APPROVED PRODUCT LIES

Combating the manipulation of advice

By **Jeff Morris**

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Data doesn't lie

Simon Swanson

Research on the wall of money flowing from institutionally-aligned advice licensees into related-party products suggests that a sales culture is still alive inside vertically integrated organisations and conflicts of interest are still not being adequately managed.

The data continues to raise serious concerns about the advice industry's structure; the limited product choice available to consumers, particularly in life insurance; and the ability of advisers to act in their clients' best interest.

As Commissioner Kenneth Hayne noted in his final report: *"The one-stop-shop model creates a bias towards promoting the owner's products above others, even where they may not be ideal for the consumer"*[1].

To review our internal processes, ClearView commissioned industry commentator Jeff Morris to assess the product choice and autonomy given to the 230 advisers in our advice licensees, Matrix Planning Solutions (**Matrix**) and ClearView Financial Advice (**CFA**).

This included examining the dealer groups' life insurance revenue and new business sales, and tracking ClearView's progress against its strategic goal to minimise dependence on aligned advisers for support.

Jeff was asked to benchmark ClearView's life insurance advice processes against some of Australia's largest dealer groups, in light of shifting consumer and community expectations. In this paper, he summarises his findings.

One of the most notable observations is that ClearView and most boutique Australian Financial Services Licensees (**AFSLs**) encourage their advisers to choose the most appropriate life insurance solution, based on a client's circumstances, needs and objectives.

On the other hand, the majority of institutional licensees continue to operate limited Approved Product Lists (**APLs**) to ensure that new business flows through to related-party products.

The data continues to raise serious concerns about the advice industry's structure; the limited product choice available to consumers, and the ability of advisers to act in their clients' best interest.

This has created a potentially dangerous market dynamic with consumers unknowingly receiving two different standards of advice.

1 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Final Report, January 2019

According to a 2018 report by the Australian Securities and Investments Commission (**ASIC**), institutionally-aligned AFSLs direct 68 per cent of all client funds into related party products.

ASIC Report 562 – Financial advice: Vertically integrated institutions and conflicts of interest also found that in 75 per cent of switching cases where inhouse products were recommended, the advice failed to meet the Best Interest Duty (**BID**) under the Future of Financial Advice (**FOFA**) rules.

This bias is then turbo charged by restricted APLs.

By comparison, our flagship life insurance product, ClearView LifeSolutions, represented 34 per cent of total life insurance revenue across Matrix and CFA, in the 12 months to 30 June 2019. The majority came from 10 or so other retail insurers.

The separation of product and advice will lead to improved client outcomes and accelerate the advice industry's journey to professionalism.

Focusing only on new business revenue, around half related to ClearView LifeSolutions.

As a manufacturer this is a pleasing result. It demonstrates that our life insurance product is strongly supported by the adviser network, which we believe reflects our excellent service, track record for paying claim entitlements and the strength of our relationships.

It also suggests that ClearView could significantly boost inflows to ClearView LifeSolutions, if Matrix and CFA implemented a limited APL.

As an advice licensee, we need to ensure that our advisers feel empowered to fulfil their BID obligations.

I am proud to say that Matrix and CFA advisers (and their clients) have unrestricted access to all APRA-regulated retail life insurers in Australia. They are not pushed to support ClearView LifeSolutions.

In fact, ClearView has been a staunch advocate for open life insurance APLs since our inception because we believe the separation of product and advice will lead to improved client outcomes and accelerate the advice industry's journey to professionalism.

This may sound contradictory given ClearView's integrated structure.

Over the years, we have been criticised for highlighting poorly-managed conflicts of interest inside the vertically integrated giants while operating two licensees.

But our plan was never to 'own distribution'.

When the business was being established, our single-minded objective was to be an innovative disruptor in life insurance and wealth management by manufacturing and distributing superior products.

It became clear that no matter how good our solutions were, we couldn't do business with a significant chunk of the market, due to the use of limited APLs.

Ironically, it was the vertically integrated model that forced ClearView to establish its own dealer group to gain access to financial advisers.

However, we did not restrict the life insurers our aligned advisers could recommend and one of our key strategic objectives is to expand our IFA relationships and minimise our reliance on our aligned dealer groups for support.

Pleasingly, ClearView is making strong progress towards that goal.

As at 30 June 2019, the IFA market represented 84 per cent of ClearView LifeSolutions sales, up from 80 per cent in 2018.

It's no secret that our push for open APLs isn't purely altruistic. As a relatively new player, we want to do business with as many IFAs as possible.

According to the Data Insights Life Market Report (July 2019), Australia's retail advised life insurance market is heavily concentrated between five insurers representing 90 per cent of retail inforce premium.

