

Chapter 10

General advice

...it is the context of the advice which is more influential on many consumers than the [general advice] warning.¹

10.1 Financial product advice is divided into two types: personal advice and general advice.² Personal advice is given in circumstances where the provider has, or should have, considered the person's objectives, financial situation and needs.³ Only one aspect of the person's relevant circumstances needs to have been considered for the advice to be personal advice.⁴

10.2 General advice is advice that is not personal advice: it is a recommendation or opinion that does not consider a person's relevant circumstances.⁵ ASIC makes the following distinction:

General advice about a financial product will not be personal advice if you clarify with the client at the outset that you are giving general advice, and you do not, in fact, take into account the client's objectives, financial situation or needs.⁶

10.3 Advice that is likely to be general includes the material provided at investment seminars and in marketing brochures and when advertising a particular financial product or product range.⁷

10.4 In this chapter, the committee looks at general advice in the context of agribusiness MIS. It considers whether the regulatory regime around the marketing of this product to retail investors was sufficiently robust to protect such investors. The committee also examines the role and responsibilities of research houses and the independent experts who rated MIS.

1 Financial Planning Association, *Submission 161*, p. 3.

2 *Corporations Act 2001*, s 766B(2).

3 *Corporations Act 2001*, ss 766B(3).

4 ASIC, Regulatory Guide 175, *Licensing: Financial product advisers—conduct and disclosure*, October 2013, paragraph RG 175.45.

5 *Corporations Act 2001*, ss 766B(4).

6 ASIC, Regulatory Guide 244, *Giving information, general advice and scaled advice*, December 2012, paragraph RG 244.43.

7 ASIC, Regulatory Guide 175, *Licensing: Financial product advisers—conduct and disclosure*, October 2013, p. 98.

Regulations regarding the provision of general advice

10.5 Providers are required to warn clients that general advice does not take into account a person's objectives, financial situation or needs: this warning is known as the 'general advice warning'.⁸ For example, a PDS is general advice and should contain an explicit statement that it 'does not take into account the investment objectives, financial situation, or the particular needs of any potential investor'. In this regard, ASIC provides the following guidance:

When you are giving general advice to a client, in addition to giving a general advice warning, it is good practice to take reasonable steps to ensure that the client understands upfront that they are getting general advice and not personal advice. You should take reasonable steps to ensure that the client understands that you have not taken into account their objectives, financial situation or needs in giving the general advice. This will avoid confusion and help the client to understand the nature of the advice they are getting.⁹

10.6 ASIC informed the committee, however, that despite the obligation to give a general advice warning;

...there are still instances when clients do not properly understand the nature of the advice they are receiving. Slickly presented seminars with high pressure selling tactics are an example of this.¹⁰

10.7 Recent inquiries—notably the legislation committee's inquiry into the Corporations Amendment (Streamlining of Future Financial Advice) Bill 2014 and the FSI—have considered the distinction between general advice and personal advice and the extent to which consumers understand the difference. A particular question raised during the inquiries was whether the term 'general advice' conveys adequately the nature of, and obligations associated with, the provision of general advice.

10.8 The committee's inquiry into the Corporations Amendment (Streamlining of Future Financial Advice) Bill 2014 received submissions and testimony expressing concern that consumers were often not cognisant of the nature of general advice.¹¹ For example, Mr Mark Rantall, CEO of the FPA, noted that many consumers do not appreciate that general advice does not consider a person's relevant circumstances:

8 *Corporations Act 2001*, s 949A.

9 ASIC, Regulatory Guide 244, *Giving information, general advice and scaled advice*, December 2012, RG 244.44, <http://download.asic.gov.au/media/1247129/rg-244.pdf> (accessed 20 August 2015).

10 ASIC, answer to questions on notice, No. 6, p. 16, 2 October 2015.

11 Senate Economics Legislation Committee, *Corporations Amendment (Streamlining of Future of Financial Advice Bill 2014 [Provisions]*, June 2014.

