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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

CORPORATIONS AMENDMENT (FUTURE OF FINANCIAL ADVICE) BILL 2011

EXPLANATORY MEMORANDUM

(Circulated by the authority of the
Assistant Treasurer and Minister for Financial Services and Superannuation, the Hon
Bill Shorten MP.)

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

Abbreviation	***Definition***
AAT	Administrative Appeals Tribunal
ASIC	Australian Securities and Investments Commission
Bill	Corporations Amendment (Future of Financial Advice) Bill 2011
Corporations Act	*Corporations Act 2001*
FOFA	Future of Financial Advice
Licence	Australian Financial Services Licence
Licensee	Holder of an Australian Financial Services License
PJC Inquiry	*Inquiry into Financial Products and Services in Australia by the Parliamentary Joint Committee on Corporations and Financial Services (2009)*

General outline and financial impact

Outline

On 26 April 2010, the then Minister for Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen MP, announced the Future of Financial Advice (FOFA) reforms.

The FOFA reforms represent the Government's response to the 2009 *Inquiry into Financial Products and Services in Australia by the Parliamentary Joint Committee on Corporations and Financial Services* (PJC Inquiry), which considered a variety of issues associated with corporate collapses, including Storm Financial and Opes Prime.

The Corporations Amendment (Future of Financial Advice) Bill 2011 (the Bill) implements the FOFA reforms. The reforms focus on the framework for the provision of financial advice. The underlying objective of the reforms is to improve the quality of financial advice while building trust and confidence in the financial planning industry through enhanced standards which align the interests of the adviser with the client and reduce conflicts of interest. The reforms also focus on facilitating access to financial advice, through the provision of simple or limited advice. To this end, the Bill sets up a framework with the following features:

- a best interests obligation for financial advisers requiring them to act in the best interests of their clients and to place the interests of their clients ahead of their own when providing personal advice to retail clients (best interests obligation);
- a requirement for providers of financial advice to obtain client agreement to ongoing advice fees and enhanced disclosure of fees and services associated with ongoing fees (charging ongoing fees to clients);
- enhancement of the ability of the Australian Securities and Investments Commission (ASIC) to supervise the financial services industry through changes to its licensing and banning powers.

The reforms also include a ban on conflicted remuneration, including commissions, volume payments and soft-dollar benefits. These measures will be exposed for public consultation at a later date.

Date of effect: The reforms commence on 1 July 2012.

Proposal announced: On 26 April 2010, the then Minister for Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen MP, announced the Future of Financial Advice (FOFA) reforms. On 28 April 2011, further detail on the operation of the FOFA reforms was announced by the Assistant Treasurer and Minister for Financial Services and Superannuation, the Hon Bill Shorten MP.

Financial impact: This Bill has no significant financial impact on Commonwealth expenditure or revenue.

Chapter 1
Best interests obligations

Outline of chapter

1.1 Schedule 1 to the Corporations Amendment (Future of Financial Advice) Bill 2011 (the Bill) amends the *Corporations Act 2001* (Corporations Act) to require persons providing personal advice to retail clients to act in the best interests of the clients and to give priority to the interests of the client. Schedule 1 also amends existing regulatory requirements so they apply more directly to individual advisers. ***[Schedule 1, item 13, divisions 1 and 2].***

Context of amendments

1.1 Under the structure of the financial advice industry in Australia, individuals involved in the provision of personal advice to retail clients may receive remuneration from parties other than the client. The most common example of such a form of non-client remuneration is a commission paid from a product provider to a financial adviser in situations when a client of the adviser acquires a product from the product issuer.

1.2 The existing Corporations Act does not prohibit such non-client remuneration to be made and implicitly recognises its ability to influence the provision of financial advice to clients. Given this, the Corporations Act requires licensees to have adequate arrangements in place to manage conflicts of interests (section 912A(1)(aa)) and for information about remuneration and interests that are capable of influencing the advice to be disclosed to clients through the statement of advice (section 947B when the statement of advice is provided by licensees and section 947C when the statement of advice is provided by the authorised representative). In addition, the Corporations Act places an obligation on licensees and authorised representatives to ensure that the advice is appropriate for the client (section 945A).

1.3 However, there are no requirements in the Corporations Act that require a financial adviser to act in the best interests of the client or to give priority to the interests of the client when providing advice. This meant that as long as the advice met the standard of being appropriate and the necessary disclosures were made, the adviser was not prohibited by the Act from giving advice that benefited the adviser.

1.4 In its report on Financial Products and Services in Australia, the Parliamentary Joint Committee on Corporations and Financial Services (PJC) recommended a “duty on financial advisers requiring them to place their clients’ interests ahead of their own”. Further, the PJC noted “[T]here is no reason why advisers should not be required to meet this professional standard, nor is there any justification for the current arrangement whereby advisers can provide advice not in their clients’ best interests, yet comply with section 945A of the Corporations Act”.

1.5 In response to this recommendation, the Government announced in April 2010 that it would introduce a statutory duty to require financial advisers to act in the best interests of their clients. The duty would also clarify that in no circumstances is it permissible for advisers to place their own interests ahead of their clients’ interests.

1.6 In addition, the amendments aim to address concerns that the existing regulatory obligations in relation to the provision of financial advice impose requirements on licensees and authorised representatives rather than on the individual providing the advice. In situations where advice was provided that breached these requirements (for example, the advice was inappropriate contrary to section 945A), while action could be taken against the relevant licensee or authorised representative, it was difficult to take action against the individual adviser.

Summary of new law

1.7 The Bill amends the Corporations Act to require individuals who provide personal advice to retail clients to:

- act in the best interests of the client when providing that advice and sets out a number of steps that must be followed in complying with the duty; and

- give priority to the interests of the client in the event of conflict between the interests of the client and the interests of the individual providing the advice, the licensee or the authorised representative (where different).

1.8 In addition, the Bill amends the existing requirements in the Corporations Act to have a reasonable basis for providing advice (section 945A) and to warn clients if the advice is based on incomplete or inaccurate information (section 945B) in order to:

- clarify the relationship between the new best interest obligations and these requirements; and

- impose these requirements on the individual who provides the advice.

1.9 In situations where the obligations imposed have been contravened by an individual adviser, penalties following from that breach will rest with the relevant licensee or authorised representative. The individual adviser who contravened the obligation may face administrative action in the form of a banning order.

1.10 In addition to the obligations directly imposed on individuals who provide personal advice, the amendments impose a direct obligation on the licensee to take reasonable steps to ensure their representatives comply with their obligations.

Comparison of key features of new law and current law

New law	***Current law***
Statutory obligation for individuals who provide personal advice to act in the best interests of client.	There is no existing statutory obligation for individuals who provide personal advice to act in the best interests of clients.
Statutory obligation for individuals who provide personal advice to give priority to the interests of the client in the event of a conflict of interest	There is no existing statutory obligation for individuals who provide personal advice to give priority to the interests of the clients.
Statutory obligation for individuals who provide personal advice to ensure that the advice is appropriate.	Statutory obligation on the licensee or authorised representative to ensure who advice is appropriate.
Statutory obligation for individuals who provide personal advice to warn clients if the advice is based on incomplete or inaccurate information.	Statutory obligation on the licensee or authorised representative to warn clients if the advice is based on incomplete or inaccurate information.
Penalties for breaching obligations to give appropriate advice and warn client rest with the licensee or the authorised representative and are civil in nature.	Penalties for breaching obligations to give appropriate advice and warn client rest with the licensee or the authorised representative and are criminal in nature.
Statutory obligation on licensees to take reasonable steps to ensure their representatives comply with the obligations outlined above.	Statutory obligation on the licensee to take reasonable steps to ensure compliance with the obligation to provide appropriate advice only.

