TOPIC 2

KAPLAN PROFESSIONAL EDUCATION

2

The financial planning process and planner skills

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Overview

Financial planners follow a structured process when developing a financial plan and providing advice to clients. There are many ways in which the various steps and stages involved in this process can be broken down, but a common approach is to use a six-step process. Although financial planning situations will differ from client to client, the six-step process contains principles that can generally be applied across all manner of client circumstances.

This topic examines what occurs at each stage of the process, with a focus on planner skills and legislative compliance. The ongoing business of a financial planner depends on being able to develop and maintain positive and productive relationships with clients, in which every interaction is underpinned by integrity and compliance with legal standards.

This topic introduces you to a sample case study. This case study and the associated statement of advice (SOA) will be used throughout the subject to reinforce learning concepts. Working through the sample case study and learning each new concept will help you to complete your assignment.

Learning objectives

In this topic, you will learn:

- key skills that a planner should possess to develop positive relationships with clients
- the requirements for the complaints resolution process in the financial services industry
- what is involved in each stage of the financial planning process
- the role and contents of a financial services guide (FSG)
- aspects of the collection and analysis of client information, which forms the cornerstone of an effective financial plan
- how to define and identify quantitative and qualitative information
- how to identify a client's financial goals and objectives
- how to determine a client's risk profile
- key areas to be addressed when developing recommendations
- how to develop recommendations
- the role and content of an SOA
- the role and content of a product disclosure statement (PDS)
- requirements of the presentation interview
- how a financial plan is implemented
- the purpose and importance of the client review process.

1 Developing and maintaining positive client relationships

The relationship between the client and the financial planner is the key to successful financial planning. It is essential that a financial planner take a client-centric approach.

Clients expect ...	For example ...
Reliability	• When a commitment is made, it happens, as promised. • The provider follows up to ensure client needs are met. • Appointments are kept. If the provider is going to be late they let the client know.
Responsiveness	• When a client leaves a message the provider returns the call as soon as possible. • When a client asks for something, they get it on time.
Quality of service and product	• The provider delivers the best service they can for the client. • Products recommended are of high quality and the most appropriate to the client's needs.
Positive, friendly working relationship	• The provider genuinely cares about the client and their needs. • The provider makes an effort to find out the client's needs. • The provider is always friendly and makes an effort to develop a positive working relationship, even in difficult circumstances.
Credibility	• The client has confidence in the provider because they project an image that says, 'I know my area of work. If I don't know something, I will find out or refer you to a good alternative provider.' • The provider projects a credible, professional image of themselves and their team.
Achievement	• The ability to deliver on agreed outcomes.

Financial planners are encouraged to develop the appropriate people skills to enable them to see and hear when clients are being honest with them and themselves. A financial planner is there to:

- listen
- filter for the truth, in terms of client needs and objectives
- discuss with the client(s) their interpretation or concerns
- document any new agreed understanding.

Client satisfaction is not simply a measure of how good a service is relative to the fee that is charged. Client satisfaction is really about client expectations and how they perceive that those expectations have, or have not, been met.

An approach to consider is to use every contact and communication with the client to set expectations at appropriate levels and to reinforce their perception of the service they are receiving.

The following are some key points to keep in mind when establishing and maintaining client relationships:

- Send messages that are:
  - non-judgemental
  - honest
  - open
  - direct.
- Listen and show:
  - interest
  - understanding.
- Respond in a way that:
  - is respectful
  - raises the client's self-esteem
  - seeks contribution from the client.
- Solve problems in a collaborative way.

Resource 1 — On track: Building trust in trying times

(Kaplan Professional)

Read this article about the importance of planners offering more than just superior financial products and services. In difficult markets, planners also need to develop and maintain a high level of client trust throughout the relationship.

Note: You can access this resource at KapLearn.

1.1 Getting to know clients

It is important to remember that, before a financial planner can start to think about financial products and strategies, they have a legal obligation to know their client — this includes understanding their financial goals, circumstances and the degree of risk they are comfortable with. It is more than likely that clients will come from a variety of backgrounds, with a range of previous financial experience, objectives, needs and preconceived ideas.

No single approach or solution will meet the needs of all clients, and a planner's own ideas and preferences may not sit comfortably with all clients. Skilled planners can quickly establish rapport and a free flow of information with their clients.

To be able to provide appropriate advice to clients, it is essential for planners to:

- undertake a detailed analysis of the client's current situation
- have an understanding of the client's current commitments and financial needs
- consider the client's future goals
- appraise the client's exposure to financial risk.

1.2 Clients with special needs

A financial planner needs to be able to handle clients with special needs, such as people from different cultural backgrounds and clients who may have difficulty in understanding the financial planning advice provided to them. It is important that the financial planner ensures the right questions are being asked during the first contact with client, for example: 'Do you have any special requirements?'

Once any special needs have been identified, the financial planner should take appropriate action and make any referrals, such as organising an interpreter.

2 Communication in the advising process

It is very important for financial planners to communicate with clients in a way that is appropriate to each client. A professional and comfortable atmosphere is also essential.

Communication should be personalised, targeted, regular and ongoing, and should be of value to the client on each occasion. Communication can be face-to-face or by telephone, email or mail.

It is essential for financial planners to develop good people skills. They must be skilled listeners, so that they gain a more holistic view of their client — what they are concerned about, their attitude toward particular issues and what they value.

By developing skills in communication, a financial planner is able to:

- read the hidden meaning in clients' verbal and non-verbal signals
- convey information, empathy and a desire to help meet clients' needs.

An effective communicator has proficient observation and listening skills and pays attention to words and silences, activity and inactivity.

2.1 Verbal and non-verbal communication

Verbal communication has several levels:

- the literal meaning of what is being said
- what the speaker thinks is being said
- what the listener thinks is being said.

More often than might be expected, this results in three very different interpretations of the same message. At times, the listener has to read between the lines to understand what the speaker really means.

A financial planner should use clear language suited to the particular client. This language needs to be free of jargon and ambiguity. Verbal communication should align with tone of voice and non-verbal communication.

The tone of a person's voice can suggest emotions, such as happiness or nervousness, and can be gathered from:

- where the speaker places emphasis
- pitch, volume and timing
- voice reflexes, such as coughing and sighing.

Non-verbal communication can aid a planner in understanding what the client really means, as well as in helping the planner to convey meaning and confirm and reinforce what they are saying. Non-verbal communication includes body language, such as:

- posture
- gestures and body movements
- appearance (grooming and clothing)
- facial expressions.

Apply your knowledge 1: Verbal and non-verbal clues case study

Martin was interviewing prospective new clients, Bernie and Mary. Bernie indicated that, overall, they had done well with past investment choices they had made themselves. Although he admitted some failures, Bernie felt they could demonstrate that they had come out ahead and had done so as often as many of the funds reported in the papers.

Bernie said:

> *'Things are now getting a bit more complicated, with so many choices that Mary and I feel it might be time to get some advice and perhaps put things in the hands of a financial planner. Besides, it's time-consuming managing things ourselves, and we'd like to take more time for our leisure pursuits.'*

Mary shuffled in her seat and rearranged her hands on the table but added no comment.

When asked by Martin how she felt about allocating the investment responsibility to a financial planner after doing it themselves for so long, Mary replied briefly that she: 'hadn't had much to do with it'.

> *'I don't feel like I'm giving up much. Bernie always handles things himself and … well, we won't go into that. What can you do for us, Martin?'*

At this point, Bernie started to look uncomfortable. He sat back in his chair and folded his arms but did not comment, awaiting Martin's reply to Mary's question.

a. List the clients' verbal and non-verbal clues.

Verbal clues	Non-verbal clues

b. What techniques/methods could Martin have applied to improve the outcome and value of the interview?

Note: You can access 'Suggested answers' for this activity at the end of this topic.

2.2 Listening skills

The effective communicator recognises that talking and listening are equally important in verbal communication.

Some barriers to understanding what the other person is really saying and what they really mean are:

- personal bias
- assumptions and false conclusions
- hearing what we want to hear
- pre-judging the problem or the solution
- talking too much
- a mind closed to alternatives and other opinions
- fear of being wrong
- jargon.

By developing sound listening skills, financial planners are aiding effective communication and relationship-building by:

- showing interest in what the other person is saying
- understanding what is being said.

The skill used by effective listeners is called ‘active listening’ and involves feedback, gestures, expressions and ensuring that what is being heard is not being misinterpreted.

Active listening is used to obtain more information and involves:

- showing the listener you are interested — for example, through eye contact, nods and body posture
- paraphrasing and acknowledging what is being said
- using questioning and summarising techniques to convey understanding and confirm understanding
- using silence when appropriate.

Feedback can be:

- non-verbal (e.g. a friendly smile, head nod and eye contact)
- verbal (e.g. ‘I see’, ‘Go on’ and ‘Is that right?’)

Apply your knowledge 2: Active listening

The table below contains statements made by clients. Insert the underlying feelings that influence each statement.

The statement	Underlying feelings
'My wife always makes the financial decisions, and she's the careful one.'	
'John filled in the form you sent us before the meeting — we didn't discuss it.'	
'I'm getting too old to work, but I need the money.'	
'It seems so final to be making decisions about retirement.'	
'I'm not good with calculations.'	

Note: You can access 'Suggested answers' for this activity at the end of this topic.

2.3 Questioning skills

The whole exercise of getting to know the client revolves around asking questions. It is up to the financial planner to gather as much information from their client as possible.

Questions are tools that can be used to help obtain information, build rapport and confirm understanding.

Techniques to make the questioning process more effective and more comfortable for the client include:

- asking one question at a time
- allowing the client time to answer
- using different types of questions.

The financial planner should be clear about the purpose in asking particular questions at a particular time. For example:

- clarification when information provided is vague or inconclusive
- when more general information is needed to fill in the gaps
- to probe a little deeper to obtain specific details.

Types of questions

There are many types of questions. Some may be used at any time; some need only be used at certain stages.

Open-ended questions

Open-ended questions seek to open up the communication and begin with words such as, 'How …?' or 'What …?' The aim of open-ended questions is to:

- uncover the other person's real view or problem
- elicit underlying feelings
- allow the client to finish what they are saying
- identify common ground.

Reflective questions

Reflective questions are open-ended questions that build rapport, show empathy and often begin with, 'So, you feel that …?' or 'So, this experience has left you feeling …?'

When using reflective questions, it is important to:

- listen for key words and underlying feelings
- 'mirror back' and summarise key words and feelings
- be non-judgemental.

Closed questions

Closed questions call for a 'yes' or 'no' answer. They can be used to confirm understanding and pieces of information.

Apply your knowledge 3: Difference between open and closed questions

Turn each of the following closed questions into open questions.

Closed question	Open question
'Are you happy with your current financial set-up?'	
'Do you have a share portfolio?'	
'Do you have expectations of me?'	
'Do you have superannuation?'	

Note: You can access 'Suggested answers' for this activity at the end of this topic.

3 Dealing with disputes and misunderstandings

Complaints, problems and misunderstandings arise even in the best client–planner relationships. If handled correctly, problems can be turned around and used to enhance the relationship. With few exceptions, clients will feel even more comfortable with a planner if they can satisfactorily resolve a problem situation.

3.1 Managing disputes with clients

When a client first makes a complaint, the financial planner should:

- listen and demonstrate active listening skills
- involve the client in defining the problem
- deal with feelings first
- uncover the facts
- take notes and summarise — write possible actions for the planner and the client
- show that the client has been both heard and understood. Summarise both the facts and the feelings
- recommend or take action: present solutions, tell the client what will happen and set time frames
- follow up — take action and let the client know what is happening.

3.2 Formal dispute resolution

If attempts to resolve a complaint or dispute with a client fail, the planner's licensee organisation must have a formal dispute resolution process in place.

This is a legal obligation, and the process must be approved by the Australian Securities and Investments Commission (ASIC).

Dispute resolution systems must consist of:

- an internal dispute resolution procedure that complies with standards made or approved by ASIC under the Corporations Regulations 2001(Cth) (including Australian Standard AS ISO 10002-2006 *Customer satisfaction — guidelines for complaints handling in organizations*)
- membership of an ASIC-approved external dispute resolution (EDR) scheme.

The FSG given to clients must contain a simple and easy-to-use guide explaining the procedures for making a complaint.

Internal procedures must be able to deal with all complaints made by retail clients concerning financial services covered by the licensee. ASIC's Regulatory Guide RG 165 'Licensing: Internal and external dispute resolution' requires licensees to ensure that their internal dispute resolution procedures are transparent and accessible to employees and clients. All staff must have a copy of these procedures.

Apply your knowledge 4: Dispute resolution

Briefly describe the internal dispute resolution process in your current workplace.

State the EDR scheme used by your licensee.

Note: This answer will be specific to your organisation.

The Financial Ombudsman Service (FOS) is the primary organisation providing ASIC-approved external complaints resolution services for consumers who are unable to resolve a dispute directly with their financial service provider. In addition, the Credit Ombudsman Service (COS) provides EDR for the credit industry, and the Superannuation Complaints Tribunal (SCT) deals with complaints about superannuation funds.

The availability of an EDR scheme that is binding on the licensee means that complaints that would not normally be brought before a court, owing to the cost of legal proceedings, can be aired and resolved.

Example

ASIC takes this requirement seriously. In the middle of 2012, ASIC cancelled the credit licence of a Sydney finance broking firm for failing to maintain its membership of an approved EDR scheme. The firm was expelled from membership of the FOS and had failed to obtain membership of the other approved EDR scheme, the COS. ASIC then cancelled their credit licence.

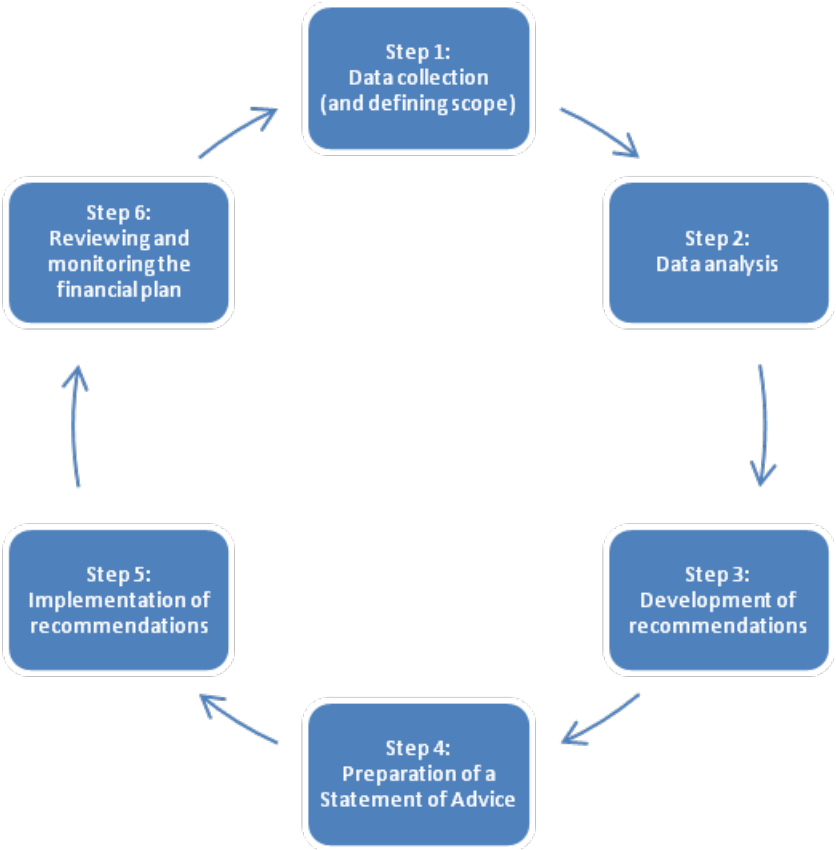
4 The financial planning process

The financial planning process can be viewed as a series of logical steps, each requiring the application of a wide range of skills and knowledge on the part of the financial planner.

4.1 The six steps of financial planning

The process is generally broken down into six steps, as set out in Figure 1. Some financial planners follow variations in the six-step process but all models generally cover the same areas. The Financial Planning Association of Australia (FPA) and the Association of Financial Advisers (AFA) have their own versions of the process that are, in essence, the same as that shown in Figure 1. It is important to note that the six-step process is a cyclical and ongoing process.

Figure 1 Six steps of financial planning



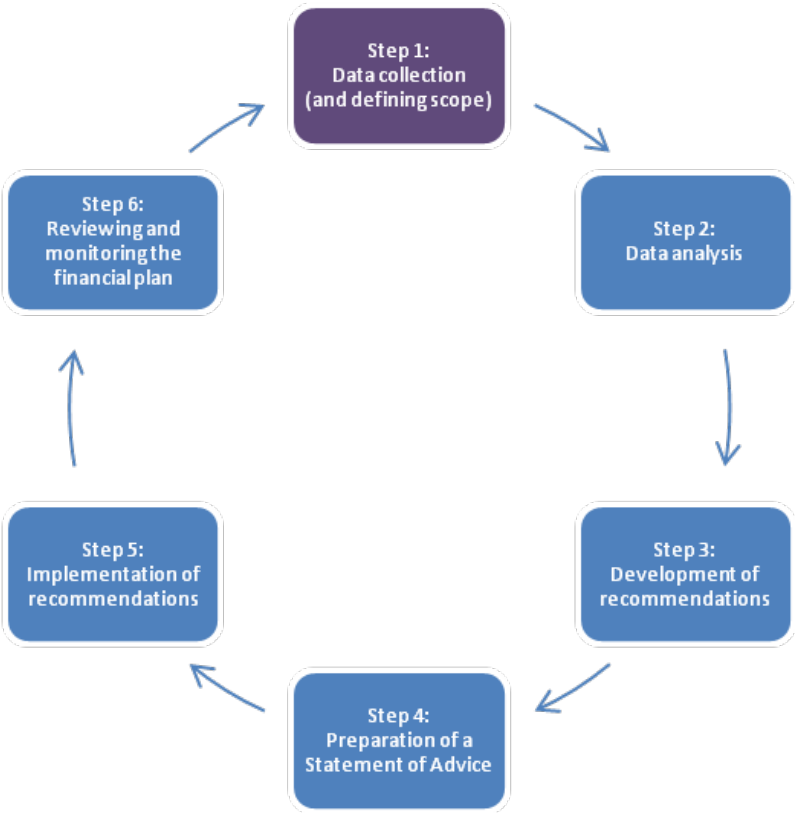
1. **Data collection:** A fact-finding interview with the client intended to gather comprehensive financial, non-financial and attitudinal information. This information includes expenses, personal assets, liabilities, insurances, investments, taxation considerations, estate planning issues, superannuation and attitudes to risk. Planners must also be aware of clients' short-, medium- and long-term financial needs, goals and objectives.
2. **Data analysis:** Analysis of the client's personal and financial information to identify and assess financial planning issues relevant to the client and to the achievement of their goals and objectives.

3. **Development of recommendations:** Consideration of alternative options when formulating financial strategies, and development of a comprehensive plan to effectively achieve the client's goals and objectives.
4. **Preparation of an SOA:** An SOA is a compulsory disclosure document that assists clients in understanding the recommendations a planner is making. By law, an SOA must be presented to the client at the same time that the advice is provided (with few exceptions). Another industry related term for this document is a financial plan.
5. **Implementation of recommendations:** Completing and documenting administrative processes, such as opening accounts, lodging application forms, arranging insurance and purchasing investments. Also includes the lodging of all paperwork and obtaining all necessary signatures and approvals.
6. **Reviewing and monitoring the financial plan:** Periodic review of the client's circumstances, the investments and the plan. The plan should be modified when a need is identified by the review.

As previously mentioned, one of the most critical skill sets that a financial planner needs to demonstrate is effective communication. Establishing and maintaining a high level of constructive communication with clients is a component of all the steps of the process, although some steps emphasise communication more than others.

Each step in the process is discussed in detail in the following sections.

5 Data collection



5.1 Initial client contact

The first contact a financial planner has with a new client is often on the telephone. This can be challenging because non-verbal communication forms a large part of the successful communication process and once visual clues and eye contact have been removed, communication and understanding can be difficult. However, the financial planner must not overlook the significance of facial expression, even on the telephone.

Choice of language on the telephone is also important. If the financial planner is the initiator of the telephone call, they should be aware that the call might be intrusive at that particular time. The financial planner should briefly introduce themself and state the reason for the call, then ask if it is a good time to talk or if it would be more appropriate to call back.

This initial call is the beginning of the relationship with the client and, once rapport is established, the next step is to start identifying the client's needs.

Information gathered during the initial contact

During the initial contact, questions can be asked to obtain some background information before a face-to-face meeting. Questions might include:

- Is the client single or in a partnership? If they have a partner, suggest that the partner also attend the meeting.
- Are they employed?
- Do they have children?
- What do they aim to achieve from the financial advice offered?

Prior to the first meeting, it may be appropriate to provide the client with a list of items or information to bring to the meeting, which could include:

- planned budget
- superannuation details
- a list of assets and liabilities
- income and expenses details.

It may also be appropriate to suggest some factors the client could consider and discuss with their partner, if they have one, such as:

- short-, medium- and long-term objectives
- any planned capital expenditures, such as holidays, home renovations or study.

The key is to encourage the client to come to the meeting as prepared as possible. That way, the actual client meeting will be more productive.

Refining the technique

There is a limit to how much information can be requested during the first contact, especially if it is over the telephone. Over time, a planner will refine their techniques for data collection before and during the initial face-to-face interview. For example, a planner may:

- send out a fact finder, either as a standard form or as one specific to the client
- provide a list of specific information the client should bring to the meeting
- prefer to leave everything until the first face-to-face meeting.

Reflection

Think about yourself as a client: how would you prefer to provide personal and financial information? Would the information be available immediately to you or would you need time to gather it?

