

3 February 2022

By email: AdviceReview@treasury.gov.au

Retirement, Advice and Investment Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Secretariat

Quality of financial advice review – Draft Terms of Reference

Thank you for the opportunity to comment on [Draft Terms of Reference \(December 2021\)](#) (Draft TOR) for the Quality of Financial Advice Review (**Advice Review**).

About Consumer Action Law Centre

Consumer Action is an independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work, campaigns, outreach, community engagement and more. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just marketplace for all Australians.

Executive Summary

Conflicted remuneration is the root cause of many of the problems uncovered by the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**). The Advice Review is a critical opportunity to end conflicted remuneration in financial advice and insurance for good.

The Draft TOR states the Government is commissioning the Advice Review 'consistent with' the following recommendations of the Final Report of the Royal Commission:

Recommendation 2.3 — Review of measures to improve the quality of advice

In three years' time, there should be a review by Government in consultation with ASIC of the effectiveness of measures that have been implemented by the Government, regulators and financial services entities to improve the quality of financial advice. The review should preferably be completed by 30 June 2022, but no later than 31 December 2022. Among other things, that review should consider whether it is necessary to retain the 'safe harbour' provision in section 961B(2) of the Corporations Act. Unless there is a clear justification for retaining that provision, it should be repealed.

Recommendation 2.5 – Life risk insurance commissions

When ASIC conducts its review of conflicted remuneration relating to life risk insurance products and the operation of the ASIC Corporations (Life Insurance Commissions) Instrument 2017/510, ASIC should consider further reducing the cap on commissions in respect of life risk insurance products. Unless there is a clear justification for retaining those commissions, the cap should ultimately be reduced to zero.

Recommendation 2.6 – General insurance and consumer credit insurance commissions

The review referred to in Recommendation 2.3 [the current review] should also consider whether each remaining exemption to the ban on conflicted remuneration remains justified, including: the exemptions for general insurance products and consumer credit insurance products; and the exemptions for non-monetary benefits set out in section 963C of the Corporations Act.

However, the Advice Review cannot be said to be meaningfully implementing these recommendations without considering Commissioner Hayne’s commentary on the conflicts between interest and duty in financial services. These findings, and the evidence at the Royal Commission of atrocious sales behaviour motivated by commissions and incentives,¹ appear to have been forgotten in the drafting of the TOR, which make no reference to these issues. Treasury’s landing page for the Advice Review makes no reference to ‘conflicted remuneration’ or even ‘insurance’.² A casual reader may not discern that the Advice Review purports to implement Commissioner Hayne’s recommendations to review conflicted remuneration in life and general insurance.

For the Advice Review to have any credibility in responding to the recommendations of the Royal Commission, the Draft TOR must be expanded to include the following additions at paragraph 4:

1. The Review should have regard to the findings and commentary of the Financial Services Royal Commission regarding conflicts between duty and interest in financial services and advice, and the benefits of removing all forms of conflicted remuneration
2. The Review should have regard to the need to ensure good consumer outcomes and preventing misconduct and harm.

This submission primarily comments on conflicted remuneration in insurance, but our concerns about the harm caused by conflicted remuneration—and the benefits to consumers in removing all forms of conflicted remuneration—also extend to financial advice more broadly.

Evidence at the Royal Commission

Below we include a brief refresher on some of the harm caused by conflicted remuneration that was uncovered by the Royal Commission. We strongly recommend that the Interim and Final Reports, including the two volumes Case Studies and Appendices, are reviewed in full for the purposes of the Advice Review.

Life insurance

As Commissioner Hayne noted:

Conflicts between an adviser’s duty to his or her client and an adviser’s interests are a particular issue where financial advice is given in connection with insurance products, because insurance products were excluded from aspects of the Future of Financial Advice (FoFA) reforms designed to address those conflicts.³

These conflicts were apparent in the appalling selling practices of ClearView and Freedom Insurance, which were predominantly driven by conflicted remuneration including commissions and incentives.