Detailed explanation of new law

Preliminary

1.11 Key terms that are used in Part 7.7A of the Bill are defined. Further discussion of these terms is contained in the relevant parts of this Explanatory Memorandum. It also specifies that it is not possible to contract out of the requirements imposed by Part 7.7A and that the obligations imposed are in addition to any other obligations to which the provider is subject to under any law. ***[Schedule 1, item 13, division 1].***

1.12 The obligations imposed under Division 2 of item 13 apply in relation to personal advice as defined under the Corporations Act. In situations where only general advice is being provided, the obligations under Division 2 will not apply. ***[Schedule 1, item 13, division 2, subsection 961(1)].***

1.13 In addition, the application of the obligations is limited to the provision of advice to retail clients. This is consistent with the broader Future of Financial Advice reforms where the focus is on advice to retail clients given the need to ensure a higher standard of consumer protection for retail clients. Financial advice to wholesale clients is not covered by the obligations. ***[Schedule 1, item 13, division 2, subsection 961(1)].***

1.14 The obligations under Division 2 are intended to directly apply to the individual who provides the advice. This individual is referred to in the Division as the 'provider'. Placing obligations directly on the individual is a shift from many of the existing provisions in the Corporations Act where obligations have been imposed at the level of the licensee or the authorised representative. ***[Schedule 1, item 13, division 2, subsection 961(2)].***

1.15 This shift in focus to the individual facilitates administrative action to stop individual advisers who give poor quality advice from providing advice in the future (for example, by use of banning orders). This outcome is more difficult to achieve in situations where the obligations are imposed only at the level of the licensee or the authorised representative. The shift also gives individual advisers a clear standard for them to meet in providing advice. Any penalties flowing from the breach of an obligation will continue to flow through to the licensee or authorised representative rather than the individual adviser (unless that individual is also the licensee or authorised representative).

1.16 In situations where two or more individuals provide the advice, the obligations imposed under Division 2 will apply to both individuals. This is to avoid any uncertainty in how the obligations apply in situations where multiple individuals provide the advice. ***[Schedule 1, item 13, division 2, subsection 961(3)].***

1.17 Where it is not reasonably possible to identify the individual who provides the advice, the obligations will flow onto the person that provides the advice. This will be a licensee or authorised representative of a licensee who may be structured as a corporate entity. ***[Schedule 1, item 13, division 2, subsection 961(5)].***

1.18 The reforms are also designed to take into account the growing use of computer programs to deliver advice to clients. In such cases, often no person, whether individual or artificial, can be said to provide each individual piece of advice. In this situation, the person that offers the advice through the computer program is subject to the obligations imposed in the Division. This person will need to ensure that the computer program is able to operate in a manner that complies with the obligations imposed through Division 2. ***[Schedule 1, item 13, division 2, subsection 961(6)].***

1.19 In the limited situations where a licensee is providing advice as an authorised representative of another licensee, for the purposes of item 13, the licensee that provided the advice is considered to do this in their capacity as an authorised representative (not a licensee) and should be treated accordingly. This is aimed at clarifying the situation where the licensee is acting under a binder in accordance with section 916E of the existing Corporations Act. ***[Schedule 1, item 13, division 2, section 961A].***

Act in the best interests of the client

1.20 Subdivision B, division 2 of Schedule 1 establishes the framework for the obligation to act in the best interests of the client. ***[Schedule 1, item 13, division 2, subdivision B].***

1.21 There is a general obligation on providers of advice to act in the best interests of the client. ***[Schedule 1, item 13, division 2, subsection 961C(1)].*** Further detail is specified on some of the steps that will need to be taken by providers of advice in meeting the general obligation. These steps have been imposed based on the specific conditions under which advisers currently operate. This approach is needed given the broad nature of a best interests obligation.

1.22 The principle guiding the application of the best interests obligation is that meeting the objectives, financial situation and needs of the client must be the paramount consideration when providing advice. This principle is embedded in the framework for the best interests obligation.

1.23 There are steps that providers must take in acting in the best interests of the client. These steps are not exhaustive, and are not intended to operate as a checklist for compliance with the best interest obligation. This is because it is not possible in advance for the legislation to address the broad range of financial advice relationships and situations. However, they operate to provide an indication of what, as a minimum, is expected of financial advisers in order to be considered to have acted in the best interests of the client. In addition, they should guide advisers as to the nature of action required under the best interests obligation. ***[Schedule 1, item 13, division 2, subsection 961C(2)].***

1.24 Consistent with the principle outlined above, the starting point is for the provider to identify the objectives, financial situation and needs of the client as disclosed to the provider through the client's instructions and the subject matter of the advice requested by the client. ***[Schedule 1, item 13, division 2, paragraphs 961C(2)(a) and (b)].***

1.25 However, the provider cannot solely rely on the instructions from the client, but is also obligated to make further inquiries in situations where it is reasonably apparent that the information provided by the client is incomplete for the purposes of providing the advice on the subject matter requested or is inaccurate. The information only needs to be complete in relation to the subject matter of the advice. This means that it is not necessary for providers to obtain every piece of information possible about the client, but only information that is necessary for the subject matter of the advice. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(c)].***

1.26 In addition, if it is reasonably apparent to the provider that the client's objectives and needs could be better achieved through the provision of advice on another subject matter, the provider must advise the client of this in writing. This could be contained in the statement of advice that is provided to the client. However, a provider will need to raise this earlier if it affects the substance of the advice given to the client. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(d)].***

1.27 The test for what is reasonably apparent is determined by reference to what would be apparent to a person with a reasonable level of expertise in the subject matter of the advice. This is an objective test based on the specific subject matter of the advice in question. This means that the test is of a higher standard when the subject matter of the advice is highly complex and technical in nature. ***[Schedule 1, item 13, division 2, section 961D].***

1.28 If the provider does not have the expertise to provide the advice requested by the client, the adviser must decline to provide that advice. In most cases, as long as the provider is competent for the purposes of the Corporations Act to provide advice for that class of financial product, the provider would satisfy this requirement. However, in situation where the client requests advice on a particularly technical or complex aspect of the financial product, the provider may not have the expertise to provide this advice even though they are generally competent to provide advice about that class of product. In this situation, in order to act in the client's best interests, the provider should decline to provide the advice. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(e)].***

1.29 These requirements are designed to accommodate the provision of limited advice (also referred to as 'scaled advice') that only looks at a specific issue (for example, single issue advice on retirement planning) and 'holistic' advice that looks at all the financial circumstances of the client. In situations where limited advice has been requested by the client the adviser is able to tailor the information they obtain about the client solely to what is necessary to provide that form of advice. However, the adviser is required to exercise professional judgement and advise the client if they believe advice on another subject matter could better meet the client's needs and objectives. This reflects the fact that retail clients may not always know what type of advice will meet their needs and objectives.

