EXPLANATORY STATEMENT

Select Legislative Instrument No. 102, 2014

Issued by authority of the Treasurer

Corporations Act 2001

Corporations Amendment (Streamlining Future of Financial Advice) Regulation 2014

Subsection 1364(1) of the *Corporations Act 2001* (the Act) provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed, for carrying out or giving effect to the Act.

The *Corporations Amendment (Streamlining Future of Financial Advice) Regulation 2014* (the Regulation) makes a number of amendments to the *Corporations Regulations 2001* (the Principal Regulations). The amendments relate to Part 7.7A of the Act: the Future of Financial Advice (FOFA) provisions.

As part of its 2013 election campaign, the Government committed to reduce compliance costs for small businesses, financial advisers, and the broader financial services industry, whilst maintaining the quality of advice for consumers who access financial advice.

The Regulation makes the following changes:

- broadening the circumstances when the grandfathering arrangements for the ban on conflicted remuneration apply;
- clarifying that benefits can be paid under a balanced scorecard arrangement;
- clarifying that bonuses paid in relation to 'permissible revenue' are not conflicted remuneration;
- clarifying the application of the stamping fee provision to capital raising activities and broadening its application to include investment entities;
- amending the application of the existing brokerage fee provisions to include brokerage fees paid in relation to financial products traded on the ASX24;
- ensuring that the wholesale and retail client distinction that currently applies in other parts of the Act also applies in respect of the FOFA provisions; and
- clarifying the operation of the 'mixed benefits' provisions.

Details of these changes in the Regulation are set out in Attachment A.

The Government has also announced that time sensitive FOFA amendments will be dealt with through regulations and then put into legislation. This approach provides

certainty to industry and allows industry to benefit from the cost savings of the changes as soon as possible.

To the extent possible under the primary legislation, the Regulation makes these interim changes until the Corporations Amendment (Streamlining of Future of Advice) Bill 2014 passes the Australian Parliament and receives Royal Assent.

The Regulation makes the following changes:

- removing the need for clients to renew their ongoing fee arrangement with their adviser every two years (also known as the 'opt-in' requirement); this change will apply from the time the Regulation commences until 31 December 2015;

- removing the requirement to provide an annual fee disclosure statement to clients in ongoing fee arrangements prior to 1 July 2013; this change will apply from the time the Regulation commences until 31 December 2015;

- removing the 'catch-all' provision from the list of steps an advice provider may take to satisfy the best interests obligation, and facilitating scaled advice; this change will apply from the time the Regulation commences until 31 December 2015;

- clarifying the treatment of ‘intra-fund advice’; and

- amending the application of the ban on conflicted remuneration including:

  – providing that benefits relating to general advice are not conflicted, subject to certain conditions;

  – amending the execution-only services provision;

  – clarifying the application of the existing client-pays provision;

  – broadening the training and education provision; and

  – broadening the basic banking products provision.

The interim changes will be repealed (to the extent appropriate) following the commencement of the Corporations Amendment (Streamlining of Future of Advice) Bill 2014.

Details of the interim changes in the Regulation are set out in Attachment B.

A draft of the Regulation was published on the Future of Financial Advice website on 29 January 2014 for a three-week consultation period. A total of 57 formal submissions (including 8 confidential submissions) were received from a wide range of stakeholders in the financial services sector, including the Australian Bankers’ Association, the Association of Financial Advisers, Australian Financial Markets Association, Choice, the Financial Planners’ Association, the Financial Services Council, Industry Super Australia and the Law Council of Australia. Further targeted consultation was undertaken following the referral of the Corporations

Amendment (Streamlining Future of Financial Advice) Bill 2014 to the Senate Economics Committee.

The Senate Economics Committee released its report on 16 June 2014. The Regulation is consistent with the recommendations from that report.

Financial advisers and industry associations were broadly supportive of the draft Regulation with consumer groups opposing the changes. A wide range of views were canvassed ranging from requests to make technical changes, to broadening the scope of the changes, to not making any changes. The Government considered these views in preparing this Regulation. For example, some submissions raised concern that the proposal to provide that all benefits relating to general advice are not conflicted remuneration was too broad and would produce adverse outcomes for consumers. In response, the Government decided to limit this exemption to specific circumstances.

A Regulation Impact Statement is at Attachment C.

The Regulation is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The *Corporations Act 2001* does not specify any conditions that need to be satisfied before the power to make the Regulation may be exercised.

A Statement of Compatibility with Human Rights is at Attachment D.

This Regulation commences on 1 July 2014.

Objectives of Government action

In its pre-election *Policy to Boost Productivity and Reduce Regulation*, the Coalition committed to amend FOFA to: "reduce compliance costs for small business financial advisers and consumers who access financial advice[44]". In particular, it indicated that it would: "implement all 16 recommendations made as part of the Parliamentary Joint Committee inquiry into FOFA[45]".

Since the election, the Assistant Treasurer has, in a number of speeches, re-affirmed the Government's commitment to: "reducing the regulatory overreach of FOFA[46]".

The objective of Government action is threefold:

1) Remove the unnecessary burdens imposed on the financial advice industry from FOFA measures that went beyond the recommendations of the Ripoll Inquiry;

2) Properly implement the finding of the Ripoll Inquiry so as to reduce regulatory overreach whilst maintaining the important consumer protection measures introduced by FOFA; and

3) Address other technical and consequential concerns raised by industry.