To ensure an innovative and competitive landscape, new entrants like ClearView must be given the opportunity to compete on merit. Industry bodies like the Financial Services Council (**FSC**) have an important role to play in securing this vibrant future.

As part of his brief, Jeff was asked to assess the effectiveness of the FSC's APL standard against its government mandate to promote competitive access and choice for advisers and consumers.

The FSC was invited to provide an update on the standard's progress, since its launch in late 2017.

Unfortunately, the FSC did not know if any of its members had adopted the APL standard.

"The FSC does not hold the information you seek... The life insurance APL standard ensures greater transparency to customers around APL arrangements and establishes a minimum number of insurers that must be on an APL to ensure choice and competition for customers," said FSC CEO Sally Loane in response to Jeff's initial query.

When pressed again, Loane responded: *"We are a member-based association and we do not act as a coordination body to assist consultants"*.

Of the four institutions approached by Jeff, which represent 15 licensees, only one provided some of the information requested.

All, with the exception of ClearView and MLC, declined to provide the most basic piece of information: the number of life insurance companies on their APL. As such, the APL graphic on page 20 is largely based on information from external sources.

This is despite the FSC requirement for members to disclose the number of products and providers on their life insurance APL as part of the advice process *"to ensure consumers have full transparency to make an informed choice"*.

While Jeff was not requesting information as a potential client, he is a well-known consumer advocate. The unwillingness of the FSC and some dealer groups to cooperate questions the adequacy of the industry's response to key Royal Commission criticisms around the industry's management of conflicts.

In our opinion, it is woefully inadequate.

It is clear that the FSC standard has failed to achieve change around APLs.

ClearView supports the Coalition Government's recent call to expand the Financial System Inquiry into the financial services sector. At the moment, the Royal Commission's recommendations are just that; recommendations, so it's important that momentum is not lost. The industry must continue to pursue reforms that strengthen consumer protections such as the abolition of life insurance APLs.

The APL dilemma

Jeff Morris

The absence of trust in financial services is a major problem for an industry with a value proposition predicated on it.

Yet the banks and institutions have repeatedly proven they are untrustworthy.

To bridge the trust deficit, they are saying all the right things but this crisis can't be fixed with rhetoric.

It can't even be fixed with better products and services. The time for that has passed.

The institutions have a reputation for being greedy, deceitful and unethical, and the only way to fix it is to genuinely be honest, transparent and repentant for their failures.

But fessing up to historical mistakes only won't cut it if the underlying culture and behaviour remains the same.

They need to acknowledge and address the poor practices that continue inside their organisations today.

A good place to start is restricted life insurance APLs, which hide in plain sight but are sneaky and opaque.

APLs are positioned by institutional dealer groups as useful advice and risk management tools, designed to help financial advisers filter through the plethora of complex products in the market to identify the best solutions, based on thorough research.

They are made out to be standard industry practice, leading to compliant advice in the best interest of clients.

This hypothesis needs to be examined, challenged and tested by all industry participants.

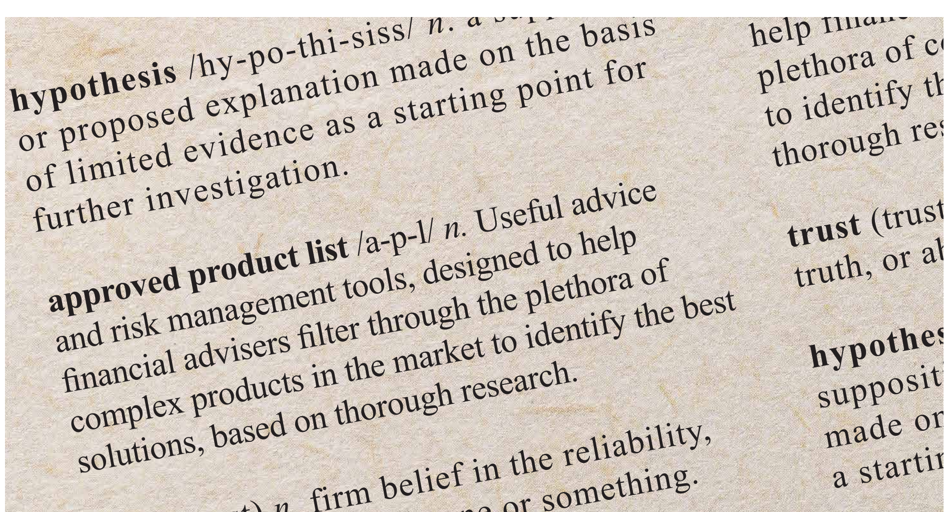
What is an APL?

An Approved Product List (**APL**) is a limited menu of financial products curated by a licensee, based on arbitrary factors.

Advisers are confined to the products on their licensee's APL.

APLs are broadly an institutional phenomena. The vast majority of privately-owned boutique AFSLs don't use an APL.

