



**ASIC**

Australian Securities & Investments Commission

**REPORT 69**

# **Shadow shopping survey on superannuation advice**

April 2006

# Highlights

The purpose of the survey was to assess whether the advice given to consumers after the introduction of Super Choice complied with the law.

The survey assessed 306 examples of advice given to real consumers between June and December 2005. Roy Morgan Research recruited the consumers in the survey.

The most positive finding was that the 'strategic' advice provided by advisers was generally helpful to consumers. This advice covered issues such as asset allocation, how much to contribute to superannuation and the tax advantages.

The survey also identified very few unlicensed people who should not have given superannuation advice at all.

However, the survey found the financial advice industry still has significant work to do before the quality of advice will be consistently at a level that ASIC and consumers would regard as acceptable.

The survey identified several key problem areas:

- 16% of advice was not reasonable, given the client's needs (as required by law) and a further 3% was probably not reasonable.
- Where consumers were advised to switch funds, a third of this advice lacked credible reasons and risked leaving the consumer worse off.
- Unreasonable advice was 3–6 times more common where the adviser had an actual conflict of interest over remuneration (e.g. commissions) or recommending associated products.
- Consumers were rarely able to detect bad advice.
- In 46% of cases, advisers failed to give a written Statement of Advice (SOA) where one was required. However in a fifth of these cases, the verbal advice was a reasonable, non-conflicted recommendation for the person to stay in their current fund.

ASIC will be conducting specific follow up action with 14 licensees in response to issues raised in the survey. ASIC expects all licensees will act quickly to fix the problems identified in the survey, as compliance problems were noted across a wide range of firms.

The survey has clear implications for the licensees and financial conglomerates who create the working environment for advisers. While some progress has been made, the cultural changes mandated by the *Financial Services Reform Act* are not happening quickly enough.

ASIC will be accelerating pressure on the industry to consistently achieve acceptable standards of advice and disclosure.

# Contents

---

<b>Highlights .....</b>	<b>2</b>
<b>Executive summary .....</b>	<b>5</b>
<b>About the survey .....</b>	<b>5</b>
<b>How the survey was conducted .....</b>	<b>5</b>
<b>Findings.....</b>	<b>7</b>
<b>Broader observations.....</b>	<b>11</b>
<b>Issues for the future.....</b>	<b>12</b>
<b>Section 1: Background .....</b>	<b>14</b>
<b>Aim of the survey .....</b>	<b>14</b>
<b>Context .....</b>	<b>14</b>
<b>Section 2: Survey methodology.....</b>	<b>15</b>
<b>Stage 1: Participant recruitment.....</b>	<b>15</b>
<b>Demographics of participants in the survey .....</b>	<b>18</b>
<b>Operation of the survey.....</b>	<b>19</b>
<b>Stage 2: Advice assessed for compliance .....</b>	<b>19</b>
<b>Stage 3: Analysis and reporting.....</b>	<b>20</b>
<b>Section 3: Nature of advice .....</b>	<b>21</b>
<b>Profile of advisers .....</b>	<b>21</b>
<b>Experience of consumers in seeking advice.....</b>	<b>22</b>
<b>Reasons for seeking advice .....</b>	<b>22</b>
<b>Satisfaction with advice and implementation.....</b>	<b>22</b>
<b>Nature of advice given.....</b>	<b>23</b>
<b>Initial cost of advice .....</b>	<b>24</b>
<b>Conflicts of interest.....</b>	<b>25</b>
<b>Section 4: Findings on compliance .....</b>	<b>27</b>
<b>Level of compliance: authorised representatives.....</b>	<b>27</b>
<b>Know your client.....</b>	<b>28</b>
<b>Reasonable basis for advice .....</b>	<b>29</b>
<b>Analysis where a switch recommended .....</b>	<b>33</b>
<b>SOA provided.....</b>	<b>38</b>
<b>SOA content .....</b>	<b>40</b>
<b>Disclosing the consequences of replacing funds .....</b>	<b>41</b>
<b>Disclosing conflicts of interest .....</b>	<b>43</b>
<b>Quality and length of SOAs.....</b>	<b>43</b>
<b>Level of compliance: unlicensed advisers.....</b>	<b>43</b>

<b>Section 5: Broader observations.....</b>	<b>45</b>
<b>The advice market involves many levels of assistance ....</b>	<b>45</b>
<b>The value of strategic advice.....</b>	<b>45</b>
<b>The practical limits of disclosure .....</b>	<b>46</b>
<b>Some signs of selling rather than advising .....</b>	<b>46</b>
<b>Disclosure has improved but needs to be more effective</b>	<b>47</b>
<b>Hard to get simple, compliant advice .....</b>	<b>47</b>
<b>Section 6: Follow-up action and future directions .</b>	<b>48</b>
<b>Issues for ASIC.....</b>	<b>48</b>
<b>Our expectations of industry.....</b>	<b>50</b>
<b>Appendix A: Detailed demographic information ....</b>	<b>53</b>
<b>Appendix B: Detailed methodology .....</b>	<b>55</b>
<b>Stage 1: Participant recruitment.....</b>	<b>55</b>
<b>Stage 2: Advice assessed for compliance .....</b>	<b>57</b>
<b>Comparison with previous surveys .....</b>	<b>59</b>

# Executive summary

## About the survey

ASIC's shadow shopping survey monitored the compliance standards of superannuation advice against legal obligations during the first seven months of super choice.

A secondary aim was to research consumers' experiences in getting that advice.

## How the survey was conducted

### Participant recruitment

ASIC engaged Roy Morgan Research (Roy Morgan) to recruit survey participants and gather examples of the superannuation advice they were given.

Roy Morgan phoned households at random to identify people who met the survey's selection criteria. The key criterion was that the person intended to seek (or had recently received) professional superannuation advice. The survey covered advice given between June and December 2005.

*Participants were real consumers who wanted advice for their own purposes. Some were existing clients of advisers; others were new clients. The survey process did not interfere with how the consumers got their advice—the consumers themselves chose who to see for advice and what issues they wanted advice about.*

The demographic profile of our 306 survey participants broadly reflected the profile of people in the Australian market for superannuation advice. Advisers in the survey were mainly financial planners (86%), with the remainder being accountants (13%) and a few life insurance specialists and advisers directly employed by super funds.

Survey participants gave ASIC written material they got from their adviser, such as Statements of Advice (SOAs). Participants also completed a diary and two questionnaires so that we had the participant's own information about their personal circumstances, as well as their own written record of each contact with the adviser and their feedback after getting advice.

The recruitment process gave us 306 samples of advice to assess. The survey covers 259 individual advisers and 102 Australian financial services (AFS) licensees of varying sizes. This is the largest survey of this kind ever published by ASIC.

## Assessment and analysis

Each sample of super advice was assessed for legal compliance on key issues. A team of ASIC analysts, experienced in financial planning reviews, conducted this assessment. A manager with legal qualifications and financial planning experience supervised the team.

The key legal issues we checked were:

- whether the adviser was authorised (where required) to give financial advice;
- whether the advice provided had a ‘reasonable basis’, i.e. whether:
  - the adviser had investigated and considered key factual issues (e.g. client’s personal and financial circumstances such as age, family circumstances, goals, income and assets, existing super arrangements); and
  - the advice was appropriate to the client’s circumstances;
- whether the adviser had given a written SOA (if required); and
- whether the SOA contained all necessary information that needed to be disclosed to the client.

In assessing the advice, we referred to:

- the SOA (where the consumer got one);
- the consumer’s own written account of getting advice;
- the consumer’s own written account of their personal circumstances; and
- the fund Product Disclosure Statements (PDS).

*We recognised that there will generally be a range of appropriate advice for any individual consumer, not a single correct recommendation.*

The assessment focused on legal compliance and reflects minimum professional standards, not best practice.

## Issues outside the scope of the survey

The survey assessed whether advice was legally compliant. We did not look at whether the ‘best’ advice was given.

We also did not seek to cross-check the information and answers given to us by consumers with the advisers themselves. This would have compromised the confidentiality of the participants and would have changed the nature of the survey entirely. Shadow shopping is a particular type of market research that specifically does not involve the identification of individual consumers to the relevant advisers.

## Findings

### Giving advice under a licence

The vast majority of advice was from licensed advisers or advisers exempt from the licensing requirements. 284 (93%) were representatives of licensees (including 22 accountants). Four others were accountants advising on aspects of self-managed superannuation funds and other issues where they did not require a licence.

The survey revealed 18 advisers apparently in breach of licensing rules - 14 accountants, two tax agents and two mortgage brokers.

The main analysis in this report looks at the 284 representatives of licensees in the survey, assessed against the standards that apply to them. The last section considers accountants and others who were not licensed.

### Reasonable basis of advice

The survey revealed a wide range in the quality of advice—from highly sophisticated advice at one end, through to basic (but valuable) advice in the middle, and negligent and inappropriate advice at the lower end.

Our assessment of whether advice had a reasonable basis was not limited to just the SOA given to the consumer. We also considered reasons mentioned in the consumer's written account of their verbal advice. Where the details of the advice given to the consumer were still uncertain, we did not draw adverse conclusions against the adviser.

16% of the advice *clearly* did not have a reasonable basis in some respect and a further 3% *probably*<sup>1</sup> *did not* have a reasonable basis. Key problems were where the advice was not appropriate for the client's needs in some respect, or the adviser had not made sufficient inquiries to assess appropriateness. Advice that was non-compliant or probably non-compliant came from 24 different licensees, including several large firms.

The proportion of poor advice remained higher than we consider acceptable, because it was well beyond what could be explained by non-systemic human error.

Where the adviser had made at least basic inquiries, few problems were identified on strategic advice issues such as asset allocation and the benefit of extra super contributions. This advice would clearly help consumers working towards their retirement goals. We only saw a few cases of advice on self-managed super funds (SMSFs) and most contained reasonable advice (some recommending SMSFs; some advising against). In contrast, problems were more common in advice to switch funds.

---

<sup>1</sup> 'Probably' non-compliant refers to the situation where, based on all of the information we had, the advice appeared to be non-compliant, but gaps in the information prevented us from forming a definitive view.

## Conflicts of interest

We looked at whether the advice involved an actual conflict of interest, that is:

- the adviser would get higher remuneration if the advice was followed (e.g. trail commission); and/or
- the adviser recommended a product from a company associated with the adviser's licensee (e.g. an in-house fund).

Advice that was clearly or probably non-compliant was about six times more common where the adviser had an actual conflict of interest over remuneration. Where the adviser had a conflict over remuneration, 28% of the advice clearly did not have a reasonable basis and a further 7% probably did not. In contrast, where the adviser did not have a conflict, the percentages were 5% and 1% respectively.

Non-compliant advice was three times more likely where the adviser recommended an associated product.

## Switching advice

In 124 cases (44% of advice given), a recommendation to switch funds was made.<sup>2</sup> In 80 of those cases (67%), the advice to switch appeared to have a reasonable basis.<sup>3</sup>

Of the remaining 40 cases, 34 cases (28%) clearly did not have a reasonable basis and a further six cases (5%) probably did not. The major problems in those cases involved advice to switch to higher fee funds with no countervailing benefits (e.g. from government, corporate or industry funds to retail funds) or the loss of important insurance cover through fund switching.

Where a fund switch was recommended, 62% of licensed advisers recommended a higher fee fund.<sup>4</sup> Only 22% recommended a fund with lower fees. Where advisers did provide a comparison of fees between the existing and recommended fund, most either demonstrated a fee saving or gave credible reasons why the consumer would be better off through other benefits.<sup>5</sup> However, these cases comprised only a minority of the switching recommendations.

As mentioned above, 40 cases of switching advice either did not, or probably did not, have a reasonable basis. We were not able to obtain exact fund information in 17 of these cases. However, in the remaining

---

<sup>2</sup> 'Switching' includes consolidating funds.

<sup>3</sup> In four cases we had insufficient information about the advice to assess its basis.

<sup>4</sup> In 38 cases we had insufficient fee information.

<sup>5</sup> This was assessed by ASIC as having a reasonable basis and therefore being compliant advice.

23 cases where relevant information was available, we used the ASIC superannuation calculator to estimate the consumer's retirement benefit within the recommended fund compared to their existing fund.<sup>6</sup> In 20 of those cases, the ASIC superannuation calculator projected to leave the affected clients worse off at retirement. The average hypothetical difference in retirement benefit was a reduction of \$37,043 or -16%.

This analysis suggests that the advice that was clearly or probably non-compliant was likely to leave consumers significantly worse off. Only one of these advisers claimed that the new fund was likely to deliver higher investment returns. These advisers should have considered the option of the client staying in their existing fund.

### **Providing a Statement of Advice**

Where an adviser gives personal financial advice, the law generally<sup>7</sup> requires the adviser to provide a written SOA. A written SOA gives the consumer the information necessary to make an informed decision whether to accept the advice.

