31th July 2009

Committee Secretary, Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
PO Box 6100 Parliament House
Canberra ACT 2600

Dear Sirs

Submission

You have sought public submissions in relation to the 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.

As an adviser who is authorised to provide advice under the present regulatory regime I would offer my comments and suggestions below for your consideration.

My Perspective and History

I have formed my views from a history of 16 years experience in operative, compliance and middle management positions within the taxation regulator, followed by some 10 years as a dedicated financial adviser providing personal advice to retail clients. Over my 10 years as an adviser I would have assisted more than 2,000 individuals, couples, families and small businesses.

I hold a Bachelor of Business with Majors in Accouting and in Finance, a Graduate Diploma in Financial Planning and professional qualifications as a Certified Practicing Accountant (Financal Planning Specialist), CPA Public Pracice certificate holder and also Certified Financial Planner membership of the Financial Planning Association of Australia. I am also a member of the Taxation Institute of Australia.

I have held a Proper Authority and then Authorised Representative status under a large dealer group (Count) for 5 years, then applied and was granted my own AFSL operating as an individual licensee. I have had occasion to since make application for two other financial services licenses: one after a short period of operating under a letter of no-action from ASIC due to their inadvertant administrative cancellation of my initial license, and secondly the license I have obtained for my present employer, and tax accounting and business advisory practice.

I invested four years of my life attempting, ulitmately unsuccessfully, to develop a truly "independent" advice practice. Although that folly is probably outside the scope of your inquiry, I would note that experience has only strengthened my resolve to deliver quality advice to Australians who have the potential to benefit so greatly from reliable, professional, appropriate, financial guidance.

I believe in concision, and will add but a few comments under the headings of each term of reference. I also believe in never raising a question without having thought through at least one potential solution, and have concluded my submission accordingly. But first to the terms of reference…

the role of financial advisers

Clearly the role of advisers is to assist their clients to make better decisions. An adviser must accordingly appreciate the circumstances of the client (including their goals) and understand the likely consequences of their recommendations to clients. This is presently acronised to KYC (know your client) and KYP (know your product).

Where conflicts of interest arise, the professional adviser would put the client's interests above their own - as the accounting, legal and other professions require their members to do. The issue of conflicts is a professional one, requiring professional vigilance rather than regulatory prescription.

In the suject financial product and services provider collapses, the actions of advisers clearly influenced investor decisions and ultimate outcomes. Firstly in recommendations of strategy, and secondly in recommendations of product.

I would suggest that had there been no failure of products, the issue of advice might not have been so closely scrutinised. However the situation exists and it appears responsibility for losses lies across three aspects: the adviser (for their

advice), the product provider (for their product failure)and the investor (for their ultimate decision to invest).

Each investor might have declined to invest, but should have proceeded knowing that they became responisble for their decision and consequences (both upside and downside). They must share some of the blame.

Each adviser, as an industry participant, would have known their responsibility to meet the KYC and KYP requirements for their advice. If the advice was inappropriate, then they should be held responsible for the advice, to the extent of their advice (but not perhaps to the extent of any product failure). The extent of adviser responsibility *for their advice* would be a question of fact and degree, and that is a matter for the courts.

Responsibility for product failure would fall to the product provider. If all prudent measures were taken, in accordance with the stated intention of the product provider, then the consequences are the consequences. If the product provider failed in their duty of care, then responsibility for such failure lies with them.

the general regulatory environment for these products and services

I believe the present laws that blend the responsibility for products and with the responsibility for advice contribute significantly to the complexity of the regulatory regime. This environment is further clouded by permitting the conflict of interest apparent when a fiancial product provider also owns an adviser and constrains their otherwise professional, independent advice.

A clear separation of the capacity to issue financial products from the ability to provide personal advice would go some way toward making the industry less prone to inappropriate activities which have resulted in so much financial harm to investors. I recognise that the present industry position does not enforce such a distinction.

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

My preliminary note here is that anyone can call themselves a "financial adviser". Legislation limiting the use of that term (or similarly protecting a similar term) would go some way toward clarifying the term in the eyes of the public.

I do believe that sunlight is a great disinfectant, so support appropriate disclosure of commissions and other pecuniary interests. Appropriate need not mean complex, not should it mean burried under 140 pages of "Statement of Advice".

Remuneration models for advice should be a matter between client and adviser. Market forces will dictate and eventually prevail over inappropriate practices.

Having been a vigilant "independent" for four years, I took great care with my advice. I took the time to know my clients and to bring them to clear expectations of what I could, and could not, deliver. As an "independent" I knew my reputation and AFSL were on the line if my actions fell short of professionalism.

The present regime would seem to have somehow fallen short of making AFSL responsible for the advice they issue through their Authorised Representatives.

Limiting the issue of AFSL's permitting the provision of personal advice to retail clients to smaller business units (say individuals and partnerships) would, I feel, bring home the responsibility for sound advice to advisers who might presently fell they are in some way not going to be held responsible for their failings.