APLs are designed to influence advice recommendations and channel clients into inhouse products.



Testing the APL hypothesis

Industry associations, product manufacturers, regulators and advisers all have a responsibility to make sure the APL value proposition stacks up.

Let's evaluate it.

Advice and risk management tool

Professional advice is not about product.

At a high level, an adviser's role is to:

- Understand a client's personal circumstances, goals and priorities;
- Develop an investment and insurance strategy that maximises the probability of them achieving their goals;
- Implement the strategy; and
- Keep them on track towards their goals year-after-year.

Risk profile questionnaires, financial modelling and retirement calculators, budgeting and cashflow management Apps, and Statement of Advice (**SOA**) templates are examples of useful advice tools. They help advisers determine the most appropriate strategy for a client and visually illustrate the benefits of that strategy so clients can make informed decisions.

An adviser may recommend one or more financial products to implement the strategy.

An APL, on the other hand, is a menu of products an adviser can choose from. It doesn't help them determine how much income a client needs to maintain their lifestyle in retirement or whether a person's existing insurance strategy is still appropriate for their age and stage in life.

Life insurance APLs are an overhang of an outdated advice era when a financial product sale was a foregone conclusion.

As for a risk management tool, there are only 12 APRA-regulated retail life insurers in Australia.

According to Michael Gottlieb, CEO and Founder of BizCover, restricting life insurance choice only creates additional risk for licensees and advisers because it curbs their ability to meet the BID obligations.

"The need for an APL for non-mainstream investment products is high but there is limited, if any, value in having a life insurance APL," he said.

"So long as a life insurer is APRA-regulated and approved, professional indemnity (**PI**) insurers across the board should be comfortable with advisers recommending them to their clients."

Designed to help financial advisers

The majority of advisers shun APLs.

According to new research by Adviser Ratings, which examined the reasons why an increasing number of advisers had joined non-institutionally owned licensees, two key factors drove the decision-making process, being:

- Compliance support; and
- Choice of product.

Their first consideration; compliance support, is not surprising given the heightened regulatory focus.

However, the second most important consideration, product choice, is an indication that many aligned advisers feel constrained and compromised by their licensee's attitude and support.

According to Adviser Ratings, vertical integration and restricted APLs are "on the nose", with respondents noting the comparable ease at which they could recommend alternative products at their new licensee.

In the non-aligned segment, APLs are an anomaly (see standard industry practice on page 9).

Most privately-owned licensees embrace open architecture.

To stop advisers from leaving, institutional licensees commonly operate multiple dealership brands that offer varying levels of product choice.

Advisers willing to accept a limited APL typically pay lower dealer fees than those who demand broad choice.

This is the case because institutions still see personal advice as a distribution channel.

Vertical integration only makes commercial sense if aligned advisers sell related-party product because:

- Institutionally-owned dealer groups are unprofitable;
- Aligned advisers benefit from subsidised dealer fees; and
- Institutions make their money from product sales.

Plethora of complex products

There is no question that life insurance is a complex financial product but by and large, today's products are of similar high quality.

Life insurers may argue otherwise but all contemporary products broadly offer the same features and benefits, although premiums vary from product-to-product based on a client's unique circumstances.

As professionals, advisers can access product information using a number of comparison tools. They can combine their product knowledge and experience dealing with insurers to make appropriate recommendations.

Currently there are only 12 APRA-regulated retail life insurers in the Australian market. That number will shrink to around eight or nine after the latest round of consolidation is completed.

APRA-regulated retail advised life insurers
AIA
AMP
BT Life
ClearView
CommInsure
Integrity
Metlife
MLC Life
Noble Oak (NEOS Life and PPS Mutual)
OnePath
TAL
Zurich
12

Best solutions based on thorough research

Life insurance APLs are typically put together internally by dealer group staff.

Senator Jane Hume, Assistant Minister for Superannuation, Financial Services and Financial Technology

Interestingly, at the 2019 FSC Summit in August, Senator Jane Hume, Assistant Minister for Superannuation, Financial Services and Financial Technology, disclosed that as a 26-year-old working for a large financial planning dealer group, she had the enormous responsibility of constructing an APL for the group's aligned advisers with nothing more than a commerce degree.

Experience and qualifications aside, the way APLs are constructed represent a significant conflict of interest for institutionally-owned dealer groups because staff are ultimately paid by the product manufacturer.

There are also generally no formal, structured APL review processes in place, meaning APLs are reviewed on an ad-hoc basis at a licensee's discretion.

Standard industry practice

The FSC's APL standard applies only to its 20 or so advice licensee members.

It does not apply to the majority of Australia's 1,500 AFSLs.

The majority of advisers don't use a life insurance APL. The graphic on page 21 illustrates the open nature of most boutique AFSLs.

