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Financial System Division
The Treasury
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Quality of Advice Review – Response to Issues Paper

We welcome the opportunity to respond to the issues paper published in March 2022.

Kit Legal is a specialist financial services law firm. We act for over 100 financial services firms around Australia, assisting them to comply with their regulatory obligations. Most of our clients are SMEs that hold their own AFSL.

In our experience, financial advisers want to comply with their obligations and have the best interests of their clients at the forefront of their activities. However, the regulatory framework is complex, layered and ambiguous, making compliance an overwhelming burden for many firms.

The complexity and ambiguity also doesn't serve consumers' interests and has negatively impacted both the quality and accessibility of advice. It's resulted in excessively long and inpenetrable disclosure documents. It's also created an environment in which advisers can, in some circumstances, act effectively as product salespeople, rather than as true financial advisers who are largely product agnostic.

Our attached submission responds only to those questions where we feel we can usefully contribute to the discussion.

We welcome any queries on our submission and otherwise look forward to reading the final report.

Kind regards

The team at Kit Legal
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Response to Quality of Advice Review – Issues Paper

3.1 Quality financial advice

1. What are the characteristics of quality advice for providers of advice?

We agree with the comment that quality advice can be hard to define and views may differ. However, we consider that quality advice will be advice that's in the best interests of the client and that delivers value aligned to the client's goals no matter who is measuring the advice.

In our experience, this central tenet is complicated from the provider's perspective by the tension between wanting to run an efficient advice business and acting in the client's best interests.

For example, it's more costly/less efficient for advisers if clients are on multiple platforms for ongoing investment advice, reporting and reconciliation purposes. This can mean that new clients are advised to consolidate their superannuation and/or investments onto the adviser's preferred platform. This is not necessarily in the client's best interests based on their goals and objectives.

Ultimately we don't believe providers will always be providing quality advice if they are tied to a particular product, especially if that product is an in-house product (e.g. an MDA/SMA). We discuss this issue further below in question 20.

2. What are the characteristics of quality advice for consumers?

In principle, quality advice is advice that's in the best interests of the client and that delivers value aligned to the client's goals.

Quality advice for consumers should also be assessed against practical measures, including:

- the advice is easy to understand;
- is communicated in a limited number of pages (1-2); and
- the value of the advice exceeds the cost of the advice.

3. Have previous regulatory changes improved the quality of advice (for example the best interests duty and the safe harbour (see section 4.2))?

The best interests duty, together with the ban on conflicted remuneration, have gone a long way towards aligning the client's interests and the adviser's interests.

We don't think repealing the safe harbour is necessary to keep these interests aligned, as discussed further below in question 43.

4. What are the factors the Review should consider in deciding whether a measure has increased the quality of advice?

The measures should be linked to how advice given in the best interests of the client will improve the client's financial position relative to their existing position and aligned to their goals/objectives.

This could be shown by including cashflow and asset and liabilities projections in the advice documents so the client can see clearly how their current situation compares to the proposed situation. The projections should factor in the adviser's fees and use reasonable assumptions so the client can see how much benefit is derived from implementing the advice, after all costs are taken into account.

3.3 Accessibility of financial advice

11. Could financial technology (fintech) reduce the cost of providing advice?

Yes, fintech could be used to reduce the cost of providing advice.

This question is often considered in the context of generating administrative efficiencies that can help lower the cost of advice.

Back office efficiency is important, but we think efficiencies should also be viewed more broadly. Fintech tools should be used to generate efficiencies that help build value for the client rather than merely improving process.

We are aware of at least one firm that has shown how fintech can be used to generate client value, rather than firm value. The firm uses algorithms to analyse investment performance across their client base to monitor whether all clients are receiving quality advice. Where the algorithm identifies outliers, this prompts the firm to query what the cause is – is it an advice issue or an adviser issue?

This approach helps the firm to limit the impact of human bias and control the parameters they set around providing quality advice.

See also our answer to question 40.

16. How could advice be more accessible?

We see the main pathways to improving accessibility as:

- simplifying disclosure in advice documents, by adopting a principles-based approach to disclosure, rather than prescribing content (see question 65);
- (as above) improving uptake of fintech solutions that enhance quality advice (i.e. that create client-centric efficiencies as well as firm-centric or process efficiencies);
- creating a regulatory environment that encourages digital advice solutions in appropriate circumstances (see question 40).

The current regulatory regime also creates complexity that indirectly impacts accessibility of advice. One example is the unnecessary complexity of the "providing entity" model, and drawing a distinction between licensee, representative and authorised representative.