As long as the differences between general advice and personal advice are insufficiently clear to consumers, general advice will be perceived as a less costly form of personal advice.¹²

10.9 Mr Alan Kirkland, CEO of CHOICE, took the view that it was unrealistic to expect all consumers to understand the differences in the regulation of general advice and personal advice:

We depend on consumers to work out, 'That's general advice, so there is a lower bar and I should be much more cautious'...It is just not realistic to expect the consumer to understand that distinction between personal and general advice.¹³

10.10 Noting the concerns about the possible misuse or misunderstanding of the term general advice, the committee recommended in June 2014 that:

...the government give consideration to the terminology used in the Explanatory Memorandum and legislation (for example, section 766B), such as information, general advice and personal advice, with a view to making the distinction between them much sharper and more applicable in a practical sense when it comes to allowing exemptions from conflicted remuneration.¹⁴

10.11 In its interim report, released in July 2014, the FSI noted the committee's recommendation about making the distinction between general advice and personal advice clearer to consumers. It stated further:

One issue with general advice is whether it is properly labelled. Some submissions argue that some of the conduct regulated as general advice could more accurately be described as sales information, advertising or guidance. The aim of this relabelling would be to give consumers a clearer indication of what is involved.¹⁵

10.12 The FSI report called for submissions on the proposal to rename general advice as 'sales' or 'product information', and to mandate that the term 'advice' could only be used in relation to personal advice.¹⁶

10.13 In the second round of submissions to the FSI, most stakeholders agreed that the term general advice was often confusing to consumers but there was no consensus on the term that should be used instead of general advice. The Australian Bankers'

12 *Committee Hansard*, 22 May 2014, p. 19.

13 *Committee Hansard*, 22 May 2014, p. 17.

14 Senate Economics Legislation Committee, *Corporations Amendment (Streamlining of Future of Financial Advice Bill 2014 [Provisions]*, June 2014, p. 77.

15 Australian Government, Financial System Inquiry, *Interim Report*, July 2014, p. 3-73.

16 Australian Government, Financial System Inquiry, *Interim Report*, July 2014, p. 3-74.

Association stated that the industry 'acknowledges that general advice is not widely understood to be financial advice by consumers'.¹⁷

10.14 The FPA, which has consistently argued that the regulation of general advice was insufficient, suggested that the term 'general advice' should be replaced with 'product sales', 'general information', 'financial product information' or another term which clarifies the distinction between product sales and financial advice. In its second-round submission to the FSI, the FPA wrote:

Framing general advice as financial advice plays into the behavioural aspects of financial decision-making by giving the impression that the advice has a reasonable basis or is appropriate for the client, and thereby exposes retail investors to decisions made under uncertainty about the regulatory framework for that advice.

As with many other problems in the Australian financial system, our reliance on a disclosure-based regulatory approach has contributed to this confusion. While a general advice warning is required to be issued when providing general advice, it is the context of the advice which is more influential on many consumers than the warning.¹⁸

10.15 In the FPA's view, financial products, particularly complex financial products such as interests in MIS, should 'not be promoted or sold in circumstances where retail clients may reasonably believe that they are being offered advice that takes into account their personal circumstances'. The FPA also suggested that 'financial products should not be promoted or sold in circumstances where the consumer protection framework that applies to the individual is ambiguous'.¹⁹ In its final report, released in November 2014, the FSI noted:

...consumers may misinterpret or excessively rely on guidance, advertising, and promotional and sales material when it is described as 'general advice'. The use of the word 'advice' may cause consumers to believe the information is tailored to their needs. Behavioural economics literature and ASIC's financial literacy and consumer research suggests that terminology affects consumer understanding and perceptions.²⁰

10.16 While recommending that general advice be renamed, the FSI's final report did not suggest a particular term to replace general advice: instead, it recommended a more appropriate term be chosen through consumer testing.²¹ It considered that the

17 Australian Bankers' Association, *Response to Interim Report*, Submission to the Financial System Inquiry, August 2014, pp. 55 and 58, http://fsi.gov.au/files/2014/08/Australian_Bankers_Association_2.pdf (accessed 10 July 2015).

18 *Submission 161*, p. 3.

19 *Submission 161*, p. 3.

