



Association of Financial Advisers Ltd
ACN: 008 619 921
ABN: 29 008 921
PO Box Q279
Queen Victoria Building NSW 1230
T 02 9267 4003 F 02 9267 5003
Member Freecall: 1800 656 009
www.afa.asn.au

26 July 2017

ASIC Enforcement Review
Financial System Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: ASICenforcementreview@treasury.gov.au

Dear Taskforce Members

AFA Submission – Consultation: Strengthening ASIC’s Licensing Powers

The Association of Financial Advisers Limited (**AFA**) has served the financial advice industry for 70 years. Our objective is to achieve *Great Advice for More Australians* and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

The Board of the AFA is elected by the Membership and all Directors are required to be practicing financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting wealth.

Introduction

The AFA supports measures that will have the effect of preventing the wrong people from entering the financial services industry or having the ability to operate within the industry. Accordingly, we support measures that sensibly increase the powers of ASIC to deal with parties who are not suitable to obtain or retain an Australian Financial Services Licence.

We are also supportive of measures to sensibly align the requirements under the AFSL regime and the Credit Licence regime.

Whilst we are supportive of sensible additional powers, it is important that the complexity and cost of applying for and retaining a licence does not place an excessive restraint upon people applying for a licence or continuing to run their licence. It is important that seeking to be self-licenced remains a

viable alternative for financial advisers who are seeking greater freedom in how they run their business. In essence, making it sensibly more challenging, but not impossible, is the right balance.

Response to Questions Raised in the Consultation Paper

Position 1 – ASIC Should be Able to Refuse a Licence Application if it is not Satisfied Controllers are Fit and Proper

1. Should ASIC be able to refuse a licence application if it is not satisfied that the applicant’s controllers are fit and proper to control a licensee?

The AFA supports this proposal. The person or company who controls a business, by definition, has a great deal of influence and can impact upon the business model, culture and practices of a business. For this reason, they should be required to meet the fit and proper obligations.

2. What would be the impact of this position on licence applicants?

This will have a marginal increase in the amount of work involved in a licence application, however the benefit is likely to be the removal of some people who should not be allowed to operate in the financial services industry.

3. When notifying ASIC of a change of control should licensees be required to provide ASIC with sufficient information to enable ASIC to assess whether:

- a. The proposed new controllers are fit and proper to control a licensee? and/or
- b. The licensee remains competent to provide the financial services covered by the licence and able to comply with its obligations under the new controller?

The AFA accepts that the change of control of a licensee is an important change that could have a material impact upon the operation of the business. For this reason, it is appropriate for ASIC to be made aware and to have the ability to assess whether this will impact upon the appropriateness of the licence.

We note however that a change of control event might involve someone completely new coming into the business or it might also involve someone who is already involved in the business taking a greater stake in the business. As an example, an existing shareholder, who is already a responsible manager, might increase their stake so that they move above the 50% ownership level. It might also be the case that someone who already has an existing business, and their own licence, purchases another business in a similar location. For this reason, we suggest that change of control not be treated in a one-size-fits-all approach, but rather the requirements should take into account the existing involvement of the controller in the business or their experience in running another business. We would suggest that this process should focus upon new controllers who have not been involved in the business previously and who have not been running a similar business.

4. Should ASIC be able to take action to suspend or cancel an AFS or credit licence (after offering a private hearing) if it is no longer satisfied that the controllers of the licensee are fit and proper to control the licensee?

The AFA supports ASIC being provided with this power subject to its application being based upon clear documented information that supports such a conclusion. We are conscious that from time to time things can be said about a person or a business by either a dissatisfied client or a competitor that presents the person/business in a poor light. This is not always accurate or at least fully accurate. We don’t believe that ASIC should be able to suspend or cancel a licence on the basis of

hearsay, but rather the first step should be to investigate the claim and then once the circumstances have been confirmed to take further action if appropriate. We recommend that ASIC must be reasonably satisfied to form this conclusion.

5. Should a change of control require pre-approval by ASIC?

As discussed above, change of control events will vary between someone already in the business taking a greater stake, through an existing industry participant taking control and then someone completely new taking control. The sale of a business is a critical step that can have a material impact upon the value of the business. Where the sale of a business occurs, and ASIC subsequently rejects the new controller, then this would pose a significant problem for the new owner and the clients. With financial advice businesses, it is common for the new owner to negotiate an arrangement where the former owner stays involved with the business for a transition period, with a final payment dependent upon issues such as client retention. The rejection of a change of control by ASIC could have a large impact upon both the purchaser and the seller.

It is our view that where there are any potential grounds for concern that ASIC might oppose a change of control, that the business should have the opportunity to seek pre-approval from ASIC. We would equally suggest that if the new controller was already a director or responsible manager or had experience in running another licensed business then pre-approval should not be required.