5.2 Developing client rapport

Good client rapport leads to an open and harmonious relationship, ensuring all of the relevant facts will be revealed during the fact-finding interview and a complete picture will be established. It also means that, should something be overlooked, neither party will be inhibited about asking questions.

Establishing rapport begins immediately. If the planner is late for the meeting or has kept the client waiting, the client may feel that the planner does not consider their business important. Building rapport can be helped by:

- greeting the client in a warm, open and courteous manner
- addressing the client by name during the interview
- ensuring the client is comfortably seated and at ease for the interview
- offering the client tea or coffee or a glass of water
- where appropriate, engaging in ‘small talk’ to establish some common ground with the client
- setting a time frame for the interview and outlining what will happen
- using suitable body language
- observing and responding to the client’s body language.

An important element is empathy. A skilled interviewer must ask the kinds of questions that will encourage the clients to talk about themselves.

Early in the meeting, the planner should let the client know about:

- the steps involved in the financial advisory process
- the planner’s role and capacity to do the job.

5.3 The first meeting

The purpose of the first 'fact-finding' interview is to gather all of the information required as a basis for the recommendations that will be included in the SOA. The end result of this initial interview should be a profile of the client that provides information on the client's current financial position, needs, objectives and personal details. It is also important at this first meeting to define the scope of the advice that can or will be provided to the client.

It is important to ensure that you have prepared adequately for the first meeting, including briefing the client on the process and setting expectations, preparing your own environment, having an agenda ready, and having everything you will need for the meeting at hand.

Resource 2 — Sample case study and sample SOA

This comprehensive case study applies the principles and foundations of financial planning. Each element of the financial advice process is considered and an SOA is prepared for the client in this scenario. This will be referred to many times as you progress through this topic.

***Note**:* In performing various designated tasks in this topic regarding the sample case study, you will come across technical terms and concepts that you may not be familiar with. Explanations of these terms etc. will emerge in other topics. They have been introduced now to give you exposure of their positioning in the process leading up to the creation of an SOA.

Note: You can access this resource at KapLearn.

Sample case study

Open the sample case study and read
Section 1: Introduction, initial client contact and the first meeting.

Here you will find an example of the sort of information that can be obtained by clients in the initial meeting.

Where should the first meeting be held?

There are no hard and fast rules about where meetings with clients should be held. It is more likely that the meeting will be held in the planner's office, where formal documents and investment information are readily accessible and can be given to the client immediately.

However, there will be times when a client's circumstances mean that the meeting will occur at their home.

For example, a married couple with young children may not be able to arrange a trip to an office. Occasionally, it may be necessary to meet the client at their own office if they want advice but are too busy to travel.

In any situation, it is up to the planner to be punctual, polite, informative and prepared, and to have financial services information to hand.

The venue chosen for the meeting should allow for privacy, be comfortable, neat and tidy (if it is your space), and should be non-threatening for the client.

How long should the meeting be?

Although it is necessary to gather all relevant details about the client and their needs, the financial planner should be efficient and keep the meeting as short as possible. The planner should assess the client's attitudes and expectations as the meeting progresses.

How should the meeting proceed?

Every efficiently run meeting has an agenda, which is usually in a written format. A fact-finding interview is no exception. The planner should list everything they intend to cover in enough detail to ensure that all relevant issues are discussed and that the required quantitative and qualitative data are obtained. The agenda can also be given to the client at the start of the interview.

An agenda keeps the planner on track and avoids wasting time. It can also provide part of a legal defence if there is later litigation, in particular by highlighting the issues the planner covered when investigating the client's personal circumstances.

A list of objectives should be prepared as well as an agenda. Preparing the list will help the planner to focus on the important issues. The list will vary according to the nature of the meeting being held. Sample objectives are:

- complete a fact finder
- understand the client's needs and objectives
- establish the client's risk profile.

Apply your knowledge 5: Create an agenda for the first meeting

List, in order, the items that should be included in the first meeting.

Note: You can access 'Suggested answers' for this activity at the end of this topic.

5.4 Disclosure requirements: The FSG

The Corporations Act 2001 (Cth) (Corporations Act) requires that financial planners provide clients with an FSG as soon as possible, before advice is provided. The FSG can be delivered personally, mailed, emailed, faxed, or delivered in any other agreed manner. Some planners send it out with other paperwork prior to the first meeting, whereas others provide it at the beginning of the first client interview.

ASIC does not specify at which point in the client relationship an FSG is to be provided, but recommends that FSGs are given:

> *… in enough time to give retail clients an adequate opportunity to consider the information they contain before deciding whether to obtain financial services from the providing entity.*

and that providing entities:

> *make their FSGs available to potential clients through their publicly available website (if any) and at their offices or branches*
>
> (ASIC Regulatory Guide 175.81 October 2013)

The purpose of an FSG is to provide clients with clear key information on the nature of the advisory services offered so they are able to make a decision about whether they want to proceed with obtaining advice. The minimum requirements for an FSG are set out in sections 942B and 942C of the Corporations Act and in RG 175. The 'Apply your knowledge' activity below lists the minimum information required. Note that other information can be included but only in addition to the legislative minimum.

The purpose of the FSG is to enable the client to at least:

- identify the licensee, the planner giving the advice and the capacity under which the planner is acting
- understand the nature of the advice and any fees and charges for that advice
- understand their basic rights
- compare advice between different providers
- understand the planner's complaints procedures.

Apply your knowledge 6: Analyse and evaluate an FSG

Read the sample FSG in Appendix 1.

Evaluate its content in light of the requirements stated above and the more detailed list of requirements provided below (all of which are the minimum inclusions listed in the Corporations Act).

To confirm your understanding of what the sample FSG enables investors to do, check the boxes below:

- ❑ Determine the date the FSG was prepared.
- ❑ Determine what their rights are in seeking financial advice.
- ❑ Identify the licensee.
- ❑ Identify the individual planner who will be providing them with advice.
- ❑ Understand that the planner is acting in a representative capacity.
- ❑ Identify who is responsible for the advice provided.
- ❑ Identify the scope and type of financial advisory services offered.
- ❑ Identify how the licensee and their representative will be paid.
- ❑ Understand remuneration (payment) arrangements.
- ❑ Determine whether commission is paid to the licensee and/or representative.
- ❑ Have a basic understanding of how commission is calculated and paid.
- ❑ Identify available complaints resolution schemes.

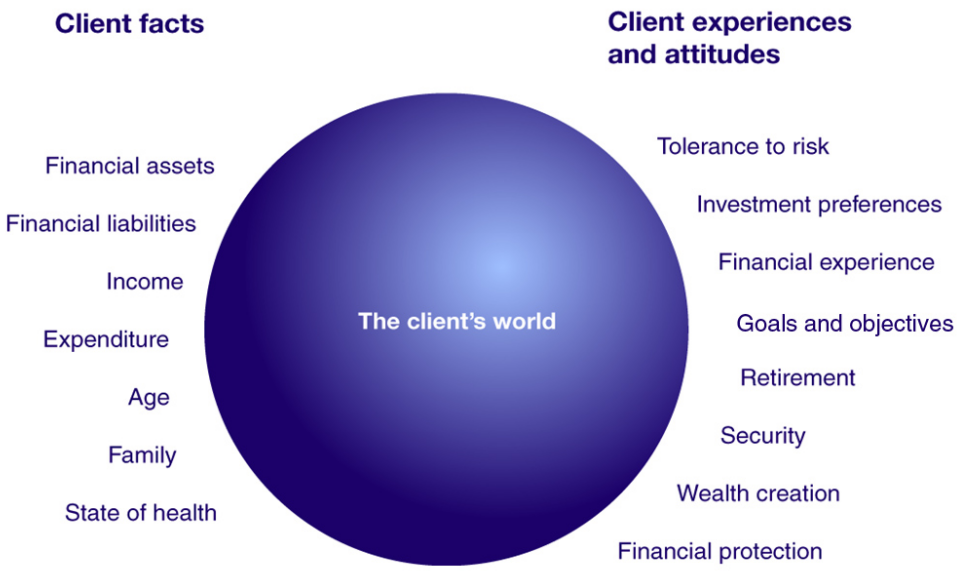
Note: You can access 'Suggested answers' for this activity at the end of this topic.

5.5 Gathering client information

Data collection is the foundation of financial planning, and if it is not carried out thoroughly, it is virtually impossible to create a plan individually tailored to meet the client's requirements. As illustrated in Figure 2, there are many client factors that can have an impact on the advice provided to them, including:

- facts
- experiences and attitudes
- goals and objectives.

Figure 2 Client factors to be considered as part of the financial planning process



Planners are legally required to act in the best interests of their client and to make sure that they identify:

> *(i) the subject matter of the advice that has been sought by the client (whether explicitly or implicitly); and*
>
> *(ii) the objectives, financial situation and needs of the client that would reasonably be considered as relevant to advice sought on that subject matter (the **client's relevant circumstances**)*
>
> (section 961B Corporations Act 2001)

The planner must also make sure that, if it was reasonably apparent that information relating to the client's relevant circumstances was incomplete or inaccurate, they have made reasonable inquiries to obtain complete and accurate information. In other words, they must try to gather as much relevant information as is necessary to provide advice.

Planners need to create a clear picture of the client's financial assets and liabilities, their goals and objectives, their attitude towards investing, and their risk tolerance. Furthermore, the adviser must ascertain whether they are able to provide the advice sought by the client, based on their own experience and licence conditions. If they are unable to provide the advice, they must decline to do so and record this on the client file.

Prior to offering advice, a planner needs to collect sufficient data to enable them to determine the client's current position, including their:

- business or work situation
- income
- expenses
- assets and liabilities
- cash
- existing investments
- insurance cover
- superannuation savings
- commitments (e.g. home mortgage, personal loans and credit cards)
- cash flow timings.

If the client chooses to limit the scope of the advice or wishes to restrict the advice to discussion of a specific need or needs, the planner should still ensure that they collect sufficient information to be sure that they are acting in the best interests of the client. For example, a client may only want advice about a limited range of insurance, but the information collected must still be sufficient to ensure the advice provided and any accompanying product recommendations are appropriate to the needs of the client.

Fact finders

An effective way of collecting information about the client is to use a form designed for the purpose, commonly referred to as a needs analysis form or a fact finder. Refer to Appendix 2 for a sample fact finder.

Fact finders are comprehensive through necessity, and they can prove time-consuming for the client. Some planners send a copy of the fact finder, along with the FSG, to their clients before the first face-to-face interview. This helps to expedite the data collection process and ensure that as much information as possible is available at the time of meeting.

In trying to develop a comprehensive picture of the client's needs, the planner should also make every effort to explore their aims, attitudes and opinions.

Sample case study

Open the sample case study and go to Appendix 1: The fact finder

Compare the information in the fact finder with the information in the case study that you have read so far (Section 1: Introduction, initial client contact and the first meeting).

Note: You can access this resource at KapLearn.

Apply your knowledge 7: Completing a fact finder

Complete the fact finder in Appendix 2 using yourself as an example to familiarise yourself with the type of information the planner must collect from the client before constructing an SOA or financial plan. You may prefer to complete the fact finder used in your workplace. If you do not wish to complete it on yourself, you could ask a friend or family member.

Note: The answer will be specific to your personal circumstances.

Defining quantitative information

Quantitative information is the information gathered about the client and their financial situation that can be easily identified in terms of numbers or amounts. It may also include stated facts.

Examples of quantitative data include the client's name, their date of birth, their occupation, what investments they have and who owns them, what insurance they have and how it is owned, their assets and their liabilities.

The full financial facts concerning the client's affairs should be recorded in detail in the fact-finding document so that it is very clear what they own and what they owe. Relevant documents pertaining to this information should also be obtained, copied and filed by the planner.

It is particularly important to determine the client's current cost of living. This information can best be obtained by having the client complete a budget showing their estimated income and expenditure. From this, the planner can determine the extent and potential of their discretionary savings. This information is important for almost any recommendation, and particularly for recommending asset protection, wealth accumulation or debt reduction strategies.

After properly collecting all quantitative information, a summary can then be prepared showing projected income and expenses, investment assets and liabilities. This is commonly referred to as the client's 'statement of financial position'.

The statement of financial position is also an integral part of the decision-making process about all areas of financial planning — risk management, tax planning and management, retirement and estate planning, and investment strategy.

Sample case study

Open the case study and read Section 2: Data analysis. You will see a series of tables relating to quantitative information about the clients.

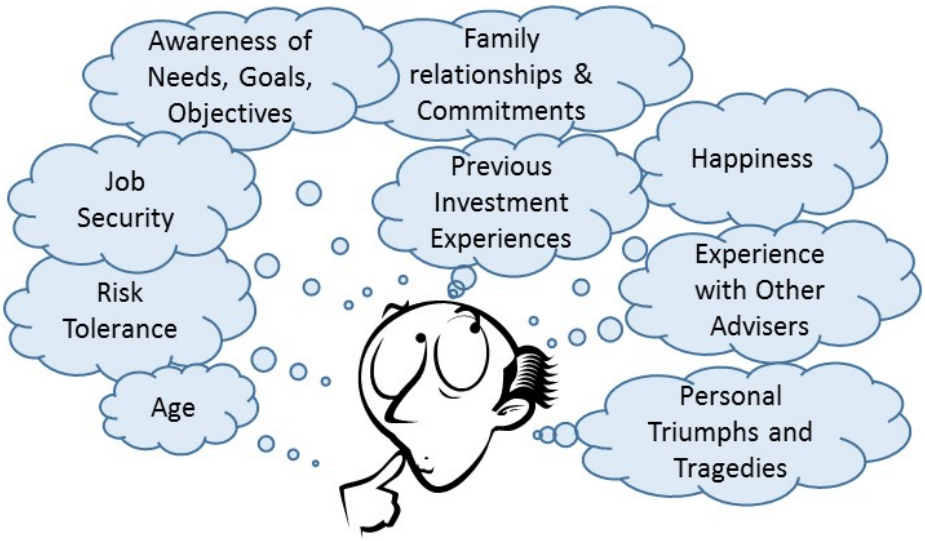
Look at Table 2. Check that the income entered for both clients match with the information gathered in the initial meeting. Check that all the investment income is correct.

At this stage do not worry about the tax calculations etc. as they will be explained in the next topic.

Defining qualitative information

Qualitative information relates to aspects of the client's situation that are not as easily expressed in terms of numbers or amounts, such as their motivations, values and beliefs (refer to Figure 3). It includes the information gathered on the psychological aspects of a client's situation and may include the client's goals and their attitude to, and acceptance of, investment risk. This is referred to as the client's 'risk profile' and will help determine where the client's funds should be invested.

Figure 3 What is on the client's mind?



Qualitative information depends on analysis of attitudes and feelings towards particular issues, and is more difficult to assess than quantitative data. Effective data gathering is based on a sensitive interpretation of the client's response to questions. Planners should be aware that the client may respond one way but mean something completely different; they may hesitate or change the subject. The planner must be skilled in both questioning and providing feedback to the client, carefully probing and clarifying until they are certain they have interpreted the information correctly.

In all aspects of data collection, planners must be aware of the confidentiality of the information they are collecting and their compliance with all aspects of the privacy legislation as outlined in Topic 1.

Apply your knowledge 8: Distinguish between quantitative and qualitative information

Classify the following types of information as either qualitative (i.e. relating to psychological aspects) or quantitative (i.e. numerical data or facts).

Information	Quantitative or qualitative?
Age of client	
Future priorities	
Family relationships	
Retirement plans	
Liabilities	`
Attitude towards risk and loss	
Previous investment experience	
Personal goals and objectives	
Education costs	
Cash flow requirements	
Desire to access capital	
Insurance held	
Superannuation information	
Need for income protection	
Home ownership status	
Personal history	
Current financial commitments	
Assets	
Funds available for investment	
Current sources of income	
Attitudes toward types of investment and asset classes	
Centrelink entitlements	
Desire to reduce tax	
Existence of Wills and power of attorney	

Note: You can access 'Suggested answers' for this activity at the end of this topic.

Apply your knowledge 9: Determine your financial position

The cornerstone of preparing a good financial plan is accurately assessing the client's financial position.

Determine your own current financial position using the following guide and the expenses tables below.

a. What is your combined annual net (after-tax) income?

From your most recent tax return work out your annual income after tax by subtracting the tax from all the income you earned in the year, including interest from cash accounts, dividends received (but not franking credits as they are not income received), rent from investment properties and any other payments made to you. At this stage do not consider any expenses you may have in relation to your investments.

If you do not have a tax return, you can make an estimate based on your net pay from your employer, assuming you are an employee.

b. What are your annual living costs (ALC)?

Major expenses (year total) (Complete Table 1)	$
Cash expenses (year total) (Complete Table 2)	$
Mortgage repayments/rent (year total)	$
Gifts (presents/donations) (estimated year total)	$
Holiday costs (annual average)	$
ALC (total of all expenses)	**$**
What is your annual savings capacity? (= Net income – ALC)	$

Table 1 Major expenses

	Weekly	Monthly	Quarterly	Annually
Rates				
Electricity				
Gas				
Telephone — mobile				
Telephone — fixed				
Internet				
House and contents insurance				
House maintenance				
Medical insurance				
Car — registration				
Car — insurance				
Car — repairs/servicing				
Car — roadside assistance membership				
Subscriptions/memberships				
Life insurance premiums				
Education/extra-curricular				
Professional fees				
Other				
Total expenses				

Table 2 Cash expenses

	Weekly	Annually
Groceries		
Entertainment		
Petrol		
Alcohol/cigarettes		
Sport/clubs		
Grooming		
Clothing		
Incidentals/miscellaneous		
Other		
Total cash expenses		

Note: The answer will be specific to your personal circumstances.

Your net income less your ALC will give you the amount of total net cash flow, also known as your disposable income. In other words, the amount of money you could contribute to investing etc.

Sample case study

Open the case study and read Section 2: Data analysis. You will see a series of tables relating to quantitative information about the clients.

Look at Table 2. Here you will see the clients' total net cash flow calculation. You will see that the income the clients actually received is added up, the expenses and tax are subtracted, and a net cash flow amount is determined.

At this stage do not worry about the tax calculations as they will be explained in the next topic.

Note: You can access this resource at KapLearn.

Apply your knowledge 10: Current financial portfolio

a. Complete Table 3 to determine your net worth. Include the following:

- Investment assets (shares, term deposits, cash management accounts, superannuation etc.) and liabilities (investment property loans, margin loans, etc.).
- Personal assets (home, car, bank accounts, etc.) and liabilities (mortgage, personal loans, credit cards, etc.).

Table 3 Current financial portfolio — assets and liabilities

Investment assets	Owner	Market value	Income p.a.		Capital growth p.a.		Loan amount	Loan interest or repayments p.a.	
			%	$	%	$		%	$
Personal assets	**Owner**	**Market value**	**Income p.a.**		**Capital growth p.a.**		**Loan Amount**	**Loan Interest or repayments p.a.**	
			%	$	%	$		%	$

b. What is the net value of your investment portfolio (= assets – liabilities)?

c. What is the net value of your personal assets (= assets – liabilities)?

Note: The answer will be specific to your personal circumstances.

Sample case study

Open the case study and read Section 2: Data analysis. You will see a series of tables relating to quantitative information about the clients.

Look at Tables 3 and 4. Check that the assets entered for both clients match with the information gathered in the initial meeting. Check that the liabilities are also entered correctly.

Observe how the sum of all of the clients' assets minus all of their liabilities gives you their overall 'net worth'.

You should also notice that the table has been split into 'personal assets', 'superannuation' and 'investment assets' just as a way of distinguishing between the different types of assets. Personal assets are usually those 'assets' that are not used to generate income and are often not sold to generate wealth for the clients, such as jewellery, cars, and home contents. The family home is usually included here too, although in some cases it is an asset that a client may sell at retirement to increase their wealth. In many cases it is retained and hence counted as a personal asset rather than an investment.

Note: You can access this resource at KapLearn.

5.6 Determining client expectations

The next step in the data collection process is establishing the client's personal objectives and lifestyle goals. Careful questioning may be needed, as many people have difficulty expressing their financial goals.

For example, a client may have originally sought advice based on their recognition of the need to plan to receive an adequate income during retirement. During the fact-finding interview, some taxation and estate planning issues may have emerged. Consequently, the development of the recommendation will need to be more comprehensive than originally thought.

The financial planner should make a written record of this information before making any recommendations. All of this information is essential in demonstrating a reasonable basis for recommendations under the new 'best interests' obligation (which replaced the 'know your client' rule from 1 July 2013).

Needs versus objectives

Needs are often defined as basic requirements that must be met. For example:

- paying the bills
- paying taxes
- paying rent
- maintaining the home.

These needs must be provided with reasonable security and minimal volatility (i.e. a low degree of variation in income flow). Income projections connected with needs should be conservative and take into account any fees or costs.

Objectives can be defined as the client's desired goals, which will change over time. A process to deal with changes needs to be incorporated into the recommended plan and forms part of the ongoing service offered to the client.

Examples of financial objectives might include to:

- achieve a certain level of income by a certain time
- accumulate a certain level of assets by a certain time.

More specific financial objectives might include to:

- save a sufficient amount for a deposit on a home within five years
- have enough money put aside to pay for a child's private school education
- have enough superannuation at age 60 to generate an income of $50,000 per year.

At times, the distinction between needs and objectives can become blurred, and one person's objective can be another person's need.

For example, some people might consider an overseas holiday every year or so an objective; others might consider it a need.

Common client needs

Common client needs, and some of the factors that should be considered when assessing these needs, are explored below.

Income and expenses

When establishing a client's income needs, their living expenses should be broken down into fixed and variable categories. This differentiation is important, as fixed cost expenses require a component of the investment portfolio to be allocated to provide income on a regular basis.

