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"High risk" advisers need to act now to elevate consumer needs

Sydney, Australia (November 13, 2014) – FinaMetrica has welcomed the Australian Securities & Investment Commission's (ASIC) inaugural Strategic Outlook, in which it has identified financial advisers as a "high risk area" for consumers. ASIC will target advisers in its surveillance program in 2014-15.

ASIC said in its recently released Strategic Outlook that it is concerned by gaps "in core areas of [consumer] financial literacy, such as keeping track of finances, planning ahead, and understanding risk and return."

FinaMetrica Co-Founder Paul Resnik said ASIC's statements should cause some advisory firms to question the effectiveness of their communication practices about risk.

"The Federal Government and Parliament have increased their focus on the advisory profession and we hear that many advisory firms are beginning to review the quality of their advice and the way they explain risk to clients," said Mr Resnik.

"We welcome this closer scrutiny. Advisory firms have been navigating The Future of Financial Advice (FoFA) reforms over last several years and the largely conflicted remuneration objectives of those reforms and consequently can no longer be regarded as a global role model for client-centric advice," Mr Resnik said.

"For example, the financial services industry as a whole provides risk and return illustrations to prospective investors which often downplay downside risk, particularly the likelihood of outliers or rare events, while focusing on upside potential. Financial advisors often rely on these illustrations when explaining risk to clients. The end result is that many clients take on more risk than they are naturally comfortable with, or are over exposed to risk and don't understand the risks they have taken.

"FinaMetrica's Risk and Return Guide can be used by advisers to educate clients about investment risks and radically diminish this problem. FinaMetrica provides historical performance reports (for 40-plus years) for a representative set of 11 illustrative asset allocations, ranging from very conservative to fully growth-asset exposed. These user-friendly reports help educate clients so that they have realistic return expectations based on their tolerance for financial risk. As a result, they are less likely to be unpleasantly surprised by what happens to their investments when markets fall."

Mr Resnik said advisers also needed to work harder to identify consumer financial needs in order to give suitable investment advice.

"ASIC has acknowledged in its Strategic Outlook that weak compliance systems and poor cultures, as well as vertical integration, can compromise the quality of financial advice. An adviser's conflicts of interest and lack of competence can lead to investors being advised to buy products which are not suitable taking into account their needs and risk preferences," Mr Resnik said.

"Advisory firms should have policies and procedures in place to ensure that customers' needs are at the heart of their business and that their advisers comply with their legal obligations.

"The adoption of FinaMetrica's Five Suitability Proofs by advisory firms would work well as a safeguard for consumers. The Five Proofs are the key steps advisers should follow to confirm they have delivered relevant and personal financial advice. They are:

1. **Prove** you know the client's circumstances, needs and aspirations
2. **Prove** you have explored alternative financial behaviours and strategies
3. **Prove** you know the products and services being recommended to a client
4. **Prove** you have explained to the client the risks in the plan and the products through which the plan will be implemented
5. **Prove** you have received the client's informed consent to the risks in the plan.

Mr Resnik said the "enhanced, industry-wide public register of financial advisers" which the Federal Government will establish by March 2015 could help to improve consumer confidence in the financial advice industry. However, this alone would not prevent advisers giving unsuitable advice.

"A greater cultural change is needed. Consumers' needs must be elevated to a priority if we want Australians to value and take our financial advice," Mr Resnik said.

<u>About FinaMetrica</u>
FinaMetrica specialises in risk tolerance and risk-related matters. The FinaMetrica risk profiling system is based on a psychometric test of personal financial risk tolerance. Psychometrics, a blend of psychology and statistics, is the scientific discipline for testing attributes such as risk tolerance. Launched in 1998, the system is used by than 5,500 advisers in 23 countries in seven languages. More than 700,000 risk tolerance tests have been completed. The FinaMetrica system enables advisers to make valid and reliable assessments of their clients' risk tolerance, incorporate those assessments into the financial advising process and explain risk more meaningfully. More information: *www.riskprofiling.com*.

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