



5 December 2014

Senator Sam Dastyari
Chair
Senate Economics References Committee
PO Box 6100
Parliament House
Canberra ACT 2600

Email: economics.sen@aph.gov.au

Dear Senator Dastyari

Re: Inquiry into the Scrutiny of financial advice

The Financial Planning Association of Australia (FPA) welcomes the opportunity to provide input to the Senate Economics References Committee Inquiry into the Scrutiny of financial advice.

In the past few years there has been numerous Parliamentary Inquiries relating to the financial services industry and financial advice providers including:

- Inquiry into the performance of ASIC
- Inquiry into education, professional and ethical standards for financial advisers
- Two inquiries into the Future of Financial Advice (FoFA) Amendment Bill
- Financial Systems Inquiry interim Report
- PJC Inquiry into Trio
- Richard St John review of compensation arrangements for consumers of financial services
- PJC Inquiry into financial products and services in Australia

Many of these inquiries had Terms of Reference and have made clear recommendations addressing many of the issues which are to be considered by the Committee's Inquiry into the Scrutiny of Financial Advice. The recommendations made by these inquiries are still being appropriately considered, implemented and tested by the relevant parties.

However, the FPA believes that any changes to protect consumers must include

- Raising education and professional standards
- Restrictions of who can call themselves a financial planner or financial adviser



- A co-regulatory model to support existing professional frameworks and complement the regulatory obligations for financial planners and financial advisers

The FPA is committed to ensuring financial planners and financial advisers in Australia practice professionally. We believe all providers of personal financial advice who use the title financial planner or financial adviser must be compelled to meet professional and ethical standards set by a recognised professional body in order to practice.

The FPA would welcome the opportunity to discuss our recommendations further. We would also like to express our desire to appear as a witness at a public hearing of the Inquiry, should the Committee deem this appropriate.

If you have any questions, please do not hesitate to contact our General Manager Policy and Conduct, Dante De Gori, or myself on 02 9220 4500 or dante.degori@fpa.asn.au / mark.rantall@fpa.asn.au.

Yours sincerely

Mark Rantall
CEO

Financial Planning Association of Australia Limited¹

¹ The Financial Planning Association (FPA) has more than 10,000 members and affiliates of whom 7,500 are practising financial planners and 5,500 CFP professionals. The FPA has taken a leadership role in the financial planning profession in Australia and globally:

- Our first "policy pillar" is to act in the public interest at all times.
- In 2009 we announced a remuneration policy banning all commissions and conflicted remuneration on investments and superannuation for our members – years ahead of FOFA.
- We have an independent conduct review panel, Chaired by Dr June Smith, dealing with investigations and complaints against our members for breaches of our professional rules.
- The first financial planning professional body in the world to have a full suite of professional regulations incorporating a set of ethical principles, practice standards and professional conduct rules that explain and underpin professional financial planning practices. This is being exported to 24 member countries and the 150,000 CFP practitioners that make up the FPSB globally.
- We have built a curriculum with 17 Australian Universities for degrees in financial planning. From 1 July 2013 all new members of the FPA are required to hold, as a minimum, an approved undergraduate degree.
- CFP certification is the pre-eminent certification in financial planning globally. The educational requirements and standards to attain CFP standing are equal to other professional bodies, eg CPA Australia.
- We are recognised as a professional body by the Tax Practitioners Board



Senate Economics References Committee Inquiry into the Scrutiny of financial advice

FPA submission to:
Senate Economics References Committee

5 December 2014



Professional and education standards

FPA SUBMISSION TO PJC ON CORPORATIONS AND FINANCIAL SERVICES | DATE: 05.09.2014

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Attachment 1: Summary of FPA professional framework

Attachment 2: FPA submission to the Inquiry into the performance of ASIC

Attachment 3: FPA submission to the PJC Inquiry into the proposals to lift the professional, ethical and education standards in the financial services industry

Attachment 4: FPA submission to the Review of compensation arrangements for consumers of financial services

Attachment 5: FPA submission to the PJC Inquiry into the collapse of Trio Capital and related matters

Attachment 6: Reference checking in the financial services industry

Attachment 7: Recommendations to improve the regulatory oversight and accountability of product providers and research houses



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FPA SUBMISSION TO SENATE ECONOMICS REFERENCES COMMITTEE | DATE: 05.12.2014

Terms of Reference

Implications of financial advice reforms, with particular reference to:

- a) the current level of consumer protections;
- b) the role of, and oversight by, regulatory agencies in preventing the provision of unethical and misleading financial advice;
- c) whether existing mechanisms are appropriate in any compensation process relating to unethical or misleading financial advice and instances where these mechanisms may have failed;
- d) mechanisms, including a centralised register, that would ensure financial planners found to have breached any law or professional standards in their employment are transparent, for both the sector and consumers;
- e) how financial services providers and companies have responded to misconduct in the industry;
- f) other regulatory or legislative reforms that would prevent misconduct; and
- g) any related matters.



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Introduction

The FPA supports and believes in the protection of consumers through preventative measures to reduce the risk of misconduct and the problems that lead to events that cause consumer loss or damage. The FPA has been a long-term champion of raising professional obligations of financial planners to improve protections and the quality of advice for consumers. This position is reflected in our Code of Professional Practice, membership requirements, ongoing professional obligations and accountability action.

There have been numerous parliamentary inquiries and independent reviews over recent years covering all aspects of financial advice, which have led to clear and in many cases, sensible recommendations to progress the professionalism of the financial services industry and improve the quality of advice for consumers. The profession and governments, both past and present, have acted on many of these recommendations, with a clear roadmap for changes including:

- the introduction of the Future of Financial Advice (FoFA) reforms,
- establishment of a National Adviser Register by March 2015
- the application of the Tax Agent Services regime to financial planners and financial advisers
- an increase in education standards to a degree requirement for new financial planners and financial advisers, driven by the profession
- a requirement to be a member of a profession body, driven by the profession, and
- changes to remuneration structures including the banning of commissions, driven by the profession since 2009 and subsequently picked up in the FoFA reforms.

However, such changes take time to establish within the regulatory framework, be implemented by providers, felt by consumers, and evaluated for their effectiveness. While this process of significant change for the financial planning profession, and the financial services industry more broadly, has made substantial advancements, it is not complete. The FPA believes it is vital that changes currently under development be permitted to be fully implemented and tested.

