

FINANCIAL PLANNING
ASSOCIATION *of* AUSTRALIA



5 November 2013

Senator David Bushby
Chair
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600

Email: economics.sen@aph.gov.au

Dear Senator Bushby

Re. Senate Inquiry into the performance of the Australian Securities and Investments Commission (ASIC)

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

The Regulator plays a fundamental role in ensuring the confidence and protection of consumers which is paramount to the effective and sustainable operation of the financial service sector in Australia.

The FPA would welcome the opportunity to discuss these issues further. The FPA would like to formally register our interest in appearing before the Committee, should the Committee determine it appropriate to undertake hearings on this matter.

If you have any questions, please contact me or our General Manager Policy and Conduct, Dante De Gori

Yours sincerely

Mark Rantall
CEO
Financial Planning Association of Australia¹

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 Professor Dimity Kingsford 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. As at the 1st July 2013 all new members of the FPA will be 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

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The performance of the Australian Securities and Investments Commission

FPA submission to:
Senate Economics References Committee

4 November 2013



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Contents

	Page
The Terms of Reference of the Senate Inquiry	2
1. Introduction	3
2. Regulatory Design	5
What is professionalism and professionalisation?	9
Role of professional bodies	10
Legal facilitation of co-regulation	12
Support co-regulation	14
Issues of dual-regulation in regulatory design	17
3. The role of gatekeepers and ASIC obligations	23
Product Providers (including platforms)	25
Research Houses	28
Attachment 1: Summary of FPA requirements	32
Attachment 2: Precedent for co-regulation	40
Attachment 3: Regulator approved professional body	47



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The Terms of Reference of the Senate Inquiry

The Senate Economics References Committee has been asked to undertake an inquiry into and report on the performance of the Australian Securities and Investments Commission (ASIC), with particular reference to:

- A. *ASIC's enabling legislation, and whether there are any barriers preventing ASIC from fulfilling its legislative responsibilities and obligations;*
- B. *the accountability framework to which ASIC is subject, and whether this needs to be strengthened;*
- C. *the workings of ASIC's collaboration, and working relationships, with other regulators and law enforcement bodies;*
- D. *ASIC's complaints management policies and practices;*
- E. *the protections afforded by ASIC to corporate and private whistleblowers; and*
- F. *any related matters.*



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

1. Introduction

The FPA supports the Federal Parliament's decision to call on the Senate Economics References Committee to undertake an Inquiry into the performance of ASIC.

ASIC has an important role play in the financial services system, confidence (whether real or not) in the Regulator is paramount not only for the market but more importantly to investors. Confidence drives behaviour and stimulates investment, which creates jobs and economic growth.

The FPA therefore has taken this opportunity to provide constructive feedback and recommendations that will enable confidence and support to be improved.

In considering the performance of ASIC, we do acknowledge the work the Regulator has done on the protection of Australian consumers, and some improvements ASIC has made over the years including:

- Progressing Australia's financial literacy strategy, and specifically the success of MoneySmart.
- Recent increase in ASIC enforcement activity.
- Engagement with and access to senior ASIC employees, particularly for the purposes of industry presentations and training.

It is also important to understand the restricted resources of ASIC given its responsibilities in overseeing the regulation of all corporations operating in Australia. The FPA believe the need to balance respectively limited resources and regulatory oversight responsibilities has pushed ASIC to operate more as an 'after-event' or reactionary Regulator with limited operations in proactive oversight or ongoing supervision and monitoring.

The FPA notes ASIC's role as the Regulator overseeing the Corporations Act extends beyond the financial services sector, to govern all corporations and companies. While the FPA's submission draws on our experience as a professional body in the financial services sector, the issues we articulate and the recommendations we propose offer regulatory enhancements and efficiencies for all industries governed by ASIC as we believe they will support and re-direct the Regulator to focus on its core and most valuable consumer protection role of preventing and prosecuting matters of dishonest and fraudulent conduct.

The FPA recommends 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.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The FPA supports the Terms of Reference focus on identifying issues and constraints in the regulatory environment within which ASIC must operate. However, the FPA believes ASIC over-reaches in some areas, and under-reaches in others, leaving consumers of financial products and services unprotected in some instances and exposing them to unnecessarily high risks.

The FPA urges the Committee to also consider current gaps in ASIC's legislative responsibilities and obligations which significantly undermine consumer protection measures in Australian financial services law.

Of equal importance when examining ASIC's performance is the perception and expectations consumers, politicians, the media, and industry participants have regarding the role, powers and actions of the Regulator. While some may support ASIC's past performance based on their understanding of the role, powers, and resources of the Regulator; others may hold different expectations and be extremely disappointed and critical, particularly in the area of consumer compensation. Carefully identifying and managing stakeholder expectations can assist in addressing the legislative and regulatory gaps impacting consumer protection.

Structure of the FPA submission

As a professional body, the FPA takes very seriously its obligation to provide advice to Government that is credible and that considers: the public interest and consumer protection implications; the impact on the community standing of the financial planning profession; the effectiveness and efficiency of regulation; and the alignment with the FPA's professional obligations.

With that in mind, we have taken the opportunity to provide a detailed submission that not only addresses the stated Terms of Reference but also seeks to address the real issues that we believe will lead to more effective regulation of the financial services sector, better consumer protection, and a more efficient marketplace in financial products and services. The FPA has drawn on the experience of past high profile consumer protection issues in financial services to illustrate our concerns.

For the benefit of the Committee and readers, our submission is constructed as follows:

Section 1: The regulatory design – this section examines issues and limitations of the existing regulatory design, and presents alternative regulatory approaches that support ASIC in protecting Australian consumers.

Section 2: The role of gatekeepers and ASIC obligations – when a serious financial loss occurs, investors and clients are left shocked, angry and confused. This section will discuss the role gatekeeper participants have in influencing consumer behaviour and decisions, and highlight the failings and legislative gaps in consumer protection that limit ASIC's performance in protecting consumers and regulatory oversight of industry participants.



The performance of ASIC

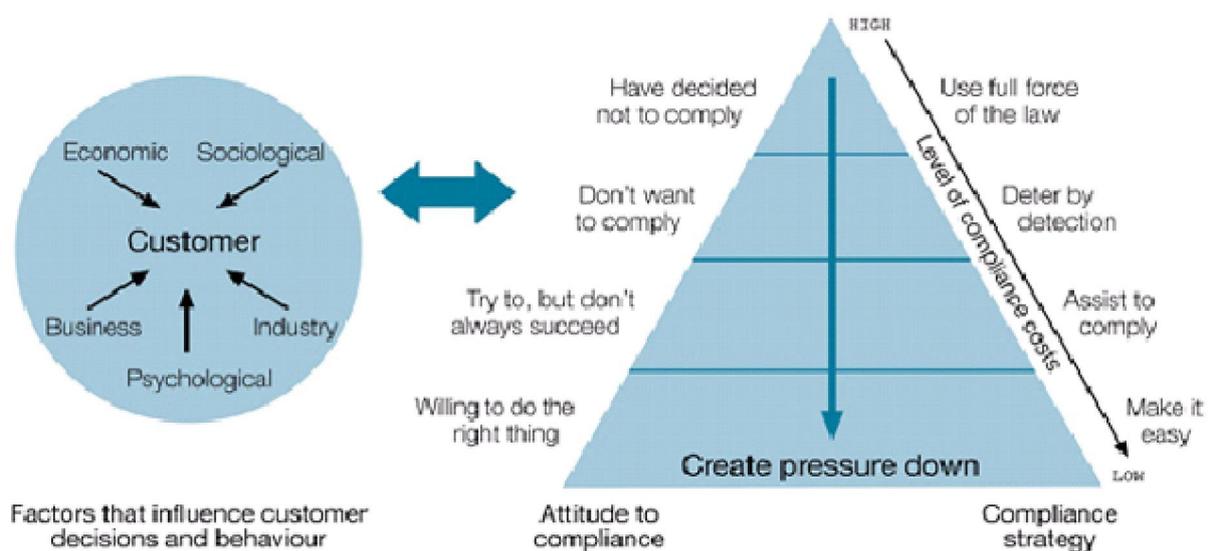
SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

2. Regulatory Design

This section relates primarily to Terms of Reference C. *the workings of ASIC's collaboration, and working relationships, with other regulators and law enforcement bodies*; and F. *any related matters*. However, it also touches on issues relevant to Terms of Reference B. *the accountability framework to which ASIC is subject, and whether this needs to be strengthened*; and D. *ASIC's complaints management policies and practices*.

ASIC's role as Regulator of the Corporations Act is to ensure Australia's corporate, markets and financial services are fair and transparent, and supported by confident and informed investors and consumers². ASIC has powers to protect consumers against the misleading or deceptive and unconscionable conduct of all financial product and service providers.

When the reaction of the Regulator is tied to the behaviour of the provider, it is known as a responsive compliance model³ often represented as a compliance pyramid.



The shape of the compliance pyramid indicates:

- the number of clients that might be found at each level in the model,
- the hierarchical and escalating nature of regulatory engagement, and
- the increasing focus towards the apex on the small minority who appear to deliberately seek to contravene the system.

² www.asic.gov.au/ourrole

³ The responsive compliance model was suggested by [Ian Ayres](#) and [John Braithwaite](#) in their book "Responsive Regulation: Transcending the deregulation debate"⁴ which built on earlier work by [John Scholz](#).



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The choice of remedy (e.g. financial penalties, criminal imprisonment) imposed by the Regulator becomes increasingly severe higher up the pyramid – with the view of creating an incentive for entities to move towards more compliant behaviours.

This approach has been widely adopted, particularly within Australia. It is also described as the Enforcement Pyramid by some regulators although enforcement is only one of the compliance strategies implicit in the model. The strength of the model is the Regulator being seen to apply the right remedy to the right situation, by taking an entity's apparent motivation (including their efforts to comply) into account.

Former ASIC Chairman, Jeffery Lucy, described the Commission's regulatory approach in terms of a tri-partite pyramid. At its base are those who comply with the law. For this group, ASIC sees that its role is "to provide guidance to help them continue to comply." The middle group contains opportunists who are "prepared to bend the rules if they think they can get away with it." ASIC's strategy with this band is to influence their views and conduct. The peak of the ASIC pyramid consists of those who engage in improper and illegal behaviour. ASIC uses its full enforcement strength to regulate this group.⁴ ASIC places a strong emphasis on enforcement as the essential component of effective regulation. It also acknowledges the importance of longer-term education and persuasion, in guaranteeing the success of regulatory enforcement. This approach is articulated in ASIC Information Sheet 151 *ASIC's approach to enforcement*.

However, Information Sheet 151 and Information Sheet 145 *ASIC's compulsory information-gathering powers*, also demonstrate the need to deliberately limit ASIC's powers to ensure the Regulator is able to "direct their finite resources appropriately". The Information Sheets state that ASIC does not undertake a formal investigation of every matter that comes to the Regulator's attention; and further, that a number of ASIC's compulsory information-gathering powers can only be used when the Regulator is actually conducting, or intending to conduct, a formal investigation.⁵

Further, Information Sheet 151 states that:

We can seek a remedy that punishes a person or entity in response to a wide variety of types of misconduct, from minor regulatory offences (e.g. failure to file a form) through to serious offences involving dishonesty or that have a large impact (e.g. through loss of investor funds or damage to the integrity of our markets).

However, many submissions provided by consumers to the Senate Inquiry indicated that ASIC was unable to assist them in relation to their complaint. Our review of these submissions indicate that in most of these incidences, the complaints related to minor regulatory offences at the bottom sections of the regulatory pyramid. This highlights the mis-alignment between the consumer perception of the role ASIC should play in assisting them when things go wrong, versus what ASIC can actually deliver.

