FSC FINANCIAL SERVICES COUNCIL

Australian Law Reform Commission - Financial Services Legislation Inquiry: *ALRC Report 137*

FSC Submission

February 2022

Contents

1. About the Financial Services Council

The FSC is a peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers and financial advice licensees. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

2. Executive Summary

The FSC welcomes the opportunity to submit on Interim Report A **(ALRC Report 137)** of the Australian Law Reform Commission's **(ALRC)** Inquiry into financial services legislation **("the Inquiry"**).

The FSC supports making the law simpler and easier to navigate, while recognising that reform of the Corporations Act 2001 **("the Corporations Act")** and supporting legislation is a significant task that will take considerable time.

The FSC's submission provides general comment on the ALRC's recommendations, and has focused on providing specific feedback in respect of several proposals and questions the Inquiry has sought. In summary, the FSC recommends:

- Central online storage to support navigation
- Mapping of the cost impact of duplication of regulation under the current framework
- An approach which balances the level of principles-based and prescriptive approaches to the law
- Uniform definitions of financial product and financial service and the retention of lists clarifying how activities are defined
- The removal of the power to notionally amend provisions but the retention of the power to create exclusions and grant exemptions
- Removal of the definition of financial product advice, and replacing it with *personal advice* and *general information* (which facilitates accessible and affordable information and assistance to customers who do not seek personal advice having regard to their own individual circumstances)
- Retention of the distinction between wholesale and retail client and increase in the asset threshold for making this distinction and broader simplification of these terms
- In Chapter 7 of the Corporations Act, expanding the objects clause to include the proposed norms
- Not separating the words 'efficiently', 'honestly', and fairly into individual paragraphs, and further consideration before replacing the word 'efficiently'
- Inclusion of examples of conduct that would fail to satisfy the 'fairly' standard

The ALRC's proposals should be implemented with great care and not disturb the meaning of the existing legal framework. To do so would be counteractive to the Inquiry's objectives of improved simplicity and navigability. Many recommendations directly impact the financial advice regulatory framework, itself subject to a comprehensive review by Government. The ALRC, while independent, should develop its recommendations appreciative of the outcomes of the Government's Review.

The FSC will be actively contributing to the ALRC's Inquiry ahead of it reporting in December 2023. We would welcome the opportunity to discuss our submission further.

3. FSC Recommendations

1. The FSC supports in principle recommendations to simplify the legislative framework for financial advice by repealing or amending the Corporations Act. However, support for each individual recommendation would depend on final proposals which should be subject to further consultation with the sector. Such changes could further complicate the legislative framework and avoiding such a scenario is essential to their implementation.

2. Financial advice-related recommendations should interact cohesively with outcomes of the Government's Review of the quality of financial advice that will report in December 2022

3. Given the time it will take to reform the Corporations Act, an online version of existing financial services laws with hyperlinks to all subsidiary legislation and definitions required under a particular area of financial services law should be made feely available through a definitive Government source. Further, all defined terms should be capitalised so that the reader knows to look for a definition.

4. Changes made by legislative instrument should be incorporated into the Corporations Act periodically.

5. The Inquiry should examine the cost of the legislative framework in developing its recommendations with three measures:

    a. the impact of the existing framework against simpler alternatives it proposes
    b. mapping the laws and regulations where interpretation has gone beyond the original policy intent envisaged by Parliament and costing this impact and savings that could be achieved by better realigning regulation with legislative intent
    c. the cost impact of duplicative laws or siloed policy-making where new laws duplicate or conflict with existing laws and regulations that are not repealed and where carve-outs could reduce cost and enable a more seamlessly applied legal framework.

6. The FSC supports the ALRC's proposed definitional principles to reduce complexity. The primary regulatory principle guiding the definition of the law should be certainty to protect consumers and promote market confidence. 'Black letter law' should be the preferred approach to defining the law in areas that carry higher penalties for misconduct and a more principles-based approach could be used for areas carrying lower penalties.

7. Presentation of the law online is a key way to ensure every day professionals can access and understand their obligations. Close attention should be paid to its online presentation (eg hyperlinks, platforms that are easy to navigate and access, and centralised repositories of information).

8. The FSC supports uniform definitions of 'financial product' and 'financial service' and any changes must be sensitive to all current laws which contemplate the definitions

currently in place without changing the intent of the legislation. or bringing about unintended changes to the policy of the law. These changes should align with the outcomes of the Government's Review of the Quality of Financial Advice.

9. In implementing uniform definitions, the FSC does not support the removal of lists clarifying what are products or services under the law as this would be counteractive to the simplicity and accessibility the Inquiry aims to achieve. The current in force Acts Interpretation Act (AIA) should be the primary source of definitions (rather than an "as at" 2005 (AIA).

10. The FSC supports aligning definitions with the National Consumer Credit Protection Act 2009, however, this is contrary to the proposal to have all definitions in one place and not in separate Acts.

11. The FSC supports the adoption of the term 'preparer' however outcomes-based disclosure should be avoided adding to underlying uncertainty as to the disclosure and comparability of financial products.

12. The FSC supports removing the power to notionally amend provisions of Chapter 7 of the Corporations Act by regulation or other legislative instrument (particularly where notional provisions add obligations or conditional obligations not passed by Parliament)). However, the FSC believes that the power to grant exemptions and exclusions from obligations in Chapter 7 of the Act does need to be retained where it is used to narrow the scope of existing obligations to remedy inappropriate or unintended consequences or where the regulatory burden is shown to be unduly excessive.