1.30 There are also obligations dealing with the selection of financial products for the client. Under these obligations, the provider must not limit themselves to only considering financial products. Rather, the provider must consider the needs and objectives of the client and make an assessment about whether these needs and objectives can be satisfied through means other than the acquisition of financial products. This step will be most relevant in situations when the adviser is formulating broad, strategic advice. In cases where the needs and objectives of the client relate to a specific aspect of a financial product, only a limited assessment is required. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(f)].***

1.31 In relation to the assessment of financial products, there must be a reasonable investigation into the products of which the provider is aware that might achieve the objectives and needs of the client. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(g)].*** This does not require an investigation into every product that is available on the market given that in many cases this would be impractical and costly. ***[Schedule 1, item 13, division 2, section 961E].*** In situations where the range of products that a provider can consider is limited by the imposition of an approved product list, the provider may still be able to comply with the reasonable investigation obligation even though they limit their investigation to the products on the list, but they must not recommend a product on the list if it does not meet the needs and objectives of the client. ***[Schedule 1, item 13, division 2, section 961G].***

1.32 As part of selecting a financial product for the client, the provider must assess the advantages and disadvantages of the client acquiring a new product in addition to, or in substitution of, another financial product. One area of particular relevance is situations where the client already owns a financial product that is substantially similar to the product that the provider proposes to recommend for the client. If the provider proposes to recommend to the client that they switch out of their existing product, the provider will also need to comply with the specific disclosure requirement in relation to switching in existing section 947D of the Corporations Act. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(h)].***

1.33 The final step is an obligation for providers to base all judgement in advising clients on the objectives, financial situation and needs of the client. This is an explicit statement of the guiding principle identified above that it is the objectives, financial situation and needs of the client that is of paramount consideration when advising clients. ***[Schedule 1, item 13, division 2, paragraph 961C(2)(i)].***

1.34 There is nothing in the best interest obligation that necessarily prohibits a provider from receiving remuneration other than from the client (for example, a commission from an insurance provider). However, a provider in receipt of this remuneration must ensure they are complying with the steps above and are giving paramount consideration to the objectives, financial situation and needs of the client.

1.35 Particular arrangements are established dealing with the provision of advice solely about basic banking products given by an employee or agent of an Australian ADI. ***[Schedule 1, item 13, division 2, subsection 961C(3)].***

1.36 Basic banking products are: a basic deposit product or non cash payment facility relating to a basic deposit product, a first home saver account, a travellers' cheque facility and other products prescribed by regulation. This provides flexibility to add additional products in the future if it is considered appropriate for them to fall within this arrangement given the constant rate of development in the financial product market. ***[Schedule 1, item 13, division 2, section 961F].***

1.37 When an employee or agent of an Australian ADI provides advice in relation to these products, they are deemed to have complied with the best interests duty obligation if they:

- identify the objectives, financial situation and needs of the client;
- identify the subject matter of the advice; and

- make reasonable enquires to obtain further information if it is reasonably apparent the information provided by the client is incomplete or inaccurate.

[Schedule 1, item 13, division 2, subsection 961C(3)].

1.38 Basic banking products are recognised as being simple in nature and are more widely understood by consumers. This means that there is a lower risk of consumer detriment in relation to the provision of advice on these products. For this reason, a modified best interests obligation was considered to more appropriately balance the benefits to consumers with the compliance costs to providers.

Appropriate advice

1.39 The Bill repeals existing section 945A of the Corporations Act ***[Schedule 1, item 9]*** and introduces provisions dealing with appropriate advice which also take account of the best interest obligations. ***[Schedule 1,item 13, division 2, section 961H].***

1.40 In contrast with existing section 945A, the provision does not contain the process related elements in paragraphs 945A(1)(a) and (b) that have now been incorporated into the steps of the best interest obligation. This has been done to avoid overlap between the provider’s best interest obligations and their obligation to give appropriate advice. Incorporating these process elements into the best interest obligation is not intended lessen the standard of conduct expected of providers. Providers are still expected to follow a ‘know your client’ and ‘know your product’ process in providing advice as it currently required by paragraphs 945A(1)(a) and (b). The steps required by the best interests obligations are more expansive than previously required by existing paragraphs 945A(1)(a) and (b) and would be expected to raise the standard of conduct of advisers.

1.41 The obligation in relation to appropriate advice is placed directly on the person that provides the advice rather than the licensee or authorised representative. Currently only licensees and authorised representatives are required to comply with existing section 945A. As noted previously, this change is necessary to ensure that administrative actions may be taken against providers that fail to comply with the obligation. The penalties resulting from any breach will flow to the relevant licensee or authorised representative. ***[Schedule 1,item 13, division 2, section 961H].***

1.42 The obligation to give appropriate advice takes direct account of the best interest obligations. This means that, regardless of whether the provider has actually complied with their best interest obligations, in testing whether the advice is appropriate it is assumed that the provider has all the knowledge that they would have had if they had complied with the best interest obligation. That is, when a court considers whether advice is appropriate it will have regard to what the provider would have known had they fully complied with the best interests obligation. If the appropriate advice obligation did not make this assumption, providers that did not comply with their best interest obligations may be held to a lower standard than providers that do comply. ***[Schedule 1,item 13, division 2, section 961H].***

Incomplete or inaccurate information

1.43 The Bill repeals existing section 945B of the Corporations Act and introduces an arrangement for disclosure when the provider has incomplete or inaccurate information. The amendments ensure that the disclosure arrangements for incomplete or inaccurate information are consistent with the best interests obligation. ***[Schedule 1, item 13, division 2, section 961J].***

1.44 As with the other provisions, this obligation is imposed directly on the provider. The provider is required to warn the client in situations when, despite making reasonable inquiries as required by the best interests obligation, it is still reasonably apparent that there is information that is either incomplete or inaccurate. ***[Schedule 1, item 13, division 2, section 961J].***

1.45 For the avoidance of doubt, the provision makes it clear that the arrangements for disclosure do not reduces or diminish a provider's best interest obligations, particularly as they relate to the obligation to make reasonable inquiries to obtain complete and accurate information. ***[Schedule 1, item 13, division 2, section 961J].***

Priority of interests

1.46 Providers must give priority to the interests of the client in situations where there is a conflict between the interests of the client and the interests of the provider. ***[Schedule 1, item 13, division 2, section 961K].***

1.47 In addition, the provider must give priority to the interests of the client in situations where the provider knows, or reasonably ought to know, there is a conflict between the interests of the client and the interests of the:

- licensee of whom the provider is a representative; or
- authorised representative of whom the provider is an employee (this is only relevant in situations where the provider is an employee of an authorised representative).

[Schedule 1, item 13, division 2, section 961K].

1.48 The obligation to give priority reinforces the best interest obligations imposed under Subdivision B where the objectives, financial situation and needs of the client must be given paramount consideration by the provider.

1.49 The obligation to give priority to the interests of the client does not mean that the provider can never pursue their own interests or the interests of another party (for example, the licensee). However, the provider will breach this obligation if, in pursuing their own interests or the interests of another party, the provider fails to give priority to the interests of the client if there is a conflict.

1.50 Consistent with the best interest obligations, a provider does not breach the obligation to give priority merely by accepting remuneration from a source other the client (for example, a commission paid by an insurance provider). However, if the provider gives priority to maximising a non-client source of remuneration over the interests of the client, the provider will be held in breach of their obligations.

Licensee obligations

1.51 A licensee must take reasonable steps to ensure that its representatives comply with the obligation relating to acting in the client's interest, giving appropriate advice, warn clients and giving priority to the interests of the client. ***[Schedule 1, item 13, division 2, section 961N].***

1.52 This is consistent with the general obligation imposed on licensees under existing paragraph 912A(1)(ca) of the Corporations Act to take reasonable steps to ensure that its representatives comply with financial services law. It also reflects the current approach adopted for the obligation to give appropriate advice in existing section 945A of the Corporations Act (prior to the passage of the Bill), where the licensee is under an obligation to take reasonable steps to ensure an authorised representative complies with the obligation.