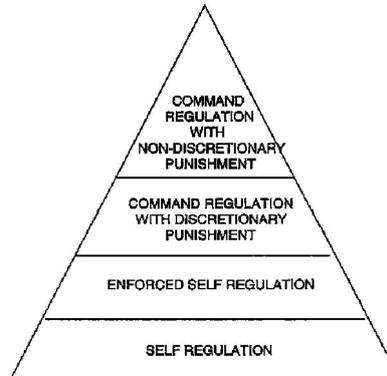
⁴ Regulatory Institutions Network, Applications of responsive regulatory theory in Australia and overseas, June 2010.

⁵ Information Sheet 151 *ASIC's approach to Enforcement*; and Information Sheet 145 *ASIC's compulsory information-gathering powers*



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013



While we understand the constraints on ASIC's resources, the FPA believes the 'bottom portions of the regulatory pyramid are a vital part of the overall protection of consumers. Regulatory design, and ASIC's role, is not just about responding to complaints or acting when things go wrong. As indicated by ASIC's annual reports, setting standards, education, and guidance, among other regulatory components, are a vital part of effective regulatory design. These base sections of the pyramid offer a vital avenue for identifying, monitoring and responding to emerging trends of market behavior and practice that impact on consumers.

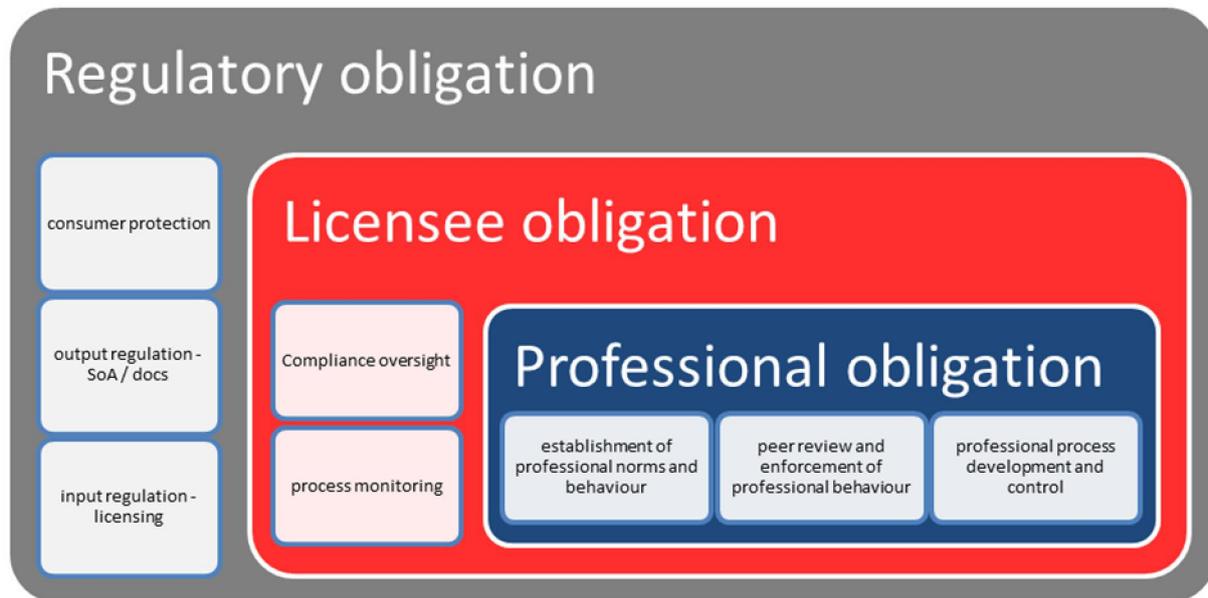
The FPA suggest there is a fundamental need to recognise, in the regulatory design, the role professional bodies can play in assisting ASIC to achieve its mandate under the ASIC Act, in order to maximise the capabilities of the system, as a whole, to improve overall consumer protection, particularly in relation to the bottom sections of the regulatory pyramid.

The FPA believes the regulatory design should be a dynamic interaction between the government imposed legal requirements, the licensee business imposed rules, and the expectation of professional participants as codified in professional obligations. This model is based on the 'best practice' Accountable Governance approaches proposed by O'Brien (2010) and Sanders (2010) and also the Australian government's Office of Best Practice Regulation Handbook 2007, all of which emphasize the regulatory benefits of the separation of complementary roles between the Regulator, the regulated, and the professional bodies.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013



As illustrated by the above diagram, in the financial planning profession individual financial planner behaviour is subject to a series of inter-locking obligations. To encourage improvements in individual planner behaviour, the regulatory design must be effective for all three areas of obligation - regulatory, licensee and professional. Without formal recognition and encouragement of adherence to professional obligations, there is a gap in the regulatory design as applied to individual providers of financial services to consumers, and consumer protection becomes reliant on the limitations of regulatory and licensee obligations alone.

The FPA's professional obligations and activity are focused on the part of the financial services sector to which the FPA belongs, that is the financial planning profession. Our obligations and activity are specifically designed to govern the conduct of our members in the provision of financial planning services to consumers, and in turn the needs of the consumers seeking the services of our members. Therefore, they have a significant impact on the conduct of our members and the consumers they serve.

Industry specific obligations set and enforced by professional bodies, greatly complement the requirements of Corporations Law regulated by ASIC. Corporations Law requirements are overarching and do not speak to the specific roles, services, and interactions provided to consumers by the various industries within the Australian financial services sector. Professional obligations are industry specific and are a vital part of the regulatory design.

The FPA therefore, believes the role of professional membership and obligations must be recognised in the regulatory design, including ensuring the legal environment facilitates the establishment of co-regulatory approaches between professional bodies and regulators.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

True co-regulation, enabled by supporting legislation requiring membership of a Regulator recognised professional body, and based on a collaborative two-way partnership between the Regulator and professional bodies, is a cost-effective way to enhance consumer protection.

Setting performance measures concerning the bottom half of the regulatory pyramid will help ASIC to appropriately resource allocation decisions between its current focus on high end enforcement activity versus capacity building to complement and encourage the development of relationships with professional bodies at the bottom end of the pyramid.

In the medium to long term, investment in these systems of regulatory power is likely to prove far more cost effective and be a more responsive mechanism for consumer redress.

What is professionalism and professionalisation?

The Australian Council of Professions defined a profession as:

“..a disciplined group of individuals who adhere to ethical standards and uphold themselves to, and are accepted by the public as possessing special knowledge and skills in a widely recognised body of learning derived from research, education and training at a high level, and who are prepared to exercise this knowledge and these skills in the interest of others”.
(Australian Council of Professions, AGM, 1997)

Another way of identifying professionalism is to consider the leading structures, routines and practices of a professional association. For example, Friedman, Hanson and Williams⁶ suggest that a professional association will have three main pillars of operation: entry standards, ethical codes with a complaints and discipline regime and finally, continuing professional education and other positive supports to professional conduct.

Sometimes professional associations will be the sole source of regulation of the professional group although these days it is more usual to find statutory support for the professional group's regulatory role. This is true of the legal and medical professions in Australia. In some instances, the professional body works side-by-side with a government regulator which registers or licenses the individual professional or the business entity they practice through. This is the position of financial planners under the Corporations Act who are also members of the FPA.

Professionalisation is the process over time by which a group of occupational participants differentiate (membership entry requirements, education, experience etc) to adopt agreed norms of behaviour (professional conduct, codes of ethics, practice standards), become accountable to higher ethical and professional standards than required by legal minimum requirements (professional accountability, complaints and discipline systems) and the community comes to confer social status (professional recognition) upon the occupational group.

⁶ A Friedman, W Hanson & C Williams 'Professional Standards Bodies: Standards, Levels of Compliance and Measuring Success' Financial Services Authority, (25 Sept 2009) at: <http://www.compliance-exchange.com/governance/library/pamreportethics.pdf>



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

To guarantee the necessary focus by ASIC, the Parliament must set and monitor performance goals (Key Result Areas - KRAs) for ASIC, designed to encourage overall regulatory efficacy in the bottom half of the regulatory pyramid against ASIC's broader mandate of consumer protection and efficient markets.

These could include measures of:

- ASIC's co-operation with professional bodies
- The extension of consumer protection regulatory benefits over time through co-regulation
- The establishment and ongoing maintenance of co-regulatory infrastructure

Role of professional bodies

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.

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. (In other fields there may not be a licensee but an employer.) This is a vital difference and benefit professional bodies bring to the regulatory design. 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.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

In assuming the obligations and duties of a professional body, members aspire to a higher status in the eyes of the public. The Parliamentary intent to allow for ASIC approved professional Codes, which encourages professionalisation, is a key co-regulatory tool in the enhancement of consumer protection.

Co-regulation and enhanced cooperation between ASIC and professional bodies will deliver significant consumer protection benefits with 'public interest' at the core of the co-regulatory relationship.

However, it is important to distinguish the difference between cooperation with a professional body that enforces professional standards which go beyond the requirements of the law and that complement the work of the Regulator, and are in the public interest; versus influence of an industry association whose lobbying efforts are primarily motivated by the commercial interests of their members.

Further, we acknowledge the need for ASIC to be close to industry so the Regulator knows 'what is going on' inside the industry. However, the Regulator must stand independently of the commercial interests of the industry's participants. This is a challenging issue and highlights the need for balance in relation to 'regulatory capture'. This issue can be overcome by establishing formal working arrangements between ASIC and professional bodies.

Currently ASIC work with professional bodies is based on limited ad hoc issues. The FPA argues that formal arrangements should be established between ASIC and professional bodies, through a Memorandum of Understanding (MOU), that ensures a focused and ongoing partnership that enables parties to work openly together to deliver a stronger and more effective regulatory environment for all stakeholders.

The FPA provides leadership and a professional framework to provide for the delivery of quality financial advice to consumers. Since 2009, it has collected and analysed publicly available data on ASIC enforcement action concerning individuals in relation to financial advice. This analysis shows that FPA members, in each calendar year since 2009, accounted for significantly less than 5% of the overall ASIC enforcement action, and on average less than 10% of financial adviser related ASIC enforcement activity. The fact that more than 90% of financial adviser related ASIC enforcement activity is against providers who are not members of the FPA and therefore not subject to the additional regulatory oversight of professional obligations, clearly demonstrates the consumer protection benefits of professional bodies in the regulatory design.

Statistical under-representation when compared to the total financial adviser/financial planner population in ASIC enforcement activity is a proof point of the normative 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.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Refer to *Attachment 1: Summary of FPA requirements* for the details of 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 design.

Legal facilitation of co-regulation

The Australian Law Reform Commission (ALRC) states that co-regulation typically refers to situations where industry develops and administers its own arrangements, but government provides legislative backing to enable the arrangements to be enforced⁷.

Further, the FPA believes by ensuring the regulatory design encourages and leverages a collaborative and cooperative two-way working relationship between co-regulatory professional bodies and ASIC, the capabilities of the regulatory system, as a whole, will be maximised to improve overall consumer protection. To ensure co-regulation functions at optimum effectiveness in working together to protect consumers, the professional body / ASIC relationship must have the public interest at its core, be based on trust, and allow the two-way exchange of information on a confidential basis, particularly relating to consumer complaints and provider conduct issues.

The FPA notes the legal ability for ASIC to work collaboratively with professional bodies exists in relation to information sharing in s127 of the ASIC Act, and as articulated in Regulatory Guide 103. Importantly, s127(4)(d) states:

Where the Chairperson is satisfied that particular information will enable or assist a prescribed professional disciplinary body to perform one of its functions ... the disclosure of the information to the agency, government, officer or body by a person whom the Chairperson authorises for the purpose is taken to be authorised use and disclosure of the information.

However, ASIC Regulations 2001 – Regulation 8AA, limits the application of s127(4)(d) to the following prescribed professional disciplinary bodies:

- a) The Institute of Chartered Accountants in Australia;
- b) CPA Australia;
- c) Institute of Public Accountants.