13. The FSC supports amending the Corporations Act to provide for a power to create exclusions and grant exemptions from Chapter 7 of the Act in a consolidated legislative instrument, but submits that careful consideration should be given to whether it is appropriate for ASIC alone to have that power, given that their primary function is as a regulator and that law making is the job of the Parliament, supported by the Commonwealth Treasury.

14. The FSC supports an interim measure to improve the visibility and accessibility of notional amendments to the Act.

15. Following abolition of the safe harbour steps, and reforms to the documentation requirements**,** the definition of 'financial product advice' in section 766B in the Corporations Act should be removed and the definitions of 'personal advice' and 'general information'(capturing what is factual information and general advice) legislated in its place and de-anchored from financial product. 'Intra-fund' advice, 'strategic' advice, 'specialised' advice should simply be personal advice. Specialised advice should be a restricted form of personal advice and the persons authorised to provide such advice should be a matter for the profession and enforced through standards. The scope of restrictions that should apply to providers of specialised personal advice should be a matter for ASIC and Treasury. Changes to the definitions

should align with the outcomes of the Government's review of the quality of financial advice.

16. Personal advice should be defined in legislation as advice that in fact considers the personal circumstances of an individual consumer. The current education and professional standards should continue to apply to providers of personal advice. Personal financial advice should only be provided by a trained qualified financial adviser.

17. 'General Information' should be defined as factual information that is not specific to an individual's circumstances and which does not make or imply recommendations based on an individual's own financial circumstances (but general information should encompass factual information and what is now described as general advice). General Information should be legislated and consolidate the remaining elements of 'General Advice', as well as the existing concepts of 'Education' and 'Factual Information'. ASIC should support the interpretation of General Information with regulatory guidance.

18. The distinction between wholesale and retail client should be retained, as well as an objective test for assessing clients, but the asset test threshold amended and indexed.

    - In 2023 the threshold for the asset test for determining a wholesale client should increase to $5 million and be indexed to the Consumer Price Index.
    - The other tests should remain unchanged, including the $250,000 income threshold.
    - An existing wholesale client that would be reclassified as a retail client as a result of this change can opt to remain a wholesale client if this election is made within a two-year transition period.

    Following the completion of the FASEA transition period in 2026, the Government should review whether an objective threshold is necessary and instead be replaced by allowing financial advisers to use their professional judgement to determine who is a wholesale client, as guided by the statutory Best Interests Duty and Code of Ethics framework.

19. Any simplification of these terms should ensure their meaning is retained. The policy consequences of removing these terms should be carefully considered. The type of products should not determine whether a consumer is a wholesale or a retail investor. The terms wholesale, professional or sophisticated investors should be relabelled with one term to reduce complexity.

20. The FSC supports the proposal to amend Chapter 7 of the Corporations Act 2001 to insert certain norms as an objects clause. This amendment should not duplicate similar provisions in other legislation or sections of the Corporations Act.

21. The FSC agrees with the objective of removing provisions in the Corporations Act that are already captured by the 'efficiently, honestly and fairly' obligation, however we would suggest caution in respect of removing s 912A(1)(aa)) and s 912A(1)(h) given

ASIC has emphasised the importance of these two aspects in their surveillance activities in relation to management of conflicts and risks in recent years.

22. The FSC does not recommend separating the words ‘efficiently’, ‘honestly’, and ‘fairly’ into individual paragraphs.

The FSC would support further consideration of replacing the word “efficiently” with a more appropriate word, although we would suggest that “professionally” be considered alongside the word “competently”. Also, support has been expressed for inclusion of the word “reasonable”.

In principle, the FSC agrees with inserting a note containing examples of conduct that would fail to satisfy the ‘fairly’ standard, and that there be clarification of how such examples would apply in practice.

4. General comment on the ALRC's Recommendations

This submission focuses its response on the specific questions asked of submitters by the ALRC

Recommendation
The FSC supports in principle recommendations to simplify the legislative framework for financial advice by repealing or amending the Corporations Act. However, support for each individual recommendation would depend on final proposals which should be subject to further consultation with the sector. Such changes could further complicate the legislative framework and avoiding such a scenario is essential to their implementation.

Recommendation
Financial advice-related recommendations should interact cohesively with outcomes of the Government's Review of the quality of financial advice that will report in December 2022.

Recommendation
Given the time it will take to reform the Corporations Act, an online version of existing financial services laws with hyperlinks to all subsidiary legislation and definitions required under a particular area of financial services law should be made feely available through a definitive Government source. Further, all defined terms should be capitalised so that the reader knows to look for a definition.

Centrally locating the existing law will enable more seamless access than is the case currently, before the longer-term task of reforming the Corporations Act is embarked on.

The Corporations Act, Regulations and associated legislation have become unmanageable and inscrutable in recent years, leading to costs and delays. Some law reforms have been beneficial for consumers and/or market participants[1], and in other cases the increased weight of regulatory burden or confusion created has been disproportionate to these gains[2].

The ALRC's work in calling out certain aspects of the law as dysfunctional, such as notional amendments to the Corporations Act through Class Orders being "deeply inaccessible"[3], is commendable. If participants in financial services and markets are to comply with the law, they must first understand it.

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[1] For example, Chapter 5C (managed investment schemes) introduced in 1998 is brief and simply drafted, and has been a relatively effective reform.
[2] The detailed requirements to apply for or vary an Australian Financial Services Licence, and the legislative instruments associated with ASIC's Regulatory Guide 97 (disclosure of fees and costs), are examples of excessively complex and difficult rules that waste resources.
[3] Paragraph 17 of the Report.

