FINANCIAL SERVICES COMPENSATION SCHEME OF LAST RESORT

Submission by
AIOFP Executive Director Peter Johnston

October 2022

CSLR@treasury.gov.au

INDEX

1. Executive Summary…………………………………………………….Page 3
2. Anti - Consumer behaviour………………………………………Page 4
3. The Scourge of Political Donations……………………………..Page 5
4. Summary……………………………………………………………………Page 6

EXECUTIVE SUMMARY

The Association of Independently Owned Financial Professionals [AIOFP] is a not-for-profit Association formed in 1998 to act in the best interests of its Financial Adviser [Adviser] members.

Inextricably linked to Advisers' legal and ethical obligations is that they must act in the best interests of their clients. This relationship places positive consumer outcomes firmly within the AIOFP charter and objectives.

The Compensation Scheme of Last Resort [CSLR] is fundamentally a consumer-focused solution initially created by the Ramsey Reviews then perfected by Comm Hayne Royal Commission Recommendations in 2019 to protect consumers from poor financial advice and/or financial product failure.

We stress that poor financial advice AND product failure are two entirely separate issues that needs to be addressed in isolation from each other.

It should be noted that the Morrison Coalition Government pledged unconditional public support for Comm Haynes Recommendations on numerous occasions, which was met with similar bipartisan support from the then Labor Opposition.

Furthermore, CSLR was specifically mentioned in ***the 2019 FSRC – GOVERNMENT RESPONSE TO HAYNE RC Report*** by former Treasurer Frydenberg to implement it in the Royal Commission recommended format, and which, again, received enthusiastic bipartisan support. [see attached document]

The recent political backflips by both major parties over implementing CSLR in its original Hayne recommended form, raises serious concerns that anti – consumer vested interests are trying to change the operational format of CSLR to suit their own position, rather than that of the consumer.

Once the stakeholder structure of the Financial Services industry is examined there appears to be only one participant who will benefit directly from the three critical aspects being touted for amendment. This stakeholder are the product manufacturers which includes the Banks and Financial Institutions [the Banks]

The foreshadowed attempts by those interest groups to eliminate the 1/1/2008 retrospective date and replace it with a date of legislation, and further to seek to exclude Managed Investment Schemes [MIS] in the catchment zone, will disadvantage those consumers who fall outside that retrospective date, which in turn, will benefit the Banks.

Furthermore, the suggestion to cap the compensation level outside the current AFCA guidelines will again be detrimental to consumers and thereby benefit the Banks, whose liability exposure will be further reduced.

It is clear to most, that the Banks are the only stakeholder which will benefit from these attempted anti - consumer CSLR amendments.

It is time for all Politicians and Bureaucrats to also act in the best interests of consumers by firmly rejecting the 3 proposed CSLR amendments. After the unequivocal bipartisan support of CSLR leading into the 2019/2022 elections, we are somewhat bemused that this Treasury process is required or even necessary.

ANTI – CONSUMER BEHAVIOR

As indicated, once all the facts around industry stakeholders' intent and participation in lobbying for the proposed amendments are considered, then, prima facie, there is only one conclusion which can be drawn - the proposed restriction on the breadth of the CSLR scheme will benefit Banks to the great detriment of the consumer.

The Financial Services diverse landscape has 5 major stakeholders with a varied and vested interest in the CSLR outcome, they are –

1. Consumers.
2. Financial Advisers.
3. Regulators [ASIC, APRA].
4. Politicians.
5. Product manufacturers [Banks/Financial Institutions - Banks]

Politicians and the Regulators are public servants and therefore, presumably, committed to achieving the best outcomes for taxpayers/consumers. Financial Advisers have a legal obligation to act in Consumers' best interests.

It is the AIOFP's position that, based on the above, Stakeholders 1-4 should NOT BE seeking to change the Hayne recommended format. Stakeholder 5 is the only entity which, potentially has a conflict-of-interest element in their corporate structure against consumers. Often the main focus for a Bank is on the return to their shareholders, and the consumers' best interests are often unmet in the marketing hyperbole of products offered to the market.

The only stakeholder to benefit from these diluted/changed benchmarks would appear to be the Banks. For the obvious reasons, the proposed change to the scheme reduces their exposure to claims for compensation by consumers. The reduction of the retrospective time

period, the reduction of the monetary cap and the proposed carving out of the MIS failures of the past and the future is clearly not in the best interests of consumers.

Up until recently Banks have cleverly and strategically avoided accountability for poor management of their own internal MIS financial products by deflecting the blame onto Advisers.

Clearly, Advisers do NOT manufacture, own or manage institutional MIS's. Essentially Advisers are also consumers of these ASIC registered/Bank managed MIS products, along with their consumer clients seeking advice and direction.

All stakeholders are now realizing that Advisers are not to blame for product failure. This is further backed up by the latest AFCA complaints data exposing Banks accounting for 98.5% of all complaints, and Advisers only 1.5%.