It is wise to allow for contingencies, as clients often underestimate living expenses. The size of this factor will depend on the perception formed of the client's estimates. If a client is vague or indifferent about their estimates, it might be an indication that the contingency component should be significant.

A planner's communication and thinking model is unlikely to be exactly the same as the client's. For this reason, budgeting expenses is crucial to some clients but not others. With clients for who budgeting is inappropriate, the planner should make sure they document what the client knows they can save and what they can save if 'motivated'. These amounts will be different.

Liquidity

Investment liquidity usually refers to the ease or speed with which an investment can be converted back into cash, with little or no loss of value.

For example, a share in a major company can be sold and the money made available within a few days of the transaction. Money from a cash management trust (CMT) can often be obtained the same day. Although both options are relatively liquid, of the two, the CMT has more liquidity.

Flexibility

The ability of an investment to provide differing return characteristics is one aspect of investment flexibility. An example of this is the 'split trust' concept, where investors can switch from one investment class to another, resulting in a change in the investment return characteristics (i.e. income to growth, or growth to income). This is beneficial should the needs, or the lifestyle, of the client change.

Like a client's risk profile, a client's liquidity and flexibility requirements may be difficult to quantify. It is important that the planner achieves a good understanding of the client's needs in these areas so that money, if required, can be easily accessed with little, if any, loss to the client.

Growth

Generally, all clients want the highest return for the lowest risk. As risk and return are interrelated, a compromise, or balancing, is required. For some clients, the reason behind their growth requirements is their desire to provide a hedge against inflation. Others may want to maximise their estate for the benefit of their family.

The following factors will have a bearing on the client's need for growth:

- **client's income** — they need to be able to satisfy their immediate needs and have surplus income to invest for future growth.
- **client's risk tolerance** — they may be so averse to risk that they will not accept the higher risks associated with growth assets.
- **client's financial knowledge to date** — note that many clients' risk tolerance will change as the financial education process continues.

Other factors, such as the client's age, lifestyle and concern for inflation, may mitigate their need for growth investments.

Taxation

Taxation factors form a critical part of financial advice but should not be the dominant investment strategy. The planner must understand the overall tax position of the client, as well as the tax structure of available investments. It is therefore essential to have a well-grounded understanding of tax basics. The planner may need to work with the client's accountant or tax adviser to ensure proper coverage of taxation issues, as they usually will not legally be able to give specific tax advice.

Setting specific goals

Clear client goals give the planner specific targets on which the recommendations can be built. At the same time, the client grows to understand that there are real-time events towards which the recommendations will be moving. These events are then clearly defined and identified so progress can be measured, evaluated and reviewed over time.

Of the many types of client objectives, most fit into three general categories:

- protection against personal risk
- the accumulation of capital
- the distribution of capital.

Objectives should be stated explicitly

Good objectives are SMART: specific, measurable, achievable, realistic and time-bound.

Achieving objectives is dependent on a precise definition of what the objectives are. Consequently, all specifics about an objective should be clearly and carefully analysed and outlined. Questions such as the following should be posed:

- Who will be involved in accomplishing the objective?
- What resources will be expended in seeing the objectives through to completion?
- What liabilities would be incurred in accomplishing the objective?
- What personal financial changes/sacrifices will be needed?
- According to the plan, when is the objective to be achieved?

Objectives should be realistic

It is the planner's role to explain to the client whether the objectives they have communicated are realistic and achievable, given their current situation.

For example, if a client does not wish to pay for insurance because they have limited financial resources, the planner must explain to the client the potential financial consequences that may arise as a result of unexpected medical costs, loss of income due to disability or sickness, premature death, property loss or liability; costs which may far outweigh the initial outlay on insurance.

Objectives should have a specified time frame

The planner must know whether the objective is a short-, medium- or long-term commitment. Setting a time frame to achieve a financial objective and clarifying the length of their financial commitment helps to avoid disappointing the client, who may expect unreasonably fast results.

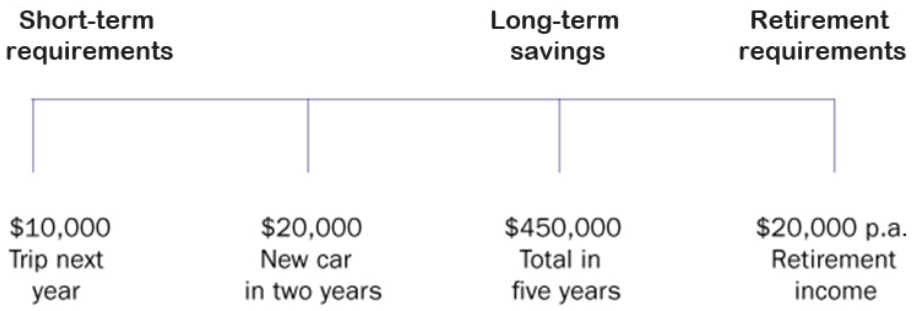
Throughout the fact-finding process, the planner must remember to allow the client as much scope as possible to 'do the talking' and reveal their own situation.

Construct a time line

The planner should ask the client to consider short-, medium- and long-term financial goals. Although it may be a difficult subject to raise, the client should also make plans for the transfer of assets after their death.

With this information, a planner can use a time line to put the client's cash needs into perspective (an example time line is shown in Figure 4). This time line can then be overlaid onto a cash flow analysis to see where funding falls short.

Figure 4 Time line of cash needs



Apply your knowledge 11: Your financial objectives

Now that you have determined your current financial position, ALC and annual saving capacity, give some thought to your financial goals, objectives and concerns.

Divide your objectives into the following time frames:

- short term (within one to two years)
- medium term (within two to five years)
- long term (time frame longer than five years).

The following pointers may assist you. Try to estimate their dollar value where possible.

- insurance needs
- superannuation/retirement plans (e.g. retire in five years)
- taxation concerns
- estate planning (e.g. wills, enduring powers of attorney, etc.)
- income requirements
- anticipated expenditure (e.g. paint house, holidays, buy car, etc.)
- education costs
- what to do with surplus income
- purchase/sale of assets

Note: The answer will be specific to your personal circumstances.

5.7 Risk profiling

The next important step in the data collection process is the development of a risk profile of the client.

ASIC states that, where advice relates to financial products with an investment component, collected data needs to include the client's:

- need for regular income
- need for capital growth
- tolerance of the risk of capital loss, especially where this is a significant possibility if the advice is followed
- tolerance of the risk that the advice will not produce the expected benefits
- existing investment portfolio (if applicable).

Experts in risk management generally talk about two types of risk:

- **Pure risk**, which is defined as uncertainty as to whether a loss will actually occur. This is the only risk that is able to be insured. Put simply, pure risk is the concept that a person either suffers a loss or does not suffer a loss. It includes:
  - **personal risks** — these are risks associated with the individual person and cover areas such as death and disability
  - **property risks** — these have to do with the destruction of, or damage to property
  - **liability risks** — these risks concern loss or damage to a third party. A third party is anyone else apart from the insured person and the insurer
  - **non-performance risks** — this is where one party agrees to do something but does not do it and, as a result, another party suffers a financial loss.
- **Speculative risk**, which is normally associated with investments and is defined as a situation in which there is the chance of a loss or a gain.

  For example, on the one hand, the client may lose the money they have invested or not receive the return they had expected. On the other hand, there may be a gain from the investment.

Explaining risk to clients

Risk is often described as the ability to recover total investment capital at any point in the future. In reality, the concept of investment risk goes much further and includes the degree to which investment returns will fluctuate or vary.

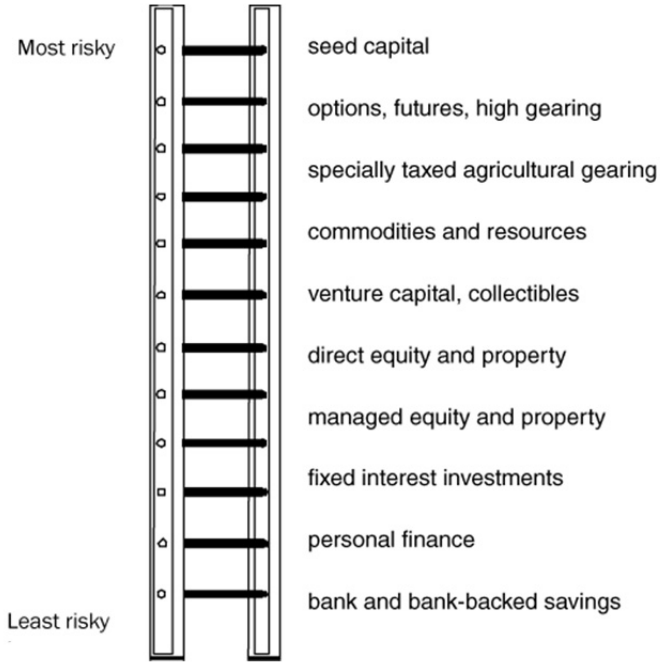
When explaining investment risk to a client, it is important to ensure that the client understands the elements of risk involved in any proposed investment strategy.

A basic but sometimes overlooked point is that higher returns are generally associated with higher risk investments. Lower risk investments generally offer lower returns.

This is sometimes referred to as the 'risk–reward trade-off'.

Clients must be made aware of the level of risk associated with the financial products being considered and/or recommended. Figure 5 provides a simple illustration of how various investment products can be ranked according to their potential risk.

Figure 5 Investment products ranked by risk



A client's understanding of investment risk

A client's risk tolerance is generally defined as their comfort level with the short-term volatility of their portfolio, and the concern that their investment portfolio balance will be less than expected in the future.

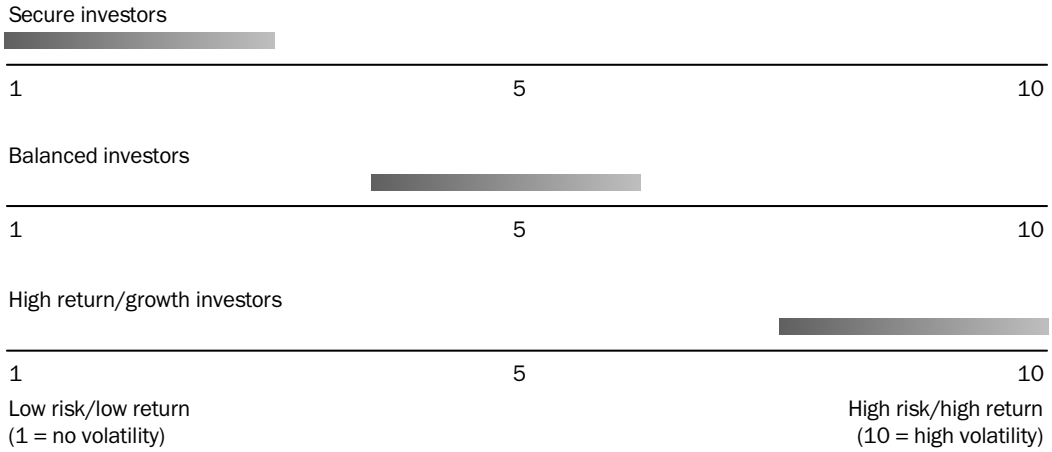
Most people only focus on volatility in the short term and do not understand the trade-off between short-term volatility and long-term performance.

The more risk-averse (i.e. uncomfortable with short-term volatility) a person is, the more future growth they are likely to trade for security today. These people may not be able to see beyond today's discomfort to tomorrow's funding needs. They may say: 'What if I need my money today? The price may have dropped', rather than: 'This is my retirement money, which I do not need for 15 years. Short-term volatility is expected if I am going to save more money in the long term.'

Each person has a preferred portfolio. However, many people will select this preferred portfolio without knowing what their preference means in regard to risk or return.

Risk profiling is one method used for defining what an acceptable level of risk is to an investor. This helps to manage client expectations so that they are reasonable in relation to their tolerance for risk. A risk profile helps determine the appropriate risk–return trade-off for the particular investor, which can then be compared to the investor's desired financial goals and the time period agreed to achieve those goals. Risk profiles of different types of investors are shown in Figure 6.

Figure 6 Examples of investor risk profiles



If an investor has indicated that they do not need their investments to supplement their income and are prepared to invest for the long term, this could indicate that they are able to bear a higher risk. These investors contrast with investors who may be dependent on investment income for survival, and with those who are only prepared to invest on a short-term basis. Thus, the investor's time horizon, disposition, current income requirements and lifestyle aspirations are crucial to determining their risk tolerance. The longer the time horizon, the greater time the investor will have to 'ride out' the rises and falls of the portfolio value.

A client's understanding of, and comfort with, risk often increases as the investor becomes more knowledgeable and experienced in investment issues. They become able to see past short-term fluctuations in the investment value of their portfolio and to focus more on the long-term return that higher risk growth assets can provide.

Apply your knowledge 12: Risk profiling

What are your major investment concerns? What type of investor are you?

Note: The answer will be specific to your personal circumstances.

Determining a risk profile

A financial planner must not rely on their intuition when determining a client's appropriate risk profile. It is important to ask the client many questions about their particular goals and fears to determine whether they will be able to bear a fall in the markets without undergoing undue hardship or stress.

Determining the appropriate risk profile of a client is more than just good practice; it is a requirement for financial planners.

Risk profiling is not an exact science. Arriving at an appropriate risk profile for the client can be tricky, although there are a number of tools available to financial planners. The modern versions of these tools incorporate both anxiety-based risk assessment and lifestyle requirements of the client.

Risk diagnostic tools

There are several tools available to help assess the client risk tolerance.
At the conclusion of the risk profiling exercise, the planner and the client should be able to agree on the particular requirements that categorise them as a 'type' of investor.

Tools include:

- questionnaires
- psychometric testing
- online tools.

Questionnaires

Diagnostic questionnaires are available to help assess the client risk profile. They can range from half a dozen multiple-choice questions to complex questionnaires.

Psychometric testing

Psychometric testing is any method, whether in the form of a questionnaire or a behavioural study that assesses an individual's psychological profile. In the context of financial advising, a psychometric test assesses a client's psychological acceptance of risk in the pursuit of an investment objective.

Many financial planners already use simple psychometric tests. Some financial advisory organisations have either developed their own psychometric tests or adopted proprietary products and systems.

Psychometric testing and planner obligations

Psychometric testing has been available for some time and, despite initial setbacks, its popularity has increased in recent years.

Financial planners should be cautious when using these products because the know your client rule (along with the current best interests obligations) require more of a financial planner than merely conducting a test. The danger with over-reliance on any risk-profiling tool is the assumption that, if the client can cope with risk, the risk should be taken.

A sensible approach would involve both psychometric testing and an analysis of the client's circumstances.

For example, psychologically, the client may seem to be a risk taker; however, owing to personal circumstances, it may not be advisable to take the risk because the client has a very short investment time horizon. In this case, a low-risk strategy would be the most appropriate.

Online tools

There are numerous online tools that can be used to assess a client's risk tolerance. They include systems that can be used to determine a client's personality profile and internet-based tools that are similar to a client questionnaire.

Risk categories

After gathering data on the client's risk tolerance, it is important to come to some conclusions about their tolerance to risk in order to formulate the strategy. Clients can be generally grouped into the risk categories set out in Table 4.

Table 4 Common risk tolerance categories

Category	Definition
Highly conservative	Highly averse to risk
Conservative	Reasonably averse to risk
Balanced	A neutral approach to risk — will tolerate a degree of risk
High growth	Tolerant to risk to achieve objectives
Aggressive	A seeker of risk in return for higher gains

This can be a rather arbitrary way to categorise people. Some clients might disagree with the classifications, and there is overlap between categories. Some clients might want to invest in a range of products with varying levels of risk. Others might want to invest only in products in one risk category.

Despite the difficulties that come with general classifications, the importance of risk profiling cannot be overstated. During audits, ASIC may ask: 'How did you assess the client's attitudes towards risk?'

With a formal risk tolerance assessment agreed and signed, it is possible to provide ASIC with proof of agreement. When the client accepts a recommendation, the documentation should always include a signed copy for the client file.

Sample case study

Appendix 1 in the sample case study shows the risk profile analysis of the clients using a tool that they completed together.

You have been provided with a single risk profile for the couple as they genuinely agreed on all of the answers to the questions.

Have a look at the responses that the clients gave and the score that they received. Consider what answer would best match them for the first question on page 41 (they did not answer this question) and recalculate their score.

Identify the risk profile category into which the clients fit, based on this score.

Note: You can access this resource at KapLearn.

Profiling couples

When interviewing a couple, a financial planner will require the risk profile of each member of the couple. This is because each member may have different attitudes to risk and be at different stages of their investment time horizon. Both parties must be comfortable with their risk profiles. Even if there are small differences between risk profiles, these need to be accounted for in the overall risk profiling and in the recommended strategy. If risk profiles differ greatly, split portfolios may be the answer.

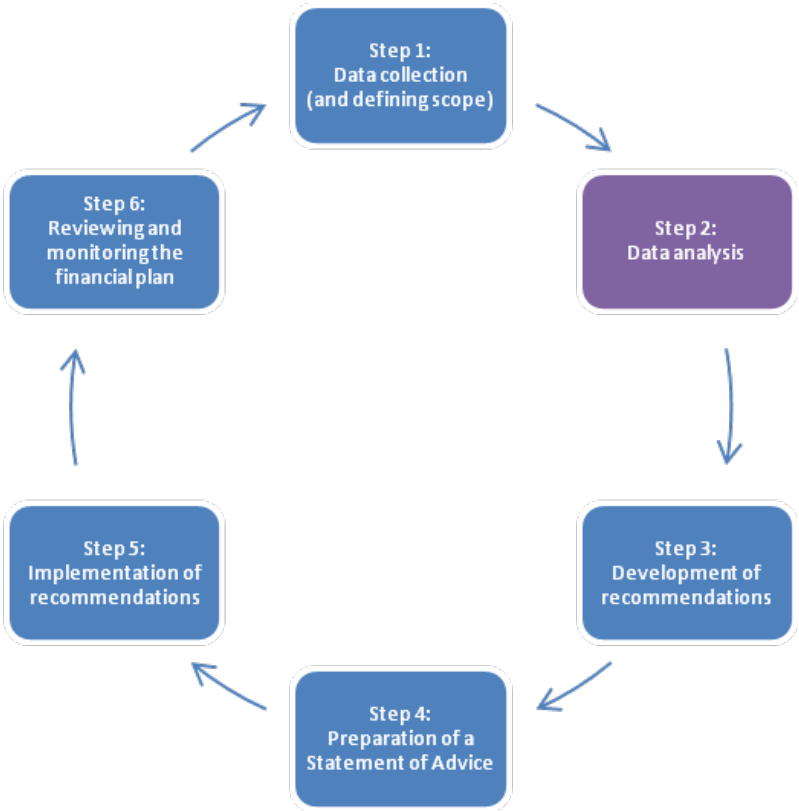
5.8 Closing the initial interview

There are several steps which should be taken before closing the fact-finding interview, assuming that there is an identified need for advice. The planner should:

- Provide an opportunity for the client to supply any additional information that may have an impact on the development of recommendations. Establish time frames and priorities for any requested information.
- Reassure the client that the information collected will be treated with confidentiality and stored in adherence with privacy legislation.
- Summarise the key client goals and objectives and explain to the client where they feel that they can add value by providing advice. It is generally not a good idea to provide details of the actual strategies they intend to recommend but it may be useful to explain some of the strategies that they will consider as part of your development of recommendations.
- Explain to the client what they can expect from the next stage of the process; that is, that the planner will consider the information that they obtained from the meeting to come up with the most appropriate recommendations for the client. They will then document those recommendations in an SOA, which they will then provide to the client for their review and, ideally, acceptance.

- Supply the client with some basic marketing material that gives background information about the planner and their company (optional, and only relevant if it adds information not already included in the FSG).
- Inform the client about any areas for which the planner cannot give advice or where specialised assistance may be required (e.g. estate planning, stockbroking or business taxation). Referrals to specific parties may be provided as part of the service, being certain to disclose any benefit that might accrue to the planner as a consequence of the referral.
- Obtain the client's authority to proceed to the next stage of the financial planning process and their acceptance of any fee that may be applicable for the preparation of this advice.
- Make a follow-up appointment to present the SOA to the client.

6 Data analysis



As part of the new best interests obligation under the Corporations Act, the financial planner must study the information gathered from the client with a view to developing appropriate recommendations.

The financial planner needs to analyse this information and understand the client's financial situation before recommending strategies for the client. The client's financial situation can be determined from budgets, cash flow and net worth. These statements, used in combination, will give a complete 'snapshot' of a client's financial situation.

By the end of the data collecting and analysis stages, the planner should have:

- determined the scope of the advice required, including what the client is trying to achieve for short-, medium- and long-term goals
- assessed the client's financial strengths and resources
- decided which objectives are achievable
- analysed the potential of existing assets
- identified available sources of finance that can be used to achieve the client's goals
- gained a good understanding of the client's attitudes towards risk.

Data analysis can be classified under the following 11 general headings, which are explained in Table 5:

1. Review the fact-finding stage
2. Current position
3. Determine debt management requirements
4. Determine risk protection requirements
5. Determine savings requirements
6. Determine investment requirements
7. Consider retirement funding
8. Plan retirement income stream
9. Review social security entitlements
10. Plan taxation strategies
11. Consider estate planning issues.