Certainty should be the guiding principle behind future changes and reapportioning a balance between the level of objectivity or prescription in the law where needed, with greater principles-based approaches in respect of other provisions. Changes to the Corporations Act arising from the Inquiry should not remove efficiency or clarity from the obligations of the law and avoid the unintended consequences of changing words in seeking to make it presentable and easier to access.

Many of the issues within the scope of the Inquiry are also within the scope of a Government Review of financial advice that is effectively underway. The ALRC's recommendations will come a year after this Review makes its recommendations to government. The ALRC's recommendations in relation to financial advice should interact cohesively with the recommendations from the Government's review. The ALRC should incorporate the feedback of industry to the Government's Review given its critical relevance to the Inquiry's scope.

Recommendation
Changes made by legislative instrument should be incorporated into the Corporations Act periodically.

A defining lever of the legislative framework has been the regular and comprehensive use of Legislative instruments. Changes to requirements by legislative instruments should periodically be incorporated into the Corporations Act. The Inquiry should consider an approach that regulations are still used to make changes in a timely manner and then on a regular basis (eg annually, matters specified in regulations become absorbed into the Act). This would ensure regulations do not become unwieldy while ensuring appropriate parliamentary oversight.

A recent example of how this could be done is the *Corporate Collective Investment Vehicles and Other Measures Bill* which amends the Corporations Act to incorporate some items currently specified in the regulations into the primary legislation to improve readability of the law. Areas where this approach could be picked up for financial advice laws include, the requirement to issue an Statement of Advice **(SOA)** within five business days when providing time-critical advice and requirements around an authorised representative authorising a representative.

5. Empirical data – Proposal A1

Recommendation
The Inquiry should examine the cost of the legislative framework in developing its recommendations with three measures:

a. the impact of the existing framework against simpler alternatives it proposes
b. mapping the laws and regulations where interpretation has gone beyond the original policy intent envisaged by Parliament and costing this impact and savings that could be achieved by better realigning regulation with legislative intent
c. the cost impact of duplicative laws or siloed policy-making where new laws duplicate or conflict with existing laws and regulations that are not repealed and where carve-outs could reduce cost and enable a more seamlessly applied legal framework.

The direct benefit of making the legislative framework simpler and easier to navigate must correspond with reductions in the costs of compliance. The fundamentals of consumer protection should be maintained, while ensuring the framework can anticipate dynamic changes long-term.

The cost impact should consider the framework and how it is being applied in real terms across the financial services sector. This should have regard for the impact of duplication. For example, the introduction of the Design and Distribution Obligations **(DDO)** conflicts with a pre-existing disclosure framework or makes aspects of that framework redundant, and the costs of these changes should be considered.

The Inquiry should have regard for the interpretations made by independent financial regulators and the extent to which the derogation of these interpretations from Parliament's intent is exacerbating cost as well as its acceptability at law. There is a disconnect between how legislation is intended to operate and how it is interpreted by bodies like the Australian Securities and Investments Commission **(ASIC)** and the Australian Financial Complaints Authority **(AFCA)**. AFCA outcomes and ASIC outcomes could be assessed for the extent to which they reflect the policy intent of legislation captured in second reading speeches to Parliament, to see if the intent of the law correlates to how it is being interpreted by these bodies.

To generate these insights the ALRC can leverage the following data points:

- Articles and commentary made historically about aspects and application of financial services law
- Data from the former Financial Ombudsman Service **(FOS)** and the Superannuation Complaints Tribunal **(SCT)** in addition to the data they have considered from AFCA
- The ALRC could also look at notification of serious compliance concerns as this may indicate aspects of the law that are not clear or where there are issues with compliance with the law.

- Another data point to highlight the complexity of the law is the average number of pages a licensee has to pull together for an adviser to understand their obligations. Advisers should be able to just read the law and understand what is required.

Examples where industry can incur significant legal costs for complying with laws with minimal consumer benefit include:

- Application of licensing laws to investment structures which are internal to an organisation or all involved are professional investors.
- The licensing and licence variation process, a detailed and slow process that could be improved through a fixed timeframe for processing and less granular information required.
- The disclosure of fees and costs. While ASIC Regulatory Guide 97 has been the subject of independent review, it is still complicated to apply and is one area where principles-based rules could work effectively.
- Holding assets as trustee falls within the definition of “custodial or depository service” with the result that wholesale arrangements can require complex analysis and structuring, or slow and costly licence variations, with little or no regulatory benefit.

6. When to define – Proposal A2

Recommendation
The FSC supports the ALRC's proposed definitional principles to reduce complexity. The primary regulatory principle guiding the definition of the law should be ***certainty*** to protect consumers and promote market confidence. 'Black letter law' should be the preferred approach to defining the law in areas that carry higher penalties for misconduct and a more principles-based approach could be used for areas carrying lower penalties.

Presentation of the law online is a key way to ensure every day professionals can access and understand their obligations. Close attention should be paid to its online presentation (eg hyperlinks, platforms that are easy to navigate and access and centralised repositories of information).

Principles based regulation

A principles-based approach to defining the law would ensure it keeps pace with dynamic change and requires little amendment over time. Implementing this approach should ensure balanced levels of *objectivity* (and precision) and *subjectivity* at different parts of the framework, as opposed to a purely principles-based regime as seen, for example, in European jurisdictions. It is helpful for certainty that Australian law is currently mostly black-letter law, but over time the Corporations Act has become outdated, complex and costly.