While such changes aim to improve the quality of advice and consumer protections, there is a gap in public policy. Government policy must support and facilitate membership of a professional body through a co-regulatory model, to ensure providers are obliged to adhere to professional obligations which will broaden the reach of the overall regulatory system and strengthen consumer protection.



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Summary of key recommendations

1. The FPA recommends the Committee propose a regulatory framework where ASIC regulates corporations and companies who are licensed to provide financial advice, and the profession regulates individual financial planning practitioners.
2. The Government adopt a co-regulatory model to restrict the use of the terms financial planner and financial adviser to those who are a member of and hold a practicing certificate from a recognised professional body.
3. The Parliament set and monitor performance goals (Key Result Areas - KRAs) for ASIC, and all regulators, that facilitates a co-regulatory model with professional bodies
4. The Government facilitates the establishment of Memorandum(s) of Understanding (MoUs) between ASIC and professional bodies:
 - to enable confidential information sharing on 'bad apples', bad practice and emerging risks, and
 - to permit a more collaborative and cooperative two-way working relationship, or co-regulatory partnership.
5. The Committee support an holistic Education and Professional Standards Framework that leverages existing networks and bodies to minimise the regulatory impact on all stakeholders.
6. The Committee review the recommendations made by Richard St John and consider whether they are appropriate to implement in the current post-FoFA regulatory environment.
7. The Committee recommend the Corporations Act definition of General Advice be re-termed 'general or product information' and be limited to the provision of 'factual information and/or explanations' relating to financial products.
8. The Committee recommend a review of the definitions of 'retail', 'wholesale', and 'sophisticated' investors in the Corporations Act.
9. The Committee call for greater regulatory oversight of product providers and research houses.



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ToR a) the current level of consumer protections

Current environment and responsibilities

According to ASIC licensing data, there are 5,027² Australian Financial Services License holders and 51,147³ authorised representatives of AFSL holders who are licensed to provide 'financial product advice' as defined under the Corporations Act. Such people might work as bank tellers, product provider call centre staff, financial advisers, stock brokers, accountants, or fully-fledged financial planners, all providing different types of financial advice services to consumers depending on their training, competency, and authorisation.

The FPA has more than 10,750 members and affiliates of whom 8,055 are practicing financial planners and more than 5,500 CFP professionals. The professional obligations and standards set by the FPA's enforceable Code of Professional Practice plays a fundamental role in protecting consumers and the financial wellbeing of Australians, and is vital to ensure our members provide quality advice to their clients.

Thus, there are 10,000 financial planners in Australia who are FPA members and approximately 2,000 are members of professional accounting bodies. Based on ASIC's figures, this potentially leaves approximately 39,147 authorised representatives providing financial advice to consumers without a requirement to comply with the additional standards of ethics, conduct and education of professional membership. This significantly reduces the consumer protections available to the clients of approximately 76% of financial planners and financial advisers currently operating in the market.

Australians deserve the best possible advice from the most qualified practitioners and these practitioners should be bound by a professional framework that goes beyond the law and requires adherence to standards of conduct, ethics and education which are specifically tailored to the provision of quality personal financial advice.

The FPA notes that ASIC's figures do not include employed representatives who also provide personal financial advice. The FPA also does not know whether the 76% of authorised representatives who are currently not bound by professional standards are deemed to be or want to be financial planners or financial advisers.

However, the FPA knows that Australian consumers deserve the added protections of a regulatory framework which supports and facilitates collaboration and cooperation between ASIC and professional bodies. Government policy that supports and facilitates membership of a professional body through a co-regulatory model, will ensure providers are obliged to adhere to professional obligations which will broaden the reach of the overall regulatory system and strengthen consumer protection.

² ASIC figures as at 10 May 2013 as provided to PJC Inquiry, answers to questions on notice 22 April (received 13 May 2013)

³ ASIC figures as at 10 May 2013 as provided to PJC Inquiry, answers to questions on notice 22 April (received 13 May 2013)



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The Regulators

Providers of tier 1 personal advice are regulated by both ASIC and the Tax Practitioners Board (TPB). The primary role of regulators is to enforce the law – the Corporations Act and the Tax Agent Service Act, respectively.

ASIC oversees the Corporations Act:

- by regulating corporations which does not deliver the same benefits as directly regulating individual conduct
- has limited power to approve industry code rather than professional bodies and professional codes

The TPB oversees the Tax Agent Service Act:

- is limited to the provision of tax advice which does not capture all financial advice services provided to consumers.
- is compliance focused
- TPB can recognise professional bodies based on high level tick-a-box criteria
- do not require recognised professional bodies to continually improve standards and practices of its members

The following table compares what ASIC and the TPB are responsible for and who they regulate in relation to financial advice providers.

	ASIC	TPB
Responsibilities	Corporations Act ASIC Act National Consumer Credit Protection Act	Tax Agent Services Act
Who do they regulate	Businesses who hold a Australian Financial Services License (AFSL)	Companies and individuals who provide tax (financial) advice services
Services regulated entities provide	Financial product advice	Tax advice (including advice on tax and superannuation laws)
Relationship with professional bodies	s1101A of the Corporations Act and RG183 permit ASIC to approve codes of conduct (mainly for purposes of opt-in which has now been removed)	TASR permit TPB to recognise professional bodies – goes beyond just the Code. Includes all professional obligations; and provides exemptions for members of recognised professional bodies
Education requirements	Set minimum requirements, with no quantum, in RG146 – AFQ 5	Set minimum requirements of diploma (AQF5) for tax and commercial law course.
Experience requirements	No requirements	Experience requirements vary depending on education level.
Professional obligations	No requirement	No requirement But encourage adherence to professional obligations through exemptions for members of recognised professional bodies



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Future of Financial Advice (FoFA) Reforms

The FPA believe it must be recognised that the FoFA reforms, while implemented by the Labor Government to improve the quality of advice for consumers, have been in limbo and under a cloud of uncertainty for some time. As demonstrated by the following timeline, the profession has had to grapple with what is required one day and not required the next, significantly hindering their ability to implement any necessary changes to their advice processes and systems.