Table 5 Data analysis

1. Review the fact-finding stage	The fact finder is the base document from which the planner develops recommendations. It is imperative that the information is comprehensive and correct: • Is the information complete? • Are the objectives logical and achievable in a general sense? If not, what adjustments might need to be made? • Will the plan being formulated suit the client's particular risk profile? If not, seek alternative strategies.
2. Current position	To prepare a plan to achieve client objectives, it is necessary to know where clients are starting from. In analysing the client's current position, the planner should: • prepare a statement showing the client's net worth. Both assets and liabilities should be categorised as personal/lifestyle or investment • prepare a statement showing the income earned (from all sources) and expenses incurred, categorised as fixed, variable and discretionary.
3. Determine debt management requirements	Many clients have existing debt. It is important to examine: • the level of debts carried • the types of debts held • whether it is appropriate to reduce, restructure and/or consolidate these debts.
4. Determine risk protection requirements	Clients should be made aware of their exposure to unforeseen changes of circumstances brought about by loss of income, ill health, loss of, or damage to, assets and even loss of life. Where appropriate, the planner may arrange insurance cover. As well as insurance cover, the planner needs to ensure that funds are available for any emergency that may arise. The range of risk exposure changes as the client enters different life stages.
5. Determine savings requirements	Projecting how much money will be available to meet objectives is an essential part of financial planning. This may involve producing a projection of superannuation needs for the future or creating a plan to meet a more short-term goal, or both. During the analysis stage, a projection will illustrate if, and how, a desired outcome may be achieved. After examining spending habits or ALC during the fact-finding stage, the planner can determine the client's annual savings capacity (net income *less* ALC). A savings requirements projection should look ahead to factor in any predictable expenses, changes in income, or future windfalls that may occur, as well taking inflation into account.
6. Determine investment requirements	Financial objectives may be achieved via a range of strategies; for example, saving, or by purchasing assets, such as property or shares, either directly or through a managed fund. The basic aim is to increase the value of the investments over time. The investments and methods by which income and growth in capital value are achieved will vary from plan to plan according to the client's financial situation, objectives, investment preferences and risk tolerance but, whatever the method chosen, the basic goal remains the same. It is also important to consider the client's need for liquidity, flexibility and security when selecting investments.
7. Consider retirement funding	A comprehensive financial plan will include a projection outlining how a client's retirement income requirements will be met. Individuals can expect to live longer than members of earlier generations and yet, at the same time, there is an ever-decreasing pool of government funds available to provide support for the retired. Consequently, a careful analysis of the most suitable strategy for funding retirement is essential. Maximum advantage ought to be taken of the favourable taxation treatment of superannuation; however, because superannuation is a heavily regulated long-term investment, it is prudent to use other investments as well to provide flexibility.
8. Plan retirement income stream	Whether the client is retired or not, the planner must take into account their requirements for a future stream of income. There must be a close correlation between investment choices, projected product performance and the likely needs of the client within the projected time frame.

9. Review social security entitlements	There will often be clients who qualify for some sort of social security support, or who may do so in the future. Careful analysis of income and assets will put the planner in a position to structure the recommendation to ensure they do not negate any current or potential social security benefits.
10. Plan taxation strategies	It is important for clients' financial affairs to be structured in the most tax-effective way possible. Although individuals should pay the tax for which they are liable (tax evasion is a crime), tax minimisation is often possible via an appropriate strategy that is both legal and ethical, such as the use of investment products with particular tax advantages, income splitting and negative gearing. However, tax effectiveness should not be the primary reason for selecting an investment. Planners should always refer clients to taxation professionals for confirmation of all taxation matters.
11. Consider estate planning issues	Accumulation of assets brings with it concerns about their preservation and distribution after death. In creating a financial plan, the planner must work with the client to determine: • total assets likely to be owned by the client in the future • probable future distribution of assets • estate implications of premature death • existence of enduring powers of attorney and wills • appropriateness of any financial structures in the event of the client's death. Referral to estate planning professionals for assistance in any of the above matters may be warranted.

6.1 Assessing the current budget

A budget identifies the various sources of a client's income and expenditure. The number of income and expense items will generally increase as the client accumulates assets and debts and as their personal and family commitments change. The client's financial situation will become more complex as they move through life until they reach retirement, which is when simplification usually occurs.

The starting point when analysing a client's financial situation is their current budget. The budget will determine day-to-day money management and spending patterns. This will enable the client and the financial planner to not only determine where money is spent but also identify fixed and discretionary spending.

A budget focuses on the specific detail of the client's income and expenditure, (e.g. groceries, insurance and car maintenance).

It is best to prepare the budget for each month, as income is normally received fortnightly or monthly and many bills are incurred monthly. When monthly budgets have been prepared, these can then be combined into an annual budget. Monthly budgets allow the financial planner to mark the months in which expenses may exceed income or vice versa and determine where short-term planning is required.

Estimating income

The financial planner needs to ensure that the client has made a reasonable assessment of their income. Many clients will know their pre-tax income and many will also know what they receive into their bank account from their employer. It is important that the after-tax income is used by the planner when talking about the net position of the client. The calculation of after-tax income is described in detail in Topic 4.

Income should only be included if it is certain. If a client receives a bonus for achieving a certain level of sales or a certain performance, this should only be included when the sales or performance has been achieved. The inclusion of money which is based on special circumstances can lead to problems if it is not received as expected.

Estimating expenses

The next step in the budget process is determining expenses that are likely to be incurred. This should be on the basis of expenses incurred in the previous year or based on known actual expenses for the coming year.

Expenses can be divided into:

- **fixed expenses** — generally predetermined and usually set by a contract or agreement (e.g. mortgage repayments, loan repayments, insurance premiums, etc.)
- **variable expenses** — where the amounts may change depending on the time of the year (e.g. food, clothing, utilities, medical expenses, etc.).

The financial planner should ensure that expenses factor in increases in living costs and prices. In addition, expenses should also include any planned savings or investments.

Finalising and reviewing the budget

When the monthly budgets and the annual budget have been prepared, the financial planner should compare budgeted income with budgeted expenses on both a monthly and an annual basis and note the variances between the two time frames.

If the overall annual budget is in deficit then the financial planner needs to look at ways to balance the budget. In most cases, such deficits may not be obvious until the annual cash flow is generated, at which stage budget details may need to be reviewed.

Some solutions to an annual budget deficit are:

- Reduce expenditure in lower priority areas so that assets and wealth are maintained.
- The client should identify those expenses which are needs, such as housing, food and clothing, and those that are wants (i.e. items that are nice to have but can wait).
- Increase income through overtime, a second job, a higher paying job or another financial venture.
- Borrow money or liquidate savings or investments to fund the shortfall. This is generally not recommended as it not good budgeting practice and reduces future worth.

ASIC's consumer website, MoneySmart, has several financial calculators, including a budget planner. It can be accessed at <www.moneysmart.gov.au>.

Budgeting information can also be found on the ASIC website, which is accessible at <www.asic.gov.au>.

Apply your knowledge 13: Prepare a budget

Using the budget calculator located on the MoneySmart website at <www.moneysmart.gov.au> → Tools & resources → Calculators & Tools → Budget planner, prepare a budget based on your personal circumstances and review the budget to see if there are any areas in which it could be improved (viewed 24 April 2014).

Note: The answer will be specific to your personal circumstances.

6.2 Preparing a cash flow statement

A cash flow statement, also known as an income and expenditure statement, provides the client with an assessment of their financial activities that have occurred over a period of time, commonly one year. The cash flow statement enables the client to establish the amount of saving and investment that has occurred and allows for comparison with financial goals.

When the financial planner has completed a monthly budget, preparing a cash flow statement is relatively easy. The components of a cash flow statement are income, expenditure and cash surplus or deficit. The main differences between a cash flow statement and a budget are that the cash flow statement is usually completed on an annual basis and will group expenses together.

In order to prepare an effective cash flow statement, the client must be able to accurately identify their income and expenses, which is done when creating the budget. This will enable the financial planner to make a detailed analysis of the client's financial situation and recommend appropriate strategies.

Table 6 is a sample cash flow statement.

Table 6 Cash flow statement

Tax calculations			
	Client 1	**Client 2**	**Notes**
Income from employment			
Salary			
Salary sacrifice			(state % if applicable)
Salary after salary sacrifice			
Other income			
Bank account interest			(state % return if applicable)
Interest from other investments			(state % return if applicable)
Share dividends			(state % return if applicable
Imputation credits			(state % return if applicable
Other income liable for tax (e.g. rental income)			
Assessable capital gains			

Total assessable income			
Deductable expenses (e.g. rental repairs)			
Taxable income			
Income tax on taxable income			**(state tax rates and year applied)**
less tax offsets (e.g. Low Income Tax Offset)			
plus Medicare levy			
plus Medicare levy surcharge			
less imputation credits			
less refundable tax offsets			
Net tax payable			

Cash flow calculation				
Family cash flow				
	Client 1	**Client 2**	**Combined**	**Comment**
Salary *less* any salary sacrificed amount				
Non-taxable income (e.g. income from a superannuation pension for a person aged over 60, Family tax benefits, etc.)				
Interest income				
Dividends received (excluding franking credits)				
Other income				
Total income received before tax				
Investment expenses				
Living expenses				
Other expenses				
Total expenses				
Total income received before tax *less* expenses				
Net tax payable from tax table above				
Total net cash flow				

The cash flow recorded in Table 6 should be suitably detailed to ensure that all items are accounted for. For each inflow or outflow item, further detail should be provided to clarify the item; for example, the outflow of loans may include a car loan or personal loan. This is to give the client a better comprehension of their income and expenses position.

Determine net position

When all the income and expenditures have been identified, the financial planner can then determine the net position (i.e. the difference between income and expenditure).

Net position is the net result of the financial activity during the period. If income is greater than expenditure then there is a cash surplus, which a financial planner may consider as an opportunity for investments or loan repayments. If expenditure is greater than income then there is a cash deficit, and this may indicate a need for some expenditure restraint.

Although the net result will show either a cash surplus or a cash deficit, the financial planner will need to analyse the result to determine what strategies or actions are required to manage the client's financial situation. In addition to the surplus or deficit, the financial planner needs to review the numbers that make up this result to ensure appropriate advice is given and specific strategies relating to cash flows are identified.

Instructions on how to construct a cash flow statement will be covered in the next topic. Note in the sample case study (section 2, Table 2) that the clients have surplus disposable income, which could be applied to a variety of wealth creation purposes depending on their goals and objectives.

6.3 Net worth statement

A client's net worth is the difference between what they own (i.e. assets) and what they owe (i.e. liabilities). A net worth statement shows a client's financial position at a particular point in time. A net worth statement is often referred to as a 'balance sheet' because it balances what is owned against what is owed and therefore states what the client is worth.

For companies, a balance sheet is usually prepared at the end of the financial year, so that the company can determine its financial position. A client's net worth can be prepared at any time.

The way a financial planner lists the assets will depend on the profile of the client and what the financial planner is trying to establish from the net worth statement. For instance, if the client has a lot of debts then the financial planner may try and match the assets against the payment of the debts.

Calculating net worth

After the assets and liabilities have been determined, the net worth is worked out as the difference between total assets and total liabilities.

Net worth = Total assets – Total liabilities

6.4 Analysing the risk profile

The risk profile of a client needs to be matched against the client's goals and objectives. While the risk profile may indicate that a client is risk averse, this may not be in line with their goals and objectives.

For example, the client may have goals and objectives to accumulate wealth within 10 years, and the only way to do this might be through growth or speculative investments, which are not in line with their risk profile. The financial planner will need to educate the client on risks and determine if the risk profile and/or goals are appropriate. There may be a need to review the risk profile or reassess the goals and objectives.

Sample case study

Appendix 1 in the sample case study shows the risk profile analysis of the clients in the case study using a tool that they completed together.

At this stage as a planner, you should consider the responses that the clients have made in light of the other information in the initial client meeting and the clients' goals and objectives and check that they align. You should check that there is consistency between a profile score and a client's needs, goals and attitudes.

In the case study you will see that the clients have agreed with the planner that they are 'growth' investors.

Note: You can access this resource at KapLearn.

Matching investment products to client risk profile

Once the client's investment risk profile is established and their investment needs and objectives are determined, the financial planner will start the process of matching these attributes with suitable investment products. Although many products will meet the risk profile requirements of the client, investment products need to be closely analysed to ensure that all the safeguards and compliance requirements of these products meet the required regulatory standards.

6.5 Analysing financial goals

The client's financial goals should be reviewed by the financial planner to determine if they are appropriate given the client's financial position, determined from the financial statements. If necessary, new or adjusted financial goals should be developed in conjunction with the client. The financial planner should ensure that the goals do not conflict with each other and, if necessary, be prepared to recommend that sacrifices be made in the short term in order to meet long-term goals.

When assessing client needs, it is important to understand the difference between values, goals and objectives. The financial planner needs to determine what is important about money to their client. People make decisions based on what they value, and goals cannot be separated from values. Therefore the financial planner must take time to know what their client values and what they want to achieve.

If the financial planner establishes what is important to the client and then uses this information to define their desires, the financial planner will understand what is required to achieve their financial goals. Financial goals provide the specific detail required to obtain the objectives. They provide precise information, such as dollar amounts and time frames.

Sample case study

From the sample case study you should be able to identify the key goals that the clients have.

Open the sample case study SOA, and look at the executive summary where you will find the section 'What you would like to achieve'.

The key goals identified in the case study should be listed here.

Check that these do in fact match with those in the sample case study section 1 and the Fact finder in Appendix 1.

Note: You can access this resource at KapLearn.

6.6 Tools for financial analysis

Much of the quantitative information collected has to do with numbers and dollars, both in present and future values. Income needs must be calculated based on projections of income and inflation, as well as other factors (e.g. a volatile economic environment). Income projections for various investment products are needed. Calculations of taxation on all types of income, as well as capital gains tax if applicable, must be made.

Some calculations and projections may be obtained from specialist advisers and product issuers. The licensee may have some form of financial modelling tool, often referred to as financial planning software. Even a standard spreadsheet package on a personal computer can provide adequate analysis.

The key point is that a financial planner must have access to suitable tools to carry out the required level of financial analysis.

By considering the client's current and projected personal circumstances, their present and future income and expenditure requirements, and their risk–return profile, the planner can begin to determine and evaluate strategies that might be appropriate for meeting the needs of the client. The planner also begins to consider which types of products will best meet the client's needs in the implementation of the selected strategies.

If the data analysis is carried out in a logical and sequential manner, then recommended action should become naturally apparent as the process unfolds.

6.7 Seeking more information from the client

At this point, it is important to note that the stages in the advising process are not necessarily distinctly separate, and that the direction of the communication and information flow is not necessarily one way. The client and the planner will have to take the time to work together to gather the required information and communicate this to each other.

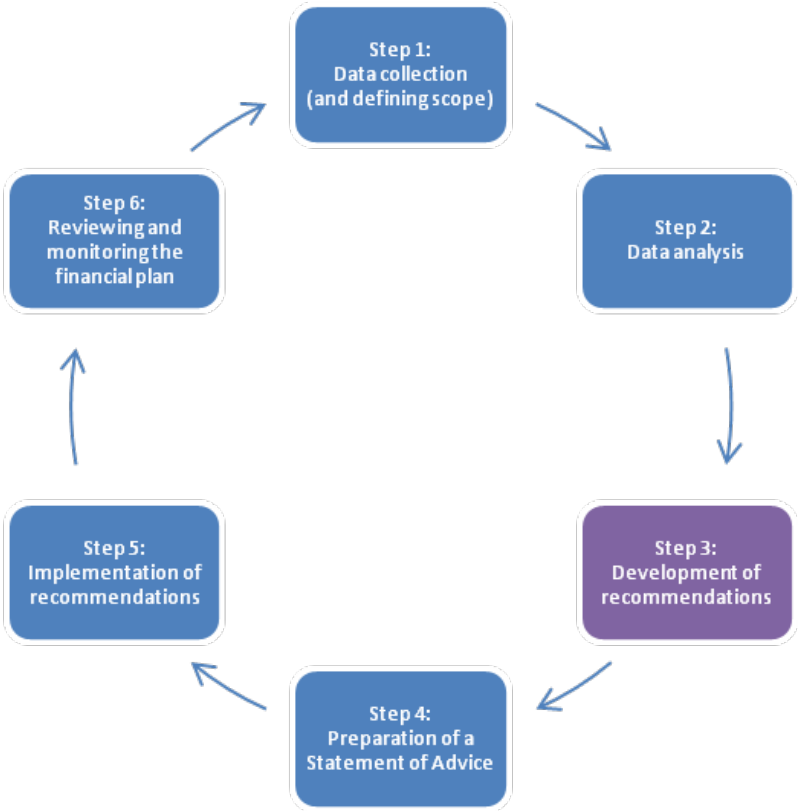
For example, there will be questions asked by the planner during the initial fact finding that the client will have to go back to find additional information to answer.

There will also be times, during analysis, when a planner realises they need to ask more questions. Possible gaps to be filled can include:

- confirming the client's decision about conflicting priorities
- timing uncertainty
- quantifying an amount
- an estate planning question.

When these situations arise, the advising process develops an internal feedback loop. This situation can arise at any stage of the process. Follow-up questions to the client should not cause concern or embarrassment. Rather, they are a sign of the thorough way in which the planner approaches the job. It will cause less distress to fill gaps by asking questions as soon as they arise than to wait until later in the process.

7 Development of recommendations



Following a detailed analysis of the information collected, the financial planner will be well equipped to think about formulating appropriate solutions and strategies and incorporating these into a series of recommendations for the client.

The recommended strategies should incorporate:

- the client's short-, medium- and long-term needs and objectives
- the client's risk profile, including whether the planner feels it is possible for the client to achieve their goals if they invest following their risk profile. If this is not possible, then the difference between their risk profile and desired return will need to be discussed
- recommended solutions for the client's needs and objectives to be achieved, highlighting where the planner feels that these are unrealistic or under ambitious.

Although a recommended strategy or strategies will be provided to the client, they make the final decision to accept or reject a strategy. Therefore, the strategy must be clearly communicated to the client.

The key areas to be addressed in strategy development reflect the data analysis process and the client's needs and objectives. They are:

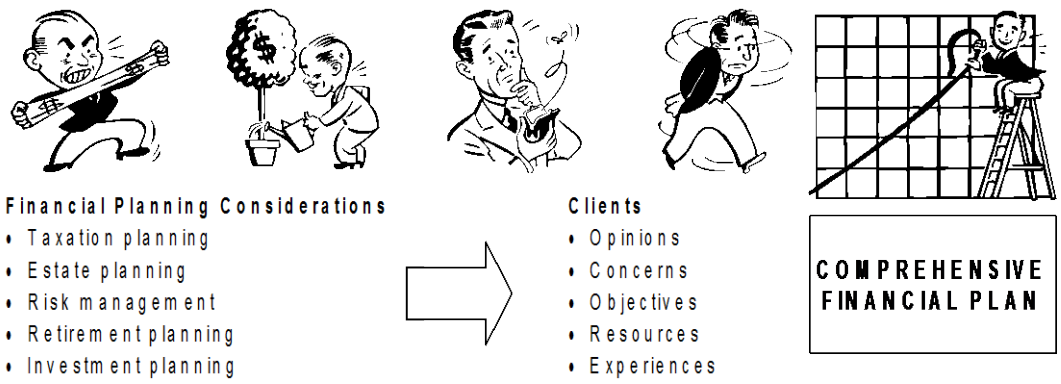
- debt management
- risk management, including general insurance cover
- savings capacity
- wealth accumulation (investment) — and the appropriate investments to implement the strategy, such as shares, property and unit trusts
- funds for retirement — investments inside and/or outside superannuation
- income generation in retirement — potentially including the use of annuities and pensions
- social security considerations
- taxation considerations
- protection of beneficiaries — life insurances, estate planning and wills.

The development of a recommendation is the bringing together of detailed analysis, an empathic understanding of the client's opinions and concerns and a thorough understanding of which investments or financial products are available to meet the client's objectives and are within the adviser's authority to provide advice on.

Essentially, the goal is to use the client's resources in the most effective manner to allow them to achieve as many of their objectives as possible. This may be about better management of their expenses, including debt, better or different use of their assets, or improvement of their net income position through tax reduction.

The combination of these factors leads to a tailored recommendation for the client that will withstand the scrutiny of a compliance audit. The main areas that should be considered by the planner are shown in Figure 7.

Figure 7 Putting the pieces together



7.1 Considering issues external to the client

When developing strategies, financial planners need to be conscious of the factors external to the client's personal situation that may have an impact on their financial outcomes. These include macro-economic issues, such as broad trends in the economic environment, interest rates, inflation and unemployment.

There are also various regulatory issues that planners need to comply with when providing advice to clients. In addition to the regulations imposed on planners, other policies and legislation implemented by governments can dramatically affect the strategic development of a client's financial plan.

Federal budget decisions may affect the financial planning strategy of a client. These might include tax cuts and changes to the tax system, superannuation or the treatment of certain assets or income in relation to social security.

For example, consecutive federal budgets have announced significant changes to the superannuation regime. These changes mean that planners have to review the strategies they have developed for many of their clients and reassess whether they are still appropriate.

It is essential that planners keep abreast of these issues and develop or modify their clients' financial planning strategies accordingly.

7.2 Developing strategies

The starting point for developing strategies should be to look at the clients' goals in terms of priority and try to develop strategies by focusing on the most important goals first. Often, a strategy will have an impact on other strategies, and it is therefore important that the highest priority is attended to first, and a number of options may need to be considered, tested and then accepted or rejected. The most appropriate combination of strategies for the client is then put together to provide the overall recommendations.

The data analysis phase should have provided you with a good understanding of the available resources that the client has, their tax position and their attitudes towards investing. Optimisation of the available resources towards the achievement of goals can then be undertaken.

This approach to finding the best solutions is also the best way to present the strategy to the client in the SOA: explain the goal you are aiming to achieve, and then how your strategy either meets or helps to meet that goal, with calculations, charts, etc. to support your recommendation as needed.

The following case studies illustrate the strategy development process.

Case study 1:

Samara met with her financial planner and explained that she wanted to:

- pay off her home loan as soon as possible
- protect her income in the event of something happening to her
- increase her savings for a $10,000 holiday in five years' time.

