

Chapter 1

Introduction

Terms of reference

1.1 On 25 February 2009 the Parliamentary Joint Committee on Corporations and Financial Services resolved to inquire into and report by 23 November 2009 on the issues associated with recent financial product and services provider collapses, such as Storm Financial, Opes Prime and other similar collapses, with particular reference to:

1. the role of financial advisers;
2. the general regulatory environment for these products and services;
3. the role played by commission arrangements relating to product sales and advice, including the potential for conflicts of interest, the need for appropriate disclosure, and remuneration models for financial advisers;
4. the role played by marketing and advertising campaigns;
5. the adequacy of licensing arrangements for those who sold the products and services;
6. the appropriateness of information and advice provided to consumers considering investing in those products and services, and how the interests of consumers can best be served;
7. consumer education and understanding of these financial products and services;
8. the adequacy of professional indemnity insurance arrangements for those who sold the products and services, and the impact on consumers; and
9. the need for any legislative or regulatory change.

1.2 On 16 March 2009 the Senate agreed that the following additional matter be referred to the Parliamentary Joint Committee on Corporations and Financial Services as part of that committee's inquiry into financial products and services in Australia, adopted by the committee on 25 February 2009 for inquiry and report by 23 November 2009:

The committee will investigate the involvement of the banking and finance industry in providing finance for investors in and through Storm Financial, Opes Prime and other similar businesses, and the practices of banks and other financial institutions in relation to margin lending associated with those businesses.

Definitions of key inquiry terms

Financial product

1.3 Section 763A of the *Corporations Act 2001* sets out the general definition of a financial product as follows:

(1)... a **financial product** is a facility through which, or through the acquisition of which, a person does one or more of the following:

- (a) makes a financial investment ...;
- (b) manages financial risk ...;
- (c) makes non-cash payments ...

(2) ... a particular facility that is of a kind through which people commonly make financial investments, manage financial risks or make non-cash payments is a **financial product** even if that facility is acquired by a particular person for some other purpose.

(3) A facility does not cease to be a financial product merely because:

- (a) the facility has been acquired by a person other than the person to whom it was originally issued; and
- (b) that person, in acquiring the product, was not making a financial investment or managing a financial risk.¹

Financial service

1.4 Section 766A of the *Corporations Act 2001* identifies a financial service as follows:

(1)... a person provides a **financial service** if they:

- (a) provide financial product advice...; or
- (b) deal in a financial product...; or
- (c) make a market for a financial product ...; or
- (d) operate a registered scheme; or
- (e) provide a custodial or depository service...; or
- (f) engage in conduct of a kind prescribed by regulations made for the purposes of this paragraph.²

1 The full text of the *Corporations Act 2001* is available at <http://www.comlaw.gov.au/comlaw/management.nsf/lookupindexpagesbyid/IP200401854?OpenDocument> (accessed on 17 September 2009).

2 The full text of the *Corporations Act 2001* is available at <http://www.comlaw.gov.au/comlaw/management.nsf/lookupindexpagesbyid/IP200401854?OpenDocument> (accessed on 17 September 2009).

Conduct of the inquiry

1.5 The inquiry was advertised in *The Australian* newspaper, *The Australian Financial Review* newspaper and through the internet. The committee invited submissions from a wide range of interested organisations, government departments and authorities, and individuals. The closing date for submissions was 31 July 2009, and the committee agreed to table its report on 23 November 2009. The Senate also set 23 November 2009 as the reporting date for the additional term of reference that was added to the committee's initial terms of reference, although the committee subsequently sought an extension of the Senate reporting date until 24 November in order to fit in with standard parliamentary administrative processes.

1.6 In conducting its inquiry, the committee made a decision to focus specifically on non-superannuation products and services.

1.7 The committee received 398 formal submissions and 37 supplementary submissions, as well as associated correspondence and supporting material. A list of individuals and organisations that made public submissions to the inquiry is at Appendix 1.