4.1 Types of advice

General and personal advice

20. Is there a practical difference between financial advice and financial product advice and should they be treated in the same way by the regulatory framework?

We believe there should be a difference between financial advice and financial product advice and it should be made clear to clients which type of advice they're receiving.

In our view, financial product advice should be characterised as advice that is limited to the appropriateness of a particular product (or limited number of products) and how to invest in that particular product.

Financial advice on the other hand gives primacy to the consideration of appropriate financial strategies for the client in light of their personal circumstances and goals. This can be quite broad-ranging and include consideration of financial strategies that aren't linked to financial products and therefore fall outside the regulatory regime, including cashflow management and aged care considerations. Once the strategy is agreed, the advice may recommend appropriate products to achieve the strategy. As such, an APL can still be used. This aligns to some extent with the FSC proposal to amend the existing definition of 'personal advice' to cover advice that considers the personal circumstances of an individual consumer.

Some advisers provide what we'd call financial product advice, where clients believe they're receiving financial advice. This can be particularly evident where providers make the same or very similar recommendations to all clients and/or have an in-house product (e.g. SMA/MDA). In this situation, it appears that:

- a one-size-fits all approach is taken with recommendations (on the basis that only consumers who fit this model are taken on as clients);
- a high percentage of the firm's clients are recommended to invest in the in-house product; and/or
- in practice, there is little or no genuine consideration given to alternative strategies or products, other than as a compliance requirement.

22. What types of financial advice should be regulated and to what extent?

Three types of financial advice should be regulated.

Advice type	Level of regulation
General information (replacing general advice)	• 'General information' should cover factual information that does not take into account the client's personal circumstances. • A general information warning should be required to advise clients that their personal circumstances have not been considered. • No specific disclosure requirements.

Advice type	Level of regulation
Personal financial advice	• 'Personal financial advice' should cover financial advice that takes into account the client's personal circumstances and can include a broad range of strategies from cashflow to investment. • Best interests duty, including safe harbour, and code of ethics should apply. • Amended disclosure requirements. See question 65.
Personal product advice	• 'Personal product advice' should cover advice limited to recommending a particular product that takes into account the client's personal circumstances. • Best interests duty and code of ethics should apply, but the safe harbour principles would not make sense here. • Disclosure should include a clear statement that the advice has not considered any other products beyond those mentioned in the advice.

23. Should there be different categories of financial advice and financial product advice and if so for what purpose?

Yes, there should be different categories as above. The primary purpose is to clearly inform clients of the nature of the advice they're receiving.

24. How should the different categories of advice be labelled?

As above.

26. How should alternative advice providers, such as financial coaches or influencers, be regulated, if at all?

To the extent that financial coaches or influencers provide financial product advice, they will be caught by the existing regime. If a broader category of 'personal financial advice' is also introduced, this will expand the reach of regulation to include financial coaches and potentially some influencers. We don't think there's any need to introduce a separate regime for alternative advisers.

We do think ASIC should issue additional specific and practical guidance to assist alternative providers in what they can and can't do and say. In particular, ASIC should provide example scenarios of how 'factual information' can be provided rather than advice, as well as what's permitted in terms of 'mere referrals' and 'passing on pre-prepared information' in this space (Corporations Regulations 7.6.01(1)(e) and 7.1.31 respectively).

ASIC should also provide examples of key phrases that influencers can use. Many influencers don't have formal financial backgrounds so practical guidance and examples would assist them to do the right thing.

As a matter of accessibility, this approach recognises that people (especially younger people) get their information from a wide range of sources, including influencers. Early and accurate financial education has benefits not only for the individual, but also for society. This approach balances accessibility to quality information and regulation of advice.

Limited scope advice

32. Do you think that limited scope advice can be valuable for consumers?

Yes, we think that limited scope advice can be valuable for consumers as long as they understand the implications of limiting the scope. It can be difficult for advisers to ascertain and explain the implications of limited scope advice and give appropriate warnings to the consumer. In our view, there is hesitancy in doing this because of fear of missing an important issue that wasn't brought to the client's attention appropriately.

In addition, limited scope advice can be more problematic when there's an ongoing advice relationship as scope can change over time. This may be one of the reasons why advice firms take a more holistic view of advice initially and can then give more specific or limited scope advice at different intervals throughout the advice relationship. Limited scope advice is more appropriate where there is a once-off piece of advice rather than an ongoing relationship.

33. What legislative changes are necessary to facilitate the delivery of limited scope advice?

Changes are required to Standard 6 of the Code of Ethics in order to facilitate limited scope advice.