Where an adviser was required to give a written SOA, 52% of the advisers complied. Most of the remaining advice was 'verbal only', with only a few other instances where the written formats did not fully comply (e.g. an informal email that was clearly not an SOA).

In 132 cases, the adviser failed to provide an SOA when required. Our impression is that these cases mainly fell into four broad advice scenarios:

- quick advice that could (and should) have been phrased as general advice, which does not require an SOA (with the warning that the adviser has not investigated the client's personal circumstances) (estimated as a third of the cases);
- quick advice that consumers stay in their current fund because it suited their needs (which we observed was almost always quite reasonable advice) (estimated as a quarter of the cases);
- personal financial advice given during an initial client interview, where the client did not proceed to further advice. This should either have been general advice or expressed as issues to be further explored (estimated as a quarter of the cases); and
- where the adviser wanted the client to commit to the recommendation before the adviser would put anything in writing (often contentious switching advice) (only a few of the verbal cases).

---

<sup>6</sup> Assuming the same strategy adopted, same gross investment returns and no change in fees over time.

<sup>7</sup> See page 38 for an explanation of exemptions.

## Content of Statement of Advice

The law requires that an SOA disclose:

- the adviser's recommendations;
- the basis of the advice (e.g. key considerations in making the recommendations and how the advice is appropriate to the client's needs);
- the specific costs and consequences of switching financial products (if relevant); and
- adviser remuneration and any conflicts of interest.

For asset allocation and insurance recommendations, disclosure of the reasons for advice was generally compliant. However, only half of the SOAs properly disclosed reasons and considerations for fund selection (mainly with switching recommendations).

We saw some excellent examples where the consequences of switching were clearly set out. We believe this quality of disclosure was encouraged by the use of a good template provided by the adviser's licensee, combined with advisers who had the information and training to use the template effectively. This might illustrate good practice for licensees generally.

Disclosure of adviser remuneration and conflicts of interest appeared compliant in most cases where an SOA was given, although there is still room for improvement (73% compliant, 15% probably non-compliant, 12% non-compliant).

Disclosure of the cost and consequences of switching was often unsatisfactory. Of the 124 consumers who got advice to replace one product with another, only 24 (20%) got compliant disclosure about the costs and consequences.<sup>8</sup> Many advisers did not disclose whether the consumer would lose insurance cover by switching out of their current fund. The likely longer-term consequences of higher fees in a new fund were rarely explained. This was exacerbated by the fact that 32% the consumers did not get an SOA at all.

### Clear, concise and effective

ASIC analysts considered how clear, concise and effective each SOA was. We have also seen many examples of written advice from before the *Financial Services Reform Act* was introduced. Our impression is that while progress has been made, there is still room for improvement.

### Spread of compliance problems

Across the range of compliance issues assessed in the survey, problems were detected with a wide range of licensees and advisers. Problems were not confined to a minority of advisers or licensees.

---

<sup>8</sup> In three cases, the level of compliance was unknown.

### **Advisers who were not licensed representatives**

Twenty-two cases in the survey involved advisers who were *not* representatives of licensees.

In some limited circumstances, accountants can give advice on superannuation issues without needing to come within the AFS licensing regime. In broad terms, these include:

- advice to set up an SMSF; and
- advice on the tax aspects of a superannuation product, so long as there is a written warning that other factors may be relevant and the client should seek advice from a licensed adviser.

In four cases, unlicensed accountants stayed within the accountant's exemption and the advice seemed to have a reasonable basis. However, in 14 other cases, unlicensed accountants illegally gave advice on issues that required they be licensed. These cases included advice about non-SMSF super funds, including contribution levels, consolidation and asset allocation.

## **Broader observations**

In this section, we provide observations that go beyond legal compliance issues. They are based on our impressions, rather than statistical findings.

### **The value of strategic advice**

Where strategic advice<sup>9</sup> was given, it generally appeared beneficial for the client (often highly beneficial), even if the advice was quite simple. We did see many cases where advice did not address all key strategic issues (e.g. insurance cover, adequacy of retirement savings), and therefore could have been even more valuable.

### **Practical limits of disclosure**

Survey participants were rarely able to tell whether they had received poor advice, including whether the advice was likely to leave them worse off. In cases where we could see that the advice clearly lacked a reasonable basis, 85% of consumers still felt satisfied with the advice. This is not surprising since consumers are generally not expert in these matters and that is why they were seeking professional advice in the first place.

SOAs generally disclosed the adviser's conflicts of interest. However, we were not comfortable that all consumers could use this information to adequately judge whether the conflicts had influenced, or had the potential to

---

<sup>9</sup> In ASIC's view, strategic advice includes advice about issues like how much to invest, how much insurance cover, asset allocation, tax advantages, etc. It is distinct from advice about which fund to use to implement the strategy. See page 45 for further information.

influence, the advice. Anecdotal evidence gave us the impression that the typical consumer did not readily appreciate the impact that various types of conflict could have on the quality of the advice they were given.

While disclosure is a critical part of consumer protection, this survey suggests that it can only play a limited role in protecting consumers from inappropriate or conflicted advice.

### **Some signs of selling rather than objective advice**

In cases where advisers recommended a switch to a commission-paying fund or an in-house fund, much of the fund selection advice gave the impression of ‘selling’ rather than impartial advice. This is not necessarily harmful in all cases; however, it again highlights an area where licensees should ensure that advisers recognise their responsibility to advise their clients properly and not simply sell products.

Strategic advice appeared more impartial, with clearer reasons and relevance to consumers’ needs.

## **Issues for the future**

### **Issues for ASIC**

#### *ASIC compliance activity*

The broad legal framework is that licensees (e.g. financial planning firms and banks) supervise their representatives who give advice. Licensees are required to take reasonable steps to ensure that their representatives comply with the law, through training, establishing work systems and monitoring. ASIC, in turn, supervises licensees.

The survey findings raise concerns that not all licensees are taking adequate steps to ensure their representatives comply with the law. We will be writing to all those licensees identified in the survey findings. Taking into account those findings and other intelligence about individual licensees (including in a number of cases, surveillance activities already underway), we propose to conduct specific follow-up action for 14 licensees.

We will focus our future compliance activities on the following areas:

- *conflict handling arrangements*—the extent to which these take into account the findings of this report and the higher risk of non-compliance that arises where advisers have conflicts of interest;
- *adequate training and tools*—the extent to which licensees are providing these resources to their representatives to help them comply with their obligations;
- *compliance monitoring and testing*—the extent to which these ensure that licensees satisfy themselves that they and their representatives are complying with their obligations; and

- *breach rectification processes*—the extent to which licensees have adequate processes in place to remedy breaches detected by their compliance monitoring (e.g. notification of and compensation to clients, disciplinary action against representatives who breach their obligations).

We also have a project underway focusing on the provision of advice by unlicensed advisers.

#### *Verbal hold recommendations*

To facilitate access to simple advice, ASIC (in consultation with Treasury) will review whether to waive the obligation to give an SOA where an adviser without a conflict of interest gives free advice that is just a hold recommendation (e.g. 'stay in your current fund').

#### *Managing conflicts of interest*

It is clear from the survey that there was a higher risk of inappropriate advice where either the adviser received commission-based remuneration or the adviser recommended a product from an associated company. Licensees and advisers have traditionally relied heavily on disclosure to manage these conflicts. However, disclosure (even where comprehensible) is not, by itself, always an adequate response if the conflict still leads to advice that is inappropriate or compromises the client's interests.

We will hold discussions with relevant licensees and industry associations about the issue of further guidance by ASIC, industry or a combination of these, on how such conflicts might best be disclosed or managed and what conflicts need to be avoided by licensees.

### **Our expectations of industry**

We expect industry to continue to address its work on consolidation advice, investigating client's current funds and disclosing the consequences of switching.

Licensees should review their supervision and compliance systems, in particular, to ensure any switching advice is compliant. The comprehensive report recommends five steps for licensees to consider: see page 51.

In addition, we expect that licensees and their advisers will revise their practices to ensure an SOA is given whenever required by law.

# Section 1: Background

## Aim of the survey

The major aim of the project was to monitor the compliance standards of superannuation advice during the introduction of super choice. A secondary aim was to research consumers' experiences in getting that advice.

The project is one avenue by which ASIC can identify if the quality of advice given to consumers could adversely affect the benefits of superannuation choice. It also allows ASIC to assess what action needs to be taken to address any problem areas identified by the survey.

## Context

The Financial Services Reform Act 2001 introduced a new licensing regime with a key aim being to raise the standard of financial advice. All industry participants were required to be licensed under the new regime by March 2004. The broad structure is that ASIC monitors licensees, and licensees are responsible for supervising their representatives.

This survey forms one part of ASIC's broader work aimed at ensuring that industry participants meet the relevant legal standards.

ASIC has also conducted a number of recent projects to clarify obligations and monitor compliance. These included:

- ASIC Policy Statement 175 *Licensing: Financial product advisers—conduct and disclosure* [PS 175], which provides guidance on complying with the reasonable basis of advice and SOA obligations;
- ASIC Policy Statement 181 *Licensing: Managing conflicts of interest* [PS 181];
- ASIC's report on its Superannuation Switching Surveillance (August 2005), which alerted industry to widespread non-compliance with the obligation to disclose the consequences of switching;<sup>10</sup> and
- ASIC's Guide 'Super Switching Advice: Questions & Answers' (June 2005), which gave clear guidance about legal obligations in common scenarios.<sup>11</sup>

<sup>10</sup> ASIC also provided an analysis of this project in a report to the Parliamentary Joint Committee on Corporations and Financial Services (9 November 2005).

<sup>11</sup> The Financial Planning Association and CPA Australia had released similar detailed guidance in the first quarter of 2005. *FPA Business Tool 7—Super Choice* (April 2005); *CPA Australia—FSR: Your obligations and options* (revised edition April 2005).

## Section 2: Survey methodology

This survey involved real consumers who genuinely wanted superannuation advice about their own individual circumstances on normal commercial terms.

The survey used a *random* sample of people:

- for whom superannuation choice was relevant; and
- who were in the market for superannuation advice during the survey period.

The survey involved three stages:

- participant recruitment;
- assessment of advice for legal compliance; and
- analysis and reporting.

A summary of the survey methodology is given here, and a more detailed description is in Appendix B.

### Stage 1: Participant recruitment

Roy Morgan Research (Roy Morgan) was engaged to recruit survey participants and gather examples of the superannuation advice given to them. Roy Morgan is one of Australia's largest and most experienced market research firms.

Roy Morgan talked to over 19,000 households in order to identify people at random who met the survey's selection criteria. These were:

- people in employment, but not self-employed or employed by the Commonwealth Government (so super choice was likely to be relevant);
- people aged between 18 and 65;
- people who intended to seek (or had already received) professional financial advice that included advice about superannuation within the survey period of July to November 2005<sup>12</sup>; and
- not people who worked (or whose spouse worked) in the financial services industry, as they might have had a conflict of interest in participating in the survey.

---

<sup>12</sup> While this is the basis on which we recruited people, the advice they sent in covered a slightly wider period. The statistical analysis included 21 examples where the advice was given in June 2005 for later implementation and five examples of advice that late participants received in December.

This filtering exercise gave Roy Morgan a reasonably accurate profile of the underlying population for the survey (i.e. all Australians who fitted the criteria above and were seeking superannuation advice). We refer to this as the ‘target population’.

Roy Morgan then asked people who met the selection criteria if they would be interested in participating in the survey. Of the 1,192 people expressing interest, 414 sent material back to Roy Morgan. From this group, we identified 306 examples of advice that could be assessed. A significant non-completion rate occurs in any survey of this nature, which is why Roy Morgan sought such a large number of recruits at the outset.

Other key features of the survey methodology were that:

- Participants made their own decisions about how to seek advice and who to approach, without any influence from ASIC or Roy Morgan. Great care was taken to ensure that the survey did not influence the participant’s advice-seeking process or the advice quality.

We did not give any directions on how the consumers sought advice—the consumers themselves chose who to see for advice and what issues they wanted advice about. The survey covers advice from a range of advisers, such as representatives of banks, financial planning firms and accountants.

- The sample includes both people who had an existing relationship with the adviser or company (59%) and people using the adviser/company for the first time (41%)<sup>13</sup>. ‘Existing relationship’ may include banking, tax advice, etc.
- Participants used a diary to record their experience in seeking advice. This meant that ASIC had the participant’s own written record of each contact with the adviser. This revealed, for example, where people sought advice but couldn’t get it, or received ‘verbal only’ personal advice. The diary also revealed any major discrepancies between the verbal advice and any later written advice. Where survey recruits had already received advice, the diary was completed after the event.
- Participants completed a personal details form that recorded their demographic details and financial circumstances. This information meant ASIC’s assessment of the advice was not limited by the summary of ‘know your client’ in a Statement of Advice (SOA).