In fact, the non-aligned segment of the market has been built by advisers fleeing institutional control and influence. Their value proposition is predicated on having no ownership ties to a product manufacturer and product choice.

A formal APL serves to direct advisers to a limited list, with licensee-level approval required to go 'off-piste' for any one client's product solution. In contrast to the principle of dictating where to direct business, many non-aligned advisers actively avoid those insurers which, experience has told them, provide less efficient

or less 'fair' treatment of policyholders. Such avoidance also reflects slow, inefficient or unsatisfactory adviser experience, which hinders productivity. This common (but not universal) non-aligned practice results in an informal 'preferred provider' list. In developing such a list the licensee acknowledges adviser expertise and client-centricity of purpose. Thus a choice of product is accompanied and even driven partly by a choice in favour of service and efficiency, using knowledge and professional judgement by those advisers.

As such, 'preferred provider' lists bear no resemblance to APLs. They also respect advisers' rights to use whichever product providers they wish to, without accounting to the licensee for their choices.

What is the FSC APL standard?

FSC members are required to offer a choice of three or more life insurance providers and support a robust off-APL process.

The standard, which commenced in December 2017, is not compulsory. The FSC announced that the standard would be "reviewed within 18 months of commencement".

Compliant advice in the best interest of clients

It is hard to see how limited APLs fit in with the nature of FOFA and specifically the best interest requirement.

As Michael Gottlieb pointed out, narrow life insurance APLs pose a higher risk than broad APLs.

Under FOFA, financial advisers have a duty to act in the best interest of a client, demonstrable by conducting a 'reasonable investigation' into the financial products that may help a client achieve their goals and objectives.

However, limited APLs encourage advisers to automatically bypass the reasonable investigation stage and defer to recommendations by their licensee.

FOFA also states: *"If an adviser knows, or reasonably ought to know, that there is a conflict between the interests of the client and the interests of their licensee, they must give priority to the client's interest"*.

It is difficult to see how advisers can provide compliant advice under FOFA if they are routinely recommending sub-optimal life insurance solutions.

Ultimately, the law does not address APLs. There is no mention of APLs in legislation. Advisers are not under any legal obligation to use them as they are an arbitrary, artificial construct.

It is clear that the APL hypothesis does not stack up, therefore, licensees who adhere to them need to get real about why they are enforced.

Removing life insurance APLs is a quick, easy and efficient way that the institutions, and potentially the regulator, can start the long process of rebuilding trust in financial services.

Tracing the origins of APLs

Jeff Morris

From altruistic origins to blatant self-interest

According to Australian life insurance folklore, the APL originated from the preferred product list which sprung out of life insurance research.

I traced the origins of APLs back to the late 1980s to discover that the pioneers of risk research in Australia were motivated by an altruistic desire to help advisers interpret and understand complicated, technical and sometimes ‘unsafe’ policies, the purveyors of which practised zero adviser training or education on the policy terms and conditions.

These researchers had no ties to a product manufacturer but were acting purely on behalf of advisers, for the benefit of clients.

Risk research in Australia emerged in the late 1980s and early 1990s when the tied agency distribution model was breaking down.

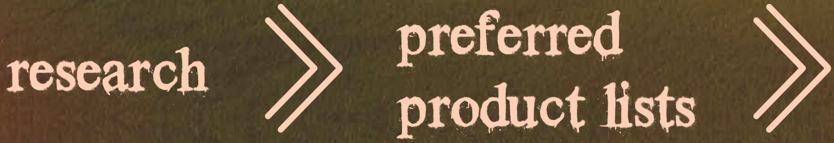
Until that time, life insurance in Australia had only been sold by tied agents, who were more or less product salesmen for one of the big four mutuals: AMP, National Mutual, Colonial Mutual and City Mutual.

They had no formal education or industry technical training. Few, if any, read or at least understood the policy document. They relied on information fed to them by insurance business development managers (**BDMs**).

Meanwhile, emerging product innovation, the rise of superannuation and shifting consumer preferences from the mid-1970s resulted in the separation of the savings/investment and protection components of traditional whole of life and endowment policies, leading to a proliferation of investment options and a wider range of unbundled pure risk products.

This created a need for product *advice* and the multi-agent model (from which today’s financial planning industry stems) was born. Product transparency blossomed and these new multi-agency advisers had the freedom to choose how to best service their clients’ need for quality products and how to avoid outdated, poor policy terms. Research into comparative contractual wordings became an essential tool.

The entry of the banks and institutions into wealth management and the introduction of the Financial Services Reform Act (**FSRA**), saw preferred product lists morph into APLs.



limited APLs

broader APLs

open architecture

Industry stalwarts, Sue Laing and John Butterworth, pioneered product research and technical adviser training in Australia.