- July 2012 – Licensees and Authorised Representatives were permitted to choose voluntary compliance with FOFA
- July 2013 – Compliance with FOFA becomes mandatory, except for some conflicted remuneration issues and transition arrangements for certain requirements.
- 5 August 2013 Government enters caretaker period – Coalition announces package of 16 changes to the FoFA requirements if elected.
- December 2013 – Coalition government announces changes to FOFA (Streamlining FOFA); ASIC compliance on measures to be changed on hold
- 30 June 2014 – Coalition Government introduced FoFA Regulations amendments to remove some FoFA requirements and change others, making these amendments law. ASIC compliance action remains on hold.
- July 2014 – November 2014 – regular disallowance motions against the Regulation Amendments tabled in the Senate; FoFA Bill introduced into Parliament, passed the House of Representatives, faced two Senate Inquiries.
- 19 November 2014 – Senate voted in support of a disallowance motion on the FoFA Regulation Amendments. The law immediately reverts back to the original FoFA requirements.
- 27 November 2014 – Government and the Opposition released statements confirming an agreement to amend the grandfathering regulations with more changes likely to come.

The FPA notes this Inquiry's Terms of Reference state that the Committee inquire and report on the "*Implications of financial advice reforms...*". As the reforms are yet to be settled in their final form, it is difficult to provide an informed response to the Committee on the effectiveness of the FoFA requirements at this stage.

Professional standards

Professional standards impose obligations that exceed the minimum requirements set in the law. Professional standards and professional membership are more than a set of additional rules and standards. They encourage the 'norming' of ethical conduct and professional behaviours building a sense of professional aspiration, pride and commitment to high professional ideals.



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The primary emphasis of professional regulation is in the setting and enforcement of professional norms and behaviours, negotiated directly with the community of professionals themselves, for the national public benefit the profession serves. Another feature of professional regulation is an emphasis on providing clarity and depth to the professional community's expectations of good process, identifying the boundaries of good practice, over and above the expectations of the law. Working in concert, these overlapping systems can provide enhanced consumer protection and help build the broader community's trust and confidence in the sector, and the regulatory system.

Whilst firms may play a significant role in setting standards of behaviour and conduct, it is the normative power of professional standards and their appeal to ethical behaviour, which offers the best prospects to significantly improve consumer outcomes across the variations in service offerings and business models in the financial services sector. Professional standards speak universally to all members of the profession as they are business model agnostic. They encourage individual professionals to strive for client-centred outcomes and to resist adverse commercial interests. They install pride, a sense of belonging and public purpose in their adherents.

By their nature professional bodies seek to bind individual practitioners rather than the licensee, to professional standards and rules, as is the case with financial advice. This is a vital difference and benefit professional bodies bring to the regulatory landscape. Where ASIC in its capacity as Regulator of the Corporations Act, governs corporations and licensees, professional bodies set and enforce professional standards for their members who are individual practitioners on the 'frontline' interacting with and providing the direct service to consumers.

There are strong reasons for compelling the adoption of professional standards for individuals to call themselves a financial planner or financial adviser. In recent years, numerous cases of poor financial advice and fraud have come to light, with some consumers making considerable losses and the reputation of the financial advice industry being damaged in the process. For example, the collapse of Trio Capital resulted in consumers losing roughly \$176 million from their superannuation.⁴

While corporate collapses such as Trio Capital, Opes Prime, and Westpoint involved fraud, many consumers who invested in these products received personal financial advice. Professional, ethical and education standards should serve to assist financial planners and financial advisers to identify appropriate financial strategies and investments suitable to each client's circumstances, goals and needs. This is a fundamental form of consumer protection and must be at the core of providing personal financial advice to clients.

The FPA's review of data collected since 2009 on ASIC enforcement action concerning individuals in relation to financial advice, shows that FPA members represent significantly less than 5% of the overall ASIC enforcement action each year⁵. FPA members have also accounted for significantly less than 10% of financial advisers banned by ASIC. **The fact that more than 90% of financial advisers banned by ASIC were providers who are not members of the FPA and therefore not subject to the additional regulatory oversight of our professional obligations, clearly demonstrates the consumer protection benefits of professional standards⁶.**

⁴ Parliamentary Joint Committee on Corporations and Financial Services Inquiry into the collapse of Trio Capital, Final Report, 16 May 2012

⁵ Based on publicly available enforcement information released by ASIC

⁶ ASIC bannings analysed against FPA membership data



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Statistical under-representation when compared to the total financial adviser and financial planner population in ASIC enforcement activity is a proof point of the positive effect of professional obligations. It demonstrates the vital role professional bodies play in 'norming' good professional behaviour beyond legal minimum standards, and the necessity of such obligations for the protection of consumers.

Attachment 1: Summary of FPA professional framework details the professional obligations set by the FPA and an overview of our enforcement activity as further demonstration of the vital role professional bodies play in the regulatory oversight of financial planning practitioner.

Current education and professional standards requirements

Adviser competency and requirements to meet professional standards significantly impact on the quality of advice consumers receive and improve consumer protections. There are significant gaps in the current education and professional standard requirements for financial planners and financial advisers and who they apply to.

	ASIC		TPB	
Education requirement	✓	RG146	✓	Tax law course approved by the Board Commercial law course approved by the Board
Education level	✓	AQF5	✓	AQF5
Qualification requirement	✗	No requirement for diploma	✗	No requirement for diploma
Course duration	✗	Not stipulated	✓	Minimum 100hrs
Assessment criteria	✗		✓	range of appropriate assessment tools
Course approval mechanism	✗	closed	✓	Approval against relevant Course requirement policy
Approval of course providers	✗ ✓	ASIC no longer approves courses Education regulators set competencies against RG146	✓	Information Sheet TPB(1) 07/2011 Approval process for course providers
Course / training register	✗	closed	✓	
Minimum CPD requirements	✗	There is no prescribed minimum requirement. ASIC requires licensees to ensure advisers undertake CPD appropriate for their activities.	✓	60 hours per three years; minimum of 7 hours per year
Experience requirements	✗		✓	Varies depending on qualifications
Code of Conduct requirements	✓ ✗	s1101A and RG183 permit ASIC to approve codes of conduct (mainly for purposes of opt-in which has now been removed) ASIC has not approved any Code to date	✓	TASA Code
Professional bodies	✗	3 accounting bodies recognised in Corps Regs for the purposes of verifying practitioner qualifications for limited licensing regime	✓	Recognises professional bodies
Application		Financial product advice provided by AFS licensees		Tax advice only (including advice on tax and superannuation laws) provided by TPB registered individuals and companies



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The Gaps

As previously discussed, ASIC in its capacity as Regulator of the Corporations Act, governs corporations and licensees, professional bodies set and enforce professional standards for their members who are individual practitioners on the 'frontline' interacting with and providing the direct service to consumers.