The policy implications and transition costs of changes must be considered. The FSC suggests areas which carry high penalties for misconduct should be regulated with areas of higher prescription, and areas for which the penalties are lower should attract a principles-based approach reflecting and encouraging the use of judgement, choice and a more holistic consideration of the circumstances. For example, principles-based procedures offer less certainty for the sector systemising compliance with breach reporting obligations than a more objective, prescriptive approach.

The FSC has proposed a principles-based regulatory framework for the advice sector to be rolled out by 2026 where prescription is currently exacerbating costs and conflicting the implementation of the a principles-based Code of Ethics, following the removal of the safe harbour steps for meeting the Best Interests Duty and consolidation of the disclosure regime and definitions of financial advice to enable a simpler advice process that recognises the professional judgement of financial advice providers than on 'tick-box' approaches to compliance.

Definitions

While simplification of definitions, such as removing the handful that are not used, grouping definitions all in one place, correcting anomalies such as the multiple meanings of "securities" and capitalising terms throughout, are worthy objectives, changing the scope of key definitions such as 'financial product' and 'financial service' have significant ramifications. Activities that are currently regulated may cease to be so, and some that are

not may be caught, in unintended ways. Removal of definitions from the Corporations Act that are, for example, in the Acts Interpretation Act as this would be contrary to a key objective of making the law more accessible and intelligible.

Corporations Act terms are widely used in contracts and disclosure documents and are the foundation of compliance and reporting systems in financial institutions. Caution should be exercised before removing the definition of "of". The term "securities of a body" could be interpreted incorrectly if not expanded by this definition. It relates to the responsible entity (which is a body) of a managed investment scheme (which is not, as a trust is not a separate legal person), and provides that "of" means, in the case of a managed investment scheme, "made available by". This is important to distinguish the responsible entity company's own shares from units in a trust issued by it as trustee.

By contrast, statutory duties of directors and officers that carry civil penalties or are offence provisions should be clear and certain, and be able to reference past decisions of the courts as much as practical.

7. Definitions of ‘financial product’ and ‘financial service’ – proposals A3, A4, A5 and A6

Recommendation
The FSC supports uniform definitions of ‘financial product’ and ‘financial service’ and any changes must be sensitive to all current laws which contemplate the definitions currently in place without changing the intent of the legislation or bringing about unintended changes to the policy of the law. These changes should align with the outcomes of the Government’s Review of the Quality of Financial Advice.

Recommendation
In implementing uniform definitions, the FSC does not support the removal of lists clarifying what are products or services under the law as this would be counteractive to the simplicity and accessibility the Inquiry aims to achieve. The current in force Acts Interpretation Act (AIA) should be the primary source of definitions (rather than an “as at” 2005 (AIA).

Enacting changes to these definitions can have significant implications for innovation and the consistency of the law. Readers of the law will have to consult other legislative acts to understand the law, the lack of capitalisation of defined terms in the Corporations Act creates ample room for widespread error that this change needs to guard against.

The proposal to retain the broad functional definition of “financial product” but remove the list of inclusions and exclusions may reduce the number of pages in the Corporations Act but the law’s clarity and accessibility will be severely compromised. It is unclear, for example, if an an ordinary citizen or the operator of a small business would then be able to know if, a share is a financial product. The sections that would remain, ss763A to 763E are technical and difficult to apply in the legislation.

Further, taking out the specific inclusions and exclusions in the meaning of “financial product” would remove the clear parts, leaving only the parts that are difficult to understand and apply. An alternative approach would be to leave the specific lists, remove the definitions in ss763B to 763D, and give s763A a descriptive (not determinative) purpose, like an objects clause. The lists would need to be amended to capture new types of financial products that are invented. For example, some types of cryptocurrency assets are financial products and some are not, depending on their structure.

There is a trade-off between certainty and simplicity and the rule of law against seeking to ensure that all new activities are automatically regulated, in which certainty is the primary objective. There is still the need for a mechanism to allow for the evolution of financial services and financial products.

Recommendation
The FSC supports aligning definitions with the National Consumer Credit Protection Act 2009, however, this is contrary to the proposal to have all definitions in one place and not in separate Acts.

Referencing this definition in the Corporations Act and Australian Securities and Investments Commission Act 2001 **("the ASIC Act")** does not solve the issue of complexity and needing to cross reference. If the definitions do not cross reference and cut and paste it across, then the definition will need to be amended in each other Act that uses it if changes are made in the future. As such, we do not see the benefit of adding credit to the definition of a financial product. If it is added to the definition of financial product in the Corporations Act we anticipate that further exclusions will need to be incorporated to other parts of the Corporations Act (eg the requirement to provide a Statement of Advice which does not achieve the goal of reduced complexity).

8. Disclosure – proposals A7 and A8

Recommendation
The FSC supports the adoption of the term 'preparer' however outcomes-based disclosure should be avoided adding to underlying uncertainty as to the disclosure and comparability of financial products.

While "preparer" is a more logical term than "responsible person", if adopted it will be necessary to define "preparer" to include the person on whose behalf the product disclosure statement **(PDS)** is prepared. For example, the responsible entity **(RE)** of a registered scheme must be the issuer of the PDS for the scheme (section 1013A) but as a practical matter it might be the investment manager for the scheme that prepares the PDS. In this scenario, the RE should be the party with liability.

