



FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA

Brooke Stewart
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Australian Securities and Investments Commission
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18 May 2016

Dear Ms Stewart

REF: ASIC CP 254: Regulating digital financial product advice

The Financial Planning Association of Australia (FPA)¹ welcomes the opportunity to provide input to ASIC consultation on the regulation of digital financial product advice. The FPA feels that in particular this guidance will be useful as a starting place for new entrants looking to understand the regulatory environment around Australian financial services licensing, and provides ASIC with an opportunity to lead these new players through the broader regulatory guidance provided by ASIC.

We welcome the opportunity to discuss our submission with ASIC. If you would like further information about our submission, please contact me on (02) 9220 4544 or email: ben.marshan@fpa.com.au.

Yours sincerely

Benjamin Marshan
Professional Standards and Advocacy Manager

¹ The Financial Planning Association (FPA) represents 12,000 members and affiliates of whom 9,000 are practicing financial planners and more than 5,500 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first “policy pillar” is to act in the public interest at all times.
- We banned commissions and conflicted remuneration on investments and superannuation for our members in 2009 – years ahead of FOFA.
- We have an independent conduct review panel, Chaired by Mark Vincent, dealing with investigations and complaints against our members for breaches of our professional rules.
- The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices. This is being exported to 24 member countries and the 150,000 CFP practitioners that make up the FPSB globally.
- We have built a curriculum with 17 Australian Universities for degrees in financial planning. All new members of the FPA are required to hold, as a minimum, an approved undergraduate degree.
- CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional bodies, eg CPA Australia.
- We are recognised as a professional body by the Tax Practitioners Board



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ASIC CONSULTATION PAPER 254: REGULATING DIGITAL FINANCIAL PRODUCT ADVICE

Prepared for ASIC
18 May 2016

INTRODUCTION

The FPA welcomes the opportunity to provide feedback on the proposed guidance contained in ASIC Consultation Paper 254: Regulating digital financial product advice. We congratulate ASIC on seeking to provide guidance on this emerging sector of the financial advice market. In particular this guidance will be particularly useful as a starting place for new entrants looking to understand the regulatory environment around Australian financial services licensing, and provides ASIC with an opportunity to lead these new players through the broader regulatory guidance provided by ASIC.

The emergence of digital advice and robo-tools are a significant positive in the view of the FPA, and will help more consumers engage with their finances to better understand their financial position. Therefore any assistance ASIC can provide to this emerging sector of software developers to understand their obligations in providing advice to consumers is strongly encouraged.

We would note however that there are aspects of the proposed guidance which are not new, and in some instances risk creating an uneven playing field for organisations looking to provide financial advice to consumers. ASIC has always been proactive in confirming that its regulatory guidance and the framework created are channel agnostic, particularly during the transition to FOFA. We would therefore ask ASIC to consider whether some aspects of this proposed regulatory guidance are required (i.e. could reference be made to other Regulatory Guides be made rather than restating existing guidance) or have the unintended consequence of favouring one advice channel over another to the detriment of consumers.

The FPA believe in principal, any organisation providing financial advice to a consumer must meet the same level of organisation compliance, and operate in the same regulatory environment. We therefore provide feedback to the questions proposed by ASIC below.

Compelling adoption of professional standards

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?

Yes, the proposed guidance is generally helpful as a starting place for new licensees who are looking to provide digital advice, or produce digital advice tools.

We would note however that ASIC has always stated publicly in the past, including in other Regulatory Guides that ASIC guidance is channel agnostic and applies irrespective of how the advice is being delivered. From this perspective, beyond providing new guidance around the testing of algorithms, the FPA believes that the rest of the guide would be better developed as an information sheet for new digital advice providers on where to find obligations they need to comply with in other regulatory guides. ASIC should also be careful to not unintentionally introduce new,

amended or lesser obligations on any AFSL providing advice and advice services to retail consumers by providing separate guidance on an existing area of regulatory guidance in a new location as this is likely to lead to confusion and unintended non-compliance through the increased complexity created.

The principal we believe which must be applied is that any provider of advice must be held to the same standards irrespective of the channel the advice is provided by. Ensuring organisational competence, compliance with legislated obligations and appropriate systems of monitoring the provision of advice are universal measures to ensure consumer protection.

