MinterEllison LAWYERS

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AURORA PLACE 88 PHILLIP STREET SYDNEY
GPO BOX 521 SYDNEY NSW 2001 AUSTRALIA
DX 117 SYDNEY www.minterellison.com
TELEPHONE +61 2 9921 8888 FACSIMILE +61 2 9921 8123

BY EMAIL: futureofadvice@treasury.gov.au

General Manager
Retail Investor Division
The Treasury
Langton Crescent
PARKES ACT 2600

Attention: Richard Sandlant

Dear Sir/Madam

Exposure Draft - Corporations Amendment (Future of Financial Advice) Bill 2011

Minter Ellison is a full service commercial law firm which provides legal services to clients in a variety of industries and sectors, including the financial services industry and the wealth management sector of that industry. Our clients include fund managers, insurance companies, investment platform operators and other administrators and financial planning dealer groups. As a service provider to the industry (and consumers of the products and services offered by that industry), we are well placed to provide a balanced view on the potential consequences of the draft FOFA legislation.

We appreciate the opportunity to provide comments on the draft bill. Our comments are provided in two sections:

(a) set out below in this letter are high level comments on the likely impact on industry and consumers of some of the proposed legislative provisions; and

(b) the schedule to this letter includes a table of more detailed comments on certain provisions.

Best interests duty

We believe that the role and responsibilities of retail financial advisers does need clarification. It is challenging to develop a higher level of duty on financial advisers which is in keeping with the duties the law imposes on members of other professions (e.g. solicitors and accountants), but which also recognises, and which can be accommodated by, the licensing framework under the current statute. The current licensing framework is based on a premise which is inconsistent with accepted principles of equity and the law of agency, namely that a fiduciary or agent (whether or not also a fiduciary) can not serve two principals at the same time in relation to the same subject matter. Yet, the relevant provisions of Part 7.6 of the Corporations Act basically require representatives (whether authorised representatives or employee representatives) to act on behalf of their appointing licensees, whilst allowing those representatives to hold themselves out as client advisers.

While the current licensing system has limitations (notably when trying to scope and superimpose a higher duty like the proposed statutory 'best interests' duty), we do not advocate wholesale change. We believe that the benefits of having such a licensing regime (e.g. support for advisers by substantial and reputable licensees; the flexibility, client alignment and entrepreneurship of separately owned adviser practices; the growth of diffuse advice networks covering much of Australia; and enhanced product and service innovation) outweigh the disadvantages.

Turning to the proposed 'best interests' duty in the draft legislation, we understand that, in the wake of the failure of Storm Financial, the Government has determined it necessary to introduce the statutory equivalent of a fiduciary duty. The difficulty with this approach is that the existence of a fiduciary relationship at general law will depend very much on the circumstances of each case unless a particular person is a fiduciary *per se* (e.g. solicitor, medical doctor or trustee). Another issue is that the responsibilities of a fiduciary can not easily be distilled into a bite-sized 'best interests' duty. The responsibilities of fiduciaries are characterised by negative obligations rather than by any positive requirement. For example, the fiduciary must not put themselves in a position where their duty to their principal conflicts with a duty owed to a third party, or where the interests of the principal conflict with their own interests, and they must not make an undisclosed profit out of the principal.

The concern we have with the proposed 'best interests' duty in the draft FOFA legislation is that, rather than clarify the responsibilities of financial advisers, it creates two additional general duties the scope of which is unclear. We would submit that beyond not accepting commissions from product issuers (other than where not prohibited from doing so under the new legislation), giving priority to the interests of the client, and following a rigorous process designed to ensure that the adviser is acting with reasonable care and diligence, there should be no higher duty on a financial adviser in addition to any duty which the law and equity already impose. In other words, we believe that the removal of commissions, the requirement to give priority to the client's interests and any existing general law duties cover all the bases adequately.

We submit that the introduction of a vague 'best interests' duty along with a prescriptive list of minimum requirements will merely result in increased litigation, and uncertainty and costs for practitioners and consumers. The proposed introduction of up to '12 steps' as set out in draft Division 2 of Part 7.7A seems to us to be an unnecessary rewriting of the relatively straightforward and flexible reasonable basis for advice requirements in section 945A.

Unless the 'best interests' duty is removed or defined precisely, or some form of reasonable steps defence is included as promised by the Government in the second FOFA paper released on 28 April 2011, we believe that the Government will be missing the opportunity to clarify the role and responsibilities of advisers.