The Reverend Grant Stewart gave evidence to the Royal Commission of the aggressive selling and retention practices of Freedom Insurance, when it cold-called his son, who has Down Syndrome, and sold him life insurance that he didn’t want or need. Mr Stewart’s evidence, as summarised by Commissioner Hayne in the Final Report, is included at **Appendix A**.

¹ <https://www.smh.com.au/business/banking-and-finance/insurer-sold-life-cover-to-26-year-old-with-down-syndrome-20180911-p5030w.html>.

² <https://treasury.gov.au/consultation/c2021-224992>, accessed 1 February 2022.

³ Final Report, Vol 1, p 279.

Freedom Insurance admitted its provision of sales incentives to direct sales staff, including commissions, a 'boat party' and a trip to Bali, encouraged aggressive and inappropriate sales,⁴ in particular to vulnerable customers.⁵ This is supported by evidence of complaints reported to ASIC by Freedom which were all made by family members in relation to customers living with a disability, bar one.⁶ Freedom also gave evidence of selling accidental death policies to customers attempting to cancel their life insurance,⁷ noting that only 28.5% of calls where customers were seeking to cancel were able to cancel their policies.⁸

Commissioner Hayne found:

Between 2013 and 2015, Freedom used a volume-based commission structure. In about 2015, Freedom began introducing variants to this model. Amongst other things, Freedom introduced requirements that sales agents cover their 'seat cost', and the cost of their leads, before they would be eligible to earn commission. Mr Orton conceded that this increased the possibility that sales agents would engage in aggressive sales tactics. More broadly, Mr Orton recognised that Freedom's commission structure over recent years had created a situation in which sales agents had been incentivised to pursue sales aggressively.

...

Freedom informed ASIC that from 1 October 2018, no commission-based incentives would be paid to Freedom's sales teams. Mr Orton told the Commission that this was because of concerns that commissions may inappropriately influence the conduct of sales agents: in Mr Orton's words, 'any commission payable [to] a sales agent has the potential to be conflicted'.⁹

The Royal Commission heard that the sales representative involved had been warned about their behaviour and was the subject of complaints – despite this, was praised by the team leader for "smashing over 200 lives and earning amazing commissions".¹⁰

Mr Stewart, following his evidence, criticised the practice of paying commissions to insurance sales staff, saying this gave staff the incentive to "make sales and hang the consequences, really."¹¹ Mr Stewart also stated that these practices had a lasting impact on his son, who blamed himself for the sale and who had lost self-confidence.¹²

The harm caused by commission-motivated selling was not unique to Freedom Insurance. Witness statements to the Royal Commission revealed that \$6.1 billion was paid in commissions by 10 insurers to financial advisers in connection with the sale of life insurance products in about five years.¹³ The Chief Actuary and Chief Risk Officer of ClearView Wealth Limited, accepted at the Royal Commission that 'ClearView's commission structure was a contributor to inappropriate behaviour, as it incentivised aggressive sales tactics with the aim of making as many sales as possible at whatever cost.'¹⁴

⁴ Royal Commission, Transcript of Proceedings (Day 51, 11 September 2018) 5466.

⁵ Royal Commission, Transcript of Proceedings (Day 51, 11 September 2018) 5453; Exhibit #6.74.

⁶ Royal Commission, Exhibit #6.74, ASIC.0073.0001.0001, 0003–4.

⁷ Royal Commission, Exhibit #6.70, FIG.0008.0008.0013, 0044; Mr Orton accepted that this practice occurred and that it was inappropriate. See Transcript of Proceedings (Day 51, 11 September 2018) 5435.

⁸ Royal Commission, Transcript of Proceedings (Day 52, 12 September 2018) 5499–5506.

⁹ Final Report, Vol 2: Case Studies, p 309-10 (internal citations omitted).

¹⁰ <https://www.smh.com.au/business/banking-and-finance/insurer-sold-life-cover-to-26-year-old-with-down-syndrome-20180911-p5030w.html>.

¹¹ <https://www.smh.com.au/business/banking-and-finance/insurer-sold-life-cover-to-26-year-old-with-down-syndrome-20180911-p5030w.html>.

