ASIC

Australian Securities & Investments Commission

REPORT 499

Financial advice: Fees for no service

October 2016

About this report

In 2015, ASIC commenced a project to review the extent of failure to deliver ongoing advice services to financial advice customers who were paying fees to receive those services.

The project covers Australian financial services (AFS) licensees that are product issuers or provide personal advice to retail clients, and that are part of AMP Limited, Australia and New Zealand Banking Group Limited, Commonwealth Bank of Australia, Macquarie Group Limited, National Australia Bank Limited and Westpac Banking Corporation.

This report outlines the findings and outcomes to date.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

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Executive summary

1 In April 2015, we announced—as part of ASIC's Wealth Management Project—that we were investigating multiple instances of Australian financial services (AFS) licensees charging customers fees for annual financial advice reviews where the reviews were not provided. Most of these fees had been charged as part of a customer's ongoing service agreement with their financial adviser or the licensee.

Note: See Media Release 15-081MR *ASIC update on Wealth Management Project—Investigation into charging of advice fees without providing advice* (16 April 2015).

2 ASIC has commenced several enforcement investigations in relation to this conduct.

3 We consider that, regardless of any enforcement investigation, AFS licensees should compensate affected customers through review and remediation.

4 Our work has therefore also involved:

(a) ensuring that customers affected by any known failures would be identified and compensated by AFS licensees in an efficient, honest and fair manner;

(b) monitoring wider reviews, instigated by AFS licensees at ASIC's request, to determine whether the licensees had further ongoing advice service failures; and

(c) monitoring the changes made by AFS licensees to their systems and processes to prevent such failures from recurring in the future.

Note: We use the term 'customer' or 'client' in this report to mean 'retail client'.

5 Under our Wealth Management Project, we are focusing on the conduct of six of Australia's largest banking and financial services institutions:

(a) AMP Limited (AMP);

(b) Australia and New Zealand Banking Group Limited (ANZ);

(c) Commonwealth Bank of Australia (CBA);

(d) Macquarie Group Limited (Macquarie);

(e) National Australia Bank Limited (NAB); and

(f) Westpac Banking Corporation (Westpac).

6 The project covered by this report focuses more specifically on AFS licensees that are part of these banking and financial services institutions, where these licensees:

(a) are authorised to provide personal advice to retail clients; or

(b) are product issuers that have identified a systemic failure in relation to the charging of ongoing advice fees to customers.

Note: We use the term 'advice licensees' in this report to refer to AFS licensees that provide personal advice to retail clients. 'Personal advice' is defined in s766B(3) of the *Corporations Act 2001* (Corporations Act): see also 'Key terms'.

7 AMP, ANZ, CBA and NAB have all identified systemic issues in relation to the charging of ongoing advice fees. Westpac has also identified a systemic issue but in relation to one adviser only. Macquarie has not identified any systemic failures in this area (likely reflecting its different business model) and is therefore excluded from our discussion of compensation for already identified failures in Section B. However, Macquarie is included in our description in Section C of the related checks and reviews that each of the institutions has performed, with the results to be reported on.

8 This report discusses the systemic failure by advice licensees to discharge their obligations to ensure that ongoing advice services were provided to customers who paid fees to receive these services, and the failure of advisers to provide such services. It also discusses the systemic failure of product issuers to stop charging ongoing advice fees to customers who did not have a financial adviser.

9 We discuss the actions taken by the AFS licensees to compensate customers affected by these failures (see Section B), the progress and outcomes to date of the further reviews instigated by the licensees at ASIC's request (see Section C), and the steps AFS licensees are taking to fix their systems and processes to prevent recurrence of these failures (see Section D). The report also sets out our observations from this project (see Section E).

10 In the course of this project, we have successfully obtained a range of positive and improved compensation outcomes for affected customers. These relate to:

(a) the number of customers identified for refunds and compensation;

(b) the fairness and amount of compensation paid to affected customers; and

(c) the scope of the further reviews conducted by the advice licensees, which have resulted in additional customers being identified for refunds and compensation.

11 We are also requiring licensees to prevent these failures from continuing and to significantly reduce the likelihood that similar failures will occur in the future.

12 To date, we have no evidence of fee-for-service failures of a similar scale occurring in advice licensees outside of the banking and financial services institutions covered by this report. However, we strongly encourage other advice licensees to review their operations to ensure they do not have similar issues.

Nature of ongoing advice service failures

13 We initiated this project in response to information we obtained, including through breach notifications from some AFS licensees, suggesting that customers were being charged fees for ongoing advice but were not receiving that advice.

14 In this report, we confirm that these systemic failures have affected 21 AFS licensees that were part of the banking and financial services institutions in ASIC's Wealth Management Project. These licensees included both advice licensees and the issuers of financial products such as superannuation.

15 The systemic failures—referred to in this report as 'fee-for-service failures'—related to instances where customers were being charged a fee to receive an ongoing advice service, but had not been provided with this service because:

(a) the customer did not have an adviser allocated to them; or

(b) the adviser allocated to the customer failed to deliver on their obligation to provide the ongoing advice service, and the advice licensee failed to ensure that the service was provided.

Positive impact of FOFA reforms

16 Most of the systemic failures identified in the project covered in this report occurred before the Future of Financial Advice (FOFA) reforms, which became mandatory on 1 July 2013.

17 ASIC supported the introduction of the FOFA reforms, which have helped to address systemic problems in the financial advice industry, including conflicted remuneration and the lack of transparency of advice services and advice fees.

18 The changes made under the FOFA reforms—in particular, the requirement that customers opt in to receiving ongoing advice services, and the introduction of fee disclosure statements—contributed to some AFS licensees identifying the fee-for-service failures. This is discussed in Section A.

19 In addition, these provisions, and the system changes they have required, substantially reduce the likelihood that the type of systemic failures described in this report will recur.

Compensation

20 As at 31 August 2016, compensation arising from the fee-for-service failures that were reported to ASIC was approximately $23.7 million in total. This was paid, or agreed to be paid, to over 27,000 customers. We report on these outcomes in Section B.

Note: As at 31 August 2016, some of these AFS licensees were still in the process of communicating with and compensating affected customers.

21 We expect these compensation figures to increase substantially in the coming months as the process to identify and compensate affected customers continues. Our current estimate is that compensation may increase by approximately $154 million plus interest to over 176,000 further customers, meaning that total compensation for related failures could be over $178 million.

22 We stress that these figures are estimates based on information reported to ASIC by the AFS licensees in October 2016. We will report on the actual compensation figures at a later date.

Further reviews

23 Because of the extent of the specific failures identified by the advice licensees, we requested that each of the six banking and financial services institutions conduct further large-scale reviews of their advice licensees to determine whether they had any additional fee-for-service failures.

24 While most of these large-scale reviews—generally covering periods of seven years across multiple advice licensees—have yet to be completed, some have resulted in further failures being identified and compensation of approximately $250,000 being paid to a small number of additional customers. We report on these outcomes in Section C.

Systems changes to prevent future failures

25 We asked the advice licensees and product issuers that had identified fee-for-service failures to describe the changes they were making to their systems and processes to prevent such failures from recurring in the future, or to enable early detection of any failures that did occur.

26 In Section D, we report on the changes that some of the advice licensees and product issuers have made to their systems to ensure that ongoing advice services are provided to customers who are paying fees to receive these services. We also give details of the further work to be done. We are following up with the banking and financial services institutions in relation to the adequacy of their systems changes.

Our observations

27 In Section E, we record our observations to date from our work on this fee-for-service project.

28 Some of the advice licensees and product issuers that identified fee-for-service failures demonstrated a proactive approach in identifying affected customers—presenting ASIC with an acceptable process for customer review and remediation—and showed a commitment to paying refunds and compensation within a reasonable timeframe.

29 However, we also identified, from the licensees we reviewed in our project, the issues outlined in Table 1. We continue to address these issues with the licensees.

Table 1: Our concerns about fee-for-service failures and review and remediation

Culture and remuneration	During the period of time covered by this project, the financial advice industry still had a culture of reliance on automatic periodic payments, such as sales commissions and adviser service fees. Some advice licensees prioritised advice revenue and fee generation over ensuring that they delivered the required services. Cultural factors in the banking and financial services institutions covered by this report may have contributed to the systemic failures we observed.
Record keeping and monitoring	Some licensees and advisers failed to keep adequate records or to capture sufficient data electronically to enable monitoring and analysis. Some licensees did not develop and enforce effective monitoring and checking procedures to prevent systemic failures.
Review and remediation	On some occasions advice licensees proposed review and remediation processes that were legalistic and did not prioritise the interests of customers.