1.8 The committee held nine public hearings, in Canberra (four hearings), Melbourne, Cairns, Townsville, Brisbane and Sydney. A list of witnesses who gave evidence at the public hearings is at Appendix 2.

1.9 Some witnesses took questions on notice at public hearings. Answers received are published in Appendix 3.

1.10 A list of material tabled during the inquiry or provided to the committee as additional information is published at Appendix 4.

Acknowledgement and thanks to contributors

1.11 The committee thanks those organisations and individuals that made written submissions and gave evidence at the public hearings. In particular, the committee recognises the trauma experienced by many investors in Storm Financial, Opes Prime and similar collapsed providers and is grateful to investors who were prepared to share their experiences with the committee.

1.12 Across the program of public hearings, the committee's aim was to hear from a balanced selection of investors, advisers, product providers, finance providers, representative groups and individuals. Nevertheless, the committee acknowledges that there were many people who wanted to give evidence at hearings but who did not get the opportunity to do so. The committee thanks all of these people for their willingness to assist the committee in its work.

Note on references

1.13 References to submissions in this report are to individual submissions received by the committee and published on the internet.³ References to the committee Hansard are to the official Hansard transcript of the public hearings, with the exception of the 28 October hearing, for which only a proof transcript was available at the time of writing.⁴ Please note that page numbers may vary between the proof and the official Hansard transcripts.

Report structure

1.14 Chapter 2 summarises the current regulatory regime for financial services and products in Australia, particularly the provisions of Chapter 7 of the *Corporations Act 2001*, and the role of the regulator, the Australian Securities and Investments Commission (ASIC). This chapter also provides a current snapshot of Australia's financial advice sector.

1.15 Chapter 3 addresses the events surrounding the collapse of Storm Financial, the consequences of that collapse, and the evidence provided to the committee about what caused the collapse and why it has been so devastating for so many investors.

1.16 Chapter 4 presents the evidence the committee received regarding the collapse of Opes Prime, including the effect on investors, the evidence received by the committee about what caused the collapse, and the scheme of arrangement accepted by creditors to recover a portion of their money.

1.17 Chapter 5 highlights problems or issues in the provision of financial products and services that were drawn to the committee's attention during the course of its inquiry. Matters discussed include the sales-advice conflict; whether it is poor advice or poor products that lead to poor investment outcomes; the adequacy (or otherwise) of the current regulation of financial advice provision, including the conduct and disclosure-based approach to managing conflicts of interest; the Australian Financial Services licensing regime; professional indemnity (PI) insurance arrangements; and financial literacy levels. The suggestion that the current regulatory regime is appropriate but is not effectively enforced is also discussed in this chapter.

1.18 Chapter 6 sets out a range of solutions or reforms that were proposed to the committee during the course of the inquiry. Suggestions for change in the sector that are canvassed in this chapter include raising standards of advice; making disclosure more effective; removing conflicted remuneration practices; ensuring better

3 Submissions to the inquiry are available at the following link:
http://www.aph.gov.au/senate/committee/corporations_ctte/fps/submissions/sublist.htm
(accessed on 17 September 2009).

4 Transcripts of the committee's public hearings can be accessed at the following link:
http://www.aph.gov.au/senate/committee/corporations_ctte/fps/hearings/index.htm (accessed on 17 September 2009).

transparency, competency and accountability through the financial services licensing system; reforming lending practices; limiting access to complex and/or risky investment products; and introducing a last resort statutory compensation scheme. The committee makes eleven recommendations in this chapter.

1.19 Chapter 7 summarises the committee's views and reiterates the committee's recommendations for change arising out of this inquiry.

Privilege issue

1.20 During the course of the inquiry, a matter of parliamentary privilege arose. A person who had made a submission to the inquiry drew the committee's attention to a letter in which they were threatened with a penalty as a direct result of making that submission.

1.21 The committee considered this to be a serious incident and took immediate action to resolve the matter, as detailed in Appendix 5.