Position 2 – Introduce a Statutory Obligation to Notify Change of Control Within 10 Days of Control Passing and Impose Penalties for Failure to Notify

6. Would it be appropriate for the requirement to notify ASIC of licensee changes in control to be a statutory obligation rather than a statutory licence condition?

The AFA would not oppose this becoming a statutory obligation, although notes that a number of obligations are imposed by the means of licence conditions and that this can still be an effective means of inserting a requirement.

7. Would it be appropriate for the obligation to require notification within 10 business days of the change of control taking effect?

In some cases, 10 business days should be sufficient, however we note that licensees have 30 business days to notify ASIC that a representative has started or ceased. In certain circumstances, particularly where the provision of additional information is required, 10 days may not be sufficient. This will depend upon what additional information is required when a change of control notification is submitted. With smaller organisations where there is a greater reliance on part time resources or external service providers, 10 days would be much more challenging. We believe that this needs to be taken into account.

There will be certain circumstances where more time might be required and where special arrangements would be necessary. As an example, a situation such as the death of the existing controller would need to be treated differently, particularly where the owner was also a responsible manager and potentially the only responsible manager.

We therefore recommend standardisation with the timeframe for notifying new or ceasing financial advisers and therefore suggest a 30 day timeframe. An increased timeframe is particularly necessary where penalties apply.

We note that there may be circumstances where a change of control occurs, however for some reason this is not immediately apparent. This scenario should be addressed.

8. Would it be appropriate to introduce penalties for failure to notify ASIC of a change in licensee control?

Yes, this would be appropriate, however ASIC should have discretion to apply or waive the penalty if there are particular extenuating circumstances such as the example raised above with respect to the death of the existing owner. We also note that the failure to notify ASIC might be either unintentional or deliberate. We would recommend that they be treated differently.

9. If so, what penalties should apply? Should the penalty be criminal, civil penalty or both?

It is our view that any penalty should be civil and not large. To treat it as criminal would be to view this in terms of a deliberate failure to notify ASIC in order to retain the licence when it might be expected that ASIC would have taken action to suspend or cancel the licence. It would seem to be excessive to treat it as criminal if ASIC was never likely to have had any objection to the change of control. The penalty should reflect the fact that in the vast majority of cases it would be an administrative error and not a deliberate attempt to hide important information.

Position 3 – Align the Assessment Requirements for AFS Licence Applications with the Enhanced Credit Licence Assessment Requirements

10. Should the assessment requirements for AFS and credit licence applications be uniform? Or are there factors relevant to each sector that justify differences?

Whilst the AFSL regime is a different regime to the Credit licensing regime, we accept the proposition that alignment makes sense. This would not necessarily mean that everything should be the same, but it should be the default position.

11. If so, should the Corporations Act be amended to reflect the provisions of the Credit Act with respect to licence applications? In particular should:

- a. **directors, secretaries and senior managers, rather than only responsible officers be assessed for AFS licence applications?**
- b. **individuals be assessed against a ‘fit and proper’ rather than a test of ‘good fame or character’ for AFS licence applications?**
- c. **the requirement to consider whether an AFS licence applicant’s ability to provide financial services would nevertheless not be significantly impaired after forming a reasonable belief that individuals are not of good fame and character (or fit and proper) be removed?**
- d. **ASIC be able to require an audit report from AFS licence applicants?**
- e. **a failure to provide additional information requested by ASIC result in a deemed withdrawal of an AFS licence application?**

The AFA supports extending the licence application process to include directors, secretaries and senior managers and to apply the fit and proper test. We believe that senior managers should be limited to people in a position running a licensee and should not include other managers in the business, who are not already a responsible manager. The term senior manager needs to be clearly defined. We also support (c) above in that a determination with respect to fit and proper should not be subject to a second test on ability to provide financial services. We would also support the deemed withdrawal of a licence application where there has been a failure to provide additional information within a reasonable timeframe.

With respect to the ability to require an audit report, this is not well defined in the National Consumer Credit Protection Act 2009. It seems that this could be any special purpose audit to be

completed by a suitably qualified person. Obtaining an annual audit is something that public companies are required to do, however an audit is not required for proprietary companies. Such companies will most likely not have an auditor at the time of applying. Having said this, we note that once they had obtained an AFSL, they would be required to complete an annual audit.

We believe that there is a need for greater clarity with respect to the nature of such an audit report. We do not support an open-ended power to call for an audit report. Given the likely cost and delay involved in the completion of such a report, we would suggest that there would need to be strong grounds to require it.

12. What will be the impact on AFS licence applicants?

Whilst we appreciate that these changes would raise the bar for AFSL applications and will require additional information, we do not believe that this will be overwhelming and recognise that these changes will deliver long term benefits for the financial services industry.

Position 4 – ASIC to be Empowered to Cancel or Suspend a Licence if the Licensee Fails to Commence Business within Six Months

13. Should ASIC be able to immediately suspend or cancel an AFS or credit licence if the licensee fails to commence engaging in a financial services or credit business within six months of being granted a licence?