Regulatory Guide 256

30 In September 2016, ASIC published Regulatory Guide 256 *Client review and remediation conducted by advice licensees* (RG 256). This guidance was based on our observations and experience gained from reviewing past review and remediation conducted by advice licensees, including this fee-for-service project.

31 RG 256 should be used by advice licensees when considering:

(a) when to initiate the process of review and remediation;

(b) the scope of review and remediation;

(c) designing and implementing a comprehensive and effective process for review and remediation;

(d) communicating effectively with customers; and

(e) ensuring that customers have access to the external review of decisions.

Future reporting

32 We intend to provide a public update, in the first half of 2017, on the progress and outcomes of the advice licensees' review and remediation activities: see Section F.

33 We will also make a public statement where we take enforcement action.

A Background

Key points

The financial advice industry relies heavily on receiving periodic payments from customers, usually by automatic deductions from their financial products, to remunerate advisers and advice licensees. Under the arrangements made with customers, there may or may not be an obligation to provide a specific advice service in return for these payments.

Our review of the AFS licensees in our project demonstrated that:

- there were systemic failures by advice licensees to provide ongoing advice services to customers who were paying a fee to receive such services; and
- there have been systemic failures relating to the charging of ongoing advice fees to customers who did not have an adviser.

This work forms part of ASIC's Wealth Management Project, which focuses on the conduct of Australia's largest banking and financial services institutions, and reports on systemic failures by that industry sector.

Exploring the problem

34 The problems covered in this report arise in two situations:

(a) a customer who has a financial adviser pays fees to receive ongoing advice from that adviser, but the adviser does not provide the advice; or

(b) a customer who does not have a financial adviser (because, for example, the adviser departed the advice licensee or retired) is charged a fee for ongoing advice, which the customer does not receive.

35 To provide context for how these problems have emerged, this section describes the prevalent methods of remuneration in the financial advice industry.

36 For many years, three key features of the financial advice industry in Australia have been:

(a) the prevalence of adviser remuneration structures based on periodic payments from customers, usually by automatic deductions from their financial products, to remunerate advisers and advice licensees—these periodic payments also include sales commissions paid by product issuers to advice licensees and advisers;

(b) in the case of commissions, the absence of a clear agreement between advisers and customers about the specific services to be provided in return for these automatic payments; and

(c) the prevalence of large numbers of 'passive' customers who do not receive regular advice from their adviser or the advice licensee.

37 Automatic payments may comprise initial and trail commissions paid by financial product issuers to advice licensees and their representatives (advisers), based on the amount of the customer's investment or insurance premium. In aggregate, these commissions increase the product costs or insurance premiums paid by customers. There is generally no specific advice service obligation tied to these commissions, which continue to be paid to advice licensees and advisers whether or not they give customers ongoing advice.

38 Periodic payments may also be in the form of adviser fees that customers authorise to be automatically deducted from their financial products and to be paid by product issuers to advice licensees and their representatives.

39 In Report 407 *Review of the financial advice industry's implementation of the FOFA reforms* (REP 407), released in September 2014, ASIC reported on the prevalence in the industry of 'passive' customers. We defined these as customers who have not received advice or services in the previous 12 months. REP 407 found low levels of ongoing advice service delivery to customers, particularly by advice licensees associated with large banks. The report stated at paragraphs 53–54 that:

> On average, licensees in the sample indicated that about 60% of their clients were 'active' clients, having received some advice or service in the previous 12 months, while 40% of the clients were 'passive' clients.
>
> However, there were wide variations between the different size categories of licensee. Some large licensees, including several bank-owned licensees, reported that between 60% and 80% of their clients had received no advice or service in the past year.

40 Customers who did not enter into an agreement to receive a specific advice service in return for the commissions they funded, or the adviser fees they paid, are not covered by this report. This is because there is no obligation on the advice licensee or adviser to provide an advice service to these customers.

41 Many customers, however, paid periodic advice fees for ongoing advice services that they did not receive. We focus on these customers in this report.

Positive impact of FOFA

Introduction of fee disclosure statements

42 Following the introduction of the FOFA reforms, which became mandatory on 1 July 2013, the Corporations Act was amended to require AFS licensees and their representatives who have ongoing fee arrangements with retail

clients (fee recipients) to comply with the fee disclosure statement obligations. These obligations are designed to help customers ascertain whether they are receiving a service commensurate with the ongoing fees that they are paying.

43 An ongoing fee arrangement exists when an advice licensee or its representative gives personal advice to a retail client and the client enters into an arrangement with the licensee or representative, the terms of which provide for the payment of a fee during a period of more than 12 months.

Note: An ongoing fee (including a commission) paid by a third party to an AFS licensee or its representative will generally not constitute an ongoing fee for the purposes of the Corporations Act, unless the fee is paid with the clear consent of, or at the direction of, the customer.

44 For the purposes of the definition of 'ongoing fee arrangement', a fee is any fee (however described or structured) that is paid under the terms of the ongoing fee arrangement between the AFS licensee or representative and the customer.

45 A fee disclosure statement is a statement in writing that includes information relating to the previous 12-month period of an ongoing fee arrangement.

46 Based on our discussions with advice licensees, we understand that the introduction of fee disclosure statements was a key factor that enabled licensees and customers to gain a better understanding of the advice services being charged for and provided, and that this contributed to a number of the systemic failures in relation to ongoing fees and services being identified by advice licensees. We expect that fee disclosure statements will also help to reduce the likelihood of related systemic failures in the future.

Opt-in (renewal notices)

47 Following the introduction of the FOFA reforms, in an ongoing fee arrangement for financial advice, the fee recipient must provide the customer with a renewal notice for the arrangement every two years. The notice must include a statement that:

(a) the customer may renew the arrangement by giving the current fee recipient notice in writing;

(b) the arrangement will terminate, and no further advice will be provided or fee charged, if the customer does not renew the arrangement;

(c) if the customer does not renew the arrangement before the end of the renewal period, the fee recipient will assume the customer has chosen not to renew the arrangement; and

(d) the renewal period is a period of 60 days beginning on the day on which the renewal notice and fee disclosure statement is given to the customer.

48 This reform significantly reduces the likelihood that customers will continue to pay fees for ongoing advice services if they do not wish to receive those services or pay those fees.

Scope and methodology of our review

49 Our project had the following main objectives:

(a) *compensation*—to ensure that customers who were affected by known fee-for-service failures were identified and compensated by the AFS licensees;

(b) *further review*—to ensure that advice licensees conducted reviews for the period from 1 July 2008 to 30 June 2015 (or a different relevant seven-year period) and that other licensees where systemic failures had not been identified would be included in this review. The purpose of these reviews was to identify whether other licensees had fee-for-service failures and whether there were further customers requiring refunds and compensation; and

(c) *systems changes*—to inquire about and assess the adequacy of changes licensees have made to their processes and systems to reduce the likelihood of similar fee-for-service failures occurring in the future.

50 As noted at paragraph 2, we have also commenced several enforcement investigations in relation to this conduct.

51 The project focused on AFS licensees that are part of the banking and financial services institutions covered by the Wealth Management Project, where these licensees:

(a) are authorised to provide personal advice to retail clients (i.e. advice licensees); or

(b) are product issuers that have identified:

(i) a failure to provide ongoing advice services to customers; or

(ii) the incorrect charging of ongoing advice fees to customers.

52 For the ‘further review’ part of this project (see Section C), we wrote to each of the six institutions, requesting that they undertake a review of the provision of ongoing advice services to customers by their advice licensees between 1 July 2008 and 30 June 2015.

53 We held meetings with the institutions so that we could understand, negotiate and provide guidance on:

(a) the steps that they should take to assess which customers were affected by known fee-for-service failures;

(b) communications with customers;

(c) processes for further reviews to investigate other potential fee-for-service failures; and

(d) compensation methodologies.

54 We have required regular reporting from the institutions on the progress of their customer review and remediation. This report provides the key outcomes to date.

B Compensation

Key points

Between 1 August 2013 and 31 December 2015, we received 22 significant breach notifications about fee-for-service failures, from 21 AFS licensees representing five of the banking and financial services institutions covered by ASIC's Wealth Management Project.

Our focus has been on overseeing the licensees' processes to identify affected customers and to compensate them in an efficient, honest and fair manner.

As at 31 August 2016, these review and remediation activities have resulted in approximately $23.7 million in compensation being paid, or agreed to be paid, to over 27,000 customers.