Professional bodies set obligations which individual practitioner members must adhere to. The benefits of professional membership are recognised by licensees, many of whom require their representatives to be a member of a professional body. As discussed throughout this submission, the ability of professional bodies to provide regulatory oversight of individual practitioners greatly complements ASIC's supervision of licensees.

To enhance the oversight of individual practitioners, the FPA believes government policy should recognise the value and consumer benefits of professional obligations by compelling membership of professional bodies.

This issue is discussed in more detail in *Attachment 2: FPA submission to the Inquiry into the performance of ASIC*.

Recommendation:

The FPA recommends the Committee propose

- the Government adopt a co-regulatory model to restrict the use of the terms financial planner and financial adviser to those who are a member of and hold a practicing certificate from a recognised professional body.
- the Parliament set and monitor performance goals (Key Result Areas - KRAs) for ASIC, and all regulators, that facilitates a co-regulatory model with professional bodies
- establishing Memorandum(s) of Understanding (MoUs) between ASIC and professional bodies to enable confidential information sharing on 'bad apples', bad practice and emerging risks; and facilitates and permits a more collaborative and cooperative two-way working relationship, or co-regulatory partnership.



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ToR b) the role of, and oversight by, regulatory agencies in preventing the provision of unethical and misleading financial advice

Co-regulatory model

The FPA presented its views on the role of and oversight by regulatory agencies, with clear recommendations, to this Committee's Inquiry into the performance of ASIC (see *Attachment 2: FPA submission to the Inquiry into the performance of ASIC*). The views and recommendations made in our previous submission stand and are still relevant to this Inquiry.

In summary, the FPA recommended that with a closer two-way working collaboration with professional bodies, ASIC could more effectively discharge its legislative mandate to support investor confidence, freeing up the Regulator to enable it to expand its legislative responsibilities into areas currently lacking in regulatory oversight. It also discussed FPA's belief that there must be a clear separation of advice from product.

Many, both in the industry and in political cycles, have suggested the introduction of individual licensing. However, this would require careful analysis and consideration of the risks and benefits, as well as the practical implications for how an individual licensing regime would work to ensure the desired outcomes are delivered and consumer protections are enhanced. Particular consideration should be given to the practicalities of and impact on the dispute resolution requirements, and structure of the professional indemnity insurance market and availability of PII for financial planners.

The FPA has previously called for a co-regulatory model that requires advisers to be individual voting members of a recognised professional body in order to practice and use the title financial planner or financial adviser. This model would see ASIC regulating the business, complemented by the profession overseeing individual practitioners.

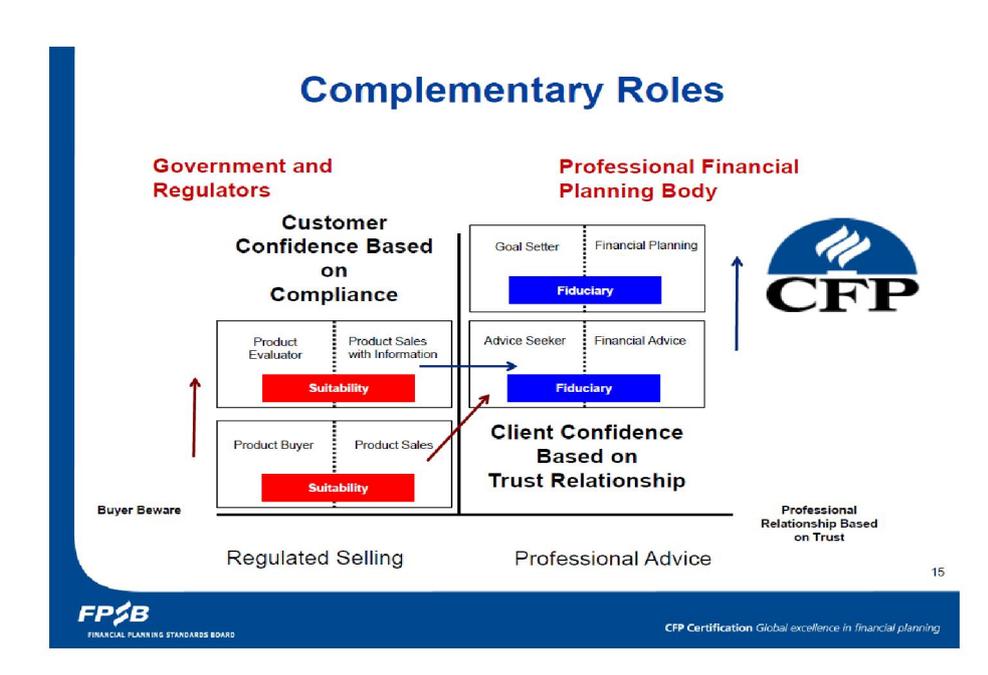
Co-regulation strengthens consumer protections by facilitating and encouraging the development, advancement and growth of professions:

- by improving the standards of practice of service providers and improving the regulatory capacity of professional communities, reducing the burden of regulation and supervision on government
- improving individual consumers' access to services and generating a higher contribution to the economy through service delivery
- enhancing the reputation and skills of practitioners by adherence to professional standards and CPD requirements specifically design for the type of service they provide to consumers
- by requiring the establishment and policing of standards that ensure community expectations of good practice are met
- as ASIC's powers relate to the corporations; obligations set by professional bodies apply to the individual practitioner, directly regulating individual conduct.

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The following co-regulatory model demonstrates the complementary roles of Government/Regulators and the profession.