A summary of the key proposed changes is presented in table 2. These are detailed further in the "impact of changes" section later in this document.

Table 2: Summary of changes to FOFA

FOFA component	Concern	Change
Best interests duty	The best interests duty, as currently drafted, has created significant uncertainty amongst advisers. Many industry stakeholders have argued that this uncertainty is ongoing and needs to be addressed by regulatory change. These stakeholders argue that the open-ended nature of the duty leaves advisers uncertain on how to satisfy their duty. They also expressed concern that advisers are vulnerable to legal action because adviser's obligations under the duty is not well defined nor well understood.	Government action will remove the open-ended nature of the best interests duty. Whilst the Ripoll Inquiry recommended imposing a fiduciary duty on advisers, it did not recommend it to be an open-ended obligation.
Scaled advice	Scaled advice (a form of targeted advice that is limited in scope, and is typically much cheaper than full, holistic advice), was supposed to have been accommodated	Government action will facilitate the provision of scaled advice, whilst ensuring advice remains appropriate to the

[44] The Coalition's Policy to Boost Productivity and Reduce Regulation, July 2013, p26.
[45] The Coalition's Policy to Boost Productivity and Reduce Regulation, July 2013, p26.
[46] Assistant Treasurer, Keynote Address to the 2014 Insurance Council of Australia Regulatory Update Seminar, 28 February 2014, available from: http://axs.ministers.treasury.gov.au/speech/008-2014/.

FOFA component	Concern	Change
	by the best interests duty. However, many advisers have indicated that they are not confident that they can legally provide this form of advice. This uncertainty has resulted in advisers spending more time and money on activities than otherwise necessary, such as understanding their legal obligations and documenting compliance with the best interests duty.	client. This action will properly implement the policy intent of the Ripoll Inquiry.
Fee disclosure statements	Fee disclosure statements are currently required to be provided to all clients, including those in ongoing fee arrangements prior to the introduction of FOFA on 1 July 2013, and were designed to increase the engagement of clients and improve transparency in the industry. According to industry stakeholders, providing fee disclosure statements to pre-1 July 2013 clients is difficult and expensive: many of these clients are on old legacy systems, predating the FOFA changes; as such, significant manual work is required to prepare statements for these clients. By contrast, as post-1 July 2013 clients are on newer, FOFA compliant systems, it is—comparatively speaking—much cheaper and efficient to produce fee disclosure statements for these clients. In the exposure draft of the original FOFA legislation, fee disclosure statements were only intended for post-1 July 2013 clients.	Government action will remove the requirement for fee disclosure statements to pre-1 July 2013 clients, but keep the requirement for post-1 July 2013 clients. The requirement to provide fee disclosure statements was not a recommendation from the Ripoll Inquiry.
Opt-in provisions	The opt-in requirement was introduced to increase client engagement. However, many industry stakeholders have argued that the opt-in notices do not offer substantial benefits to consumers; particularly as consumers already have the ability to opt-out of their arrangements. Many stakeholders have also indicated that, whilst the opt-in provisions are trying to institute a behavioural shift in the way clients interact with advisers, the changes required are too great for the financial	Government action will remove the opt-in requirement. Opt-in was not a recommendation from the Ripoll Inquiry.

FOFA component	Concern	Change
	advice industry to bear alone; rather, any changes in consumer engagement should be part of a broader strategy.	

Options that may achieve the objectives

This regulation impact statement (RIS) assesses the impacts of the Government's proposed amendments based on its election commitment; it does not explore any other options (in accordance with the Office of Best Practice Regulation's (OBPR) guidelines).

Whilst the Government's election commitment was to implement the 16 recommendations of the Dissenting Report, a number of the recommendations are no longer applicable as changes have already been made to FOFA that achieve the objectives sought, or the recommendations are no longer relevant due to the passage of time.

As such, this RIS considers the impact of a package of amendments to FOFA, including all of the (still relevant) Dissenting Report recommendations, as well as some additional amendments to address industry concerns.

Impact analysis

Overview of impact on industry and consumers

The proposed amendments to FOFA seek to navigate the fine line between ensuring that unnecessary and burdensome regulations that drive up the cost of business are removed, whilst ensuring that the consumer protections of FOFA are maintained.

The proposed amendments to FOFA are deregulatory and will reduce the compliance burden on the financial advice industry. Feedback from consultations and submissions on the draft amendments varied, and ranged from a complete rejection that any changes need to be made to FOFA, through to wholesale support.

Many industry stakeholders indicated that the proposed amendments will result in a more practical framework for financial planners and their clients. These stakeholders have argued that the changes will: provide clarity to industry, more closely align FOFA with the intentions of the Ripoll Inquiry, and deliver significant cost savings that will ultimately benefit consumers.

Consumer groups—and some industry stakeholders—are far less enthused. Most of the submissions have argued that the proposed package of amendments go too far in winding back the consumer protections introduced by FOFA. In particular, some stakeholders expressed concern that a number of proposed amendments, including the changes to the best interests duty, the removal of opt-in provisions, and exempting general advice from the definition of conflicted remuneration, will leave consumers vulnerable to poor quality advice by reducing the standard of advice provided. Furthermore, it is suggested that the amendments could reduce the level of trust and confidence in the financial advice industry, all of which runs contrary to the recommendations of both FOFA—as introduced by the former Government—and the Ripoll Inquiry.

A more detailed analysis of the benefits and costs of each of the amendments is presented below.