20 Australian Government, Financial System Inquiry, *Final Report*, November 2014, p. 271.

21 Australian Government, Financial System Inquiry, *Final Report*, November 2014, Recommendation 40, pp. 271–272.

benefits to consumers from the clearer distinction between general advice and personal advice would outweigh the costs of consumer testing and the costs of updating existing disclosure documents.

10.17 In its response to the FSI report, the government agreed to rename 'general advice' to improve consumer understanding. It noted that it would consult with a wide range of stakeholders and conduct consumer testing before finalising the new term.²²

10.18 The committee welcomes the government's undertaking to replace the term 'general advice' with one that clarifies the distinction between product sales and financial advice. It is not convinced, however, that renaming the term in and of itself provides adequate consumer protection particularly in circumstances where the product producer uses seminars and dinners to promote the product. The committee heard numerous accounts of growers, who attended seminars or promotional dinners, being encouraged to sign up to invest in agribusiness MIS.²³ It has highlighted the role that these investment seminars had in influencing investors and is particularly concerned about the way in which scheme promoters used high pressure or hard selling techniques during so called public 'information' or 'educational' sessions. This advice would be classified as general advice. Industry Super Australia drew attention to the risk stemming from the use of general advice to push complex products such as forestry MIS.²⁴

10.19 The committee takes this opportunity to cite similar concerns about general advice given during investment seminars or 'wealth creation' sessions by property spruikers detailed in the committee's report on land banking.²⁵

10.20 In this highly charged environment around information or promotional events, there should be clear obligations on the promoters engaging in this type of marketing to ensure that potential investors are fully aware of the risks carried by the product they are promoting. Investors must have access to full and accurate information about the product and be discouraged from signing up before they have the opportunity to seek independent financial advice—that is receiving personal advice. In this respect, however, the committee heard of occasions where the financial adviser was very much part of the promotional team.²⁶

22 Australian Government, *Improving Australia's financial system, Government response to the Financial System*, p. 22, http://treasury.gov.au/~media/Treasury/Publications%20and%20Media/Publications/2015/Government%20response%20to%20the%20Financial%20System%20Inquiry/Downloads/PDF/Government_response_to_FSI_2015.ashx (accessed 26 October 2015).

23 See paragraphs 5.65, 5.72, 5.76 and 9.65–9.70.

24 *Submission 136*, p. 3.

25 Senate Economics References Committee, *Scrutiny of Financial Advice, Part 1—land banking: a ticking time bomb*, February 2016, paragraphs 3.53–3.55 and 8.80–8.90.

26 See paragraph 9.65, which noted Mr Steve Navra's participation at seminars promoting an agribusiness MIS.

Recommendation 9

10.21 The committee recommends that the government consider not only renaming general advice but strengthening the consumer protection safeguards around investment or product sales information presented during promotional events.

Recommendation 10

10.22 The committee recommends that ASIC strengthen the language used in its regulatory guides dealing with general advice. This would include changing 'should' to 'must' in the following example:

You must take reasonable steps to ensure that the client understands that you have not taken into account their objectives, financial situation or needs in giving the general advice.

Referral networks

10.23 According to the FPA, referral networks played a significant role in the massive consumer losses from Timbercorp, Great Southern, and other widely marketed schemes. It noted that referral advice was not regulated by the Corporations Act even where major financial decisions were at stake because this advice did 'not of itself constitute a financial product recommendation'. It was concerned with the role of business models that rely on referral networks providing adequate consumer protection.²⁷

10.24 In addition to recommending replacing the general advice definition with a term that would not pose the risk of misleading retail clients about the service they are being provided, the FPA recognised the need to:

- investigate the role that referral networks played in the distribution of failed forestry and agribusiness managed investment schemes; and
- examine whether consumers are adequately protected from referral strategies intended to transition between legal and regulatory frameworks of varying levels of consumer protection.²⁸

Recommendation 11

10.25 In light of the concerns about the lack of understanding about the role that referral networks had in selling agribusiness MIS without appropriate consumer protections, the committee recommends that the government's consideration of 'general advice' also look closely at the role of referral networks and determine whether stronger regulations are required.