We expect the amount of compensation to substantially increase as the process to identify and remediate affected customers continues.

Nature of ongoing advice service failures

55 Between 1 August 2013 and 31 December 2015, we received 22 significant breach notifications about fee-for-service failures from 21 AFS licensees representing five of the banking and financial services institutions covered by ASIC's Wealth Management Project.

56 The majority of the fee-for-service failures identified by the institutions fell into the following categories:

(a) failure of the advice licensee or adviser to provide an advice service to a customer who had an adviser allocated to them and who was paying fees to receive such a service; and

(b) charging ongoing advice fees to customers who did not have an adviser allocated to them. The reasons for this happening included:

  (i) that the adviser had departed from the licensee;

  (ii) that the customer had requested that the advice service be discontinued;

  (iii) that the advice fees were charged from a no-advice service package; or

  (iv) other reasons why the advice fee was not 'turned off' by the licensee, such as information technology (IT) or communications failures.

Processes to identify affected customers

57 After determining that there were systemic fee-for-service failures, the AFS licensees designed and implemented processes to identify the customers affected.

58 Most of the AFS licensees in our project have engaged external consultancy firms as part of their work to identify and compensate affected customers, or to provide some level of assurance in relation to those activities.

59 In general, the banking and financial services institutions and their external advisers have used the following high-level processes to identify potentially affected customers.

Data analysis to determine who paid the fees

60 The licensees analysed their revenue data systems to try to identify all customers who had paid ongoing advice fees.

61 Generally, this method was used by the advice licensees because they did not have complete or accurate information about the customers to whom they promised to provide ongoing advice services. The revenue data allows the advice licensees to identify the customers who have made payments, and therefore are likely to have been entitled to advice services.

62 In some cases, this process involved the advice licensees making assumptions—for example, an assumption that every client who paid an annual advice fee of 1% of their assets was likely to be an ongoing advice customer because this was the fee usually charged by the licensee's advisers.

63 We consider that the scope of customers identified by this analysis should extend (if applicable) to at least seven years before the date that the advice licensee identified the systemic failure. A minimum seven-year period is consistent with an AFS licensee's record-keeping obligations and the guidance in RG 256.

Assessment of advice provision

64 To determine whether advice had been provided to customers who had an allocated adviser, advice licensees often needed to conduct a 'manual' or case-by-case review of customers' hard copy or electronic files. This was because the licensees often did not have adequate data or systems to more efficiently determine whether advice was provided to large groups of customers.

65 In many cases, this identification work is ongoing. Several advice licensees are still trying to determine how many customers, and which customers,

were affected by the fee-for-service failures and will require refunds and compensation.

66 In some cases, advice licensees are taking a pragmatic and customer-focused approach to refunds, where the cost and time for the licensee to assess whether ongoing advice was provided to certain groups of customers is likely to outweigh the value of the fees and interest to be refunded to them. In such cases, some advice licensees are paying refunds without going through the full file review process.

Our observations

67 The ability of AFS licensees to efficiently identify affected customers has been affected by factors including:

(a) the nature of the failure and the extent to which affected customers could be identified through the analysis of data and systems, or whether manual checking of customer files was required;

(b) the quality and availability of the licensees' systems, records and data;

(c) the magnitude of the failure—for example, the time period of the failure and the number of potentially affected customers; and

(d) the extent to which the licensees have prioritised and adequately resourced their review and remediation programs.

68 The AFS licensees could generally identify affected customers most efficiently where they could rely on existing data systems rather than manual processes, provided that:

(a) the complete data was available and accessible to the licensees;

(b) record keeping was of a reasonable quality;

(c) the nature of the failure was limited to a specific problem;

(d) the process proposed by the licensee to define and identify affected customers was, in ASIC's view, acceptable; and

(e) the program was adequately resourced and prioritised by the licensee.

Compensation methodologies

69 ASIC's view, which we communicated to the AFS licensees, is that compensation processes for customers affected by the fee-for-service failures identified in this report should comprise the following elements:

(a) a refund of the fees that were incorrectly charged (fee refund);

(b) a payment to compensate for the interest or earnings that would have been earned on the amount of the fee refund if it had not been incorrectly deducted; and

(c) clear communications with affected customers explaining:

  (i) why a refund and compensation was required, and their right to complain or seek a review including through the licensee's dispute resolution system (which includes internal dispute resolution (IDR) and membership of the Financial Ombudsman Service, an external dispute resolution (EDR) scheme); and

  (ii) the basis for their compensation amount and the method of calculation (e.g. interest rate or lost earnings).

Calculating interest or earnings

70 In relation to the interest or earnings calculation, affected customers were generally compensated in one of the following three ways, depending on the quality of the AFS licensee's customer data.

(1) Where data was available and of adequate quality

71 Most licensees advised ASIC that, for the majority of affected customers, they had been able to accurately calculate the interest or earnings that their customers would have earned if the systemic failure had not occurred.

72 This was possible through data analysis of the source of the fees. For example, AFS licensees were able to track the performance of the investment accounts or funds that the fees were deducted from, and to include an equivalent amount in their compensation payments.

(2) Where data was limited

73 In some instances, the advice licensees had some data about the affected customers that would enable them to calculate an approximate compensation amount in a relatively short period of time, but they had inadequate data to enable them to both perform precise individual calculations of loss and compensate customers reasonably promptly.

74 In these cases, the advice licensees calculated the approximate interest or earnings that customers would have received if the systemic failures had not occurred.

75 For example, an advice licensee that had data about the risk profile of its affected customers (e.g. conservative, balanced, growth) based its compensation amounts on the benchmark returns from those asset classes.

76 All customers, if they are unhappy about the compensation they are offered, can seek a review or lodge a complaint through the AFS licensee's IDR process and the Financial Ombudsman Service.

(3) Where no data was available

77 In some instances, the advice licensees had no data about groups of customers to enable them to apply the approach in either (1) or (2), or to do so in a reasonable period of time.

78 A common example was where advice fees were deducted from financial products issued by third parties that were unrelated to the customer's financial institution or advice licensee, and the institution or licensee did not keep relevant data and was unable to obtain such data from the third party as part of its review and remediation assessment.

79 Another example was where advice licensees provided advice services through their authorised representatives and:

(a) the licensees did not retain copies of customers' files; and

(b) the authorised representatives took the client files with them when they departed from the licensee.

Note: To change this conduct in the future, we have amended Class Order [CO 14/923] *Record-keeping obligations for Australian financial services licensees when giving personal advice* to clarify that, when an advice licensee or one of its representatives provides personal advice, the licensee must ensure not only that client records are kept, but also that the licensee continues to have access to these records during the period in which they are required to be retained.

80 In these instances, some licensees have applied a proxy interest rate that is consistent with the principles outlined in paragraph 83. In other cases we are having discussions with licensees to ensure they apply a fair and reasonable compensation methodology: see paragraph 86.

Note: For an example of how an AFS licensee has applied a proxy interest rate in the absence of adequate data to calculate accurate compensation, see Example 8 in RG 256.

Estimating interest or earnings

81 Our clear preference is for the licensees to apply the approach outlined in paragraph 71. This means that customers are compensated in a timely way with an amount that accurately reflects the interest or earnings they lost as a result of the systemic failure.

82 However, we consider that, for the purposes of this project, where customer records are incomplete, it is sometimes acceptable and provides a better outcome for customers if the AFS licensee promptly compensates customers with an approximation of the interest or earnings forgone, as outlined in paragraph 74. In these instances, it is critical that customers are given information about how they may seek a review of the compensation amount.

83 Where licensees have little or no data to calculate compensation, as described in paragraph 77, they should use a fair and reasonable rate to calculate the lost

returns or interest, by applying the following principles which are set out in RG 256:

(a) the rate should be reasonably high—to ensure that clients will not be disadvantaged by an advice licensee’s inability to determine the actual investment returns or interest, and to remove any incentive for licensees to use a proxy to calculate foregone returns or interest instead of working out the actual investment returns or interest that a client would have received;

(b) the rate should be relatively stable (compared, for example, to market-linked returns); and

(c) the rate should be objectively set by an independent body.

84 An example of a rate that meets these criteria is the Reserve Bank of Australia cash rate plus a margin of 6% per year.

85 Some of the licensees that do not have adequate data to perform accurate compensation calculations agreed to implement the principles described in paragraph 77, and this is reflected in the compensation payments made to their customers.

86 In other instances, where licensees failed to keep adequate client records and data, we continue to discuss with licensees the interest rates to be applied to provide a fair and reasonable outcome for customers.