⁷ <http://www.alrc.gov.au/publications/13-codes-and-co-regulation/regulatory-forms>



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The FPA understands the introduction of the *Corporations Amendment Regulation 2013 (No. 3)* creates a limited licensing regime for accountants, allowing them to provide a broader range of financial product advice. This change will also mean that accountants are now covered by the same duties towards consumers as financial products advisers, including the best interests duty. However, in order to supplement the transition of accountants to the AFSL licensing regime, the then Government allowed for accountants' existing professional qualifications to be recognised under 'Regulatory Guide 146 Licensing: Training of financial product advisers' (RG 146)⁸. These streamlining arrangements will only be available to accountants that hold a practising certificate from a professional accounting body such as CPA Australia, the Institute of Chartered Accountants in Australia and the Institute of Public Accountants. Therefore, ASIC is able to assume, provided that a practising certificate has been obtained from a professional body, that each accountant has the necessary experience to provide the broader range of services.⁹

The Corporations Act also allows ASIC to declare that members of specific accounting professional bodies are 'qualified accountants'¹⁰ for the purposes of investor disclosure in s708(8)(c) of the Corporations Act. When providing financial advice, a product disclosure statement must be provided. However, section 88B(2) provides for an exemption in relation to the disclosure for a sophisticated investor. Disclosure is not in a mandated form if the provider is offering securities to a person who is the subject of a current certificate from a qualified accountant, certifying they have a prescribed net asset or gross income level. Before approving, ASIC will consider the nature and extent of relevant education and experience requirements applied by the professional body, and whether the relevant professional body has appropriate and effective disciplinary procedures.¹¹ 'Regulatory Guide 154 - Certificate by a qualified accountant' provides guidance as to how ASIC approves an individual as a qualified accountant.

This demonstrates a clear precedent for legally incentivising membership of a professional body to ensure market participants are captured and adhere to professional obligations, and to facilitate co-regulation to assist the Regulator to protect consumers.

The Regulations show a clear precedent and ability for ASIC to enter into a collaborative and cooperative two-way working relationship with professional bodies, including the legal ability to share information.

The FPA has provided further evidence of the legal precedent for co-regulation and information sharing between regulators and professional bodies in *Attachment 2: Precedent for co-regulation*. Also provided is an overview of co-regulatory approaches used in Australia outside the financial services sector, and in international jurisdictions.

⁸ <http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2012/036.htm&min=brs&DocType=0>

⁹ <http://ministers.treasury.gov.au/Ministers/brs/Content/pressreleases/2012/attachments/36/Replacement-for-accountants-exemption.pdf>

¹⁰ Section 88B(2) Corporations Act

¹¹ RG 154.10



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Support for co-regulation

To facilitate the implementation of an effective regulatory structure where professional bodies assist ASIC in its mandate to support consumer confidence and protection, legislative changes will further incentivise an ongoing commitment to professional obligations and accountability.

The Regulatory design should focus on and facilitate the emergence of professional bodies to provide positive incentives for the right behavior; and negative incentives for the wrong behaviour, when providing services to consumers.

It is our strong belief that to strengthen consumer protection and to facilitate a more effective regulatory design based on cooperative co-regulation, consideration must be given to restricting the term financial planner / financial adviser to only those that have the highest level of education, competency, ethics and standards, and are a member of a Regulator 'prescribed professional body'.

The FPA recommends

- Restricting the ability for individual's to call themselves a financial planner if they are only selling a product.
- Requiring financial planners to adhere to professional obligations by requiring financial planners to be members of a Regulator 'prescribed professional association'.

For co-regulation to be effective, legislative support is required to ensure membership of Regulator 'prescribed professional bodies', and therefore adherence to professional obligations. Without the support of a legal requirement to adhere to professional obligations, there is a gap in the regulatory design as applied to individual providers of financial services to consumers, and consumer protection becomes reliant on the limitations of regulatory and licensee obligations alone.

Enshrine the terms financial planner / adviser in law

The FPA suggests this could be achieved by restricting the use of the terms financial planner/planning and financial adviser under s923B of the Corporations Act (or in the Corporations Regulations as per s923B(4)(a)(vi) of the Act); including a requirement for professional membership.

Precedent exists in this regard as the use of the terms stockbroker, futures broker, insurance broker, general insurance broker, and life insurance broker are currently restricted under s923B. However, it is unclear why some expressions are restricted by s923B and not others. Why do such terms carry more weight under law than that of financial planner / adviser considering the role financial planners play in assisting consumers with vital financial matters?

The terms financial planner/advisers are increasingly being used in marketing and promotional material by persons who provide non-traditional ancillary services, such as realtors, property sprukers, sales agents of various investment vehicles, and other unlicensed advisers. Consumers are continuing



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

to be influenced by advice provided by those outside the Regulator's reach. This issue has become evident in the SMSF sector with many property sprukers influencing the use of SMSFs to purchase property. It has also been exacerbated by the commentary on financial matters provided by media outlets who are exempt from licensing obligations under s911A(2) of the Corporations Act yet play a highly influencing role in consumer decision making.

A lack of restrictions on the use of the terms financial planner/adviser is, among other things, a significant gap in consumer protection. It leaves trusting consumers open to influence by individuals incorrectly representing themselves to consumers as financial planners/advisers without holding the specific competency, training, license, professional standing required. This significantly erodes consumer protection. The lack of constraint on individuals calling themselves financial planners puts consumers' at risk of receiving poor advice from incompetent providers. A key role of effective regulatory design should be to enable consumers to be able to clearly identify providers they can trust in the marketplace.

Enshrinement of the terms financial planner / adviser must include a requirement for membership of a professional association, and is therefore an important mechanism to facilitate adherence to professional obligation.

The public interest of facilitating co-regulation and adherence to professional standards

Professional standards serve to strengthen the accountability of financial services providers when servicing the needs of Australians by complementing the legal obligations under the relevant laws. Professional standards go beyond the requirements of the law and therefore play a vital role in protecting consumers. A key consumer protection element of professional standards lies in their enforceability through compliance and disciplinary measures. While professional standards also provide an additional complaint mechanism for consumers, more importantly they serve as a vital measure to prevent the issues that give rise to consumer complaints.

Professional obligations serve to assist Government in protecting consumers by raising the bar of accountability, ethical obligations and education of its members, beyond the requirements of the law. Professional obligations complement and reinforce the legal obligations regulated by ASIC. It is in the public interest for the Government to encourage and support the adherence to professional obligation through effective and efficient regulatory design which facilitates co-regulation, restricts the use of the terms financial planner/adviser and the requires membership of a Regulator prescribed professional body, particularly in the financial services sector which influences the financial wellbeing of all Australians.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Precedent and criteria for Regulator prescribed professional bodies has been set, for example, in the Tax Agent Services Regulations Schedule 1 Part 2 Recognised tax agent association, which permits membership of a Tax Practitioners Board (TPB) approved professional body as a TPB registration option. This is a long-standing precedent which existed in the Income Tax Assessment Act prior to the introduction of the Tax Agent Service regime. (See [Attachment 3: Regulator approved professional bodies](#) for further details of criteria of Regulator 'prescribed associations'.)

According to ASIC licensing data, there are 5,027¹² Australian Financial Services License holders and 51,147¹³ 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, or fully-fledged financial planners all providing different types of advice services to consumers depending on their training, competency, and authorisation. However, from a consumer perspective there is minimal understanding in the different roles and more importantly restrictions placed on the different providers and the limitations of the advice information consumers may be provided.

The FPA has more than 10,000 members and affiliates of whom 7,500 are practising financial planners and 5,500 CFP professionals. FPA members advise over 3,000,000 Australians and are entrusted with over \$630 billion of life savings of Australians. 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 (see [Attachment 1: Summary of FPA requirements](#) for more detail).

However, of the estimated 15,000 to 17,000 financial planners in Australia only 10,000 of them are FPA members and approximately 2,000 are members of professional accounting bodies. This means there are 5,000 to 7,000 financial planners – more than a third – providing financial planning advice to consumers without a requirement to comply with the additional standards of ethics, conduct and education. This significantly reduces the consumer protections available to the clients of a third of financial planners 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 financial planning advice.

Australian consumers deserve the added protections of a regulatory design which supports and facilitates collaboration and cooperation between ASIC and professional bodies. Mandating professional membership in the law will ensure providers are obliged to adhere to professional

¹² ASIC figures as at 10 May 2013 as provided to PJC Inquiry, answers to questions on notice 22 April (received 13 May 2013)

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



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

obligations, which will broaden the reach of the overall regulatory system and strengthen consumer protection.

Issues of dual-regulation in regulatory design

A current feature of Australia's regulatory design is dual regulation. That is, where two (or more) regulators have regulatory oversight of one industry.

The regulation of the financial services sector involves multiple regulators each established to perform a separate primary function. The FPA acknowledges the challenges this creates in avoiding duplication and regulatory overlap, while ensuring effective regulatory cover for consumer protection purposes. However, the FPA believes there is complete duplication of activity by some regulators which is not only extremely inefficient and a costly drain on Regulator resources, but has created confusion for industry participants and consumers alike.

The absence of effective regulatory design has produced duplicate regulatory regimes with little regard for the establishment of a positive co-regulation environment to support professionalisation. Treasury has a key role to play in regulatory design that results in dual-regulation, and therefore must help regulators identify and overcome overlaps and inefficiencies. Regulators must examine how they work together, and improve their working collaboration at all levels, to ensure the efficiency and effectiveness of the system. Professional bodies can assist in this regard.

The FPA believes the issues associated with dual regulation impact on ASIC's performance and relate to Terms of Reference C: *the workings of ASIC's collaboration, and working relationships, with other regulators and law enforcement bodies.*

The FPA provides the following examples of dual regulation which significantly impact on the efficiency, effectiveness, and understanding of the regulatory system.

ASIC and the Tax Practitioners Board (TPB)

The enactment of the Tax Agent Services Act (TASA) Amendment Bill in June 2013 has created dual regulatory oversight for financial planners between ASIC and the Tax Practitioners Board (TPB). The FPA notes the following statements included in the Explanatory memorandum to the Bill which serve to encourage and require the establishment of streamlined processes between the regulators to ensure efficiency.

1.21 A key objective of this new regulatory regime is to minimise compliance costs by avoiding regulatory overlap between the TPB and ASIC.

1.81 In determining its compliance processes, the TPB should ensure these processes are as efficient as possible to avoid any unnecessary duplication with ASIC's processes.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

1.88 As noted in paragraphs 1.19 to 1.21, the administrative effectiveness of this new regulatory regime requires the TPB and ASIC to have a close and collaborative working relationship, particularly in relation to matters that may have regulatory consequences for entities under both the TASA 2009 and the Corporations Act. This requires both agencies to be able to share relevant information with the other.

1.89 The TPB and ASIC have advised that they are currently developing a memorandum of understanding (MOU) to underpin their future relationship, with a commitment to work closely together through an open and consultative approach and to provide each other with positive assistance wherever possible.

Further, on 7 April 2011, the then Minister for Financial Services and Superannuation, Bill Shorten stated:

ASIC and the Board will collaborate closely under the proposed arrangements...Under this collaborative approach, streamlined arrangements will be implemented as far as possible. For example, there will be one set of tax competencies.¹⁴

Under this dual system both regulators – ASIC and the TPB – are charged with regulating the same function of ‘advice’ provided by financial planners. Unlike other dual regulators such as ASIC and APRA, or ASIC and AUSTRAC, which regulate different functions, ASIC and the TPB will be regulating the same function.

While streamlined processes and efficiencies were supposed to be established between the regulators, this has already failed. The review of financial planner education requirements by both regulators is a key example of this failure.

There appears to be minimal coordination between the regulators, or on their behalf through Treasury, in an effort to streamline the requirements to ensure complementary, consistent, and appropriate education requirements are developed.