---

<sup>13</sup> n=298, Don’t know=8

- Participants completed a questionnaire on issues such as the reasons why they had sought advice. After getting advice, they also completed a questionnaire about the identity of the adviser and the participant's reaction after receiving the advice.
- Participants sent all documents to ASIC via Roy Morgan (SOA, product disclosure statement, diary, personal details form, etc). Client names were removed to protect privacy.
- Due to the high level of 'verbal only' advice, participants who had only received verbal advice were recontacted by Roy Morgan at the end of the survey to see if they had subsequently received a Statement of Advice. If they had, they were asked to send it in and it was incorporated in the assessment.
- Participants received a \$200 'thank you' for participating in the survey.<sup>14</sup>

The main part of the survey only included participants who met all the selection criteria and had received personal financial advice from an adviser, plus any other family members that received advice as part of the same process. Advice to this group was assessed and forms the statistical part of the survey.

In 44 cases, superannuation advice was also given to another member of the participant's family (usually partner) at the same time. In six cases, the participant received personal advice from more than one adviser.

Allowing for these multiples, the survey covers:

- 306 examples of personal superannuation advice;
- 300 individuals receiving advice; and
- 259 different advisers representing 102 licensees.

Apart from the 306 examples of personal superannuation advice, we received information back from 115 other participants. This wider group did not meet the selection criteria in one or more respects, often because their contact with an adviser did not amount to personal financial advice. The experience of this group only contributed to our broad observations, not the statistical analysis.

A fuller description of the methodology is in Appendix B.

---

<sup>14</sup> A few participants also received a wine gift and/or additional dollar amount where extra effort was involved (for example a small group of respondents were given \$30 for providing extra information following a recontact survey).

## Demographics of participants in the survey

The demographic profile of our survey participants broadly reflected the profile of people in the Australian market for superannuation advice (as surveyed by Roy Morgan Research).

**Table 1: Amount in superannuation**<sup>15</sup>

	Survey cases	Survey percent	Target population (Roy Morgan)
Less than \$5,000	12	4%	5%
\$5,000–\$24,999	53	18%	23%
\$25,000–\$49,999	54	18%	19%
\$50,000–\$99,999	57	19%	18%
\$100,000–\$249,999	73	25%	20%
\$250,000 or more	47	16%	14%
<b>Total</b>	<b>296</b>	<b>100%</b>	<b>100%</b>

*n*=296, Don't know=10

Roy Morgan: *n*=1,228, Don't know=367

The survey covered consumers with a wide range of circumstances. At the modest end, one participant was an apprentice who wanted to know where to put the \$100 he would be paid in superannuation. The most affluent participants were a couple with a net worth of over \$3 million.

As would be expected, older consumers were more likely to have larger superannuation savings and more likely to be seeking advice on superannuation.

**Table 2: Amount in superannuation by age**

	Cases	Minimum	Maximum	Average amount in super
18–24	5	\$300	\$15,213	\$5,106
25–34	29	\$2,900	\$114,000	\$30,150
35–49	107	\$50	\$690,000	\$85,330
50+	153	\$45	\$945,974	\$188,525
<b>Total</b>	<b>294</b>	<b>\$45</b>	<b>\$945,974</b>	<b>\$132,266*</b>

*n*=294, Don't know=12

\*correction at 10 April 2006. Previously reported as \$77,277

In the survey Tasmania was over-represented and NSW was under-represented (compared to Roy Morgan's estimate of the target population).

<sup>15</sup> Percentages in tables may not add to 100% due to rounding.

Most of the advice in the survey was given in July to November 2005, with a few examples from June and December. About a third of the advice was given in September.<sup>16</sup>

Appendix A contains more detailed information about the demographic profile of survey participants.

## **Operation of the survey**

ASIC sought Roy Morgan Research's opinion about the design and operation of the survey. They said:

*'Roy Morgan Research has confidence in the overall methodology and has no reason to doubt that the sample drawn reflects the underlying population of consumers in the market for financial advice that includes advice about superannuation.'*

*'The final sample size of respondents which meet all ASIC's criteria for being in-scope is 306 cases, of which 284 cases involve representatives of Australian financial services licensees. These sample sizes are sufficiently robust to draw conclusions about the advice received.'*

The survey had been widely publicised in the financial planning industry. Several participants noted in their diaries that their advisers mentioned ASIC's shadow shopping survey.

Participants generally did not disclose that they were participating in a survey. Only six participants reported that the adviser became aware they were part of the survey. Five of these advisers continued to provide advice but not all of this advice was compliant.<sup>17</sup>

## **Stage 2: Advice assessed for compliance**

In Stage 2 of the survey, a select group of ASIC staff assessed the participant's examples of advice for legal compliance.

ASIC selected staff who were experienced in file reviews and superannuation issues. The assessment team included people who had worked in the financial planning industry and lawyers. The leader of the assessment team had extensive experience, having previously worked as a financial planner as well as a commercial lawyer, and with formal financial planning qualifications. The team also got specific training in the assessment methodology and the relevant law.

<sup>16</sup> The amount of advice from September (32%) reflects the timing of survey recruiting, not other factors about the advice market.

<sup>17</sup> Of these five cases, advice from three was compliant and one was probably non-compliant. In the remaining case, the advice was clearly non-compliant and the disclosure was non-compliant in major respects.

Staff used a detailed checklist to standardise assessments. The assessment checklist was reviewed after initial pilot testing. To ensure quality control, senior staff cross-checked a proportion of the assessments and cross-checked all assessments where serious advice deficiencies were suspected. Senior staff frequently discussed emerging issues to ensure consistency and check legal interpretations.

We also did not seek to cross-check the information and answers given to us by consumers with the advisers themselves. This would have compromised the confidentiality of the participants and would have changed the nature of the survey entirely. Shadow shopping is a particular type of market research that specifically does not involve the identification of individual consumers to the relevant advisers.

A fuller description of the assessment methodology is in Appendix B.

### **Stage 3: Analysis and reporting**

For each example of superannuation advice, ASIC staff completed a data form. This covered information about the participant, the adviser, the advice and an assessment of legal compliance. After checking, the data was analysed with SPSS statistical analysis software.

Each table contains an ‘*n*=’ figure. This is the size of the valid sample for that particular table. Each table also mentions the number of additional cases that are not shown in the table because answers are unknown or not applicable.

Cases and quotations in the report have been superficially altered to avoid participants from being identified.

## Section 3: Nature of advice

### Profile of advisers

Ninety-three percent of advisers were representatives of Australian financial services licensees (AFSLs). Of the 284 cases of advice from AFSL representatives, most involved financial planners (254). Twenty-two were accountants who were also AFSL representatives. The other AFSL representatives included a few life insurance specialists and advisers employed directly by superannuation funds.<sup>18</sup>

Most of the remaining 22 advisers were unlicensed accountants (18).

The survey specifically recruited people who were seeking professional advice, so this result is not surprising. However, the survey detected two tax agents and two mortgage brokers who should not have been giving any superannuation advice at all and 13 accountants who gave advice outside the limits of their exemption from licensing.<sup>19</sup>

**Table 3: Adviser category**

	Cases	Percent
AFSL representative—accountant	22	7%
AFSL representative—other	262	86%
Accountant (not AFSL representative)	18	6%
Other (not AFSL representative)	4	1%
<b>Total</b>	<b>306</b>	<b>100%</b>

The survey covered 259 advisers and 102 licensees. 35% of the advice came from the eight largest dealer groups (the four major bank conglomerates and the four largest non-bank dealer groups).<sup>20</sup>

Ninety-eight percent of participants only told us about advice from one adviser.<sup>21</sup>

<sup>18</sup> To give financial product advice, a person must either hold an AFS licence personally, be an 'authorised representative' of an AFSL or otherwise be a 'representative' (such as an employee or director of an AFSL). Accountants have a limited exemption, as explained below.

<sup>19</sup> Advice provided by an accountant to acquire or dispose of an interest in a self managed superannuation fund is exempt from being 'personal advice' under the Corporations Act if the accountant is a member of CPA Australia, the Institute of Chartered Accountants in Australia or the National Institute of Accountants: see reg 7.1.29A and 7.1.29. Advice to trustees of a SMSF about investments to be held by the SMSF is not exempt personal advice.

<sup>20</sup> i.e. size in terms of number of representatives

<sup>21</sup>  $n=306$

Fifty-nine percent of participants had received advice from their adviser in the survey (or the adviser's company) before.<sup>22</sup> For some of these, the previous advice was on a different issue (e.g. tax). In other cases the advice was given within a regular annual review with a financial planner.

## Experience of consumers in seeking advice

In 14% of cases, super advice was given to the participant and their spouse at the same time.<sup>23</sup> For the purposes of this survey, this was treated as two cases, because superannuation is specific to the individual.

## Reasons for seeking advice

Participants' most common reasons for seeking advice on superannuation are listed below. Most people had more than one reason.

**Table 4: Reasons for seeking advice**

	Cases	Percent
Increase savings for retirement	217	71%
Advice on super generally	192	63%
Increased performance	141	46%
Pay less tax	127	42%
Get advice on which super fund to choose	102	33%
Consolidate super	72	24%

*n*=306

## Satisfaction with advice and implementation

Most participants intend to follow the advice they were given—53% said they would follow it fully, and 34% partially. Only 3% of people had decided they would probably not follow the advice, with 11% still undecided.<sup>24</sup>

The vast majority of participants (88%) were satisfied with the advice they received.<sup>25</sup> However, care needs to be taken when interpreting this level of satisfaction. Consumers appeared unable to detect serious problems in the advice. Of the advice by AFSL representatives where ASIC judged the advice to clearly lack a reasonable basis, 85% of the consumers were still satisfied with the advice.<sup>26</sup> This suggests that most clients do not have the ability to assess the merits of advice they receive,

<sup>22</sup> *n*=298, Don't know=8

<sup>23</sup> *n*=306

<sup>24</sup> *n*=293, Don't know=13

<sup>25</sup> *n*=258, Don't know=26

<sup>26</sup> *n*=41

and take the advice on trust. For example, several participants were told (incorrectly) that they could not make further contributions to an existing fund.

**Table 5: Satisfaction with advice compared with assessment of reasonable basis for advice (AFSL only)**

	Satisfied	Neutral	Dissatisfied	Total
Compliant	186 (89%)	14 (7%)	8 (4%)	208 (100%)
Probably non-compliant	7 (78%)	1 (11%)	1 (11%)	9 (100%)
Non-compliant	35 (85%)	3 (7%)	3 (7%)	41 (100%)
<b>Total</b>	<b>228 (88%)</b>	<b>18 (7%)</b>	<b>12 (5%)</b>	<b>258 (100%)</b>

*n*=258, Don't know=26

#### Example

Robert was advised to switch to a more expensive fund. The adviser had verbally given the rationale that the new fund was 'a bit more expensive', but Robert would have the benefit of his advice. The SOA did not clearly disclose the costs and did not mention their impact. When contacted by ASIC, Robert was shocked to hear ASIC's calculation that 'a bit more expensive' could reduce his final retirement benefit by over \$100,000.

## Nature of advice given

Most participants received product advice about which fund to choose (73%). Almost half (47%) were given strategic advice about asset allocation and 39% got advice on contribution levels. Surprisingly few consumers were given advice about life and disability insurance issues (21%).

**Table 6: Coverage of advice received—issues**

Issue related to superannuation	Cases	Percent
Selection of super fund	221	73%
Investment issues (asset allocation, investment option) within super	142	47%
Contribution, rollover and withdrawal issues within super	118	39%
Insurance issues related to super	63	21%
Other issues within super	41	14%

*n* ranges from 299–303

The issues on which advice was ultimately given differed somewhat from the advice participants initially sought. More people got advice on fund selection (73% compared to 33% who wanted advice on which super fund to choose).

Where advice was given on fund selection, we looked at the main current fund advised on ('from') and the recommended fund for the future ('to').<sup>27</sup> Where advice was given on fund selection, 60% of participants in retail funds were switched to another retail fund (generally one associated with the adviser's licensee).

In contrast, the majority of participants in government, industry, corporate and self-managed super funds were advised to stay in their current funds.<sup>28</sup> This was often given via informal verbal advice.

**Table 7: Type of main current fund and destination fund**

Main fund advised on	Destination fund type						
	Same fund	Govt	Industry	Corporate	Retail	SMSF	Total
Government	23 (64%)	1 (3%)	2 (6%)	—	9 (25%)	1 (3%)	36 (100%)
Industry	30 (53%)	—	3 (5%)	3 (5%)	17 (30%)	4 (7%)	57 (100%)
Corporate	10 (53%)	—	1 (5%)	—	8 (42%)	—	19 (100%)
Retail	35 (32%)	1 (<1%)	7 (6%)	1 (<1%)	66 (60%)	1 (<1%)	111 (100%)
SMSF	1 (100%)	—	—	—	—	—	1 (100%)
No existing fund	—	—	—	—	3 (60%)	2 (40%)	5 (100%)
Total	99 (43%)	2 (<1%)	13 (6%)	4 (2%)	103 (45%)	8 (4%)	229 (100%)

*n*=229, Not applicable (no advice on fund selection)=68, Don't know (fund not named)=9

Apart from the eight cases of advice to move into a self-managed super fund, several participants were advised that a SMSF was not suitable for them.

