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In recent years, the world has been awash in new fiduciary regulation for financial advisors, including the Future of Financial Advice (FOFA) reforms in Australia, the Retail Distribution Review (RDR) changes in the United Kingdom, and both the Department of Labor (DOL) rule and the more recent Securities and Exchange Commission (SEC) Regulation Best Interest proposals in the United States. These reforms all have focused on requiring financial advisors to act in the best interests of their clients and to reduce or eliminate conflicts of interest, especially around commission compensation. And although the DOL fiduciary rule was ultimately vacated in the United States and the SEC's Regulation Best Interest proposals are still being debated, in many other countries the fiduciary reforms already have taken effect—and now we're beginning to see the next stage of fiduciary legislation emerge.

This article examines the new round of financial advisor regulation emerging in Australia in particular, which focuses specifically on competency standards; what it suggests may come next for advisor regulation in the United States; and how U.S. financial advisors should be preparing to protect their own careers against potential future standards-raising regulation.

AUSTRALIAN FIDUCIARY REFORMS UNDER FOFA

In summer 2012, Australian regulators implemented new rules for financial advisors under their FOFA reforms.[1] The core of the new FOFA reforms required financial advisors to act as fiduciaries and place the best interests of clients ahead of their own interests, similar to the original DOL fiduciary rule here in the United States.[2] The difference is that although we've been debating a fiduciary rule since 2010, Australia just did it—proposed it in 2012 and fully implemented it by the summer of 2013.

And in fact, Australia's version of a fiduciary rule is more stringent than those being considered here in the United States. Australia flat-out banned all investment commissions for financial advisors. Australia also banned soft-dollar payments, shelf space, and revenue-sharing agreements to Australian dealer groups (roughly the equivalent of wirehouse broker-dealers in the United States). FOFA reforms also eliminated "recruiting" payments to advisors for switching dealer groups, because advisors should only need to switch to new platforms to benefit their clients, not themselves directly.

FOFA rules also limit assets under management (AUM) fees for investing into leveraged portfolios, to discourage anyone from taking out margin loans to increase the size of their portfolio assets for billing purposes, which doesn't happen much in the United States but was unfortunately more common in Australia. And FOFA also requires that clients re-opt into their advisory agreements every two years, to ensure that they really want to still be clients.

These changes should sound familiar, because many are the same kinds of rules we've been debating in the United States. The DOL fiduciary rule would have required advisors to act in the best interests of their clients, and the SEC's advice rule would as well. The DOL fiduciary rule didn't entirely ban commissions, but it triggered more scrutiny about reasonable compensation, and it already was starting to curtail some broker-dealers regarding revenue-sharing agreements. In addition, the Financial Industry Regulatory Authority (FINRA) has itself been examining whether we need to at least require better disclosures of the compensation that advisors get when they switch broker-dealers (a less stringent version than the FOFA reforms that banned such payments altogether).

AUSTRALIA PROPOSES NEW FINANCIAL ADVISOR COMPETENCY STANDARDS

Now that Australia is more than five years into its fiduciary rule, we can look to it as a "post-fiduciary world" to understand what comes next. The answer: Now Australia is moving to add new financial advisor competency standards as well.

Arguably, this is a good thing, because the reality is that it's not enough to just have a fiduciary duty for advisors to act in the best interest of clients. It's also essential for advisors to have technical competency and training in the first place.[3] Otherwise, you may not even know what's actually, truly, in the best interest of clients—because their situations may be too complex for you to analyze without the requisite education and training.

In the United States, fiduciary duty always has encompassed two core duties. The first is the duty of loyalty (to act in the best interest of the client), and the second is the duty of care (to only give advice in areas in which you're actually competent to do so). Other professions also impose a similar duty of care. A brain surgeon can operate on your brain and that's fine, but if a brain surgeon operates on your knee, that's a problem because a brain surgeon isn't trained in knee surgery.

In this context, we can see the logic of Australia following up its first round of FOFA reforms that imposed a requirement of the fiduciary duty of loyalty with the second round of reforms specifically targeted at financial advisor competency or the fiduciary duty of care.[4] The new competency rules in Australia would require each advisor to have the following:[5]

1. A college bachelor's degree
2. A full year of professional experience
3. A successful completion of a comprehensive exam to demonstrate competency in core knowledge areas
4. A commitment to ongoing education with the code of ethics

A new independent body called the Financial Adviser Standards and Ethics Authority will be responsible in Australia for determining the details, such as which college degrees qualify, creating and administering the new advisor exam, setting continuing education requirements, and establishing the new code of ethics.[6]

This is expected to be quite disruptive in Australia, because it's estimated that only about 25 percent of Australian advisors have the CFP marks or some equivalent, which would effectively cover advisors under the new competency rules and meet all these requirements.

In recognition of this challenge, Australian regulators are providing a substantial transition period for all Australian advisors. New advisors must meet the new requirements starting in 2019, but existing advisors will have until 2021 to take the exam, and until 2024 to earn college degrees.