Standard 6 currently states *"You must take into account the broad effects arising from the client acting on your advice and actively consider the client's broader, long-term interests and likely circumstances*." While this is relevant for holistic advice, it's difficult to implement in giving limited scope advice and causes confusion for advisers in how far to go in reviewing client circumstances.

34. Other than uncertainty about legal obligations, are there other factors that might encourage financial advisers to provide comprehensive advice rather than limited scope advice?

In our view, advisers who want to do the right thing and ensure the client receives quality advice are very scared about missing something or being later found to have not brought something important to a client's attention.

On this basis, there's a view that it's better to be comprehensive in giving advice. In addition, while a client may seek limited scope advice initially, once they understand other areas that may benefit from advice (as part of the fact finding and scoping discussions), the initial scope can change.

Digital advice

35. Do you agree that digital advice can make financial advice more accessible and affordable?

Yes. We believe that digital advice can reach consumers who wouldn't otherwise see an adviser and that digital advice tools can help advisers reduce the cost of providing advice.

36. Are there any types of advice that might be better suited to digital advice than other types of advice, for example limited scope advice about specific topics?

For digital-only advice (where there's no adviser), limited scope or simple advice topics would be better suited such as debt consolidation, superannuation contributions, simple superannuation strategies or simple personal insurance advice. Digital advice with no adviser would not be suited to complex family group structures or some of the emotional elements that arise in giving holistic advice.

37. Are the risks for consumers different when they receive digital advice and when they receive it from a financial adviser?

The only risk that we consider to be different is where a systemic issue in an algorithm impacts many consumers. This can occur with financial advice given by a financial adviser (for instance fee errors or template errors) but is less likely and may have less of an impact as far as consumers impacted.

However, all other risks we believe are very similar.

38. Should different forms of advice be regulated differently, e.g. advice provided by a digital advice tool from advice provided by a financial adviser?

We support a technology-neutral approach to regulation and don't believe that the method of providing the advice should be regulated differently.

39. Are you concerned that the quality of advice might be compromised by digital advice?

No. In fact, when used well digital advice can result in quality advice.

The most important thing for a consumer to understand when receiving digital advice is the biaises and assumptions that may be built into algorithms and any conflicts of interest that exist. However, this is the same for receiving financial advice from a financial adviser. Financial advisers will have their own biaises or investment philosophies that will drive the advice they provide.

40. Are any changes to the regulatory framework necessary to facilitate digital advice?

In our view, the largest barrier to digital advice (and in fact many digital tools and automation that could be used in financial advice businesses) is a standard and open data set used across investment platforms and industry participants.

Access to standard and complete data seems to be the biggest issue preventing innovation in this industry.

A common standard for investment and fee data would mean that software systems could pull data more easily rather than having multiple manual inputs and variables.

In addition to driving digital advice, this would also enable the development of digital tools for use by advice firms and also assist with automation efforts, all driving down the cost of advice.

41. If technology is part of the solution to making advice more accessible, who should be responsible for the advice provided (for example, an AFS licensee)?

The advice provided by digital advice tools should be the responsibility of the AFS licensee who is the operator of the tool.

Where an advice tool is used by an adviser to complement or supplement advice given to their clients, then the adviser would be responsible for the advice given to the client.

42. In what ways can digital advice complement human-provided advice and when should it be a substitute?

Digital advice can complement many aspects of human-provided advice and could be used to drive better and more consistent outcomes for clients. Both individual advisers and investment committees could use these types of tools to monitor portfolios, identify outliers in terms of returns etc.

For clients not wanting an ongoing relationship with an adviser, digital advice could be a substitute for more simple advice or more simple structures. We think it can be challenging to use digital advice with no human-provided advice for more complex family structures.

4.2 Best interests and related obligations

43. Do you consider that the statutory safe harbour for the best interests duty provides any benefit to consumers or advisers and would there be any prejudice to either of them if it was removed?

Yes, the safe harbour does provide benefit to consumers and to advisers because it provides an indication of what best interests looks like in practice. It's helpful in shaping what steps an adviser should take to give advice in the client's best interests.

We do recognise that the current drafting of the safe harbour has encouraged a tick-box approach. We suggest the section could be redrafted to express the safe harbour as a set of considerations in line with a principles-based approach to regulation. The requirement to 'prove' each step has been taken should also be deleted. These changes would introduce an element of professional judgment on the part of the adviser to take and record the appropriate steps to meet the duty.

46. To what extent can the best interests obligations (including the best interests duty, appropriate advice obligation and the conflicts priority rule) be streamlined to remove duplication?

Section 961B(2)(g) is vague and should be removed.

The appropriate advice obligation should be removed as only advice that is appropriate should be considered to be in the best interests of the client.

