

Future of Financial Advice (FOFA) reforms

FOFA- What does it mean?

The driver for Future of Financial Advice (FOFA) reform was a combination of the fallout from the GFC and in particular, financial advice disasters such as "the one size fits all" type model.

While disclosure remains a key plank of FOFA with the introduction of fee disclosure statements and renewal notices, the key thrust of the best interests duty and ban on conflicted remuneration is mandating the manner in which conflicts of interest are to be managed.

These changes are brought about by inserting, amongst other things, Part 7.7A by means of two Acts of Parliament titled the *Corporations Amendment (Future of Financial Advice) Act 2012* and the *Corporations Amendment (Further Future of Financial Advice Measures) Act 2012*. In addition, there have been, regulations released which have added further detail to the legislation.

What are the key elements of FOFA?

There are four big ticket items. These are:

1. The best interests duty obligation imposed on the provider of personal financial product advice to retail clients.
2. A ban on conflicted remuneration being monetary and non-monetary benefits given to a licensee or representative who provides financial product advice (personal and general) to retail clients which could reasonably be expected to influence the choice of financial product recommended or the financial advice given.
3. On-going fee arrangements requiring the provision of fee disclosure statements and renewal notices to retail clients receiving personal advice.
4. An increase in ASIC's powers - this occurs in two ways. The first is the change in wording from "will" to "is likely to" (eg ASIC may ban a person if "ASIC has reason to believe that the person is likely to contravene a financial services law"). The second is the extension of the civil penalty regime to licensees and authorised representatives for a range of contraventions of the FOFA provisions.

When does all this start?

For most businesses, the commencement date will be 1 July 2013.

What are some of the new terms?

There will be a range of new terms that need to be understood.

- civil penalties - FOFA is a civil penalty world; not criminal. This may seem like a good thing which in a sense it is. But because the standard of proof is less (no longer guilt beyond reasonable doubt), it is not unreasonable to expect ASIC to be active in bringing civil penalty proceedings against licensees and authorised representatives for breaches of the best interest duties, failure to provide disclosure statements, accepting conflicted remuneration, etc. While not criminal, the penalties can still be hefty - up to \$1 million for a company licensee or corporate authorised representative!
- fee disclosure statement
- renewal notice
- on-going fee arrangement
- fee recipient
- disclosure day
- responsible licensee; and so on.

Will the way that advice is given change?

Yes and no. What is different? Section 945A has been replaced with an obligation that the advice must be in the best interests of the client. The new section 961B replaces the (a) and (b) of 945A(1) with a series of steps which, if discharged, satisfies the best interests obligation.

While advice providers will need to consider strategies to “prove” that the “safe harbour” steps have been addressed, the real challenge in these steps is left to the last step which is *"take any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interests of the client, given the client's relevant circumstances."*

The requirement to act in the best interests of the client takes it beyond the requirement that we have been used to; namely, that the advice must be appropriate to the client. This is because best interests is coming from a higher ethical stance - something approaching a fiduciary duty. It places a responsibility on the advice provider to be totally upfront with the client and to place the client's interests first.

What has not changed? Section 961G requires that the advice must still be appropriate as is the case now under section 945A.

The definition of financial product advice which we know stays the same as does personal advice and general advice.

Also, the importance of determining the scope of the advice remains the linchpin of the advice process. FOFA describes this as "the subject matter of the advice" which must be ascertained after identifying the client's financial circumstances, needs and objectives. This does not require a full fact find at this stage. A searching, detailed and targeted fact find comes later when the adviser is required to ascertain "the client's relevant circumstances".

The warnings in relation to incomplete and inaccurate information from the client remain.

What should you be doing now?

1. Reviewing your advice processes and documentation to specifically address the changes brought about by the best interests obligation. This review should also consider the provision of practical training workshops to ensure that your advisers understand the requirements.
2. How you are going to address the fee disclosure statement requirement which applies to existing retail clients as well as new retail clients post 1 July 2013.

There are two main challenges with meeting the fee disclosure statement obligation. These are:

- a. What needs to go into the FDS?
- b. When do I need to provide the FDS to the client?

ASIC has provided good guidance in relation to these issues which can be found in RG 245.

3. You will also have to look at your remuneration structures and determine what forms of remuneration will be considered to be conflicted remuneration. Remember the test is “could reasonably be expected to influence” and not a subjective “does this actually influence me?” test. Also the prohibition applies to remuneration given to the provider of financial product advice (ie both personal and general advice).

Numerous issues have arisen such as which benefits are exempt from the ban, how the grandfathering arrangements apply and what happens when benefits are passed on from the licensee to representatives which are not conflicted remuneration when received by the licensee but might be when paid by the licensee and received by the representative.

ASIC has provided guidance by way of RG246.

4. The risk management framework may be visited regularly but many licensees don't. It is important to revisit it and using the framework to risk manage FOFA? This doesn't just mean identify the adverse outcomes that FOFA might present to your business. There are also opportunities that FOFA might throw up which you don't want to miss. The risk of missing such opportunities is a risk that should be managed.

Finally, the ASIC website has a dedicated FOFA site and your industry association will be providing valuable resources to their members. Licensees and compliance professionals will also be providing regular updates on developments.