This has resulted in the release of multiple consultations currently taking place on the same issue – financial planner education requirements:

- Tax Practitioners Board – TPB(PG) D04/2013
- Treasury – Proposed registration requirements for registered tax (financial) advisers discussion paper
- ASIC – Consultation Paper 212: Licensing: Training of financial product advisers – Updates to RG 146

¹⁴ Media release No.049: Future Regulation of Financial Planners Providing Tax Advice, 7 April 2011



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

- ASIC Consultation Paper 215: Assessment and approval of training courses for financial product advisers: Update to RG146
- Proposed Self Regulatory Organisation (SRO) to deal with advice providers training obligations.

While there is obvious regulatory overlap between the TPB and ASIC in this instance, there is an apparent lack of alignment of the proposed requirements for planner education, and the different approaches used by the two regulators. For example:

Table 1.1

	TPB	ASIC
Training register	Approves appropriate training courses and maintains register of courses approved by the Board as meeting its requirements	Proposes to permanently close its training register
Education level	Proposes education level of AQF5 or equivalent	Proposes increasing the minimum education level to AQF7
Course duration	Proposes a course duration of 100 to 130 hours or equivalent of one semester	Is silent on course duration.
Assessment criteria	Proposes a range of appropriate assessment tools; and to mandate independent supervision requirements	Is silent on assessment

While this is not a detailed analysis or extensive list of the requirements proposed by the TPB and ASIC, the above table serves to illustrate the differences in both the requirements and the approach to financial planner education being adopted by the regulators. This will only lead to confusion for financial planners, licensees and education providers; and drain regulator resources. The lack of a consistent and streamlined approach to financial planner education will also increase training costs, which may lead to an increase in advice fees for consumers.

In addition, the timelines for transition and implementation for the changes in planner education proposed by the TPB, Treasury and ASIC are not aligned. This will result in the proposed additional TASA training requirements for financial planners being outdated by ASIC's proposed changes to RG146, even prior to the TASA requirements applying to one single financial planner.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013



There is further misalignment of knowledge versus competency requirements, and the tax course topic areas proposed by both regulators. If this issue is not resolved, it could result in planners having to undertake two different courses on the topic of tax in order to comply with both ASIC and the TPB requirements.

This has resulted from a lack of communication, coordination and collaboration between the TPB, Treasury, and ASIC. Each of these Government agencies has a dedicated team responsible for the regulation of financial planners / financial advice providers. We suggest that, as experts in this area, these teams must improve their working relationship, at all levels, and be aware of the activity being undertaken by other regulators. This issue has been exacerbated by the fact that it was industry that identified the overlap and brought it to the attention of both regulators over a period of a number of months. It appeared to take some time for the regulators to act and commence communication regarding this obvious overlap in activity. During this delay, two additional consultation papers relating to planner education were released - one from ASIC and one from Treasury (on further Tax Agent Service regime education requirements for planners).

ASIC's work to update RG146 and the introduction of the TASA regime for financial planners, are both extremely significant and high profile regulatory activities in the financial planning space. The overlap should have been easily identified by both regulators and Treasury.

The FPA notes the recent efforts of the TPB and ASIC to commence discussions to address this issue.

Importantly, the FPA agrees that competency standards should be increased both for tax related advice given by financial planners and for financial advice generally. A key tenet of the FPA's drive towards achieving the highest standards of professionalism is the requirement for higher levels of education for financial planners.

ASIC and the Australian Tax Office (ATO)

Another example of confusion and inefficiencies of dual regulation is role of ASIC and the ATO in regulating Self Managed Super Funds (SMSFs).



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

This is particularly confusing for consumers who are a member or trustee of an SMSF. Further, it has led to a mis-alignment of expectations of the role each regulator has in assisting consumer/trustees when things go wrong.

Managing an SMSF is complex. This is exacerbated as trustees must navigate the quagmire of rules and obligations which are split between the ATO and ASIC. It is important to keep in mind that many SMSF trustees are consumers, not professionals working in the financial services industry.

This example of dual regulation also highlights the risk of gaps resulting in the rules governing an industry when multiple regulators are involved. We believe this hinders the performance of both the regulators and the regulatory system.

	ATO	ASIC
Implementation of investments	The ATO have set a list of rules on investments around the acquisition of assets placed on trustees.	Only until recently, the same knowledge and licensing requirements of professionals giving the investment advice on SMSFs were lacking
Strategic recommendations to trustees	The suitability of strategic recommendations do not get assessed by the ATO and professionals giving the advice are not accountable whereas the trustees being recommended to are.	ASIC's involvement in SMSFs and its licensing regime of those providing SMSF advice have been lacking. An SMSF structure have not been defined as in itself as a financial product until recently.
Guidance to trustees on rules	The ATO provides rules and guidelines on SMSFs. However the majority of trustees are not themselves competent to maintain their SMSFs. The penalties to trustees are however as strictly applied to those of a large superannuation fund.	Until recently, ASIC has not provided sufficient guidance to professionals or have a licensing regime to govern those giving SMSF advice. The gap between ATO's expectations of trustees, versus ASIC's role in the SMSF advice space has created industry wide issues including consumer losses and lack compensation.
Responsibility of activities	The ATO expects trustees to manage their superfunds according to rules set on SMSFs. The penalties of rules on trustees are somewhat more imbalanced towards the consumer compared to the professionals who recommend them.	Until recently Accountants and Advisers who recommend SMSFs are not under ASIC's radar. Requirements on licensing and competence of those initiating the SMSF strategic advice are lacking.

Recommendations – Regulatory design

The FPA recommends:

- the development and implement of a regulatory design which recognises and facilitates the role of professional bodies in assisting ASIC to achieve its consumer protection and confidence mandates.
- the Parliament set and monitor performance goals (Key Result Areas - KRAs) for ASIC, and all regulators, designed to encourage overall regulatory efficacy in the bottom half of the



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

regulatory pyramid against ASICs broader mandate of consumer protection and efficient markets.

- amend Regulation 8AA of the ASIC Regulations to include other financial services professional bodies, including the Financial Planning Association, and permit collaborative and confidential information sharing between ASIC and professional bodies to enhance consumer protection.
- establish a Memorandum of Understanding between ASIC and professional bodies that facilitates and permits a more collaborative and cooperative two-way working relationship, or co-regulatory partnership.
- amend the law to restrict the use of the terms financial planner/adviser, and require every financial planner to become a member of a Regulator prescribed / recognised professional body.
- specific Key Result Areas (KRAs) be set by the Parliament for ASIC, and other regulators, that require the Regulator to measure its performance in:
 - identifying specific areas of regulatory overlap with other regulators; and
 - determining and implementing appropriate demarcation of responsibilities and the establishment of working collaborations that leverage the best expertise and systems of all regulators,

to minimise duplication and improve the efficiency and effectiveness of the regulatory system for consumers and industry.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

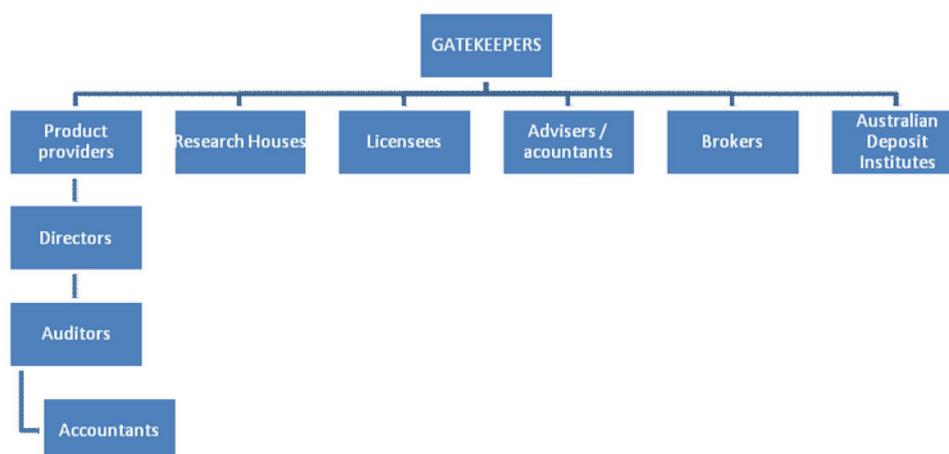
3. The role of gatekeepers and ASIC obligations

This section relates to Terms of Reference A. *ASIC's enabling legislation, and whether there are any barriers preventing ASIC from fulfilling its legislative responsibilities and obligations;* and F. *any related matters.*

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. These gaps in the law create significant risks for consumers and significantly undermine the role and powers of ASIC and the value of legislation which serves to protect consumers.

The FPA implores the Committee to look beyond ASIC's existing *legislative responsibilities and obligations* (as stated in the Terms of Reference), and consider the vital role ASIC was established to fulfil in protecting consumers and how the following issues and gaps in legislative requirements hinders the Regulator's effectiveness in this regard. These legislative gaps also cause ASIC to 'over-reach' into areas that would be better regulated through professional obligations, taking up valuable ASIC resources; and 'under-reach' in areas which only the Regulator can provide effective regulatory oversight to protect consumers.

The ASIC Chairman, Greg Medcraft, in a speech to the Senate Economics Legislation Committee¹⁵ 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."



¹⁵ Hansard Senate Economics Legislation Committee, 31 May 2011



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

There is a need to consider preventative measures to reduce the risk of misconduct and the problems that lead to the events that cause consumer loss or damage. A holistic approach that considers all financial services is required. A starting point would be to examine the types of financial services providers that have played a role in past events that resulted in significant consumer loss.

The FPA urges the Committee to ensure they take an holistic approach to the issues identified through the *Inquiry into the performance of ASIC* and consider the role of each gatekeeper participant in the financial services industry.

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.

However, because of the existing legislative requirements, ASIC is limited in its response to hold all parties to account for their role in these collapses.

It is well established that, rather than all fault lying with the advice provider, there are multiple participants who offer products or services within the financial advice value chain, all of whom influence, directly or indirectly, consumers' decisions on financial matters. However, accountability of these participants to the end consumer is variable, limited and for some practically non-existent, which significantly restricts ASIC's ability to act. They include:

- Product manufacturers and fund managers
- Platforms
- Property schemes
- Ratings agencies and research houses
- Investment banks (funding the development of financial products sold to consumers)
- Auditors (of products and product manufacturers)



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

- Accountants (of product manufacturers)
- Accountants (of consumer) operating under the accountants exemption
- Stockbroker / share broker
- Futures broker
- Australian Deposit Institutes (banks, building societies, credit unions)
- Insurance brokers and companies
- Unregulated participants (including some Accountants) acting as financial planners
- Regulatory agencies including ASIC and the ACCC
- Professional Indemnity Insurers

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. Therefore ASIC must have the legislative power to hold each participant accountable for the responsibility they have to the consumer for the 'gatekeeper' role they play, and the consumer's compensation needs.

Tighter regulation and greater scrutiny of all participants, particularly product providers and research houses, will reduce the opportunity for fraud and provide greater transparency and protections for consumers from the outset. ASIC must be legally obliged to take a larger role in the regulatory oversight of gatekeepers, particularly products before they are released for consumer investment and product research reports.

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



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

However, ASIC does not have legislative obligations to regulate financial products, only responsibilities for oversight of product providers which focus on matters of corporate governance and disclosure, and in the main not on the design and other issues related to the products they sell to consumers.

For example, a product provider such as Trio Capital as the “Responsible Entity” of the company 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. However, auditor reports indicated the Trio funds complied with all requirements and were included in positive reports on the funds produced by various research houses.

Problems with products should be addressed through product regulation. Legislation must enable ASIC to effectively and proactively regulate product providers and the products they develop and sell to consumers. 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.

In 2011, the UK’s Financial Services Authority (FSA) provided a warning to product manufactures stating that: “the financial services industry has developed a growing and innovative market for products, including structured products, which are often described as ‘guaranteed’, ‘protected’ or ‘secure’. The FSA has reviewed this market and concluded that some firms promote these products without any clear and adequate justification for the descriptions used. We believe that this could be implicitly misleading and could lead to consumers misunderstanding what is actually offered to them.¹⁶ This follows comments made by the former CEO of the FSA Hector Sants that “our focus has been too late in the product lifecycle to ensure that we identify potential issues early enough to prevent consumer detriment”¹⁷

There is a vital need to enhance the responsibility of product providers and fund managers in developing products for consumers, which go beyond ensuring compliance with the existing 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.