Summary of compensation outcomes and projections

87 Table 2 shows, by banking or financial services institution, the compensation that had been reported to ASIC as paid or agreed to be paid by 31 August 2016. It also shows the future expected compensation.

88 These summary figures are further broken down by AFS licensee in Table 3 and Table 4.

Table 2: Compensation outcomes as at 31 August 2016, and future projections

Group	Compensation paid or agreed to be paid	Estimated future compensation	Total (estimate)
AMP	$2,120,000	$2.4m (see Note 1)	$4.6m
ANZ	$16,202,860	$33.5m	$49.7m
CBA	$575,587	$105.1m plus interest	$105.7m plus interest

Group	Compensation paid or agreed to be paid	Estimated future compensation	Total (estimate)
NAB	$3,523,500	$13.4m plus interest	$16.9m plus interest
Westpac	$1,244,659	Not yet available	$1.2m
Totals	**$23,666,606**	**$154.4m plus interest**	**$178.0m plus interest**

Source: Data is based on estimates provided to ASIC by the institutions and will change as the reviews to determine customer impact continue. For further details, see Table 3–Table 4.

Note 1: AMP's estimate is for compensation where the customer did not have an adviser allocated to them, but does not include a future projection for remediation where the adviser allocated to the customer failed to deliver on their obligation to provide the ongoing advice service and where the AFS licensee failed to ensure that the service was provided.

Compensation progress to date

89 Table 3 shows, by AFS licensee, the compensation paid, or agreed to be paid, to customers as a result of the identified fee-for-service failures, as at 31 August 2016. It shows that approximately $23.7 million has been paid, or agreed to be paid, to over 27,000 customers.

90 Some of the licensees in Table 3 have not yet completed their review and remediation activities. Their estimates of further compensation to be paid are shown in Table 4. We will report publicly on their progress and the outcomes at a later date: see Section F.

Table 3: Compensation progress reported to ASIC as at 31 August 2016

Group	AFS licensee	Customers offered compensation	Compensation amount offered
AMP	AMP Financial Planning Pty Limited, Charter Financial Planning Limited, Hillross Financial Services Limited (see Note 1)	8,178	$2,120,000
ANZ	Australia and New Zealand Banking Group Limited (see Note 2)	4,872	$14,507,451
ANZ	OnePath Custodians Pty Limited	2,389	$1,362,590
ANZ	OnePath Funds Management Limited	129	$145,356
ANZ	OnePath Life Limited	127	$187,463
CBA	Commonwealth Financial Planning Limited	165	$321,797
CBA	Commonwealth Private Limited (see Note 3)	17	$253,652
CBA	Commonwealth Securities Limited (see Note 3)	2	$138
NAB	MLC Investments Limited	96	$49,173
NAB	MLC Limited (see Note 4)	7	$887
NAB	MLC Nominees Pty Limited (see Note 4)	7,597	$1,982,274
NAB	National Australia Bank Limited	2,659	$1,118,747
NAB	Navigator Australia Limited	235	$120,743
NAB	NULIS Nominees (Australia) Pty Limited	529	$251,676
Westpac	Westpac Banking Corporation (see Note 5)	177	$1,244,659
Totals		**27,179**	**$23,666,606**

Note 1: As described at paragraph 126, before this project began, 14 AMP-owned advice licensees had paid further compensation of $193,519 to 196 customers for fee-for-service failures. The compensation for the three licensees shown in this table is not complete: see Table 4 for AMP's estimate of further compensation to be paid.

Note 2: Compensation is not complete: see Table 4 for ANZ's estimate of further compensation to be paid.

Note 3: The table shows compensation paid by Commonwealth Private Limited and Commonwealth Securities Limited arising from the further reviews described in Section C.

Note 4: On 3 October 2016, NAB divested 80% of its shareholding in the MLC Limited Life Insurance business. On 1 July 2016, trusteeship of superannuation assets previously governed by MLC Nominees Pty Limited transferred to NULIS Nominees (Australia) Limited (NULIS) effective 1 July 2016. However, accountability for remediation activity (including compensation) of the above events reported by MLC Limited and MLC Nominees Pty Ltd remains within the NAB Group. See the 'Key terms' for further information.

Note 5: Westpac's failure relates to an individual adviser who was identified by the licensee before our project started. The compensation amount shown relates to fee refunds only; some customers were also offered further compensation for other failures by the adviser, such as inappropriate advice.

Source: ASIC, AFS licensees.

91 Table 4 shows the further compensation estimates provided by the AFS licensees for customers that had not yet been compensated as at October 2016.

92 We note that these estimates are subject to confirmation by the advice licensees. We will provide an update on the licensees' progress and the outcomes at a later date: see Section F.

Table 4: Estimated further compensation, as reported to ASIC in October 2016

Group	AFS licensee	Affected customers	Compensation estimate
AMP	AMP Financial Planning Pty Limited, Charter Financial Planning Limited, Hillross Financial Services Limited (see Note 1)	9,800 (estimate)	$2.4m
ANZ	Australia and New Zealand Banking Group Limited	5,128 (estimate)	$33.5m
CBA	BW Financial Advice Limited	3,000 (estimate)	$4m plus interest
CBA	Commonwealth Financial Planning Limited	40,000 (estimate)	$100m plus interest
CBA	Count Financial Limited	5,000 (estimate)	$1.1m plus interest
NAB	Apogee Financial Planning Limited	554	$156,000 plus interest
NAB	Godfrey Pembroke Limited	1,708	$220,000 plus interest
NAB	GWM Adviser Services Limited	1,909	$490,000 plus interest
NAB	Meritum Financial Group Pty Limited	307	$81,000 plus interest
NAB	MLC Nominees Pty Limited (see Note 2 and Note 3)	108,867	$12.4m plus interest
Totals (of estimates reported to ASIC)		**176,273**	**$154.4m plus interest**

Note 1: AMP's estimate is for compensation where the customer did not have an adviser allocated to them, but does not include a future projection for remediation where the adviser allocated to the customer failed to deliver on their obligation to provide the ongoing advice service and where the licensee failed to ensure that the service was provided.

Note 2: MLC Nominees Pty Limited's failure relates to the deduction of fees for general advice from members of an employer superannuation plan, where there was no financial adviser attached to the plan and members did not receive the general advice services they paid for.

Note 3: On 1 July 2016 trusteeship of superannuation assets previously governed by MLC Nominees Pty Limited transferred to NULIS Nominees (Australia) Limited. However, accountability for remediation activity (including compensation) of the above event reported by MLC Nominees Pty Ltd remains within the NAB Group. See the 'Key terms' for further information.

Source: ASIC, AFS licensees.

C Further reviews

Key points

Apart from the processes to identify and compensate customers affected by the known fee-for-service failures described in Section B, the banking and financial services institutions agreed to conduct further reviews to determine whether they had additional related failures.

Some of these large-scale reviews have been completed, while most still need to be conducted and/or finalised.

As a result of these further reviews, some advice licensees have identified the need for additional customer compensation.

Background

Purpose of review

93 Since the project started, we have written to each of the six banking and financial services institutions covered by the Wealth Management Project, requesting that they conduct further reviews of their advice licensees to determine whether ongoing advice services were being provided to customers who were paying fees for such services, or whether there had been any systemic failure to do so.

94 We requested these further reviews because of the extent of the identified failures for the majority of the banking and financial services institutions, as outlined in Section B. We wanted to gain some assurance that advice licensees did not have further fee-for-service failures.

95 We consider it likely that, where this process identifies further systemic failures, advice licensees will need to compensate customers through review and remediation.

Scope of further reviews

96 We requested that the scope of these reviews should cover:

(a) AFS licensees that are part of the group and that are authorised to give personal advice to retail clients;

(b) the seven-year period preceding our request; and

(c) where sample testing of customer files was used, a sufficient sample to provide meaningful results.

97 Table 5 describes the scope of each review by the banking and financial services institutions.

Table 5: Scope of further reviews

Group	Covers all advice licensees?	Seven-year period reviewed?	Sample test methodology	Expected completion
AMP	No (see paragraph 127)	Yes	Risk-based (see paragraph 127)	September 2017
ANZ	No (see paragraph 132)	Yes	Risk-based (see paragraph 132)	To be confirmed
CBA	Yes	Varied (see paragraphs 104, 110, 135, 140, 144)	Random	2016
Macquarie	No (see paragraph 153)	Yes	Risk-based	To be confirmed
NAB	Yes	Yes	Random and risk-based as appropriate	31 December 2017
Westpac	Yes	Yes	Risk-based	To be confirmed

Source: ASIC, AFS licensees.