The planner worked with Samara to determine that her order of priority for the three goals is the same as the order above. The planner conducted a full needs analysis and a risk assessment for Samara.

Samara has a mortgage of $150,000, with variable interest of 6.5% and current minimum monthly repayments of $950. Samara is making the minimum repayments.

The financial planner has calculated that Samara has an extra $1000 per month that could be used for either savings or investing. This represents 90% of her current disposable income after all her expenses, and the planner believes it is wise to leave a buffer of 10% in case extra expenses crop up or her budget is not completely accurate.

The planner now has to do the following to consider the best options for Samara:

- Consider how fast the loan could be repaid using all of this excess income.
- Work out how much interest this would save Samara.
- Compare the saving in interest with the alternative of investing the funds.
- Consider how this strategy will affect her ability to protect her income: how will premiums be paid?
- Decide if a balance between paying down the loan and saving for the holiday is a better option.

In order to meet Samara's objectives, the planner decides that focusing on clearing her loan is in the best interest of the client.

To protect Samara's income objective, the planner decides that an income protection policy should be used. This can be owned partially or totally inside superannuation to reduce the impact on her cash flow, and Samara's redraw facility attached to her mortgage can be used to fund her holiday.

The planner calculates that, in five years time, Samara's loan will have reduced to just below $70,000. If she continued this way without spending for the holiday, she would clear her loan in just under nine years and she will have saved over $140,000 in interest.

In this way the planner has considered all of her goals, in order of priority and made strategy recommendations that help to meet all these goals.

Note: There are many online calculators that you can use to check this value. One is provided by Citibank at <http://www.citibank.com.au> → Home Loans → Home Loans Overview → Calculators and Tools → Extra Repayment Calculator (viewed 2 December 2013).

Case study 2:

Luis, age 55, wants to retire or reduce his working hours as soon as possible. Luis has $650,000 in his superannuation fund, currently earns $65,000 p.a. plus superannuation guarantee, and his current expenses are about $45,000 p.a. He usually waits until after he has completed his tax return to make a contribution to superannuation of any leftover money, and averages about $4000 p.a.

Luis has told his planner that he wants to have $40,000 p.a. after tax. Luis has no dependants and he is not interested in discussing insurance. His goals are all related to his impending retirement; he does not believe that he will have any major capital expenses any time soon and is just focused on income generation to last him for his retirement. He would not be prepared to retire on any less income. Luis has said that he believes he would only take social security benefits if he had no other way of supporting himself.

The planner talks to Luis about the possibility of working less now and delaying his full retirement for a few years in order to enable him to be truly self-sufficient in retirement. Luis is agreeable to the concept, but would only work if it was required to reach his goals. The planner also spoke to him about how comfortable he would be in taking on additional risk to meet the goal. Luis said he would rather work longer than take on too much risk. His risk profile came out as 'balanced'.

In order to meet Luis's objective, the planner needs to consider the following questions:

- How long will Luis's current savings be able to provide him with his desired income, or how much income can he generate now, based on his superannuation and life expectancy?
- How much more money does he need to have?
- How much longer will he have to work full-time or part-time?
- Will a 'transition to retirement' strategy work for him? Will the improved tax efficiency help him to achieve his goal earlier or would full-time work and salary sacrificing alone be better for him?
- Will he have to take on more risk anyway, because he cannot reach his goals any other way or can he reduce his spending now, to increase his savings capacity?

The planner calculates that if Luis retired today, he could generate approximately $32,000 p.a. until his life expectancy is reached. Given his priority is to have $40,000 p.a., he has to increase his savings or retire later. The planner then looks at the best ways to increase Luis's savings to meet his goal, and found that salary sacrificing will help him to put more into his superannuation fund each year without compromising his current lifestyle, through more efficient taxation. He also determines that, by working until he is 60, Luis will be able to meet his goal without taking any additional risk.

Note: There are many online calculators that you can use to check this value. One is provided by ASIC at <https://www.moneysmart.gov.au> → Tools & resources → Retirement planner (viewed 2 December 2013).

7.3 Summarising the strategy

Once all the strategy development factors have been considered, the planner should be able to provide a summary of how the strategy will move the clients in the direction they want to go.

This summary takes the form of a strategy statement. The focus of the strategy statement will change depending on which of the two basic life stages the client is at:

1. **The accumulation stage:** Where the strategy statement will focus on wealth accumulation and tax management.
2. **The drawdown stage:** Where the focus is on wealth preservation and management of income.

An example strategy statement for Luis in 'Case study 2' (who is a client in the accumulation stage) is:

'Understanding that your goals are early retirement and a desire to be self-funded for as long as possible, the strategy I am recommending seeks to increase your savings through superannuation and to reduce the tax you are paying on your current income. My strategy will help you to reach your desired income of $40,000 p.a. by the time are 60 years old.'

Sample case study

From the goals identified in the sample case study you should now be able to find strategies to address these goals in the SOA.

Open the sample case study SOA, and look at the executive summary where you will find the section 'Summary of our recommendations'.

The key goals identified in the case study should have strategies listed here to address them.

Check that these do in fact match with those in the sample case study section 1 and the Fact finder in Appendix 1.

Note: You can access this resource at KapLearn.

7.4 Investment strategy and portfolio construction

After the appropriate strategies have been developed for the client, it is likely that some recommendations will involve the investment of money into a product, or the movement of one investment to another. This is typically the case when a client is looking to accumulate wealth for some goal or objective.

The financial planner's first step in the process of deciding which investments to recommend is to consider the goal that they are aiming to achieve and the type of growth or income mix that is needed to achieve that goal. The planner should then analyse how the asset should be owned: inside superannuation, by the client, their spouse or both directly, or by a trust, etc. For example, if the client is in need of income and they are under their preservation age, it would be unwise to invest all of their money in superannuation. If, in this same scenario, they are a couple, investing in the person with the lowest income may mean a higher after-tax return can be achieved. All of these need to be considered when determining the investment strategy.

It may be appropriate, if the client's risk profile is suitable, to recommend gearing. However, gearing is a relatively high-risk strategy that requires a client who can invest for the longer term and who has a desire for, or need of, this level of risk.

The planner will then recommend what is referred to as an 'asset allocation' for the investment portfolio. This is the process of deciding into which market segments the client's funds should be invested (e.g. shares, fixed interest and property) and in what proportions. The planner may need to make a trade-off between the client's desired risk and return, and their objectives. The asset allocation must be in line with at least one of these: either asset allocation matching their risk profile or, if different from the risk profile, the asset allocation needed to achieve a client's goal. This deviation from their risk profile needs to be clearly explained to the client, and their agreement must be obtained.

Finally, the particular product type and, where appropriate, providers are selected. The decision as to whether direct investments or managed investments are better suited to the client should be made clear. Appropriate research should be made by the planner before deciding on the specific investments for the client. This is covered in section 7.5, in which the product selection process is expanded upon.

This process can be summarised as:

- **investment strategy** — how to achieve the desired income/capital growth mix (e.g. ownership, considering superannuation versus non-superannuation, personal, joint or trust).
- **portfolio** — matching the clients' market exposure with their risk profile and goals (e.g. determining the right allocation of assets, such as shares, property, fixed interest and cash).
- **investment product type** — direct or managed.

For most clients, it is important that there is a spread of investments across the various asset classes, as well as a spread among various institutions or managers. The aim of such diversification is to try and protect the client from legislative changes or negative returns from a particular asset class, company or product.

It is important the planner builds a portfolio that:

- meets the client's financial goals and objectives over the agreed time horizon
- is diversified
- manages risk to the client
- is flexible
- provides for capital growth or income as required
- is tax effective.

The recommendations should incorporate a statement of income and any capital growth projections, together with specific reasons as to why selected strategies have been put forward.

Before a plan is recommended to a client, the planner should take every precaution to explore all viable strategic options and alternatives.

This process includes researching the product providers. The Corporations Act provides an explanation of what a reasonable investigation is:

(1) A **reasonable investigation** *into the financial products that might achieve those of the objectives and meet those of the needs of the client that would reasonably be considered relevant to advice on the subject matter sought by the client does not require an investigation into every financial product available.*

(2) However, if the client requests the provider to consider a specified financial product, a reasonable investigation into the financial products that might achieve those of the objectives and meet those of the needs of the client that would reasonably be considered relevant to advice on the subject matter sought by the client includes an investigation into that financial product.

(section 961D Corporations Act 2001)

7.5 Selecting appropriate products

Once the recommended strategy is document in the SOA, appropriate products will need to be identified to implement the strategy, where applicable. This may involve reference to the licensee's approved product list (APL) and/or the planner conducting separate research.

Licensee APLs

Licensees often provide their financial planners with an APL. These lists may have been developed in-house or purchased from an external provider. They contain products that have met certain criteria determined by the licensee or the external providers. An APL can be very comprehensive, limited to the licensee's own products, or somewhere in-between.

However, ASIC believes that a financial planner, as the providing entity, should understand the subject matter of the advice (i.e. 'know your product'). Where the planner is relying on external research, they should ensure that the information is accurate, complete, reliable and up to date. Extreme care should be taken when recommending complex or non-standard products to clients, even if the products appear on the licensee's APL.

The regulatory requirements

The Corporations Act states the 'providing entity', which includes financial planners, licensees and their representatives, needs to ensure that any advice provided to a retail client is appropriate, having taken into account all relevant information about the client and having undertaken reasonable investigation into the financial products that might achieve the client's objectives.

This was often referred to as the 'suitability rule', and it can be broken down further into 'knowing your client' and 'knowing your product'. This has now been replaced by the best interests obligation.

> *It would reasonably be regarded as in the best interests of the client to take a step, if a person with a reasonable level of expertise in the subject matter of the advice that has been sought by the client, exercising care and objectively assessing the client's relevant circumstances, would regard it as in the best interests of the client, given the client's relevant circumstances, to take that step.*

As explained in Topic 1, RG 175 provides details on what is appropriate in terms of meeting the best interest obligations.

RG 175 includes the obligation to 'conduct a reasonable investigation into the financial products that might achieve the objectives and meet the needs of the client that would reasonably be considered relevant to advice on that subject matter; and to assess the information gathered in the investigation.'

Under the current RG 175 (October 2013), the providing entity must:

- make reasonable inquiries about the client's relevant circumstances
- reasonably consider and investigate the subject matter of the advice
- ensure the advice is appropriate to the client.

ASIC considers advice will be appropriate if it satisfies the client's 'relevant circumstances'.

In addition to the legal obligations, the FPA's Code of Professional Practice state planners must understand the products, financial planning strategy or strategies they are recommending (rules 4.6 to 4.10 outline the specific obligations when recommending a financial product).

For example, rule 4.6 states 'a member must not recommend a product or service unless the member understands its characteristics, risks and key features'. This is in addition to 4.11(d), which states that planners need to outline 'the reasonably foreseeable risks and consequences of each recommendation' to their clients.

In order to meet these obligations, planners need to research the products they are recommending to clients and satisfy themselves that the product will perform in line with their expectations.

7.6 Researching products

There are many products that planners can recommend to clients. Research houses play an important part in providing planners with independent qualitative and quantitative information to help them understand how these products function and whether they might be suitable for clients.

In order to recommend products that best match the client's needs, in addition to meeting the legislative requirements of the Corporations Act, it may be necessary for planners to look outside the approved lists and conduct their own research to demonstrate compliance.

Consider

The introduction of the best interests duty in the Corporations Act reforms raises an interesting question for licensees that use an APL.

Firstly, a planner may not be able to recommend a product if it is not approved by their licensee and on their list. Licensees may have to change this rule in light of the new regulation. Accordingly, they will need to ensure that the planners are correctly and thoroughly researching products, and that they have a procedure in place for approving products not on their APL.

Secondly, many professional indemnity insurers of financial planners require that recommended products have an investment grade rating. This is an important consideration for both planners and the licensee.

Lastly, if there is a product or an investment that is not available on the APL but may be suitable for a client, a planner may be required to look outside of the APL to meet the best interests duty in the Corporations Act. How will the planner manage this?

Planners' own research

It is essential that planners conduct their own research to understand how a product performs in different market conditions.

Monthly updates, media and market commentary also play an important part in keeping up to date on any changes that might affect products.

Planners may also attend specialist training provided through their licensee and should ensure they read any updates provided by fund managers, particularly if they lead to a new investment style or change of management.

Where products are new or particularly complex, such as structured products, planners may need to seek extra information and do their best to ensure the information they have is up to date.

Financial product information is available from a variety of sources. Online publications provide an efficient means of searching for information and obtaining up-to-date data.

Many licensees provide their own websites to gather critical information and tools into a single site for the convenience of planners.

The major sources of information include:

- financial media, including newspapers and financial and investment magazines
- annual reports
- brokerage firms
- research providers
- in-house research
- investment information/advisory services
- government publications
- computerised investment information and tools.

Doing the right research

Financial planning is a complex business. In addition to understanding the world of investments, superannuation and social security, planners have a range of legal obligations and professional standards to adhere to.

There is no shortcut for understanding a client's needs, and planners must spend time listening to their clients and completing a fact finder.

However, when it comes to researching products, planners can rely on numerous sources to inform them of how specific investments are expected to perform in different market conditions.

Although they can outsource some of the research, they cannot outsource the responsibility for understanding how this product will have an impact on clients.

As a result, it is important to examine the role of research houses in producing reports on products and how planners can use this information while upholding their obligations towards their clients.

Independent research houses

Independent research houses are the main source of research on managed investments for a licensee and their planners. They play an essential part in the financial system through providing third-party analysis of products.

Research houses provide extensive qualitative and quantitative information across the broad spectrum of managed fund investments, as well as research on direct equities, exchange traded funds and alternative investments.

Some of the major research providers for product information in Australia include:

- Lonsec
- Standard & Poor's (S&P)
- Van Eyk
- Morningstar
- Mercer
- Zenith Investment Partners.

Each of these rating agencies will have their own approach to investigating and measuring fund managers and fund performance.

Example

S&P's approach to fund ratings is 100% qualitative. It involves interview-based research, analysis and the application of professional expertise to provide an understanding beyond the data alone.

S&P fund ratings are awarded on a scale of one (low) to five (high) stars, with additional 'on hold' and 'sell' categories. A star rating is a forward-looking qualitative assessment of a manager's ability to generate consistently superior risk-adjusted fund returns, net of fees relative to relevant investment objectives and peers.

The S&P system for rating managed funds is outlined in Table 7.

Table 7 Standard & Poor's fund ratings definitions

★★★★★	Standard & Poor's has a very high conviction that the manager will consistently generate risk-adjusted returns in excess of relevant investment objectives and relative to peers.
★★★★	Standard & Poor's has high conviction that the manager will consistently generate risk-adjusted fund returns in excess of relevant investment objectives and relative to peers.
★★★	Standard & Poor's has conviction that the manager can generate risk-adjusted fund returns in excess of relevant investment objectives and relative to peers.
★★	Standard & Poor's has conviction that the manager will not generate risk-adjusted fund returns in excess of relevant investment objectives and relative to peers.
★	Standard & Poor's has high conviction that the manager will not generate risk-adjusted returns in line with relevant investment objectives and relative to peers.
ON HOLD	Issues potentially affecting the management of the fund have emerged, and the fund rating is temporarily suspended, pending clarification.
SELL	A manager with significant issues that have the potential to adversely impact performance. Existing investors should consider obtaining advice regarding switching or redemption.
Fund-Rating Subscript	
–NEW–	Where the investment process, fund manager or analytical team has changed significantly, or where the fund has a relatively short history, but a relevant and demonstrable track record can be shown on similar funds.

Source: Standard & Poor's 2007

Internal research team

In addition to information provided by independent houses, most licensees will supplement this with their own internal product research team. This helps fill in the gaps from external research and to tailor information to suit their target market.

Information provided by external providers can focus heavily on products. Internal research teams play a crucial role in digesting this information and packaging it in a way that is useful for planners and clients.

7.7 Research reports

Conducting research and establishing ratings is an intensive process. These are generally completed on an annual basis for every sector, with monthly and quarterly updates issued to reflect intra-cycle changes.

Some research houses have incorporated a qualitative component which looks at the risks of using a product. This may include an assessment of the corporate risk or the risks that are unique to the individual product or sector.

Assessing corporate risk involves meeting those involved in managing the products and gaining a sense of the team, experience and views on risk management. This is particularly important given the number of boutique fund managers that may only have a single product on offer.

Product risk involves looking at aspects such as leverage, counterparty and liquidity in the product, as well as any challenges for the sector in future.

As research houses produce reports on a huge range of products, from equities to more complex fixed interest products and structured products, they must consider the need to tailor the research to suit the complexity of the investment.

Once all the information has been collected, a research house will undertake an internal review process to scrutinise decisions and discuss strengths and weaknesses before making a final assessment on the rating. This is an important time to play 'devil's advocate' and discuss what is being proposed.

Reading a research report

Research reports are crucial for helping planners develop their understanding of different products. However, it is equally important to understand their limitations.

For instance, although a product may be rated well, it might not be suitable for clients with a low risk tolerance.

Where quantitative data are used to show historical returns, planners must also be aware that this does not necessarily indicate how a product will perform in the future. It can also disguise volatility through the use of headline returns rather than risk-adjusted returns.

When comparing information across different products, planners also need to ensure they are making valid comparisons.

7.8 Credit rating agencies

The Australian credit rating agency (CRA) market is almost entirely made up of three major global CRAs:

- Moody's Investor Service Pty Ltd (commonly known as Moody's)
- Standard & Poor's (Australia) Pty Ltd (S&P)
- Fitch Australia Pty Ltd (Fitch)

Many fund managers in Australia use S&P, as it has a long history as a domestic ratings agency.

Credit ratings agencies provide an estimate of the credit worthiness of the company or entity that has issued the debt. These ratings are not to be confused with the managed fund manager research ratings discussed previously.

Credit ratings agencies generally provide ratings for issuers of certain types of debt obligations as well as the debt instruments themselves. The issuers include companies, state and local governments, not-for-profit organisations and national governments issuing debt-like securities (i.e. bonds).

The rating is an evaluation made by a CRA of a borrower's ability to repay its debt. A poor credit rating typically indicates a higher risk of an entity defaulting on its borrowings and thus typically should attract a higher interest rate to compensate for this risk.

Credit ratings are either long term (i.e. obligations with a term of more than one year) or short term (i.e. with an original maturity of 365 days or fewer).

Long-term ratings are often reported in the media in relation to national and state debt in particular, and range from 'AAA' as the highest rating to 'D', for 'default', as the lowest. Short-term debt is rated from 'a-1' at the top end to 'd', for 'default', at the bottom end.

A user pays model

ASIC proposed a user pays model for research into managed investments in response to the failure of CRAs during the global financial crisis.

Most research houses currently use a combination of issuer pays (i.e. fund managers pay a fee to be rated) and subscription-based business models. However, there are a range of models on the market.

Note: There have been several major reviews and regulatory changes in response to the role of CRAs in the global financial crisis.

These include revisions to the 2004 International Organization of Securities Commissions (IOSCO) Code, U.S. Securities and Exchange Commission (SEC) draft rule proposals and a European Commission draft directive.

7.9 How much research is enough?

Research houses and ratings agencies provide an efficient way of screening financial products. However, planners must ensure they do enough independent research to satisfy the best interest and other related obligations.

The current ASIC RG 175 states that the providing entity is responsible for investigating the financial products, classes of financial product and strategies on which advice is provided to the client.

In certain circumstances, they can rely on information from external research houses. However, planners must take their own 'reasonable steps' to ensure research is accurate, complete, reliable and up to date.

ASIC currently does not consider that the Corporations Act requires detailed investigation of products they are not authorised to advise on. However, planners will need to have general knowledge about products' classes and strategies that are commonly available to ensure their advice is appropriate.

Under the new best interest duty in the Corporations Act, the interpretation of what is considered a 'reasonable investigation' is the new test by which planners will be measured.

The following example shows the consequences of failing to conduct adequate research as illustrated by the FOS decision on Basis Capital.

Example: Basis Capital — FOS determination 18959

FOS determination 18959 was made in response to an investor who challenged his planner's recommendation to place him in the Basis Yield Fund.

Despite making up only 5–6% of the client's portfolio, the client lost money when the product collapsed during the global financial crisis. FOS ruled that the planner breached their statutory duty under section 945A of the Corporations Act and duty of care by recommending a product that was inappropriate to the client.

In their defence, the planner and licensee argued they had based their decision on information that was freely available in the PDS and the fact it was on the APL.

However, FOS found the advice to invest in the product did not meet obligations under section 945A of the Corporations Act. The main reasons for this were:

- Asset allocation within the client's portfolio was made without 'any real understanding' of the Basis Yield Fund.
- The product was 'arbitrarily placed' as a defensive asset, despite characteristics to the contrary.
- The fund had a mandate which, if exercised, would make it unsuitable for the clients risk profile.
- The investment did not perform in line with the client's expectations.

According to FOS, planners need to go beyond their APL to gain a detailed understanding of a product to ensure it is suitable for their client and thus demonstrate a duty of care to that client.

Source: Nethercote 2009.

7.10 Planner responsibility

The global financial crisis provided a major wake-up call for the financial services industry, particularly regarding reliance on resources from external providers.

Ultimately, planners need to use a variety of sources of research, including research reports, ratings, specialist training and independent investigation. Currently, their key obligation is to know their client and match this information to their needs and objectives. From 1 July 2013, their obligation will be to always act in the best interests of their client in all elements of the advice provision process.

Explaining a product

Communicating research findings to clients is an important part of the advice process. Face-to-face discussions, the SOA and the inclusion of separate fact sheets and information are all important ways of conveying how the product is expected to perform.

Planners may also need to deconstruct ratings jargon and explain why a product is suitable for a client.