This issue was carefully considered by Mr Richard St John in his review of the consumer compensation system:

5.38 As has been noted most cases of large case consumer loss are associated with the failure of financial products, and managed investment schemes in particular. In such cases a common issue appears to be that consumers had not been properly informed of, or had not understood, the complexity, suitability or risks of their investments.

5.39 Under the current regulatory approach, there is limited regulation of the development and marketing of new investment products. There is no pre-vetting of new products and any

¹⁶ FSA CP11/11 Quarterly Consultation no.29 (chapter 5)

¹⁷ Hector Sants, CEO, FSA, 2009



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

financial product can be placed on the retail market by a registered and licensed financial product issuer if accompanied by the required disclosure statements.

5.31 More fundamentally, it may be timely to review the adequacy of the underlying conduct and disclosure approach to the regulation of financial product issuers as the means of protecting consumers. There has now been some ten years' experience of the current approach which relies largely on the disclosure of information to consumers and sets some standards for the quality of that information. Any additional measures would be aimed at reducing the risk to consumers that they acquire financial products that are not suited to their needs. They would be preventative measures that aim to reduce consumer loss, and the eventual need for consumer compensation.

The FPA supports St John's Recommendation 3.1: Review regulation of product issuers, which states:

(a) Subject product issuers to more positive obligations in regard to the suitability of their product for retail clients. Such obligations might be applied in particular to managed investment schemes in issuing products to the retail market, and would apply at each stage of a product's life cycle including its distribution and marketing. Amongst other things, the product issuer might be required to state the particular classes of consumers for whom the product is suitable and for whom the product is unsuitable, and the potential risks of investing in the product.

A stronger approach by managed investment schemes to the management of risk of fraud, particularly by employees or representatives, might also be sought.

(b) Consider the development of standardised product labelling so that financial products, particularly managed investment schemes, are described on a consistent and more meaningful basis. This might apply to such terms as capital guaranteed, capital protected, conservative, balanced, diversified, growth, defensive, fixed interest, or hedged, as well as other like descriptors.

(c) While the review has not looked into these matters in any depth, the significance of the role of gatekeepers, such as research houses, should be kept in mind in any strategic consideration of consumer protection in the financial services sector.

However, such recommendations should not be limited to managed investment schemes.

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



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

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. While the FPA acknowledges recent changes by the International Organisation of Securities Commissions (IOSCO) and ASIC to the regulation of Credit Rating Agencies (CRAs) and research houses, CRAs and research houses should also be held accountable for their roles in product failures.

There are multiple stakeholders who offer products or services within the retail wealth management value chain whose accountability to the end consumer remains unclear, particularly with regard to significant unforeseen events. Each of these stakeholders influences consumers' financial decisions, either directly or indirectly.

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. ASIC legislative requirements in this regard should be bolstered.

The role research houses play in consumers' investment decisions

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 products and service to Australian consumers.

- 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.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

- 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.

Research houses play an important gatekeeping role in the financial system. This must be recognised by enhancing ASIC's regulatory oversight of such participants.

Role of research houses in product failures

A US Congress Joint Economics Committee Report¹⁸ found systemic biases and methodological errors at credit rating agencies distorted investment decisions and had a profound negative effect on financial markets, financial institutions, and the broader economy. The Report concluded that when credit rating agencies award overly high ratings to any class of debt or derivative securities, financial institutions and other investors purchase more of these securities for their investment portfolios. At the same time, systemic biases and errors in credit ratings encourage issuers to supply more of these overly rated securities to financial markets. Thus, systemic biases and errors in credit ratings erroneously stimulate the flow of credit to economic sectors that are receiving funds through these overly rated securities.

Further, the Report found the "issuer pays" business model of credit rating agencies made them financially dependent upon the providers of the products they were assessing. These agencies pressed their analysts to give favourable ratings to maintain or increase market share with these product providers. Credit rating agencies were found to employ flawed methodologies to evaluate structured credit products resulting in higher ratings to many structured credit products than they deserved.

While credit rating agencies in the main assess and rate credit products, and research houses assess and rate non-credit products (or all other classes of financial products), this is their only point of difference. The systemic biases, conflicts of interest, and potential for errors in assessment and ratings of products, are the same across credit rating agencies and research houses. Hence, the FPA suggest it is relevant and important to consider international findings on these issues.

A clear example of an Australian product failure with the same symptoms to those of the credit rating agency issues faced in the US, 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.

¹⁸ The US housing bubble and the global financial crisis: Vulnerabilities of the alternative financial system, Research Report #110-26, October 2008



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Westpoint is another notable example where some reputable research houses continued to give the product a highly positive rating. Many consumers impacted by the Westpoint failure invested directly with the product provider or through a broker.

In the case of Trio Capital, 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.

The role research houses play in providing research and specialist assessments of financial products which influence consumers' investment decisions is not recognised by the research house industry, or in the regulatory and dispute resolution environment.

Further, the licensing requirements for research houses are dependent on the services the entity provides. If they provide services to wholesale clients only, they are not required to be licensed; if they provide services to retail clients, they are. We note that ASIC changed its requirements regarding product manufacturers including in their PDS information sourced from research houses. Now 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 (PI) 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 PI 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 PI cover (RG126.23) 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, such as Trio Capital, Westpoint and Basis Capital.

This again highlights a gap in ASIC's regulatory responsibilities that significantly impacts on consumer protection.

Financial planners and research:

The FPA strongly supports the fundamental requirement for financial planners to consider and investigate the subject matter of the advice they provide under s945(1)(b). In fact, the FPA's Code of Professional Practice goes beyond these legal obligations to require our members to conduct thorough independent research to ensure suitability to client needs, objectives and risk tolerance and circumstances.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

However, research published by research houses plays a role in financial planners' consideration of client suitability of a product or service. Research houses are used in different ways by financial planning professionals and licensees depending on their size and business model.

It is unclear how much and in what way licensees and financial planners can rely on research house research and ratings in relation to errors of fact, timing of ratings and adjustment of ratings. There is no accountability for research houses in this regard.

- Small dealer groups do not have the capacity of dedicated research teams and compliance officers other than the Responsible Officer who is usually the Principal of the organisation.
- The practicalities/ability of licensees and financial planners in regional areas conducting their own research on all products is questionable, as they do not have the ability/access to meet with fund managers on a regular basis in order to carry out the indepth research expected by FOS and ASIC due to geographical and resource limitations. Hence the role of research houses is vital.
- Without being able to rely upon research houses, financial planners must rely upon publicly available product information. Research house information offers greater insight into the products.

Recommendations - Gatekeepers:

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 regulatory system be designed to encourage the establishment of professional bodies to impose appropriate and enforceable professional standards that exceed the law, on financial product providers, research houses, and other industries in the gatekeeper space.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Attachment 1: Summary of FPA requirements

In most professions, regulation is a dynamic interaction between government imposed legal requirements, business imposed rules of work, and the expectations of professional peers, as manifested in professional obligations. Each of these systems of regulation have the potential for overlap with each other, but it is the goal of the FPA's professional regulation to respond to those issues that are not covered in law or which the law does not provide sufficient standard for professional financial planning practice in the view of the profession.

The FPA's professionalism framework applies to all CFP® and AFP® practitioner members as a directly enforceable form of professional regulation. It also provides a foundation of expectations and norms for wider industry application and provides a vital link between overarching statutory regulation, licensee obligations and expected professional behaviour.

In order to fulfil our obligations as a professional body the FPA has not only led the global community in the development of professional regulation, but as an organisation we ourselves undergone substantial changes. Since 2009, the FPA has undertaken the following initiatives to strengthen the professional obligations on our members:

- Effective 1 July 2012, the FPA changed its membership structure (with the support of members) to move to a professional body with a membership solely of financial planner practitioners (this received a 94% yes vote from membership at our EGM in April 2011).
- The membership change ensured the accountability to adhere to professional obligations sits with the financial planner when providing services to consumers, which complements the regulatory and licensee obligations to enhance consumer protections.
- The FPA has moved to higher standards of membership which will require, for all new members, a minimum degree qualification and one year experience from 1 July 2013.
- Continued to build a Professional Framework for financial planners, as evidenced by the introduction of a new Code of Professional Practice;
- Put in place new disciplinary regulations for enforcing the FPA's Code and professional practice obligations;
- In October 2009 (prior to FoFA), the FPA launched a Remuneration Policy on our members, banning investment commissions on new business from July 2012;
- Updated the FPA's Continuing Professional Development (CPD) policy, ensuring a qualitative approach is taken to ongoing training of financial planners.

All these initiatives served to change the professional landscape under which members of the FPA operate in Australia.



The performance of ASIC

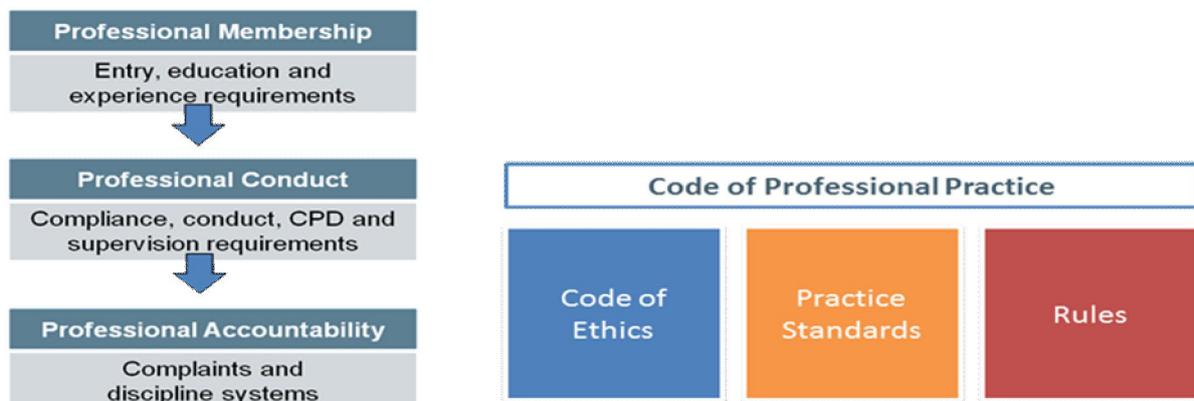
SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The FPA has harmonised nine separate layers of obligation for members into a Code of Professional Practice, with all rules and regulations being captured through:

1. Code of Ethics – enshrines the high standards of professional behaviour that a member presents in the course of the provision of professional services.
2. Practice Standards – establishes the benchmark of expectations in professional practices, and promotes the six-step financial planning process in delivering quality advice and the professional conduct of FPA members that enhances the reputation of the profession.
3. Rules of Professional Conduct – underpins the minimum requirements with which a member must conform in order to demonstrate professionalism.
4. Guidance – provides guidance to members in interpreting elements of the single code framework and establishes best practice models that assist the members' day to day activities in providing professional services.

This is world leading, but in itself it is not enough. A profession must also have a professional framework. The FPA has a framework for:

- professional membership
- professional conduct
- professional accountability



Binding professional obligations

The FPA first adopted a binding Code of Ethics and Rules of Professional Conduct on 5 February 1992. In 1997, in anticipation of the introduction of the FPA's revised Code of Ethics and Rules of Professional Conduct on 1 May 1997, the FPA Compliance Handbook noted:



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

As a condition of FPA membership, members sign a declaration agreeing to abide by the FPA Code of Ethics.

