

ROYAL COMMISSION REPORT - FINANCIAL ADVICE BUSINESSES

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Financial Services Alert

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The Final Report from the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry was published early last week. In addressing the findings from hearings into the Financial Advice Industry, Commissioner Kenneth Hayne made several recommendations for the government to consider and implement into law.

EARLIER ROYAL COMMISSION FINDINGS

From the hearings on the Financial Advice Industry in March 2018, two systemic forms of misconduct by financial advisers were identified and then explored in further detail in the Interim Report (published in September 2018). Broadly, these issues related to:

- advisers charging fees to clients for services they did not receive and
- advisers providing inappropriate advice and, despite the introduction of best interests obligations with the FOFA reforms, prioritising their own self-interest over the interests of their clients.

Advisers from each of the Big 4 banks, AMP as well as some smaller advice practices were found to have engaged, in varying degrees, in the misconduct described above.

The Commissioner was also critical of licensees, Financial Advice Industry bodies and ASIC. In particular, the Commissioner stated:

- licensees did not have appropriate policies or procedures in place to detect or ensure prevention of adviser misconduct
- there was limited information sharing between licensees, industry bodies and ASIC meaning that adviser misconduct was often not detected in a timely or efficient manner and
- the industry bodies, FPA and AFA, were ineffective in playing a significant role in maintaining or enforcing proper standards of conduct by financial advisers.

Case studies from the Interim Report described, at length, the extent to which advisers and licensees had ended up failing to act in their clients' best interests.

ROYAL COMMISSION FINAL REPORT Financial advisers

For advisers, the Commissioner has made several recommendations that will, when implemented, impose several additional obligations upon them in providing financial advice to retail clients. Specifically, the following measures were recommended by the Commissioner:

- renewal notices to be issued to retail clients annually (rather than once every 2 years) which would include a consent by the client for the fee to be deducted from their account
- fee disclosure statements must include specific details about the prospective fees that are to be charged to a client in the coming year
- removal of grandfathered commissions and the further capping of life insurance commissions
- requirement of explicit disclosure, by written notice, to a retail client by an adviser if he or she is not 'independent, impartial or unbiased' (as defined in the Corporations Act) and an explanation as to why the adviser is not independent, impartial or unbiased in forming his or her advice and
- compulsory registration with a new disciplinary system for any financial adviser who provides advice to retail clients. Affected clients and other stakeholders would also be permitted to report information about the conduct of the financial advisers to the disciplinary body.

AFSL licensees

For licensees, the key theme in the Commissioner's recommendations is to make them more accountable for the actions and any potential misconduct perpetrated by authorised representatives. This includes the following recommendations:

- licensees would be required to implement more detailed reference checking and information sharing protocols when monitoring their advisers in order to be consistent with the requirements set out in the ABA's "Financial Advice – Recruitment and Termination Reference Checking and Information Sharing Protocol"
- Section 912A of the Corporations Act to be amended to require that licensees take reasonable steps to co-operate with AFCA including making all relevant documents in connection with a dispute available to AFCA. A breach of this section would result in the licensees being stripped of their AFSL licence
- reporting of serious compliance concerns about individuals to ASIC and the new disciplinary body on a quarterly basis and
- upon detecting that an adviser has engaged in misconduct, the licensee would need to conduct a full investigation and where there is sufficient information to suggest misconduct, the licensee must inform and remediate affected clients.

Further initiatives

In addition to the above changes for licensees and advisers, the Commissioner has also recommended broader law reform for the industry which would include government undertaking an investigation to assess the effectiveness of measures implemented to improve the quality of advice within 3 years. In particular, the review would consider:

- whether it is necessary to retain the 'safe harbour' provisions and

- whether the exemption to banning commissions for general insurance products and consumer credit insurance products remains justified.

As a final note, licensees and advisers should be aware that the implications from the Final Report will extend further than the specific recommendations made by the Commissioner. In particular, advisers and licensees should brace for a more active regulator in ASIC with its broadened mandate to investigate and bring enforcement proceedings against any individuals or groups it identifies as not being compliant with the current regulatory regime.

TIMELINE FOR REFORMS

The [timeline](#) as to when each of the proposed reforms becomes actually implemented into law (as well as to what degree) remains an issue that is currently being discussed by government with the opposition having some alternate views. To assist with assessing the timing of the recommendations, we attach a document which sets out the proposals recommended by the Commissioner as well as the possible timelines under a Labour or Liberal government.

[Click here](#) for the timeline.

EXISTING ASIC ENFORCEMENT PROGRAMS

On top of the emerging issues from the Royal Commission are the existing ASIC enforcement initiatives which were commenced or announced during 2018 and which will continue to play out probably with increased vigour during 2019. They include:

- conflicted remuneration and ongoing fees
- quality of life insurance advice
- MDAs and platforms
- vertical integration and conflicts management and
- advice in superannuation.

WHAT NOW?

We are recommending that all advice businesses, whether they be representatives or licensees, begin the process of preparing for a new regulatory environment. At the very least, advice businesses should, as a starting point:

- familiarise themselves with the recommendations
- closely monitor any developments from government and regulators and
- consider how they would implement measures in order to comply with each of the Commissioner's recommendations and the more aggressive enforcement attitude from ASIC.

If you would like to discuss the findings by the Commissioner in the Final Report and its potential impact on your business activities, please contact one of the authors listed below.

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