An outcomes-based standard of disclosure approach could add a level of uncertainty for industry that recommendations from the Inquiry should guard against and an objective (and somewhat prescriptive) approach is needed. ASIC has, through issuing class orders, been making enforceable laws or sections of the act without oversight of Parliament albeit that administrative action by ASIC can be subject to disallowance motions from Parliament. The outcomes-based standards should be supported by detailed requirements and clear guidance to facilitate comparability.

There are questions as to how this change will support the policy objective of the comparability of products. Paragraphs 9.127-8 of Interim Report A contemplates this obligation to be adapted depending on the product by framing the obligation as "reasonable steps" (eg at paragraph 9.128 the ALRC considers "reasonable steps" for a novel product may include consumer testing of disclosure approach). Unless there is clear regulatory guidance, this may lead to reticence of product issuers to take advantage of innovative methods for PDSs. If Proposal A8 is adopted, it may succeed if there is a requirement for regulator consent for action to be taken under the provision. Otherwise, there appears to be inconsistent interaction with the AFCA regime – which does not consider the legal obligation alone of a product issue but makes determinations also on the basis of fairness. The AFCA standard of fairness is inconsistent with the "reasonable steps" framework as what is "reasonable" is not necessarily "fair"

There are several issues with the existing disclosure regime the ALRC should consider as it formulates its recommendations:

- There is no obvious justification for having securities offered under a prospectus regime in Chapter 6D and other financial products under a PDS in Chapter 7, with the duplicative result that stapled securities comprising a unit and share must be offered under a document complying with both regimes.
- Documents for initial public offers typically run to more than 100 pages which are probably only read by advisers and not investors, and they are often prepared more for the issuer's compliance and risk management than communication about the investment.

- The “shorter” PDS regime that requires an eight page PDS for “simple managed investment schemes” requires so many prescribed statements that there is no room for the issuer to give a useful explanation of the product to investors.
- With the introduction of the design and distribution obligations, the philosophy of consumer protection in relation to financial products has shifted from the traditional reliance on disclosure and “buyer beware” to the issuer and distributor taking responsibility for the suitability of the product for the persons likely to be in the target market to which it is promoted. This reduces, although does not eliminate, the importance of disclosure documents. The commencement of DDO may mean it is appropriate to ascertain if other obligations (now superseded by DDO) should be removed.

9. Exclusions, Exemptions and Notional Amendments – proposals A9, A10, A11 and A12

Recommendation
The FSC supports removing the power to notionally amend provisions of Chapter 7 of the Corporations Act by regulation or other legislative instrument (particularly where notional provisions add obligations or conditional obligations not passed by Parliament). However, the FSC believes that the power to grant exemptions and exclusions from obligations in Chapter 7 of the Act does need to be retained where it is used to narrow the scope of existing obligations to remedy inappropriate or unintended consequences or where the regulatory burden is shown to be unduly excessive.

The power to notionally amend provisions of Chapter 7 of the Act gives rise to numerous problems and difficulties, as outlined in some detail in the ALRC Report. The power to notionally amend the Corporations Act should be removed.

With regard to exemptions and exclusions, there is an important distinction to be made between:

a. the power to expand the scope of existing obligations, and
b. the power to narrow the scope of existing obligations.

In our view, ASIC's power to expand the scope of existing obligations by way of additional requirements should be removed.

ASIC's role is to administer and regulate compliance with the law, and the Court's role is to determine interpretation of the law. We believe Executive oversight is required for regulations relating to the financial services industry. Whilst the Australian Tax Office **(ATO)** can make rules, we see the agencies as different, because they relate to scenarios that can be anticipated. For example if 'situation A' occurs, then this is how it will be treated for tax.

However, it is essential for ASIC's discretion to provide relief by way of creating exclusions and granting exemptions (in both general and particular instances) be retained (albeit not by way of notional amendment where obligations are added or conditional obligations are added, rather than exclusions). Modifications to allow legitimate business activity that would otherwise be prevented by laws with inappropriate or unintended consequences are part of the everyday operation of the financial services sector.

Changes sometimes need to be made urgently and transparently. The ability for ASIC to move relatively quickly to address inappropriate or unintended consequences is an important part of the framework of financial services regulation in Australia. Financial services businesses often require relief to be granted outside the parliamentary process in order to carry on business operations. If ASIC's power to act in this way is completely removed such that only parliament or the courts are able to carry out this role, our concern is the process would become unwieldy, cumbersome and too slow and ineffective.

Recommendation
The FSC supports amending the Corporations Act to provide for a power to create exclusions and grant exemptions from Chapter 7 of the Act in a consolidated legislative instrument, but submits that careful consideration should be given to whether it is appropriate for ASIC alone to have that power, given that their primary function is as a regulator and that law making is the job of the Parliament, supported by the Commonwealth Treasury.

The FSC supports the objective of having a single consolidated legislative instrument which would serve as the sole source of these exclusions and exemptions. However, steps will need to be taken to ensure that such an instrument is navigable and does not become unwieldy or overly difficult to use and understand.

We support further analysis to determine whether such power should be granted to ASIC or some other body or bodies. As an interim measure, ASIC, the Department of the Treasury (Cth), and the Office of Parliamentary Counsel (Cth) should develop a mechanism to improve the visibility and accessibility of notional amendments to the Corporations Act (Cth) made by delegated legislation.

Recommendation
The FSC supports an interim measure to improve the visibility and accessibility of notional amendments to the Act.