1.53 For example, in the context of the best interest obligations in order to take reasonable steps to ensure compliance, a licensee would be expected to explain to providers that they are obligated not to recommend a product from an approved product list if there is no product that would meet the needs and objectives of the client. Further, licensees will need to take positive steps to ensure that providers do comply with this (for example, through periodic audits of advice given to clients).

1.54 Determining whether this is no product on the approved product list that would need the objectives and needs of the client is be a judgement call for the provider once they meet the client and understand the client's needs and objectives. As the licensee often does not have direct contact with the client, the licensee cannot be expected to make this determination. However, the narrower that the licensee constructs an approved product list, the more likely it is that its providers will not be able to recommend a product from that list. This means that it is in the interests of the licensee to construct approved product lists that are suited to their target client.

Penalties and action for loss or damage

1.55 As discussed previously noted, even though most of the obligations in division 2 are imposed on the individual that provides the advice, the penalties resulting from any breach flow through to the relevant licensee or authorised representative. ***[Schedule 1, item 13, division 2, subdivision F].***

1.56 Breaches of any of the obligations in division result in a civil penalty. This is a de-criminalisation of the existing obligations to give appropriate advice (section 945A) and to warn clients (section 945B). The interrelationship between these obligations and the best interest obligations imposed in this Bill makes it desirable to have consistent penalty arrangements.

1.57 The licensee breaches a civil penalty provision if a representative, other than an authorised representative, breaches the obligation to act in the best interests of the client, the obligation to give appropriate advice, the obligation to warn the client or the obligation to give priority to the interests of the client. ***[Schedule 1, item 13, division 2, section 961M].***

1.58 Licensees do not incur the penalty for breaches by authorised representative as the authorised representative is a separate entity from the licensee and therefore must be accountable for their own actions. As such, similar penalty arrangements to those that apply to licensees also apply to authorised representatives. ***[Schedule 1, item 13, division 2, section 961S].***

1.59 However, given the degree of control that a licensee is potentially able to exercise over its authorised representative, an authorised representatives does not contravene the requirement in situations where the breach resulted from reasonable reliance by the authorised representative on information or material provided by the licensee. The onus is on the authorised representative to establish that the exception applies. This is intended to reflect the existing defence provision available to authorised representatives under section 945A(2) of the Corporations Act. ***[Schedule 1, item 13, division 2, subsection 961S(2)].***

1.60 As noted above, licensees also have a general obligation to take reasonable steps to ensure that their representatives comply with their obligations. The penalty for a licensee that breaches this obligation is the same as the penalty for the obligation that the licensee failed to take reasonable steps to ensure compliance. ***[Schedule 1, item 13, division 2, section 961N].***

1.61 Consistent with the existing section 953B of the Corporations Act, regardless of whether it is the licensee or authorised representative that incurs the penalty for a breach of an obligation, a person that suffers loss or damage resulting from the breach is able to recover that amount from the licensee. This reflects the fact that, under the Corporations Act, it is ultimately the licensee that is accountable for the advice that is provided by one of its representatives and that the Corporation Act imposes an obligation on licensees, not representatives, to have in place arrangements for compensating clients that suffer loss or damage (see existing section 912B). ***[Schedule 1, item 13, division 2, section 961P].***

Application and transitional provisions

1.1 The obligations in Division 2 apply to personal advice provided to a retail client on or after 1 July 2012 whether or not the request for advice was made before this date. ***[Items 2 and 17]***.

Consequential amendments

1.1 Existing Subdivision B of Division 3 of Part 7.7 (that contains sections 945A and 945B) is repealed as the requirements are replaced by sections 961H and 961J of Division 2 of Item 13. ***[Schedule 1, item 9].*** As a consequence, references to the existing section 945B in paragraphs 947B(2)(f) and 947C(2)(g) of the Corporations Act are updated to refer to section 961J (as this will replace section 945B). ***[Schedule 1, items 10 and 11].***

1.2 In addition, references to sections 945A and 945B in paragraph 953B(1)(c) of the existing Corporations Act are removed. Sections 961H and 961J of Division 2 of Item 13 that replace the existing sections 945A and 945B have their own section dealing with actions for loss or damage (in section 961Q of Division 2 of Item 13) and therefore are not included in section 953B. ***[Schedule 1, item 12].***

Chapter 2
Charging ongoing fees to clients

Outline of chapter

2.1 Schedule 1 to the Corporations Amendment (Future of Financial Advice) Bill 2011 (the Bill) amends the *Corporations Act 2001* (Corporations Act) to require financial advisers (persons who hold a license with an authorisation to provide financial product advice or their representatives) to obtain their retail clients' agreement in order to charge them ongoing fees for financial advice. ***[Schedule 1, item 13, division 3]***.

Context of amendments

2.2 Licensees that provide financial product advice to retail clients ('advisers'), are traditionally remunerated differently from other occupations. For example, many advisers have traditionally received commissions from product providers for placing clients with particular products, sometimes paid as a percentage of funds under management. Some commissions are ongoing in nature, forming what are known as 'trail' commissions.

2.3 In situations where the client pays a substantial proportion of the adviser's remuneration directly (known as 'fee for service') it is common for this remuneration to be ongoing in nature. For example, an adviser might charge a client an ongoing annual fee calculated as a percentage of the client's funds under management (known as asset-based fees) or a flat dollar amount. This annual fee generally covers a range of advisory services provided to (or available to) clients. As opposed to professions or other occupations that tend to charge for transactional, one-off services or advice, advisers' remuneration structure is partly reflective of the notion that the benefits of financial advice tend to be realised over the medium to long-term, and therefore remuneration structures tend to reflect the ongoing nature of the adviser/client relationship.

2.4 As a result of this unique remuneration structure, in some situations clients of advisers that pay ongoing fees for financial advice receive little or no service. Of the clients that do receive a service for the fees they are paying, some are unaware of the precise magnitude of those fees (or the fees advisers are receiving from third parties) or they continue paying ongoing fees as a result of their own disengagement. This is despite the fact that most ongoing advice contracts allow a client to 'opt-out' at any time.

2.5 The concept of compulsory renewal of ongoing advice fees, requiring the active renewal by the client to ongoing fees, is designed to protect disengaged clients from paying ongoing financial advice fees where they are receiving little or no service. For those that are not disengaged, the renewal requirement will provide the client with an opportunity to consider whether the service they are receiving equates to value for money.

2.6 Although ongoing fees are disclosed to clients upon engagement of the adviser's services (via the Statement of Advice requirement prescribed under the Corporations Act), there is no ongoing advice fee disclosure requirement. This initial disclosure requirement alone is not a guaranteed safeguard for clients that become disengaged after a number of years of 'passively' paying ongoing advice fees.

Summary of new law

2.7 Where an ongoing financial advice relationship exists between an adviser (the 'fee recipient') and a retail client which involves the charging of an ongoing advice fee (however described), the fee recipient is required to discharge two separate (albeit intertwined) obligations.

1. Disclosure obligation: In order to continue charging an ongoing fee for a period longer than 12 months, the fee recipient must provide a fee disclosure statement to the client outlining fee and service information relevant to the client.

2. Renewal notice obligation: In order to continue charging an ongoing fee for a period longer than 24 months, the fee recipient must provide both a fee disclosure statement and a renewal notice to the client.

2.8 If the fee recipient does not fulfil these obligations, the client is not liable to continue paying the ongoing advice fee past the relevant 12 or 24 month period.

