Giving Advice on Managed Accounts – Best Interest and Other Considerations

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Moderated by Jenny Mulders – IMAP Regulatory Group Chair

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How to ask a Question

GIVING ADVICE ON MANAGED ACCOUNTS .

Simon Carrodus
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the fold

WHAT WE'LL COVER TODAY.

+ Post-Royal Commission world.
+ In-house products.
+ Best interests duty as it applies to managed accounts.
+ Where do advisers go wrong?
+ Product research and comparison.
+ Questions.

POST-ROYAL COMMISSION WORLD.

- Since the Royal Commission, ASIC has been prolific in pursuing fines, disqualifications and criminal charges against individuals and businesses.
- Hundreds of millions of dollars in compensation has been paid to clients.
- Advisers and licensees have been forced to adapt to a much tougher regulatory environment.
- Sharper focus on the adviser's obligation to act in the client's the best interests.
- During the same period, managed accounts have soared in popularity.
- Let's look at what the law asks advisers to do when advising on managed accounts.
- Keep in mind that many managed accounts are ***in-house products***.

IN-HOUSE PRODUCTS.

- Licensee (or related party) will receive an additional benefit when adviser recommends the product.
- No ban on recommending in-house products.
- Conflict exists and must be managed.
- Prioritise client's interests (s961J).
- Standard 3 of FASEA Code.
- Clear area of focus for ASIC.

BEST INTERESTS DUTY.

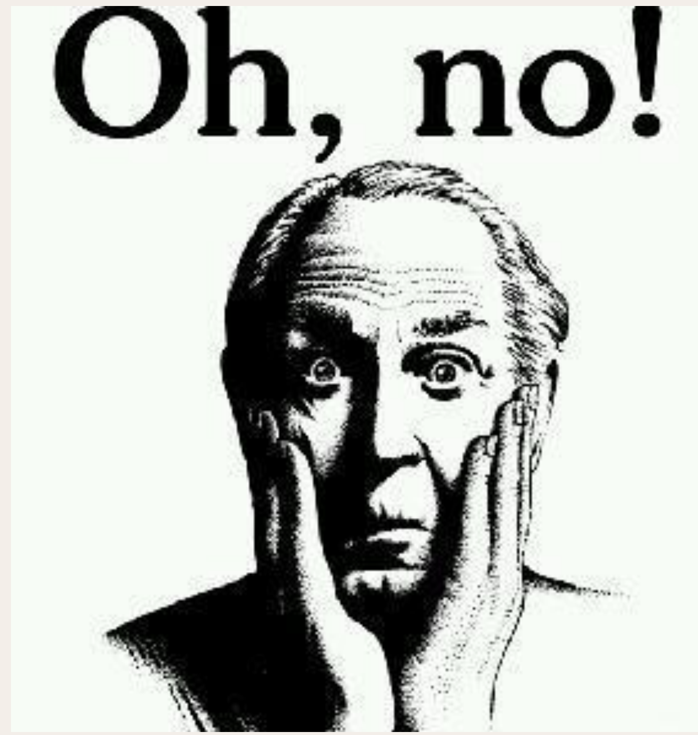
- Act in the client's best interests.
- Safe harbour provision.
  - Identify client's needs and objectives
  - Identify subject matter of advice
  - Make reasonable enquiries
  - Assess own expertise
  - Do your product research
  - Base all judgements on client's needs and objectives

APPROPRIATE ADVICE.

- Advisers should be able to demonstrate a ***clear client benefit*** to every recommendation they make.
- If you cannot articulate a clear client benefit, you should reconsider the recommendation.
- You should explain:
  - How the recommended managed account addresses client's needs and objectives; and
  - Why the recommended managed account is likely to leave client in a better position.
- The recommendation should be linked to one or more of the client's needs, objectives and preferences.
- Price is a consideration, but other product features and benefits are important too.

WHERE DO ADVISERS GO WRONG?

+ ASIC Reports 515 and 562.
+ Failure to do adequate product research.
+ Failure to tailor the advice to each individual client.
+ Failure to keep proper documentation.
+ Tree falling in the woods.



