3 November 2016

Ms Tanja Cvijanovic
First Assistant Secretary
Regulatory Reform Division
Department of the Prime Minister and Cabinet

Dear Ms Cvijanovic

REFORMS TO RAISE THE PROFESSIONAL STANDARDS OF FINANCIAL ADVISERS - REGULATION IMPACT STATEMENT (RIS)

This letter certifies that the *Parliamentary Joint Committee on Corporations and Financial Services, Inquiry into proposals to lift the professional, ethical and education standards in the financial services industry* (PJC Report) and the Financial System Inquiry Final Report (Murray Inquiry), have involved a process and level of analysis equivalent to a final assessment Regulatory Impact Statement (RIS), as set out in the Australian Government Guide to Regulation March 2014 (the Guide). The reports will support the introduction of the Corporations Amendment (Professional Standards of Financial Advisers) Bill 2016 (the Bill) in early 2016.

Overview

In recent years, numerous cases of inappropriate financial advice have decreased consumers' confidence in the financial services industry. This lack of trust has become a barrier to consumers seeking financial advice. The financial services industry, consumer groups, the Government, and the Australian Securities and Investments Commission (ASIC) have raised concerns about the existing education and training requirements applicable to financial advisers.

The Bill makes amendments to the Corporations Act 2001 (Corporations Act) to raise the education, training and ethical standards of financial advisers by requiring relevant providers to hold a degree, undertake a professional year, pass an exam, undertake continuous professional development and comply with a Code of Ethics.

Independent Reviews

The two reports used to independently certify the regulatory impacts of these reforms examine the current professional standards in the financial service industry and make recommendations for improvements to these standards.

The Parliamentary Joint Committee on Corporations and Financial Services (the PJC) resolved on 14 July 2014, to inquire into proposals to lift the professional, ethical and education standards in the financial services industry. Following stakeholder consultation, on 19 December 2014, the PJC reported on ways to lift professional standards in the financial services industry.

The Murray Inquiry made recommendations on lifting the competency of financial advisers to improve the quality of financial advice. The Inquiry was established by the former Treasurer in November 2013, with Mr David Murray AO appointed as the Inquiry Chair. Following consultation, the Inquiry delivered its final report to the Government in November 2014, and this was publicly released by the former Treasurer on 7 December 2014. The Government responded to the Murray Inquiry on 20 October 2015, following consultation with stakeholders that included more than 180 written submissions as well as extensive stakeholder engagement through meetings and roundtables.

Addressing the RIS questions

Treasury considers that in meeting its statutory obligations relating to the review, the matters that must be covered in a final assessment RIS have been addressed through the PJC Report and the Murray Inquiry, as well as through substantive consultation with key stakeholders. The PJC Report can be found at: http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/Financial_Adviser_Qualifications; and the Murray Inquiry at: http://fsi.gov.au/publications/final-report/.

Question 1 and 2 – the problem and why government action is needed

Currently, the Corporations Act imposes a general obligation on a licensee to ensure that its representatives are adequately trained and competent to provide financial services. ASIC's Regulatory Guide 146: Licensing: Training of financial product advisers (RG 146) sets out the minimum knowledge, skill and education level standards for financial advisers and provides information on how advisers can meet these standards.

Various inquiries, including the Murray Inquiry and the PJC Report have identified that the existing professional standards for financial advisers are too low and do not ensure that all financial advisers have the necessary skills to provide high quality advice to consumers. These reviews recognise that the current regulatory framework has acted as a barrier to generating consumer confidence in the industry, has discouraged professionalisation and has not encouraged industry to take a greater lead in setting standards.

In addition, the current educational framework for financial advisers does not include specific requirements for monitoring and supervising a new adviser (or an adviser new to a particular specialisation) to enable the adviser to develop the requisite minimum skills to provide sound financial advice.

There have been many regulatory interventions by the Australian Government in recent years to help improve trust and confidence in the financial services industry, and the quality of information for which consumers of financial services have access. Government intervention is justified because of the significant costs to individuals, the community and/or taxpayers that can result from poor information on the benefits and risks of financial services, including complex financial advice provided to retail clients.

Question 3 and 4 – the policy options and the costs and benefits of each option

The PJC Report and Murray Inquiry consider and discuss a range of policy options to raise the standards of financial advisers in Australia. The benefits of reform are considered, with a preference for a co-regulatory approach between Government and industry to enhance professional standards in the financial advice industry.

The current system of professional standards for financial advisers, as outlined in the PJC Report, provides minimum standards for financial advisers to meet. However, licensees and professional associations retain discretion to set higher education standards for their advisers.

The Murray Inquiry recommended that the minimum standards for financial advisers providing advice to retail clients on complex products should include; a relevant tertiary degree; competence in specialised areas, where relevant; ongoing professional development, including technical skills, relationship skill compliance and ethical requirements; and the relevant transitional arrangements to allow the opportunity for financial advisers to upskill, including recognition of professional experience. The Murray Inquiry also noted that a national exam for advisers could be considered if issues with adviser competency persist and indicated enhancements to the register of advisers were needed.