We have provided more detailed commentary on the '12 steps' in the schedule to this letter.

'Opt-in'

The arguments for and against opt-in have been exhaustively played out in the media and elsewhere. We believe that there is merit in the argument that a looming 23 month deadline (if you factor in the minimum 30 day renewal notice requirement) may encourage short-termism where wealth creation needs to be a long-term exercise.

We are also concerned that the proposed approach is an inappropriate intervention into the ability of advisers and clients to agree on the basis on which they deal with each other. This level of regulatory intervention is not found in other professions or retail dealings. It is also inconsistent with the Government's avowed intent to remove red tape and to encourage the development of a financial planning profession.

ASIC powers

We support the proposals to expand ASIC's administrative licensing and banning powers, subject to certain technical issues which we have raised in the schedule to this letter.

Yours faithfully
MINTER ELLISON

Christopher Brown
Partner

Richard Batten
Partner

Contact: Richard Batten Direct phone: +61 2 9921 4712 Direct fax: +61 2 9921 8036
Email: richard.batten@minterellison.com
Our reference:

Exposure Draft - Corporations Amendment (Future of Financial Advice) Bill 2011
Detailed comments

	Section	Subject matter	Issue
'Best interests' duty			
1.	961(6)	Use of technologies to provide low-cost financial advice	It is not clear whether and to what extent the new regime will allow simple personal advice to be provided over the internet. One of the stated objectives of the proposed legislation (per the Minister's 29 August press release) is to "remove the red tape that has prevented low-cost, good quality advice being delivered to millions of Australians". ASIC has also shown it is receptive to alternative means of advice delivery in, for example, its Report on Access to financial advice in Australia (REP 224). It would seem to us that the most effective way of achieving this outcome for Australians who have fairly basic advice requirements is via the internet. The potential for the internet to both deliver low-cost scaled advice to such clients, while serving as a distribution channel for product issuers, has not been fully explored. Our concern is that such low-cost advice channels may become less available as a result of the prescriptive legislative requirements which make scoping advice more difficult and impose obligations requiring the adviser to identify areas where the client needs advice outside the adviser's particular expertise. This would be very difficult for an electronic system to do based on our understanding of current technology.
2.	961A	Licensees acting as authorised representatives	We are unsure what this provision is seeking to achieve. It is not possible for a licensee to act as an authorised representative of another licensee when giving personal advice.
3.	961B	General law obligations	Given the extensive prescription proposed in the draft legislation, we believe that it would be appropriate to override general law obligations. Potentially, the proposed obligations will cover the entire field in any case. Retaining the existing law in this area therefore simply adds to cost and

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			uncertainty.
4.	961C(1)	'Best interests' duty	We are uncomfortable with the combination of a vague, principles-based 'best interests' duty and the more prescriptive approach set out in draft s.961C(2). The '12 steps' set out in s.961C(2) and other provisions of Division 2 suggest that the general duty is really a duty of skill and care. If so, then it is unclear why such a duty should be imposed on financial advisers and no other profession (as opposed to officeholders, eg. directors and certain trustees). We believe that it is critical to provide a precise definition of 'best interests' if this duty is to be retained as this term has not been judicially considered in an advice context and therefore would have a very uncertain meaning. The contexts in which it is currently used generally relate to officeholders who need to identify the interests of a group rather than the interests of an individual and there is a risk, given the separation of this duty from the duty to give priority to client interests, that the 'best interests' duty could be interpreted as a duty to give 'best advice'. In any case, there will be considerable uncertainty in the industry and for consumers about the extent and requirements of this duty until it has been judicially considered which may not occur for many years. It is also important for there to be a reasonable steps defence as promised by the Government in the original proposals. We believe that it is unsatisfactory that s.961C(2) is a minimum requirement. If included, it should operate as an exhaustive statement of what an adviser needs to do to comply with the 'best interests' duty. On the other hand if a general 'best interests' duty is to be retained, then we believe that the '12 steps' in s.961C(2) and other provisions in Division 2 would operate better as guidance on how to comply with the duty to avoid the problems posed by prescriptive requirements.

