
Response to ASIC CP 254 Regulating Digital Financial Product Advice

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Executive Summary

Rubik Financial Group welcomes ASIC's approach with consultation paper 254, and encourages discussion about regulating direct-to-consumer digital advice providers.

We are committed to working with ASIC and the industry to ensure Australian consumers consistently receive accurate and high quality advice that complies with Australian regulations.

As a technology provider we promote digital advice as a relatively cost efficient method for delivering advice augmenting traditional channels and providing access to quality advice to a boarder part of the Australian population. It represents one component of the omni-channel offer that supports goals-based scaled advice, as well as specialist and comprehensive advice. In our opinion, the future of advice technology is a digital ecosystem that integrates 'best of breed' applications and processes with an open architecture that supports enterprise-level control for ongoing compliance and risk management of all advice types.

Overall, Rubik supports the issues ASIC raises for debate in this consultation. However, we believe a number of key concerns require further exploration, and we have provided recommendations for how these might be resolved, including:

- **Responsible Manager (RM)** — We agree that a digital advice licensee should have at least one RM who meets the minimum training and competence standards for advisers. However, we also believe this RM should hold a prominent strategic role in the organisation. (Refer answer to B1Q1.)

- **Ongoing Audit** — Digital Advice is a paradigm shift in how advice is constructed and brings into play sophisticated algorithms and potentially Artificial Intelligence and as such requires a different audit approach to traditional audit approaches focused on file reviews, compliance and professional standards. More information is needed about how ASIC will monitor digital advice providers and ensure their algorithms are accurate and fit for purpose. This becomes more important given the reliance placed on them when delivering financial product advice to clients. There's limited discussion about reviewing the overall digital advice produced, and how this advice will be audited.

We believe the solution is an independent actuarial assessment of the model to verify the calculations are accurate and the digital advice provider has incorporated the legislation correctly. We consider this to be essential, since an RM will be unlikely to understand the science of developing mathematical models (as opposed to calculating a strategy or projection). ASIC puts the onus on the RM, which works in a typical advice business where the RM can review all aspects of the advice before giving it to their client. In that case, the RM is looking at an outcome and making sure its basis is appropriate. But digital advice lets consumers vary inputs at their own discretion, and relies on the algorithms to deliver an appropriate solution.

However, we also understand that actuarial sign-off would significantly impede the self-service, 24/7 benefits consumers expect from digital advice. We would consider that actuarial sign-off would be needed when significant changes have been made to the underlying algorithm.

- **Algorithm testing** — Algorithm accuracy is critical to providing advice, and should not be underestimated. Each advice topic may have more than 100 different scenarios to handle all the situations that could potentially cause problems. This vast array of options could have an impact on the accuracy/quality of the algorithm. In our opinion, this is the single most critical factor affecting the quality of digital advice.

In our opinion, ASIC's stated expectations don't adequately address this factor under terms such as 'robust testing' We would prefer words to the effect of 'robust testing that emphasises scenario testing to encompass the range of possible circumstances represented by users of the tool'. Ideally there would even be guidelines to highlight what needs to be considered. We would expect ASIC to further involve the market/industry in consulting on this. Further analysis is needed on the cost/benefit of having independent third parties testing algorithms compared to self-regulation.

- **Consistency** — Rubik also believes consistency should be considered. A digital advice engine should give consistent results not only when the same inputs are used, but also irrespective of the channel (e.g. phone, face-to-face). For example, if an individual accesses advice through a licensee's mobile app, they should receive the same results on their laptop via their client portal. This is a matter of ensuring not only that the software is accurate, but also that the software is configured/integrated accurately and consistently for that channel.
- **Competition** — More analysis is needed as to how this will affect competition. Innovation in digital advice should be encouraged and should benefit consumers. However, ASIC should ensure regulation of new products and services is appropriate, effective, and promotes trust and confidence in both investors and consumers.

Further considerations we would like to bring to ASIC's attention:

The speed of technology change is rapid and there needs to be a regulatory framework that protects and safeguards clients while acknowledging that technology advancements will continue to occur in this space. For example the testing of defined repeatable algorithms today will morph into the use of more and more machine learning in the future.

There needs to be greater focus on potential conflicts of interest and how client best interests are observed in this channel. We believe the commercial models that support Digital Advice Channels are more likely to have vertical integration with product outcomes.

Consultation paper 254

Response to ASIC CP 254 Regulating Digital Financial Product Advice

Thank you for the opportunity to respond to ASIC CP 254.