The FSC agrees that interim arrangements would be helpful. It would also be desirable to discontinue ASIC's practice of reviewing and reissuing Class Orders every 10 years. Changing the date and number of a necessary exemption could make it more difficult for users to find, use up regulatory resources, and might not be a useful process. In pursuing this change the ALRC should be mindful of the sunsetting clauses set out in the Legislation Act 2003 which apply to all legislative instrument potentially outside the scope of the Inquiry.

The "black letter" law should remain in the Corporations Act and not be replaced by broad statements and a "rule book" issued by the regulator, as in the UK and some other jurisdictions. Giving such broad powers to the regulator effectively makes them a legislator, reducing oversight and accountability in law-making.

10. Definition of 'financial product advice' – proposals A13, A14 and A15

Recommendation
Following the abolition of the safe harbour steps, and reforms to the documentation requirements, the definition of 'financial product advice' in Section 766B in the Corporations Act should be removed and the definitions of 'personal advice' and 'general information' (capturing what is factual information and general advice) legislated in its place and de-anchored from financial product. 'Intra-fund' advice, 'strategic' advice, 'specialised' advice should simply be personal advice. Specialised advice should be a restricted form of personal advice and the persons authorised to provide such advice should be a matter for the profession and enforced through standards. The scope of restrictions that should apply to providers of specialised personal advice should be a matter for ASIC and Treasury. Changes to the definitions should align with the outcomes of the Government's review of the quality of financial advice.

To make financial advice more accessible to consumers the FSC proposes the multiple complex labels used to describe different types of advice are consolidated and remove the nexus between advice and product. Reducing cost is only part of the objective of this change. Consumers do not readily understand the difference between advice and information and do not always have an understanding of what good financial advice entails. The rise of technological disruption and 'finfluencers' demonstrates just how fluid the borders between different definitions of advice and information have become. Removing the definition of 'financial product advice' from the Corporations Act will help ensure advice is agnostic of financial product. The FSC recognises that consumers seek strategic advice over product specific recommendations, and advice regulation should focus on how to use products to achieve consumers' goals.

The High Court's decision[4] on the parameters of General Advice has also rendered the current definitions of financial advice uncertain. The DDO require consideration of a consumer's circumstances to fit the target market determination **(TMD)**. These changes have given rise to the need for a clear definition of personal advice that can be seamlessly provided by the many interlocking segments of the advice industry, including advisers, licensees, product issuers, stockbrokers and accountants. The existing framework consists of nine different definitions of advice[5] such as 'intra-fund advice', 'strategic advice', 'scaled/limited advice', which are confusing regulatory terms that do not resonate with consumers. Analogous with other professions, the FSC seeks a regime in which an advice provider either provides financial advice based on an individual's objectives, financial situation and needs or does not, with all advice considered personal advice except where it is simply general information or assistance (namely, it is not personal advice).

[4] Westpac Securities Administration Ltd & Anor v ASIC (2021) HCA 3.
[5] Page 3, Future of Advice. Rice Warner.

Pursuit of much clearer terminology will better distinguish advice and information, and their regulatory requirements, while supporting compliance. KPMG estimates that re-labelling or simplifying the model of financial advice will likely result in a 9 per cent reduction in the cost of advice or reduce the cost of the advice process from $5,334.64 to $4,865.39.[6]

	Personal Advice	General Information
Definitions and classifications to be repealed	'Intra-fund' 'Strategic' 'Comprehensive 'Specialised' 'Scaled' or 'Limited'	'Factual information' 'Education'

Personal advice

Recommendation
Personal advice should be defined in legislation as advice that in fact considers the personal circumstances of an individual consumer. The current education and professional standards should continue to apply to providers of personal financial advice. Personal financial advice should only be provided by a trained qualified financial adviser.

Any information that considers the individual circumstances of a consumer would constitute personal advice.

General information

Recommendation
'General Information' should be defined as factual information that is not specific to an individual consumer's circumstances and which does not make or imply product recommendations. General Information should be legislated and consolidate the remaining elements of 'General Advice', as well as the existing concepts of 'Education' and 'Factual Information'. ASIC should support the interpretation of General Information with regulatory guidance.

The result of the High Court's General Advice decision means much of the activity undertaken by advice businesses previously considered general advice now constitutes personal advice. The FSC proposes resolving this issue by creating a clear legal distinction between what is *personal advice* and what is *general information (or not personal advice)*, and that distinction is accounting for an individual's circumstances. Information outside the personal advice framework would constitute general information (and encompass what is now called general advice). The regulator should make determinations and exemptions in

[6] KPMG Research, *Cost profile of the financial advice sector*. Page 28.

respect of activity that might include targeted information aimed at a cohort of people rather than accounting for an individual's circumstances.

Just providing general information in and of itself should not qualify as personal advice for example if it targets groups of people. As such, definitions should emphasise the "individual client's circumstances", not personal circumstances, which could have a much broader application. For example, a seminar with an audience of 30 people where an employee of the fund said "the XYZ MySuper product is a good product" (or even implied that it is a good product) might be considered a recommendation or opinion under the existing law. Another example could be a call centre employee for a super fund taking a call where they are assisting a member with enquiries the member has to consolidate their superannuation. Under the current provisions the employee will provide information to the member and may make a general recommendation (eg 'someone in your age group may consider moving into a pension phase product').

The 'general information' proposed definition should allow for these types of scenarios.