The FPA recommends professional bodies should be recognised by the Professional Standards Councils (PSC). The PSC:

- was specifically established to recognise, monitor and enforce professional bodies to help industries and government raise the standards practitioners put into practice when delivering services to consumers. This is the sole purpose and speciality of the PSC.
- requires professional bodies to improve their professional standards by implementing robust risk management strategies and adhere to professional indemnity insurance standards
- recognised professional bodies must ensure members implement risk management strategies throughout their business and service deliver to continuously improve outcomes for consumers.
- aims to limit the occupational liability of practitioner members, which will drive down the cost of advice, reduce reliance on large licensees, and increases consumer protections.
- has demonstrated capacity and experience in the oversight of the professional body side of the co-regulatory model
- The PSC scheme is a successful demonstration of cooperative federal / state government initiative for the public regulation of professions through individual professional membership.



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The FPA does not support expanding ASIC's role to recognise professional bodies under our proposed Education and Professional Standards Framework.

Education and Professional Standards Framework

The FPA's submission to the Parliamentary Joint Committee Inquiry into the proposals to lift the professional, ethical and education standards in the financial services industry, further examined the need for a co-regulatory approach to preventing unethical and misleading behaviour (see *Attachment 3: FPA submission to the PJC Inquiry into the proposals to lift the professional, ethical and education standards in the financial services industry*). Our key recommendation to the PJC was:

To ensure consumers are protected, the FPA calls on the Committee to recommend the Government adopt a co-regulatory model that compels all providers of personal financial advice to meet higher education standards, and to restrict the use of the terms financial planner and financial adviser to those who are a member of and hold a practicing certificate from a recognised professional body.

The FPA proposed an Education and Professional Standards Framework which we believe would enhance the regulatory oversight of advice providers by leveraging existing bodies to minimise the regulatory impact of any reforms.

The FPA's framework acknowledges that the expertise and structures required to develop, implement and enforce professional and ethical standards, are fundamentally different to those required for identifying, developing and implementing appropriate education standards for financial advice providers. Hence, a co-regulatory model should be implemented via a dual holistic education and professional standards framework which includes:

1. An education framework - based on the existing Financial Planning Education Council's (FPEC) National Accreditation and Curriculum framework (see *Attachment 3: FPA submission to the PJC Inquiry into the proposals to lift the professional, ethical and education standards in the financial services industry* for further detail on FPEC), and
2. A professional and ethical standards framework - which leverages the existing additional oversight of advice providers through membership of recognised professional bodies.

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EDUCATION

Education Council
(FPEC)

- Council is independent and has representation of professional bodies and education providers
- Council is funded by professional bodies and education providers (no institutions so as to remove any conflicts)
- Sets education for all providers of personal advice
- Sets national curriculum for education providers to meet minimum education standards
- Approves education courses as meeting minimum education standards
- Sets and approves bridging options to meet minimum education standards
- Audits education providers
- Maintains register of approved education providers/courses that meet curriculum

STANDARDS

ASIC

- Licensing
- Register
- Enforce Corporations Act
- Provide regulatory guidance to comply with the law

TPB

- Tax Agent Approval
- Register
- Enforce TASA requirements
- Set minimum CPD
- Set minimum experience requirements
- Provide regulatory guidance to comply with the law

Professional Standards
Council

Recognised Professional
Bodies
(i.e. meet criteria recognised by PSC)

- Set entry standards for members
- Set Code of Conduct for members
- Set Professional standards for members
- Set CPD requirements for members
- Has responsibility for enforcement of the Code, Standards and CPD on members
- Financial Advisers/Planners must be members of a recognised professional body



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Recommendations:

The FPA recommends the Committee support:

- The development and implementation of a co-regulatory design, which recognises and facilitates the role of 'recognised' professional bodies in assisting the regulator to achieve its consumer protection and confidence mandates
- Professional bodies to be recognised by meeting certain qualification criteria - through the Professional Standards Council (PSC)
- The use of the titles financial planner and financial adviser to be permitted only by individuals holding a Practising Certificate as a member of a recognised professional body
- An holistic Education and Professional Standards Framework that leverages existing networks and bodies to minimise the regulatory impact on all stakeholders.



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ToR c) whether existing mechanisms are appropriate in any compensation process relating to unethical or misleading financial advice and instances where these mechanisms may have failed

The FPA believe consumers deserve a substantially improved consumer compensation regime in financial services. This is best achieved by an improved regime that protects consumers from poor products and poor advice in the first instance, supported by an improved obligation regime that will deliver better justice and compensation to consumers in the event of fault.

The FPA detailed our concerns about the current compensation system in our submission to the Review of compensation arrangements for consumers of financial services, undertaken by Richard St John in April 2011 (see *Attachment 4: FPA submission to the Review of compensation arrangements for consumers of financial services*). The FPA notes that while the recommendations made by Mr St John have been considered by subsequent Inquiries, many have never been implemented. Therefore, the issues discussed in our submission are still relevant in the current environment.

The FPA further discussed these issues in a FoFA context in its submission to the PJC Inquiry into the collapse of Trio Capital and related matters (see *Attachment 5: FPA submission to the PJC Inquiry into the collapse of Trio Capital and related matters*). This submission also discusses instances where such mechanisms may have failed, such as for consumers with self managed super funds.

Australian consumers of financial services deserve a compensation regime that not only offers comprehensive redress but that also acts to improve the financial services industry for future consumers.

Achieving that goal requires a complete overhaul of Australia's compensation regime to recognise its influencing role in a broader consumer protection regime designed to protect consumers from poor products and poor advice in the first instance. When supported by an improved obligation regime that attaches responsibility for compensation to the parties with a causal link to the fault, we can deliver better compensation to consumers and positive reform to the industry.

A fundamental concern of the current consumer compensation system in Australia is its reliance on professional indemnity insurance (PII). There is an extreme inadequacy and unavailability of PII for financial planners and licensees in Australia. This issue differs significantly from other global jurisdictions, hence the FPA would caution against assuming compensation methods of other countries would work effectively in the Australian market.

This is not a fault of the advice industry but the lack of regulation of other financial service providers, namely product providers. In assessing the risk of a licensee, the PII industry commonly look at the products in the market and assess the risks associated with the products, rather than the quality of the advice.