Planners that provide an ongoing portfolio monitoring service must conduct the same amount of due diligence when rebalancing as was conducted during initial portfolio allocation.

Sample case study

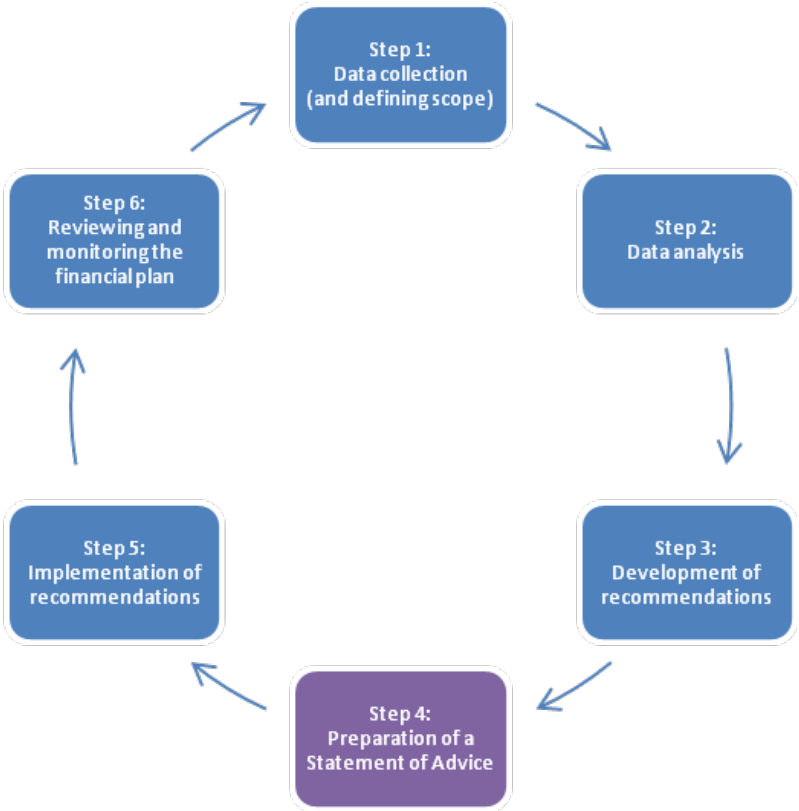
From the strategies described to address the clients' goals, you will find that some products have been recommended.

Open the sample case study SOA, and look at the strategy recommendations and investment product recommendations of the SOA.

Here you will find explanations as to why the products recommended to implement the strategies were chosen. Check that each product has been described, together with a reason for its choice.

Note: You can access this resource at KapLearn.

8 Preparation of an SOA



An important part of the investment planning process is the preparation of the SOA. Under the Corporations Act, when a licensee or their authorised representative gives personal advice to a retail client, an SOA must be provided (unless an exception applies). The industry terminology for this document is a financial plan.

The SOA formally documents key information from the financial advisory process, including the client's financial goals and objectives, the financial strategy and recommendations, and the expected outcomes. An SOA has three key objectives:

- **Documentation of client information:** Financial analysis and assessment, including data collection material, asset and liability charts, cash flow analysis, goals and objectives, risk tolerance, investment risk and establishment of the asset allocation. Data collection and data analysis provide the framework on which the strategy of the SOA can be built.
- **Deliver the strategy, tactics and products:** Present recommendations and the products that will carry the recommendations, and how those recommendations will address the client's objectives.
- **Detail the implementation process and evidence of compliance:** Inclusion of mandatory information in the SOA, client agreement to implement the SOA, the costs, and what the client needs to be aware of regarding important information, the recommendations and the advice that they have been given.

8.1 Content of an SOA

Some of the content of an SOA is determined by legal and regulatory requirements.

The title 'statement of advice' must be used on the cover or at or near the front of the document. It can be abbreviated to 'SOA' in the rest of the document.

The SOA must include:

- name and contact details of the licensee
- name and contact details of the representative and a statement that they are an authorised representative of the licensee
- a statement setting out the advice
- information about the basis on which the advice is given
- information about remuneration (payment) or other benefits which may be received by the representative, related body, employer, director or any associated person that may influence the provision of the advice
- information about any interests, associations or relationships that might influence the provision of the advice.

However, much of the actual content will be determined by the scope of the advice.

It is important to point out that there is no right way to construct an SOA. SOA structure, content and language will depend on the client's needs, financial literacy and the scope of the advice. You may have access to SOA templates and software in your workplace.

A comprehensive SOA usually includes the following, usually in this order:

- the name and contact details of the licensee and the authorised representative preparing the plan
- a statement of the client's personal details
- a summary of the client's existing financial position and cash flows
- a summary and analysis of the client's needs, goals, financial objectives and concerns (usually risk protection, investment, retirement, tax planning, social security and estate planning)
- a summary of the client's risk profile
- a description of the strategies considered in the formulation of the plan (including portfolio construction and asset allocation), together with the rationale for the strategies recommended
- a schedule of investment and/or insurance recommendations
- product recommendations for investments and/or insurance, together with a rationale for their selection
- research information on the investments/products selected
- schedules of expected cash flows and their effects on tax after the plan is implemented

- a realistic estimation of the capital growth prospects of the products
- coverage of any estate planning, risk or other issues assessed during the data collection process, with recommendations as to how they should be handled
- a schedule for the implementation of the advice
- details of future reviews and ongoing monitoring
- a clear description of fees, charges, commissions and any other remuneration or benefits that may be received, or that might be capable of influencing the advice provided
- any assumptions that have been used to make projections and estimates, (e.g. inflation, taxation rates, growth rates, returns or the overall macro-economic environment). These assumptions should be clearly stated as a disclaimer so that the reader can take them into account.

The SOA can be a lengthy and complex document; however, it is essential that it is clear, concise and effective — this is a legal requirement. There is therefore a balance between providing proper information to the client, in an efficient and communicative manner, and complying with legal requirements. The SOA itself becomes the record of actions taken and the justification for taking such action. It also supplies the disclosure information required by legislation.

An SOA is a communication document

The SOA is a documented two-way communication. Initially, the client, with careful guidance, communicates to the planner their financial resources and expectations.

When the planner knows where the client is now, and where they want to get to, they need to assess what attitudes regarding financial matters will assist or hinder the client in achieving their goals.

The financial planner's role is to help clients test their attitudes and establish their priorities. This can be done through education, working on 'what if' scenarios and client assessment tools, such as risk tolerance assessments.

Where goals and attitudes are changed, this needs to be stated within the SOA.

An SOA is a marketing tool

The SOA is also a marketing document, and it must be attractive to the client. Assuming the planner has developed a solid strategy and has identified investment structures and products that will assist the client in meeting their goals, it is important that the communication of this makes a compelling case for the client to agree to implement the SOA. Some of the key attributes of an effective SOA are:

- a logical structure and organisation
- a clear flow of information
- the concise treatment of each component
- the constructive use of charts and graphs
- the use of simple language
- that it contains only pertinent information
- that it is clearly directed to respective clients
- a positive approach
- the relevant but limited use of appendices.

An SOA is a legal document

An SOA, if agreed to, becomes a legal document that exchanges advice for fees and, as such, can be considered part of an overall contractual arrangement. The overall contractual arrangement is the sum of all promises — FSG, verbal statements and agreements and any other separate contracts (client agreements) — made to the client. In addition, because of the government's stated objective to provide consumer protection through regulation, the SOA, when properly constructed, should provide evidence of compliance with some of these regulations.

An SOA is a story

An SOA is also a story about the client, their past behaviours, what they are doing now and what their future may be like. A financial planner must use all of their skills and knowledge to ensure it is a work of fact, not fiction.

Incomplete or inaccurate information

A financial planner is obliged to warn a client if their advice is based on incomplete or inaccurate information relating to the client's personal circumstances. If this is the case, the client should consider the appropriateness of the advice before acting on the recommendation.

Where this warning needs to be provided, it must be given to the client at the same time that the advice is provided. If the advice is being provided via an SOA, the warning may be included within the SOA.

However, whether the warning in provided at the time the advice is given to the client or is included within the SOA, the SOA must provide a statement setting out or recording the warning provided to the client.

Sample case study

Open the sample case study SOA and review the cover page and contents pages to ensure that the information required by legislation is contained in the SOA.

Read the SOA and observe how it tells the story of the clients' current situation, their goals and objectives, and the recommended strategies to meet those goals. Observe that the executive summary contains an explanation of the outcome for the clients if they follow the recommendations.

Look at the SOA Appendix 1 and 3 that have been presented to show the clients how the strategies will help them to reach their goals. (More details on how the calculations were made follow in later topics so don't worry if you are not sure yet how these values were derived.)

Note: You can access this resource at KapLearn.

8.2 Other advice documents

An SOA is generally the format for providing advice to a new client. After reading the SOA, the client should be able to understand the advice and be able to decide whether to rely on it and proceed with the recommendations. An SOA is required whenever personal advice is given to a retail client, unless an exemption applies.

In some circumstances, it may be appropriate to record delivery of advice in an alternative document, such as a record of advice (ROA). The correct method depends on the situation at the time.

Record of advice

Essentially, an ROA can be used when providing further advice to existing clients. In this case, an alternative to providing a written SOA is to create an ROA and ensure that relevant disclosure is made to the client and contained in the record.

By default, the most useful evidence of advice for existing clients will be a written SOA. This is because often an ROA cannot be used every time advice is provided to an existing client.

The regulations note that a planner can only rely on this ROA relief if the:

- client had previously been given an SOA by the planner or their licensee that sets out the relevant circumstances in relation to the advice
- client's relevant circumstances in relation to the further advice, having regard to objectives, financial situation and needs, are not 'significantly different' from their relevant circumstances in regards to the previous SOA
- basis of the advice is not 'significantly different' from the advice in the previous SOA (i.e. it is consistent with the advice in the previous SOA).

The explanatory statement that accompanied the regulations noted that the regulations do not define when a client's relevant circumstances or the basis for the advice will be considered 'significantly different'.

The explanatory statement provides an example, whereby a change in annual income of $20,000 may represent a significant change in the financial situation of a person with an annual income of $50,000 but not in that of a person with an annual income of $200,000.

This means that the definition of 'significant' is dependent on the individual client. The planner will need to know the client and determine at the time of preparing the advice whether the event in question is significant for that particular client.

An ROA given to the client must be kept on the client's file and a diary note recording the change would seem to be sufficient in cases of ongoing amendments or adjustments to a client's plan. Details should include a note of any fee changes and confirmation that the client has been informed of these fee changes.

Incorporation by reference

Where a client has previously received an 'eligible advice document' and now requires additional advice, they may receive either an SOA or ROA, depending on the extent and type of the advice. However, these subsequent disclosure documents may incorporate, by reference, information in the initial 'eligible advice document'.

The reference must enable the client to clearly identify and locate the information incorporated by reference. If the client is unable to locate the original document that is being referred to, the planner must provide another copy of it free of charge and as soon as possible.

This provision negates the need to repeat important information in the new disclosure document, allowing it to be included by clearly identifying where it can be found in the initial 'eligible advice document'.

Incorporation by reference is not acceptable where the client is to be issued a warning that the advice is based on incomplete or inaccurate information or where a replacement product is being recommended.

Where the additional advice is being provided by a different planner, incorporation by reference may only be used if the previous planner was also a representative of the same Australian Financial Services licensee.

What is a significant change?

Where advice relates to financial products with an investment component, RG 175 provides a list of relevant circumstances (175.287 October 2013). Although not an exhaustive list, it is a reminder of what areas should be considered when considering if a change is a significant change in a client's relevant circumstances.

If a significant change occurs in the client's circumstances, then an ROA cannot be used to record the advice. An SOA is the more suitable document as it allows a planner to outline any changes to the client's relevant circumstances since the earlier advice.

RG 175.287 (October 2013) notes the following as relevant circumstances where the advice relates to a product that has an investment component:

- need for regular income (e.g. retirement income)
- need for capital growth
- desire to minimise fees and costs
- tolerance of the risk of capital loss, especially where this is a significant possibility if the advice is followed
- tolerance of the risk that the advice, if followed, will not produce the expected benefits
- existing investment portfolio
- need to be able to readily cash in the investment
- capacity to service any loan provided for a financial product
- tax position, social security entitlements, family commitments, employment security and expected retirement age.

It advises that the above list is not exhaustive and consideration should be given to any other matters that could be relevant to the advice.

Examples of common changes that would be acceptable for the issue of an ROA are:

- an additional amount lodged in an existing investment
- rebalancing of an asset allocation to the recommended level
- redemption of funds where the amount is not large
- renewal of a maturing investment.

Despite its potential complexity, it is essential the SOA be fully understood by the client. In light of this, the planner must strive, as much as possible, for clarity and simplicity. It is important to remember that a well-constructed SOA will achieve a number of outcomes.

8.3 Constructing the SOA

It is not easy to produce an SOA. There are several components that have to be developed, cross-referenced and checked.

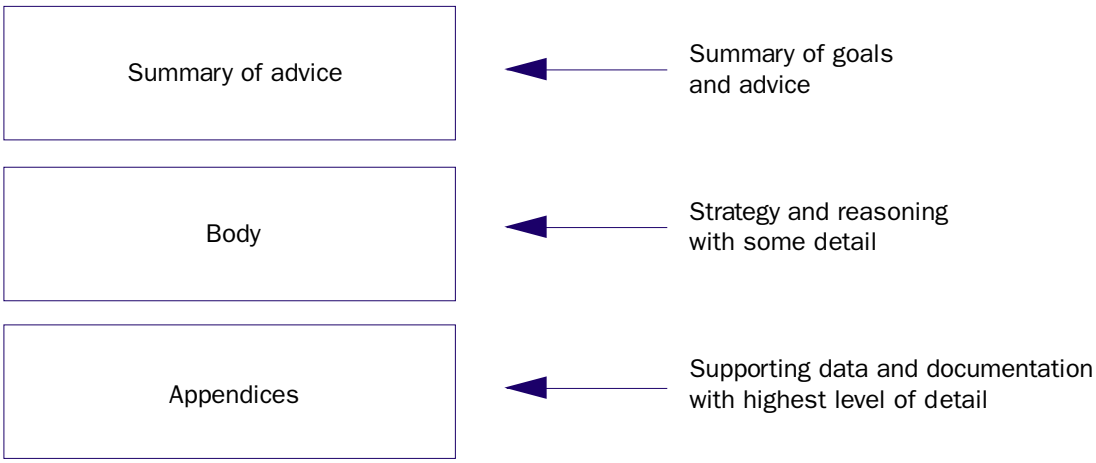
The structure and size of an SOA will vary depending on a number of issues, not the least of which is the complexity of the client's financial situation and the extent of advice required.

Although there are no hard and fast rules about the structure and format of the SOA, it must comply with ASIC requirements and the requirements of the licensee. The format presented here is only a suggested model. It is the planner's responsibility to ensure that the SOAs they produce comply with ASIC's requirements and those of the licensee.

One approach is to construct the SOA in three different levels, as shown in Figure 8. Each level should contain increasing levels of detail.

Level 1 is a summary of advice and other important information, level 2 is the body of the statement, and level 3 is the appendices, which support and enhance the client's understanding of the developed strategy.

Figure 8 Structure of an SOA



Suggested content for each section of the SOA

The construction of an SOA has three different sections; the details are shown in Table 8.

Table 8 Contents of the SOA

Executive Summary	This section provides a concise summary of: • the client's situation • the client's objectives • the strategy and recommendations to achieve the objectives • the outcomes expected from adopting the strategy. The client should be able to read the summary of advice, understand it and the reasoning underpinning it, and determine whether their goals have been achieved. There should be sufficient detail to allow the client to make a decision. It should be written in clear, unambiguous language, without jargon and appropriate to the level of financial understanding of the client.
Body	This section may contain headings similar to those in the summary. The information is at a greater level of detail and supports the recommendations made. As with the summary, it should be in clear language and appropriate to the level of understanding of the client.
Appendices	This section should contain any supporting documentation, such as charts, spreadsheets or projections, used in the formulation of the strategy and recommendations, but which are not necessarily essential for the decision-making process. If appendices are included, ensure the calculations, spreadsheets and projections are relevant to the advice.

Key points about the SOA

The following are some key points to keep in mind when developing the SOA:

- The SOA should be viewed as one part of the communication process, which began with the initial contact with the client.
- The SOA should be unique to the client and address their individual needs and objectives. Only material relevant to the client should be included.
- The SOA should be written from the client's perspective.
- The SOA should be concise, particularly in the summary. Most clients do not want to read more than they have to in order to understand the advice being given.
- The financial planner should know the client and their level of financial sophistication. The SOA should be written at a level they can understand, without jargon and unfamiliar terms.
- The SOA should be written in plain English (i.e. language the client will understand).
- The SOA should use short sentences and paragraphs that deal with only one idea.
- The planner should use the active voice (e.g. 'We will issue instructions…', rather than: 'Instructions will be issued …').
- The writing should be unambiguous.

When the SOA has been finished, the planner should review the SOA and answer the following questions:

- Does it show clearly that the client's needs and objectives have been met?
- Is the language and explanation level used appropriate for the client's level of financial literacy?
- Is the design and format of the SOA clear, easy to read and to follow, and appealing to the eye?
- Is it clear who the providing advisory entity is, and their details and contact information is included?
- Is it clear whether there are any remuneration details that may influence the client's decisions?
- Has all of the information about associations and relationships been disclosed, including those of the licensee?

Above all, the planner should give the SOA a last check to make sure that what has been developed is clear, concise and effective.

8.4 Presenting the SOA

Once the SOA has been drafted, it will be presented to the client, which usually involves a face-to-face meeting. The financial planner needs to be prepared to make adjustments as required, and to negotiate changes. A checklist of what needs to be discussed and highlighted to the client will help to ensure that the client is in a position to make informed decisions.

Some more complex situations might require a number of alternative recommended strategies, not just one recommended strategy. If this is required, then an evaluation of each alternative recommended strategy should also be provided to the client, indicating any advantages or disadvantages of each recommended strategy.

In all cases, the client has to be made aware of the level of risk relating to each product included in the strategy. The risk proposed has to be appropriate to the client's risk profile.

Presentation meeting

Before the planner presents their recommendations to the client, it may be beneficial to revisit the financial planning process with the client and where they are in that process.

This will allow the financial planner to set the scene for the presentation meeting, and to encourage questions as they arise.

During the presentation meeting, the financial planner should:

- educate clients on the risks involved in a clear and concise manner, so that there are no surprises
- present the written recommendations
- explain how the recommendations address the client's needs, objectives and financial situation
- explain the rationale behind the recommendations
- explain all of the fees, charges and expenses
- reinforce important product/service information to the client, such as cooling-off periods and the complaints process
- allow the client to ask questions
- explain any forms to ensure the client is aware of what is being signed
- provide the client with an opportunity to review the advice documents and any PDSs in their own time
- confirm the client's understanding of the implications of the advice provided
- discuss the broad strategy.

Checking for understanding

There are several ways to check that the client has understood the plan, including asking questions and observing body language.

Ask questions

Possible questions to ask the client are:

- Is the summary of your [the client] financial goals correct?
- Do you think that your risk profile is accurate?
- Would you like to discuss the reasoning behind the recommended strategy?

Body language

Body language might indicate that the client does not understand the plan and the planner should follow up with further questions, such as:

- Is there anything there that you do not understand or you would like clarified?
- Is there anything in the SOA that concerns you?
- Is there anything you would like me to explain further?

Dealing with client concerns

Take client concerns as a positive sign. It means that they are really considering the proposal and need to feel comfortable with the solution.

It is important to acknowledge all concerns. Where a couple is involved, ensure that the concerns and questions of both partners are addressed and not just those of the more vocal partner.

Some concerns need to be dealt with in full when they are raised. Others may be addressed by acknowledging them when they are raised and saying that their questions will be addressed later in the interview. Others may require additional research, and this should be explained to the clients.

Ensure that client concerns and the way they have been dealt with are documented. This will help to make sure all concerns are addressed and that compliance obligations have been met.

Explain associated fees and costs

At this point, it is important that the financial planner explains all fees and costs associated with implementing the recommendations.

A financial planner should have a system and process for positioning their fees. Communicating these fees and getting the go-ahead from the client is essential. The value to the client must be articulated.

Adjusting the SOA

The process of providing financial advice is not always a clear-cut, one-way street. After the plan has been presented and checked for understanding, it may be necessary to go back, revise the strategy and adjust the SOA.

Apply your knowledge 14: Adjusting the SOA

List four (4) reasons why adjustments to an SOA might be needed.

Note: You can access 'Suggested answers' for this activity at the end of this topic.

Even after extensive data gathering and analysis of the client's needs, objectives and financial situation, the first SOA may not be totally acceptable to the client. There may be several reasons for this, including:

- the costs of implementing the recommendation may not be acceptable to the client
- after consideration, the client may not be comfortable with the degree of risk involved
- although the strategy proposed is acceptable to the client, they may not be comfortable with the products selected
- through the discussion surrounding the presentation of the SOA, it becomes apparent that an important aspect of the client's situation has not come to light before.

It is necessary to be flexible when dealing with these situations. Depending on the reasons and degree to which the recommended solution is unacceptable to the client, it may be necessary to make adjustments to the SOA or revise the strategy to gain the client's acceptance.

Apply your knowledge 15: Making amendments to an SOA

List three (3) factors financial planners should be mindful of when making amendments to an SOA requested by a client?

Note: You can access 'Suggested answers' for this activity at the end of this topic.

Providing a PDS

At this point, where a financial product has been recommended, a PDS must be made available to the client. The PDS applies to all financial products, with the exception of 'securities' (i.e. shares and debentures). Offers of securities are by way of a prospectus, which contains information similar to that in a PDS.