In this submission:

Rubik Financial Group supports ASIC in its approach to developing a healthy and robust digital advice market in Australia and welcomes ASIC's approach with consultation paper 254. The proposed guidance will certainly help generate discussion about the need for clarity in the regulatory duties of direct-to-consumer digital advice providers.

We support ASIC's proposal that a digital advice licensee have at least one responsible manager who meets the minimum training and competence standards for advisers. However, we believe it would be better if this responsible manager held a prominent strategic role in the organisation. (We elaborate on this in our answer to B1Q1.)

Rubik would also like to raise some key concerns about:

- The way ASIC proposes to monitor digital advice providers and make sure their algorithms are accurate, given the reliance placed on them when delivering financial product advice to clients.
- The cost/benefit of having independent third parties testing algorithms compared to self-regulation.
- Making sure there are consistent results in providing digital advice through any channel.
- The proposal not stating whether any consumer groups were involved in the draft process.
- The need for more analysis on how it will affect competition.

A1. We propose to release draft Regulatory Guide 000 Providing digital financial product advice to retail clients (RG 000) to assist digital advice providers in complying with the law.

A1Q1. Overall, is the proposed guidance helpful? If not, why not?

The proposed guidance will certainly help generate discussion about the clarity needed regarding the regulatory duties of direct-to-consumer digital advice providers. It also clarifies ASIC's position and intention to assign the same regulatory frameworks to both digital and non-digital advice providers.

The proposal didn't make it clear whether any consumer groups were involved in the draft process, especially in regards to understanding what digital advice customers would need in terms of disclosures. With no opportunity to meet their adviser face to face and investigate/ask for additional information in person, what would make consumers feel protected in a digital environment and what would make sure that the advice is being provided in the best interest of the client? Possible solutions include:

- Making a clear distinction between actual past performance versus projected past performance (for newly born services)
- Clearly indicating who in that organisation the qualified responsible manager is, and including their track record.
- Under what conditions should a customer be allowed to execute advice 100% digitally, vs when should the advice provider (or advice system) ask more questions/decline to provide advice. The digital advice system could have inbuilt red flags that triage issues to a real adviser or give an alternative option prior to advice progressing. This would help in determining that the advice being provided is in the best interest of the client.

A1Q2. Is our proposed guidance (in Section D of the draft regulatory guide) helpful in assisting digital advice providers to provide scaled advice that is in the best interests of clients? If not, why not?

Yes it is. The most successful outcome will be to consider all feasible options and give clients access to high-quality, low-cost digital advice. The challenge will be striking a balance between:

- The complexity of advice being provided. For example, switching bank accounts vs switching super funds and the complexity of providing that advice. A bank account switch may be completed 100% digitally, but a super switch would require much more investigation and perhaps the involvement of an adviser.
- Avoiding heavy regulatory checks on digital advice providers that would have material financial impact on young companies

- Guaranteeing enough compliance checks to fully protect consumers and making sure that the advice is being provided in the best interest of the client.

The risk is that by trying to support small start-ups and transform Australia into an attractive Fintech market with a lighter regulatory environment, the focus on the consumers' interests could be lost.

B1. We propose to require that a digital advice licensee has at least one responsible manager who meets the minimum training and competence standards for advisers. To assist existing AFS licensees that may not have a responsible manager who meets these standards, we propose a transition period of six months.

Note: See RG 000.44–RG 000.51 of the draft regulatory guide for more details.

B1Q1. Do you agree with this proposal? Please provide supporting arguments.

Having at least one responsible manager who meets the minimum training and competence standards for advisers is a good first step in ensuring the business has the necessary knowledge and qualifications. But how can this person fully influence the algorithms outcome if they aren't technically minded and rely on other members of the organisation to execute the guidelines—especially if they were hired only to check the compliance box and don't hold a prominent strategic role in the company?

If there is a responsible manager, they should have to comply with the proposed ethical standards. We should also consider the ratio of responsible manager to consumers they service to ensure the clients' needs are met and their queries are clarified.

It isn't clear what the "continuing professional development requirements" actually mean in terms of a time commitment. It would be great to get clarification on this point, and whether this commitment will be in line with current continual professional development points required by financial advisers.

B1Q2. Do you agree that, if the changes proposed in the Corporations Amendment (Professional Standards of Financial Advisers) Bill 2015 become law, at least one responsible manager should: (a) meet the new higher training and competence standards (i.e. have a degree or equivalent, pass an exam, complete a professional year and undertake continuing professional development); and (b) comply with the proposed ethical standards (i.e. comply with a code of ethics and be covered by an approved compliance scheme)?