¹² <https://www.smh.com.au/business/banking-and-finance/insurer-sold-life-cover-to-26-year-old-with-down-syndrome-20180911-p5030w.html>.

¹³ Final Report, Vol 1, p 186.

¹⁴ Final Report, Vol 2: Case Studies, p 296 (internal citations omitted).

Consumer Credit Insurance

The harm caused by conflicted remuneration in general insurance was abundantly clear from the case study on consumer credit insurance at the Royal Commission. Commissions drive the sale of junk add-on insurance (and extended warranties – an unresolved problem) in car dealerships. As Commissioner Hayne summarised:

Evidence given in the Commission's sixth round of hearings showed that the levels of commissions paid to motor vehicle dealers in connection with the sale of add-on insurance products contributed to the mis-selling of those products. In its September 2016 report on the sale of add-on insurance through dealers, ASIC noted that, in the 2015 financial year, the commissions paid to dealers for the sale of add-on insurance products were as high as 79% of the premium. ASIC also observed that the amounts paid in *commissions* on these products exceeded the amounts paid out to customers who made claims.¹⁵

The profits of insurers, advisors and other intermediaries—not customer need—are the rationale for the car yard add-on insurance market. 'Reverse competition' through insurers paying commissions and incentives to dealers has driven this market. This perverse market rationale and structure has led to significant consumer detriment, including high commissions, pressure selling of unsuitable and poor-value products. Despite recent reforms, claims ratios remain low.

The clean-up bill for this flagrant mis-selling is staggering. Our self-help tool DemandaRefund.com helped people demand back over \$30 million in junk insurances and warranties. Taking into account remediation schemes, the total bill is well into hundreds of millions of dollars.

The evidence and findings before the Royal Commission are crucial to the Advice Review in its examination of Recommendation 2.6.

Commentary on conflicted remuneration

Throughout the Interim and Final Reports, Commissioner Hayne made findings and comments on conflicted remuneration that are highly relevant to the Advice Review.

At the outset, Commissioner Hayne states that 'the definition of "conflicted remuneration" in the Corporations Act shows why the practice should be prohibited.'¹⁶

In respect of insurance:

I doubt that a complete ban on conflicted remuneration in respect of life insurance products would lead to significant underinsurance. ... I am not convinced that a move away from commissions for life insurance products would see large numbers of Australians without an appropriate level of life insurance.¹⁷

Commissioner Hayne goes on to state, in respect of the foreshadowed post-implementation review of changes to life insurance commissions:

If that review indicates that the cap on commissions has not contributed (or, at least, not significantly contributed) to underinsurance, then I would urge ASIC to continue reducing the cap – ultimately, to zero. *Unless the reduction in life insurance commissions can be shown to contribute significantly to underinsurance, I can see no justification for allowing this form of conflicted remuneration to continue to be paid.* While the decision will ultimately be one for ASIC, any decision that commissions should continue to be paid and received in relation to life insurance products should be based on *clear evidence that the harm that would*

¹⁵ Final Report, Vol 1, p 291 (emphasis in original).

¹⁶ Final Report, Vol 1, p 14.

¹⁷ Final Report, Vol 1, p 188 (emphasis added).

*flow from abolishing commissions would outweigh the harm that already flows from allowing this form of conflicted remuneration to continue.*¹⁸

Recommended changes to TOR

For the Advice Review to properly implement Recommendations 2.3, 2.5, and 2.6, it must have regard to the evidence before the Royal Commission and the commentary in its reports.

Paragraph 4.3 of the Draft TOR allows for the Review to have regard to 'the level of demand for advice and the needs and preferences of consumers'. While this is a good start, this does not go far enough to ensure the Advice Review properly considers the issue of conflict between duty and interest.

At a minimum, we recommend the following

1. The Review should have regard to the findings and commentary of the Financial Services Royal Commission regarding conflicts between duty and interest in financial services and advice, and the benefits of removing all forms of conflicted remuneration
2. The Review should have regard to the need to ensure good consumer outcomes and preventing misconduct and harm.

Super Consumers' Australia submission

Separate from the issues in this submission, we have had the opportunity to review the submission authored by Super Consumers Australia and we endorse those recommendations.