## Initial cost of advice

We recorded the initial cost of advice, through either a fee or initial commission if the advice was implemented, or both. Eighty-one percent of the unwritten advice had no upfront cost, while 72% of advice with an SOA did have an upfront cost.

<sup>27</sup> For example, say a consumer has three funds, \$100,000 in a government defined benefit fund, \$50,000 in a corporate fund and \$5,000 in an industry fund. The adviser recommends consolidating the corporate and industry funds into a retail fund. No advice is given on the government fund. This would be categorised as 'main fund advised on: corporate; recommended fund: retail'.

<sup>28</sup> We used a database from APRA to check funds' functional category.

**Table 8: Initial cost of advice and whether verbal or written**

Type of advice given	Initial cost		
	No upfront cost	Upfront cost	Total
Verbal only	72 (81%)	17 (19%)	89 (100%)
Written but no SOA	5 (45%)	6 (55%)	11 (100%)
SOA	37 (28%)	93 (72%)	130 (100%)
<b>Total</b>	<b>114 (50%)</b>	<b>116 (50%)</b>	<b>230 (100%)</b>

*n*=230, Don't know=76

50% of participants paid an upfront fee for the advice.

In a few cases, the fee was primarily for tax or accounting services, with superannuation advice on the side.

We did not record the future remuneration for the adviser through trail commissions, adviser service fees or fee for service. In most cases of advice about a retail fund, the adviser would receive ongoing trail commission if the advice were implemented.

## Conflicts of interest

We recorded whether the adviser's recommendation resulted in an actual conflict of interest for the adviser, if the advice was implemented.

One conflict of interest was where the remuneration paid to the adviser increased because of the particular advice given. 'Increased remuneration' covers a range of remuneration types—commission, salary bonuses based on sales and a salary level dependent on sales targets. 'Increased remuneration' contrasts with situations where the adviser is paid the same, regardless of what action he or she recommends.

### Examples

Adviser A recommends Fred move from an industry super fund to a retail fund. The industry fund does not pay commission. The retail fund pays commission to Adviser A's licensee, and Adviser A will get a proportion of this. The adviser has a conflict of interest through increased remuneration.

Adviser B works on a combination of fee for service basis and commissions (where relevant). Adviser B recommends Fred change investment options within his industry super fund and make extra contributions. The industry fund does not pay commission. Adviser B will not get extra remuneration above his flat fee because of the content of the advice. The adviser does not have a conflict of interest through increased remuneration in respect of this particular advice.

Another conflict of interest was where the adviser recommended an increased investment or life insurance in a product associated with the licensee (such as an in-house fund or other products with ownership links).<sup>29 30</sup>

**Example**

Adviser C is a representative of ABC Financial Planning, which is owned by ABC Bank. Adviser C recommends Fred switch to the ABC Super Fund, also owned by ABC Bank. Adviser C has a conflict of interest as his licensee has ownership links to the recommended product (and will receive management fees as a result).

In 48% of licensed cases,<sup>31</sup> the advice involved an actual conflict of interest around adviser remuneration (the first type of conflict mentioned above). In 38% of licensed cases,<sup>32</sup> the advice involved an actual conflict of interest around a fund associated with the licensee (the second type of conflict mentioned above). In most cases, the two conflicts existed together.

---

<sup>29</sup> We did not record an additional conflict of interest, which is where the advice results in the continuation of a trail commission that the adviser is already receiving.

<sup>30</sup> In some cases the ownership link was readily apparent to us (and we presume the survey participants) as the brand name of the licensee and the product provider were the same. In other cases the names and branding were different and we needed to read the SOA, Financial Services Guide (FSG) or website closely to detect the link.

<sup>31</sup>  $n=269$ , Don't know=15

<sup>32</sup>  $n=264$ , Don't know =20

## Section 4: Findings on compliance

A key element of the survey was to assess advice for legal compliance. Different legal standards apply to different scenarios for superannuation advice.

Scenario for superannuation advice	Cases	Legal obligations
Advice by AFSL representatives	284	Obligations under Corporations Act <sup>33</sup> , ASIC Act and common law.
Advice by accountants within the licensing exemption from the Corporations Act	4	Obligations under conditions of relief from Corporations Act, plus ASIC Act and common law obligations.
Advice by people who are not AFSL representatives, and who are not accountants or tax agents providing advice within the exemption from the Corporations Act	18	In breach of Corporations Act (unlicensed advice). Common law and ASIC Act obligations also apply.

### Level of compliance: authorised representatives

Authorised representatives have two main legal obligations when providing personal financial advice:

- They must understand the client's relevant circumstances and needs, investigate and consider relevant issues about the advice, and provide advice that is appropriate to the client's needs.
- They must provide a written copy of the advice (called a Statement of Advice) within the required time, so the client can make an informed and considered decision whether to follow the advice.<sup>34</sup> This includes:
  - what the adviser recommends the client do;
  - the basis of the advice (the key considerations and why the advice suits the client's needs);
  - the consequences of switching from one product to another (if relevant); and
  - disclosure of any adviser remuneration and relevant conflicts of interest.

The assessment focused on legal compliance and reflects minimum professional standards, not best advice or best practice.

<sup>33</sup> We assessed compliance as though the financial services regulation (FSR) refinements had already become law, i.e. the *Corporations Amendment Regulations 2005 (No. 5)* made on 15 December 2005.

<sup>34</sup> In this report 'Statement of Advice' includes a Statement of Additional Advice.

In most cases, we could form a clear conclusion on compliance. However, we were cautious in cases where we did not have full information or where there may be grey areas in interpreting the facts. Advice or disclosure was categorised as:

- ‘non-compliant’ if it was clearly non-compliant on any view of the facts;
- ‘probably non-compliant’ if it was more likely than not to be non-compliant, but we did not have sufficient information to form a definitive view;
- ‘compliant’ if more likely than not to be compliant; and
- ‘don’t know’ if there was a significant lack of information.

‘Probably non-compliant’ means that the case appeared non-compliant on the available information, but we recognised it was possible (although unlikely) that extra information could move it into the ‘compliant’ category.

We did not seek to cross-check the information and answers given to us by consumers with the advisers themselves. This would have compromised the confidentiality of the participants and would have changed the nature of the survey entirely. Shadow shopping is a particular type of market research that specifically does not involve the identification of individual consumers to the relevant advisers.

## Know your client

The methodology of our survey was not specifically designed to detect shortcomings in the ‘know your client’ obligation. However, in 15% of cases it appeared that the adviser did not know enough about the client’s circumstances or goals (i.e. clearly or probably non-compliant).<sup>35</sup> Where a ‘fact-find’ had been completed, we assumed it was adequate.

Examples of breaches of the ‘know your client’ rule included:

- giving advice for a client’s spouse or children who the adviser had never met;
- giving advice with complex implications to a new client after a five minute discussion;
- advice based on the incorrect assumptions about whether the client did or did not have superannuation choice; and
- recommending the client switch to another fund, but overlooking that the client’s employer would match voluntary contributions to the client’s existing fund but not in the recommended fund.

---

<sup>35</sup> n=265, Don’t know=19

## Reasonable basis for advice

At a broad level we looked at whether the super advice appeared to have a reasonable basis—a key legal obligation.<sup>36</sup> Put simply, we considered that advice did not have a reasonable basis if:

- the adviser had not considered or investigated issues that were critical to the advice given;
- the advice did not fit the client’s needs; or
- the advice was likely to leave the client worse off.

This survey assessed whether advice was legally compliant. We recognised that there will generally be a range of reasonable advice for any individual consumer, not a single correct recommendation. ASIC did not look at whether the ‘best’ advice was given.

Of the cases where we had enough information to form a view, 16% of advice from AFSL representatives was lacking a reasonable basis in some respect (clearly non-compliant), with another 3% probably non-compliant and 80% compliant.<sup>37</sup> This poor advice came from representatives of 24 different licensees, including several large firms.

**Table 9: Overall compliance with reasonable basis of advice (AFSL only)**

	Cases	Percent
Compliant	220	80%
Probably non-compliant	9	3%
Non-compliant	45	16%
<b>Total</b>	<b>274</b>	<b>100%</b>

*n*= 274, Don’t know=10

We also recorded the particular area/s of advice in which that problem arose. We discuss each area of advice below.

<sup>36</sup> Corporations Act, s945A

<sup>37</sup> *n*=274, Don’t know=10 (where we had insufficient detail about aspects of the actual advice). Where the advice or the reasons for advice appeared plausible, we gave the adviser the benefit of the doubt.

**Table 10: Compliance with ‘reasonable basis for advice’ on each issue (AFSL only)**

Issue	Compliant	Probably non-compliant	Non-compliant	Total cases*
Selection of super fund	166 (79%)	7 (3%)	36 (17%)	209 (100%)
Investment issues (asset allocation, investment option) within super	141 (97%)	2 (1%)	2 (1%)	145 (100%)
Contribution, rollover and withdrawal issues within super	145 (91%)	2 (1%)	13 (8%)	160 (100%)
Insurance issues related to super	45 (65%)	4 (6%)	20 (29%)	69 (100%)
Other issues within super	32 (100%)	—	—	32 (100%)

\*Excludes ‘No recommendations on this issue’ and ‘Don’t know’ items

### Selection of super fund

Advice to stay in the current fund was almost always reasonable. Advice to switch funds is discussed on page 33.

### Insurance issues

24% of advice specifically dealt with insurance issues.<sup>38</sup>

Where specific advice was given on insurance issues, it generally appeared compliant (65%).<sup>39</sup> Where the adviser analysed the client’s insurance needs and made a specific recommendation, a reasonable basis was almost always clear. In other compliant examples, the adviser recommended insurance, but left the client to assess the amount needed.

There were fewer than 10 cases where the adviser specifically noted that the client should wait until they were accepted for insurance in a new fund before relinquishing the existing insurance in their current fund. Advisers failing to address this issue risk leaving their clients without insurance if they are refused insurance in the new fund due to ill-health, occupation or other high risk factors.<sup>40</sup>

Problems with insurance issues more often arose where the adviser did not give specific insurance advice. The most common problem was where the adviser recommended a fund switch but appeared to not notice that the client would lose insurance in an existing fund and did not

<sup>38</sup> n=284

<sup>39</sup> n=69, Excludes ‘No recommendations on this issue’ and ‘Don’t know’ items.

<sup>40</sup> We recognise that some advisers may cover this issue at the implementation stage if they are handling all the paperwork for fund transfers.

address whether replacement insurance was needed.<sup>41</sup> Many participants had around \$30,000 insurance cover in their existing fund. In an extreme case, an adviser overlooked that a participant had a default of \$500,000 life and total and permanent disability (TPD) insurance in the current corporate fund, regardless of health.<sup>42</sup> A switch out of this fund was recommended without insurance issues being considered.

### Investment issues

Most advice about investment issues was compliant (97%).<sup>43</sup> This involved either recommending an investment option (e.g. 'balanced', 'growth') or specifying underlying funds in a master trust or rebalancing. Advice was clearly non-compliant where the adviser identified the client's risk profile, but then recommended a quite different asset allocation without any reason being given. Advice was assessed as 'probably non-compliant' where the adviser did not appear to have any process to assess risk issues.

### Fund contribution and withdrawal issues

Most advice on contribution issues had a reasonable basis (91%).<sup>44</sup> Advisers pointed out the benefits of making voluntary contributions in order to qualify for the government co-contribution and the tax benefits of salary sacrifice. Good salary sacrifice advice showed the cash flow implications.

Poor advice made specific recommendations for extra contributions:

- to low income or highly leveraged clients without considering the cash flow implications, or
- to highly leveraged clients without considering the option of repaying debt faster instead.

Cash flow issues are particularly important in superannuation advice, because superannuation savings are usually locked away for years or decades.

#### Example

'Willy and Sue', in their 30s, had saved a considerable lump sum for a deposit on a house. Their adviser recommended they put the money into superannuation to grow their retirement benefit. There was no SOA, and their diary did not mention any warning about the limits on accessing money in superannuation.

<sup>41</sup> ASIC discovered these gaps where the fund had compulsory or default insurance (common in government, corporate and industry funds) by checking the PDS or phoning the fund's customer service line.

<sup>42</sup> In this case and others like it, we attempted to contact the client via Roy Morgan to alert them about a potential issue with the advice.

<sup>43</sup>  $n=145$ , Excludes 'No recommendations on this issue' and 'Don't know' items.