47. Do you consider that financial advisers should be required to consider the target market determination for a financial product before providing personal advice about the product?

Advisers providing personal advice shouldn't have to consider the TMD. If they're complying with the best interests duty, then they're already taking into account the considerations covered by the TMD.

The current hybrid approach of excluding personal advice from the requirement to consider the TMD but then requiring advisers to consider the TMD anyway as part of the best interests duty does not provide additional value or protection for the client.

We suggest the only obligation on advisers providing personal advice is that they pass on product-related complaints to the issuer of the product.

The requirement to consider the TMD makes more sense for execution-only and general advice services.

4.3 Conflicted remuneration

48. To what extent has the ban on conflicted remuneration assisted in aligning adviser and consumer interests?

In our view the ban on conflicted remuneration has gone a long way in aligning adviser and consumer interests. It has highlighted the importance of removing conflicts of interest that may influence the advice provided.

49. Has the ban contributed towards improving the quality of advice?

Yes.

51. What would be the implications for consumers if the exemptions from the ban on conflicted remuneration were removed, including on the quality of financial advice and the affordability and accessibility of advice? Please indicate which exemption you are referring to in providing your feedback.

We're not in a position to comment on the financial impact on firms of removing these exemptions.

The only exemption that we see from time-to-time used in a way that we do not believe upholds the intention of the law is para 963B(1)(d) and regulation 7.7A.12EA. It may be useful to have this exemption limited to personal advice provided to the client to capture the intention that it covers FUM-based fees charged for ongoing personal advice only.

4.4 Charging arrangements

57. To what extent can the requirements around the ongoing fee arrangements be streamlined, simplified or made more principles-based to reduce compliance costs?

The intention of the fee disclosure regime is for consumers to understand whether they received the services they paid for so they can make an informed decision in electing to renew their ongoing fee arrangement.

However, a number of participants are avoiding this disclosure by ensuring the contract term with the consumer is for no more than 12 months (even though for all practical purposes, the services provided and fees charged are ongoing in nature). This means that the current disclosure regime is not working, as it is largely avoided.

For advice firms wanting to do the right thing, fee disclosure is a frustrating and costly process due to lack of consistent fee data out of multiple platforms and superannuation funds. It's impossible to manage anniversary dates under the new regime and the inconsistent dates for fee consents given the duplication between adviser-obtained consents and platform consents.

Ongoing Fee Arrangements and Fee Disclosure Statements

Given that fee disclosure is largely ignored at present, our view is that the FDS requirement should be removed.

The legislation should require all firms to have a written agreement with the client which clearly specifies what services will be delivered and the fee that will be charged.

Annual Consents

The primary issue identified in the Royal Commission was hidden fees being charged without consumers' active knowledge. This isn't an issue where a client pays fees after receiving an invoice or where fees are debited via direct debit from a deposit product.

In our view, on this basis, fee consent requirements should remain for fees debited from superannuation or platform accounts. The account provider in this situation should provide a statement of fees paid from the account during the last 12 months and obtain consent to continue to pay fees for the following 12-month period. We agree with keeping the current buffer of 150 days before fees are turned off if consent isn't obtained.

58. How could these documents be improved for consumers?

As above, there should be one fee consent signed by the client each year where fees are debited from superannuation or platform accounts. Apart from this, services provided and fees charged should be subject to the contract between the adviser/firm and client.

59. Are there other ways that could more effectively provide accountability and transparency around ongoing fee arrangements and protect consumers from being charged a fee for no service?

Rather than having to provide a FDS, there should be a legislative provision to the effect that if services contractually promised to the client are not provided to the client during the relevant period, the adviser/firm must notify the client about this with reasons as to why. Instead of getting a generic FDS, this would highlight specific information about services not provided). Failure to do this could result in termination of the existing ongoing fee arrangement and a requirement to refund fees.

4.5 Disclosure documents

63. How successful have SOAs been in addressing information asymmetry?

We don't think SOAs have been very successful in addressing information asymmetry.

As part of our practice, we review many SOAs. In the majority of cases they're very hard to understand. They're often extremely long (> 40 pages) and filled with template information that isn't tailored to the individual client's circumstances.

When it comes to financial information, more information does not automatically benefit the client, yet this appears to be the way the SOA addresses information asymmetry.

65. To what extent can the content requirements for SOAs and ROAs be streamlined, simplified or made more principles-based to reduce compliance costs while still ensuring that consumers have the information they need to make an informed decision?

Advice documents should still be required for personal financial advice, but they should short, highly-tailored documents.