Fundamentally, though, the new requirements are built around the basic concept that if you're going to give people financial advice, you should be required to know what you're talking about beyond the handful of products your company offers. Indeed, this is a worldwide trend. As advisors, we're not salespeople anymore. We're advisors who give advice about a lot more than a particular product our company manufactures for sale.

THE RISE OF COMPETENCY STANDARDS FOR FINANCIAL ADVISORS?

For those who have CFP certification in the United States, these Australian competency requirements should sound familiar. They are based on the same framework as the CFP Board's "Four E's": education, exam, experience, and ethics requirements.[7] The CFP Board implemented a bachelor's degree requirement back in 2007, already has an experience requirement of two to three years (depending on the nature of the experience), has had a comprehensive exam requirement since 1991,[8] and has long had a code of ethics (which was just recently updated).[9]

In other words, although CFP certification isn't required to be a financial advisor in the United States, CFP certification looks just like Australia's proposed requirements being implemented for all financial advisors, which may be the next shoe to drop in the United States. It's not clear whether regulators here literally would require the CFP marks to practice and make the CFP certification a minimum competency standard for all advisors.[10] Or maybe, similar to Australia, it would be some separate but similar competency requirement administered by a government regulator or independent entity the regulator creates, for which CFP certificants likely would be grandfathered.

FINANCIAL ADVISOR COMPETENCY STANDARDS INCREASE TRUST IN FINANCIAL ADVISORS

Improving competency among advisors does more than ensure the quality of advice, it also improves consumer trust in financial advisors. Herman Brodie of Prospecta, a firm in the United Kingdom, made this exact point at the recent Finology conference held in Sydney, Australia, February 14, 2018.[11] Brodie and Harnack (2018) examined how consumers decide whether to trust a financial advisor and found that it comes down to two factors: warmth and competency.

Warmth doesn't necessarily mean you must be ultra-friendly and extroverted with clients. It simply means that clients need to believe you care, and that you're really there to try to help them achieve better outcomes. But Brodie and Harnack (2018) found that warmth alone is not enough. If clients are going to trust your advice, they also need to believe you're competent in the first place—that you know what you're talking about, and that they can trust your advice.

Brodie and Harnack (2018) showed that plenty of industries and firms, particularly in financial services, are doing pretty well on perceived competency. The problem is that they have no perceived warmth. Indeed, there is a strong perception that shareholders and bottom lines come first at financial services firms, not clients.

On the other hand, competency is still an issue for many advisors as well. Legally, one can hold out as a financial advisor and be responsible for someone's entire life savings with little more than a high school diploma and a three-hour licensing exam.[12] (The exam doesn't test anything about your competency in delivering financial advice, it just tests your knowledge of the regulations—and the high school diploma is actually optional.) And barely 30 percent of all financial advisors have CFP certification, which means that more than 70 percent do not. A few might have a comparable education designation such as the Chartered Financial Consultant® credential or the Personal Financial Specialist credential for CPAs, or have pursued advanced designations such as the Certified Private Wealth Advisor® (CPWA®), but most financial advisors have no substantive education or designations in the subject of financial advice. Although many are experienced and have learned a great deal by working with clients, they simply don't have the training needed to be comprehensive advisors and ensure they know what the best advice for their clients actually would be.

FUTURE-PROOFING YOUR CAREER AS A FINANCIAL ADVISOR

Back when financial advisors primarily were selling insurance and investment products, we didn't need high competency standards in advice, we just needed to be competent in the products being sold. Most advisors now, however, are still being regulated like product salespeople even though the whole industry—worldwide—is shifting from a product focus to actual advice, where competency and quality matter.

This suggests that although Australia may be the first to formally lift the financial advisor competency standards, it probably won't be the last. Just as Australia was one of the first to propose a fiduciary rule and certainly wasn't the last. As a result, if you're a financial advisor who wants to future-proof your own career, you should be looking at investing in and advancing your education with marks such as CFP certification. As Australia has shown, there will probably be some grace or transition period. If you're five to 10 years from retirement, you're probably safe riding out with the status quo. But if you've got more than 10 years left in the business, you'll likely still be practicing after the first round of fiduciary rule to act in the client's best interest is done and the next round about competency standards gets going. Competency standards will be the battle of the 2020s.

And it's important to note that even though many suggest, "That can't happen here, it won't happen here," Australia made the change even though fewer than 25 percent of advisors have the CFP marks. The fact that we're approaching 30 percent of advisors with the CFP marks in the United States means, in theory, it would be easier to do it here than it was in Australia. This is a real warning to the 70 percent of advisors in the United States who don't have the CFP marks or an equivalent, and to advisors who are concerned about future-proofing their careers. If I were one of those folks, I'd be working on getting ahead of this trend sooner rather than later.

In the meantime, for those who are already CFP certificants, don't rest on your laurels. Once the bar is raised, your CFP marks won't differentiate you nearly so well, just as many advisors are now finding that marketing themselves as a fiduciary doesn't differentiate them in a world where everyone is a fiduciary. The regulators lifting the standards effectively eliminate these differentiators. That's why it's important to specialize,[13] or get some kind of post-CFP education[14] to stay one step ahead.

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