Practical issues with changing the definitions of advice

The ALRC should ensure that the recommended structure of definitions ensures appropriate clarity in pursuit of all of its proposals in this area.

For example, it is not clear whether the definition under Proposal A13(c) will be exhaustive. Otherwise, is there scope for exclusions from the definition (e.g. under ASIC's new power under Proposal A10) in particular relating to the following circumstances:

- Activities under DDO obligations which could foreseeably enliven personal advice obligations under the "expectation" formulation of the High Court *Westpac v ASIC*
- Activities under the upcoming Retirement Income Covenant obligations which could foreseeably enliven personal advice obligations under the "expectation" formulation of the High Court *Westpac v ASIC*, and
- To grandfather existing exemptions from financial advice laws (e.g. exclusions under ss766B)

Alternatively, the ALRC should consider whether the law be restructured or redrafted in a way that prevents the existing inconsistency between different provisions with often different policy objectives. For example, between the advice laws which on the *Westpac v ASIC* interpretation where a reasonable expectation that personal circumstances lead to personal advice, and the upcoming Retirement Income Covenant or the DDO regime which require providers to actively contemplate the personal circumstances of cohorts of members. This could lead to expensive and time-consuming litigation on which set of laws prevail in given circumstances. The statute needs to be clear that conflicts of laws within its own provisions shouldn't be raised.

11. Definition of 'Retail Client' and 'Wholesale Client' – proposals A16 and A17

Recommendation
The distinction between wholesale and retail client should be retained, as well as an objective test for assessing clients, but the asset test threshold amended and indexed.

a. In 2023 the threshold for the asset test for determining a wholesale client should increase to $5 million and be indexed to the Consumer Price Index.
b. The other tests should remain unchanged, including the $250,000 income threshold.
c. An existing wholesale client that would be reclassified as a retail client as a result of this change can opt to remain a wholesale client if this election is made within a two-year transition period.
d. Following the completion of the FASEA transition period in 2026, the Government should review whether an objective threshold is necessary and instead be replaced by allowing financial advisers to use their professional judgement to determine who is a wholesale client, as guided by the statutory Best Interests Duty and Code of Ethics framework

The FSC supports amending the definition of retail and wholesale clients to ensure a greater proportion of financial advice consumers are considered 'retail' clients, and hence fall within the consumer protection framework.

The Corporations Act presumes all consumers are retail clients unless they can satisfy a test to be classified a wholesale investor. However, the thresholds for meeting the requirements of a wholesale client are based on 1991 figures.

The wholesale client asset test threshold should be increased to $5 million and indexed to protect 275,000 more consumers and keep pace with changes in the level of wealth of consumers. At the same time, the other tests should remain unchanged, including the $250,000 income threshold.

A decade ago in 2011, Treasury produced a consultation paper, proposing to update the wholesale/retail client distinction as part of the Future of Financial Advice **(FoFA)** reforms, but changes did not follow. At the time, it was asserted that changing the test would have the effect of preventing Australian entities from rapid access to institutional capital, affecting mergers and acquisitions activity and capital management strategies. To accept this as the overriding consideration is to suggest that the test can never be changed, even though asset price inflation has turned the $500,000 threshold for the "price test" and the $2 million asset requirement for the "wealth test" to sums held by many Australians who are not expert investors, simply through their home or superannuation holdings.

It is recognised that the test is used in many contexts – AFS licence conditions, relief instruments including Class Orders facilitating cross-border transactions and various sections of the Corporations Act– but grandfathering existing arrangements with a two year transition period for new investments to be classified under a reformed test should resolve any difficulties.

Recommendation
Any simplification of these terms should ensure their meaning is retained. The policy consequences of removing these terms should be carefully considered. The type of products should not determine whether a consumer is a wholesale or a retail investor. The terms wholesale, professional or sophisticated investors should be relabelled with one term to reduce complexity.

While the wholesale-retail distinctions should be retained, steps should be pursued cautiously to simplify terminology without altering their overall meaning. For example, removing subsections would have substantive policy consequences, for example in relation to self-managed super funds.

Better acknowledgement of the purpose of which a financial product or service is provided, is needed in determining the nature of the distinction – for example, personal use versus business use. Personal net worth is a blunt instrument which does not correlate with financial sophistication, and perhaps whether professional advice is received is also relevant (eg the exclusions in DDO legislation for advised retail clients).

12. Conduct Obligations – proposals A18, A19, A20, A21, A22, A23 and A24

Recommendation
The FSC supports the proposal to amend Chapter 7 of the Corporations Act 2001 to insert certain norms as an objects clause. This amendment should not duplicate similar provisions in other legislation or sections of the Corporations Act.

The FSC supports the suggestion to expand the current objects clause for Chapter 7 of the Corporations Act (in section 760A) to include certain norms as further set out below. This could potentially strengthen the expressive power of the law and improve understanding of the key principles that underpin the more detailed and prescriptive elements of the Corporations Act. This would more adequately distinguish the serious obligations (for example, duties to look after other people's money and act honestly) as opposed to administrative obligations such as to lodge reports.

The FSC broadly supports the norms identified by the Financial Services Royal Commission[7] being included in the Corporations Act, except for the norm of 'obey the law' which we do not think is necessary given that it is not specific to financial services and virtually all businesses and consumers would consider obeying the law is "a given". To include this norm in the Corporations Act might actually be counterproductive if it makes the reader question the overall sense of the Corporations Act. There is however merit in stating the full particulars of the applicable sanction for any contravention within the part, division or section stating the obligation, so that these are readily identifiable. The norms should inform interpretation but be subject to more detailed provisions which the norms provide an interpretation framework for.