The lack of regulation and accountability on product providers, the absence of proportionate liability from the compensation system, and the reliance on financial planner PII requirements for consumer compensation, essentially means that PI insurers charge licensees for all risks in the financial services market as financial planners are the most likely avenue for consumers to access compensation.



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Australia cannot afford to have an adequate compensation system or a penalty system for inadequate PII if there is not an adequate PI market to choose from in the first place.

The PII problem in Australia will not be fixed by the introduction of a scheme of last resort. This will only exacerbate the issue as licensees seek to gain additional cover against the likelihood of incurring a future levy for someone else's wrong-doing.

The opportunity to improve consumer compensation should also be considered in the context of improving the link between causal responsibility (fault) and the remedies that should be available (both in terms of justice and compensation).

It is well established that, rather than all fault lying with the advice provider, there are multiple stakeholders who offer products or services within the financial planning value chain, all of whom influence consumers' decisions on financial matters. However accountability of these participants to the end client is variable, limited and for some practically non-existent.

Each of these stakeholders play some part, either directly or indirectly, in influencing a consumers' decision to invest in a financial product and the ongoing stability of that product, and each has responsibility to the client and their compensation needs for the role they play.

Instead of a suggestion for another layer of financial obligation that will deliver additional redress to only a few consumers without any improvement in the overall compensation and protection regime, the FPA's proposal for an improved compensation system includes:

- Improved regulation of financial products
- Introduction of best interest obligations on all participants of the financial services system
- Improved quality and type of product disclosure
- Introduction of a penalties regime for product manufacturers
- Improve standards of licensee conduct
- Improve consumer financial literacy and supportive education
- Improve the market for Professional Indemnity Insurance

This view aligns to the intent of the FoFA reforms and ensures better gatekeeper regulation that works in the full interests of Australian consumers.

A better consumer protection and appropriate consumer compensation regime is the responsibility of all participants who have a role in causing, or an influence in allowing, consumer detriment. Until the regulatory and compensation framework is able to ensure that each stakeholder has responsibility and financial accountability to the end client for their role in ensuring the effective and ethical delivery of products and services, then the FPA is unable to support a proposal for a Financial Services Claims Scheme (FSCS) that appears to attach further liability and obligation to the financial advice community alone or at least in a disproportionate way to other participants with an often greater capacity to cause detriment on a community wide scale.

The FPA believe there is a need to find solutions to the underlying issues in the marketplace and supporting laws, rather than *additions* to the system that is intended to only apply to financial advice and fail to address the opportunity for application to the entire system of financial services more broadly. Such an approach is only likely to exacerbate the problems in the future.



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The FPA strongly believes that the debate must encompass all in the financial services community and we must all, as participants, take responsibility for our actions. Continuing to only concentrate on one aspect or participant of the financial services sector continues to deny consumers their right to fair and equitable justice when failure occurs.

Recommendations:

The FPA recommends the Committee review the recommendations made by Richard St John and consider whether they are appropriate to implement in the current post-FoFA regulatory environment.



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ToR d) mechanisms, including a centralised register, that would ensure financial planners found to have breached any law or professional standards in their employment are transparent, for both the sector and consumers

Adviser Register

The FPA acknowledges and supports the work the Government has undertaken to develop an Adviser Register through its Industry Working Group (IWG). An Adviser Registry is vital as it will provide consumers with greater transparency into the financial advice profession. More importantly, it will enhance consumer protection as it provides an authoritative source of validation about each individual financial planner and financial adviser and their bone fides.

The FPA notes that on 27 November, Treasury released the Exposure Draft of the *Corporations Amendment (Register of Relevant Providers) Regulation 2014* to:

- enable ASIC to establish and maintain a public register of financial advisers; and
- for Australian Financial Service licensees to collect and provide information to ASIC concerning financial advisers that operate under their licence.

Recommendation:

The FPA recommends the Committee disregard this Terms of Reference as the Regulations to implement the National Adviser Register have been drafted and therefore this matter has been dealt with.

Licensee due diligence

In 2007, ASIC released a voluntary standard aimed at improving pre-employment reference checking within the financial services industry to limit the ability of individuals with previous unprofessional behaviour from moving between licensees (see *Attachment 6: Reference Checking in the financial services industry*). This standard was developed jointly with the FPA and has been widely supported by the financial services industry.

Industry supports the need for due diligence when appointing new planners, such as background checks, as well as supervision once a new representative has commenced with a licensee. However, licensees are concerned that the ASIC standard does not provide protections from potential defamation action, should they follow all the requirements in the standard.

The FPA notes the role of the new Adviser Register in assisting industry with background checks on new representatives.

Recommendation:

The FPA recommends the Committee consider how the ASIC 'Bad Apples' standard can be adapted to become a licensee requirement while protecting licensees from potential defamation action.



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ToR e) how financial services providers and companies have responded to misconduct in the industry

As demonstrated in *Attachment 1: Summary of FPA professional framework*, a profession puts in place proactive and reactive measures to combat bad behaviour and misconduct. Reactive measures include accountability and disciplinary action, as well as the collection of data to identify emerging issues. Proactive measures are then put in place to combat potential issues from emerging and to tackle bad behaviour and issues that may lead to deliberate misconduct.

Since 2009, the FPA has expelled terminated 26 individuals for misconduct related breaches of our professional obligations; and sanctioned 12 other individuals for bad behaviour.

The FPA, like other professional bodies, has systems in place to monitor, detect and respond to *misconduct* by our own members, and to encourage reporting when our members discover misconduct by someone else.

FPA has available disciplinary systems for our members. FPA makes avenues publicly available to those who chose to participate in the financial planning profession to encourage the reporting of suspected misconduct through FPA confidential.

Financial advice providers have recognised the need to lift the standards of the advice provided to consumers. This has been evidenced by the recent announcements made on education standards by many of the financial institutions.

The profession itself is leading the way in raising standards in a manner that will minimise any impact of the change on the provision of financial advice services and on consumers. Many of these organisations now require membership of a professional body for all their representatives.

Recommendation:

The FPA calls on the Committee to recommend the Government adopt a co-regulatory model to restrict the use of the terms financial planner and financial adviser to those who are a member of and hold a practicing certificate from a recognised professional body.