27 *Submission 161*, p. 3.

28 *Submission 161*, p. 3.

Gatekeepers—research houses

10.26 The FPA maintained that other gatekeepers, such as research houses, had also failed their obligations to retail investors.²⁹ It observed that in the case of forestry MIS collapses and the resultant massive consumer losses, the shortcomings of gatekeepers within research houses, AFS licensees, responsible managers, and product issuers have been understated.³⁰ In this regard, the FPA raised an important matter that warrants close consideration—the role of research houses in promoting the agribusiness MIS.

Role and function of experts' reports

10.27 Research or experts' reports provide another important source of information for financial advisers and investors in agribusiness MIS and were often a major selling point for agribusiness MIS. For example, Dr Judith Ajani explained that typically PDSs for plantation MIS do not include 'any direct statement or information about forecast project returns'. Instead, she noted, that relevant information was presented in 'an independent (forestry consultant) expert's report included in the PDS, but limited to forecast wood yields and prices'.³¹ The committee has considered, and commented on, the unreliable yield projections contained in prospectuses and PDSs in agribusiness MIS.³²

10.28 An RE would normally engage external experts to provide potential investors with independent opinion on what they 'consider to be reasonable agricultural performance parameters' for the scheme. For example, in 2008, Great Southern explained that the soundness of an MIS project structure was 'further ensured by independent research houses'. It then described the work of those research houses:

Assessment of the project viability by these credit rating agencies is extremely thorough and all assumptions used in the MIS operator's financial model under scrutiny, including past performance, management skills and an assessment of the MIS company's corporate governance. A range of sensitivities is provided whereas the potential investor is being made aware of the assumptions the project is most sensitive to (i.e. commodity price or yield or both)...Project weaknesses and benefits are highlighted as applicable throughout the report culminating to what the research house

29 *Submission 161*, p. 5.

30 *Submission 161*, p. 4.

31 Judith Ajani, 'Climate change policy distortions in the wood and food market', Contributed paper to the Australian Agricultural and Resource Economics Society National Conference 2010, Adelaide Convention Centre, 8–2 February 2010 in Dr Judith Ajani, *Submission 26*, p. 13.

32 See paragraphs 9.26–9.35.

considers to be a reasonable rate of return for the project and a project rating is finally issued.³³

10.29 These independent reports were a critical component of the marketing strategy. Mr Bryant noted that insurers would not have given any adviser indemnity insurance unless they had something like the research report to back up their decision to recommend it to their clients.³⁴ Mr Peterson, general manager of distribution at Timbercorp from September 2004 to December 2009, explained further:

...if you were a dealer group, whether you were owned by ANZ, NAB, CBA or Westpac, or whatever dealer you belonged to, for the research committees to put your product on the APL, the approved product list, they needed a research report from AAG, Adviser Edge or Lonsec. Without those reports, they would not put the Timbercorp, Great Southern or Macquarie Forestry projects on their approved product list.³⁵

10.30 Representatives from FPA highlighted the importance of having robust research sit behind any analysis of products. Mr Rantall told the committee that he had sat on approved product committees for 30 years and noted the reliance placed on research that 'comes across your desk'.³⁶ Thus, research reports perform a valuable 'gatekeeping' function in the financial advice industry for both financial advisers and retail investors by:

- identifying products to consider for inclusion on approved product lists;
- assisting financial advisers to formulate financial advice for retail investors; and
- providing research for use directly by retail investors in making investment decisions.³⁷

10.31 It is also important to note that the ATO advised the committee that part of the process of issuing a product ruling involves the applicant providing an independent expert's opinion on the scheme that go to matters such as management decision on the location, species and number of trees. The ATO relies on these opinions when it is

33 Great Southern Limited, submission to the Review of Non-Forestry Managed Investment Schemes, September 2008, p. 11, http://archive.treasury.gov.au/documents/1423/PDF/Great_Southern_Limited.PDF (accessed 7 September 2015).

34 *Proof Committee Hansard*, 12 November 2014, p. 23.

35 *Proof Committee Hansard*, 12 November 2014, p. 24.