Principal and Practitioner members acknowledge and agree that the substance and contents of any charge for violation of FPA Code of Ethics and Rules of Professional Conduct against a member and the action taken in respect of such a charge, may be notified to any relevant government or statutory authority, and the disciplinary finding published with or without disclosure of the name of the member in the official publication of the Association by notification to the members of the Association.¹⁹

The FPA completed a further round of modifications to the Code of Ethics and Rules of Professional Conduct effective from 1 July 2009. These changes developed and aligned FPA professional standards into a 'single code of practice', committing financial planning in Australia to the FPSB global Code of Ethics and new global Practice Standards and introduced a revised set of 122 Rules of Professional Conduct effective from 1 July 2010. In July 2011, the FPA completed an historic restructure of its membership to refocus on the individual practitioner professional, dissolving the Principal (AFSL) Member category and bringing further changes to its Code of Professional Practice. Most recently, in October 2012 the FPA embarked on an ambitious further update of its professional code to reflect the profession's response to the legislative enactment of the Future of Financial Advice reforms to the Corporations Act 2001.

Just like the application of statutory regulation, professional regulation is a combination of stated rules and supporting regulations. As the governing entity of a professional association the FPA Board is empowered by the FPA Constitution to make rules and regulations that govern member behaviour. In addition to governing member behaviour, these rules place obligations on the FPA to monitor behaviour and enforce the regulations according to specific requirements. This activity is undertaken by the FPA's Professionalism Division (Policy and Conduct, Professional Standards, Professional Designations). The division oversees the development and application of standards, as well as the active investigation of complaints and general investigation of malpractice risks in the membership. In addition to a Professional Accountability team, the FPA has a formally constituted and independently chaired Conduct Review Commission which follows a private tribunal model of justice in disciplinary complaints against members.

It is currently best practice for Australian Financial Services licensees to map their own adviser requirements and business rules to the expectations established in the FPA Code of Professional Practice.

The Financial Ombudsman Service (FOS) has publicly recognised the FPA Code of Professional Practice²⁰, providing evidence of the normative status of the Code for financial planners as an industry standard upheld by the leading External Dispute Resolution Scheme in financial planning disputes.

¹⁹ FPA Compliance Handbook- A Handbook of Compliance Best Practice for Financial Planners 5.2 Apr/97

²⁰



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Client Conduct – Putting Client First

Rule 1 of the FPA's Code of Ethics is a requirement for "Putting the Client First", and was introduced by the FPA in 2009, pre-FoFA.

"Putting the Client First", together with the rest of the FPA's Code of Professional Practice has been shown to comply with the statutory "Best Interest Duty" test introduced in the FoFA regulations. FPA members remain one step ahead of the curve, continuing to focus on delivering best in class financial advice to clients at a time when the wider industry is dealing with a rapidly shifting regulatory environment.

The FPA's 'client first' obligation was introduced and embedded by our members well before the 'best interests duty' was proposed by the Government to be mandated in the Corporations Law. While this shows the ability of professional bodies to respond to the consumer protection needs of specific professions, the fact that a best interests duty was legislated highlights how the voluntary nature of professional membership leaves many industry participants unaccountable to professional obligations. This shows the need for the regulatory design to facilitate a legislative environment that encourages industry participants to be members of professional bodies to ensure professional obligations are extended to all service providers.

Conflicted Remuneration

In October 2009, the FPA Board led the industry by committing to ban conflicted remuneration. The FPA's Code of Professional Practice was amended accordingly and since 1 July 2012, FPA members have committed that all new advice will be free from conflicted remuneration arrangements. Many of the recommendations published in FPA's Remuneration Committee Report now appear under the FoFA regulations.

Public Complaints System and Investigations Handling

The FPA has a formal complaints and investigation handling system codified in the FPA Disciplinary Regulations. The system works as a cooperation between the FPA's accountability team and Conduct Review Commission (CRC).

The accountability team is responsible for investigating complaints, gathering evidence, conducting preliminary investigations, inviting the member to assist and to allow the member every opportunity to give an explanation, and assisting complainants throughout the process. The aim is to deliver a recommendation to the Chair of the CRC as to whether FPA's Code of Professional Practice has been contravened and if the Chair should issue a breach notice.

The Conduct Review Commission (CRC), through its independent Chair, is responsible for reviewing the recommendation made to it by the FPA's accountability team, issuing a breach notice if satisfied



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

that the evidence and legal arguments are sound, arranging and conducting hearings and determining the most appropriate disciplinary action to take.

The FPA receives complaints by consumers regarding breaches made by FPA members. In the quarter from October - December 2012, there were 12 new investigations received and 13 investigations closed²¹. In the June 2013 quarter (April to June 2013), the FPA received five new complaints, finalised eight investigations and had nine ongoing investigations.²² The FPA publishes quarterly Professional Standard reports on its complaints procedures, which includes the identification of any remedial tips for planners to help educate members in adhering to the Code obligations, and minimise the risk of breach reoccurrence for consumers.

Active Professional Disciplinary Panel

The CRC receives complaints, with almost half of them being Members providing unsuitable recommendations (44%)²³. Twenty one percent of complaints are regarding misleading conduct, and 9% making up non-disclosure of fees, risks and conflicts of interest.²⁴ In 2011-12, the most common reason for a breach in which a determination was provided was Rule 111 - *providing explanation of risks in terms the client is likely to understand*²⁵.

There are a number of sanctions available for the CRC to enforce, depending on the extent of the breach and amount of Member cooperation. The most regular sanctions given by the CRC are admonitions, further education and supervised practice and fines, ranging from \$1,500 to \$20,000 per contravention²⁶. Although expulsion and suspension is an uncommon sanction, with the CRC aiming to promote ethical behaviour in the industry and reintegration into good standing, the CRC had 2 terminations of memberships and one suspension over the October-December 2012 quarter²⁷. Where the CRC believes that the individual can provide good evidence that their experience and expertise can contribute to the financial planning industry and there remains some scope that the individual will regain adherence to the professional obligations, the CRC will be more encouraged to designate further education as a sanction rather than expelling or suspending the individual.

Once a decision is made by the Panel, the decision can be appealed. The CRC has had only one appeal of its determinations to date, which was dismissed²⁸, demonstrating that the decisions are fairly and accurately made and the sanctions provided are reasonable.

The powers and activity of the CRC demonstrate the significant role professional bodies can play in the regulatory design, particularly in responding to consumer complaints and ensuring appropriate action is taken against inappropriate conduct of individual providers.

²¹ <http://www.financialplanningmagazine.com.au/analysis/quarterly-complaints-and-discipline-report-oct-1>

²² <http://www.financialplanningmagazine.com.au/analysis/quarterly-complaints-and-discipline-report-april-1>

²³ From Bad Practice to Good Practice and the FPA's Conduct Review Commission - Dimity Kingsford-Smith's article

²⁴ From Bad Practice to Good Practice and the FPA's Conduct Review Commission - Dimity Kingsford-Smith's article

²⁵ http://www.fpa.asn.au/media/FPA/FPA%20Standards/FPA_ProfessionalStandardsReport2012-FINAL.pdf - FPA Annual Report 2011-12 p20

²⁶ From Bad Practice to Good Practice and the FPA's Conduct Review Commission - Dimity Kingsford-Smith's article

²⁷ <http://www.financialplanningmagazine.com.au/analysis/quarterly-complaints-and-discipline-report-oct-1>

²⁸ http://www.fpa.asn.au/media/FPA/FPA%20Standards/FPA_ProfessionalStandardsReport2012-FINAL.pdf - FPA Annual Report 2011-12 p20



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The FPA notes the civil penalty provisions within the Corporations Act as an alternative to criminal prosecution and to give ASIC sanctions to meet non-fraudulent contraventions. However, the Corporations Act is specific and express that they are to be civil in procedure, rules of evidence and standard of proof. While the FPA understands the need for such legal requirements for ASIC, in contrast the FPA's Conduct Review Commission Disciplinary Panel may inform itself as it deems necessary and is not restricted to the rules of evidence. It must make its determination on the basis of material before it on the balance of probabilities. This enhances our ability to respond to consumer complaints and allows for flexible and more nimble solutions to be implemented to enhance the protection of the public and the profession.

The FPA has a demonstrated capacity to act promptly to inappropriate behaviour that puts consumers at risk, with sufficient flexibility to achieve results.

For example, the following timeline in response to the collapse of Storm Financial, particularly in relation to the conduct of CEO, Emmanuel Cassimatis, demonstrates the FPA's ability to investigate and act on issues of poor conduct effecting consumers:

Date	Action
October 2009	Initial media article published concerns about practices within Storm Financial
6 November 2008	The FPA <u>initiated</u> a complaint against Storm Financial. The FPA was interested in allegations raised in a media article concerning the widespread use of a high risk gearing strategy and possible client exposure to margin calls in the then volatile market environment.
23 December 2008	FPA issued a Breach Notice to Storm Financial
20 January 2009	Under FPA procedures Storm Financial had until 20 January 2009 to respond to the charges.
12 January 2009	Storm Financial entered into voluntary administration
May 2009	The FPA received a consumer complaint against Mr Cassimatis
September 2009	FPA Breach Notice was issued
March / April 2010	CRC Hearing was held
October 2010	CRC Determination was issued – Cassimatis was expelled from the FPA
February 2011	Cassimatis Appeal was heard
July 2011	Appeal dismissed – expulsion confirmed

Publication of Disciplinary Decisions with Reasons

Under Part 10 of the FPA Disciplinary Regulations, the CRC is required to produce a statement of reasons for its determination regarding a breach. Part 13 allows the FPA to publish the outcome of the determination on the FPA's website and in the Financial Planning Magazine. Publication can be following a special breach due to non cooperation, following a Disciplinary Panel determination or following a summary dismissal. The Member's name is published in the case of expulsions and the name of the complainant withheld.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

The FPA also acts to incorporate the reasons for the determination into training and feedback to members. This ensures that recurrences of common breaches are significantly reduced, and members are made aware of areas in which they have to take extra care.

Complaint procedures and the activity of the CRC is one strategy the FPA uses for reducing infringements of the Code of Professional Practice. In addition, the FPA uses training, continuing professional development (CPD) obligations, and improvements to the Code of Professional Practice itself, to continuously improve the professional conduct of individual members and enhance consumer protection.

Supervision and Oversight of Members

A key aspect of consumer protection is the accountability of financial services providers through compliance monitoring and complaints management. A vital element of this process is the ability to identify and track trends and systemic issues, and to modify regulatory requirements to ensure consumer protection is improved. Professional bodies play a key role in this regard.

In addition to acting on complaints from consumers, the FPA also has the power to initiate investigations of its own under its supervisory and oversight capacity.

The FPA analyses information from its complaints procedures and compliance monitoring to identify and address issues affecting consumers and the quality of advice. This could range from planner education initiatives, to a review of the adequacy of professional obligations in extreme cases.

Managing these arrangements in-house also provides for the efficient use of member information and market intelligence to screen new applicants and to maintain an effective member registry.

Entry Requirements

Membership of the FPA requires a qualifying degree.²⁹ This is on top of requiring at least one year's supervised experience and set well above the minimum standards in the law (eg. compliance with RG146 Licensing: Training of Financial Product Advisers).

Training and Competence

Members have minimum ongoing training requirements in line with FPA's Continuing Professional Development (CPD) Policy. Compliance is mandatory and audited annually. Failure to demonstrate compliance can result in disciplinary sanction including expulsion.

The FPA's dedicated in-house team of training development and delivery experts oversee the implementation of its world class CPD Program. Programs span 6 disciplines: Capability, Professional Conduct, Critical thinking, Reflective Practice, Interdependence, Attributes and Performance.

²⁹ http://www.fpa.asn.au/media/FPA/CFP/Education_2013ApprovedDegreeList1_13.pdf



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Programs go beyond the requirements in RG146 (Licensing: Training of Financial Product Advisers) while achieving compliance.

Certification and Accreditation

The FPA administers a two tiered accreditation system through the certification of either an AFP[®] or CFP[®] mark which are both tightly integrated with the CPD Program.

The AFP[®] mark confirms that the financial planner is a professional, qualified and experienced member of the FPA, committed to the world-leading FPA Code of Professional Practice.