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ToR f) other regulatory or legislative reforms that would prevent misconduct

Defining advice for the consumer

Consumers are continuing to be misled by those selling a product under the guise of financial advice.

This issue has been raised by the FPA in several Parliamentary Inquiries with a number of recommendations to address this issue through our 10-point plan to raise the standards of advice for consumers. Fundamental to this issue is the need for the separation of advice from product selling.

This can only be achieved through a change to the definition of 'general advice' in the Corporations Act to underpin the achievement of the objective of the Inquiry to improve consumer protections in the financial services industry.

There is a high level of confusion in the market, within industry, media, Government and consumers about the definitions and roles of financial advisers and financial planners, and those that sell financial products.

Some consumers incorrectly mistake the use of the word 'advice' to be a standard definition when in fact there is a significant legal and technical difference between 'general' and 'personal' advice.

The Law defines the act of providing 'financial product advice', specified as general advice and personal advice:

- Personal advice (s766B) is given when the provider of the "financial product advice" has considered one or more of the consumer's objectives, financial situation and needs.
- General advice is financial product advice that is not personal advice.

We are concerned that defining financial product advice on this basis makes it more difficult for consumers to distinguish personal financial advice from marketing material or product sales. This risk is confirmed by ASIC's *Report 384 – Regulating Complex Products*, where the Report states;

*"Our research has indicated that marketing information plays a particularly strong role in product distribution and may influence investors' decision making more than other product disclosure. In particular, when investors approach product issuers or other intermediaries responsible for selling products directly, rather than going through advisers, the information contained or implied in product issuers' marketing information is often the first, and may be the only, information that investors use to decide whether or not to invest in that product."*⁷

Framing 'general advice' as advice plays into the behavioural aspects of financial decision-making by giving the impression that the advice has a reasonable basis or is appropriate for the client, and thereby exposes retail investors to decisions made under uncertainty about the regulatory framework for that advice. Anecdotal evidence shows that it is common for individuals to interpret general advice as personal advice because it is relevant to their circumstances at the time it is provided. To ensure consumers can easily distinguish between the various roles and services in the financial services

⁷ ASIC, *Report 384 – Regulating Complex Products* (January 2014), at [46]



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sector, providers of general or product information should not be permitted to use the titles financial planner or financial adviser.

Recommendations:

The FPA recommends the Committee support additional consumer protection measures by recommending:

- General Advice be re-termed 'general or product information' and be limited to the provision of 'factual information and/or explanations' relating to financial products.

We also reiterate our recommendation that the use of the titles financial planner and financial adviser be permitted only by individuals holding a Practising Certificate as a member of a recognised professional body.

Wholesale / retail definitions

The FPA does not believe that the current regulatory structure appropriately identifies and addresses the needs of various end users of the financial system. This is particularly true of the way that the Corporations Act defines categories of end users and regulates financial services differently depending on the end user – under the definitions of wholesale investor, sophisticated investor, and retail investor. There are weaknesses in the current system because:

- the distinction is based on the wealth of the investor, rather than a measure of their financial literacy;
- the distinction does not incorporate behavioural elements into the categorisation or basic understanding of how these participants will operate;
- the distinction functions to remove judgement and discretion from financial intermediaries regarding their conduct towards clients with differing degrees of financial capability, and;
- the distinction, when paired with a disclosure-based system of regulation, encourages documentary compliance with little consumer protection benefit or improvement in financial capability or opportunity.

The FPA proposes alternative regulatory schemes which better address the realities of the end user's engagement with the Australian financial system:

- Investor/consumer: Market participants could be categorised with respect to the purpose they have engaged with the financial system. In particular, users who rely on carrying risk for profit as the basis of their use of the financial system should have different regulatory rights and obligations to users who purchase financial products as a consumer.^[1]

^[1]For more detail on the investor/consumer distinction, see Niamh Moloney, 'The Investor Model Underlying the EU's Investor Protection Regime: Consumers or Investors?' (2012) *European Business Organization Law Review* 13, 169-193; Dimity Kingsford-



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- Suitability regulation: Suitability regulation may also be appropriate outside of recommending complex products. If financial intermediaries are required to form a judgement about the financial capability of the clients they serve, it will help them to tailor their disclosure obligations to the needs of the client and to reasonably adjust the scope of their professional obligations to those needs as well.
- Institutional/individual: This distinction relies on the institutional checks and balances available to the client in order to mitigate behavioural, capability, and exclusion-based inefficiencies. Where suitability regulation is intended to respond to the unique financial capability of the client, regulation which focuses on the ability of the investor to access financial intermediaries to help that investor make better financial decisions.

Recommendation:

The FPA calls on the Committee to recommend a review of the definitions of 'retail', 'wholesale', and 'sophisticated' investors in the Corporations Act.



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ToR g) any related matters

Gatekeeper and product regulation

The FPA has made recommendations to previous Inquiries regarding the oversight of gatekeepers and products, including research houses.

While the objective of the FoFA reforms was to improve consumer protection and the quality of advice, there has been very limited progress / changes to mirror this intent in relation to financial products that are developed for retail clients.

Regulators in Australia serve a vital role in protecting consumers of financial products and services. This role includes the oversight of the various gatekeepers in the market. While each sector of the financial market has a gatekeeper role to play, the current regulatory system fails to hold all gatekeepers accountable for their actions.

The ASIC Chairman, Greg Medcraft, in a speech to the Senate Economics Legislation Committee⁸ stated his view that gatekeepers are important in our financial system. “Gatekeepers actually form a cornerstone of the system. Making sure they are held to account is actually quite important. I include in that accountants, financial planners, product manufacturers and distributors and also lawyers—even though we do not regulate them, they are advisers to key participants in the system.”

Only focusing on advice and those licensed under Chapter 7 of the Corporations Act excludes many parties who have been proven in the past to have contributed significantly to dishonest and fraudulent behaviour and insolvencies that have resulted in detrimental consumer loss, such as Trio Capital, Opes Prime and Westpoint.