2.9 If, after receiving the renewal notice, the client decides not to renew or fails to respond to the fee recipient's renewal notice, the ongoing fee arrangement terminates. This means that the fee recipient is not obligated to provide ongoing financial advice to the client, and the client is not obligated to continue paying the ongoing fee.

Comparison of key features of new law and current law

New law	*Current law*
In order to charge an ongoing advice fee to a retail client for a period of longer than 12 months, the fee recipient will be required to provide a fee disclosure statement to the client detailing advice fee and service information for both the previous and forthcoming 12 months.	There is no requirement under the current law for advisers/fee recipients to provide ongoing disclosure of advice fees to retail clients.
In order to charge an ongoing advice fee to a retail client for a period of longer than 24 months, the fee recipient will be required to provide a renewal notice and a fee disclosure statement to the client, which will detail advice fee and service information for both the previous and forthcoming 12 months. If the client opts not to renew the advice arrangement with the fee recipient, or does not respond to the renewal notice, the arrangement ceases and an ongoing advice fee can no longer be charged to the retail client.	There is no requirement under the current law for advisers/fee recipients to obtain the agreement of retail clients to continue charging ongoing advice fees.
For ongoing fee arrangements, the client can 'opt-out' or terminate the arrangement at any time.	There is no implied term under the current law that retail clients have the right to opt-out of ongoing financial advice arrangements at any time (however, it is a common practice in the industry to allow clients to opt-out at any time).

Detailed explanation of new law

Application

2.10 The compulsory disclosure and renewal notice obligations will apply to advisers ('fee recipients') in situations where they provide financial product advice to a retail client, and the client pays a fee which does not relate to advice that has already been given. This is so the compulsory disclosure and renewal notice obligations apply to ongoing advice fees, but not to payment plans for advice or services already provided to the client ***[Item 13, division 3, sections 962 and 962A].***

2.11 In practical terms, these obligations are imposed on fee recipients only when an ongoing fee is to be charged for a period longer than 12 months (in the case of the disclosure obligation) or 24 months (in the case of the renewal notice obligation).

Disclosure obligation

2.12 If an ongoing fee arrangement is to remain in place for a period longer than 12 months, the fee recipient is required to provide the client with a fee disclosure statement at least 30 days before the 12 month anniversary of the day the arrangement was entered into ***[Item 13, division 3, sub paragraph 962D(1) and section 962F].***

2.13 The fee disclosure statement will need to contain fee information which has been prescribed to assist the client in ascertaining whether they are receiving a service from their fee recipient commensurate with the ongoing fee that they are paying. Information to be contained in the statement would include fee and service information about the previous and forthcoming 12 months ***[Item 13, division 3, sub sections 962E(1)&(2)].***

2.14 The regulations may provide that certain information is not required to be contained in a fee disclosure statement, or that a more detailed statement of the information required be included. The diversity and complexity of the financial services industry make it necessary for the Minister to be able to exclude certain arrangements that this obligation is not intended to apply to, including arrangements that may not currently exist. This regulation-making power therefore serves several functions, including keeping the legislation up to date, providing commercial certainty quickly and efficiently to industry participants that are unintentionally exposed to the disclosure obligation, and to provide efficacy to the legislation ***[Item 13, division 3, sub section 962E(3)].***

2.15 Where the disclosure obligation coincides with the renewal notice obligation (which applies every 24 months to ongoing fee arrangements) the fee disclosure statement will serve the additional purpose of assisting the client to decide whether they should renew the ongoing fee arrangement.

2.16 If the fee recipient does not comply with the requirement to provide the fee disclosure statement within the specified time, the client is not liable to continue paying the ongoing fee ***[Item 13, Division 3, sub section 962C(1)].*** Any ongoing fee paid after the failure to comply with the disclosure obligation must be refunded on the request of the client. The fact that the client continued paying the ongoing fee after the failure of the fee recipient to comply does not waive the client's right to a refund. This is because often the mechanism by which clients pay for ongoing advice services is through an automated process (for example, by a monthly direct debit from the client's investment) ***[Item 13, division 3, sub sections 962C(2)&(3)].***

2.17 Even where the identity of the fee recipient changes (for example, where a fee recipient sells a 'book' of business to another fee recipient) and it was the previous fee recipient that failed to comply with the fee disclosure obligation, this does not alter the fact that the client is not liable to continue paying the ongoing fee ***[Item 13, division 3, sub section 962C(1)].***

2.18 The regulations may provide that the requirement to provide a fee disclosure statement does not apply in certain situations. The diversity and complexity of the financial services industry make it necessary for the Minister to be able to exclude certain arrangements that this obligation is not intended to apply to, including arrangements that may not currently exist. This regulation-making power therefore serves several functions, including providing a mechanism to help keep the legislation up to date and provide commercial certainty quickly and efficiently to industry participants that are unintentionally exposed to the disclosure obligation, and to provide efficacy to the legislation ***[Item 13, division 3, sub section 962D(2)].***

Renewal obligation

2.19 If an ongoing fee arrangement is to remain in place for a period longer than 24 months, the fee recipient is required to provide the client with a renewal notice at least 30 days before the 24 month anniversary of the day the arrangement was entered into ***[Item 13, division 3, sub section 962G(1) and section 962H].***

2.20 The renewal notice will need to contain information indicating that the client may renew the ongoing fee arrangement. It will also contain information setting out what will happen if the client elects not to renew the arrangement, or if they do not respond to the renewal notice, in particular, that the arrangement (including the provision of advice and the ongoing fee) will terminate. Fee recipients may choose to elaborate in the renewal notice on the potential deleterious consequences to the client if they do not renew the ongoing fee arrangement including, for example, that will lose access to ongoing advice including in situations where they may value it most (for example, in times where there are sudden shocks to capital markets) ***[Item 13, division 3, sub paragraph 962G(2)].***

2.21 Because fee recipients will be required to provide a fee disclosure statement at the same time they provide a renewal notice to the client, the fee disclosure statement will also the assist the client in deciding whether they should agree to renew the ongoing fee arrangement. Where the fee recipient is required to send a client both the fee disclosure statement and renewal notice, it is expected that fee recipients will be able to satisfy both of these requirements by providing one comprehensive notice which contains all of the information required under sub sections 962E(2) and 962G(2).

2.22 It is envisaged that the fee disclosure statement and renewal notice could take simple forms. Provided the required information is contained in those notices, fee recipients have flexibility in how they present these documents, which need not be longer than one page in length.

