

On the nose, now it's time for a bath

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No matter how you spin it, there's something seriously smelly about an industry that survives on kickbacks and commissions. Claiming you act for your client, but getting paid by people who want you to flog products to that client, is the sort of behaviour that is rightly seen as corrupt. And so it should be in financial planning.

For too long the remnants of the old life insurance industry have told investors it's OK for their adviser to be paid by fund managers, margin lenders, tax scheme promoters and anyone else with a financial product they want pushed. Golly gee, you can have this advice free. And because I've disclosed the payment in this 96-page document, the whole arrangement is ethical and above board. And was that a pig we just saw flying by?

It is long overdue. The Financial Services Minister, Chris Bowen, has taken the lily-livered recommendations of the Ripoll inquiry into the collapse of Storm Financial and come up with turbo-charged reforms that will address some of the worst conflicts of interest.

From 2012, advisers will be banned from receiving commissions from promoters of financial products. The industry had already announced its own plans to phase out such payments. But the government also intends to ban insidious commissions in disguise such as volume rebates and bonuses, and the practice of recommending clients borrow to invest, then charging a percentage fee on the total value of their investments.

Advisers will have to negotiate transparent fees and send clients an annual renewal notice giving a choice about ongoing payments. If they are no longer getting advice, or are unhappy with the service, they can turn off the fee tap - in contrast to many current arrangements where annual fees, often ongoing or "trail" commissions, can continue indefinitely.

The measures won't address all conflicts, but combined with the introduction of a duty for advisers to act in their clients' best interests, and enhanced policing powers for the Australian Securities and Investments Commission, they should weed out the worst excesses. The fact the industry has almost uniformly welcomed the reforms speaks volumes about the damage done to financial planners' reputations since the collapse of Storm, Westpoint, Timbercorp and a long list of others.

Not all planners recommended these investments, but all have been tarred by the kickback brush.

Make no mistake. Some of the initiatives in the Bowen plan will seriously disrupt the cosy nexus between planners and product providers and will be strongly resisted during the "industry consultations" to come.

While planners have been moving away from overt commissions, the research company Investment Trends reports planners on average still derive 56 per cent of their revenue from upfront and trailing commissions. One group, the Association of Financial Advisers, has already deemed the proposed ban "disempowerment of the individual" - though it stands alone in not conceding commissions are a lost cause.

Areas where the industry is likely to be less accommodating include the murkier area of "volume-based" incentives and rebates where planners directing larger volumes of business to a particular product receive additional benefits, and the need for advice arrangements to be renewed annually - both of which threaten easy income for planners. Bowen has also flagged a crackdown on "soft-dollar" payments and commissions on life insurance policies - though these have not been included in the reform package.

The Investment and Financial Services Association, in welcoming the reforms, said it would work with the government to ensure new measures "do not put financial advice out of the reach of all Australians".

This is a blatant play to the old argument that commissions and like payments make advice affordable for lower income earners who could not stump up, say, \$3000 or \$4000 for a comprehensive retirement plan.

But Bowen has a plan there, too.

He wants super funds to provide simple financial advice on retirement planning, superannuation and Centrelink payments.

Easing the advice requirements for those needing less complex financial help, and making advice tax-deductible, could also make advice more affordable - though this is not included in the plan.

Poll: Will these financial reforms see an improvement in the advice offered to investors?

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» «

»I worked as a Financial Planner for nine years. I worked in one dealership that received most of its income from one source. It provided a 'wrap' service that the dealer group has re-labelled. It is probably the most expensive in Australia and more than half the Administration fees the client pays go back to the dealer group. There are a lot of accountants using this wrap service. Due to the payments the Adviser does not have to pay any dealership fees. That one source has costs of approximately 0.15% but the client is paying approximately 0.9% with the source and dealer group splitting the difference. This is outrageous profiteering. I worked in another dealer group where the clients were paying approximately 0.7% in Administration fees for a wrap account and 0.2% was being paid back to the dealer group with no disclosure to the clients. I think that by the time the client is paying 1% to the Financial Planner, 1% to the Fund Managers and close to another 1% to Administrators/Dealer Groups, there's insufficient return to justify the investment. There are alternatives out there that are lower cost. There are some good Financial Advisers. I would recommend anyone to only deal with someone who can call themselves 'Independent'. This term has been regulated and generally means paying by the hour fees. During my time in the industry I worked with (at least) 4 psychopaths of the white collar type. These people had absolutely no regard for the client or the rules. Unfortunately the finance industry will attract these types of con men due to the rewards available. Additional regulation to rid the industry of the opportunity for supernormal profits is needed so the investments can be worthwhile for the investor.«

»«

Michael - April 27, 2010, 9:19AM

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Michael

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