The AFA supports this proposal on the basis as explained in the consultation paper that licences should not be warehoused. We question which factors might determine whether ASIC makes the decision to suspend or cancel an AFSL or credit licence. If there are not obvious reasons to only suspend, then we would think that cancelling AFSLs and Credit licences should be the default position. We note the option discussed below about providing an extension.

If ASIC was to only suspend a licence for failing to commence operations within six months, then under what circumstances might it be possible for the suspension to be lifted? We believe that there is a need for some greater clarity on the operations of this power.

14. If so, should licensees be given an opportunity to seek an extension of time?

Whilst we fully support the position that a licensee should commence operations within six months, we do envisage that there might be some reasons why this might not always eventuate. Where there are justifiable reasons for the delay in commencement, then we believe that it is reasonable for the licensee to be able to submit an application to ASIC for consideration. It might be that there should be a maximum period of extension that should be defined.

15. Is six months an appropriate initial time frame?

The AFA supports a six month time limit for the commencement of operations.

Position 5 – Align Consequences for Making False or Misleading Statements in Documents Provided to ASIC in the AFS and Credit Contexts

16. Should the consequences for making false or misleading statements in documents provided to ASIC in the AFS and credit contexts be aligned?

The AFA supports a consistent approach between the AFS regime and the Credit regime. Given the similarities between the two regimes and the fact that a number of entities are licenced under both regimes, consistency would seem to be appropriate.

17. Should the same penalties, including a combination of criminal and civil penalties, apply?

The AFA is supportive of a strong penalty for false or misleading statements, suggesting that the severity should be steeper where it can be proved that it is deliberately false or misleading. In terms of the scale of penalties, we note that some of the penalties such as 2,000 penalty units can be extremely costly, particularly for a small to medium sized business. We question whether the penalties should be that large for smaller entities.

Position 6 – Making a Materially False or Misleading Statements in a License Application Should be a Specific Basis for Refusing to Grant the Licence

18. Should ASIC be able to refuse to grant an AFS or credit licence if the application or documents accompanying the licence application are false or materially misleading?

The AFA supports ASIC having the power to refuse to grant an AFS or Credit licence where the application included materially false or misleading information. We note that the applicant will be able to present their case at a hearing as set out in Section 913B(5) of the Corporations Act.

We note the different wording used in the position statement and question 18 as to whether it is “materially false or misleading” or “false and materially misleading”. It is our view that it would need to be either false in a material sense or materially misleading. We believe that this needs to be clearly defined as we would not be supportive of a licence being rejected as a result of an unintentional mistake that had no material impact upon the application.

Position 7 – Introduce an Express Obligation Requiring Applicants to Confirm that there have been no Material Changes to Information Given in the Application Before the Licence is Granted

19. Should applicants seeking an AFS or credit licence or to vary an existing licence have an express obligation to confirm, before the licence is granted, that there have been no material changes in the applicant’s circumstances that would render statements or information in the application false or materially misleading?

We note that the probability of information becoming out of date will increase the longer it takes to finalise the application or variation. It would be preferable for the application/variation to be processed in the shortest time possible, however it is appreciated that this is not always possible where important information is missing.

It would make sense that the applicant should have an obligation to confirm that there has been no material change to the applicant’s circumstances prior to the formal approval of the

application/variation. We believe that it is important that there is some clarity with respect to what would constitute a material change.

20. Alternatively, should applicants be required to notify ASIC of material changes in the applicant’s circumstances on an ongoing basis between the time of lodging an application for a licence or licence variation and ASIC making a decision with respect to the application?

Once again this depends upon how long it takes to process the application and at what point the change arises and how material it is. For example, if a key person, who was critical to the application, announces their resignation soon after the application was submitted, then it would make best sense for the applicant to advise ASIC immediately. This would not allow them an option to develop an alternative solution, and might sensibly result in the application being put on hold until an alternative solution can be developed. The applicant should then have the ability and a reasonable timeframe to change the application to address the required changes.

In our opinion this is not an alternative, but an addition. The applicant should both confirm at the time of finalisation of the application that nothing material has changed and should also have an obligation to notify ASIC of any significant change that arises whilst the application is in the process of being assessed. Once again, we believe that it is important that there is some clarity with respect to what would constitute a material change.

Concluding Remarks

The AFA is strongly committed to supporting legislative measures that ensure that only suitable people and entities are able to operate in the financial services industry and the financial advice sector in particular and is therefore welcoming of steps that will prevent unsuitable people and entities from joining the sector. We also welcome sensible amendments that will facilitate the removal of unsuitable people from the financial advice sector. We are also supportive of sensible alignment of the AFSL and Credit licensing regimes, noting that there will be circumstances where differences are justified.

The AFA welcomes further consultation with the Taskforce should it require clarification of anything in this submission. If required, please contact us on 02 9267 4003.

Yours faithfully



Philip Kewin
Chief Executive Officer
Association of Financial Advisers Ltd