The CFP[®] designation is the highest level of certification that a financial planner can achieve. The CFP[®] mark is internationally recognised and represents standards of excellence. It demonstrates a commitment to professionalism in financial planning to the public and peers alike.

From a regulatory perspective, CFP[®] professionals account for over 35% of the planner population but less than 2% of ASIC enforcement action.³⁰ This exemplifies the effectiveness of FPA's systems, policies and vision to professionalise the industry, and the vital role professional bodies play in 'norming' good professional behaviour beyond legal minimum standards.

³⁰ According to ASIC and FPA Data over the past 3 years.



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Attachment 2: Precedent for co-regulation

Existing legal provisions that support co-regulation

Precedent has been established through existing provisions in financial services law and regulations which support the role of professional bodies as a co-regulation partner in effective regulatory design, to assist regulators in protecting consumers.

(a) Corporations Act 2001 (Cth)

There are no explicit exemptions in the Corporations Act which alter licensing requirements for individuals who are members of a professional association. The only sections that are remotely related are sections 926A³¹ and 926B³². These sections represent the general exemptions made by ASIC and Regulations, provided for in every Part of the Act. However, the exemptions outlined in these sections do not apply to Division 4 of Chapter 7 (in relation to applying for a license) and Division 8 (disqualification).

Although not present in the Corporations Act until recently, the *Corporations Legislation Amendment (Membership Designations and Other Measures) Regulation 2013* now provides relief for registered company auditors to be deemed to hold practising certificates, provided they are members of professional accounting bodies. A practising certificate is a qualification issued by a professional accounting body to members certifying that they have a specific level of training and experience. Instead of an individual having to hold a practising certificate, registered company auditors will be required to have a professional membership designation from a registered professional body. The Regulation's Explanatory Notes claim that this will not only allow a greater number of individuals to undertake a review, but it will ensure that all these individuals are qualified to do so³³. These membership designations are different for every professional body, with a variety of designations representing different "qualifications, training and experience".³⁴

³¹ Exemptions and Modifications by ASIC - allows ASIC to exempt an individual or financial product from the requirements under Part 7.6, Licensing of Financial Services

³² Exemptions and Modifications by Regulations - allows the regulations to exempt an individual or financial product from the requirements under Part 7.6, Licensing of Financial Services

³³ http://www.austlii.edu.au/au/legis/cth/num_reg_es/cladaomr2013n125o2013930.html

³⁴ http://www.austlii.edu.au/au/legis/cth/num_reg_es/cladaomr2013n125o2013930.html



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Also, the *Corporations Amendment Regulation 2013 (No. 3)* creates a limited licensing regime for accountants, allowing them to provide a broader range of financial product advice. The limited AFSL for accountants will allow them to provide advice on self managed super funds, deposit products, securities and much more. This change will also mean that accountants are now covered by the same duties towards consumers as financial products advisers, including the best interests duty. However, in order to supplement the transition of accountants to the AFSL licensing regime, the then Government allowed for accountants' existing professional qualifications to be recognised under 'Regulatory Guide 146 Licensing: Training of financial product advisers' (RG 146)³⁵. These streamlining arrangements will only be available to accountants that hold a practising certificate from a professional accounting body such as CPA Australia, the Institute of Chartered Accountants in Australia and the Institute of Public Accountants. Therefore, ASIC is able to assume, provided that a practising certificate has been obtained from a professional body, that each accountant has the necessary experience to provide the broader range of services.³⁶

The Corporations Act allows ASIC to declare that members of specific accounting professional bodies are 'qualified accountants'³⁷ for the purposes of investor disclosure in s708(8)(c) of the Corporations Act. When providing financial advice, a product disclosure statement must be provided. However, section 88B(2) provides for an exemption in relation to the disclosure for a sophisticated investor. Disclosure is not in a mandated form if the provider is offering securities to a person who is the subject of a current certificate from a qualified accountant, certifying they have a prescribed net asset or gross income level. Before approving, ASIC will consider the nature and extent of relevant education and experience requirements applied by the professional body, and whether the relevant professional body has appropriate and effective disciplinary procedures.³⁸ 'Regulatory Guide 154 - Certificate by a qualified accountant' provides guidance as to how ASIC approves an individual as a qualified accountant.

j) FOFA Reforms

The Future of Financial Advice (FOFA) Reforms introduced a requirement for all financial planners who enter into ongoing fee arrangements for a period of 12 months or more with new retail clients (from 1 July 2013) must renew their clients' agreement to pay ongoing advice fees every two years (the 'opt-in' requirement under s962K of the Corporations Act).

However, financial service providers who are members of an association with a code of conduct which has been approved by ASIC as "obviating the need for opt in", are not required to comply with the opt-in requirement.³⁹ s962(1)CA of the Corporations Act allows ASIC to exempt an individual from the opt-

³⁵ <http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2012/036.htm&min=brs&DocType=0>

³⁶ <http://ministers.treasury.gov.au/Ministers/brs/Content/pressreleases/2012/attachments/36/Replacement-for-accountants-exemption.pdf>

³⁷ Section 88B(2) Corporations Act

³⁸ RG 154.10

³⁹ <http://www.asic.gov.au/asic/asic.nsf/byheadline/13-037MR+ASIC+releases+guidance+on+code+approval+under+FOFA?openDocument>



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

in requirement if advice providers are bound by an approved code of conduct and the code obviates the need to be bound by the opt-in requirement.

'Regulatory Guide 183 Approval of financial services sector codes of conduct' (RG 183) has been amended to take into account the changes made by FOFA, in particular the opt-in code of conduct alternative. RG 183 provides guidance to code applicants, as well as licensees and authorised representatives to decide whether to comply with the opt-in requirement or submit a code for approval. ASIC's Commissioner, Peter Kell states that to be approved, an opt-in code must promote client engagement and ensure that clients are paying ongoing fees only if services are provided⁴⁰. RG 183 provides useful information for code applicants, requiring threshold criteria: namely that the code has an enforcement mechanism, is binding and transparent and is reviewed regularly, before any code will even be considered as ASIC approved⁴¹.

For a Code to be approved by ASIC, it must not only satisfy the threshold criteria outlined in RG 183, but it must also satisfy s1101A and s962CA.

ASIC also has the power to approve codes of conduct more generally in relation to the conduct of financial service licensees, authorised representatives and issuers of financial products under s1101A of the Corporations Act.⁴² ASIC must approve the code if it is satisfied that the code isn't inconsistent with any Commonwealth legislation under which ASIC has regulatory responsibilities. ASIC must also consider if it is appropriate to approve the code, having regard to the ability of the applicant to ensure that the persons will comply with the code and the desirability of codes of conduct being harmonised⁴³. The requirement of the harmonisation of codes of conduct means that ASIC will ensure that all approved codes have certain characteristics and meet certain standards of enforcement, administration and review.⁴⁴ However, this does not mean that a code which enforces higher standards will not be approved. Once ASIC has determined that the code meets the threshold criteria under RG 183, they will then need to determine whether the statutory criteria has been satisfied under s1101A(3)⁴⁵.

ii) Regulation of auditors and insolvency practitioners

Both auditors and insolvency practitioners are required to be registered under Part 9.2 of the Corporations Act. Insolvency practitioners must be registered by ASIC provided that ASIC is satisfied that they are adequately educated through a degree, diploma or certificate, satisfied as to experience and are capable of performing the duties of a liquidator⁴⁶.

⁴⁰ <http://www.asic.gov.au/asic/asic.nsf/byheadline/13-037MR+ASIC+releases+guidance+on+code+approval+under+FOFA?openDocument>

⁴¹ RG 183.19 - RG 183.21

⁴² Section 1101A(1)

⁴³ Section 1101A(3)

⁴⁴ RG 183.38

⁴⁵ RG 183.28

⁴⁶ Section 1282 Corporations Act



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Similarly, ASIC must register an auditor if it is satisfied that the applicant is adequately educated through a degree, diploma or certificate from a prescribed institution, has practical experience and satisfied all competency requirements and is capable of performing the duties of an auditor⁴⁷. There are practical exemptions provided in the Corporations Act. Section 324BD provides an exemption from registration for an auditor if it is impracticable for the company to obtain services from a registered auditor due to the locality of the company's business.

(b) The ASIC Act

While there are no provisions in the ASIC Act which alter licensing requirements for members of professional associations, the Act does set a precedent for the facilitation of a co-regulatory partnership by permitting the exchange of information between ASIC and a prescribed professional body under s127.

(c) Other ASIC administered legislation

ASIC administers a number of legislation, especially in relation to credit licensing. The *National Consumer Credit Protection Act 2009* (Cth) (NCCP) requires an individual engaging in credit activities to obtain an Australian credit licence⁴⁸. ASIC must grant the licence to the individual provided that an approved form is submitted, the person isn't likely to contravene their obligations and they are a fit and proper person⁴⁹. There are no provisions in the NCCP Act which relate to licensing when an individual is also a member of a professional association.

(d) ASIC Regulatory Guides and Other Instruments

Apart from RG183 and RG154 discussed above, there is also 'Regulatory Guide 126 - Compensation and insurance arrangements for AFS licensees' (RG 126) which provides some guidance as to how ASIC may treat members of professional bodies in satisfying their licensing requirement to have compensation arrangements. Under RG 126, ASIC is willing to take into account minimum standards set by industry and professional bodies. However, it has explicitly stated that even though individuals may comply with these standards, it doesn't necessarily mean that they have complied with licensing requirements under the Corporations Act⁵⁰.

Under s912B, arrangements for compensation must be stated when dealing with retail clients under a license. This obligation is covered in RG 126 which provides a guide for licensees to determine whether their professional indemnity insurance is adequate. RG 126 gives industry bodies the freedom to determine their own compensation arrangements, such as group compensation arrangements, which ASIC may consider as alternative arrangements that satisfy s912B(2)(b)⁵¹.

⁴⁷ Section 1280 Corporations Act

⁴⁸ Section 35 NCCP

⁴⁹ Section 37 of NCCP Act

⁵⁰ RG 126.34

⁵¹ RG 126.49



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Co-regulation precedent in Australia and overseas

In Australia - by industry

*Legal Industry*⁵²

Historically the legal profession in Australia has been self-regulating. Since 1994 this has gradually changed: lawyers' professional associations now form part of a co-regulatory framework that includes independent statutory authorities and the courts.

The statutory authorities administer the rules, handle complaints, undertake investigations, resolve consumer disputes and conduct research and education. The rules themselves are established by each jurisdiction's legislature. The professional associations assist with disciplinary matters and are also responsible for admission procedures and the like. While statutory authorities and professional associations can and do issue cautions, reprimands and impose minor penalties, serious conduct matters are determined by the Tribunals. The Tribunals also hear appeals and can review decisions.

The balance in these co-regulatory frameworks between government authorities and professional associations varies from jurisdiction to jurisdiction and reflects local conditions. Nonetheless, there is a general tendency towards investing more regulatory power in independent statutory authorities.

Regulatory authorities include professional associations (i.e. law societies and bar associations) and statutory authorities (e.g. Legal Services Commissioners), and the Legal Ombudsman in each State. Functions of regulatory authorities include admitting people to legal practice, issuing practising certificates, making practice rules, receiving complaints against lawyers, resolving consumer disputes and investigating conduct matters.

*Pharmacy Industry*⁵³

The pharmacy industry is currently under reform. These changes are brought about to address the concerns that current regulatory arrangements do not provide adequate public protection regarding compounded medicines. One recommendation is to enhance co-regulation with pharmacy and pharmacist regulators by amendments to Commonwealth legislation to reference the role of professional oversight and requirements, including pharmacy approvals, and clearer requirements regarding medicines exempt from Therapeutic Goods Administration (TGA) processes.