2.23 If the fee recipient does not comply with the requirement to provide the renewal notice within the specified time, the client is not liable to continue paying the ongoing fee ***[Item 13, division 3, sub section 962C(1)].*** Any ongoing fee paid after the failure to comply with the renewal notice obligation must be refunded on the request of the client. The fact that the client continued paying the ongoing fee after the failure of the fee recipient to comply does not waive the client's right to a refund. This is because often the mechanism by which clients pay for ongoing advice services is through an automated process (for example, by a monthly direct debit from the client's investment) ***[Item 13, division 3, sub sections 962C(2)&(3)].***

2.24 Even where the identity of the fee recipient changes (for example, where a fee recipient sells a 'book' of business to another fee recipient) and it was the previous fee recipient that failed to comply with the renewal notice obligation, this does not alter the fact that the client is not liable to continue paying the ongoing fee ***[Item 13, division 3, sub section 962C(1)].***

2.25 The regulations may provide that the requirement to provide a renewal notice does not apply in certain situations. The diversity and complexity of the financial services industry make it necessary for the Minister to be able to exclude certain arrangements that this obligation is not intended to apply to, including arrangements that may not currently exist. It therefore serves several functions, including keeping the legislation up to date, providing commercial certainty quickly and efficiently to industry participants that are unintentionally exposed to the renewal notice obligation, and to provide efficacy to the legislation ***[Item 13, division 3, sub section 962G(3)].***

Flexibility of disclosure and renewal notice obligations

2.26 Although the fee disclosure statement and the renewal notice are required to be sent 30 days prior to the relevant anniversary date (12 months since the arrangement began in respect of the disclosure obligation, and 24 months since the arrangement began in respect of the renewal notice obligation), there is nothing preventing a fee recipient from providing these notices in advance of the prescribed time periods in order to satisfy the obligations sooner than is actually required if it is convenient to do so. To the extent these obligations are fulfilled by fee recipients in advance of the prescribed periods, the time within which these obligations need to be fulfilled in the future 'reset', with the creation of new disclosure and renewal notice days ***[Item 13, division 3, section 962F and sub section 962H(1)].***

2.27 This provides flexibility for fee recipients in choosing when they discharge these obligations. For example, if the fee recipient and client have a face-to-face meeting well in advance or the disclosure or renewal notice days, they can take the opportunity to provide these notices or obtain their client's agreement to renew in advance the applicable anniversary.

Example 2.1 Adviser A and Client B have an ongoing fee arrangement which commenced on 1 July 2012. Adviser A would ordinarily be required to provide a fee disclosure statement no later than 30 days before 1 July 2013, and a renewal notice no later than 30 days before 1 July 2014 in order to continue charging an ongoing fee past the applicable dates. However, if Adviser A and Client B undertake a face-to-face client review on 27 February 2013, Adviser A can provide a fee disclosure statement to Client B at that meeting, which will negate the need to provide the notice later in the year. Similarly, Adviser A can provide Client B with a fee disclosure statement and a renewal notice and obtain the client's agreement to renew then and there, meaning Adviser A would not have to provide the fee disclosure statement to Client B until 30 days before 27 February 2014, and would not have to provide a renewal notice until 30 days before 27 February 2015.

Opt-out process

2.28 The renewal notice requirement establishes a framework by which clients are asked by the fee recipient if they wish to renew the ongoing fee arrangement. If the client does not actively renew that agreement within the renewal period, the client is assumed to have opted out of the ongoing fee arrangement.

2.29 If the client communicates to the fee recipient in writing within the renewal period that they do not wish to renew the ongoing fee arrangement, the arrangement terminates at the end of a further period of 30 days after the renewal period. The additional 30 days provides the fee recipient with additional time to facilitate the termination of the arrangement, including, for example, notifying third parties (such as product providers) to cease collecting ongoing fees on behalf of the fee recipient ***[Item 13, division 3, section 962J].***

2.30 If the client does not notify the fee recipient in writing that they wish to renew the ongoing fee arrangement, the arrangement terminates at the end of an additional 30 days after the renewal period. The Bill infers a client's failure to respond to a renewal notice to mean that the client does not wish to renew the ongoing fee arrangement. This might be due either to the client's disengagement or to a conscious decision by the client not to actively renew because, for example, they considered they were not receiving value for the fees they are paying ***[Item 13, division 3, section 962K].***

2.31 In terms of clients notifying the fee recipient in writing of their decision to renew or not renew the ongoing advice fee, this can be administered flexibly and by using a range of mediums and technologies. For example, the client can notify the fee recipient in a number of recordable forms, including by facsimile, email, SMS, or through an online facility (including, for example, through a client's account login on a product provider's website).

2.32 If an ongoing fee arrangement terminates under section 962J or 962K, and the fee recipient continues to charge the ongoing fee, they will be subject to a civil penalty. Because a breach of such a provision is likely to be relatively less serious than, for example, a breach of the best interests duty, it is subject to lower maximum civil penalties ($50,000 for an individual and $250,000 for a body corporate) ***[Item 13, division 3, section 962L].***

2.33 It is expected that maximum penalties would apply only in the most serious of breaches of these provisions. Simpler breaches, for example where a single breach is accidental, would attract a smaller proportionate penalty (to the extent any action is taken at all).

2.34 The ongoing fee arrangement contains an implied term that the client may terminate the arrangement at any time. This is intended to prevent clients being locked into fixed term ongoing fee arrangements as a result of the new disclosure and renewal notice obligations. It also reflects a right that clients currently enjoy as a matter of common practice within the financial planning industry ***[Item 13, division 3, sub section 962B(1)].***

2.35 To ensure that clients will not be deleteriously impacted as a result of sub section 962B(1), sub section 962B(2) voids any condition of an ongoing fee arrangement that requires a client to pay an amount on terminating the ongoing fee arrangement to the extent the amount exceeds the sum of any liability that the client has accrued but not satisfied before the termination, or the costs the fee recipient has incurred solely and directly because of the termination.

2.36 This effectively prohibits fee recipients from applying an 'exit' or 'penalty' fee to clients that choose to terminate an ongoing fee arrangement in accordance with sub section 962B(1). However, this would not prevent a fee recipient from recovering monies already owed by the client (for example, for services already rendered). 'Exit' fees would remain permissible under paragraph 962B(2)(b) to the extent that they represent no more than a cost-recovery fee incurred as a result of the termination, which in most situations is likely to constitute only a modest sum ***[Item 13, division 3, sub section 962B(2)].***

2.37 To the extent the continued provision of a service by the fee recipient is dependent on the continued payment of an ongoing fee under the ongoing fee arrangement, the obligation to continue to provide the service also terminates. This provides certainty to the fee recipient that in most cases their obligation to provide continued advice services ceases after termination, as does their liability for the failure to provide continued advice services.

2.38 This clarification is particularly important for the situation that arises under section 962K, particularly where the client does not consciously choose to not renew, but terminates the ongoing fee arrangement by virtue of failing to respond to the fee recipient's renewal notice. While a fee recipient remains liable for any advice they have provided prior to termination, they cannot be liable for client losses as a result of failure to provide advice to a client after termination (for example, in the event of sudden movements in capital markets after the ongoing fee arrangement is terminated). Fee recipients may wish to emphasise these matters to the client when they provide them with the renewal notice ***[Item 13, division 3, section 962M].***

Application and transitional provisions

2.39 Division 3 (charging ongoing fees to clients) applies only to ongoing fee arrangements entered into on or after the commencing day and where the client has not received financial advice from the licensee prior to the commencing day ***[Item 13, division 3, section 962(3)].***

2.40 This essentially means that Division 3 will only apply to new clients.

Chapter 3
Enhancements to ASIC's licensing and banning powers

Outline of chapter

3.1 Schedule 1 to the Corporations Amendment (Future of Financial Advice) Bill 2011 (the Bill) amends the *Corporations Act 2001* (Corporations Act) to enhance the ability of the Australian Securities and Investments Commission (ASIC) to supervise the financial services industry through changes to its licensing and banning powers ***[Schedule 1, items 2 to 8]***.

Context of amendments

3.2 ASIC is responsible for regulating persons who carry on a financial services business in Australia.

3.3 Those persons who wish to carry on a business of providing financial services are generally required to hold an Australian financial services licence (licence), issued by ASIC.

3.4 Adequate licensing thresholds provide a basic screening process to facilitate investor confidence that financial services providers have appropriate skills, experience and qualifications, are of good character and that they are required to provide services with honesty and integrity. The licensing regime also enhances ASIC's ability to supervise the financial services industry.