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5.	961C(2)	'Subject matter' of advice	What is meant by "subject matter of advice"? Is this separate from needs and/or objectives? Is it the scope of the advice or the instructions provided by the client? For instance, would the subject matter be expressed as "advice on achieving a long term savings and investment goal" or would it more narrowly be "advice in relation to equity investments"? The need for clarity is important given the requirement to look beyond the subject matter in certain situations under s.961C(2)(d).
6.	961C(1)(a), (b), (c)	Scoping of advice	These provisions seem to preclude scoped or scaled advice because of the following: • paragraph (a) references circumstances disclosed by the client without referencing whether they are relevant to the advice to be provided; • paragraph (b) states that the subject matter of advice is as requested by the client rather than agreed between the client and the adviser – it is critical that the scope be agreed to ensure that the adviser is able to advise within their area of expertise and to ensure that the adviser is not required to give more advice than the client actually wants; the client's original request may be more than they need or are prepared to pay for; • paragraph (c) requires the adviser to obtain "complete and accurate information" without referencing whether the information is relevant to the advice to be provided or limiting inquiries to reasonable inquiries as we believe would be appropriate.
7.	961C(2)(d), (f)	Scaled advice	Further to our comments above, if "subject matter" has the more expansive meaning, then this will undermine the adviser's ability to limit the work they undertake and their consideration to the limited/scaled advice which the client has requested. In other words, if advisers feel compelled to advise more broadly in order to comply with an actual or perceived requirement under the Act, then this will go against the need to provide more focussed advice. This will inevitably result in the cost of advice increasing and deter clients from using

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			advisers. There is also no limit on the extent of these requirements. It appears that a financial adviser must have competence well beyond any narrow category of products for they may be experts. In fact, their competence has to extend beyond financial products to other products, investments and strategies, such as real estate. This will cause licensees (who are liable for any breach by advisers) to require advisers to undergo additional training and this in turn will increase the cost of advice and reduce the availability of advice other than full financial planning advice.
8.	961C(2)(g)	Investigation by another person	In relation to 'outsourcing' the investigation under s.961C(2)(g)(ii), it is unclear what the role of the adviser is in relation to the investigation undertaken by another person. Is the adviser required to assess whether it is reasonable to rely on that investigation? Does the adviser need to go behind the work done? We believe that it important in any case to provide that only a *reasonable* assessment is required by the adviser. Further, is s.961C(2)(g)(ii) intended to allow for research houses or internal research departments to conduct investigations into individual financial products, or is the intention that shortlisted products be investigated against individual clients' needs and objectives?
9.	961C(2)(h)	Switching and acquiring additional products.	This section should only really apply where a client is being advised to switch from one product to another (ie a substitution situation). Where the client already holds, say, a risk product, and in response to an assessment of the client's new needs and objectives, the adviser recommends investment in a managed fund, it is unclear what the enquiry under paragraph (h) would add beyond the other requirements in s.961C. It is also not clear that the adviser is required to weigh the advantages and disadvantages of acquiring the product. The bias seems to be on retaining existing

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			products which we do not believe is appropriate. The duty for the adviser should simply be to demonstrate that the new product's advantages outweigh the disadvantages of acquiring it.
10.	961C(2)(i)	Judgements to be based on objectives, financial situation and needs of client	For the sake of consistency and certainty, these objectives, financial situation and needs should be limited to those that are disclosed by the client in instructions under s.961C(2)(a), as elaborated following any reasonable further inquiry in satisfaction of the requirement under s.961C(2)(c).
11.	961D	Standard of care in enquiring as to client's needs and objectives to scope subject matter of advice	We believe that the standard of care in making this assessment should be the standard one would expect from a reasonable person in the same circumstances as the adviser.
12.	961E	'Reasonable investigation'	To the extent that the Government believes it is necessary to impose prescriptive requirements for providing advice, then s.961E would be more useful to advisers if it set out what does or might constitute a reasonable investigation of a financial product, rather than simply what advisers are not required to do. Such an approach would address the concern that advisers might be made liable for product failures or characteristics which render them unsuitable for clients and which were not reasonably ascertainable by the adviser at the time when the product recommendation was made.
13.	961E(2)	Investigation instructions	This provision is difficult to understand and therefore apply. Is it intended that the adviser should investigate all products in the class or to go outside the APL if instructed by the client? In other words, does this provision override s.961G(3)? We submit that it should not and it should be expressly made subject to s.961G(3).
14.	961G(4)	No product on APL which is suitable	We do not believe that there is any merit in imposing a prescriptive written disclosure requirement in these circumstances. It should be sufficient to simply prohibit an adviser from recommending a product if it does not meet the reasonable needs and objectives of the client.
15.	961H	Resulting advice must be appropriate to client	Given uncertainty around the scope and meaning of the 'best interest's duty (and when it has been satisfied), it is unreasonable to require advisers to base