Methodology

98 The sampling approach generally took one of two forms:

(a) *random sampling*—where the advice licensee reviewed a sample of randomly selected customer files to attempt to form conclusions about the whole population of ongoing advice customers; or

(b) *risk-based sampling*—where the advice licensee split its population of ongoing advice customers or advisers into two or more groups for the purposes of sample testing, review and remediation. This enabled the licensee to form conclusions about the level of risk or failures in different groups.

99 We were not prescriptive about whether advice licensees should take a random or risk-based approach to sampling. However, we scrutinised the methodologies they applied, or proposed to apply, to ensure that the results would be able to identify, with an acceptable degree of confidence, whether or not there was a similar systemic failure.

100 Most advice licensees obtained external advice or assistance in relation to sampling methodologies.

101 The ability of all of the advice licensees to test the provision of ongoing advice services during the seven-year period was affected by the quality of their data, record keeping and data analytics capabilities. Individual

customer files, either in hard copy or digital format, usually needed to be reviewed manually.

Compensation outcomes

102 As a result of the completed further reviews, two CBA licensees have reported to ASIC that they have paid, or agreed to pay, compensation of approximately $253,790 to 19 customers, as at 31 August 2016.

103 Reviews by all of the banking and financial institutions are continuing, as described below, and the findings may lead to further customer compensation. We will report further on the outcome of these reviews—and, in particular, whether they indicate a systemic failure—at a later date.

Reviews completed

CBA

CFPL 'Pathways' division

104 The majority of Commonwealth Financial Planning Limited's (CFPL) advisers are employees of CBA. However, CFPL also has financial advisers who are self-employed authorised representatives of CFPL, operating within a business unit called 'Pathways'.

105 For this review, CFPL reviewed its Pathways division separately to the review of its employed advisers.

106 The review of Pathways advisers covered the period from 1 July 2008 to 30 June 2014.

107 For each of the six years reviewed, the failure rate was under 5% of customer files and, for three of these years, under 1%. CFPL has reported to ASIC that 34 customers require fee refunds plus interest.

108 We are assessing the implication of these results and discussing with CFPL whether further steps should be taken to identify whether other customers outside of the sample tested should be reviewed.

109 For the identified failures, we are discussing with CFPL the processes and methodology to provide affected customers with refunds and compensation.

Commonwealth Private Limited

Review

110 This advice licensee's review of the provision of ongoing advice services for customers was split into:

(a) a review of the 2014–15 financial year; and

(b) a review of the period from 1 July 2008 to 30 June 2014.

111 For 2014–15, the licensee reviewed the files of all customers who had an ongoing service agreement. This entailed over 1,000 file reviews.

112 The 2014–15 review found that:

(a) by 30 June 2015, 40 customers had not received an annual review for the 2014–15 financial year. These late annual reviews were subsequently provided by 31 December 2015; and

(b) 10 customers did not receive an annual review for 2014–15 and, as a result, received refunds and compensation.

113 For the period from 1 July 2008 to 30 June 2014, the licensee reviewed the files of more than 200 customers, and checked over 850 annual reviews.

Note: Most of the 200 plus customers did not have ongoing service agreements for each year in the six-year period.

114 The review found that seven customers did not receive their annual review at least once during the six-year period. There were 16 instances of an annual review not being provided (across the seven customers) in that period.

115 The licensee is conducting a further review of its retail ongoing advice customers for the 1 July 2008 to 30 June 2014 period who were not included in the samples above to determine if additional customers should be compensated.

Remediation

116 The licensee advised ASIC that, for customers who did not receive a formal annual review for 2014–15 by 30 June 2015, annual reviews were subsequently completed by 31 December 2015.

117 For the 10 customers who did not receive an annual review for 2014–15, the licensee compensated these clients with refunds and interest totalling $93,924.

118 For customers who were found not to have received annual reviews in the period from 1 July 2008 to 30 June 2014, the licensee refunded the annual fees they paid, plus interest. This resulted in payments of $159,728.

119 Interest added to the refunds was calculated at 6% per year. The licensee advised ASIC that 6% per year exceeded the actual interest rate on the

accounts that the fees were drawn from, at all times during the six-year period, so customers would not be disadvantaged by the use of this rate.

Commonwealth Securities Limited

Review

120 This advice licensee's review identified that 10 advisers had an ongoing service agreement with some of their customers during the period from 1 July 2008 to 30 June 2015.

121 The licensee reviewed the customer files of these advisers, entailing approximately half of the customers who had ongoing service agreements. This sample review checked the service delivery in every financial year from 1 July 2008 to 30 June 2015, or for the life of the agreement if that was shorter.

122 The licensee reported to ASIC that:

(a) from 1 July 2008 to 30 June 2013, it identified no instances of failure to provide an ongoing service; and

(b) from 1 July 2013 to 30 June 2015, one adviser had ongoing service agreements with two customers where a fee was charged but the required service was not provided.

Remediation

123 The licensee paid compensation of $138 to two customers for the failures.

Reviews not yet completed

AMP advice licensees

Initial review

124 AMP initially conducted a review covering 14 advice licensees for the period from 1 July 2010 to 30 June 2015. AMP chose 1 July 2010 as the start date because this was when AMP licensees introduced fee-for-service arrangements for investment products, instead of commissions.

125 The licensees included in the initial review were:

(a) AMP Financial Planning Limited;

(b) Charter Financial Planning Limited;

(c) Forsythes Financial Services Pty Limited;

(d) Genesys Wealth Advisers Limited;

(e) Hillross Financial Services Limited;

(f) Ipac Securities Limited;

(g) King Financial Services Pty Limited;

(h) PPS Lifestyle Solutions Pty Limited;

(i) Prosperitus Pty Limited;

(j) SMSF Advice Pty Limited;

(k) Strategic Planning Partners Pty Limited;

(l) TFS Financial Planning Pty Limited;

(m) Total Super Solutions Pty Limited; and

(n) Tynan McKenzie Pty Limited.

126 The initial review of data from previous audits and complaints identified, across the 14 licensees, 196 instances of failure to provide customers with an ongoing advice service they had paid for. Affected customers had already been paid, before our project commenced, compensation of $193,519 for these failures.

Note: This figure is not included in Table 2 or Table 4 in Section B because it relates to compensation paid prior to our project.

Wider review

127 In May 2016, AMP agreed to conduct a wider review for the period from 1 July 2008 to 30 June 2015, using a methodology that would:

(a) include the 15 AMP-owned advice licensees that charged ongoing service fees in the relevant period;

(b) exclude the two advice licensees that did not charge ongoing service fees in the relevant period;

(c) initially focus on identifying and reviewing advice practices considered by AMP to have a higher risk of non-compliance; and

(d) entail a subsequent review of practices perceived to be lower risk.

128 AMP has commenced this review, which it expects to complete by September 2017.

ANZ advice licensees

Initial review

129 ANZ initially conducted a small risk-based review, covering the following licensees for the period from 1 July 2013 to 30 June 2015:

(a) Financial Services Partners Pty Limited;

(b) Millennium3 Financial Services Pty Limited; and

(c) RI Advice Group Pty Limited.

130 ANZ reviewed 50 files across the three licensees. The files were selected by ANZ based on the perceived risks, using factors such as the size of an authorised representative's practice and whether it had recently been acquired by ANZ or the licensee.

131 ANZ reported that it had not identified, from this initial review, any failure to provide ongoing advice services to customers. However, the review did identify instances of incorrect fee disclosure in fee disclosure statements.

Wider review

132 In June 2016, ANZ proposed a methodology that would:

(a) include the three advice licensees covered in the initial review;

(b) initially focus on identifying advisers considered by ANZ to have a higher risk of non-compliance;

(c) entail reviewing higher-risk advisers by selecting a sample of their customers, based on the size of their customer book; and

(d) entail reviewing lower-risk advisers by selecting a sample of customers from these advisers.

133 ANZ has commenced this wider review.

CBA

BW Financial Advice Limited

134 This advice licensee is still in the process of identifying customers affected by the known systemic failure described in Section B and referred to in Table 4. The licensee found that this known failure affected customers during a four-year period between 2 November 2010 and 30 June 2014.

135 We requested that the licensee conduct further reviews for the other three years in the July 2008 to 30 June 2015 period, to determine whether customers received the ongoing services they paid for during those years.

