FEBRUARY 2018

This newsletter is distributed by Amicus Advisory Pty Ltd, an independent investment advisory service for wholesale investors. To contact us please call: 02 8014 4247 or e-mail: moray@amicusadvisory.com.au

"Advisors" with Conflicts of Interest

"Recommendation 3: Product manufacturers / distributors should be excluded from being appointed investment advisors to Councils"

As a result of losses sustained by NSW councils in the global financial crisis, the Department of Local Government commissioned an enquiry led by Michael Cole. In April 2008, the "Cole Report" was published and the Department adopted all of its recommendations and issued appropriate guidelines to all NSW councils which remain in force today.

One of the key recommendations was "Recommendation 3: Product manufacturers / distributors should be excluded from being appointed investment advisors to Councils." This specific recommendation was followed up by the DLG in their investment policy guidelines in May 2010 where they made clear "The advisor must be an independent person who has no actual or potential conflicts of interest in relation to investment products being recommended."

"In 2011 an ASIC study concluded "management of conflicts of interest remains the critical risk that requires more attention from licensees""

These recommendations were at the leading edge of best practice for the wider financial advice industry within Australia. The Federal Government only started tackling the issue of conflicted remuneration in the financial planning industry in 2010 in its Future of Financial Advice (FOFA) reforms. In 2011, an ASIC study concluded "management of conflicts of interest remains the critical risk that requires more attention from licensees" after the study revealed that 90% of licensed retail financial advisors compensation came from product providers, providing an obvious conflict of interest the DLG had addressed three years earlier.

75% of advice was "non-compliant" with the "best interests duty" to put the client's needs ahead of their own remuneration

A further more recent study by ASIC, released in January 2018, showed despite legislative changes, significant conflicts of interest still remained within the industry. The study found 75% of advice from supposedly independent financial advisors, employed by the big four banks and AMP, were "non-compliant" with the "best interests duty" to put the client's needs ahead of their own remuneration. As hard evidence, it was noted although 79% of "approved products" available to be recommended by advisors originated outside the advising organisation, advisors chose to put 68% of client assets into in-house products where their parent organisations earned fees. Put simply, ANZ advisors recommended ANZ products, CBA advisors recommended CBA products, etc.

Within the institutional conservative fixed interest market in which Amicus operates, the lines are generally adhered to between independent advisors, *There is no issue with brokers providing recommendations so long as clients understand the broker has a conflict of interest*

Under the DLG guidelines, dealing platform providers should not be considered for independent advisory roles as their core business is operating a financial market

The firms providing these dealing platforms cannot be considered independent advisors because of their actual and potential conflicts of interest

Amicus is cautiously optimistic, the liquidator for Lehman Brothers Australia, PPB, will be able to pay another dividend this financial year

The bankruptcy process will continue throughout 2018 and into 2019 at least

such as Amicus, and brokers who make markets, provide products and take commissions, either in the form of direct brokerage or a bid/offer spread when acting as principal. There is no issue with brokers providing recommendations so long as investors understand the broker has a conflict of interest in that the broker does not get paid unless the investor transacts. Brokers have no fiduciary duty to offer investors the best product for their needs; rather their role is to show investors product and encourage them to trade. Most brokers accept this and do not portray or market themselves as independent advisors.

However in recent times the lines have become somewhat blurred, with those with reporting and dealing platforms responding to tenders or expressions of interest for independent advisory contracts for local councils. Under the DLG guidelines, dealing platform providers should not be considered for independent advisory roles as their core business is operating a financial market and they are remunerated directly via transactions executed on their platforms, either on a per trade basis or via a more holistic agreement to distribute products from their providers as part of an integrated business.

To be clear, Amicus sees no issues with investors using these platforms per se and Amicus often recommends investors to use such platforms where sophisticated reporting is required or for portfolio management and trade execution where appropriate. However because of the transactional nature, the firms providing these dealing platforms cannot be considered independent advisors because of their actual and potential conflicts of interest.

ASIC's latest comments in January 2018 described conflicts of interest as "inherent" in vertically integrated firms providing both advice and product, and ASIC is moving to completely separate independent advice from product provision in its latest reforms just as the DLG did ten years ago.

LBA Dividend Payments Update

Amicus is cautiously optimistic, the Liquidator for Lehman Brothers Australia, PPB, will be able to pay another dividend this financial year (i.e. before June 2018). To pay a dividend, PPB needs to have more than $10 million of free cash flow available in the estate for payment and would ideally like to have $20 million available at least. These figures equate to approximate dividend payments of 2.5c/$ and 5c/$ on each accepted claim. Paying out small dividends is administratively expensive, so PPB will not declare another dividend until these funds are available for payment.

LBA is currently involved in three main disputes or issues, and if any one of them is resolved, it will lead to sufficient monies being released so another dividend can be paid. Positively progress has been made recently on all three disputes/issues, and Amicus believes it is more likely than not that at least one of these issues is resolved in the next few months such that PPB can initiate another dividend payment process. We believe it is highly unlikely all three issues will be resolved and so the bankruptcy process will continue throughout 2018 and into 2019 at least.

Amicus
ABN 76 131 548 199
AFSL 384126

Who is Amicus?

Amicus is an investment advisory firm, licensed by ASIC to provided financial services to wholesale investors only (Australian Financial Services License No. 384126). We deliver impartial research, advice, valuations, reporting and other services to wholesale clients. We also provide assistance with the formulation of individual client investment policies and strategies, funding requirements, debt advisory assistance with transactions and help with mixed financial and legal issues.

We are 100% independent and not aligned to, nor owned by, any product provider or external organisation.

For further details please contact us at:

E-mail:	moray@amicusadvisory.com.au
Phone:	Moray 02 8014 4247
Fax:	02 8014 4222
Website:	www.amicusadvisory.com.au
Address:	Suite 2101A, T1, 520 Oxford Street, Bondi Junction, NSW 2022