Expanding the objects clause should avoid duplication. If the clause is replaced this should include object that covers "facilitating efficiency, flexibility and innovation in the provision of those products and services" (current s760A(a)).

The FSC also agrees with the ALRC suggestion that the norms could be called "Australian Financial Services Conduct Principles", which gives them a readily understandable everyday meaning and is consistent with the nomenclature adopted in the UK. The United Kingdom's "11 Principles for Business, as provided by the Financial Conduct Authority **(FCA)** in a handbook is a concept the ALRC could have reference to in incorporating the six norms identified by the Financial Services Royal Commission.

[7] Commonwealth of Australia, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (n 2) 42.

The ALRC should consider closely:

- How centralising the misleading or deceptive provisions in the ASIC Act 2001 (removed from Corps Act) would assist with Chapter 7 interpretation.
- How inclusion of the norm of providing services that are fit for purpose do not duplicate the provision in s761A: "fairness, honesty and professionalism by those who provide financial services"

Recommendation
The FSC agrees with the objective of removing provisions in the Corporations Act that are already captured by the 'efficiently, honestly and fairly' obligation, however we would suggest caution in respect of removing s 912A(1)(aa)) and s 912A(1)(h) given ASIC has emphasised the importance of these two aspects in their surveillance activities in relation to management of conflicts and risks in recent years.

The FSC agrees with the objective of removing provisions in the Act that are already captured by the 'efficiently, honestly and fairly' obligation. Caution is needed in respect of removing s 912A(1)(aa)) and s 912A(1)(h) given ASIC has emphasised the importance of these two aspects in their surveillance activities in recent years.

The FSC shares the concern identified at paragraph 13.105 of the ALRC Report:

> *"it could be argued that removal of these provisions would introduce some uncertainty for regulated entities…"*

Given this, FSC would support the alternative approach of the proposed removal of these provisions on the understanding that the desired above "ASIC emphasis" would be retained by way of enhanced ASIC regulatory guidance.

Recommendation
The FSC does not recommend separating the words 'efficiently', 'honestly', and 'fairly' into individual paragraphs.

The FSC would support further consideration of replacing the word "efficiently" with a more appropriate word, although we would suggest that "professionally" be considered alongside the word "competently". Also, support has been expressed for inclusion of the word "reasonable".

In principle, the FSC agrees with inserting a note containing examples of conduct that would fail to satisfy the 'fairly' standard, and that there be clarification of how such examples would apply in practice.

The compendious nature of these obligations is uncertain, so retention of this form of drafting perpetuates that uncertainty for the industry. This should be closely considered by the Inquiry.

However, the FSC and its members are wary of the unintended consequences from separating words 'efficiently', 'honestly', and 'fairly' into individual paragraphs. In our view it would be preferable to leave this section unamended as there is already a relevant body of judicial interpretation of the existing text. While the views of judges differ as to whether these three requirements of an AFS licensee are compendious or to be considered separately, in this regard, we prefer the judicial approach taken by Beach J in the 2020 Federal Court case *ASIC v AGM Markets Pty Ltd* (in liq) (No 3) [2020] FCA 208 as follows:

- the key words should be read together and in doing so, incorporate requirements of:
    - competence;
    - exercising sound ethical values/judgement - for the client's affairs;
    - adequate performance
    - produce desired effect
- in this context "fairness" must take into account the interests of both the consumer and the AFS Licensee;
- there is a need to consider if the AFS licensees took all necessary steps in terms of whether there has been a breach of this duty;

Separation of these words could cause the considerable uncertainty and unfortunate judicial and AFCA decisions by potentially providing for such determinations to be made on the basis of conduct not complying with just one of these elements and not to all. It is preferable not to separate these words in the manner suggested, particularly as breach of the section is a civil penalty provision with serious consequences.

The word "fairness" would be problematic given that AFCA has makes determinations on what is fair. We would invite the ALRC to provide further guidance as to what the intended impact of an AFCA determination of unfairness would have on the question of whether a licensee has breached the Act. For example, would conduct deemed unfair by AFCA be taken to be a breach of the "fairness" limb of the Act?

The FSC supports the suggestion that further guidance be provided as to the meaning of the "fairness" limb, and the ALRC proposal to insert a note with examples of what would constitute conduct that does not meet the fairness standard would seem sensible.

Similarly, while it may make some sense to impose separate obligations of honesty and fairness in the conduct of financial services, "efficiency" as a stand-alone requirement would substantially expand the current law, even if it is replaced with "professionally".

As noted above, our members support the view of keeping the three words together and without amendment to retain the benefit of the existing body of judicial interpretation and avoid uncertainty from change. However, there has been some member support for the consideration of change if consistent with the position stated above in paragraph a. above, such as:

- use of the term "reasonable", such as in the context of "necessary steps" to be taken to comply;
- use of the term "competence" rather than "professional" as a narrower term.

In principle, FSC supports the concept of setting out of examples of conduct that would fail to satisfy the 'fairly' standard. However, in practice if legislation usually sets out high level requirements/principles then such examples may be more appropriately incorporated in related Regulatory Guides. If incorporated in the legislation, clarification of how the relevant provision would apply; for example, would this in effect stop any relevant adjudicator (including courts and AFCA) from making a finding that any scenario substantially similar to the "statutory" examples as being "unfair" and making any consequential order based on that finding.