<sup>44</sup>  $n=160$ , Excludes 'No recommendations on this issue' and 'Don't know' items.

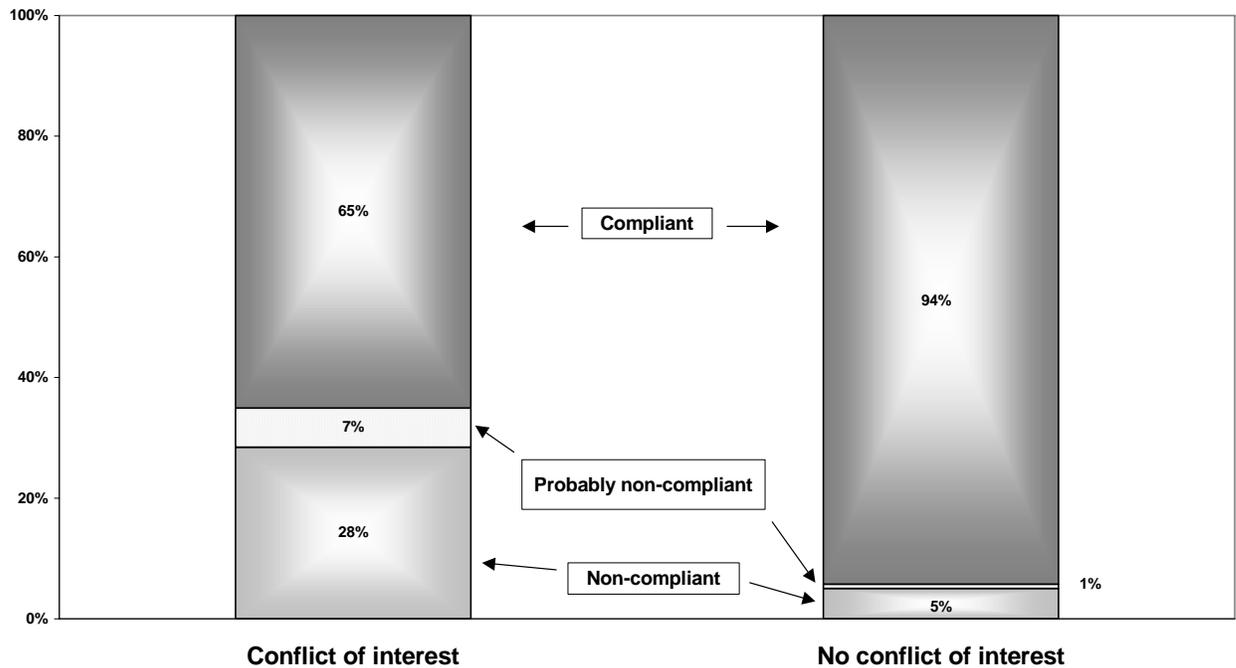
*Correlation between poor advice and conflicts of interest*

As mentioned on page 25, we recorded whether the adviser’s recommendation resulted in an actual conflict of interest for the adviser.

There was a strong correlation between these actual conflicts of interest and authorised representatives giving advice without a reasonable basis.

Where the adviser had a conflict of interest over remuneration, 35% of the advice clearly or probably did not have a reasonable basis in some respect.<sup>45</sup> This contrasts with 6% for advisers that did not have a conflict of interest on remuneration.<sup>46</sup>

**Chart 1: Remuneration conflicts versus reasonable basis for advice (AFSL only)**



Conflict of interest: n=123, Don’t know (compliance level)=5

No conflict of interest: n=139, Don’t know (compliance level)=2

A similar pattern was observed for advisers with a conflict over associated products (e.g. the product provider and the adviser's licensee are in the same corporate group). Where the adviser had a conflict because they were recommending that client invest in an associated product, 32% of the advice clearly or probably did not have a reasonable basis, compared to 11% for advisers who did not recommend associated products.<sup>47</sup>

<sup>45</sup> n=123 , Don’t know=5

<sup>46</sup> n=139, Don’t know=2

<sup>47</sup> Conflict of interest: n=96, Don’t know=4. No conflict of interest: n=161, Don’t know=3

## Analysis where a switch recommended

We looked at whether the advice recommended some kind of switch between funds. Sometimes it was a simple switch from one fund to another. Sometimes the switch was to achieve a consolidation in the number of funds.

Of the consumers with more than one fund, 42% (70 cases) were advised to consolidate.<sup>48</sup> Half of these were advised to consolidate to a new fund, rather than one of their existing funds. Advice to consolidate was generally sound in principle. However, there were often problems with the advice about which fund to consolidate to. Many advisers appeared to have not considered the option of consolidating to an existing fund, such as the fund currently receiving employer contributions.

A switch of some kind was recommended in 44% of cases (124 cases).<sup>49</sup> Advice to switch did not have a reasonable basis in 28% of cases (34 cases), probably did not have a reasonable basis in 5% of cases (6 cases) and was compliant in the remaining 67% (80 cases).<sup>50</sup> Problems arose most often in advice to switch to retail funds—39% of this advice clearly or probably did not have a reasonable basis (33% and 6% respectively).<sup>51</sup>

Examples where no reasonable basis was apparent include:

- Client would be paying higher fees in the new fund but we could not detect any countervailing benefits that related to the client's needs.
- Adviser had not considered that the employer would make bonus contributions if the employee made voluntary contributions to the existing fund.
- Adviser wrongly said that further contributions could not be made to an existing fund.
- Adviser falsely stated that the new fund had better performance history than the current fund, when the historical performance was actually identical or worse.
- Adviser recommended client switch to an in-house retail fund to access particular benefits, all of which were available in the client's existing fund. Advice gave the misleading impression that the client would gain something by switching.

---

<sup>48</sup> n=168

<sup>49</sup> n=281, Don't know=3

<sup>50</sup> n=120 Don't know =4

<sup>51</sup> n=98, Don't know =4

- In many cases, the rationale for the change to a new fund was expressed in marketing language, which was either vague or irrelevant to the client:
  - in several cases, one alleged reason for the switch was ‘consolidated reporting’, but the client was only in one fund to start with;
  - ‘diversification’, when all money is switched out of a fund with a broad spectrum of diversified, multi-manager investment options and switched into a master trust;
  - ‘flexibility’ or ‘choice of investments’ as a reason with no explanation about how this relates to the client’s needs;
  - saying the recommended fund is ‘well regarded’ (or similar);
  - ‘tax advantages’ when the tax situation is the same regardless of which fund is used.

In some cases, the reasons given for the switch either provided no evident benefit to the consumer or were not relevant to their stated needs or personal financial situation. This seemed to be due to the adviser picking standard paragraphs from a template or precedent.

#### **Example**

Mary was 58 and planning to retire from part-time work in two years. She had \$4,000 in an industry fund chosen by her employer. An adviser recommended Mary switch to an in-house master trust, with the stated reason being ‘greater diversification’. Mary’s existing fund had a variety of investment options, each of which was diversified by both asset classes and underlying fund managers.

Very few advisers recommended a change of funds on the basis that the new fund was likely to deliver higher net returns for a given risk profile. For the purposes of this survey, we always accepted the adviser’s opinion in such cases. Where the adviser highlighted that the switch to a master trust would result in a wide choice of underlying funds, we did not presume that the adviser would be able to select future out-performing funds unless the adviser specifically claimed a track record in this regard.

In some cases it was clear that the adviser had a sound knowledge of the client’s current fund. However, in many cases the adviser did not have sufficient knowledge. In a few cases, the employer matched voluntary contributions by the employee—a critical consideration.

The most common oversight was to ignore the insurance that the consumer had in their current fund. Many government, corporate and industry funds have compulsory or default insurance. In some of the cases where consumers were advised to switch out of these fund types, the consumer had existing insurance but the adviser did not deal with the issue.

Several advisers did a clear comparison of the fees where lower fees were a key reason in recommending a switch. In two other cases the adviser said that the recommended fund was cheaper, but it was actually more expensive. In several cases the adviser said that the recommended fund had higher fees but had other benefits, although the amount of the extra fee was not stated. In the vast majority of cases consumers were not provided with a fee comparison, even where the difference in fees was quite significant.

Where a switch was recommended (including to achieve consolidation), we looked at whether this would result in higher or lower fees. While the level of fees is obviously not the only factor that an adviser would consider, it is nearly always *one* of the relevant factors. Fees have a particular impact in long term products like superannuation. The fees are particularly relevant given (as mentioned above) few advisers recommended a switch on the grounds that the new fund was likely to deliver higher investment returns.

**Table 11: Switch/consolidation: leading to higher fees in new fund**

	Cases	Percent
Higher fees	53	62%
About the same	14	16%
Lower fees	19	22%
<b>Total</b>	<b>86</b>	<b>100%</b>

*n*=86, Don't know=38

Where relevant information was available<sup>52</sup>, we compared the fees in the recommended fund against the fees in the client's existing fund currently receiving employer contributions. This is an alternative that the adviser should generally have considered.<sup>53</sup>

The switch or consolidation would have resulted in higher fees in 62% of cases.

We then looked more closely at the 40 cases where advice to switch funds clearly or probably did not have a reasonable basis. We used the ASIC superannuation calculator<sup>54</sup> to estimate the consumer's retirement

<sup>52</sup> In 38 cases, we had insufficient information on the exact fund identity (e.g. we only had the brand name, not the exact fund) or the fund had several divisions with different fees. Where exact fund was known, we were able to research the fees via the PDS or a call to the fund. Comparative fee information was rarely provided in SOAs.

<sup>53</sup> The comparison was only done where the consumer had the option of staying in their current fund. Consumers are sometimes unable to stay in their current government or corporate fund or make further contributions after they have left the employer.

<sup>54</sup> The calculator is on ASIC's consumer website at [www.fido.gov.au](http://www.fido.gov.au). The site also has a guide that explains the calculator's assumptions and methodology.

benefit under both funds, assuming they achieved the same gross investment returns and the fees remained constant.<sup>55</sup>

In 43% of the cases (17 out of 40), the consumer had not been given the raw information necessary to compare the cost of funds (e.g. in an SOA) and ASIC could not obtain the information from public sources (e.g. look up a PDS). This meant that ASIC could not compare the cost of funds, and that the consumer probably could not compare the cost either (without further research).

The following table shows the projected difference in retirement benefit (where we could calculate it) for the cases where advice to switch funds clearly or probably did not have a reasonable basis. The difference in retirement benefit is expressed in today's dollars, assuming the same gross investment returns and constant fees.

**Table 12: Projected benefit difference on retirement—for switching advice that clearly or probably lacked a reasonable basis**

Case	Projected benefit with existing fund	Projected benefit with recommended fund	Dollar difference	Percentage difference
1	\$355,000	\$220,000	-\$135,000	-38%
2	\$207,000	\$143,000	-\$64,000	-31%
3	\$312,000	\$219,000	-\$93,000	-30%
4	\$425,000	\$316,000	-\$109,000	-26%
5	\$133,000	\$99,000	-\$34,000	-26%
6	\$75,000	\$56,000	-\$19,000	-25%
7	\$238,000	\$180,000	-\$58,000	-24%
8	\$32,000	\$25,000	-\$7,000	-22%
9	\$19,000	\$15,000	-\$4,000	-21%
10	\$61,000	\$49,000	-\$12,000	-20%
11	\$200,000	\$163,000	-\$37,000	-19%
12	\$182,000	\$153,000	-\$29,000	-16%
13	\$113,000	\$98,000	-\$15,000	-13%
14	\$992,000	\$874,000	-\$118,000	-12%
15	\$225,000	\$200,000	-\$25,000	-11%
16	\$437,000	\$392,000	-\$45,000	-10%

<sup>55</sup> This is a reasonable assumption, as few advisers recommended new funds on the basis that they were likely to earn higher investment returns. It was also rare for a switch to be recommended on the grounds that the existing fund lacked features that were essential to meet the client's goals.

Case	Projected benefit with existing fund	Projected benefit with recommended fund	Dollar difference	Percentage difference
17	\$99,000	\$89,000	-\$10,000	-10%
18	\$210,000	\$196,000	-\$14,000	-7%
19	\$395,000	\$371,000	-\$24,000	-6%
20	\$83,000	\$79,000	-\$4,000	-5%
21	\$19,000	\$19,000	\$0	0%
22	\$190,000	\$191,000	\$1,000	1%
23	\$122,000	\$125,000	\$3,000	2%

n=23, Don't know=17

Of these switching cases that clearly or probably lacked a reasonable basis, the average hypothetical difference in retirement benefit was a reduction of \$37,043 or -16%.<sup>56</sup> The adviser had a conflict of interest in respect of remuneration in all of the 23 cases. The adviser also had a conflict of interest in recommending an 'in house' product in 70% of the cases.

In these 23 cases, only one adviser gave the likelihood of higher investment returns as a consideration in recommending the switch.