The intention of these recommendations was to increase the likelihood of consumers receiving customer-focused quality advice, promote confident and informed consumer use of financial advisory services, and facilitate consumer access to information about financial advisers' experience and qualifications to improve transparency and competition.

The Murray Inquiry recommendations have the potential to reduce the levels of poor advice being given to retail clients. The requirement to hold a tertiary degree or equivalent would impose costs on financial advisers and licensees, some of which may be passed onto consumers. Licensees would also face costs in ensuring their financial advisers have met the relevant standards, including having undertaken a professional year. These costs could be mitigated to some extent by the various cost effective market developments that are emerging, such as scaled or limited advice and using technology to deliver advice.

In assessing the current system of professional standards, the PJC Report recommended that industry establish an independent, professional standard-setting entity that would be controlled and funded by professional associations. The PJC Report recommended a model consisting of six core elements related to: completing a degree; passing an exam; completing ongoing professional development; subscribing to a code of ethics; establishment of a new standard setting entity; and enhancements to the Register of Financial Advisers.

The PJC recommendations would assist in preventing the provision of poor advice to retail consumers. The new standards would also provide the opportunity for professional associations to build up the skills of their members. However, the PJC Report's recommendation that all financial advisers would be required to be a member of a professional association has the potential to restrict competition in industry, by creating a barrier to entry for new financial advisers and guaranteeing professional associations an inflow of members. As indicated in relation to the Murray Inquiry, the requirement to hold a degree and pass a professional year would impose costs on both financial advisers and licensees, some of which may be passed onto consumers.

The final option would be to retain the status quo. This would not impose additional costs on financial advisers or licensees. However, consumers would be unlikely to receive the benefits of higher quality financial advice.

Question 5 – who will be consulted and how?

The Parliamentary Joint Committee on Corporations and Financial Services received 39 submissions from a range of relevant stakeholders. Public hearings were held on three occasions at which stakeholders appeared before the PJC. The Financial System Inquiry took over 280 initial submissions on issues set out in the Inquiry's terms of reference and over 6,800 second round submissions in response to its Interim Report.

The Government and Treasury also consulted on a regular basis with industry stakeholders throughout the policy development process, including hosting five industry roundtables on the development of policy options and the exposure draft legislation.

During consultation, stakeholders presented views on the educational qualifications and code of ethics requirements that were integrated into the Government's framework to raise professional standards in the financial advice industry. This framework builds on the models presented in the PJC Report and Murray Inquiry.

Question 6 – agreed option

In the Government's response to the Murray Inquiry on 20 October 2015, the Government announced that it was committed to, through the introduction of legislative reforms, ensuring that consumers receive professional and fair treatment from advisers. In subsequent announcements, the Government confirmed that it would:

- require new financial advisers to hold a degree, undertake a professional year and pass an exam;
- recognise an independent standards body to set education standards, professional year and continuing professional development requirements, as well as develop a comprehensive code of ethics for financial advisers;
- require existing advisers to undertake a transition process to complete an appropriate degree equivalent (or have a recognised transition pathway determined by the independent standards body), and pass an exam; and
- require all advisers to undertake continuing professional development and be party to a code of ethics.

The regulatory costing for this reform package has been prepared, consistent with the Government's Regulatory Burden Measurement Framework. These costs are summarised in Table 1. For all reporting periods, the Treasury portfolio has reported net compliance cost reductions and there is no reason why the portfolio will not continue to deliver on its red tape reduction targets this year, in line with the Government's regulatory reform agenda.

Table 1: Regulatory burden and cost offset estimate table

Average annual regulatory costs (from business as usual)				
Change in costs ($ million)	Business	Community organisations	Individuals	Total change in costs
Total, by sector	$77.3	$0	$87.8	$165.1

Implementation and Evaluation

Implementing these reforms will begin as soon as practicable following Royal Assent. The Government will incorporate the new standards entity that will be responsible for implementing and monitoring the professional standards for financial advisers.

Existing advisers will have until 1 January 2021 to pass the exam and until 1 January 2024 to complete the required bridging courses determined by the body. If they do not satisfy these transitional requirements, they cannot continue to practice as a financial adviser giving personal advice to retail clients on complex financial products.

A review of the professional standards reforms will be conducted before the end of 2026 to consider whether the new industry arrangements for raising the professional standards of financial advisers has provided better outcomes for consumers.

I am satisfied that the PJC Report, the Murray Inquiry and the consultation process on the reforms to raise professional standards, represent a thorough analysis of the impact on stakeholders and certify that the processes and analysis above are equivalent to those required for a RIS as set out in the Guide.

Should the OBPR have any queries in relation to this matter please contact Kate Phipps on (02) 6263 3056 or kate.phipps@treasury.gov.au.

Yours sincerely

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Deputy Secretary
Markets Group