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You could be paying for it twice: financial planning advice

- Simon Hoyle
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THERE is no such thing as free financial planning and there never has been. Even if you've been to a financial planner and believe you never paid for it, you've paid for it.

But there's a big difference between believing you've had a free lunch and being asked to pay for something twice. And that's something that could happen under changes announced by the federal government if the cost of the products that financial planners recommend to us does not fall.

The reason is commissions. The cost structures of many of the products that planners recommend include an amount paid out of our funds as commissions to cover the costs of the planners' services.

But from July 1, 2012, it will be illegal for financial planners to receive just about any form of payment from product manufacturers, under changes announced last week by Financial Services, Superannuation and Corporate Law Minister Chris Bowen.

The changes generally have been lauded as a positive move to address many (but not all) of the conflicts of interest that can arise when a financial planner provides a service to a client but gets paid by someone else.

Among the government's wide-ranging changes, a financial planner will have to ask you directly for a payment for services rendered.

Commentary surrounding the changes has focused largely on financial planners. But planners cannot bear the burden of implementing the government's changes on their own.

They need the complete and committed support of financial product manufacturers; otherwise there's a serious risk that the government's changes will fail. Instead of improving consumer protection and encouraging more people to seek advice from appropriately qualified planners, advice could be priced well out of the reach of the average person.

But some planners are sceptical that the cost of products will fall much at all and certainly not any time soon.

If you're investing in a product that is structured to pay a commission to a planner, then you're asked to pay the planner directly, you could end up effectively paying twice.

A survey released last week by research group Investment Trends suggests more than half of all planners still receive income in the form of commissions. It says the proportion is falling, but it remains the dominant form of planner remuneration.

A report commissioned by Industry Super Network that was released on April 19 says \$1.3 billion was paid out last year in commissions to financial planners, including \$550 million on compulsory superannuation contributions. Some planners are sceptical that separating advice from products will have much immediate effect.

Claire Mackay, a certified financial planner and co-founder of Quantum Financial Services, says direct payments for advice are unlikely to drive down product costs far and won't do so quickly.

"While it seems logical that product costs should fall as a result of these reforms, to reflect the fact that product manufacturers no longer have to support payments to financial planners, in the short term we do not expect to see product costs fall, nor do we believe product providers will strip out the cost of advice," Mackay says.

"This is because the proposed reform is prospective, which means from July 1, 2012, the ban on commissions and volume bonuses will apply only to new financial products.

"If we assume an average product life of six years, even if we assume the industry moves faster than average, we estimate in the vast majority of cases it will not be until 2015 at the earliest that we start to see a material change away from the old commission-based regime to the new fee-based regime for the vast majority of existing legacy products.

"We argue that product costs will fall but not for the immediate reason that commissions are stripped away. Instead, we believe competition will drive down prices."

John Brogden, chief executive of the Investment and Financial Services Association, says his association's members are already unbundling advice and its associated cost from their products. He says IFSA is committed to ensuring that under the government's proposals the cost of advice to consumers does not rise.

"The fact is that there will be flow-through effects with these changes, both with respect to volume-based fees and commissions," Brogden says.

"The industry has been preparing for significant change and in some cases has been at the forefront.

"We've got two years, or a little over two years, to [make] that change. We've yet to see the legislation, and we need to see exactly what the government wants to do in a legislative sense, and we'll be very much part of that process with the government and Treasury."

Brogden says IFSA is preparing a "massive campaign to explain to Australians the value of advice".

He says that to date the industry has done a poor job on this front.

"Our sector has failed, in the sense that it has allowed the argument to be about the cost of advice, not the value of advice. We've allowed the debate, therefore, to impinge on whether you should get advice at all.

"But what is interesting is that there is no one arguing that financial advice is bad or unnecessary. As many people as possible should get financial advice because it benefits them.

"And that campaign will be damaged if financial advice becomes too expensive."

David Whiteley, chief executive of Industry Super Network, has been a staunch critic of commissions for many years and welcomes the government's proposals.

Whiteley says that "once advice, distribution and other agency and intermediation costs are stripped out from retail products, they should be better able to compete on price".

"Clearly, explicit commitment to doing so is necessary," he says.

"What is needed from the retail sector and financial planners is clarity about their degree of support for what Chris Bowen has announced.

"What is critically important is that the retail funds and planners are not hypocritical in their support for the reforms. It is inappropriate to support them publicly and then encourage the opposition to oppose reform."

We've always paid for financial planners' service, whether we knew it or not. We should not be surprised, or alarmed, by being asked to pay for those services directly, provided the cost of the product recommended to us falls commensurately.

Simon Hoyle is editor of Professional Planner magazine.

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