Unlike tied agents who sold what they were told, multi-agents could recommend a range of product to consumers.

Laing and Butterworth originally set out to help the 100 or so risk advisers operating under their managing multi-agency (today's advice licensee) to understand the product landscape.

Comparing product quality and exposing 'get-out' clauses and the like became a feature of the day-to-day support of their advisers. Word spread that they had tools to help advisers understand policy clauses and compare product features for the benefit of their clients.

That led to the establishment of Life Research, Australia's first life insurance product research company.

It was Life Research's analysis upon which managing agencies and dealer groups started constructing preferred product lists based on factors such as definitions, features, benefits, exclusions and contractual rights to claim. Later the concept of preferred provider lists gained a foothold, as product innovation slowed and product differences became a finer line to draw. Consumers' discerning demands for service from the financial services sphere drove a quiet move away by advisers from the risk of poor client experience.

At the turn of the century, the entry of banks and institutions into wealth management and the introduction of the Financial Services Reform Act (**FSRA**), saw preferred product lists morph into APLs.

Laing argues that preferred provider lists and APLs are chalk and cheese, and supports the abolition of APLs (see page 16).

The formation and adoption of restricted APLs by institutionally-owned dealer groups occurred almost by stealth, driven by two main catalysts:

- The demise of Agency Development Loans (early 90s); and
- The Financial Services Reform Act 2001.

Agency Development Loans

In the 80s and 90s, APLs weren't a thing because advice wasn't that sophisticated. People paid off their homes, put their money in the bank and maybe invested a little in the handful of expensive, very average managed funds available back then.

As Australians became more prosperous, more of them wanted to protect their wealth and the life insurance market blossomed.

Investment product proliferation and the ensuing battle for distribution lead institutions

to buy managing agencies and start handing out hundreds of millions of dollars in agency development loans (**ADLs**).

The repayment conditions attached to these ultra-cheap or free loans were murky and included lofty life insurance sales targets.

Loans could be pulled at short notice if these targets were not met.

But the demise of ADLs led to Buyer of Last Resort (**BOLR**) agreements and life insurance APLs.

BOLR guaranteed advisers a buyer for their business when they decide to sell.

The ultimate price would be calculated based on multiples of 3-4 different metrics. For example, new business and inforce premium attached to inhouse product attracted a higher multiple than external business. Under a BOLR, an adviser could increase the value of their business by selling inhouse product.

The formula had the desired effect but ultimately fell foul of changing standards and FOFA's conflicted remuneration rules.

This elevated APLs as the key remaining strategy for ushering advisers and clients into inhouse product.

As Michael Hodge QC said in relation to AMP Financial Planning at the Royal Commission: *"Each year since 2013, between 35 and 40 per cent of the investment options on the approved product list were in-house products, more than 90 per cent of new customers invested funds in, or paid insurance premiums in... one or more of AMPs in-house products, and the proportion of funds invested in or insurance premiums paid in respect of AMPs in-house products as opposed to external products by new customers was more than 70 per cent"*.

Financial services reform

FSRA brought various financial services and products under one licensing regime. The legislation focuses on three key areas:

- The licensing and conduct of financial advisers and those dealing with financial products;
- Consistent product disclosure requirements; and
- Licensing of financial markets and clearing and settlement facilities.

Under FSRA, AFSL holders are responsible for the advice provided by their authorised representatives. For the institutions, this means hundreds, if not thousands, of advisers.

This risk prompted licensees to adopt a more formal, structured approach to the construction of their investment APLs, given there are over 20,000 investment options including superannuation funds, managed funds, Australian and international shares, exchange traded funds (**ETFs**), listed investment companies (**LICs**), model portfolios, term deposits, bonds, annuities, listed and direct property, agribusiness, cryptocurrency, foreign currency and commodities.

There are around 12,000[1] managed funds alone, 500[2] superannuation funds and around 2,180 stocks on the ASX including 170 ETFs.

It is not hard to see why licensees responsible for the advice of hundreds of advisers may enforce a relatively tight investment APL.

Institutional dealer groups used FSRA as an opportunity to impose restricted life insurance APLs on their advisers, despite the enormous difference in the size and scope of the life insurance and investment market.

1 https://www.investors.asn.au/education/other-investments/managed-funds/
2 https://en.wikipedia.org/wiki/Superannuation_in_Australia

APLs are impossible to justify

When John Butterworth and I started Life Research we never dreamed it would become the progenitor of premium comparator tools and APLs.

Our research focused solely on policy terms and conditions, especially cancellation clauses and exclusions. It did not examine or compare premiums. Back then, there were considerable differences from policy-to-policy but the industry has evolved since then to the point where today, life insurance benefit types are pretty much a commodity.