DIFFERENT STROKES.

+ Not all investment structures are the same.
+ Not all clients are the same.
+ Pooled fund vs direct equities vs managed account – each have their own features and benefits.
+ Clients have specific needs, objectives and preferences that can be satisfied by some investment structures, but not others.
+ Matching product features/benefits to client objectives/preferences.
+ There is no one-size-fits-all solution.

BENEFITS OF MANAGED ACCOUNTS.

+ **Trading efficiency**: No need to separately authorise each trade. Reduces lag risk.
+ **Transparency**: Clients see where their money is invested, down to the individual asset level.
+ **Tax-efficiency**: Clients not affected by existing tax positions like in pooled structures such as managed funds.
+ **Cost savings**: Netting of trades can minimise unnecessary trading, which may reduce transaction costs and CGT.
+ **Beneficial ownership**: Underlying investments held in client's name – improved portability of assets.
+ **Customisation**: Many managed accounts can be customised by excluding or substituting certain investments.
+ **Diversification**: Easily access as diversified mix of investments in a given risk profile or assets class.

ROBUST ADVICE PROCESS.

- Identify and assess the client's needs, objectives and product preferences.
- Research the client's existing investment structure.
- Does the existing investment structure satisfy the client's needs, objectives and preferences?
- If not, you should research other products/structures that may better satisfy the client's needs, objectives and preferences.
- Conduct a comparative analysis of the existing structure vs the proposed structure (i.e. managed account).
- Justify your recommendation. You should clearly explain:
  - How a managed account will satisfy the client's needs, objectives and preferences;
  - Why a managed account is likely to leave client in a better position;
  - Any trade-offs to the recommendation, and why the recommendation is still appropriate in the circumstances; and
  - Any alternative strategies that you considered and why those strategies are less advantageous for the client.

ALTERNATIVE STRATEGIES.

- Include a summary of any alternative strategies considered by the adviser.
- This is different from alternative products.
- Alternative strategies could include:
  - Leaving the client where they are i.e. no change;
  - Paying down their mortgage or other debt;
  - [Super] Consolidating their super into a retail or industry fund;
  - [Non-super] Investing in a managed fund; or
  - [Non-super] Investing in direct equities.
- One of the best ways to demonstrate that the recommended strategy is appropriate is to explain why 1 or 2 alternative strategies are inappropriate.

PRODUCT RESEARCH.

- Research and compare the following:
  - The client's current product;
  - The recommended managed account; and
  - At least 1 external managed account that ***could*** satisfy the client's needs, objectives and preferences; and
  - Any other specific product the client asks you to consider.
- This does <u>not</u> require an investigation into every product on the market.
- Advisers can rely on research from their licensee or an external research house.
- However, the adviser is responsible for interpreting the research and applying it to the client's circumstances.
- Licensees can assist their advisers by benchmarking the price and performance of their in-house managed account vs others in the market.

WHAT DOES BAD LOOK LIKE?

"Our managed account offers online access, 20+ portfolios, consolidated reporting etc…"

"I'm switching all of my clients into our managed account because [insert reason]…"

WHAT DOES GOOD LOOK LIKE?

"Jack, you want to retain your direct equities and ETFs, but you want them managed by a professional investment manager, so I've recommended a managed account structure."

"Jill, you want beneficial ownership of your investments to take advantage of after-tax benefits. Your current managed fund does not allow for this, so I've recommended a managed account structure."

Good questions = Good advice

- Ask questions to determine the needs, objectives and preferences of the client.
- Ask about costs, but also features such as transparency, tax-efficiency, beneficial holdings, discretionary management etc.
- Match product features to client needs/preferences.
- Explain why the recommended managed account will:
  - Satisfy the client's needs, objectives and preferences; and
  - Likely leave client in a better position.
- Include evidence of:
  - Alternative strategies considered; and
  - Product research.

1. No such thing as one-size-fits-all advice.
2. Match product features to client preferences.
3. More scrutiny on in-house products.

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