3.5 ASIC must grant a licence if certain criteria are satisfied. This includes that ASIC is satisfied that there is no reason to believe that the applicant is not of good fame or character. ASIC must also have no reason to believe that the applicant will not comply with its obligations as a licensee. As long as these criteria are met and the application is made properly, ASIC must grant the applicant a licence, as it does not have the ability to refuse a licence on any other grounds.

3.6 A common exemption from the need to obtain a licence is where a person (and its employees and directors) is an authorised representative of a licensee. This reflects the approach to licence all principals rather than agents. Because of this approach, the licensee that authorises its representatives must ensure that they are competent to provide the services, and are generally liable for their actions. The approach is based on the premise that the principal conducts the relevant business through its employees and agents and is under a legal obligation to control and supervise the employees or agents.

3.7 ASIC is responsible for enforcing the law when it is breached by a licensee or a person acting on their behalf. This may involve the use of an administrative remedy, such as cancelling a licence or banning an individual from providing financial services.

3.8 ASIC has the power to ban or seek disqualification by a court of persons providing financial services in certain circumstances. ASIC's banning power applies, for example, if the person is convicted of fraud or breaches a financial services law.

3.9 During the *Inquiry into Financial Products and Services in Australia by the Parliamentary Joint Committee on Corporations and Financial Services* (PJC Inquiry), ASIC raised concern with its ability to protect investors by restricting or removing from the industry participants who might cause or contribute to investor losses. ASIC consider this issue arises as:

- the threshold for entry into the licensing regime is 'low' while the threshold for cancelling a licence is 'relatively high'; and

- the regime focuses on entities rather than its agents (such as employees or directors) which means ASIC cannot prevent persons from entering the industry and can have difficulty removing them.[1]

3.1 In its submission to the PJC, ASIC noted that its decisions in relation to licensing can be appealed to the Administrative Appeals Tribunal (AAT) and that in practice ASIC has found it very difficult to establish before the AAT that a licensee 'will not' comply with obligations in the future. More specifically, in relation to considering whether a licence should be granted, ASIC has experienced difficulty when trying to assess whether an applicant 'will not' comply with their obligations and meet their licence conditions before they have commenced business. [2]

[1] ASIC Submission to the PJC, August 2009, 24.
[2] Ibid, 26, 31.

3.2 Further, ASIC has noted that it has experienced specific issues in attempting to use its powers to ban persons from providing financial services. ASIC has found it difficult to establish that it has a reasonable belief that the person 'will not' comply with their obligations under financial services law: see *Re Howarth and ASIC* [2008] AATA 278. Specifically, ASIC found it difficult to establish that a broader range of conduct (aside from convictions for fraud) can found a belief that the individual 'will not' comply with their obligations under financial services law in the future. For example, ASIC has been unable to establish that the following conduct should give rise to a banning order based on a finding under paragraph 920A(1)(f) of the Corporations Act:

- failure to comply with the principal's internal guidelines and procedures;
- failure to comply with the relevant ASX business rules; or
- conduct which may amount to a serious conflict of interest.[3]

3.3 ASIC has also noted that it cannot currently ban individuals on the basis that they are not 'fit and proper' (i.e. not competent or of good fame or character).[4]

3.4 ASIC has experienced difficulty in relation to the banning of individuals because of the focus on entities in the Corporations Act. Licensing generally occurs at the entity level and ASIC does not approve the agents or representatives of that entity. Further the obligations in the Corporations Act are largely imposed on the licensee (the entity), not the representatives who work for that entity.[5] For example, the requirement to have a reasonable basis for advice under section 945A of the Corporations Act applies to a providing entity, which includes the licensee and authorised representative. The provision does not directly apply to an employee or director.[6]

3.5 Further to ASIC's experience in using its powers, broader concerns have been raised about the effectiveness of licensees being responsible for the actions of their representatives, with implications for

[3] Ibid, 33.
[4] Ibid, 32.
[5] Under the Corporations Act, some of the Chapter 7 conduct and disclosure obligations are also imposed on an authorised representative, in addition to the licensee. However obligations are not generally imposed on other representatives, such as employees and directors.
[6] Ibid, 26.

the professionalism of the industry, as well as investor protection. This issue was considered in the PJC Inquiry. [7]

3.6 In light of the above concerns, in its report the PJC recommended that the Corporations Act should be amended to provide extended powers for ASIC to ban people from the financial services industry under section 920A and suspend and cancel a licence under sections 913B and 915C of the Corporations Act (recommendations 6 and 8).

Summary of new law

3.7 The enhancements to ASIC's licensing and banning powers are:

- a change to the licensing threshold so that ASIC can refuse or cancel/suspend a licence where a person is likely to contravene (rather than will breach) its obligations;
- extend the statutory tests so that ASIC can ban a person who is not of good fame and character or not adequately trained or competent to provide financial services (in essence they are not a fit and proper person);
- a change to the banning threshold so that ASIC can ban a person if they are likely to (rather than will) contravene a financial services law; and
- clarification that ASIC can ban a person who is involved, or is likely to be involved, in a contravention of obligations by another person.

Comparison of key features of new law and current law

New law	***Current law***
In relation to an ASIC decision to grant a licence, the statutory test under paragraph 913B(1)(b) is whether the applicant is likely to contravene its obligations under section 912A, rather than they will	In relation to an ASIC decision to grant a licence, the statutory test under paragraph 913B(1)(b) is whether the applicant will not comply with its obligations under section 912A.

[7] PJC report, November 2009, 134, paragraph 6.130.

not comply with the obligations.	
In relation to an ASIC decision to suspend or cancel a licence, the statutory test under paragraph 915C(1)(aa) is whether the applicant is likely to contravene its obligations under section 912A, rather than they will not comply with the obligations.	In relation to an ASIC decision to suspend or cancel a licence, the statutory test under paragraph 915C(1(aa) is whether the applicant will not comply with its obligations under section 912A.
In relation to an ASIC decision to make a banning order against a person, the statutory test under paragraph 920A(1)(ba) is whether the person is likely to contravene its obligations under section 912A, rather than they will not comply with the obligations.	In relation to an ASIC decision to ban a person, the statutory test under paragraph 920A(1)(ba) is whether the person will not comply with its obligations under section 912A.
In relation to ASIC decision to make a banning order against a person, the new statutory test under paragraphs 920A(1)(d) and (da) is whether the person is not of good fame and character or that they are not adequately trained or competent to provide financial services. There is no change to existing section subsection 920B(2), where the fact that a person is not of good fame and character is relevant to determining the effect of a banning order.	There are no equivalent statutory tests. Under existing subsection 920B(2) the fact that a person is not of good fame and character can only be taken into account to determine the effect of a banning order.
In relation to an ASIC decision to make a banning order against a person, the statutory test under paragraph 920A(1)(f) is whether the person is likely to contravene a financial services law rather than they will not comply with the law.	In relation to an ASIC decision to ban a person, the statutory test under paragraph 920A(1)(f) is whether the person will not comply with a financial services law.
In relation to an ASIC decision to ban a person, the statutory test under paragraphs 920A(1)(g) and (h) is whether the person has been involved, or is likely to be involved, in a contravention of a financial services law.	There is no equivalent statutory test.

Detailed explanation of new law

3.8 The Bill amends ASIC's licensing and banning powers to clarify the operation of its powers, as well as prescribe additional tests under which ASIC can remove persons from the industry. The amendments enhance ASIC's ability to supervise the financial services industry to protect consumers of financial services.