In a virtually commoditised world, research is no longer relevant for final product choice, and processes that pick one insurer over another because they scored 89% compared to 87% are nonsensical and even illogical.

Research software is a necessary tool for many reasons, including:

- Assisting with fulfilling replacement of product requirements;
- Achieving broad premium comparisons as a starting point; and
- Providing product training.

Often research software represents the only training an adviser has access to. It makes it easy to locate a product that offers a particular feature befitting a client's circumstances.

However, it is impossible to justify using research to support an APL anymore.

Licensees (and insurers) argue that life insurers are set apart by their administration and service levels, claims experience and the strength of their relationships in the IFA market but how an insurer performs in these areas is highly subjective. Hence the non-mandated nature of preferred provider lists.

The nuances that marginally separate one insurer from another in the eyes of a licensee can form the basis of a preferred provider list but not the existence of an APL.

Experienced licensees operate a preferred provider list model, based on their vast experience in underwriting and claims management. They know which insurers are proactive and easy to deal with.

Preferred provider lists are not APLs because they don't require advisers to jump through hoops to go 'off APL'. The existence of an APL means advisers must follow a deliberately prohibitive process to recommend an alternative product.

Given the small (and getting smaller) number of non-associated APRA-regulated life insurers, choice is already limited enough. Any licensee in favour of innovation, competition and efficiency for clients would not lock out any insurer from their APL. If their argument, for example, is that they haven't had experience dealing with an insurer because they're relatively new, then that is anti-competitive (and, worse, probably short-sighted).

Sue Laing, Founder and Technical Manager, The Risk Store

Closed shops and open architecture

Jeff Morris

When I agreed to look at the APL practices of financial advice groups, I suspected it would be challenging to gather information but even I was surprised by the caginess of the institutionally-aligned dealer groups.

Of the four institutions I contacted, which represent 15 advice licensees and roughly 5,800 financial advisers, only one (NAB/MLC) was willing to share the number of life insurers on their APL.

One group did not even respond at all.

A request for information to the FSC also proved fruitless, with the organisation charged by the government for delivering an improved APL standard, admitting it wasn't across the detail of its members' practices.

As a result, the information on page 20 is based largely on external sources.

The vague responses I received to the dozen or so straightforward questions (refer to the Appendix for the full list) were not only underwhelming but unacceptable given that section 6.1 of the FSC APL standard states that "disclosure must be provided to clients to outline how many providers are on the life insurance APL".

Whether it's a client, journalist or consumer advocate asking the questions should be largely irrelevant. The nature, purpose and intent of the APL standard is to increase openness and transparency and "encourage competitive access and choice for advisers and their clients in life insurance products".

It has clearly failed to do that.

Fortunately, the FSC does not represent the majority of the advice community, probably no more than 30 of the estimated 1,500 AFSLs.

While limiting the product choice of thousands of advisers and their clients is understandably not something the institutions want to shout about in this post-Royal Commission environment, there are signs of progress.

Restricted life insurance APLs are unsustainable and unjustifiable in the emerging financial advice profession.

The life insurance APLs of many aligned dealer groups are now broader than they were a couple of years ago, suggesting that they recognise the value and importance of empowering financial advisers to choose the most appropriate solution for their clients.

Either that or they're finally bowing to pressure from the regulators, media, consumer advocates and their own advisers.

My assessment is that restricted life insurance APLs are unsustainable and unjustifiable in the emerging financial advice profession.

But that hasn't stopped the institutions trying to drag things out.

It's time to just rip the APL band-aid off.

Financial advisers are expected and required to provide objective advice in the client's best interest. Limited APLs impede the delivery of quality, objective advice.

What they said

Below is a snapshot of some responses.

"We provide a range of additional resources to ensure our advisers understand the way APLs are constructed... and have a process that enables them to select products that are not on the APL if it is in the client's best interest to do so. That process is actively used by advisers when necessary and we are confident it is not onerous."

David Wappett, Head of Research and Relationship Management

"We set Standards for our members which go over and above the minimum requirements set for them under the law. While the FSC is not a regulator, we have a board process for dealing with any breaches of Standards."

"The APL Standard ensures greater transparency to customers about APL arrangements... and establishes a minimum number of insurers that must be on an APL to ensure choice and competition for customers."

Sally Loane, Chief Executive Officer

"Our advice licensees have a life insurance APL that includes a choice of three or more life insurance providers and we are currently looking to expand this number.

"The insurance APL provides advisers with a highly-researched shortlist that we believe would be appropriate for most customers in most circumstances, however, we provide research tools to our advisers which allow these policies to be compared against almost all life insurance products in the market. This is also supported by streamlined processes that assist advisers to recommend alternative products... not on the APL."

Mark Ballantyne, General Manager Financial Wisdom and CFP-Pathways

"We remain supportive of an APL that ensures advisers have access to a wide range of insurers, allowing them to meet their clients' needs under their best interest obligations. We will not be participating in the survey."