The main components of a PDS are:

- details of the issuer and seller
- an application form
- details of significant benefits and risks
- costs of the product
- product features
- tax implications
- a 14-day cooling-off period for all products, with the exception of securities
- a disclosure of remuneration for products where the return is ultimately reduced because of charges, including any commission payments.

Client and planner sign-off

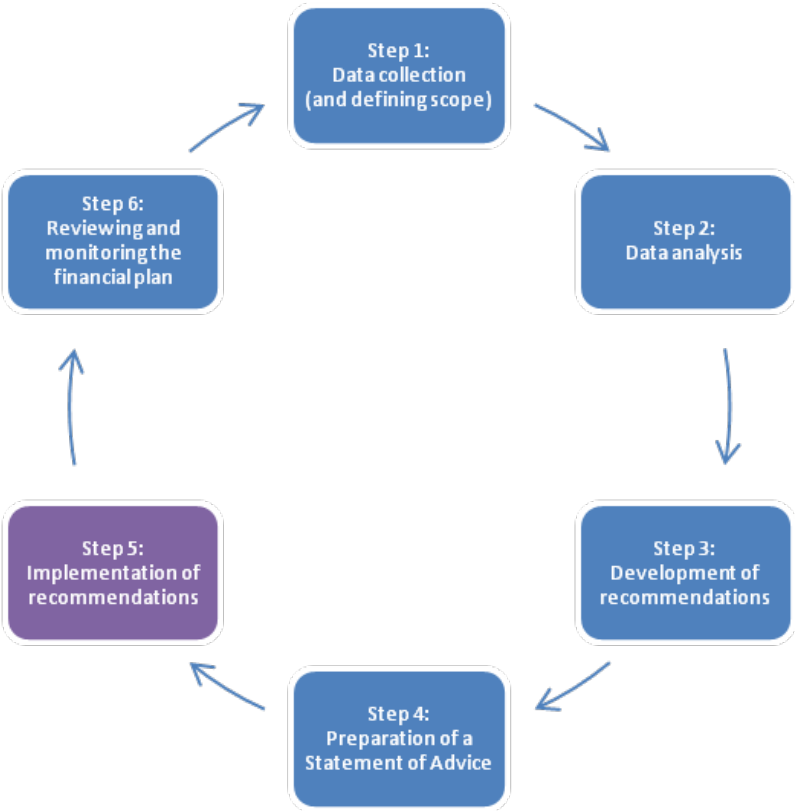
When all questions and issues have been dealt with, the financial planner should obtain the client's written approval to proceed with the implementation of the SOA. Most licensees and financial planners have a standard form for this, often referred to as an authority to proceed.

By signing the authority to proceed, the client is acknowledging that they have, among other things, received, read and understood documents, such as the FSG.

The authority to proceed allows the planner to put in place the actions required to implement the SOA. Although it is not a requirement, some authorities to proceed also include provision for the planner to sign off. This reaffirms the conditions under which the advice has been given and the role the planner plays in the process.

For the protection of both the financial planner and client, it is important that both sign off on the SOA.

9 Implementation of recommendations



9.1 Action plan for implementation

Before taking action to implement the recommendations, it is important to compile and discuss an implementation action plan with the client, and then to ensure they understand it.

The action plan gives the client another chance to review the recommendations. During the review of the action plan, it may be necessary to answer client questions and check for understanding and satisfaction with the provided answers. This process also provides another opportunity to ensure the client fully understands the strategy they are embarking upon.

As the financial planner and client work through the action plan, it is possible to ask questions to ensure the client's understanding of each implementation step.

A step-by-step implementation or action plan serves three purposes:

- It details all actions that need to be taken.
- It is a progress review (i.e. it details what has been done and what still needs to be completed).
- It acts as a prompt for additional questions by clients.

Implementation schedule

Implementation often involves putting systems into place and completing and documenting administrative processes, such as opening accounts, completing application forms, arranging insurance coverage and purchasing investments.

At this stage, a detailed implementation schedule, often referred to as an action to proceed, must be developed.

The implementation schedule should first itemise all client and planner tasks. Time frames of when tasks should be completed need to be included, for the benefit of all parties. The schedule should highlight the priority of each task, as well as the order of completion; for example, setting out that current insurances are not cancelled until after new insurances have been accepted by the new provider.

Documentation that may need to be completed at this stage of the process includes:

- disclaimers as to currency of information, outside data, etc.
- application forms contained in PDSs
- extra statements/questionnaires required for insurance proposals
- written authorisation to become the adviser, with regard to the client's existing investments, superannuation funds or life insurance policies
- a signed agreement by the client to the ongoing service that will be provided by the financial planner.

Sample case study

Open the sample case study SOA, and look at the strategy recommendations and Appendix 5 of the SOA.

Here you will find a detailed implementation schedule that should match with the recommendations made in the strategy recommendations section of the SOA.

Check that each recommendation has been listed in the implementation schedule with its relevant actions.

Note: You can access this resource at KapLearn.

Monitoring implementation

The administration of this process must be carefully monitored and documented and the client kept informed of its progress. All relevant documents should be copied and filed, with the originals forwarded to the client where appropriate.

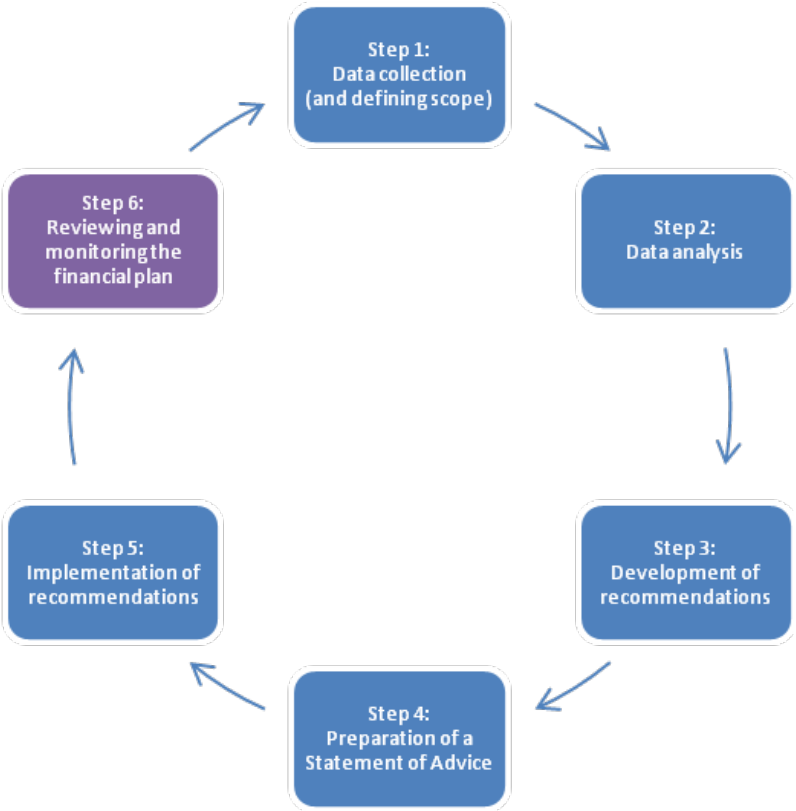
Implementation can take time, depending on the complexity of the advice and the types of recommendations made to the client.

For example, completion of a life insurance policy can be slow and time-consuming. The planner will need to keep abreast of the process and regularly update the client so that they do not lose sight of the importance of the recommendations.

Referring the client for specialist advice

If required, introductions to any specialist professional advisers who may be involved in a part of the plan, such as solicitors, accountants and actuaries, should be arranged. It may be beneficial for the financial planner to accompany the client to any interviews with third parties. It is essential that the privacy provisions are followed in all such situations and that licensee guidelines are followed where relevant.

10 Reviewing and monitoring the financial plan



Once the plan has been implemented, reviews are essential because, no matter how thorough and far-sighted the plan was when implemented, it is certain that factors affecting the plan will change over time.

A formal review process provides an opportunity to assess whether the plan continues to meet the client's financial and personal needs in an ever-changing economic environment. It could be that some aspect of the client's personal situation alters or the economy has entered another phase, or perhaps new regulation or legislation or a new style of product makes it advantageous to change the portfolio or impacts the client's long-term goals. If the change required is urgent, the financial planner is likely to initiate a special review, but more subtle changes will be picked up and corrected at a regular review.

10.1 Ongoing service packages

It is important that ongoing service is provided for clients, so the financial planner will have continuing contact with them and maintain an awareness of any changes in the their financial position, goals, needs or objectives. In most cases, the client will be looking to the financial planner for some form of continuing guidance once the advice has been implemented.

Ongoing service also helps to retain clients, which is essential for business success. It takes far less time and effort to maintain existing clients than it does to secure new clients. The review is one part of a comprehensive ongoing service package, but it should not be the only component. Usually, the SOA will contain details of the proposed ongoing service package made by the planner to the client. The client's agreement to proceed with this package will be obtained at the presentation of the SOA or at the implementation meeting.

A typical ongoing service package may include:

- full annual review service with personal circumstances, risk profile, needs and objectives revisited each year. This annual review also includes a review of relevant strategies, the investment portfolio and asset allocation
- a mid-year portfolio review
- investment reports at the end of financial year to assist the client with their tax return
- regular seminar invitations or client briefings where clients receive new market and product information
- newsletters or other adviser updates.

Sample case study

Open the sample case study SOA and look at the section 'Ongoing services', which details the reasons why ongoing advice is beneficial and outlines the service offer that the planner is making to the clients.

Note: You can access this resource at KapLearn.

10.2 Why are reviews important?

A client's needs, preferences and goals are continually changing. As life is not static, the client's financial needs and goals must be adjusted to compensate for change.

Client events that may trigger the need for a review of their plans include:

- having a baby
- divorcing
- changing jobs
- buying a house
- inheriting a sum of money.

One of the best ways to help ensure clients' financial goals are keeping pace with changes in their lives is through a review.

In addition, legislative changes and changes to the economy can potentially have a significant impact on a client's strategy.

For example, changes in the rules regarding contributions to superannuation have been made frequently by successive legislation, and each change has the potential to have a serious impact on a strategy that was commenced prior to the rules changing. It is important that a planner is aware of these changes and takes steps to inform affected clients and update their strategies.

Apply your knowledge 16: Periodic reviews

How would you justify the need for an ongoing service and review package with a client?

Note: You can access 'Suggested answers' for this activity at the end of this topic.

10.3 The review process

The review process may involve, but is not limited to, the six tasks as outlined in Table 9.

Table 9 The review process

1. Review the client's needs	Client's needs and objectives should be reviewed before considering how their investments are performing. Reviewing the client's needs involves considering their position, once again, in relation to social security, taxation, health, future plans, need for security of capital, estate planning needs and so on. The planner should also review the client's objectives. They should approach this process as they would for a new client.
2. Review financial and investment strategies	At least once a year, strategies need to be reviewed to identify: • changes, which may have affected the client • how these changes have an impact on existing strategies • how the strategies can be amended to cater for new needs.
3. Assess the current position of investments	The planner should determine the current value of the investment portfolio and compare it with the original expectations. Investment markets go through cycles, so although an investment may not have performed as expected it does not necessarily mean it is weak or should be sold.
4. Determine today's best portfolio	Here, the financial planner should forget about where the money is invested and ask, 'If the funds were in cash right now, where would I recommend they be invested?' They should choose investments in today's market that are the most appropriate to the client's current needs and objectives, without bias towards previous decisions.
5. Compare the best and current portfolios	If there are major differences between how the money is currently invested and how the planner would invest the money today, this is a signal that the money is no longer invested in the most appropriate investments. At this point, the review becomes challenging because the planner should list the differences between the current and the ideal portfolio.
6. Make decisions whether to alter investments	The objective of the review is not necessarily to change the current investments. However, when there are significant differences between the current and ideal strategy, the planner must decide what recommendations to make to the client. Where a recommendation is made to rebalance or change the current investments, consideration must be given to such issues as transaction costs, taxation and redemption penalties. In addition, ASIC requires a detailed comparison of the original and replacement products highlighting the advantages to be gained from altering the investments. At all times, recommendations to change investments must be made in the best interests of the client.

10.4 When should a review take place?

A review should take place:

- annually — review goals, lifestyle 'dreams', risk profile, etc.
- quarterly to six-monthly — review the portfolio
- at client-initiated changes.

10.5 Fees and charges

It is recommended that the financial planner and client agree at the outset on the type of ongoing service required and the applicable fees.

The agreement can be simple and brief, but it must be clear and in dollar terms. A sample wording might be: 'A review once p.a. at the anniversary of implementation, at an SOA review fee of $x, or a review once per quarter, at an SOA review fee of $x per quarter. This fee includes our monthly newsletter, invitations to client seminars, and half-yearly portfolio updates.'

It is important that this information is incorporated into the SOA. The client must also sign an agreement for the planner to provide the agreed service at the agreed fee.

11 Administration requirements

At each stage of the financial planning process, a number of different pieces of information will be collected, developed or reviewed. All of this information needs to be appropriately stored and managed in order to comply with a planner's obligations under the Corporations Act.

Client files

Every client seen by a financial planner should have a client file. The complete client file should contain the following information:

- a checklist of all the possible activities associated with the provision of financial advice
- the original referral document detailing the first client contact
- the fact-finding document (or documents)
- the data analysis papers, indicating the range of work done in preparation for the recommendation
- the original recommendations and/or SOA provided at the last interview, including the authority to proceed
- copies of completed and signed application forms and proposal forms
- the product illustrations and insurance quotations
- general correspondence applicable to the planning process
- file notes (see below)
- details of when the next contact is to take place and issues to be discussed.

File notes

Recommendations contained in the SOA, the completed fact finder, and other client documentation should contain as much detail about the client and their situation as possible; however, there is certain information that can only be recorded by the planner writing their own notes. These file notes are designed to record the interactions between the client and the planner whether that interaction is face-to-face, via email or over the telephone.

File notes should record:

- who instigated each meeting and why
- when and where the meeting took place
- who was present
- what was discussed
- the outcomes.

Recording this information, along with the demeanour of the client during the meeting, reasons for not having read documentation or not wanting to discuss certain issues and any other pertinent information, is very useful should a dispute arise in the future.

The information should be recorded as soon as possible after the interaction with the client and be written in a professional and objective manner.

Key points

- The financial planning process consists of six steps:
  - data collection (and defining scope)
  - data analysis
  - development of recommendations
  - preparation of an SOA (and presentation to the client)
  - implementation of recommendations
  - reviewing and monitoring the financial plan.
- A strong rapport between the planner and the client is vital for accurate data collection, which in turn is the foundation for the development of appropriate recommendations. A financial product adviser has a duty of care obligation to their client.
- A fact finder, or needs analysis form, allows client information to be collected in an orderly and sequential manner. It also acts as a record to endorse the planner's recommendations.
- Quantitative information gathered about the client and their financial situation is easily stated in terms of numbers, amounts or stated facts, such as their name, date of birth, occupation, investments and liabilities.
- Qualitative information is gathered on the psychological aspects of a client's situation and includes the client's values and motivations, as well as their attitude to and acceptance of investment risk (called the 'risk profile').
- Clear client goals give the planner specifics on which the recommendations can be built. Good objectives are SMART: specific, measurable, achievable, realistic and time-bound.
- Risk profiling can be conducted using several different tools, with the objective of determining a client's comfort level with the short-term volatility of their portfolio, and the concern that their investment portfolio balance will be less than expected in the future.
- Data analysis can be classified under 11 general headings:
  - review of the fact-finding stage
  - current position
  - determine debt management requirements
  - determine risk protection requirements
  - determine savings requirements
  - determine investment requirements
  - consider retirement funding
  - plan retirement income stream
  - review social security entitlements
  - plan taxation strategies
  - consider estate planning issues.

- After the data analysis stage, strategy development can be undertaken by looking at the clients goals in terms of priority and then developing strategies to meet the highest priority goal first.
- Strategies are likely to have an impact on one another, and the planner's role is to find the most appropriate set of recommendations for the client through considering how the strategies work together.
- When making an investment recommendation, it is important that the planner builds a portfolio which is well diversified, is in accordance with the client's risk profile, is flexible, provides for capital growth or income as needed, is tax effective and meets the client's financial goals and objectives over the agreed time horizon.
- Under the provisions of the Corporations Act, when a licensee or their authorised representative gives personal advice to a retail client, an SOA must be provided. An ROA can be given for subsequent advice if certain provisions are met.
- An SOA must, at least, include:
  - the name and contact details of the licensee and the authorised representative preparing the plan
  - a statement of the client's personal details and circumstances, existing financial position and an analysis of their needs, goals and concerns
  - a description of the strategies considered in the formulation of the plan (including portfolio construction and asset allocation) together with the rationale for the strategies recommended
  - a schedule of investment and product recommendations together with a rationale for their selection
  - a clear description of fees, charges and any other remuneration (including commissions) or other benefits that may be received or that might be capable of influencing the advice provided.
- Implementation of a financial plan involves putting systems into place and completing and documenting administrative processes (e.g. opening accounts, completing application forms, arranging insurance coverage and purchasing investments). A comprehensive implementation plan should be followed.
- A client's financial plan should be monitored for both the performance of the investments and the appropriateness of the plan for the client's ongoing individual circumstances. Circumstances that may require the recommendations in the plan to be revised include:
  - changes in the client's personal situation
  - changes in the client's financial situation
  - changes in the client's attitudes
  - product and legislative changes
  - external events in the marketplace.
- Every client needs to have a client file. It should contain copies of all communication with the client, comprehensive file notes of each contact, the fact finder and other fact-finding information, the SOA, any ROAs, the authority to proceed, implementation schedules, application forms and all other information relating to the client and their financial situation.

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Review questions

You can access 'Review questions' for this topic at KapLearn.

Suggested answers

Apply your knowledge 1: Verbal and non-verbal clues case study

a. **Verbal clues**

Bernie is the main talker, indicating his confidence and control in financial matters.

Silence on Mary's part may indicate lack of confidence or deference to Bernie's decisions.

'We won't go into that.' — This response from Mary flags some issues between Bernie and Mary over the decisions around financial investments.

'What can you do for us Martin?' — This question from Mary gives control of the conversation to Martin. Bernie is obviously uncomfortable with this, as his non-verbal communication indicates.

Non-verbal clues

Mary's shuffling and rearranging of her hands indicates discomfort with the course of the conversation.

Bernie's sitting back with folded arms indicates his discomfort with Mary taking the lead. The folded arms could indicate a reluctance to listen.

b. Restating key information can prompt an expansion or further disclosure of the issue. If the financial planner has not understood correctly, the client will generally correct this or reinforce their original statement. Paraphrasing can be extremely powerful. Martin could have tried using expressions like:

- 'Do you mean …?'
- 'What I hear you saying is …?'
- 'Let me see if I've got this right …'
- 'So, it seems …'

Apply your knowledge 2: Active listening

The statement	Underlying feeling
'My wife always makes the financial decisions, and she's the careful one.'	Husband feels left out of financial decisions. Husband thinks wife is too conservative.
'John filled in the form you sent us before the meeting — we didn't discuss it.'	Partner is not happy about being excluded. Partner does not know what was on the form and wants more input.
'I'm getting too old to work, but I need the money.'	Would like to retire early if possible. Would like to look at alternatives such as cutting back hours of work.
'It seems so final to be making decisions about retirement.'	Uncomfortable thinking about retirement. Need to explain the process of review and how goals and objectives can be revised as circumstances change.
'I'm not good with calculations.'	Does not want to spend time going through complicated calculations. Would prefer a verbal explanation. Has little financial experience.

Apply your knowledge 3: Difference between open and closed questions

Closed question	Open question
'Are you happy with your current financial set-up?'	'How do you feel about your current financial set-up?'
'Do you have a share portfolio?'	'How do you invest your money?'
'Do you have expectations of me?'	'What are your expectations of me?'
'Do you have superannuation?'	'What superannuation funds do you have?'

Apply your knowledge 4: Dispute resolution

The answer will be specific to your organisation.

Apply your knowledge 5: Create an agenda for the first meeting

1	Overview of XYZ Financial Planning Pty Ltd
2	Financial planner capacity and clients' rights
3	Our clients and our firm, and how we get paid
4	Introduction to the financial planning process
5	Information gathering
6	Discuss and identify the clients' goals and objectives
7	Initial strategy thoughts
8	Estimate of fee to proceed (if known and applicable)
9	Next steps: Where to go from here (setting expectations)

Apply your knowledge 6: Analyse and evaluate an FSG

The sample FSG in Appendix 1 enables investors to:

- ✓ Determine the date the FSG was prepared.
- ✓ Determine what their rights are in seeking financial advice.
- ✓ Identify the licensee.
- ✓ Identify the individual planner who will be providing them with advice.
- ✓ Understand that the planner is acting in a representative capacity.
- ✓ Identify who is responsible for the advice provided.
- ✓ Identify the scope and type of financial advisory services offered.
- ✓ Identify how the licensee and their representative will be paid.
- ✓ Understand remuneration (payment) arrangements.
- ✓ Determine whether commission is paid to the licensee and/or representative.
- ✓ Have a basic understanding of how commission is calculated and paid.
- ✓ Identify available complaints resolution schemes.

Apply your knowledge 7: Completing a fact finder

The answer will be specific to your personal circumstances.

Apply your knowledge 8: Distinguish between quantitative and qualitative information

Information	Quantitative or qualitative?
Age of client	Quantitative
Future priorities	Qualitative
Family relationships	Qualitative
Retirement plans	Qualitative
Liabilities	Quantitative
Attitude towards risk and loss	Qualitative
Previous investment experience	Qualitative
Personal goals and objectives	Qualitative
Education costs	Quantitative
Cash flow requirements	Quantitative
Desire to access capital	Qualitative
Insurance held	Quantitative
Superannuation information	Quantitative
Need for income protection	Qualitative
Home ownership status	Quantitative
Personal history	Qualitative
Current financial commitments	Quantitative
Assets	Quantitative
Funds available for investment	Quantitative
Current sources of income	Quantitative
Attitudes toward types of investment and asset classes	Qualitative
Centrelink entitlements	Quantitative
Desire to reduce tax	Qualitative
Existence of wills and power of attorney	Quantitative

Apply your knowledge 9: Determine your financial position

The answer will be specific to your personal circumstances.