36 *Proof Committee Hansard*, 6 August 2015, p. 28.

37 ASIC, Regulatory Guide 79, *Research report providers: Improving the quality of investment research*, December 2012, paragraph RG 79.2 and a joint report by the Treasury and the Australian Securities and Investments Commission, *Review of credit rating agencies and research houses*, October 2008, paragraph 94, <http://download.asic.gov.au/media/1343114/rep143.pdf> (accessed 1 September 2015).

considering whether the investors 'are carrying on a business for determining the deductibility of expenditure'.³⁸

Opinions for hire

10.32 Although often cited as independent research, product issuers commission such work as a way to promote their products. This user pays business model, whereby the product issuer directly reimburses the researchers, has the potential to undermine the independence of their findings. There may well be a conflict of interest—an incentive for researchers to downplay the negative aspects of the scheme they are reviewing and provide positive ratings.

10.33 In the context of a research report provider rating a scheme, ASIC explained further the nature of the potential conflict of interest:

...the conflict arises as a result of the RE generally paying for the rating and providing the research report provider with information about the product, including, but not limited to yield information. The research report provider should manage any conflict that may arise as a result of these arrangements. If they fail to do so, ASIC may take action to sanction them, such as administrative action.³⁹

10.34 In its 2009 report, the PJC referred to the practice of product producers obtaining opinions for hire. It recognised that independent experts had a critical role in promoting an agribusiness scheme but that questions had been asked about the independence and quality of their advice.⁴⁰ The same concerns were again raised during this current inquiry.

10.35 The committee has noted that the projected yield rates for some agribusiness MIS were overly ambitious, and that this fact became increasingly apparent as earlier plantations were harvested. The committee has also noted that some schemes were located in unsuitable areas—poor soil or removed from vital infrastructure—or involved the wrong species being planted. Yet, expert reports did not reflect such concerns. In this regard, ASIC informed the committee that in the past it found:

...investment products that failed (including agribusiness schemes) were either highly rated or the subject of very recent positive recommendations by research houses just before the product failure.⁴¹

10.36 ANZ referred to ratings given to Timbercorp:

38 ATO, answer to questions on notice, No. 4, received 8 October 2015; Mr Tim Dyce, *Proof Committee Hansard*, 14 October 2015, p. 11.

39 ASIC, answer to questions on notice, No. 3, 2 October 2015, p. 28.

40 Parliamentary Joint Committee on Corporations and Financial Services, *Inquiry into aspects of agribusiness managed investment schemes*, September 2009, p. 58.

41 *Submission 34*, paragraph 151.

In the two years leading up to Timbercorp's collapse in 2009, external research houses with experience in forestry and non-forestry managed investment schemes rated Timbercorp investments as 'Investment Grade' or above.⁴²

10.37 A number of witnesses were particularly concerned about the apparent lack of independence of experts commissioned to report on MIS. Ms Jan Davis, former CEO of the Tasmanian Farmers and Graziers Association, informed the committee that the prospectuses were 'always written by people who had a vested interest' and paid by the proponents of the scheme.⁴³ Mr Cornish similarly thought there was a problem with so-called 'independent advisers', such as Adviser Edge and AAG, that were giving non-commercial schemes four out of five stars and whose ratings were included in prospectuses. He cited a magazine that went out to financial planners at the time, including their list of 4½ and five stars. He cited one in particular that AAG rated 4½ out of five stars, despite the scheme having 'some really interesting corporate governance issues'. He stated further that they were producing investment support advice that was clearly flawed and further 'these organisations were paid—even though they called themselves 'independent'—by the promoters to provide this information'.⁴⁴ In summary, Mr Cornish argued:

...where you have the so-called keepers of the keys or the people who base the ratings, saying, 'This is an investment that you would invest in', being paid by the promoter, you have, simply, a breakdown in proper due diligence being carried out.⁴⁵

10.38 Mr Tom Ellison was also critical of the research reports. He noted that some of the AFSL had in-house research houses but others relied on external reports. For example, he informed the committee that most of the advisers in Tasmania relied on research reports from Aspect Huntley, whom he thought had given a 4½ star rating to an FEA product. He was of the view that a Perth based company was commissioned to undertake research and was pushing Great Southern, Gunns and FEA and rating them all five stars.⁴⁶ Mr Ellison indicated that some of the independent research he had seen was 'basically cut and pasted from the promoters' promotional material'.⁴⁷

10.39 Mr John Lawrence attributed the damaged caused by failed MIS to, first and foremost, the promoters who organised the schemes but also the professionals who

42 *Submission 145*, paragraph 66.

