



## CENTRE FOR LAW, MARKETS AND REGULATION

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**Submission regarding consultation on recommendations of the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into proposals to lift the professional, ethical and education standards in the financial services industry**

Professor O'Brien is the Founding Director of the Centre for Law Markets and Regulation (CLMR) within the Faculty of Law, UNSW Australia, and Dr. Gilligan is a Senior Research Fellow at the CLMR. Please find below our joint submission to the Australian Government's consultation process on recommendations of the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into proposals to lift the professional, ethical and education standards in the financial services industry.

We hope that this submission is of assistance to the Australian Government. If you require further information please do not hesitate to contact us.

Yours sincerely

Professor Justin O'Brien and Dr. George Gilligan

## Submission regarding consultation on recommendations of the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into proposals to lift the professional, ethical and education standards in the financial services industry

### Background

1. Professor O'Brien and Dr. Gilligan made an initial submission on 4 September 2014 to the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into proposals to lift the professional, ethical and education standards in the financial services industry. Dr. Gilligan appeared before the Committee at its Public Hearing in Melbourne on Monday 13 October 2014. Following his evidence Dr. Gilligan received a question on notice from the Committee to provide further information to the Committee on the subject of ethical self-reporting. Professor O'Brien and Dr. Gilligan submitted that further information to the Committee on 3 November 2014.
2. We welcome the reports, and support many of the recommendations, of two recent important inquiries, the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into proposals to lift the professional, ethical and education standards in the financial services industry<sup>1</sup> (PJC) and the Financial System Inquiry<sup>2</sup> (FSI). We commend the Australian Government on its March 2015 Consultation Paper on the PJC's recommendations and limit our response to questions 1.1 and 2.2 of that Consultation Paper.

**Recommendation One: There needs to be further tightening of licensing requirements so that the licence under which an individual gives financial advice is tied to that individual and their performance history, rather than them being sheltered under the licence of a large institution.**

**Recommendation Two: Mandatory ongoing ethical reporting should be integrated into the licensing requirements of all individuals and organisations involved in the provision of financial advice.**

3. In our submission we link Question 1.1, "What impact would the introduction of the PJC model have on the structure of the financial advice industry?" and Question 2.2, "Should licensees maintain a legal obligation to ensure advisers meet relevant training and competency standards?" We believe that the introduction of the PJC model **will** have an overall positive impact on the financial advice industry, but the proposed obligations on licensees regarding the training and competency standards for advisers are **not** high enough.
4. We believe that there is an imbalance between the privileged position that participation in the financial sector allows through the mechanism of the **licence**—which is a **gift of the state**—and what might be termed the **civic duties and obligations that potential carries with it**. We think the balance has shifted too far towards an almost automatic expectation of assuming a licence. The PJC recommendations go some way towards redressing this imbalance but not far enough. The negative effects of past and current imbalances have been compounded because of the organisational context—many of the financial planners and advisers in Australia are employed by large organisations in which vertical sales chains are common, so there is a diminution of accountability and transparency in relation to the activities of individuals who are selling products or recommending products to consumers.

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<sup>1</sup> Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into proposals to lift the professional, ethical and education standards in the financial services industry*, December 2014, available at [www.apf.gov.au](http://www.apf.gov.au).

<sup>2</sup> Financial System Inquiry, *Final Report*, November 2014, available at [www.fsi.gov.au](http://www.fsi.gov.au).

5. It is our view that **that accountability needs to be sheeted throughout an organization up to its highest levels.** The **analogy of audit** can be informative in this instance as responsibility for audit integrity is cemented at both board and senior management ranks. Why should there not be a similar regulatory infrastructure within financial institutions in terms of financial advice as there is with audit? Audit is supposedly a fair and true reflection of the financial health or otherwise of any company. **Why shouldn't the financial advice that is handled by an individual be a fair and true reflection of the financial health of that advice?** Past experience indicates that such an innovation is unlikely to emanate from the industry without substantive pressure from the state.
6. **The lever of the licence as a gift of the state and increased stringency requirements in order to maintain licensed status could be the regulatory key to unlock the door to delivering truth in financial advice in Australia.** If organisations involved in the provision of financial advice are deflecting or ignoring the harmful behaviour of some of the individuals in subsidiaries that they operate, then that surely is an indication that the fulcrum needs to be pulled back further to the centre, in order to achieve greater balance and yet still have organisations generating substantial profit for their stakeholders, **including clients who are the recipients of financial advice.**
7. We believe that **mandatory ongoing ethical self-reporting** can **raise levels of both specific and general deterrence against wrongdoing** in the finance sector and help to **sheet individual accountability** within what to date has been an ambiguous system that to an extent has nurtured ambivalence about ethical and other behavioural standards. Ongoing mandatory ethical self-reporting would make a **substantial contribution to the evidential database** thereby facilitating corporate and regulatory oversight.
8. Mandatory ongoing ethical self-reporting as part of the obligations of holding a licence can **support the individual in their efforts to be compliant**, especially in those contexts where organisational priorities may stimulate them to be ethically flexible, morally numb or downright non-compliant. Similarly, the increased evidentiary detail and subsequent transparency and accountability, can **act as powerful stimuli for organisations** involved in the provision of financial services and products to construct not only appropriate product lines, sales and marketing processes, but also incentive regimes that are less short-term and align finance sector priorities more closely with civic society goals.