Darren Whereat, General Manager, Advice

State of the industry

Number of life insurers on APL

Access to all

12

APRA-regulated retail life insurers

ASIC set to turn up the heat

Simon Swanson

ASIC has confirmed that it will commence a review into the quality of life insurance advice in 2020, in line with the Royal Commission's recommendations.

The findings of this review will be published in 2022.

In 2020/21, ASIC will also commission further research into the unmet financial advice needs of consumers. This project will examine:

- The state of the financial advice industry;
- The demand for, and supply of, financial advice; and
- Potential measures to reduce any gaps between supply and demand.

The vertically integrated model and its conflicts of interest will undoubtedly face scrutiny again.

Knowing this, the industry has a unique opportunity to clean up poor, outdated practices and make the necessary changes to drive improved consumer outcomes and prove itself trustworthy, before ASIC commences its review.

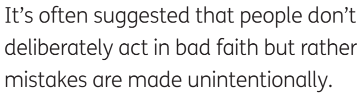
I use the word *trustworthy* deliberately.

A lot has been written about the industry's trust deficit and the urgent need to rebuild trust in the sector, however, there are two components to the word *trust-worthy*. The industry talks a lot about the former but there's less attention on the *worthy* bit.

Until it can demonstrate positive changes, consumers are right to be cynical and distrusting.
As author and trust expert Rachel Botsman says: *"We don't need more trust, we need more trustworthiness"*.

This industry needs to be worthy of trust.

That means practitioners, executives and leaders who are not only qualified and competent in their field of expertise but honest and ethical. That means organisations that are committed to building and fostering a client-first culture.



It's often suggested that people don't deliberately act in bad faith but rather mistakes are made unintentionally.

But limited APLs are no accident. It's not a coincidence that aligned advisers direct 68% client monies into inhouse products[1].

Clearly something is amiss.

Regulatory shortcomings

According to Dr Ian Enright, Adjunct Professor at the University of Technology, Sydney, the current life insurance regulatory framework has a number of important limitations.

Among them is the existence of APLs.

In his July 2019 presentation to the Melbourne Money and Finance Conference, titled *The Royal Commission and the Insurance Framework*, Dr Enright said *"restricted APLs for risk life insurance breach almost every law which applies to them (***AFSLs***) and should be prohibited"*.

His concerns are echoed by the Financial Planning Association (**FPA**).

In its submission on the FSC APL standard[2], the FPA warned of the 'high risk' of biased

A restricted APL is a red flag. It suggests an AFSL is acting like a distribution agent rather than a professional adviser.

1 ASIC Report 562 Financial Advice: Vertically integrated institutions 2018

2 https://fpa.com.au/wp-content/uploads/2017/05/2017_05_17_FPA-Submission_FSC_APL-Standard_FINAL.pdf

advice where licensees are connected to, or received special benefits (such as sponsorship and shelf space fees), from an insurer, unless APLs were scrapped.

The FPA argued that life insurers should only be excluded from APLs if their product was not independently deemed 'advice grade'.

It proposed an alternative to the FSC APL standard whereby FSC members agreed to minimum best practice requirements for inclusion on an APL.

The FPA submission stated: *"Very few products would be excluded, meaning that each APL would be extremely broad. Combined with the 'best interest' duty, a substantially open APL would provide optimal conditions for the adviser to act in the best interests of the client"*.

Recently, the Chartered Financial Analyst Institute; the global association for investment management professionals, weighed in on the debate, adding its name to the list of associations and academics calling for regulatory action to strengthen consumer protections and stamp out poor practices inside vertically integrated organisations.

The Chartered Financial Analyst Institute report; *Professionalising financial advice*, concluded that the only purpose limited APLs served was to protect entities associated with licensees from competitive pressures. It warned that this created an artificially-controlled environment where clients ended up paying more for products and services than they would if they had access to other providers.

While the Chartered Financial Analyst report focused on limited platform APLs, the same arguments apply to life insurance.

The Chartered Financial Analyst report addressed the common argument that consumers who saw an aligned adviser expected to be sold inhouse products.

"A comparison is often made to the purchase of a car: a customer enters a dealership for a certain brand and expects to be sold that particular brand of car. We strongly believe that such comparisons are inappropriate. A car dealer is not claiming to be giving advice on the best brand of car but is clearly selling a particular product. If financial advisers are in the business of giving advice to clients on the most appropriate financial plan and investments for the clients' situation, then those advisers should be completely separated from any manufacturer..."

The continued use of limited APLs adds credibility to the argument that financial advisers who can only recommend a small number of products be called agents because the term 'agent' is a more accurate description of their limited capacity.