We would also highlight that there are some terms within draft regulatory guide which should the Corporations Amendment (Professional Standards of Advisers) Bill and Regulations be passed by Government, could limit or incorrectly identify individuals under which certain obligations arise (although we would assume that this would be required across all regulatory guidance). We would highlight the “reviewing digital advice” section in particular may need some language amendments, particularly the reference to ‘adviser’.

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?

In relation to requiring ‘.. the client to actively demonstrate that they understand that the advice they are seeking is within the scope of what is being offered by the digital advice model’, you say:

We encourage you ... to conduct testing to ensure that your chosen methods are effective and take into account specific client needs.

The FPA strongly believes that ASIC should be more prescriptive. We cannot see how a digital advice provider could ensure the client understands the scope of what is being offered by the digital advice model unless the methods used to do so are tested. Unless the chosen methods are tested to ensure they are effective and take into account specific client needs, there is a material risk that clients will not understand the scope of the offer.

We would highlight that unlike in a traditional face to face or telephone based advice environment, digital advice providers would typically not have detailed conversations with clients. Detailed conversations allow traditional advisers to gauge the client’s understanding by tailoring questioning and feedback to that particular client as the conversations happens, to test understanding and provide additional education. By contrast, digital providers are at such a distance from their clients that they need to rely on a theory as to how clients in general (or particular groups of clients) will interpret communications. Theories should be tested to ensure they are correct, and if not, ASIC should require the digital advice provider to ensure additional education is provided to the consumer to ensure they have sufficient knowledge to make an informed decision around the recommendations being made. It is commonly acknowledged that there is a lack of financial literacy among Australian consumers, and this should be taken into account by digital advice providers as part of their obligations in providing an advice service.

We would also note that where the tool is being produced by a business for use by another business rather than being built directly for use by consumers, it is unclear which requirements in this guidance need to be met or whether there are other obligations being set. We would recommend that as the consuming business may not have the expertise or visibility of the algorithm it has purchased or makes use of, that the requirements equally apply.

On the topic of FOFA compliance, another issues ASIC may wish to reiterate (if the decision is made to provide a full specific regulatory guide to new entrants into the advice space) is the requirement to comply with fee disclosure statement and opt-in obligations where ongoing service fees are being charged (via subscriptions revenue models).

We would also advise ASIC to consider providing guidance around professional indemnity insurance. Face to face advice by its very nature generally limits the amount of clients that can be interacted with (as well as the aforementioned clearer understanding of the client's financial literacy). Digital advice however has the ability to scale exponentially, and therefore potential damages requiring indemnity insurance could be considerably higher. ASIC may therefore wish to be more prescriptive around PI guidance. We would further enquire as to whether ASIC has consulted with the PI market around this issue to gauge the likely issues new entrants may need to consider in developing and insuring their offering.

Following on from this, clear guidance on complaints handling and EDR scheme membership should also be highlighted or included in this guidance.

And finally, there is evidence that some start-ups have challenges with their financial position², so reference to RG166 would seem to have prudence.

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.

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

The FPA agrees that digital advice providers should meet the minimum training and competence standards required for any provider of advice to retail consumers, in fact this is a must. These requirements help ensure advice is of good quality and compliant. The policy intent of the training and competence standards is presumably to ensure that the minimum quality of advice is of the same across advice channels. Prescribing one standard for one advice channel and a lower (or no) standard for another advice channel is arbitrary unless there is some relevant difference between the different channels. Given that both digital and traditional channels deal with retail investors, we presume that applying different standards to different channels can't be justified. We would highlight ASIC's existing guidance in RG105, in particular paragraphs 3 to 6.

² The top 20 reasons startups fail, CB Insights, 07/10/2014, <https://www.cbinsights.com/blog/startup-failure-reasons-top/>

Further, we are concerned that if a digital advice provider has only one responsible manager who meets the minimum training and competence standards for advisers, there will be times when no such person is overseeing the business and provision of advice. For example, this will happen if the responsible manager is on holidays or ill or suddenly leaves the business. This creates significant risk for consumers receiving advice services from the AFSL.

A digital advice provider constantly provides advice, whereas a traditional advice provider may have periods where its services are suspended. For example, a one-person traditional adviser who takes extended leave would suspend services or refer clients to another adviser. The continual flow of advice from a digital advice provider means they always need at least one responsible manager who meets the minimum training and competence standards for financial advice providers. Setting a standard where there is likely to be periods of no responsible manager being present given the potential scale of advice being provided creates significant risk of no one with the knowledge and capability to identify advice issues overseeing the operation of the algorithm.