136 For two of those years (1 July 2008 to 31 October 2010), the licensee advised that it did not offer an ongoing advice package, and that a review of a random sample of 59 customer files for that period found no instances of advisers entering an ongoing fee or service arrangement with customers.

137 To review the delivery of ongoing advice in the remaining year during the period (i.e. 1 July 2014 to 30 June 2015), the licensee is testing service delivery and will report on the results to ASIC.

Commonwealth Financial Planning Limited

138 This advice licensee is still in the process of identifying customers affected by the known systemic failure described in Section B and referred to in Table 4. This failure relates to an ongoing service package that was available to new customers until 30 June 2013 and which some existing customers continued to pay for after that date.

139 The licensee is currently conducting further reviews to determine whether customers received the ongoing services they paid for in a new ongoing service package that was introduced in July 2013.

Count Financial Limited

140 This advice licensee reviewed a sample of 385 files for customers who had ongoing service agreements in the period from 1 January 2009 to 30 June 2015, and in some cases contacted advisers and customers for further information.

141 The licensee reported to ASIC that it found evidence of ongoing service delivery in 98% of the sample, leaving the failure rate at 2%.

142 We are currently reviewing further information obtained from the licensee to validate these results and to consider the potential implications for the licensee's wider population of customers.

143 For customers where a failure has been identified, we are discussing with the licensee its process to communicate with and compensate the customers.

Financial Wisdom Limited

144 This advice licensee reviewed a sample of 224 files for customers with ongoing service agreements in the period from 1 January 2009 to 30 June 2015 and, in a similar process to Count Financial Limited, in some cases contacted advisers and customers for further information.

145 The licensee reported to ASIC that it found substantial evidence of service delivery in 98% of files, leaving the failure rate at 2% of the sample.

146 As with Count Financial Limited (see paragraph 142), we are currently reviewing further information obtained from the licensee to validate these results and to consider the potential implications for the licensee's wider population of customers.

147 For customers where a failure has been identified, we are also discussing with the licensee its process to communicate with and compensate the customers.

NAB

148 NAB is reviewing customer files for the period from 1 July 2008 to 30 June 2015 across its advice licensees, and has engaged an external consultant for advice on an appropriate and statistically valid sampling methodology.

149 By 31 August 2016, NAB's external consultant had reviewed a sample of 59 files for the period from 1 July 2013 to 30 June 2015 for the National Australia Bank Limited AFS licensee (NAB Financial Planning). The review excluded customers who were already being reviewed and compensated in connection with the fee-for-service failures described in Section B.

150 The consultant's initial findings were that:

(a) 54 files (92%) contained evidence that suggested the customer received 'services or an offer of service as per their service agreement'; and

(b) five files (8%) contained no evidence of service delivery.

151 NAB is currently investigating whether this failure rate may indicate a wider systemic failure, and is taking steps to compensate customers where a service delivery failure has been confirmed.

152 NAB has recently advised ASIC that it may not be able to complete reviews of its other advice licensees until 31 December 2017. We are discussing the adequacy of this proposed timeframe with NAB.

Macquarie

Scope of review

153 Macquarie's review covered one advice licensee—Macquarie Equities Limited.

154 The review excluded two other advice licensees:

(a) Macquarie Bank Limited told us that in limited instances it provides advice to retail clients, which are predominantly superannuation funds with less than $10 million in assets. It advised that these clients are recorded in the same systems as Macquarie Equities Limited clients, so the review of complaints for such clients would be captured as part of the Macquarie Equities Limited analysis described below.

(b) Risk Advice Specialists Pty Limited predominantly provided insurance services and ceased to hold its AFS licence in October 2015. Insurance services are not generally paid for through ongoing advice fees.

155 Macquarie Equities Limited's business model differs from the other financial institutions covered by this report, as it generally has a greater focus on equities (direct shares) advice and transactions.

156 The review of Macquarie Equities Limited comprised the following key elements:

(a) review of advice templates;

(b) review of relevant customer complaints;

(c) review of advice fee documentation; and

(d) sample testing of client files.

157 The timeframes for the review were:

(a) advice fee data from relevant commission systems—from 1 July 2013 to 31 July 2015; and

(b) complaint and client file review data since 2004.

Findings

158 Macquarie found the following from its review:

(a) *Complaints data*: 18 complaints were identified since May 2005 where customers alleged that a fee was charged but no service was provided, or raised concerns about the level of service provided. Macquarie reported that approximately half of these cases resulted in compensation, while the remaining complaints were not upheld.

(b) *Customer file reviews*: a customer file was reviewed from each of 32 advisers who were high fee earners. Macquarie reported that the review did not find any instances where ongoing advice services had not been provided to customers.

159 We are currently obtaining further information and clarification from Macquarie about the scope of its review and whether it is sufficient to address ASIC's requirements.

Westpac

160 In January 2016, we wrote to Westpac to request that it review all advice licensees in the Westpac group to determine whether there were systemic issues relating to the incorrect charging of advice fees in the period from 2008.

161 We wrote to Westpac later than the other banking and financial services institutions because of a separate investigation that ASIC is conducting in relation to a Westpac adviser who was reported to ASIC (as referred to in Table 3, note 5).

162 Westpac agreed to review the period from 1 July 2008 to 31 December 2015 covering the following licensees:

(a) Magnitude Group Pty Limited;

(b) Securitor Financial Group Limited; and

(c) Westpac Banking Corporation.

163 We are currently discussing with Westpac an appropriate methodology for its review.

D Systems changes

Key points

We asked the AFS licensees that had found fee-for-service failures to describe any changes being made to their systems and processes.

Some of the licensees gave details of the changes they had made to their supervision and monitoring systems, which they expected to help prevent similar failures from happening in the future, or to enable early detection of failures if they did occur. Some consider their existing systems are adequate, and some are still in the course of considering or implementing changes.

Background

164 We asked the AFS licensees that had identified fee-for-service failures for information about the changes being made to:

(a) resolve the cause of the failures;

(b) reduce the likelihood of similar failures recurring in the future; and

(c) increase the likelihood that such failures would be detected if they did occur.

165 This section summarises the licensees' responses to date. We have not yet assessed the operating effectiveness of these recent changes.

166 Some of the advice licensees that had not identified systemic fee-for-service failures outlined the reasons why they considered their current systems to be adequate.

167 We have provided comments to several AFS licensees in relation to areas where we consider improvements could be made. We will report publicly on further changes at a later date.

168 This section does not describe changes made to systems which were made before our project commenced, but which may also have reduced the likelihood of fee-for-service failures occurring in the future. Some of these changes were prompted by the introduction of the FOFA reforms, which we also expect will reduce the likelihood of similar systemic failures in the future: see paragraphs 42–48.

Licensees that have implemented changes

AMP

169 AMP advised us of changes it has made to its systems to help prevent a recurrence of the identified fee-for-service failures, including:

(a) monthly reporting to monitor whether ongoing advice fees have been switched off following instructions from customers to do so;

(b) processes to ensure that instructions to switch off advice fees are provided to all relevant product divisions; and

(c) a new process where AMP will contact external product providers to request that advice fees are switched off and to monitor that this occurs, rather than relying on customers to contact these product issuers.

170 AMP advised us of further work being implemented over the next four months, including:

(a) assigning a 'process owner' to ensure that fees are switched off in accordance with instructions received from customers;

(b) establishing clearer roles and responsibilities within AMP in relation to switching off advice fees; and

(c) investigating whether automated systems processes, rather than manual processes, can be developed to ensure that relevant advice fees are switched off.

ANZ

171 Since identifying the systemic failure in 2013, ANZ Financial Planning has advised us that it has made changes to its controls and practices for delivering the Prime Access service. These are summarised below.

System controls

172 ANZ advised ASIC that:

(a) all advisers are now required to create records of providing documented annual reviews to customers, which are stored on ANZ's systems;

(b) automated alerts are sent to advisers to prompt them to complete ongoing service obligations when they are due;

(c) daily reports are provided to advisers and managers identifying customers with outstanding documented annual reviews, requiring action;

(d) compliance checks and monitoring have increased their focus on whether ongoing services have been delivered;

(e) in preparing fee disclosure statements, there is a requirement for documentary evidence that an annual review has been completed (if this is stated in the fee disclosure statement); and

(f) a new team has been established with end-to-end responsibility for ensuring that Prime Access services are delivered—with responsibilities including monitoring and oversight of the delivery of services, assessing whether systems and processes are functioning effectively and are fit for purpose, and regular and effective reporting provided to management.

173 ANZ advised that, in some instances, fees and membership for Prime Access services had been switched off—for example, where the customer could not be contacted, had moved permanently overseas, was unwilling to participate in the documented annual review process, or had repeatedly not attended scheduled meetings.

