The Royal Commission

By Phillip Win, MD, and Sarah Abood, CEO

The recent Round 2 hearings of The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, focusing on financial advice, generated a huge amount of concern and debate in our industry.

Around the same time, APRA's report on CBA was released. It identified many similar areas of concern.

Many of us thought the big legislative changes made in 2012 and 2014 had 'weeded out' these types of practices. Clearly though, plenty of work remains to be done.

In this article we take a look at some of the key areas of misconduct identified, and explain Profile's view and what we do now.

Leadership and culture

It's almost never the case that failures were the result of a single person's actions or mistakes. Issues in the organisations featured were systemic and rooted in a culture where people didn't feel safe to speak up, and when they did they were penalised. Behaviours that drove revenue and growth were rewarded excessively, whereas behaviours that prioritised the client and managed risk were hardly recognised at all. Mistakes were covered up and even when exposed, took many years and much pain to resolve for clients. 'Independent' reports were doctored. Clearly, leadership within the organisations did not live the values that were claimed on the website or on the wall!

Profile's view: Even good people find it hard to do the right thing when their job and promotion prospects depend on doing something else. It's leadership's responsibility to create an environment in which people feel safe to call out poor behaviours and practices, and are rewarded for putting the client first. Leaders must act on poor behaviour quickly and decisively. They must be held to account regularly and fearlessly to ensure this is really happening.

What we do: Basically, let the sunlight in! We seek out external scrutiny, with a non-executive chair of our board, and regular external, independent audits of our advice and client satisfaction. We're very transparent with our team, sharing strategies and financials regularly with all staff. We encourage self-reporting of incidents and don't penalise staff for being human beings who occasionally make mistakes. When we've made a mistake, we let the client know, and 'make–good' any detriment, quickly. We expect all our staff to live our values and we act if this isn't happening – and this applies to everyone, irrespective of their role.

Remuneration

Still in this day and age, some organisations pay their planners very little unless they make a sale. Top 'performers' are considered to be those planners who bring in the most $ to the organisation. They are set very high sales targets such that they have no time left to look after existing clients or improve their knowledge, if they want to pay the mortgage and feed their families.

Profile's view: What gets rewarded gets done. The remuneration structure is a pretty clear indication of what an organisation really values.

What we do: Overall, helping Profile grow is just one of five KPI areas for our planners, and it's 25% or less of the overall assessment. The other 4 areas are client satisfaction, delivering on our service & quality promises, ongoing professional development, and teamwork & leadership. To be considered a good performer in our organisation, a planner needs to be delivering across all these areas - great sales can't make up for poor client satisfaction, or poor quality advice.

Vertical integration

This term refers to businesses which combine activities at two or more stages of production – such as advice and a platform or investment product. It is the dominant business model in the financial services industry. In fact almost all businesses of any size use it – including the "big 6" of AMP, IOOF, ANZ, NAB, Westpac and CBA, as well as most industry super funds – as does Profile, and most boutiques of our size or larger. It can provide many benefits to clients (including economies of scale and the convenience of dealing with fewer providers). However it's clear from the findings so far that many institutions are poorly managing the potential conflict this structure presents. In some cases clients were given poor advice to move to in-house products that left them in a worse position than before.

Profile's view: It's critically important to manage potential conflicts effectively in any business. Advice providers have a duty to put their clients' interests before their own and must ensure that incentives structures, processes and monitoring and supervision support this.
What we do: Our planners have no targets set or bonuses paid for recommending any one product over another – or indeed, any products at all. Our processes ensure that all advice to clients is seen by at least three people in our business before being issued to clients. And we regularly audit our advice – both internally via our compliance team (which has a separate reporting line to the planning division), supplemented by external audits. Most importantly we act on any findings – including improving internal processes and training. A planner who fails an audit cannot receive a bonus.

Fee for no service

There were several examples of organisations that hadn't delivered on contractual promises of service made to their clients, but continued to charge fees. In a few cases this was deliberate – a new planner wasn't assigned to a client when the previous planner left an organisation. Many also weren't producing statutory documents, such as the FDS, that are already required by law.
There's still a grey area under this heading, which relates to products in some cases many decades old, where ongoing 'commission' is built into the fee structure. If that isn't being paid to a planner, the institution keeps it - with no saving for the client and no service either!
Profile's view: Compliance with the law isn't optional, even if the laws are hard to comply with. But further legal changes are going to be required to deal with the issue of legacy fees and products. A requirement that the client save the fee if there's no active adviser on the product, would force institutions to upgrade their systems and product rules. Even better would be legislation that helped clients in moving away from old products, such as waiving CGT, and ensuring clients can move to the latest & most favourable insurance policies with no loss of coverage.
What we do: Planners are assigned to all our review service clients. When a planner changes (which is fairly rare!) we ensure continuity of service and advice. We internally audit annually to ensure we're delivering on our service promises. And we currently produce the FDS document, and opt-in notice, annually in bulk for all our clients (which helps many at tax time).
We, along with most firms with a long history, have some clients holding legacy products with commission built in. Where it's not in the client's best interests to change products, we treat that commission as part of our overall fee (where applicable, reducing advice fees payable from other sources).

In conclusion

This isn't a complete list of issues, and the Royal Commission still has a while to run (the final report is due on 1 February 2019.) We know it's also critical that we stay vigilant and never get complacent when it comes to our culture of putting the client first. We would welcome any questions you might have about the issues raised - please don't hesitate to contact your planner, or either of us, if you'd like to discuss any of the issues further.

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