Attached is a list of all MIS Product failures since 2008, which lists the names of the Banks/Institutions involved in those product failures. It all becomes very clear why the Banks may want to avoid their accountability exposure to consumers.

CSLR will now expose the inconvenient truth about MIS product failure and who is responsible – this will also have direct connotations as to how CSLR should be funded.

Past attempts by certain Politicians to fund CSLR from the PI Insurance of Advisers is either naive or an attempt to protect and 'shelter' the obvious stakeholders from the rigours and the costs of accountability.

The funding option is very clear in our view, Banks should be required to pay for the failure of their products as Advisers are required to pay for their poor strategic advice.

If an Adviser's PI cover is to be targeted, it would be wrong on many levels. Firstly, the inevitable increased cost of premiums would be passed directly back to consumers by Advisers. It is wrong to inflict the incompetence of Bank management skills onto Advisers/consumers and those few remaining PI insurers who still write policies, could be expected to leave our shores threatening the existence of the PI market [therefore the whole industry – other than the self-insured i.e., the Banks] after a decade of losses.

THE SCOURGE OF POLITICAL DONATIONS

Political donations and the elimination of the defined benefit superannuation Scheme for Politicians in 2004 pose a real and present threat to the nation's democracy. Political parties

are finding it difficult to recruit the best people into a political career and the weight of political donations has the potential to skew political scrutiny of legislation away from what may be in the consumers' best interest.

Until external political donations are eliminated to all political parties and electoral funding is met exclusively by taxpayers/consumers, some Politicians will always be tempted by those who seek to promote their own special agendas by such donations.

If Consumers fund political capital to Parties, a Politicians loyalty and best interests' duty will be to Consumers, NOT a conflicted third party trying to 'buy/demand' favours.

Attached is a list of all donors over the past 10 years to all political parties from the AEC website, a very confronting document. Obviously, these individuals/organizations are donating hundreds of millions for a reason – it would be fair to say 'to get an outcome' would be the most common intention.

We have analysed the at times confusing data to derive a number where Banks have donated to both major political parties over recent years and discovered the following information-

- Coalition - $13,125,791
- ALP - $9,499,008

Source - https://transparency.aec.gov.au/AnnualDonor

Considering the context of this paper some questions could be asked –

- 'Do these political donations to the political parties have an influence on political outcomes, such as for instance in the proposed CSLR amendment outcomes?

- 'Would there be a threat to continued political contributions, if the CSLR amendments were not delivered?

We will leave it to others to reflect and decide on the relevancy of these proposed questions.

SUMMARY

Over the past 25 years consumers have suffered at the hands of poorly managed Financial Products owned by the Banks with many billions of their savings lost. These Financial Products are registered and released by ASIC onto the market as Managed Investment Schemes with an accompanying Product Disclosure Statement. MIS represents over 95% of all market products.

Consumers have either suffered in silence, been too intimidated to pursue legal recourse against institutions after buying online or been unaware of AFCA assistance.

The Ramsey Reports and Comm Hayne in the Royal Commission recognized this injustice and recommended a compensation scheme to hold the Banks accountable for their "misbehaviour". ***To even suggest that MIS be excluded from the CSLR catchment is breathtakingly arrogant and disrespectful to all consumers.***

We believe most stakeholders are now realizing that product failure is in the domain of those who create, own, and manage them – and it's NOT the Advisers.

The Banks past political strategy to deflect the blame onto Advisers is no longer acceptable, they must now be held to account for their own behaviour to consumers both in the past, present and the future.

We believe holding Banks to account and acting in the best interests of Consumers was at the very crux of what Ramsey and Hayne were trying to achieve. It is now time for all Politicians to honour this position.

The latest AFCA complaint numbers irrefutably confirm the industry dynamics, poor strategic advice is relatively rare and commonly resolved in the regular AFCA process anyway.

We suspect the past instances of consumer AFCA determinations failing are due to the Adviser entering administration after being caught with product failures which have destroyed their businesses.

The AFCA 'Complaints paused due to Financial insolvency', [document link https://www.afca.org.au/news/latest-news/complaints-paused-due-to-firm-insolvency-0] needs to be amended to avoid this critical confusion in our view. It does not differentiate between Product Manufacturers and Advisers by classifying all as a collective under 'financial firms'. The roles of product and advice are diametrically opposed functions and should be treated in that manner, this inaccuracy only leads to disguising the true detrimental effect of product failure on consumer losses by mixing it with Advice scenarios.

We believe all MIS should be included in the catchment, compensation capped at current AFCA levels and backdated to what both major political parties originally agreed to – 1/1/2008. Advisers should be funding advice failure and Banks funding product failure.

If CSLR is amended to a capped, non - retrospective dated structure and NOT incorporating MIS schemes, it will usher in a pitiful, and an almost functionless and futile piece of legislation which will not serve consumers' best interests.