Amendments to ASIC's licensing power

3.9 The Bill amends the operation of ASIC's licensing power to clarify that ASIC is not required to believe as a matter of certainty that the person will contravene the obligations in future.

3.10 ASIC can refuse to grant a licence if the statutory test under existing paragraph 913B(1)(b) is satisfied. The amendment to the statutory test is whether the applicant is likely to contravene its obligations as a licensee under section 912A, rather than they will contravene the obligations (i.e. the applicant will not comply with the obligations). In the 10 years since the introduction of the Financial Services Reform Act, interpretation of this provision has tended to a view that ASIC is required to believe, as a matter of certainty, that the person will contravene the obligations in future. Such a standard would be so onerous that it could result, in practice, in ASIC never being able to refuse a licence using this part of the test. This new formulation is designed to ensure that ASIC can more appropriately account for the likelihood or probability of a future contravention. ***[Schedule 1, item 2, paragraph 913B(1)(b)].***

3.11 The statutory test is whether the applicant is likely to contravene the obligations under section 912A. ASIC may take into account any information relevant to this question, such as:

- conduct of the applicant that shows deliberation and planning in wilfully disregarding the law;
- the extent of compliance by the applicant with analogous obligations in another regime; or
- any other conduct of the applicant that may lead ASIC to conclude, on reasonable grounds, that the applicant is not likely to comply.

3.12 The same amendment is also made to the statutory test under paragraph 915C(1)(aa) of the Corporations Act, which relates to an ASIC decision to suspend or cancel a licence. The amendment to the statutory test is whether a licensee is likely to contravene the obligations under section 912A, rather than they will contravene the obligations (i.e. the licensee will not comply with the obligations). Similar to the amendment in paragraph 3.11, the amendment addresses interpretation of this provision which has tended to a view that ASIC is required to believe, as a matter of certainty, that the person will contravene the obligations in future. ***[Schedule 1, item 3, paragraph 915C(1)(aa)].***

3.13 There is no policy change relating to the replacement of 'comply' with 'contravene' in both amendments. It brings consistency with similar provisions ASIC also administers under the National Consumer Credit Protection Act 2009 ***[Schedule 1, items 2 and 3, paragraphs 913B(1)(b)] and 915C(1)(aa)].***

Amendments to ASIC's banning powers

3.1 The Bill clarifies the operation of ASIC's banning power and sets out new tests under which ASIC can exercise its discretion to remove persons from the financial services industry.

Clarifications to banning power

3.2 ASIC may ban a person if either statutory tests under paragraphs 920A(1)(ba) and 920A(1)(f) of the Corporations Act are satisfied.

3.3 The amendment to the statutory tests is whether the person is likely to contravene its obligations under section 912A or financial services law, rather than they will contravene the obligations (i.e. the person will not comply with its obligations or financial services law). In the 10 years since the introduction of the Financial Services Reform Act, interpretation of this provision has tended to a view that ASIC is required to believe, as a matter of certainty, that the person will contravene the obligations in future. Such a standard would be so onerous that it could result, in practice, in ASIC never being able to ban a person using these tests. This new formulation is designed to ensure that ASIC can more appropriately account for the likelihood or probability of a future contravention. ***[Schedule 1, items 4 and 6, paragraphs 920A(1)(ba) and 920A(1)(f)].***

3.4 There is no policy change relating to the replacement of 'comply' with 'contravene' in both amendments. It brings consistency with similar provisions ASIC also administers under the National Consumer Credit Protection Act 2009 ***[Schedule 1, items 4 and 6, paragraphs 920A(1)(ba) and 920A(1)(f)].***

New statutory tests and other clarifications

3.5 The Bill includes new tests for when ASIC can make a banning order against a person. The tests relate to a person's fame and character and competence. In essence, this introduces a 'fit and proper' test however the limbs of good fame and character and competence are adopted for consistency with the rest of the Corporations Act which uses the good fame and character test.

3.6 ASIC can ban a person if their conduct gives ASIC reason to believe they are not of good fame and character ***[Schedule 1, item 5, paragraph 920A(1(d)].*** In determining whether a person is not of good fame and character ASIC must take into account (subject to Part VIIC of the Crimes Act relating to spent convictions):

- any convictions of the person, within 10 years before that time, for serious fraud; and
- whether the person has held a licence that was suspended or cancelled; and
- whether a banning order or disqualification order under Division 8 has previously been made against the person; and
- any other matter ASIC considers relevant ***[Schedule 1, item 8, subsection 920A(1)(1A].***

3.7 Given that it can be expected that ASIC will principally use this power to ban individuals, this would enable ASIC to take into account conduct such as where:

- ASIC believes the individual has committed a fraud, but the individual has not been prosecuted or there is a delay or uncertainty in prosecution;
- the individual has engaged in conduct causing serious detriment or financial loss to consumers, so that there is a need to protect the public;
- the individual has been subject to adverse findings in relevant criminal or civil proceedings, reflecting on their character;
- the individual has demonstrated a consistent failure to comply with the law, or with directions from any licensee or employer; or
- the individual has been a director or senior manager of a licensee that has had its licence suspended or cancelled.

3.8 Further, the amendment also introduces a statutory test that ASIC can ban a person if their conduct gives ASIC reason to believe they are not adequately trained or competent to provide financial services ***[Schedule 1, item 5, paragraph 920A(1)(da)].*** It is expected that ASIC will principally use this power to ban individuals where the person lacks appropriate skills, knowledge and experience to provide financial services.

3.9 The Bill also clarifies ASIC's ability to ban individuals, given the focus of obligations on the entity or licensee. The Bill extends the grounds of banning to whether the person is involved in (or likely to be involved in) a contravention of financial services law, which enables ASIC to take into account conduct where the person is not under a legal responsibility to comply with the legislation themselves but they contributed or caused another person to breach the legislation. Where the licensee is, for example a body corporate, then any contravention of the law will necessarily be the result of an act or omission of a natural person, such as a director or employee. The amendments clarify that ASIC can take into account conduct of these persons where they have been involved in a contravention of the financial services law, in deciding whether or not these individuals should be banned. The amendment also applies in circumstances where the licensee is a natural person, but an employee of the licensee was involved in a contravention of the licensee's obligations under law ***[Schedule 1, item 7, paragraphs 920A(1)(g) and (h)].***

3.10 Under existing section 79 of the Corporations Act, a person is 'involved in' a contravention of a financial services law if the person

- has aided, abetted, counselled or procured the contravention; or
- has been induced, whether by threats or promises or otherwise, the contravention; or
- has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or
- has conspired with other to effect the contravention.

3.11 To avoid doubt, the Bill also clarifies that a person contravenes a financial services law if a person fails to with comply with the duty, even if the provisions which impose the duty is not an offence or civil penalty provision. For example, under the best interests obligations the duty is placed on the person who provides the personal advice, which may be an employee of the licensee. If an employee breaches the best interests obligation, liability for civil penalty accrues to the employer and not the employee. However an employee would contravene the financial services law for the purposes of ASIC making a banning order (if appropriate in the circumstances) ***[Schedule 1, item 8, subsection 920A(1)(1A].***

Application and transitional provisions

3.12 The amendments commence on 1 July 2012, noting it is possible that in the exercise of these powers ASIC may take into account conduct that occurred before the commencement date. However the purpose of the provisions is to prevent unsuitable people from providing financial services to protect the public ***[Item 2]***.