#### Example

The case where fee impact was greatest involved 'Eric', a 30 year old. The fees with Eric's existing fund were:

- ongoing fees 0.4% of assets;
- \$52 pa management fee; and
- insurance premiums \$1,200

Fees with recommended fund:

- ongoing fees 2.3% of assets;
- 1% fee on initial and future contribution; and
- insurance premiums \$1,600 for same amount of cover.

Eric's projected retirement benefit (in today's dollars) was reduced from \$355,000 to \$220,000 (a reduction of 38%).

The advice resulted in higher remuneration to the adviser and the recommended fund was associated with the licensee.

<sup>56</sup> The apparent anomaly of 'no reasonable basis for switch' cases showing a higher return arises because the switch might be unreasonable on some other issue, such as lost insurance.

## SOA provided

Advice can be provided verbally or in writing. If initial advice is provided verbally, the adviser is generally required to provide a written Statement of Advice soon afterwards. In general, the SOA must be provided as soon as practicable, but at least before further services are provided (such as implementing the advice).<sup>57</sup>

In assessing whether an SOA should have been provided, we assessed cases as though the financial services regulation (FSR) refinements had already become law.<sup>58</sup> Therefore, in our survey of personal financial advice, an SOA was not required where:

- advice merely confirmed or implemented advice in an earlier SOA, and the basis of advice had not changed; or
- advice was within the accountant's licensing exemption from the Corporations Act.

At the end of the survey, Roy Morgan recontacted relevant participants to double-check that an SOA had not been received.

Where an adviser was required to give a written SOA, 52% of the advisers complied.

**Table 13: SOA provided by AFSL representatives**

		Cases	Percent
Compliant	SOA given where required	147	52%
Compliant	SOA not required	5	2%
Not compliant	SOA not given where required	132	46%
<b>Total</b>		<b>284</b>	<b>100%</b>

*n*=284

In 46% of cases (132 cases), AFSL representatives failed to provide an SOA where one was required. Consumers missed out on SOAs in a wide range of advice situations. The following discussion explores these situations.

- About 23% of the verbal advice cases (30 cases) were simply a hold recommendation<sup>59</sup>, such as 'You are in a good fund and I recommend you stay where you are'. Advisers only had a conflict of interest in 3 of the 30 verbal hold recommendations. Only 3 out

<sup>57</sup> In time critical situations, the SOA can be provided within five days of the advice being implemented.

<sup>58</sup> *Corporations Amendment Regulations 2005 (No. 5)* made on 15 December 2005

<sup>59</sup> *n*=132. This percentage excludes cases where an SOA is not required under FSR refinements.

of the 30 verbal hold recommendations clearly or probably lacked a reasonable basis.<sup>60</sup>

- About a third of the verbal advice could (and should) have been phrased as general advice, with a general advice warning. Many consumers appeared to presume that all comments by an adviser amounted to personal advice, unless very carefully labelled as general advice.<sup>61</sup>

#### **Examples of the boundary between general and personal advice**

A consumer has a brief chat with a financial planner at the bank. The adviser says: 'For people who have more than 10 years until they can access their super, short-term ups and downs in market values are unlikely to be a problem. If you are in this category, you should consider how much of your super to have in growth assets that go up and down in value, but have historically shown higher returns over the long term.' This is likely to be 'general advice'.

If the adviser finds out a bit about the consumer's circumstances and says: 'I think you should be in the growth option rather than the conservative option in your super fund', the adviser has given 'personal advice'.

A consumer has a quick chat with her planner. The adviser says: 'Your current fund has low fees and above average performance. You should consider whether your existing fund is meeting your needs before deciding to switch funds.' This is likely to only be considered as factual information and general advice.

- Where the adviser failed to provide an SOA, some of the advice was 'incidental'. This occurred in two main scenarios:
  - An adviser was having a preliminary 'getting to know each other' meeting before the client decided whether to engage the adviser and pay for formal advice. Instead of the adviser just identifying the issues that would be explored in formal advice, the adviser started making recommendations (e.g. 'you should be putting more money into your XYZ super fund').
  - The adviser was giving formal advice on some other issue (investments outside super, annual tax return) and gave verbal superannuation advice on the side. In extreme cases, a few advisers made recommendations for a person they had never met, such as the client's spouse or adult children.
- In 30% of the cases (39 cases), switching or consolidation was recommended.<sup>62</sup> An SOA is required in almost all these situations where specific funds are recommended and failure to provide an SOA represents a serious breach.

<sup>60</sup> One case had both conflicted and unreasonable advice.

<sup>61</sup> Where the advice was actually phrased as general advice, it was excluded from the survey.

<sup>62</sup> n=130, Don't know=2

- In a few cases, the adviser gave detailed verbal advice and said that an SOA would be completed if the client decided to accept the recommendation. This practice prevents the consumer from being able to make a considered assessment of the advice they have been given, and is clearly illegal. For example:
  - ‘I will give you my advice verbally, but you will have to pay \$600 if you want a written Statement of Advice.’
  - ‘I will do an SOA if you decide you want to implement the advice.’

Where an SOA was not provided when required, most had no upfront cost (although if implemented some cases would have generated trail commission). Of the cases where cost information was available, 77% had no upfront cost (61 cases).<sup>63</sup>

## SOA content

### Disclosure of basis of advice

The law requires that an SOA disclose the basis of the advice.<sup>64</sup> In practice, this involves disclosing the adviser’s key considerations in making the recommendations, including how the advice is appropriate to the client’s needs.

For AFSL representatives, we assessed whether the basis of advice had been disclosed for each superannuation issue where advice was given.

Overall, adequate disclosure of the basis of advice was a widespread problem. The following table summarises the overall compliance with disclosure of the basis of superannuation advice.

**Table 14: Overall compliance with disclosure of ‘basis of advice’ (AFSL only)**

	Cases	Percent
SOA compliant	83	29%
SOA probably non-compliant	27	10%
SOA non-compliant	37	13%
SOA not given where required	132	46%
SOA not required	5	2%
Total	284	100%

*n* = 284

SOAs were generally clear about the recommended action, but at times ASIC analysts had difficulty following the reasons for the advice.

<sup>63</sup> *n*=79, Don’t know=53

<sup>64</sup> See explanation of ‘basis of advice’ on page 29. See also Corporations Act s947C(2)(b) and ASIC Policy Statement 175 *Licensing: Financial product advisers—conduct and disclosure* at [PS 175.126].

Advice about fund selection was an area of noted compliance difficulty for advisers. Of the 212 consumers who were given assessable advice about fund selection, only 33% received relevant disclosure that was clearly compliant.<sup>65</sup> Twenty-six percent received an SOA with substandard disclosure (clearly or probably non-compliant—55 cases), and 41% received no SOA at all (87 cases, generally ‘stay where you are’ advice).

Advice about contribution and withdrawal issues often overlapped with fund selection advice. Our impression was that disclosure was better where advice was purely about contribution issues (salary sacrifice, co-contribution, etc).

Fee information in the SOA was sometimes incomplete, inconsistent or fragmented across different parts of SOA. Where fees were a key consideration in the advice, this meant that the basis of advice was not clearly disclosed.

**Table 15: Disclosure of ‘basis of advice’ on each advice issue (AFSL only)**

Issue	SOA compliant	SOA probably non-compliant	SOA non-compliant	No SOA given: non-compliant	Total cases*
Selection of super fund	70 (33%)	29 (14%)	26 (12%)	87 (41%)	212
Investment issues within super (e.g. asset allocation)	95 (64%)	8 (5%)	6 (4%)	39 (26%)	148
Contribution, rollover and withdrawal issues within super	72 (44%)	13 (8%)	15 (9%)	65 (39%)	165
Insurance issues related to super	35 (53%)	7 (11%)	10 (15%)	14 (21%)	66
Other issues within super	21 (64%)	4 (12%)	1 (3%)	7 (21%)	33

\*Excludes ‘No recommendations on this issue’ and ‘Don’t know’ items

## Disclosing the consequences of replacing funds

Where an adviser recommends replacing one financial product with another (in full or partly), the adviser is required to disclose the costs and consequences of the change.<sup>66</sup> ‘Replacing’ includes consolidating, other switching, and transferring contributions from one fund to another fund.

Of the consumers who were advised to replace one product with another, only 20% received compliant written disclosure about the consequences of the recommended change:<sup>67</sup>

- 39 (32%) did not receive an SOA at all (although it was required);
- 39 (32%) received an SOA with clearly non-compliant disclosure;

<sup>65</sup> n=212

<sup>66</sup> Specifically required by Corporations Act, s947D. Where these issues are a key consideration in the basis of advice, disclosure is also required by s947C(2)(b).

<sup>67</sup> n=121, Don’t know=3 (where the underlying facts about switching consequences were unclear)

- 19 (16%) received an SOA with disclosure that was probably non-compliant; and
- 24 (20%) received an SOA with compliant disclosure.

Common shortcomings in disclosure related to:

- exit fees from existing fund;
- loss of automatic insurance cover in the existing fund;
- losing access to insurance in existing fund before being accepted by the insurer in the new fund; and
- the likelihood of reduced net returns due to higher fees in the new fund (other things being equal).

ASIC analysts only recalled a handful of cases where the SOA stated that the adviser could not obtain relevant information for s947D disclosure.<sup>68</sup> In one of these cases, ASIC staff obtained the relevant information with a three-minute phone call to the fund.

**Table 16: Disclosure breaches on each s947D element (AFSL only)**

Issue	Compliant	Probably non-compliant	Non-compliant	Total cases*
Exit costs on from fund	52 (63%)	8 (10%)	23 (28%)	83 (100%)
Entry costs on to fund	73 (86%)	4 (5%)	8 (9%)	85 (100%)
Lost benefits	42 (52%)	10 (12%)	29 (36%)	81 (100%)
Other significant consequences	40 (49%)	17 (21%)	24 (30%)	81 (100%)

\*Excludes 'No SOA/no switch' and 'Don't know' items

When the required disclosure was done thoroughly, it provided clear and readable information. In a few cases, the SOA template had a clear structure for showing the comparative features of the old and new products. Where these tables were completed with short, objective information on key issues relevant to the client, they provided a useful summary. The table information was complemented with the explanation of 'why' the recommended fund was appropriate for the client and the consequences of switching. Together, this provided excellent disclosure of the basis of the advice and the consequences of switching.

In most cases, however, comparative information was unclear, where it existed at all. Some SOAs separated the s947D disclosure away from the recommendation to switch, and located it in a 'legal disclosures' section towards the back of the SOA. This made it harder for a consumer to assess the recommendation and reduces the effectiveness of the SOA.

<sup>68</sup> Unless it was obvious that the adviser had not taken reasonable steps to obtain the information, these cases were rated as compliant.

The findings on this issue are consistent with the problems identified in ASIC's Superannuation Switching Report, released in August 2005.

## Disclosing conflicts of interest

Disclosure of adviser remuneration and conflicts of interest appeared to be compliant in most cases where an SOA was given, although there is room for improvement (73% compliant, 15% probably non-compliant, 12% non-compliant). This assessment is only an estimate based on obvious omissions. While we could verify some commission levels using the PDS, other remuneration or conflicts could not be verified without independent information from the licensee.

**Table 17: Disclosure of remuneration and conflicts of interest (AFSL only)**

	Compliant	Probably non-compliant	Non-compliant	Total cases
Remuneration and conflicts disclosure	108 (73%)	22 (15%)	17 (12%)	147 (100%)

*n*=147

## Quality and length of SOAs

Out of interest, we recorded the number of pages in SOAs.<sup>69</sup> The average total length of SOAs was 39 pages with an average of 25 pages in the main body of the SOA and 18 pages in the SOA attachments.<sup>70</sup>

Having seen many examples of written advice in this survey and earlier surveys, our impression is that the overall standard of disclosure has improved since the introduction of the Financial Services Reform Act.

## Level of compliance: unlicensed advisers

This section covers the 22 cases in the survey involving advisers who were *not* representatives of AFSLs. This included 18 unlicensed accountants, two tax agents and two mortgage brokers. (The 22 accountants who were also authorised representatives of AFS licensees were covered in the previous sections).

In some limited circumstances, accountants can give advice on superannuation issues without needing to come within the AFS licensing regime. In broad terms, these include:

- advice to set up a self managed superannuation fund;<sup>71</sup> and

<sup>69</sup> The number of pages is obviously not the only factor in whether an SOA is clear concise and effective. However, consumers are less likely to read long SOAs.

<sup>70</sup> In four cases, the overall length was unknown as we received the main part of the SOA but not all the attachments.