Greater action by the regulator, such as imposing sanctions on all the advisers under an AFSL for the serious transgressions of either the management or a proportion of the total number of advisers might also be a lesson in accountability.

the role played by marketing and advertising campaigns

There is no doubt that advertising can affect decision making. However I do belienve that advertising was not a significant factor in the financial product and services provider collapses that are the scope of this inquiry.

I believe this aspect to be the realm of the Trade Practices Act rather than the role of ASIC or APRA. There is some considerable overlap in this regard, which might be a area examined in this inquiry.

the adequacy of licensing arrangements for those who sold the products and services

My comments above refer to this to some extent. And I would add that I have had exposure to several "Storm affected" clients. One who asked for my review of the recommendations in a Storm SoA, and in spite of my own recommendations, proceeded and suffered losses. They have now returned to engage my services and we are proceeding happily, albeit with lessons learned.

Another two came to me after the closure of Storm, and while I initially assisted with their stated desire to stablilise their losses, both terminated my engagement within months when I fell short of their expectations of my ability to recoup their previous losses and generate the returns promised by Storm. Both these clients lodged complaints against my services (my only two written complaints in 10 years of practice) and what I have learned is that any client with unrealistic exectaions (however acquired) is not worth assisting.

Insofar as licensing arrangements are concerned, the problem lies in the ability of a corporate licensee to authorise representatives with either limitations on the advice that they might provide to clients, or inadequate experience and professionalism, or both. In the subject cases, the AFSL would appear to be able to interpose their authorised representaives as a "shield" or at least a "buffer" for sacrifice in the event of poor advice and/or subsequent litigation.

Again, limiting the issue of "advice providing" AFSL to suitably qualified individuals or partnerships might provide the personal exposure that would often maintain the professionalism of advice, and help prevent recurrences.

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

Advice to retail client needs to be concise. My experience is that people will listen rather than read, and when a document passes 10 pages less than one in twenty will read it. This goes for both SoA and PDS.

The interests of consumers might best be served by standardising the key components of a SoA into perhaps six or eight components. In relation to the risks associated with a particular product a template diagram of where the product sits in terms of likely positive and/or negative returns, plus a recommended timeframe would be essential.

I would draw a comparison with cigarette advertising warnings. Perhaps the PDS might contain a color code or scale that indicates the likelihood of losses. Perhaps a system of product rating akin to the television classifications of "G", "M15", "R" and "X" might be applied to products or strategies involving gearing.

consumer education and understanding of these financial products and services

I believe that there is a role for the regulator and indeed the government is supporting consumer education regarding mainstream financial products, and that consumers who engage in products that are less mainstream should take responsibilty for their own education.

For instance education about industry superannuation, being both compulsory and mainstream, should be promoted. While education about put options and call options, being not so mainstream (although accessible to most Australians) would not need such promotion as it is something that a consumer would reasonably be expected to investigate if they were interested.

In the subject financial product and services provider collapses, the use of prudent gearing can be distinguished form the use of high risk gearing. In such an instance the responsibility for undertaking such strategies must ultimately lie with the consumer. *Caveat emptor*, say I.

the adequacy of professional indemnity insurance arrangements for those who sold the products and services, and the impact on consumers

I have devoted significant time and effort to this issue in my capacity as licensee, and conclude that, for the purposes of professional indemnity insurance, a distinction needs to be made, at law, between advice, and losses consequential to that advice.

The present regime seems to be unable to segregate these two aspects, and the pricing of policies is similarly inflated. Without a test case, in circumstances such as those financial product and services provider collapses that are the suject of your inquiry, there will be no grounds to make such a distinction.

Again, it seems that the AFSL licensee is able to shiedl their responsibility by interposing "adviser resonsibility" before exposing their "product responsibility".

the need for any legislative or regulatory change

I conclude that the way forward would require legislative improvement, but there is also a need for the industry associations to impose professional sanctions upon members. The ultimate solution would be a combination fo the two.

The quick and dirty solutions might look like:

- Protect the term "financial adviser" under law and limit it's application to only those natural persons (and no other entities) who are appropriately licensed under the FSR.
- Strengthen the term "independent financial adviser" to those financial advisers who do not accept "commissions" - also a term requiring definition at product level.
- Introduce a tax deduction concession to level the playing field between up-front fees and brokerage.

The longer term structural solutions would need to see implementation of the above, plus

- a rise in self regulation and professionalism amongst financial advisers (assisted by separation of product from advice).
- expulsion or separation of product providers from certain industy bodies purporting to represent adviser interests.

With the changes above, the committee and the industry would be improving the framework and displaying the resolve to enable delivery of quality advice to Australians who have the potential to benefit so greatly from reliable, professional, appropriate, financial guidance.

I wish the committed well for the months ahead.

Yours sincerely,

Crawford Peter Hillis