have "taken any other step [in addition to the six preceding ones in the safe-harbour, section 961B(2)(a) to section 961B(2)(f)] that … would reasonably be regarded as being in the best interest of the client" (that is, the 'catch-all' provision). • An agent or employee of an ADI is currently not required to satisfy the steps in the safe harbour, subsections 961B(2)(d) to (g), when the subject matter of the advice sought by the client is solely in relation to a basic banking product or solely in relation to a general insurance product.	• Catch-all: Removing the catch-all provision (section 961B(2)(g)) so that advisers can be certain they have satisfied their obligations under the best interests duty. • An agent or employee of an ADI need not satisfy the safe harbour steps in sub-sections 961B(2)(d) to (f) in relation to personal advice on a basic banking or general insurance product when the subject matter sought by the client relates to a basic banking product, general insurance product, consumer credit insurance product, or a combination of these products.	The amendments will apply in relation to the provision of personal advice to retail clients on or after the commencement day being the day after the Royal Assent.

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Scaled advice	There is uncertainty on whether clients and advisers can agree on the scope of the advice to be provided.	Clients and advisers will be explicitly allowed to agree on the subject matter of advice to be provided.	The amendments will apply in relation to the provision of personal advice to retail clients on or after the commencement day being the day after the Royal Assent.
'Intra-fund' advice	Currently not addressed in the Corporations Act or Corporations Regulations.	A note clarifying the term 'intra-fund advice'. The note provides that intra-fund advice is commonly used to describe financial product advice given by a trustee of a regulated superannuation fund to its members and links the commonly used term with the rules under section 99F of the SIS Act.	To commence the day after Royal Assent.
Conflicted remuneration	In respect of conflicted remuneration, the legislation provides the following: • General advice: The ban on conflicted remuneration applies to benefits given to a licensee or a representative that could reasonably be expected to influence the financial product advice provided or the financial products recommended to a retail client (that is, includes both personal and general advice). • Life insurance inside super: Monetary benefits paid to licensees, or representatives, in relation to: ○ life risk insurance offered outside of superannuation are exempt from the ban on conflicted remuneration; ○ life risk insurance offered	Provisions relating to conflicted remuneration is amended as follows: • General advice: Benefits relating to the provision of general advice will be exempt from the ban on conflicted remuneration. • Life insurance inside super: Monetary benefits paid in relation to certain life risk insurance offerings inside superannuation will be exempt. Ban applies to commissions on risk (life) insurance products inside superannuation in relation to MySuper or in circumstances where no personal financial advice has been provided to the member regarding life insurance.	Generally to commence the day after Royal Assent unless implemented through earlier regulations (and provided the benefit is not a grandfathered).

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	inside of superannuation are exempt from the ban on conflicted except: in relation to group life risk insurance offered inside any type of superannuation fund; or individual life risk insurance offered inside a default superannuation fund. • Training exemption: A non-monetary benefit is exempt from the ban on conflicted remuneration if it relates to education and training that is relevant to the provision of financial product advice. • Basic banking exemption: A monetary or non-monetary benefit is exempt from the ban on conflicted remuneration if it is given to an agent or employee of an ADI and the benefit relates to a basic banking product. At the time of providing advice on the basic banking product, advice must not be provided on financial products other than a basic banking product. The Corporations Regulations allow access to the exemption where the agent or employee also provides financial product advice on a general insurance product. • Execution-only exemption: A monetary benefit is exempt from the ban on conflicted remuneration if it is given in relation to the issue or sale of a financial product (i.e. execution-only), and the licensee or representative has not provided financial product advice to the client in relation to the product, or products of that class, in the previous 12 months. • CPE: A benefit given by a retail	• Training exemption: Broadening the existing training exemption (section 963C(c)), that provides for training in relation to providing financial product advice as a permitted non-monetary benefit, to include other forms of education and training that are relevant to the operation of a financial services business, which includes the provision of financial product advice. • Basic banking exemption: Broadening the existing exemption for basic banking products to allow an agent or employee of an ADI to access the exemption if, at the time of providing advice on a basic banking product, the agent or employee also provides financial product advice on other simple, 'Tier 2' financial products. • Execution-only exemption: Introducing a causal link into the exemption so that benefits are permitted where no advice has been provided to the client by the individual or licensee receiving the benefit (as opposed to the licensee or authorised representative more broadly) in the previous 12 months. • CPE: A clarificatory note that a reference to giving a benefit includes a reference to causing or authorising it to be given. This means that the benefit may be paid directly by the client or by another party where the benefit is given at the direction of the client with the client's clear	