43 *Proof Committee Hansard*, 5 August 2015, p. 24.

44 *Proof Committee Hansard*, 4 August 2015, p. 12.

45 *Proof Committee Hansard*, 4 August 2015, p. 12.

46 *Proof Committee Hansard*, 4 August 2015, p. 22.

47 *Proof Committee Hansard*, 4 August 2015, p. 23.

signed off on opinions that formed part of the PDS.⁴⁸ Similarly concerned about the reliability of experts' reports, Mr Samuel Paton argued:

...the Timbercorps and Great Southern etc and the so-called agribusiness investment houses, who were paid to promote their schemes, were never subject to any independent government audit as to the veracity of the claims that were being made in their promotional literature and their ASIC and ATO sanctioned PDSs.⁴⁹

10.40 Mr Bryant, who was employed by Timbercorp to deal with the research houses to obtain the necessary reports, suggested that the research houses provided advisers with a 'Teflon raincoat'.⁵⁰ He explained that the process for engaging a research house would normally involve a fee of around \$35,000 per report. Basically, according to Mr Bryant, Timbercorp furnished the research houses with all the information that they requested and the houses, while relying on forestry or horticultural information, did not undertake independent analysis.⁵¹ Mr Bryant also indicated that it was common practice for a company to avoid engaging a research house that may not provide the required rating. He referred to some companies not approaching Lonsec for certain projects because 'they knew that Lonsec would not give them the rating they wanted'.⁵² He gave the example, where:

...there were certain projects Great Southern did not get Lonsec to do, like their trees, because they knew that Lonsec would not give them an investment-grade rating.⁵³

10.41 He noted further that 'other research houses like Mercer and Morningstar refused to rate these sorts of projects'. Mr Bryant observed:

You have to remember that the research houses, whilst they did not check the pH or get an agronomist's report and those sorts of things, they did write the reports based on information provided by the promoter—in the case of Timbercorp products, Timbercorp. They did get out of their offices and go and kick the dirt and have a look, and they did have some very fine young minds working with them who had masters in agri et cetera and understood a little bit about what they were looking at. That can be a defence for them and it can be a negative for them as well.⁵⁴

10.42 Mr Jeff Morris was also critical of the research houses that played their part in the marketing of agribusiness MIS by 'providing defective product ratings, on which

48 *Proof Committee Hansard*, 5 August 2015, p. 5.

49 *Submission 149*, p. 3.

50 *Proof Committee Hansard*, 12 November 2014, p. 22.

51 *Proof Committee Hansard*, 12 November 2014, p. 23.

52 *Proof Committee Hansard*, 12 November 2014, p. 24.

53 *Proof Committee Hansard*, 12 November 2014, p. 24.

54 *Proof Committee Hansard*, 12 November 2014, p. 24.

these professional advisers sought to rely and used to help sell these products'.⁵⁵ The FPA maintained that, as important gatekeepers, research houses had neglected their responsibilities.⁵⁶

Obligations

10.43 The FPA suggested that research houses should be included in a review of the obligations of the main gatekeepers in the creation, operation, marketing, and distribution of forestry and agribusiness managed investment schemes.⁵⁷ It argued that 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.⁵⁸

10.44 In 2012, ASIC issued a regulatory guide with the intention of creating 'an environment where the research produced by analysts for clients is objective, clear, fair and not misleading'.⁵⁹ This objective is consistent with international regulators as set out in the IOSCO's *Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest*.⁶⁰

10.45 Two of the core measures in this statement of principles have particular relevance to this inquiry into agribusiness MIS. They are designed to hold analysts to high standards of integrity by:

- imposing general legal obligations on analysts and/or the firms that employ analysts to act honestly and fairly with clients; and
- prohibiting analysts and/or the firms that employ analysts from acting in ways that are misleading or deceptive.⁶¹

10.46 The IOSCO also suggested the following additional measures for its members to consider:

55 *Proof Committee Hansard*, 12 November 2014, p. 42.