Remuneration

174 ANZ has revised its remuneration scheme by introducing ongoing service delivery measures that must be satisfied for planners to be eligible for performance bonuses, including that there are no overdue annual review meetings for Prime Access customers in each quarter, and that at least 95% of all Prime Access obligations have been met within a 12-month fee disclosure period.

Management oversight and governance

175 ANZ told us that it has introduced detailed regular reporting to senior management on the delivery of Prime Access services, with failures to be documented and remediated.

Training

176 ANZ advised us that it has provided training and communications to advisers, managers and support staff on:

(a) their obligations in delivering ongoing services under Prime Access;

(b) the changes to processes and reporting; and

(c) remuneration scheme changes.

Review and assurance

177 ANZ informed us that, since identifying the Prime Access fee-for-service failures, its testing has identified the need for improvements to controls and practices, as described above. ANZ states that it is continuing to develop ways to improve the delivery of the Prime Access service.

CBA

Commonwealth Private Limited

178 This advice licensee advised ASIC that it has made changes to its:

(a) monitoring and workflow system used by advisers and managers; and

(b) supervision and monitoring policies and procedures.

179 The licensee advised ASIC that it had made a number of changes to its annual review monitoring tool that had been introduced in 2013, including:

(a) automatic reminders to be sent to advisers and their managers 30 and 60 days before the annual review is due;

(b) increased monitoring and testing of whether annual reviews are completed on time;

(c) notification of identified failures to management; and

(d) reporting of compliance testing results to the licensee's Compliance Review Committee.

180 However, we considered that the tool was failing to operate effectively because it did not prevent the fee-for-service failures that subsequently occurred, or it failed to detect them after they had occurred.

181 The licensee has now informed ASIC that it has made further improvements to its existing systems and processes by:

(a) improving recording of customer interactions related to annual reviews;

(b) implementing adviser training; and

(c) reporting to management about the effectiveness of these changes.

NAB

MLC Limited, MLC Nominees Pty Limited, MLC Investments Limited, NULIS Nominees (Australia) Limited, Navigator Australia Limited

182 NAB commissioned an external compliance consultant to assess the design and implementation of the process to review and remediate these licensees, and the sustainability of NAB's risk controls. The consultant's report has been provided to ASIC.

183 The consultant recommended that NAB should introduce an automated process to switch off advice fees when a customer requests that the services of their adviser be discontinued.

184 In the meantime, a quality assurance process and other manual (non-automated) controls have been implemented, which the consultant stated

were a reasonably strong short-term solution that would significantly reduce the risk of customers affected by a failure being missed.

185 The consultant noted that, because the temporary control was manual, it would be subject to potential human error; however, if a failure did recur, a control had been put in place to enable early detection and this was likely to be effective.

186 The consultant recommended that:

(a) NAB should implement the automated controls; and

(b) when the automated controls were introduced, NAB should perform a check to establish whether any customers affected since 30 November 2015 had not been remediated, and if not, to remediate such customers.

187 NAB has committed to implementing these recommendations.

NAB Financial Planning

188 NAB has made some changes to its risk controls within its National Australia Bank Limited AFS licensee (NAB Financial Planning), including that:

(a) a monthly report is to be produced, identifying incorrectly applied ongoing advice fees; and

(b) a new staff position has been created to monitor that customers transferring from an advice service to a no-advice service will have their advice fees switched off.

Institutions not described in this section

189 This section does not refer to changes made by:

(a) Macquarie—because, as described at paragraph 7, Macquarie had not identified a fee-for-service failure at the date of this report; and

(b) Westpac—because, at the time of writing this report, Westpac had only reported a fee-for-service failure in relation to one of its financial advisers. Westpac's further reviews to determine whether there are additional fee-for-service failures are not complete, as described in Section C.

E Our observations

Key points

In this section, we record our observations on:

- the fee-for-service failures of AFS licensees covered by this project; and
- steps taken by licensees to identify and compensate customers in an efficient, honest and fair manner.

We identified that some licensees showed a commitment to identifying and compensating customers in a timely way.

However, following our review, we were also concerned that:

- some licensees prioritised advice revenue and fee generation over ensuring that they delivered the required services;
- some licensees did not have adequate systems, data, policies and procedures in relation to the provision of ongoing advice services;
- some licensees adopted an overly legalistic, rather than customer-focused, approach to customer compensation;
- without ASIC's intervention, some customer remediation programs proposed by the licensees may have led to poor customer compensation outcomes; and
- cultural factors contributed to the issues identified in this report.

We describe the reasons for these observations in more detail below.

190 Our analysis of the fee-for-service failures and our work with the AFS licensees to ensure customers affected by those failures are identified and compensated has led us to make certain observations about:

(a) remuneration practices;

(b) record keeping and monitoring of advisers;

(c) approach to review and remediation of customers; and

(d) the way in which the culture of the licensees may have contributed to the fee-for-service failures and the impact of these failures on customers.

Remuneration

Prioritisation of revenue over service

191 ASIC considers that the fee-for-service failures show that AFS licensees and advisers prioritised revenue and fee generation over the delivery of advice and services paid for by their customers. For example, we are concerned that:

(a) licensees did not have systems in place to ensure that services were being provided in return for the fees being charged. By contrast, the licensees had much more effective systems for recording incoming revenue;

(b) advisers were allowed to have many more ongoing advice customers on their books than they would have been able to monitor or advise on an annual basis. For example, some advisers had many hundreds of customers—often having 'inherited' these customers, and the stream of fee revenue, from other advisers who had departed from the licensee; and

(c) some licensees charged fees for services that, arguably, had limited value for customers. For example, the customers of one licensee paid ongoing fees for services that included 'Retention of client records by your adviser … Retaining this information may reduce the cost of providing additional advice and service in the future'. However, all AFS licensees already have legal obligations to keep client records for seven years.

192 These observations indicate that advice licensees did not adequately monitor and supervise their representatives, or have had adequate business systems and practices.

Fee maximisation

193 Section A describes how a prevalent form of adviser remuneration in the financial advice industry is based on automatic deductions and payments—traditionally for sales commissions, but also for other payments such as adviser service fees based on the value of customers' assets. There is generally no specific service connected to the payment of commissions and, in many cases, the licensees have found that they and their advisers did not provide specific services that fee-paying customers were entitled to.

194 The FOFA reforms in 2013 banned certain commissions for new advice, and required increased transparency around fees charged and services provided through fee disclosure statements and opt-in renewal notices. However, we are concerned that the industry (including licensees and advisers) may still have a culture of reliance on ongoing trail revenue (through commissions and fees) for a portion of their income, without necessarily providing advice to customers in return.

195 We saw instances of fee arrangements where, in the licensees' view, there was no obligation to provide advice to customers in return for the fees they paid.

196 For example, some advice licensees considered that their ongoing service obligation was satisfied if an adviser offered or *attempted* to offer an annual review (e.g. by making three unanswered phone calls), even if this review was not provided. We are concerned that, regardless of whether there is a

legal basis to support such an approach, this may indicate business practices that support revenue and fee generation over service delivery to customers. As discussed below, we consider that this indicates there are cultural factors within the advice licensees and the institutions that need to be addressed.

Record keeping and monitoring

Data, systems and record keeping

197 We are concerned that advice licensees and advisers failed to keep adequate records or data to enable monitoring and analysis of ongoing service provision. During this project, we note the continued reliance by some licensees on hard copy customer files (which were often incomplete) to demonstrate service delivery.

198 The impacts of advice licensees' record-keeping systems and practices on this project included:

(a) significant difficulties and delays in licensees identifying affected customers;

(b) an absence of customer files, meaning that licensees were unable to determine whether customers received the services they paid for; and

(c) the inability of licensees to accurately calculate the refunds and compensation owing to customers, meaning that proxy interest or earnings rates needed to be applied to compensation payments.

199 Having proper information and data systems is fundamental to running a financial services business, supervising and monitoring representatives and ensuring that customers receive the services they pay for.

Note: As noted earlier, we have amended [CO 14/923] to clarify advice licensees' record-keeping obligations.

Policies and procedures

200 We are concerned that advice licensees failed to develop and enforce policies and procedures to ensure that:

(a) ongoing advice services were provided to customers who paid for them;

(b) fees would not be charged for ongoing advice services that were not provided; and

(c) fees would be switched off, and customers compensated, if customers continued in successive years to pay ongoing advice fees without receiving advice.