We'd suggest a principles-based approach which requires the advice document to answer the following questions:

- **Goals:** What are the client's goals and objectives?
- **Strategy:** What is the recommended strategy for achieving these specific goals?
- **Implementation:** How can this strategy be brought to life? This may include a discussion of appropriate products or classes of product.
- **Value:** How does this strategy and implementation deliver value for the client? This should include consideration of how the advice will improve the client's financial position, taking into account all costs (including advice fees) for the advice.

66. To what extent is the length of the disclosure documents driven by regulatory requirements or existing practices and attitudes towards risk and compliance adopted within industry?

The length of SOAs has been exacerbated by the perceived regulatory requirement to detail every consideration and/or risk related to the financial products recommended.

The result is that much of the information included in SOAs is templated, rather than tailored to the client's circumstances and their goals/objectives. Counterintuitively, more information often results in less understanding.

67. How could the regulatory regime be amended to facilitate the delivery of disclosure documents that are more engaging for consumers?

The key challenge to address here is the length of the advice document which could be dealt with as above.

We also see a role for fintech here, which could enable clients to control the level of detail they require. For example, the advice document could be backed by modelling tools which the client could engage with as they require e.g. to generates fees comparisons.

69. Has recent guidance assisted advisers in understanding where they are able to use ROAs rather than SOAs, and has this led to a greater provision of this simpler form of disclosure?

We continue to receive many enquiries from clients asking whether an SOA or an ROA is required in a particular set of circumstances. This suggests that the guidance hasn't been of great assistance in practice. In addition, some of the examples given by ASIC in relation to what constitutes a change of circumstances are very conservative, such as the example of change in salary meaning that with ordinary increases in salary, a ROA would not be able to be used.

4.6 Accountants providing financial advice

71. Should accountants be able to provide financial advice on superannuation products outside of the existing AFSL regime and without needing to meet the education requirements imposed on other professionals wanting to provide financial advice? If so, why?

Accountants providing advice on superannuation should be required to be licensed and have the same education requirements. However, the exam should be tailored to the specific authorisations that limited licensees can provide rather than covering all financial product topics.

72. If an exemption was granted, what range of topics should accountants be able to provide advice on? How can consumers be protected?

As above.

74. Is the limited AFS licence working as intended? What changes to the limited licence could be made to make it more accessible to accountants wanting to provide financial advice?

The limited AFS licence has not worked as intended. Many limited AFS licensees have handed back their AFSL because of their advisers having to sit an exam that was not tailored to them at all and the ongoing cost of managing an AFSL when they did not provide a significant volume of advice.

In addition, there is a lot of frustration that many accounting firms were/are providing unlicensed advice with no action by ASIC at all. Unlicensed accounting firms provide the same service very cheaply because they are not preparing Statements of Advice or Records of Advice.

75. Are there other barriers to accountants providing financial advice about SMSFs, apart from the limited AFSL regime?

As above.

4.7 Consent arrangements for wholesale client and sophisticated investor classification

76. Should there be a requirement for a client to agree with the adviser in writing to being classified as a wholesale client?

A requirement to consent to being classified as a wholesale client could be adopted for financial advisers. However, we believe this could be more problematic for wholesale product issuers and the interaction between adviser and product issuer must be thought through carefully to avoid the situation we have at the moment with adviser and platform fee consents.

If a consent requirement is imposed, we recommend that there is standard (simple) wording for the consent to avoid firms thinking they need to write pages of disclaimers to cover all bases in obtaining consent.

77. Are any changes necessary to the regulatory framework to ensure consumers understand the consequences of being a sophisticated investor or wholesale client?

As above, this could be built into standard consent wording.

78. Should there be a requirement for a client to be informed by the adviser if they are being classified as a wholesale client and be given an explanation that this means the protections for retail clients will not apply?

As above, this could be built into standard consent wording.

5.1 ASIC

81. Have ASIC's recent actions in response to consultation (CP 332), including the new financial advice hub webpage and example SOAs and ROAs, assisted licensees and advisers to provide good quality and affordable advice?

These actions go some way to assist. However, information on ASIC's website is still difficult to find.

Many firms have significant inefficiencies in dealing with ASIC's systems in general given there are multiple portals for different notification requirements. It's very easy to miss things or put in the wrong information. They're not intuitive to follow.

82. Has licensee supervision and monitoring of advisers improved since the Financial Services Royal Commission?

Yes. Licensees are taking this seriously and investing in how to supervise and monitor advice provided.

83. What further actions could ASIC, licensees or professional associations take to improve the quality, accessibility or affordability of financial advice?

ASIC could be more available for discussion/consulation about topics or further clarification of guidance. We have attempted to do so on a number of topics and it is very difficult to interact with ASIC.

End submission