Contact details

The Advice Review is a critical opportunity to end conflicted remuneration in financial services for good. Anything less will be seen as a failure to implement Commissioner Hayne's considered recommendations.

Please contact Cat Newton at cat@consumeraction.org.au if you have any questions about this submission.

Yours sincerely



Gerard Brody | CEO
CONSUMER ACTION LAW CENTRE

¹⁸ Ibid.

Appendix A – Excerpt from [Royal Commission Final Report, Vol 2: Case Studies, Freedom, pages 303-306](#)

Evidence – Mr Stewart’s son

“Mr Stewart’s son was born with Down syndrome. While Mr Stewart’s son has a degree of independence, he has difficulties understanding whether a product is ‘expensive or cheap’, and whether he has enough money to make purchases. As a result, Mr Stewart and his wife assist their son to manage his finances. In 2016, when Freedom sold Mr Stewart’s son an insurance policy, his only source of income was the Disability Support Pension.

Mr Stewart learnt that his son had taken out insurance after his son received a letter from Freedom. The letter said that Mr Stewart’s son had taken out a Freedom Protection Plan, which comprised three types of cover: funeral, accidental death and accidental injury. The letter said that premiums for the funeral cover would not be due for 12 months, but that premiums for the accidental death and accidental injury cover would be due 12 days later.

Mr Stewart was ‘flummoxed’ by the letter. He did not understand how or why his son had been signed up, so he asked his son what had happened. Mr Stewart’s son remembered speaking to someone on the phone, and providing that person with his debit card details, but could not explain why he had done so. Mr Stewart did not think that his son understood that he had provided those details in order to purchase an insurance policy.

The following day, Mr Stewart telephoned Freedom and attempted to cancel the policy on his son’s behalf. Mr Stewart was not able to do this. Instead, a Freedom representative told Mr Stewart that they would listen to a recording of the call in which Mr Stewart’s son was sold the policy and then call Mr Stewart back. The representative also told Mr Stewart that the sales agent who sold his son the policy probably did not know that his son had a disability.

Mr Stewart did not receive a call back from Freedom, and did not receive any response to an email that he sent to Freedom’s Head of Operations lodging a formal complaint. Two days later, Mr Stewart telephoned Freedom again.

During this second phone call to Freedom, Mr Stewart and his son were transferred to Freedom’s Retention team, a group within Freedom whose chief task was to dissuade customers from cancelling their policies. A Freedom retention agent that they spoke with tried to explain the potential benefits of the policy for Mr Stewart’s son, and emphasised several times that the policy was free for the first 12 months. The retention agent also said that there was no reason for Freedom to have known that Mr Stewart’s son had a disability. However, the retention agent ultimately agreed to cancel the policy. Mr Stewart’s son was asked to confirm that he wished to ‘terminate the policy’. Mr Stewart’s son had difficulty articulating those words.

After the phone call, the retention agent engaged in an instant messenger conversation with another Freedom representative, in which disparaging remarks were made about Mr Stewart and his son. Mr Orton accepted that this conduct was ‘totally inappropriate’.

During the call in which the policy was cancelled, Mr Stewart asked Freedom to provide him with copies of the recordings of the sales calls with his son. Mr Stewart did not receive these recordings until August 2018, shortly before the Commission was to take evidence about the matter.

Excerpts of two of these calls were played in the course of Mr Stewart’s evidence. In the first call, which lasted for just over two minutes, a Freedom sales agent asked Mr Stewart’s son whether his mother was at home, and discontinued the call when he determined that she was not. In the second call, which took place two days later and which lasted for eighteen and a half minutes, the same sales agent sold the policy to Mr Stewart’s son. Mr Stewart told the Commission that, having listened to that call, he did not think that his son had any understanding of what he was signing up for. I agree. Mr Orton accepted that the sales agent’s actions were inappropriate, and that he should have known that Mr Stewart’s son was not capable of understanding what was occurring during the call. Mr Orton agreed that the sales agent who sold the policy to Mr Stewart’s son had engaged in ‘deeply troubling conduct’. Again, I agree.”