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			their final assessment of whether advice is appropriate on whether or not they have satisfied the best interests requirement. This is even more so unreasonable given the possible imposition of civil penalties on advisers as a result of breach. Separating out this duty from the duty to make reasonable inquiries and undertake reasonable investigations results in a higher duty than that currently required by s.945A. This will make it very difficult for an adviser to scope or limit their advice.
16.	961K, 961L	Priority of client interests	Any fee or other form of remuneration agreed between adviser and client should be carved-out of this clause. That is, the rules of equity allow trustees and other fiduciaries to profit from their position provided that they have the fully informed consent of their principal, beneficiaries etc. Given the duty to give client interests priority is akin to an equitable duty, the right of the adviser to be remunerated with the client's consent should be explicitly recognised. Furthermore, client interests should be defined as interests that the adviser is aware of having complied with his or her other duties under Division 2. Such a definition would also be appropriate for the general 'best interests' duty
17.	961M	Penalties – licensee	We note that although a licensee is only required to take reasonable steps to ensure compliance with Division 2, a licensee is liable for each breach of the Division by an adviser whether or not reasonable steps are taken. We submit that s.961M should be subject to a reasonable steps defence.
18.	961S	Penalties – authorised representative	We also note that, unlike employees of licensees, employed authorised representatives are liable under this provision. We submit that employees should not be subject to civil penalty prosecution whether they are employed by a licensee (when they do not need to be an authorised representative) or by a corporate authorised representative (when they do).
Opt-in			
19.	962(3)	Application to existing clients	We believe that the thrust of this grandfathering provision is appropriate. However, it should be amended to make

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			certain that it applies whenever an adviser transfers client to another adviser after 1 July 2012 which we understand to be the intent of the provision as stated in paragraph 2.39 of the Explanatory Memorandum and the Minister's statement. We also believe that it would be helpful if an additional provision is added to make it clear that the grandfathering applies even if the authorised representative becomes an authorised representative of a new licensee (as we believe is intended by the provisions).
20.	962A(1)(a)	Application to beyond personal advice	We do not believe that the Division 3 requirements should apply to general advice. We are also concerned that the broad nature of an 'arrangement' (defined in s.761A) means that if an arrangement includes other elements, such as administration or dealing services, then the entire arrangement could become subject to the requirements in Division 3 which we do not believe is intended. The provisions should be amended to ensure that this does not occur.
21.	962B(2)	Ability to recover deferred plan fees and the like	It remains likely that advisers will continue to allow clients to defer the cost of initial advice (which remains unaffordable for many clients) by spreading it across the early years of a retainer. This section should be clarified to add a third limb exception which makes clear that any termination payment which reasonably represents an unpaid deferred initial advice fee should also be recoverable. This may or may not already be covered in (a), but there is a practical concern in combining an ongoing fee arrangement and a deferred initial fee arrangement in a single agreement. When does liability accrue? What happens where a planner undertakes work in preparation to provide advice to the client but the client terminates before the advice can be provided?
22.	962C(3)	Ability (or otherwise) to waive past breaches	As currently drafted, any failure to comply with s.962D (whether a major breach or an immaterial, technical oversight) might

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			expose the adviser to an obligation to refund fees which have otherwise been earned. It is not inconceivable that a client, suddenly unhappy with the performance of their investment portfolio, might seek to claw back fees paid to their adviser for a prior period where there has been a technical breach of the fee disclosure requirement. Presumably, in this situation, it should be open to the adviser to make the breach good. A further unintended consequence of the drafting in this section may be that a client, several years after the event (and after opting back into the service several times) is able to recoup all fees paid under the ongoing fee arrangement since the relevant breach. Presumably, a fairer approach would be to limit the refund up to the next renewal date. Opt-in should act as a waiver of the client's right to demand a refund of past fees for non-disclosure under 962D or a previous opt-in breach. Clearly, this would be without prejudice to the operation of any other remedy as a result of the adviser's failure to comply with the legislative requirement. There would also be a problem for an adviser/licensee who has acquired an ongoing fee arrangement if the seller committed a breach. Not only would the seller be required to refund all fees after the breach, but the acquiring adviser/licensee would also be required to refund their fees even though they did not commit the breach.
23.	962D, 962F	Timing of fee disclosure statement	The problem with requiring the fee disclosure statement to be given 30 days in advance is that an adviser cannot simply hand it over in an annual review unless meetings are held no less frequently than every 11 months. As advisers will need to ensure compliance with the obligation, they will need to send notices out before the 30 day period so in fact the disclosure period becomes less than 11 months and as the next statement is due on the anniversary of the date it is given (which will not be known to the adviser in any case) the disclosure date cannot effectively be set by the adviser.