Review and remediation

201 Some advice licensees and product issuers that identified fee-for-service failures showed a commitment to identifying affected customers and paying refunds and compensation in a timely and acceptable way.

202 Positive aspects of these licensees' approaches to review and remediation included:

(a) a proactive approach in identifying affected customers; and

(b) a commitment to developing an acceptable and customer-focused methodology for paying refunds and compensation, and implementing the process within a reasonable timeframe after it was agreed with ASIC.

203 However, we also found that on some occasions licensees initially proposed review and remediation processes that were legalistic and not focused on customers' interests. Examples of such proposals are:

(a) an opt-in approach for customer remediation;

(b) review and compensation of customers over a six-year period instead of seven years; and

(c) a narrow or legalistic approach to defining affected customers.

204 Following our intervention, the licensees generally revised their review and compensation processes to meet our expectations. We are still discussing aspects of some review and remediation processes with the licensees. We note that the need for us to intervene and review all remediation processes carefully and insist on changes has caused delays to customer compensation.

Cultural indicators

205 Culture is a set of shared values or assumptions. Values are what an organisation chooses to prioritise, and these shared values can shape and influence people's attitudes and behaviours towards, for example, treatment of customers and compliance.

206 ASIC is concerned about culture because it is a key driver of conduct within the financial services licensees that we regulate, and the financial services industry more broadly.

207 Where there are systemic failures in an organisation, the culture of that organisation is very likely to have been a contributing factor.

208 The information we have gathered for this project to date suggests that cultural factors in the specific banking and financial services institutions and advice licensees covered by this report—in particular, those where multiple

advisers and a large number of customers were involved—contributed to the systemic failures we observed. These systemic failures had direct impacts on outcomes for customers, including:

(a) financial advisers failing to provide ongoing advice services to customers who paid ongoing service fees; and

(b) relevant licensees' staff and management failing to put in place systems (e.g. for data, compliance and record keeping) to ensure such services were provided to customers who paid these fees.

209 Of particular concern is that many of the banking and financial services institutions covered by this review publicly state that their core values include being customer focused, 'doing what is right' for customers, and acting with integrity.

210 We encourage the institutions reviewed in this report to consider how their culture may have supported these systemic failures, and why their stated commitment to providing excellent service to customers is not translating into good outcomes for customers in the many instances we identified in this report.

Next steps

211 In an organisation, values and cultural leadership must come from the top. The role of the board, senior executives and management is critical in setting the right culture.

212 During this project, we have been in regular contact with senior executives of the banks and financial services institutions in relation to the issues identified in this report.

213 In addition, a copy of this report will be provided to the boards of each of the banks and financial services institutions that were covered by the review, including for the attention of the boards' risk committees. We will also meet with these institutions to discuss the findings and implications of this report.

F Future reporting

Key points

Advice licensees are expected to complete their customer review and remediation for each of the systemic failures described in Section B by 30 June 2017 or earlier.

The further reviews described in Section C will be completed after that.

We will report publicly on compensation outcomes.

214 As described in Section B, some of the review and remediation processes initiated by the advice licensees are large scale and complex, and substantial work remains to be completed by the licensees.

215 We expect that compensation may increase substantially in the coming months as the process to identify and compensate affected customers continues.

216 As described in Section C, most of the advice licensees have yet to complete their further reviews.

217 We will continue to monitor the advice licensees’ implementation of both the review and remediation processes, and the further reviews instigated at ASIC’s request. This will include regular progress reporting by the licensees to ASIC.

218 We intend to provide a public update, via media release, on the progress and outcomes of these review and remediation activities in the first half of 2017.

Key terms

Term	Meaning in this document
advice	Personal advice given to retail clients
advice licensee	An AFS licensee that provides personal advice to retail clients
adviser	A natural person providing personal advice to retail clients on behalf of an AFS licensee who is either: • an authorised representative of a licensee; or • an employee representative of a licensee
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services Note: This is a definition contained in s761A.
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act Note: This is a definition contained in s761A.
AMP	AMP Limited
ANZ	Australia and New Zealand Banking Group Limited
ASIC	Australian Securities and Investments Commission
authorised representative	A person authorised by an AFS licensee, in accordance with s916A or 916B of the Corporations Act, to provide a financial service or services on behalf of the licensee Note: This is a definition contained in s761A.
CBA	Commonwealth Bank of Australia
CFPL	Commonwealth Financial Planning Limited
Corporations Act	*Corporations Act 2001*, including regulations made for the purposes of that Act
customer (or client)	Retail client
fee disclosure statement	A document required by s962G to be given in accordance with Div 3 of Pt 7.7A of the Corporations Act. Specifically, it is a statement in writing provided by a fee recipient to their client about the previous 12 months of their ongoing fee arrangement, including information about the amount of fees paid by the client, the services received by the client, and the services that the client was entitled to receive

Term	Meaning in this document
fee-for-service failure	The systemic failure to deliver ongoing advice services to customers who are paying fees to receive these services, or the incorrect charging of ongoing advice fees to customers who do not have an adviser allocated to them
fee recipient	A fee recipient is: • the AFS licensee or its representative who enters into the ongoing fee arrangement with the client; or • if the rights of the person who entered into the ongoing fee arrangement have been assigned, the person who currently holds those rights Note: See s962C of the Corporations Act for the exact definition.
financial advice	Financial product advice
financial adviser	See 'adviser'
financial product	Generally, a facility through which, or through the acquisition of which, a person does one or more of the following: • makes a financial investment (see s763B); • manages financial risk (see s763C); • makes non-cash payments (see s763D) Note: See Div 3 of Pt 7.1 of the Corporations Act for the exact definition.
financial product advice	A recommendation or a statement of opinion, or a report of either of these things, that: • is intended to influence a person or persons in making a decision about a particular financial product or class of financial product, or an interest in a particular financial product or class of financial product; or • could reasonably be regarded as being intended to have such an influence. This does not include anything in an exempt document Note: This is a definition contained in s766B of the Corporations Act.
FOFA	Future of Financial Advice
Macquarie	Macquarie Group Limited

Term	Meaning in this document
NAB	National Australia Bank Group of Companies Note: On 3 October 2016, National Australia Bank Limited divested 80% of its shareholding in the MLC Limited Life Insurance business. Accordingly, MLC Limited ceased to form part of the NAB Group of companies. Ahead of the sale, superannuation members from the registrable superannuation entities (RSE) governed by MLC Nominees Pty Limited were transferred into a new RSE governed by NULIS Nominees (Australia) Limited. At this time, MLC Limited ceased its role as administrator of the former RSE. Regardless of these changes, NAB retains accountability for remediation of events reported by MLC Limited and MLC Nominees Pty Limited that are included in this report.
ongoing fee arrangement	An ongoing fee arrangement exists when an AFS licensee or its representative gives personal advice to a retail client and the retail client enters into an arrangement with the AFS licensee or representative, the terms of which provide for the payment of a fee during a period of more than 12 months
ongoing service agreement	An agreement between a customer and an AFS licensee or its representative, where the AFS licensee or its representative agrees to provide ongoing advice services to the customer
personal advice	Financial product advice that is given or directed to a person in circumstances where the provider of the advice has considered one or more of the person's objectives, financial situation and needs, or a reasonable person might expect the provider to have done so Note: See s766B(3) of the Corporations Act for the exact definition.
retail client	A client as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations 2001
RG 256 (for example)	An ASIC regulatory guide (in this example numbered 256)
s913B (for example)	A section of the Corporations Act (in this example numbered 913B)
Westpac	Westpac Banking Corporation

Related information

Headnotes

advice licensee, AFS licensee, annual review, banking and financial services institutions, client files, compensation, fee disclosure statement, ongoing advice fees, ongoing advice service, ongoing service agreement, remediation, review

Legislative instruments

[CO 14/923] *Record-keeping obligations for Australian financial services licensees when giving personal advice*

Regulatory guides

RG 256 *Client review and remediation conducted by advice licensees*

Legislation

Corporations Act, s766B(3)

Consultation papers and reports

CP 247 *Client review and remediation projects and update to record-keeping requirements*

REP 407 *Review of the financial advice industry's implementation of the FOFA reforms*

Media releases

15-081MR *ASIC update on Wealth Management Project—Investigation into charging of advice fees without providing advice*

15-101MR *ASIC to give guidance on review and remediation in the financial advice industry*

15-388MR *ASIC releases draft guidance on review and remediation projects and proposed changes to record-keeping requirements for advice licensees*

16-188MR *ASIC bans former ANZ financial adviser*