Apply your knowledge 10: Current financial portfolio

The answer will be specific to your personal circumstances.

Apply your knowledge 11: Your financial objectives

The answer will be specific to your personal circumstances.

Apply your knowledge 12: Risk profiling

The answer will be specific to your personal circumstances.

Apply your knowledge 13: Prepare a budget

The answer will be specific to your personal circumstances.

Apply your knowledge 14: Adjusting the SOA

Adjustments to an SOA might be needed if:

- there are errors in the document
- incorrect assumptions have been used
- the client wishes to adopt an alternative strategy
- changes have occurred since the initial interview.

Apply your knowledge 15: Making amendments to an SOA

Planners should be mindful of a number of factors when making amendments to an SOA at a client's request, including:

- their legal responsibility — it may not be appropriate to change recommendations
- the changes requested by a client may not be appropriate
- warnings may need to be given to the client.

Apply your knowledge 16: Periodic reviews

An ongoing service and review package:

- ensures that everything remains on track
- allows the client to assess their current financial position
- allows the client to explore their options and alternatives
- helps to build a long-term relationship with the financial planner.

Appendix 1 — Sample financial services guide

Financial services guide

This Financial Services Guide was prepared on 1 January 2014 and issued by XYZ Financial Planning Pty Ltd

Financial services guide

This financial services guide (FSG) is intended to inform you of certain basic matters relating to our relationship, prior to us providing you with a financial service. The matters covered by the FSG include, who we are, how we can be contacted, what services we are authorised to provide to you, how the financial advice is documented, how we (and any other relevant parties) are remunerated, details of any associations or relationships that may influence our financial services, and details of our internal and external dispute resolution procedures, along with how you can access them.

It is intended that this FSG should assist you in determining whether to use any of the services described in this document.

You should also be aware that you are entitled to receive a statement of advice (SOA) or record of advice (ROA) whenever we provide you with any advice, which takes into account your objectives, financial situation and needs.

The SOA will contain the advice, the basis on which it is given and information about fees, commissions and associations which may have influenced the provision of the advice. An ROA may be provided subsequent to the provision of an SOA, provided your personal circumstances and the basis for the initial SOA have not changed. Copies of these documents will remain in your client file and may be supplied upon request through your planner.

In the event we make a recommendation to acquire a particular financial product (other than securities), we must also provide you with a product disclosure statement (PDS) containing information about the particular product, which will enable you to make an informed decision in relation to the acquisition of that product.

1 Before you receive our advice

Your questions	Our answers
Who will be providing the financial service to me?	Licensee XYZ Financial Planning Pty Ltd ABN: 12 345 678 90 Australian Financial Services Licence Number: 12345 1 Money Lane Planning Point NSW 2345 Tel no: (02) 5555 4564 Fax: (02) 5555 4654 Email: xyz@isp.com.au Authorised Representative Anthony Planner ASIC Authorised Representative Number: 65432 22 Wealth Place Sydney NSW 2000 Tel no: (02) 5555 8797 Fax: (02) 5555 3123 Email: aplanner@isp.com.au
Who is my planner?	Your planner will be Anthony Planner, who is an authorised representative of XYZ Financial Planning Pty Ltd and who is authorised to act on behalf of XYZ Financial Planning Pty Ltd. Anthony holds an Advanced Diploma of Financial Services (Financial Planning) and is a certified financial planner (CFP).
What kinds of financial services are you authorised to provide me and what kinds of products do those services relate to?	As an authorised representative of XYZ Financial Planning Pty Ltd, Anthony Planner can provide advice on and deal in the following financial products: • deposit products • government debentures, stocks and bonds • general insurance • risk insurance products • managed investment schemes (including master trusts) • securities • annuities and pensions • superannuation • reverse mortgages.
Who do you act for when you provide financial services for me?	XYZ Financial Planning Pty Ltd is responsible for the financial services provided to you.
How will I pay for the service?	The service may be paid for in the following way: 1. Pay a fee out of the product into which you invest. This may be as a commission from: a) a contribution fee deducted by the product provider from the initial investment amount b) management costs deducted by the product provider from your account on an ongoing bases or c) an ongoing fee that is agreed upon in relation to investment in certain products. 2. A fee for service based on the time involved to prepare your advice documents. You will be invoiced directly in this instance. 3. A combination of any of the above. You will need to negotiate with your planner as to which option you prefer.

Your questions	Our answers
Do you receive remuneration, commission, fees or other benefits in relation to providing the financial services to me and how is that commission calculated?	1. I receive a salary from XYZ Financial Planning Pty Ltd. 2. Our agreed advice fees may include charges for initial advice and, if agreed, ongoing advice. 3. My firm charges fees for our advice and services based on either an agreed set dollar amount invoiced directly to you or a set dollar amount or percentage-based fee calculated on the net value of your investment(s) and paid via your product (if possible). 4. Where a life insurance company product has been recommended, the issuer of the product may pay XYZ Financial Planning Pty Ltd an initial commission. This commission ranges between 0% and 100% of your first year's premium. 5. Where a life insurance company product has been recommended, the issuer of the product may pay XYZ Financial Planning Pty Ltd an ongoing commission. This commission, which can vary depending on the product, is calculated in a range of between 0% and 20%. This commission is paid each quarter. 6. Where the services of a stockbroker are utilised to deal in shares, XYZ Financial Planning Pty Ltd may receive between 0% and 1.5% of the brokerage amount paid to the stockbroker. 7. I may be entitled to a bonus from XYZ Financial Planning Pty Ltd based on income generated by me. At this time I am not aware if I will receive that bonus. I am not aware of any other incentive that I may receive from XYZ Financial Planning Pty Ltd or any product issuer. 8. If you have been referred to me by another party I may pay that party a fee of $100. 9. XYZ Financial Planning Pty Ltd and/or myself may also receive other benefits (e.g. marketing support, sponsorship, conferences or travel). 10. The exact amounts of any fees, commissions, bonuses or other incentives received by me and XYZ Financial Planning Pty Ltd will be included in a statement of advice that I will provide to you. For more information on our service fees, please refer to our attached fee schedule.
Do any relationships or associations exist which might influence you in providing me with the financial services?	Neither I, nor XYZ Financial Planning Pty Ltd, nor any related bodies corporate have any relationships or association with any product issuer that could be expected to influence us in the provision of the financial services.

2 When you receive our advice

Your questions	Our answers
Will you provide me advice that is suitable to my needs and financial circumstances?	Yes, but to do so we need to find out your individual objectives, financial situation and needs before we recommend any financial products or services to you. You have the right not to divulge this information to us, if you do not wish to do so. In that case, we are required to warn you about the possible consequences of us not having your full personal information. You should read the warnings carefully.
What should I know about the risks of the financial products or strategies you recommend to me?	We will explain to you any significant risks of financial products and strategies which we recommend to you. The PDS issued by the product provider will also contain details of the risks inherent in their particular product. If you do not fully understand these risks, you should ask us to explain them further.
What information do you maintain in my file and can I examine my file?	We maintain a record of your personal profile, which includes details of your objectives, financial situation and needs. We also maintain records of any recommendations made to you as well as any details relating to the provision of this advice. It may also be necessary on occasions to disclose information to other professionals, superannuation trustees, product issuers or insurance providers involved in providing services to you. However, we are committed to implementing and promoting a privacy policy which will ensure the privacy and security of your personal information. A copy of our privacy policy is enclosed for your information. If you wish to examine your file, we ask that you make a request in writing and allow up to fourteen (14) working days for the information to be forwarded.
Can I provide you with instructions and tell you how I wish to instruct you to buy or sell my financial products?	Yes. You may specify how you would like to give us instructions, for example, by telephone, fax or other means.

3 If you have any complaints

Your questions	Our answers
Who can I complain to if I have a complaint about the provision of the financial services to me?	XYZ Financial Planning Pty Ltd is a member of the Financial Ombudsman Service Limited. If you have any complaints about the service provided to you, you should take the following steps: 1. Contact us and speak with us about your concerns. 2. If your complaint is not satisfactorily resolved within three (3) days, please contact the Manager of XYZ Financial Planning Pty Ltd or put your complaint in writing and send it to: XYZ Financial Planning 1 Money Lane Planning Point NSW 2345 We will seek to resolve your complaint quickly and fairly. 3. If the complaint cannot be resolved to your satisfaction, you have the right to complain to the Financial Ombudsman Service Ltd. They can be contacted on 1300 780 808. This service is provided to you free of charge. The Australian Securities and Investments Commission (ASIC) also has a free information line on 1300 300 630, which you may use to make a complaint and obtain information about your rights.

Appendix 2 — Fact finder

Fact finder
Private and confidential

Privacy statement

The information collected in this form is for the sole purpose of establishing or building a financial service relationship with you. Your personal and sensitive information is treated with the strictest of confidence and is only provided to third parties where you have consented. If you have any questions in relation to your Privacy rights or wish to access or correct personal information we hold on you, please contact our Compliance or Privacy Officers on 5555 4564.

REPRESENTATIVE NAME _____

SIGNATURE _____

DATE _____/_____/_____

The process of financial planning

Financial Services Company has adopted the definitions of financial planning as:

> *'Financial planning is the process of providing advice and assistance to a client for the purpose of achieving the client's financial goals'.*

Financial planning is a comprehensive process that encompasses and integrates:

- investments
- risk management and insurance
- superannuation/retirement planning
- taxation
- estate and asset allocation protection planning.

Financial Services Company representatives follow these steps of the financial planning process:

- collection and assessment of personal and financial data
- identification of goals and objectives
- identification of financial problems
- the provision of a written report with recommendations
- the coordination, placement and implementation of personalised recommendations
- the provision of regular monitoring, reviews and planning updates.

All of the information will be held in the strictest confidence.

Information provided by you may be used to provide recommendations that are specific to your stated financial goals and objectives. It is therefore essential that you provide us with current and accurate information.

Personal details

	Self	Partner
Title	Mr Mrs Miss Ms ☐ ☐ ☐ ☐	Mr Mrs Miss Ms ☐ ☐ ☐ ☐
Given names		
Preferred names		
Surname		
Date of birth		
Marital status		
Tax file number		

Home address .....

Suburb/town ..... State ..... Postcode .....

Home telephone (.....) ..... Preferred contact no. (.....) .....

Email .....

Do you have a postal address that is different from your home address?

YES/NO (If yes, give details)

Postal address .....

Suburb/town ..... State ..... Postcode .....

Child/dependant details

Name .....

Relationship ..... Sex ☐ Male ☐ Female

Current Age ..... Dependant ☐ Yes ☐ No

Name .....

Relationship ..... Sex ☐ Male ☐ Female

Current Age ..... Dependant ☐ Yes ☐ No

Health details

	Self	Partner
Are you a smoker?	☐ Yes ☐ No	☐ Yes ☐ No

Do you or any member of your family suffer from any physical disability or health condition that may affect current or future considerations when we are providing financial services?

YES/NO (If yes, give details)

.....

Personal goals and objectives

Short-term goals

Write here the goals and objectives that you would like to achieve for yourself and your family over the next one to two years.

Medium-term goals

Write here the goals and objectives that you would like to achieve for yourself and your family over the next two to five years.

Long-term goals

Write here the goals and objectives that you would like to achieve for yourself and your family over the next five to 10 years or longer.

Write here the outcomes that you want to achieve from working with your financial planner.

Employment details

	Self	Partner
Current employer		
Position title		
Employer name		
Work address		
Current work telephone no.		
Start date		
Previous employer(s)		
Position title		
Employer name		
Employment plans		
Preferred retirement age		
Expected retirement date		
Are you contemplating leaving your current employer?		
Do you foresee any substantial change in your income in the next two to five years?		
After retirement to you intend to work again either on a full-time or part-time basis?		

Income details

	Self	Partner
Salary		
Investment income		
Social security income		
Super/annuity income		
Deductible amount		
Other income		

Expense details

Current living expenses	Self	Partner
Weekly		
Monthly		

Planned major expenses

Nature of expense	Approximate expense amount	Expected date
Weekly		
Monthly		

Personal balance sheet

Fixed assets

	Value ($)	Ownership C/S/J	Further details
Principal residence			
Contents			
Holiday home			
Contents			
Personal property			
Motor vehicle(s)			
Caravan/boat/trailer			
Other			
Total	**$**		

Are your assets adequately insured? ☐ Yes ☐ No

Liabilities

	Finance provider	Date commenced	C/S/J	Repayment amount	Repayment frequency	Interest rate	Balance outstanding
Mortgage							
Overdraft							
Credit cards							
Personal loan							
Other							
Total							

Personal superannuation

Company	Policy no.	C/S/J	Date commenced	Contribution rate	Current balance	Current cash value

Do any of the policies contain redundancy or sick leave payments?	**YES**	**NO**
Are any of the above policies preserved?	**YES**	**NO**
Has a tax deduction been claimed for part/all?	**YES**	**NO**

Employer superannuation

Scheme	Commenced	Contribution employer annual	Contribution employee annual	Defined benefit/accumulation	Current value

Other information (e.g. pension versus lump sum, funded or unfunded)

_____

_____

_____

Leave payments

Type	Expected date of receipt	Anticipated amount
Annual		
Long service		
Other		

Investment portfolio

Investment	Reference number	C/S/J	Date invested	Number of units	Current value

Personal insurance

Insurance description	Policy number	C/S/J	Date commenced	Sum insured	Premium payable	Maturity date

Other adviser details

Accountant

Name .....

Company.....

Address.....

Do we have authority to contact? ☐ Yes ☐ No

Solicitor

Name .....

Company.....

Address.....

Do we have authority to contact? ☐ Yes ☐ No

Determining your personal investor risk profile

1.	Which of the following best describes your current stage in life?	Client	Partner	Points
a)	**Single with few financial commitments:** You are keen to accumulate wealth for the future. Some funds must be kept available for enjoyment, such as cars, clothes, travel and entertainment.			10
b)	**A couple without children:** You may be preparing for the future by establishing and furnishing a home. There are certain things you need to buy. You are probably better off financially now than you may be in the future.			8
c)	**Young family:** This is the peak home purchasing stage. You have a mortgage and a very small amount of savings. You are probably concerned with your financial position and the amount of money saved.			6
d)	**Mature family:** You are in your peak earning years and have got the mortgage under control. Your partner may also work and any children you may have are growing up and have either left home or are less financially dependent. You are starting to think about retirement, although it may be some years away.			10
e)	**Preparing for retirement:** You probably own your own home and have few financial commitments; however, you want to ensure that you can afford a comfortable retirement and are interested in travel, recreation and self-education.			4
f)	**Retired:** No longer working, you must rely on existing funds and investments to maintain your lifestyle. You may be receiving a pension and are keen to enjoy life and maintain your health.			2
2.	**In light of current interest rates, what return do you reasonably expect to achieve from your investments?**			
a)	A return without losing capital			2
b)	Current inflation rate plus 1–2% p.a.			4
c)	Current inflation rate plus 3–5% p.a.			6
d)	Current inflation rate plus 5–10% p.a.			8
e)	Current inflation rate plus over 10% p.a.			10
3.	**If you did not need your capital for more than 10 years, for how long would you be prepared to see your investment not performing well before you would change it?**			
a)	You would change if there was any loss in value			0
b)	Up to three months			2
c)	Up to six months			4
d)	Up to one year			6
e)	Up to two years			8
f)	More than two years			10

4.	**How familiar are you with the investment market?**			
a)	Very little understanding or interest			2
b)	Not very familiar			4
c)	Have enough experience to understand the importance of diversification			6
d)	Understand that the markets may fluctuate and that different market sectors offer different income, growth and taxation characteristics			8
e)	Experienced with all investment sectors and understand the various factors which may influence performance			10
5.	**The greatest tax savings are generally obtained from investments which may be more volatile. Which balance do you feel most comfortable with?**			
a)	Preferably guaranteed returns, before tax savings			2
b)	Stable, reliable returns, minimal tax savings			4
c)	Some variability in returns, some tax savings			6
d)	Moderate variability in returns, reasonable tax savings			8
e)	Unstable, but potentially higher returns, maximising tax savings			10
6.	**What would your reaction be if, in six months after placing your investments, you discover that, in line with what is happening in the financial markets generally, your portfolio has decreased in value by 20%.**			
a)	You will be distressed; security of your capital is critical and you did not intend to take risks.			2
b)	You would redeem your investment and transfer your money into more secure investment sectors.			4
c)	You would be concerned, but would wait to see if the investment improves.			6
d)	This was a calculated risk and you would leave the investments in place, expecting performance to improve.			8
e)	You would invest more funds to lower your average investment price, expecting future growth.			10
7.	**Which of the following best describes your purpose for investing?**			
a)	You want to invest for longer than five years. You understand investment markets and are mainly investing for growth in assets such as shares and property to accumulate long-term wealth.			10
b)	You are nearing retirement, have surplus funds to invest and you are aiming to accumulate long-term wealth from a balanced portfolio, comprising of shares, property, fixed interest and cash.			8
c)	You have a lump sum (e.g. an inheritance or an employment termination payment from your employer) and you are uncertain about what secure investments are available.			6
d)	You are nearing retirement and you are investing to ensure you have sufficient funds available to enjoy your retirement.			4
e)	You have some specific objectives within the next five years for which you want to save enough money.			2

8. For how long would you expect most of your capital to be invested before you would need to access it? Assume that you and/or your financial planner have made plans to meet short-term financial goals and to handle emergencies.			
a) Less than two years			2
b) Between two and three years			4
c) Between three and five years			6
d) Between five and seven years			8
e) Longer than seven years			10
Total investor risk profile score			

Now match your investor risk profile to the following investor risk profile summaries.

Investor risk profile summaries	Total points
Highly conservative You are a conservative investor. Risk must be very low and you are prepared to accept lower returns to protect capital. The negative effects of tax and inflation will not concern you, provided your initial investment is protected.	0–30
Conservative You are a moderately balanced investor with some understanding of investment market behaviour. You do not want to see all your capital eaten away by inflation and tax. While generally cautious, you are prepared to accept some short-term volatility in order to achieve some longer-term capital growth.	31–45
Balanced You are a balanced investor who wants a balanced portfolio to work towards medium- to long-term financial goals. You require an investment strategy which will cope with the effects of tax and inflation. Calculated risk will be acceptable to you to achieve good returns.	46–55
High growth You are a moderately aggressive investor, probably earning sufficient income to invest most funds for capital growth. Prepared to accept higher volatility and moderate risks, your primary concern is to accumulate assets over the medium to long term. You require a balanced portfolio, but more aggressive investments may be included.	56–70
Aggressive You are a growth investor prepared to compromise portfolio balance to pursue potentially greater long-term returns. Your investment choices are diverse, but carry with them a higher level of risk. Security of capital is secondary to the potential for wealth accumulation.	>70

The risk profile asset allocation is the benchmark to commence the investment portfolio. On review, the asset allocation may change by mutual agreement between client and planner, taking into consideration the portfolio position and investment time frame.

Investor risk profile selected:		
I/We believe that the above rating reflects my/our attitudes and would be pleased to consider a portfolio that reflects my/our risk portfolio.		
Signature	**Signature**	**Date**

Household budget planner

Expenses	Fortnightly	Monthly	Quarterly	Half-yearly	Annually	Total last year
Payments — Fixed						
Superannuation						
Mortgage/rent						
Loan/hire purchase						
Car (registration/insurance)						
Insurance (life/disability/self/partner)						
Insurance (home/contents)						
Insurance (Medical/hospital)						
Rates (council/water)						
Electricity/gas						
Telephone						
Child care/babysitting						
Fees (school/university)						
Payments — Variable						
Groceries/consumables						
Clothing/shoes						
Cars (service/tyres/petrol)						
Public transport/fares						
Chemist/dentist/optometrist						
Newspapers/magazines/books						
Home repairs/painting/garden						
Appliances/furniture (new repairs)						
Payments — Discretionary						
Holidays						
Entertainment (restaurant/movies)						
Cigarettes/alcohol/work/lunch/takeaway						
Sports/hobbies/club fees						
Children's pocket money/toys						
Hairdresser/dry cleaning						
Gifts (Christmas/birthdays)						
Donations						
Other						
Sundry cash — self Sundry cash — partner						
Total payments						
Income *less* payments (Cash over/short)						

Client comments

Adviser comments

Tax file number authorisation

I/We give permission for my/our tax file number(s) as provided, to be held by Financial Services Company and be forwarded to financial institutions as requested or as necessary.

Signature	**Signature**	**Date**

Client statement/authorisation

I/We hereby declare that the information set out in this form is true and correct to the best of my/our knowledge. I/We are not aware of any other information and have not disclosed to the person to whom this form is given any other information which would be relevant to the making of a recommendation by a Financial Services Company representative.

I/We give permission for this information to be used for the preparation of my financial plan and I/We understand that the investment recommendations will be based solely on the information supplied in this form.

Signature	**Signature**	**Date**

Client defined scope advice statement/authorisation

Legislation requires that the Financial Services Company planner must act in the best interests of the client before making certain recommendations. However, there is provision that in certain circumstances a client may be supplied with advice which has been defined as limited in scope.

If you are seeking defined scope of advice of a limited and/or particular nature you must make this known at the time of the interview. You should recognise that the recommendations will only relate to the defined advice being sought and may not be appropriate considering your overall situation and objectives.

I/We require only defined scope advice as specified below:

_____

_____

_____

_____

_____

Signature	**Signature**	**Date**