The FPA therefore recommends that a digital advice provider has at least two responsible managers who meet the minimum training and competency standards for advisers, but more broadly be required to comply with the organisational competence obligations in RG105. This will help ensure there is never a period where advice is being provided but no appropriate person is overseeing the business.

Further, we recommend that no transition period be allowed. We feel there is no basis for a transition period and this sets a dangerous precedent that businesses can enter an industry without meeting prescribed standards and won't be called to account. This puts retail consumers at significant risk.

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)?**

As already mentioned, no good policy reason has been offered for accepting conditions that will produce a different quality of advice depending on how the advice is delivered. If – as appears to be the case - the policy intent of the new framework is for higher standards to be set to ensure the same minimum quality of advice to all retail consumers irrespective of channel, how could this be achieved if digital advice providers have lower training, competence and ethical standards than face to face advisers?

Further (and, again, as already discussed), we feel that at least two responsible managers should meet any proposed training, competence and ethical standards.

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, for the reasons already discussed.

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?

As noted, we believe that providing a transition period is inappropriate as it sends a message that regulations can be flouted without consequence. We would also be concerned that there are currently consumers receiving advice and implementing recommendations which do not comply with the minimum training and organisational competence standards. We again note that ASIC guidance has always made it clear that regulatory compliance applied irrespective of the channel it is provided under, including around the use of calculators which are just simple versions of robo-tools. Further, it has always been clear that providers must meet the training and competence requirements through *some* mechanism.

Rather than providing a transition period where digital advice providers do not need to meet the training and competence standards, ASIC should instead ensure providers comply with their obligations. If the digital advice provider does not currently have at least one responsible manager who meets the training and competence standards, the provider should formally undertake to have such a manager within six months. In the meantime, an appropriately qualified individual reporting directly to the board (or ASIC if the business is unincorporated) should be engaged by the provider immediately to ensure that the quality of advice is sufficiently high. During this time, ASIC should be scrutinising the advice of such a provider particularly closely, and if there are any concerns, the tool should be turned off to consumers.

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

We do not have any figures to provide.

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.

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?

The FPA recommends that algorithms should be tested against the same standards applied to traditional advisers. In other words, does the algorithm *always* put the client in a better position (whether materially or in terms of knowledge of their situation). ASIC has already published material on the quality of advice expected of advisers, the FPA believes it is important to make clear that exactly the same minimum standards are expected of digital advice providers.

For example, it should be ensured that an algorithm would *never* recommend a switch where:

- the overall benefits likely to result from the ‘to’ fund would be lower than under the ‘from’ fund, unless outweighed by overall cost savings
- the cost of the ‘to’ fund is higher than the ‘from’ fund, unless the ‘to’ fund better satisfies the client’s needs.

When specifically considering the testing of algorithms, we would also raise with ASIC whether it is the intention of this regulatory guidance to apply equally to all “advice tools” used to provide advice to retail consumers? We note that advice tools may include digital advice providers this guidance is aimed at, but more broadly to anyone using any tools for the basis of calculating outcomes for consumers when developing a strategy and set of recommended products. For example, traditional advice software providers (for example XPlan, COIN, Midwinter, Decimal, Provisio etc.), and even advisers building their own tools (for example in Excel) to calculate outcomes for clients have the potential to be relied upon by an adviser when providing recommendations to consumers. We would suggest ASIC may want to consider the definition of “tool” as used throughout this guidance to make this clear.

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

We provide not have any figures to provide.

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?

There is an inherent conflict of interest in self-certification. Digital advice providers should instead engage independent actuaries to monitor their algorithms, the same way that there is an obligation that non-algorithmic advice providers must have independent parties (from the advice provider) review the advice they provide for monitoring and supervisory purposes. If ASIC is after visibility of these results, an obligation to provide independent review results should be included in the regulatory guidance. We would note however that an additional reporting standard has the potential to create discrepancies in the regulatory setting of different advice channels, and our point is more that an actuary has the expertise to test an algorithm in an independent manner as opposed to self-certification.

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

In all circumstances, independent third-parties should monitor and test digital advice providers' algorithms. As per our response to C1Q3, there is an inherent conflict of interest in self-certification.