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			We recommend giving the adviser the flexibility to set a disclosure date and period provided no period is ever longer than 12 months.
24.	962E	Prescription regarding services provided	It is unclear to us why clients need reminding of the services which they are entitled to receive during the periods in review and preview. Presumably, if a client is unhappy with the service which it has received, it can elect to opt-out or not opt back in when required to consider doing so. In the worst case scenario, if an adviser has not performed the services which he or she has contracted to perform, then he or she will be in breach of contract and a number of courses of action are open to the aggrieved client. We are firmly of the view that the Government should not be promoting legislation with this level of prescription, and that it should instead by working with peak industry bodies to ensure that appropriate professional standards are set which provide clear guidance on what should and should not be included in ongoing fee arrangements. Another problem with the provision is that it requires fees and services to be disclosed for the period before the period has ended. An adviser cannot know what services will necessarily be provided in the last 30 or more days of the period and more importantly where fees are calculated by reference to the value of the investment portfolio the adviser cannot determine how much the fees will be for the period. We therefore believe that the disclosure period should be for a period that ends before the requirement to provide the disclosure statement, eg. the disclosure statement should be required to be given within say 90 days after the end of the disclosure period. It is also unnecessary for advisers to be required to state the services they anticipate providing in addition to those the client is entitled to. Finally, we recommend that 'details' be

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			changed to 'information about' in paragrahs (c), (d), (e) and (f) to ensure that advisers have some flexibility in the level of detail included in the statement. We note that there is the power to prescribe details in the regulations if required.
25.	962H	Renewal notice period	While the first renewal notice period is reasonable (subject to our comments below about the ability to reset the period), subsequent renewal periods are determined by renewal by the client. This means that each time the client renews prior to the end of the renewal period, the next renewal period starts on that date, rather than on the end of the current renewal period. Renewal periods therefore will be progressively less than 2 years. We believe that advisers should be able to set and reset the renewal period in line with the disclosure period, provided no renewal period is longer than 2 years. We also note that because renewal notices need to be given at least 30 days before renewal, they will not be able to be addressed during the annual review meeting unless annual review meetings are held more often than every 12 months. We also note that it may be difficult to ascertain when an ongoing fee arrangement is entered into. We therefore suggest that this should be defined by the date any written agreement for the ongoing fee arrangement is entered into where there is a written agreement. Although we do not believe it is appropriate to require a written agreement in every instance, this approach may encourage advisers to enter into written agreements with clients.
26.	962D(1) and 962E(1)	Giving/sending notices and statements	We note that disclosure statements need to be 'given' to clients and renewal notices need to be 'sent' to clients. We submit that the same term should be used and that the definition of 'given' in s.940C should apply to Part 7.7A as well as Part 7.7.
27.	962K	Renewal notice	We note that clients are required to opt-in in writing. We acknowledge the need for appropriate evidence to be obtained of the client's decision. However, we believe that it should be possible for the client to opt-in

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			over the telephone if it is recorded or confirmed to the client in writing.
28.	962L	Civil penalty	We submit that there should be a reasonable steps defence to this obligation where the fee recipient takes reasonable steps to cease payments being received (eg. by telling the relevant platform operator) and takes reasonable steps to refund any overpayments (eg. by sending the amount to the client's last known address).
ASIC powers			
29.	920A(1)(da)	Competence to provide a financial service	This power enables ASIC to ban a person where they are not competent to provide any financial service whether or not the person represents they have any expertise in the particular service or is authorised to provide it. The power should be limited to financial services provided by the person.
30.	920A(1)(f), (g), (h)	Breach of financial services law	This power enables ASIC to ban a person where they are likely to breach any financial services law, whether the breach is significant or not. The power should be limited to significant breaches consistent with the breach reporting obligation in s.912D.