⁵² http://www.olsc.nsw.gov.au/olsc/olsc_education/lsc_lawregulate.html

⁵³ <http://www.tga.gov.au/pdf/consult/consult-medicines-130605.pdf>



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

*Recreational Aviation Industry*⁵⁴

Australian sport aviation operates under self administration. This means that the Government's Civil Aviation Safety Authority (CASA) sets the regulations and then works in close cooperation with established organisations, known as recreational aviation administration organisations or RAAOs, to make sure the regulations are applied and enforced. The RAAOs provide CASA with specialist knowledge and insight into the sport aviation industry. That is CASA makes the rules and the organisations apply the rules to their members.

The organisations exist to oversight members' activities and assure CASA that activities are being conducted safely. CASA needs to be fully confident that RAAOs have the capacity to provide the safety outcomes required.

CASA sets clear expectations for RAAOs and their board members in ensuring that self administration is providing a safe environment for sport aviators as well as other airspace users and people and property on the ground. RAAOs are required to meet performance standards as well as undergo audits. The organisations must continually assure CASA that they are providing appropriate oversight of their sport aviation activities and managing risks.

CASA works in close cooperation with RAAOs as well as receiving regular reports about activities and safety performance and auditing the organisations. As a result CASA is aware of safety issues across the industry. This builds a safer sport aviation industry for both those taking part and the general public.

Sports aviators must belong to a specified organisation. Without full membership sports aviators are not legally allowed to take part in such activities.

If organisations are unable to meet their obligations and assure CASA of their member's compliance, then CASA will not allow the organisation to continue to administer its activities under the exemption. Without the exemption the activities allowed by it cannot occur. That is, if the organisation doesn't assure CASA that it is meeting safety outcomes and overseeing activities, sports aviators are not permitted to fly under the exemption.

Without the exemption then people wanting to fly need to meet the regulations that apply to other aviation activities.

*Media Ratings Industry - ALRC Publication*⁵⁵

In the media ratings industry, links between industry peak bodies and government regulatory bodies regarding classification and content regulation would continue to be important as industry takes responsibility for more classification under the ALRC's proposed model.

⁵⁴ http://www.casa.gov.au/scripts/nc.dll?WCMS:STANDARD::pc=PC_93439

⁵⁵ <http://www.alrc.gov.au/publications/7-who-should-classify-content/industry-bodies-and-their-relationship-regulator>



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

In an ongoing capacity, industry bodies should assist the Regulator to reinforce industry classification requirements, by informing members about classification training options, disseminating information about authorised industry classifiers and collating industry classification reports that include decisions data and complaint statistics.

*Animal Welfare and Livestock Industry*⁵⁶

Several livestock industries have made significant progress in developing quality assurance (QA) programs that incorporate animal welfare requirements. The new Standards and Guidelines will be consistent with the relevant requirements of industry QA programs. It is expected that peak industry bodies will work with jurisdictional governments in a “co-regulatory” environment to establish a primary role for industry QA audit processes to monitor and enforce compliance with standards.

In developing welfare modules for QA programs and participating in development of new Australian Standards, livestock industries must commit to the principle that (minimum) standards must be verifiable (by measurement or audit) and therefore legally enforceable in order to ensure the integrity and credibility of the compliance system. Other requirements and recommendations on welfare will be referred to as guidelines in Australian Standards and Guidelines documents, which will not be legally enforceable but may represent industry best practice or recommended pathways to meeting legal standards. Published in nationally endorsed Standards and Guidelines documents they will be available for reference by courts considering charges of cruelty and for inclusion in QA programs at the discretion of industry.

By Country

UK Model

The Institute of Financial Planning is a professional body for those committed to the development of the multi-disciplinary profession of Financial Planning. It is also an Accredited Body, appointed by the Financial Conduct Authority (FCA) to issue statements of professional standing (SPS) to members who meet the requirements.

To operate as an adviser in the UK, one needs to hold a valid accreditation.

⁵⁶http://www.daff.gov.au/animal-plant-health/welfare/aaws/aaws_international_animal_welfare_conference/a_co-regulatory_approach_to_farm_animal_welfare_in_australia



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

Attachment 3: Regulator approved professional body

The FPA offers the following examples of possible criteria for establishing Regulator approved professional bodies, based on the:

1. Tax Agent Services model
2. Proposed FSA criteria

Tax Agent Services model

The following wording reflects the provisions in the Tax Agent Services Regulations Schedule 1 Part 2 Recognised tax agent association.)

(1) [Definition]

A recognised professional association is an organisation that meets the requirements in subsections (2) to (10).

(2) [The organisation]

The organisation must:

- (a) be administered by a committee of management elected by and accountable to its members; and
- (b) not be carried on for profit or gain (excluding a reasonable salary or honorarium) to:
 - (i) an office holder of the organisation; or
 - (ii) its members; or
 - (iii) members of bodies (*member bodies*) that are its members; and
 - (iv) any person who is a member of that committee of management.

(3) [Good fame, integrity and character]

The individuals who are members of that committee must be of good fame, integrity and character.

(4) [1,000 members]

The organisation must have at least 1,000 financial members who have the right to vote at meetings of the organisation.

(5) [Requirements, academic, etc]

An individual or member body must not be eligible for membership of the organisation unless the individual, or each individual who is a member of the member body (except a student member), has completed the requirements for:



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

- (a) a diploma in financial service or higher qualification issued by a registered training organisation, registered training assessor, or a higher education authority; or
- (b) some other similar qualification, or exemption from qualification, acceptable to the organisation; and
- (c) be compliant with Regulatory Guide 146; and
- (d) has a minimum of one year plus approve financial planning practitioner experience including authorised representative status for the full period; and
- (e) holds authorised representative status.

(6) [Rules of organisation]

Under the rules of the organisation, individuals who are its members or members of its member bodies and who carry on a profession must:

- (a) be subject to rules controlling their conduct in the practice of that profession; and
- (b) be subject to discipline for breaches of those rules; and
- (c) be required to undertake at least 25 hours of continuing professional education in each year (unless exempted in special circumstances); and
- (d) if they are permitted by that organisation to be in public practice - have professional indemnity insurance.

(7) [Operational procedures]

The organisation must have in place adequate operational procedures to ensure it is properly managed and its rules are enforced.

(8) [Complaints procedures]

The organisation must have satisfactory arrangements in place for:

- (a) notifying clients of its members or of members of its member bodies as to how to make complaints; and
- (b) hearing and deciding those complaints; and
- (c) taking disciplinary action if complaints are justified.

(9) [Annual statistics]

The organisation must have satisfactory arrangements in place for publishing annual statistics about:

- (a) the kinds and frequency of complaints (except complaints under this Act about registered tax agents); and
- (b) findings made as a result of the complaints; and



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

(c) action taken as a result of those findings.

(10) [Payment of debts]

The organisation must be able to pay its debts as they fall due.

FSA model

Prior to becoming two separate regulatory authorities - Financial Conduct Authority and the Prudential Regulation Authority – the Financial Services Authority in the UK developed the following criteria requirements⁵⁷ which professional bodies must meet to be granted 'FSA recognised' status.

1. has adequate resources (including financial resources) and systems and controls;
2. is controlled by a governing body comprising persons of good repute;
3. acts in the public interest so that its activities and those of its members contribute to raising consumer confidence and trust in financial planning;
4. provides ASIC with regular independent reports on its activities in respect of financial planners;
5. shares information, including that about individual members, and co-operates with ASIC in an open and transparent manner;
6. leads the professional development of financial planners;
7. has and is effective in promoting standards of professionalism for financial planners at least equivalent to those of ASIC;
8. provides help and guidance in meeting those standards;
9. has effective arrangements for monitoring members' compliance with standards; and
10. has effective arrangements for disciplinary measures against its members

The FSA has also drafted criteria for professional bodies to be accredited.⁵⁸

Acting in the public interest and furthering the development of the profession

⁵⁷ Financial Services Authority, *Delivering the Retail Distribution Review: Professionalism; Corporate pensions; and Applicability of RDR proposals to pure protection advice* (CP 09/31), December 2009 (http://www.fsa.gov.uk/pubs/cp/cp09_31.pdf)

⁵⁸ Financial Services Authority, *Delivering the RDR: Professionalism, including its applicability to pure protection advice, with feedback to CP09/18 and CP09/31* (CP10/14), June 2010, p. 75 (http://www.fsa.gov.uk/pubs/cp/cp10_14.pdf)



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

10. The *FSA* will expect an *accredited body* to have an objective to act in the public interest, to contribute to raising consumer confidence and professional standards in the retail investment advice market and promoting the profession and act in a way that is consistent with that objective.

Carrying out effective verification services

11. If independent verification of a *retail adviser's* professional standards has been carried out by an *accredited body*, the *FSA* will expect the *accredited body* to provide the *retail adviser* with evidence of that verification in a *durable medium* and in a form agreed by the *FSA*.

12. The *FSA* will expect an *accredited body* to have in place effective procedures for carrying out its verification activities. This should include:

(1) verifying that each *retail adviser* who is a member of or subscriber to the *accredited body's* verification service has made an annual declaration in writing that the *retail adviser* has, in the preceding 12 *months*, complied with *APER* and completed the continuing professional development required under *TC 2.1.14R*;

(2) verifying annually the continuing professional development records of no less than 10% of the *retail advisers* who have used its service in the previous 12 *months* to ensure that the records are accurate and the continuing professional development completed by the *retail advisers* is appropriate; and

(3) verifying that, if required by *TC*, the *retail advisers* who use its services have attained an *appropriate qualification*. This should include, where relevant, checking that appropriate qualification gap fill activities have been completed by a *retail adviser*.

13. The *FSA* will not expect an *accredited body* to carry out the verification in paragraph 12(3) if a *retail adviser* provides the *accredited body* with evidence in a *durable medium* which demonstrates that another *accredited body* has previously verified the *retail adviser's* *appropriate qualification*.

14. The *FSA* will expect an *accredited body* to make it a contractual condition of membership (where a *retail adviser* is a member of the *accredited body*) or of using its verification service (where a *retail adviser* is not a member of the *accredited body*) that, as a minimum, the *accredited body* will not continue to verify a *retail adviser's* standards and will withdraw its independent verification of those standards if the *accredited body* is provided with false or inaccurate information in relation to a *retail adviser's* qualifications or continuing professional development or a false declaration in relation to a *retail adviser's* compliance with *APER*. In this regard, an *accredited body* must have in place appropriate decision-making procedures with a suitable degree of independence and transparency. Having appropriate systems and controls in place and providing evidence to the *FSA* of continuing effectiveness



The performance of ASIC

SUBMISSION TO THE SENATE ECONOMICS REFERENCES COMMITTEE INQUIRY | DATE: 21.10.2013

15. The *FSA* will expect an *accredited body* to ensure that it has adequate resources and systems and controls in place.

16. The *FSA* will expect an *accredited body* to have effective procedures in place for the management of conflicts of interest and have a well-balanced board with at least one independent board member.

17. The *FSA* will expect an *accredited body* to have a code of ethics and to ensure that its code of ethics and verification service terms and conditions do not contain any provisions that conflict with *APER*.

Ongoing cooperation with the FSA

18. The *FSA* will expect an *accredited body* to provide the *FSA* with such documents and information as the *FSA* reasonably requires and cooperate with the *FSA* in an open and transparent manner.

19. The *FSA* will expect an *accredited body* to share information with the *FSA* (subject to any legal constraints) in relation to the professional standards of the *retail advisers* who use its service as appropriate. Examples might include conduct issues, complaints, falsification of qualifications or continuing professional development or a failure to complete appropriate continuing professional development.

20. The *FSA* will expect an *accredited body* to submit to the *FSA* an annual report by a suitable independent auditor which sets out that auditor's assessment of the body's satisfaction of the criteria in paragraphs 10 to 19 in the preceding 12 *months* and whether, in the auditor's view, the body is capable of satisfying the criteria in the subsequent 12 *months*. The *FSA* will expect this annual report to be submitted to the *FSA* within three *months* of the anniversary of the date on which the *accredited body* was added to the *Glossary* definition of *accredited body*.