We agree that the minimum standard for a responsible manager should be the same for digital advice providers.

The responsible manager should:

- Have a degree or equivalent
- Pass an exam
- Complete a professional year
- Undertake continuing professional development and
- Comply with the proposed ethical standards

The licensee responsibilities lie in monitoring and supervising education standards and activities of advisers.

We strongly agree with all points included in (b).

B1Q3. Are there any aspects of the proposed higher training and competence standards in the Corporations Amendment (Professional Standards of Financial Advisers) Bill 2015 that should not apply to at least one responsible manager of a digital advice licensee?

No.

B1Q4. Is the proposed transition period of six months long enough for existing AFS licensees to comply with the requirement to have a responsible manager who meets the minimum training and competence standards? If not, why not?

No comment.

B1Q5. Please provide feedback on any costs or benefits that may apply to your business under the proposal.

It would increase costs in the sense that the business would need to absorb the additional cost of ongoing training and professional development. There may also be upfront costs to change management from both workflow and technology changes. We imagine these costs will become more apparent later.

C1. We propose to issue guidance on the ways in which we think digital advice licensees should monitor and test the algorithms underpinning the digital advice being provided. Note: See RG 000.68–RG 000.70 of the draft regulatory guide for more details.

C1Q1. Do you think we should be more detailed in our guidance on the ways in which we think digital advice licensees should monitor and test algorithms? If so, what additional guidance should we provide?

Licensees have a duty of care to fully assess the appropriateness of using digital vendors in the same way ASIC currently requires licensees to assess all of its vendors. It should form part of the licensee's responsibilities to conduct due diligence and review the SLAs attached to providing a service to the licensee. In the case where a licensee builds its own algorithms or calculators, it should consider the ability of its staff and vendors to achieve the standards of the algorithm providers.

Rigorous testing procedures should be put in place to ensure any algorithms used by digital advice providers are compliant and robust. (We have around 100 test scenarios for each of our advice topics.) In fact, we believe "rigorous testing" should be expanded to "rigorous testing that emphasizes scenario testing to encompass the range of possible circumstances represented by users of the tool".

We would also like ASIC to elaborate on how they envisage digital advice providers monitoring and testing their algorithms. We believe algorithm tests should include:

- What is affected (i.e. what module)
- A source of truth and expected result
- Some form of scenario testing
- Confirmation that the same results are achieved across various platforms (e.g. mobile, tablet, laptop, etc.)

The algorithms themselves affect the quality of advice. We would like to see a detailed response as to how ASIC will make sure the algorithms remain accurate and their quality remains high to ensure quality advice is being delivered.

ASIC could provide more specific guidance on risk-profiling algorithms, such as test cases where particular detailed customer types fall within a specific risk profile range and algorithms need to match that outcome to be compliant.

C1Q2. Please provide feedback on any costs or savings to your business as a result of this proposed guidance.

No impact would be felt. Rubik takes compliance measures very seriously and costs associated with ensuring the quality of advice delivered via our solutions are considered necessary to our technology development, not additional.

C1Q3. Do you think we should introduce a self-certification requirement which would require digital advice licensees to certify that their algorithms have been adequately monitored and tested?

No. We don't believe self-certification is a good idea. We believe independent third-party testing would yield a better result, as not all responsible managers will understand the science of developing mathematical models as opposed to calculating a strategy or projection. And third-party assessment validates that:

- The calculations are accurate
- Legislation has been correctly incorporated
- Any number of possible outcomes will be derived appropriately

However, third-party signoffs could become a significant barrier to entry due to costs.

C1Q4. Should we require independent third-party monitoring and testing of algorithms? If so, in what circumstances would this be warranted?

With a typical advice business, the responsible manager can check the outcome before it's released to make sure it's appropriate. But with digital advice, it's the inputs that need to be scrutinised. And that's not something a typical responsible manager would be capable of doing.

Algorithms should be monitored and tested by independent third parties whenever big changes are being made to the algorithms that could have a major effect on outcomes.

Should self-certification be introduced, independent third party testing should be used whenever algorithm testing proves to be unsatisfactory (e.g. complaints have been raised that require action to be taken).

As well as testing of the algorithm, there should be guidelines on testing the implemented solution. An algorithm that works perfectly isn't much use if the system is badly configured, or the inputs aren't checked for obvious errors.