56 *Submission 161*, p. 5.

57 *Submission 161*, p. 5.

58 *Submission 161*, p. 4.

59 ASIC, Regulatory Guide 79, *Research report providers: Improving the quality of investment research*, December 2012, paragraph RG 79.44, <http://download.asic.gov.au/media/1239863/rg79-published-10-december-2012.pdf> (accessed 7 September 2015).

60 The International Organization of Securities Commissions' (IOSCO) *Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest*, <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD150.pdf> (7 September 2015).

61 The International Organization of Securities Commissions' (IOSCO) *Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest*, p. 10, <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD150.pdf> (7 September 2015).

- imposing 'fit and proper' requirements or otherwise prohibiting individuals with criminal records or demonstrably compromised integrity from being employed, indefinitely or for a period of time, as analysts;
- requiring analysts to take periodic examinations designed to test analysts' knowledge of their legal and ethical duties;
- making the disciplinary records of analysts public;
- requiring analysts to disclose their professional credentials in research reports distributed to investors;
- requiring analysts to define the terms they use when making recommendations; and
- requiring analysts to include in their reports a discussion of the assumptions underlying their recommendations and a sensitivity analysis to help investors understand how changes to these assumptions may affect the analysts' conclusions.⁶²

10.47 While ASIC's Regulatory Guide RG 79 on research report providers is helpful in providing a useful guide on measures that research providers and product issuers commissioning reports should employ, the language is tame. For example, in respect of due diligence ASIC writes:

We expect AFS licensees (including advice providers) to conduct appropriate due diligence in choosing a research report provider...⁶³

10.48 Moreover, ASIC informed the committee of the incentives and sanctions that exist for research houses and experts to make sure that their ratings are objective and well-founded:

...the incentive for research providers is compliance with their general licensing obligations and general conduct obligations such as the prohibitions against misleading or deceptive conduct.⁶⁴

10.49 ASIC also noted that it had not reviewed the conduct of research houses since the last revision of RG 79 in December 2012.⁶⁵

62 The International Organization of Securities Commissions' (IOSCO) *Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest*, p. 10, <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD150.pdf> (7 September 2015).

63 ASIC, Regulatory Guide 79, *Research report providers: Improving the quality of investment research*, December 2012, paragraph RG 79.176, <http://download.asic.gov.au/media/1239863/rg79-published-10-december-2012.pdf> (accessed 1 September 2015).

64 ASIC, answer to questions on notice, No. 3, 2 October 2015, p. 31. ASIC provided a comprehensive answer to this matter of research houses and expert advice.

65 ASIC, answer to questions on notice, No. 3, 2 October 2015, p. 32.

Conclusion

10.50 The committee acknowledges that there are numerous participants who offer products or services within the financial advice value chain that influence, directly or indirectly, consumers' decisions on financial matters. It particularly notes that research houses and subject matter experts produce reports containing important information for financial advisers and investors in agribusiness MIS. Under the user pays model, the experts' opinions may be biased by the remuneration offered and the promise of further business. In the committee's view, research houses and experts providing opinions should be held to high standards of honesty and integrity. In this regard, the committee notes the relevant IOSCO statement of principles governing integrity and ethical behaviour and is of the view that they should apply and have force in Australia.

10.51 The committee is concerned that the message about compliance and adhering to high ethical standards is not reaching all participants in the industry.

Recommendation 12

10.52 In respect of research houses and subject matter experts providing information or reports to the market on financial products such as agribusiness MIS, the committee recommends that the government implement measures to ensure that IOSCO's statement of principles governing integrity and ethical behaviour apply and have force. In particular, the committee recommends that the government consider imposing stronger legal obligations on analysts and/or firms that employ analysts to rate their products, to act honestly and fairly when preparing and issuing reports and applying ratings to financial products.