For example, ASIC has pursued charges and sought consumer compensation from Westpoint directors, the CEO and founder, and even the auditors of Westpoint for their role in the loss incurred by investors from the collapse. In addition, some reputable research houses continued to give the product a highly positive rating. However, a high proportion of consumers impacted by the Westpoint failure did not seek advice. Most consumers invested directly with the product provider or through a broker. In the case of Basis Capital, glowing reports and high ratings were received from several research houses. This influenced financial planners' views of the product and consumers decision to invest in the product.

There are multiple participants who offer products or services within the financial advice value chain, all of whom influence consumers' decisions on financial matters.

Product Providers (including platforms)

There are a variety of financial services providers who can and have played a part in dishonest conduct and insolvency events that have impacted on consumers, while not always providing a service directly to a retail client.

Many products are sold directly to consumers who may not have the capacity to clearly identify and assess the complex elements that would go into making such a determination. Though such

⁸ Hansard Senate Economics Legislation Committee, 31 May 2011



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investments may be appropriate for some investors, a degree of protection is needed for those who are more vulnerable.

For example, a product provider such as Trio Capital is the “Responsible Entity” of the company. It has legal obligations to employ a series of ‘third-party gatekeepers’, such as auditors to audit the companies finances and sign off on compliance plans. Auditor reports indicated the Trio funds complied with all requirements and were included in positive reports on the funds produced by various research houses.

The FPA recommends a holistic and appropriate solution to consumer protection should be considered by reviewing the regulation of financial products available to consumers.

Problems with products should be addressed through product regulation, rather than advice regulation. Product providers should be held accountable for failing to deliver on product benefits due to dishonest conduct, fraud or insolvency, or if there are fundamental flaws in products.

The FPA absolutely acknowledges that financial advice and some financial planners played a role in the consumer detriment resulting from previous product collapses. The banning of investment commissions and the introduction of the adviser ‘best interest duty’, in particular, under FoFA will significantly reform the advice industry and improve the protection of all consumers who receive financial advice. What is still not being addressed are the issues of product reform.

There is a vital need to enhance the responsibility of product providers and fund managers in developing products for consumers, and ensuring compliance with Responsible Entity requirements. There is also a need to ensure product providers and their appointed third-party gatekeepers are held accountable for any wrong-doing resulting in consumer loss.

Research Houses

Australian consumers rely on information from credit rating agencies and research houses to make investment decisions, so they play an important gatekeeping role in the financial system. The role of such organisations is to provide specialist assessments and detailed due diligence research on financial products for consumers and intermediaries. It is a specialised service, which comes at considerable expense. Research houses should also be held accountable for their roles in product failures.

There is a need for effective regulation within the retail wealth management chain so that each stakeholder takes responsibility and accountability to the end consumer for their role within the chain for the effective and ethical delivery of services to consumers.

The FPA acknowledges the current licensing and regulatory requirements placed on research houses, including the requirement to hold an Australian Financial Services License (AFSL), meet general advice obligations, disclosure of conflicts of interest, and dispute resolution membership. However, the FPA believes the current requirements are not effective in protecting consumers given the influence research houses have, either directly or indirectly, on consumers’ investment decision.

The role of research houses must be determined by the way in which their clients use their publications and services, the different industries within the financial services sector, and the influence their research has (directly or indirectly) on the end consumer.

The FPA believes there is a disconnect between the role research houses believe they have and the role they actually play in the provision of financial service to Australian consumers.



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- Australian consumers rely on information from research houses, either directly or indirectly, to make investment decisions;
- Consumers and intermediaries use/view the material produced by research houses as detailed due diligence research and specialist assessments of financial products.
- Product information available to financial planners (from product providers) is generally inadequate in relation to assessing suitability for individual clients. Therefore they must utilise the specialised research capabilities research houses offer.
- Licensees and financial planners use the information provided by research houses as an input for approving funds and products for Licensees' Approved Product Lists (APLs) and ultimately for recommendations to consumers.

A clear example of research house influence in an Australian product failure, is Basis Capital. Basis received glowing reports and high ratings from several research houses. This influenced financial planners' views of the product and consumers decision to invest in the product. The majority of consumers who invested in Basis were under advice.

Westpoint is another notable example where some reputable research houses continued to give the product a highly positive rating. However, many consumers impacted by the Westpoint failure did not seek advice. Consumers invested directly with the product provider or through a broker.

In the case of Trio Capital, it appears research houses relied on information provided by the product provider and failed to conduct independent investigations even though the information released by the product provider was restricted based on 'private investment contracts' and was inconsistent.

While Government and regulators have strengthened the regulations around product advertising (for example), little has been done to address the underlying issues within the research house industry that played a significant role in the collapse of these financial products.

The licensing requirements for research houses are dependent on the services the entity provides. If they provide services to wholesale clients only (such as licensees and advisers), they are not required to be licensed; if they provide services to retail clients, they are. In addition, we note that ASIC requirements regarding product manufacturers including in their PDS information sourced from research houses. Product manufacturers must gain consent from the research house to include any information they provided to the product manufacturer (wholesale client) in the PDS. In giving consent the research house is in effect agreeing to the provision of its information (via the product manufacturer) to retail clients, and as a result must have professional indemnity (PII) insurance and be a member of an external dispute resolution (EDR) scheme to support the provision of information to retail clients.

However, the FPA questions the benefits of EDR, compensation arrangements and PII for research houses as, in the main, their clients are wholesale clients (usually other licensees who are prohibited under the Corporations Act from making a claim through these mechanisms) even though the service provided by research houses influences the retail clients' decision. It is also very difficult, near impossible, for a retail client to provide causal link evidence of the failings of the research house to the event at the cause of the loss. This is exacerbated by the exclusion from PII cover (RG126.23)



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and EDR (RG139 and FOS Terms of Reference) of product failures and claims for loss solely as a result of the failure (e.g. through insolvency) of a product issuer.

Recommendations:

The FPA recommends

- the Committee recommend Government and Treasury undertake a detailed review to change legislation and regulations to strengthen ASIC's regulatory obligations and oversight of all gatekeepers, particularly financial product providers and research houses..
- legislation be amended to oblige ASIC to take a larger role in the regulatory oversight financial products before they are released for consumer investment.

(The FPA has provided detailed recommendations on the regulation of financial products and research houses in *Attachment 7: Recommendations to improve the regulatory oversight and accountability of product providers and research houses.*)