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	client to a licensee or representative is exempt from the ban on conflicted remuneration if it relates to the issue or sale of a financial product or financial product advice provided by the licensee or representative. • Balanced 'remuneration' structure: This is not legislated in the Corporations Act or Corporations Regulation. • Permissible revenue exemption: This is not legislated in the Corporations Act or Corporations Regulation. • Mixed benefits: The exemptions relating to general insurance, life risk insurance and basic banking products provide that the benefit must 'solely' relate to one of these products, meaning that a benefit cannot be given if it relates to one or more exemptions in Division 4 of the Corporations Act. This was rectified through the Corporations Regulations, however it is not reflected in the Corporations Act.	consent. • Balanced 'remuneration' structure: Amending the conflicted remuneration provisions to allow for the payment of benefits under 'balanced' remuneration structures. • Permissible revenue exemption: Exempting bonuses paid in relation to certain 'permissible revenue'. • Mixed benefits: Clarification of the operation of the mixed benefits provisions that a benefit will be exempt from the ban on conflicted remuneration to the extent that it relates to an exemption as well as circumstances which do not fall within the definition of conflicted remuneration. This means that one benefit may relate to several different exemptions.	
Volume-based shelf-space fees	Volume-based shelf-space fees paid by a funds manager to a platform operator are banned. No specific definition of a 'volume-based shelf-space fee' is provided. A benefit is presumed to be a volume-based shelf-space fee if it is based on the total number or value of the funds manager's products to which the custodial arrangement relates. Specific exemptions are provided for a reasonable fee for service and a discount or rebate which does not exceed the scale	Amending the drafting of the ban on volume-based shelf-space fees to clarify that incentive payments between fund managers and platform operators for preferential treatment of certain products on the platform "shelf" are banned.	Generally commence the day after Royal Assent unless implemented through earlier regulations (and provided the benefit is not a grandfathered).

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	efficiencies gained by the platform operator.		
Wholesale / retail client distinction	The application of the wholesale / retail client distinction does not currently extend to Part 7.7A of the Corporations Act.	Ensuring that the wholesale and retail client distinction that currently applies in other parts of the Corporations Act also applies in respect of the FOFA provisions.	From registration of the amended regulation.
Stamping fee exemption	The exemption does not apply to capital raising activities relating to certain types of entities whose primary purpose is to provide a financial investment.	Clarifying the application of the stamping fee exemption to capital raising activities and broadening its application to include investment entities.	From registration of the amended regulation.
Stockbroking related exemption	A monetary benefit is not conflicted remuneration where the benefit is a brokerage fee given to a provider who is a trading participant of a 'prescribed financial market' and the provider gives the benefit to a representative of the provider. ASX24 is not a market included in the 'prescribed financial market'.	Amending the application of the existing brokerage fee exemptions to include brokerage fees paid in relation to financial products on the ASX24 (formerly, the Sydney Futures Exchange).	From registration of the amended regulation.
Grandfathering	Broadly, the grandfathering arrangements provide that certain benefits given under arrangements (typically between product issuers and licensees) entered into prior to the application day of the ban on conflicted remuneration and that relate to clients who had an interest in the relevant platform or product prior to 1 July 2014 are not subject to the ban on conflicted remuneration.	Broadening the existing grandfathering provisions to allow advisers to move between licensees and to continue to access grandfathered benefits in certain circumstances, as well as certain other clarifications to the operation of grandfathering.	From registration of the amended regulation.