<sup>71</sup> Advice provided by an accountant to acquire or dispose of an interest in a self managed superannuation fund is exempt from being 'personal advice' under the Corporations Act if the accountant is a member of recognised accountants body (CPA

- advice on the tax implications of superannuation products, so long as there is a written warning that other factors may be relevant and the client should seek advice from a licensed adviser.<sup>72</sup>

In four cases the unlicensed accountant stayed within the accountant's exemption. In some of these cases, the consumer's recount of the advice session showed that the unlicensed accountant had a very clear understanding about the limits of the advice he could give. The advice appeared reasonable in all four cases.

However, in 16 other cases, 14 unlicensed accountants and two tax agents<sup>73</sup> illegally gave advice on issues that required a licence. These cases included:

- advising the client about particular superannuation funds (not SMSFs), including staying with an existing fund, consolidation and asset allocation decisions within funds; and
- recommending making extra contributions to a specific super fund to access tax benefits, without warning that other factors may be relevant and the client should seek advice from a licensed adviser.

The advice from unlicensed accountants and tax agents was problematic in several ways:

- All the advice was verbal. This meant that consumers may not accurately recall the fine detail of the advice. There is also more potential for misunderstanding about the limits of advice.
- It was unclear whether the accountant was trained and competent to give the relevant advice. It was often unclear to ASIC whether the adviser had done any research before offering the advice, or it was just an 'off the cuff' opinion. Survey participants, however, seemed to presume they had received professional advice.

Only two unlicensed accountants appeared to have warned that tax is not the only relevant factor in financial product advice, and that the client should seek advice from a licensed adviser. None of the unlicensed accountants or tax agents gave this warning in writing, as legally required.

The survey also revealed two examples of unlicensed mortgage brokers providing superannuation advice (apart from accountants and tax agents). One gave advice despite being aware he/she was not authorised to do so. The second person appeared to be a back office person.

---

Australia, the Institute of Chartered Accountants in Australia or the National Institute of Accountants): see reg 7.1.29A and 7.1.29.

<sup>72</sup> For more information on the limits of advice by accountants who are not AFSL representatives, see FSQ 10 *'Do the AFS licensing requirements apply to accountants?'* and FSQ 123 *'I am an accountant. What advice can I provide about self managed superannuation funds (SMSFs) and related activity under reg 7.1.29?'* on ASIC's website at [www.asic.gov.au](http://www.asic.gov.au).

<sup>73</sup> The two tax agents gave superannuation advice during a consultation on annual tax returns.

## Section 5: Broader observations

After looking at the examples of financial advice in the survey and reading consumers' diaries about seeking advice, this section makes some observations that are broader than the legal compliance issues. They are based on our impressions, rather than statistical findings.

### **The advice market involves many levels of assistance**

The financial advice market covers many different levels of assistance. Many consumers only receive general advice or factual information. A significant number have preliminary meetings with advisers, but do not go on to receive formal advice.

This is a much wider group than what advisers would consider their 'formal clients'. This has implications for business systems and compliance monitoring.

### **The value of strategic advice**

In the process of financial planning, there is a distinction between strategic advice and product advice. By strategic advice, financial planners mean issues like:

- how much to contribute to meet the client's retirement goals;
- appropriate level of insurance cover;
- appropriate asset allocation, given client's goals and risk profile;
- investing in the most tax effective way (e.g. salary sacrifice, via super, etc);
- maximising after-tax income in retirement by considering social security and tax factors; and
- becoming eligible for the government co-contribution.

The strategy is separate from the particular financial product used to implement the strategy.

Strategic advice, where given, generally appeared beneficial for the client (often highly beneficial), even if the advice was quite simple. We saw many cases where advice did not address some strategic issues (e.g. insurance cover, retirement goals) and therefore could have been even more valuable.

Although most advice included advice on fund selection, in many cases it was unclear whether advice to switch was adding value. In some cases it may well have been eroding value for the client.

## **The practical limits of disclosure**

Several findings from the survey and our impressions from the material are relevant to the debate about the limits of disclosure.

In the majority of cases, consumers were only presented with one option on each issue. Their choice was whether or not to accept the adviser's recommendation.

Superannuation can be a complex area. Our impression is that many participants had limited knowledge of the issues being considered. In many cases, the consumer would have been unaware of key issues or options (e.g. insurance, fees, fund types) if the adviser did not discuss them.

Survey participants were rarely able to tell whether or not the advice they received had a reasonable basis. In the majority of cases where ASIC staff could see major shortcomings in the advice (e.g. was likely to leave the consumer worse off), consumers thought the advice was satisfactory and said they intended to follow it. This is not surprising since consumers are generally not expert in these matters and that is why they were seeking professional advice in the first place.

While SOAs generally disclosed the adviser's conflicts of interest, it is hard to see how consumers could use this information to judge whether the conflicts had influenced the advice. Although we did not ask specifically, the commentary in the consumer diaries suggested most consumers simply trusted that the adviser's recommendation was in their (the consumer's) interest. The anecdotal evidence gave us the impression that the typical consumer did not readily appreciate the impact that various conflicts of interest could have on the quality of the advice they were given.

While disclosure is a critical part of consumer protection, this survey suggests that disclosure can only play a limited role in protecting consumers from inappropriate or biased advice.

## **Some signs of selling rather than advising**

Where the adviser recommended a switch to a commission paying fund or an in-house fund, much of the fund selection advice gave the impression of 'selling' rather than impartial advice. The reasons given for the switch were often vague or one-sided and sometimes appeared irrelevant to the individual consumer. This contrasted with the advice on strategic issues, which tended to be tightly focused on the consumer's particular needs and with clearer reasons.

Recommending a switch to a commission paying fund or an in-house fund is not necessarily inappropriate in all cases. However, it again

highlights an area where licensees should ensure that advisers recognise their responsibility to advise their clients properly and not simply sell products.

### **Disclosure has improved but needs to be more effective**

Our impression is that the Financial Services Reform Act has forced licensees to be more organised about disclosure. Disclosure is generally more complete than it used to be.

However, often the information in SOAs was unnecessarily fragmented and complex.

### **Hard to get simple, compliant advice**

After looking at the anecdotal comments from survey participants and the compliance assessment, we suspect it is difficult for consumers to find good, compliant advice on simple issues. This particularly applies when consumers just need strategic advice about decisions within their current fund. Some participants with small amounts in super reported difficulty getting advice, but so too did a few participants with large amounts in super in non-retail funds.

- Funds could investigate including simple strategic advice within the fund's ancillary services.
- Due to the legacy of commission-based insurance selling, many consumers are not used to paying for financial advice. When seeking professional financial advice for their personal circumstances, consumers should expect to pay for the advice, just as they would pay a tax accountant, doctor, or lawyer.

## Section 6: Follow-up action and future directions

This section notes future action by ASIC and suggests future directions for licensees and industry generally.

### Issues for ASIC

#### ASIC compliance action

The broad legal framework is that licensees (e.g. financial planning firms and banks) supervise their representatives who give advice. Licensees are required to take reasonable steps to ensure that their representatives comply with the law, through training, establishing work systems and monitoring.

The survey findings raise concerns that not all licensees are taking adequate steps to ensure their representatives comply with the law. We will be writing to all licensees who had one or more advisers in the survey and bringing relevant issues to their attention. After account of the survey findings and other intelligence about individual licensees (including in a number of cases, surveillance activities already underway), we propose to conduct specific follow-up action for 14 licensees. ASIC will be checking whether these licensees have serious or widespread problems with their systems. We then aim to ensure any problems are fixed.

We will focus our future compliance activities on the following areas:

- *Conflict handling arrangements*— We will look at whether licensees are taking account of ASIC’s guidance on conflicts,<sup>74</sup> the findings of this report and earlier ASIC reports (such as the Superannuation Switching Surveillance Report). ASIC’s work will recognise the higher risk of non-compliance that arises where advisers have conflicts of interest.
- *Adequate training and tools*— We will look at the extent to which licensees are providing appropriate resources to their representatives to help them comply with their obligations. These resources include training on relevant products, training on general advice and when SOAs are required, research services, assistance in completing SOAs, and the circumstances where it is not appropriate to recommend product switches.
- *Compliance monitoring and testing*— Licensees need processes to satisfy themselves that they and their representatives are complying with their legal obligations. We will look at whether

<sup>74</sup> Such as Policy Statement 181 *Licensing: Managing conflicts of interest* [PS 181].

licensees have adequate monitoring and testing procedures, and that these processes work in practice.

- *Breach rectification processes*—We will look at whether licensees have adequate processes in place to remedy breaches detected by their compliance monitoring. These include notification of clients and ASIC, compensation processes and disciplinary action against representatives who breach their obligations.

We also have a project underway focusing on the provision of advice by unlicensed advisers.

### **Verbal hold recommendations**

To facilitate access to simple advice, ASIC (in consultation with Treasury) will consider whether the obligation to provide an SOA should be waived where:

- the advice is merely to continue the consumer's current arrangements (e.g. 'stay in your current fund');
- the advice is free; and
- the adviser and the adviser's licensee do not have any conflicts of interest that require disclosure.

The survey suggests that such advice is common and that the risk of inappropriate advice is low.

### **Conflicts of interest**

It is clear from this survey that conflicts of interest bring a higher risk of inappropriate advice. Common conflicts include remuneration that is dependent on the actual advice (e.g. commissions or bonuses) and recommending the products of a company associated with the licensee.

Licensees and advisers have traditionally relied heavily on disclosure to manage these conflicts. However, disclosure (even where comprehensible) is not an adequate response where the conflict still leads to advice that is inappropriate or compromises the client's interests.

We will hold discussions with relevant licensees and industry associations about the issue of further guidance by ASIC and/or industry on how such conflicts might best be managed and what conflicts need to be avoided by licensees.<sup>75</sup>

---

<sup>75</sup> The Financial Planning Association has recently released 'Principles to Manage Conflicts of Interest' (March 2006).

## Our expectations of industry

We expect industry will focus attention on the key issues highlighted in this survey. Industry projects are already underway on some of these issues.

### Consolidation advice

Despite the potential benefits of good consolidation advice, advisers appeared to struggle to deliver consolidation advice that was beneficial for the consumer, legally compliant and commercially practical. ASIC expects industry to work on how consolidation advice can be facilitated and ASIC will work with industry on this outcome.

### Inquiry process for client's existing funds

Industry has commenced a project to develop (in conjunction with ASIC) a standard fund inquiry form. ASIC expects industry to progress this work as a priority. The form could be used where the adviser needs to get details about the client's interest in their current fund. ASIC believes that a standard form would allow advisers and funds to process requests faster and at lower cost.

### Providing SOAs where required

The survey showed a large number of cases where SOAs were not provided when required. However, ASIC believes most of this problem can be resolved relatively easily.

Advisers and their licensees need to revise their practices to ensure an SOA is given where required. Written advice needs to be seen as an integral part of quality advice which assists consumers make an informed decision, not a legal obstacle to be evaded where possible.

Depending on the circumstances, the adviser can:

- give unwritten *general* advice that is clearly framed as such, with an appropriate warning;<sup>76</sup>
- give personal advice with a written Statement of Advice (which often only needs to be brief);
- give verbal personal advice where allowed by the FSR refinements (such as confirming earlier written advice); or
- give unwritten factual information without any implied recommendation, and let the clients come to their own conclusions.

---

<sup>76</sup> See ASIC's FAQ on general advice (QFS 158) and ASIC's Policy Statement 175 *Licensing: Financial product advisers—conduct and disclosure* [PS 175].

## Preventing bad switching advice

Licensees need to review their systems to ensure any switching advice is compliant:

- While advisers generally appeared competent on fundamental issues, licensees need to ensure their representatives meet [PS 146] training standards<sup>77</sup> on the generic features of the products they advise on (especially industry, corporate and government super funds and insurance arrangements).
- Advisers can access research tools that show key features of common funds (such as fees and default compulsory insurance arrangements) as a first step in providing advice about non-retail funds. Such research tools are now available.
- Licensees should ensure their advisers make adequate inquiries about their client's particulars with their current funds. ASIC has commenced discussions with industry on developing a standard fund inquiry template to speed up this process.
- Licensees should ensure SOAs fairly summarise the advantages and disadvantages of switching. Where a switch is recommended to a higher fee fund, SOAs should have a clear *summary* of the differences in fees and their long-term impact.<sup>78</sup> Licensees should incorporate this information in their SOA templates.
- Licensees should ensure switching is only recommended where it is not contrary to the client's interests.

## Insurance issues

Advisers need to give more consideration to insurance issues when advising on superannuation. Selecting a suitable superannuation fund may depend on the client's insurance needs as well as their investment needs. Clients can inadvertently lose insurance cover when switching funds or stopping contributions to a particular fund.

## Explaining *why* the action is recommended

In many cases, consumers received poor disclosure about *why* the recommended action would be in their interests. Disadvantages were often overlooked. Advisers and licensees need to ensure consumers can make an informed decision whether to accept the adviser's advice, by having an objective summary of the major advantages and disadvantages.

<sup>77</sup> ASIC's Policy Statement 146 *Licensing: Training of financial product advisers* [PS 146].