Professional advisers should be able to use their knowledge, experience and professional judgement to choose the right solutions for their clients.

It also strengthens consumer protections.

Proposals of this nature have the broad support of the IFA community, who see the ability to recommend the most appropriate solution for clients as an important and valuable distinction. Not surprisingly, such proposals are fiercely opposed by institutionally-aligned dealer groups.

Such is the power of these institutions that they successfully lobbied to stop non-aligned advisers from using the terms *'independently-owned'*, unless they met all conditions under Section 923A of the Corporations Act.

Prior to mid-2017, privately-owned AFSLs used this term to describe their non-institutionally owned status and point of difference.

However, the power of the institutions is being eroded by higher regulatory and community expectations. It increasingly untenable for aligned AFSLs to claim they are fiduciaries who provide compliant, personal advice while clinging to limited APLs.

Unfortunately, the FSC's cosy relationship with its dominant, vertically-integrated members has resulted in a weak and ineffective APL standard. The FSC standard has proven that there will be no genuine progress on this front without regulatory action.

Our philosophy

ClearView has an integrated structure but we manage conflicts of interest by empowering our 230 aligned advisers to choose from all APRA-regulated life insurers in the market.

This is our stance because professional advisers should be able to use their knowledge, experience and professional judgement to choose the right solutions for their clients.

Furthermore, retail life insurers in Australia are regulated by APRA, subject to strict capital requirements and largely offer the same features and benefits.

The unrestricted life insurance choice given to our advisers has not impacted our PI insurance premiums.

In our experience, PI insurers examine an AFSL's insurance advice systems and processes but whether or not they use a life insurance APL is largely irrelevant.

If anything, a restricted APL is a red flag. It suggests an AFSL is acting like a distribution agent rather than a professional adviser.

Our philosophy is that financial advice businesses typically have a diverse clientbase, therefore, they should offer adequate product choice to satisfy the diverse needs of their clients. If a practice has 1,000 clients but can only recommend a small number of options, their ability to provide highly customised personal advice is compromised.

When it comes to managing risk, AFSLs should beef up their systems and processes for detecting fraud and monitoring their authorised advisers. They should not spend time constructing life insurance APLs.

Given the potential adverse consequences of poor life insurance advice, it is critical that advisers and their clients have access to all retail life insurers to secure the intended outcomes.

If the regulators agree that the products offered by Australia's APRA-regulated insurers are generally of similar high quality then there is no genuine reason to exclude any provider from consideration.

Equally, while retail life insurance products are largely comparable, every participant has a responsibility to encourage innovation and competition to ensure continuous improvement. Restricted APLs stifle progress and evolution.

Appendix

Questions submitted to institutional licensees

Do you have a life insurance APL? If so, what is the rationale behind your APL?

List the life insurance companies on your APL.

Do you intend to broaden your APL in the next 6-12 months?

Do you receive payments from third party life insurers? If so, roughly how much?

What percentage of new business is directed to a related-party insurer?

Do you believe the FSC's APL standard (a minimum of three life insurers on APL) is appropriate?

How often do you formally review your APL?

The following questions related to off-APL approval processes:

Do you have a structured, documented off-APL approval process? If so, please outline.

How many off-APL requests do you receive a month?

What percentage of off-APL requests are approved?

On average, how long does it take to approve an off-APL request?

What percentage of new business do life insurers that are not on your APL collectively receive?

About the authors

Jeff Morris studied Economics and Law at the University of Sydney and was a Certified Financial Planner. He has accumulated over 30 years in the financial services industry including roles at Deloitte & Touche, Towers Perrin, Bankers Trust Australia, NatWest and Commonwealth Bank.

In 2008 he joined Commonwealth Financial Planning and soon after exposed serious misconduct in the organisation. Jeff ultimately becoming known for his role as a whistleblower and was the catalyst for a Senate Inquiry into the Australian Securities and Investments Commission. Jeff hopes his actions have helped deliver better financial advice for ordinary Australians. He continues to speak publicly on misconduct in the industry and advocates for the rights of whistleblowers.

Simon Swanson B.EC, B. Bus, ANZIIF (Fellow), CIP, FCPA was appointed Managing Director of ClearView in 2010. His international career spans more than 30 years in financial services including roles in life insurance, funds management, general insurance and health insurance. He led the largest life insurer (CommInsure, Sovereign and Colonial) in three countries and spent half of his career in the Asia Pacific region.

Back on domestic soil, Simon has been a director of the Australian Literacy and Numeracy Foundation and was Chairman of ANZIIF's Life, Health and Retirement Income Faculty Advisory Board. He is also on the Life Board Committee of the Financial Services Council.

Simon is effectively the founder of ClearView and was instrumental in buying Bupa Australia's life insurance and wealth management businesses and transforming them into the integrated business that ClearView is today.

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