<sup>78</sup> See s947D (disclosing consequences of switching) and s947(2)(b) (disclosing the basis of the advice).

### **Supervision and compliance monitoring**

Licensees have an obligation to take reasonable steps to ensure their representatives are complying with the law. The fact that ASIC's survey found widespread breaches suggests that licensees need to review and, if necessary, improve their supervision and compliance monitoring systems. ASIC plans to look at licensees' systems and whether they work in practice.

### **Illegal advice by accountants**

All accountants need to review their business practices on superannuation advice to ensure they comply with the Corporations Act. They should either become AFSL representatives, or confine themselves to issues on which unlicensed accountants can legally give advice.

# Appendix A: Detailed demographic information

The following data refers to the 306 examples of advice in ASIC's compliance assessment.

**Table 18: Amount in superannuation (grouped)**

	Cases	Percent	Target population (Roy Morgan)
Less than \$5,000	12	4%	5%
\$5,000–\$24,999	53	18%	23%
\$25,000–\$49,999	54	18%	19%
\$50,000–\$99,999	57	19%	18%
\$100,000–\$249,999	73	25%	20%
\$250,000 or more	47	16%	14%
<b>Total</b>	<b>296</b>	<b>100%</b>	<b>100%</b>

ASIC cases:  $n=296$ , Don't know=10

Roy Morgan:  $n=1,228$ , Don't know=367

**Table 19: Amount in superannuation by age**

	Cases	Minimum	Maximum	Average amount in super
18–24	5	\$300	\$15,213	\$5,106
25–34	29	\$2,900	\$114,000	\$30,150
35–49	107	\$50	\$690,000	\$85,330
50+	153	\$45	\$945,974	\$188,525
<b>Total</b>	<b>294</b>	<b>\$45</b>	<b>\$945,974</b>	<b>\$132,266*</b>

$n=294$ , Don't know=12

\*correction at 10 April 2006. Previously reported as \$77,277

**Table 20: Age groups**

	Cases	Percent	Target population (Roy Morgan)
18–24	5	2%	3%
25–34	31	10%	14%
35–49	113	37%	42%
50+	155	51%	40%
<b>Total</b>	<b>304</b>	<b>100%</b>	<b>100%</b>

$n=304$  Don't know=2

Roy Morgan:  $n=1,595$

**Table 21: Gender**

	Cases	Percent	Target population (Roy Morgan)
Male	177	58%	55%
Female	128	42%	45%
<b>Total</b>	<b>305</b>	<b>100%</b>	<b>100%</b>

*n*=305, Don't know=1./ Roy Morgan: *n*=1,595

**Table 22: Income levels**

	Cases	Percent	Target population (Roy Morgan)
Less than \$5,000	4	1%	N/A
\$5,000–\$24,999	39	13%	N/A
\$25,000–\$49,999	112	37%	N/A
\$50,000–\$99,999	128	42%	N/A
\$100,000–\$249,999	18	6%	N/A
\$250,000 or more	1	<1%	N/A
<b>Total</b>	<b>302</b>	<b>100%</b>	<b>N/A</b>

*n*=302, Don't know=4

**Table 23: State where advice given**

	Cases	Percent	Target population (Roy Morgan)
ACT	6	2%	2%
NSW	55	18%	26%
NT	2	1%	1%
QLD	69	23%	21%
SA	29	10%	10%
TAS	40	13%	8%
VIC	79	26%	23%
WA	24	8%	8%
<b>Total</b>	<b>304</b>	<b>100%</b>	<b>100%</b>

*n*=304, Don't know=2 / Roy Morgan: *n*=1,595

**Table 24: Month in which advice was given**

	Cases	Percent
June	21	7%
July	51	17%
August	54	18%
September	97	32%
October	42	14%
November	36	12%
December	5	2%

*n*=306

# Appendix B: Detailed methodology

## Stage 1: Participant recruitment

Roy Morgan Research was engaged to recruit survey participants and gather examples of their superannuation advice. Roy Morgan is one of Australia's largest and most experienced market research firms.

Roy Morgan talked to over 19,000 households in order to identify people at random who met the survey's selection criteria. They were:

- people in employment, but not self-employed or employed by the Commonwealth Government (so super choice was likely to be relevant);
- people aged between 18 and 65;
- people who intended to seek (or had already received) professional financial advice<sup>79</sup> that included advice about superannuation within the survey period of July to November 2005;<sup>80</sup> and
- not people who worked (or whose spouse worked) in the financial services industry, as they may have had a conflict of interest in the survey.

This filtering exercise gave Roy Morgan an accurate profile of the *target population* of the survey.

For the people who confirmed they met the selection criteria, Roy Morgan then asked if they would be interested in participating in the survey. 1,192 respondents agreed to participate and 1,108 were sent an information pack that explained the survey and contained the various documents they needed to complete.<sup>81</sup>

The recruited group broadly reflected the diversity of the target population of the survey (e.g. state, age, gender, amount in superannuation). Tasmania was over-represented and NSW was under-represented.

Of the initial 1,192 survey recruits, 414 sent material to Roy Morgan. From this group, we identified 306 examples of advice that could be assessed. A significant attrition rate occurs in any survey of this nature, which is why Roy Morgan sought such a large number of recruits. Attrition occurred at various stages:

---

<sup>79</sup> i.e. not just advice from family or friends.

<sup>80</sup> While this is the basis on which we recruited people, the advice they sent in covered a slightly wider period. The statistical analysis included 21 examples where the advice was given in June 2005 for later implementation and five examples of advice that late participants received in December.

<sup>81</sup> 84 respondents withdrew from the survey prior to being sent an information pack.

- Some survey recruits had indicated that they intended getting advice, but did not actually get it within the timeframe of the survey.
- Some recruits did not get around to posting material back to Roy Morgan or changed their mind about participating in the survey.
- Of the material we received from Roy Morgan, we excluded 115 participants from the compliance assessment as their case did not fit the survey criteria in some respect (e.g. outside date range, was not personal financial advice, advice was not about superannuation).

At the end of the survey, Roy Morgan recontacted participants who had received verbal advice to double-check whether an SOA had subsequently been received. Roy Morgan was unable to contact two people. Four people said they didn't know whether they had received further written advice. We presumed they hadn't, as we believe they would have known if they had recently received an SOA. Roy Morgan confirmed that 10 consumers had subsequently received written advice. Of these 10, ASIC reassessed six cases based on the additional information, and excluded the remaining four cases where the consumer declined to forward the written advice.

### **Sampling variation**

In interpreting survey results, it must be remembered that all sample surveys are subject to sampling variation. If a large number of samples were taken in the same way, they would all produce slightly different results. The size of such sampling variation depends largely on the sample size.

The sampling variation is estimated in the table below. This shows the range (plus or minus the figure shown) within which the results of repeated equivalent samplings could be expected to vary 95% of the time, assuming the same sampling procedure, the same interviews, and the same questionnaire.

The table shows how much allowance should be made for the sampling variation of an individual percentage. For example, assume the survey found that 20% of 280 respondents had a certain attribute. In the table below, the number 4.8% is in the column labelled 'survey estimates near 80% or 20%' and in the sample size row headed '280'. This means that the observed 20% in the sample is subject to a sampling variation of plus or minus 4.8 percentage points—that is, there is a 95% chance that the 'true' result (the average of many repeated samplings) is in the range 15.2% to 24.8%.

**Table 25: Recommended allowance for sampling variation of an individual percentage**

Sample sizes near	For survey estimates near					
	95% or 5%	90% or 10%	80% or 20%	70% or 30%	60% or 40%	50%
250	2.8%	3.8%	5.1%	5.8%	6.2%	6.3%
280	2.6%	3.6%	4.8%	5.5%	5.9%	6.0%
300	2.5%	3.5%	4.6%	5.3%	5.7%	5.8%

In percentage points (at 95% confidence level)\*

\*The chances are 95 in 100 that the sampling error is not larger than the figures shown.

## Stage 2: Advice assessed for compliance

In Stage 2 of the survey, a select group of ASIC staff assessed the examples of advice for legal compliance.

We selected staff who were experienced in file reviews and superannuation issues. The assessment team included people who had worked in the financial planning industry and lawyers. The leader of the assessment team had extensive experience, having previously worked as a financial planner as well as a commercial lawyer. The team received specific training in the assessment methodology and the relevant law.

Staff used a detailed checklist to standardise assessments. The assessment checklist was refined after initial pilot testing. To ensure quality control, senior staff cross-checked a proportion of the assessments, especially assessments where serious advice deficiencies were suspected. Senior staff frequently discussed emerging issues to ensure consistency and check legal interpretations.

The compliance assessment was conservative. Where there was a doubt, we leaned towards presuming advice was compliant. In most cases we could form a clear conclusion about whether advice or disclosure was compliant or not.

<b>'Compliant'</b>	Advice or disclosure appeared compliant
<b>'Probably non-compliant'</b>	Advice or disclosure was probably non-compliant
<b>'Non-compliant'</b>	Advice or disclosure was clearly non-compliant
<b>'Don't know'</b>	We did not have enough information to form a view

In some cases, however, the case appeared non-compliant on the information available, but we recognised that we did not have all the relevant information. If extra information would be quite unlikely to reverse the conclusion, we categorised the case as 'probably non-compliant'. If extra information would quite possibly reverse the conclusion, we gave the adviser the benefit of the doubt and categorised it as 'compliant'.

Where we had insufficient to form any view on an issue, compliance was categorised as ‘Don’t know’. For example, if we had insufficient information about what the advice actually was, ‘reasonable basis’ compliance was categorised as ‘Don’t know’. ‘Don’t know’ cases have been excluded from all percentages in this report.

When assessing advice, analysts had access to a range of material:

- written material provided to the client by the adviser, including a Financial Services Guide, Statement of Advice or Product Disclosure Statement;
- other written material provided by the participant, including a fund member statement and standard choice form;
- a participant’s diary that outlined each event in seeking advice and summarised what was said;
- an ASIC ‘fact find’ questionnaire on the consumer’s financial and personal situation, attitude to risk, financial goals, reasons for seeking advice and priorities in super fund features;
- a post-advice questionnaire on the participant’s view of the advice and whether they will implement it; and
- additional product disclosure statements obtained by ASIC and, where necessary, we called the fund’s customer service line to clarify fund features.

We had assured survey participants that we would not alert their adviser to the fact that they had participated in a survey. In assessing the advice, we did not access the adviser’s client file nor seek the adviser’s account of the advice process. This does not jeopardise the compliance assessment, for several reasons:

- Many aspects of the advice are factual (e.g. was a statement of advice provided?)
- Where there was a grey area due to limited information, we gave the adviser the benefit of the doubt.
- ASIC often used the circumstances to presume that certain factors had been considered in the advice, especially if the advice was only verbal.
- We looked at the advice the consumer actually received, not what was in the adviser’s mind. If the adviser had critical considerations that shaped their recommendation, the law requires that these be provided to the client in writing.

We took steps to alert consumers of concerns where:

- advice appeared highly detrimental to survey participants;
- the consumer was not alerted to the issue in the SOA; and
- the consumer had indicated that they intended to act on the advice.

We asked Roy Morgan to contact the participant (as we had no participant names or contact details). Roy Morgan attempted to contact the participant and invite them to contact ASIC to discuss their case.

We made it clear that we were not in a position to make a definitive view on the advice, but that there were some issues that we thought we should bring to their attention. Most intended to seek further information as a result. All consumers who talked to ASIC appreciated the contact.

A copy of the survey report will be provided to all survey participants. We will advise participants that they are welcome to approach ASIC or the normal complaint resolution processes if they are concerned that they may have received non-compliant advice.

### **Comparison with previous surveys**

ASIC has conducted two previous shadow shopping surveys. These were done jointly with the Australian Consumers Association (ACA) in 1998 and 2003. The methodology is based on a survey conducted jointly by the Financial Planning Association and ACA in 1995.

While these earlier surveys had many features in common with this survey (including using real consumers), they differed in some respects.

<b>Previous survey</b>	<b>Current survey</b>
People actively volunteered in response to a public request for participants	People were randomly selected and invited to participate
Participants were told which advice firm to go to	Participants selected an adviser themselves
All participants were new clients to the advice firm	Participants could be new or existing client of the advice firm
Participants were instructed to request a full financial plan	Participants were not guided in how to seek advice
Advice could be on any financial issue	The advice had to include superannuation
Advice was assessed for overall quality, including compliance with legal and professional standards	Advice was only assessed on legal compliance
Reports named all firms surveyed and gave a mark for each example examined	Report does not name firms surveyed

Advice in previous surveys was assessed by an external panel of financial planning and compliance experts. After representations from the Financial Planning Association, ASIC decided to use its own staff to assess advice in this survey, rather than outsourcing the task.

As this survey differs from earlier surveys in several respects, the results are not directly comparable.