

INNOVATIONS IN FINANCIAL SERVICES REGULATION FOR CONSUMER PROTECTION

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ABSTRACT

Australia is widely regarded as an innovator in financial services regulation. It introduced the twin peaks model, which was later followed in the United Kingdom. Under this model of regulatory supervision, there is a split between prudential regulation of financial institutions for institutional stability and resilience, and market conduct regulation of financial service providers for efficient, transparent and fair practices and provision of information. The two institutions in Australia are the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC). The latter, ASIC, has an explicit consumer or retail client function which complements its wide array of responsibilities. Australia has disclosure and conduct regimes to protect consumers of financial services. These built on and intersect with earlier protective regimes. It also has nascent product regulation. This paper explores current regulatory issues and proposals. It is restricted to the Australian jurisdiction. Those from other jurisdictions will find echoes of their own arrangements and may find useful approaches.

CURRENT ISSUES

The market for regulatory change and innovative policy solutions in financial services has hotted up in Australia particularly since the Murray Inquiry into financial services which reported in December 2014.¹ This inquiry is one in successive inquiries into the Australian system since the second half of last century.² The Murray report does not herald major changes to the regulatory structure. It is more in the nature of a stocktake

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1 Commonwealth of Australia, Financial System Inquiry Final Report ('FSI Final Report') (December 2014).

2 For a good short history, see Commonwealth of Australia Parliamentary Joint Committee on Corporations and Financial Services, Inquiry into Proposals to Lift the Professional, Ethical and Education Standards in the Financial Services Industry, at 3–15 (December 2014).

with recommendations for improvements to the system rather than a radical overhaul. Its starting point is sustainable economic growth linked to the funding needs of the Australian economy and competition within the economy. The underlying message is efficiency. The report adopted five themes: resilience; lifting the value of the superannuation system for retirement incomes; driving economic growth through productivity and innovation; enhancing confidence and trust through an environment which treats customers fairly; enhancing the independence and accountability of regulators along with minimising the need for future regulation.³

The Murray Inquiry ran alongside other initiatives, inquiries, and revelations. These were a Senate inquiry into the performance of the prime regulator, ASIC⁴ and a Joint Parliamentary inquiry into professional and ethical standards in the financial services industry.⁵ There was a controversial attempt to amend recently introduced legislation which regulated financial advice to retail clients.⁶ Ongoing media revelations about the illegal behaviour of financial advisers in the large integrated banking firms informed the public debate.⁷

The big issues requiring resolution are about financial advice, financial advisers and financial products. This is because of the extent of losses to individual consumers who acquired inappropriate products as a result of bad advice. Losses have been estimated at \$5 billion which may not take into account some recent revelations.⁸ Currently financial advice is regulated but there is limited regulation of the financial product. There is current debate about the extent to which regulation should move beyond setting

3 Commonwealth of Australia, *supra* note 1, at 1.

4 Commonwealth of Australia Senate Economics References Committee, Performance of the Australian Securities and Investments Commission (June 2014).

5 Commonwealth of Australia Parliamentary Joint Committee on Corporations and Financial Services, *supra* note 2.

6 Senate Economics Legislation Committee, Corporations Amendment (Streamlining Future of Financial Advice) Bill 2014, September 2014 (Aust.).

7 See Commonwealth of Australia Senate Economics References Committee, *supra* note 4.

8 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 28.

a standard for financial advice to intervening between the choice of the consumer and the product. Australia already has a regulatory regime which imposes a requirement that consumer credit products should be suitable for the borrower.⁹ Whether there should be suitability standard was raised in the Murray interim report, but not pursued.¹⁰ This is discussed in greater detail below.

Depositor protection is a current issue. Australia did not introduce a deposit guarantee system until the 2008 financial crisis. It is very generous and rests on depositors ranking ahead of all other creditors in case of insolvency. The scheme is restricted to authorised deposit institutions (ADIs). Some consumers have confused finance companies who offer deposit-like products with ADIs. A Murray inquiry recommendation is that the products of finance companies which are debt securities should be clearly differentiated from deposit products offered by ADIs(banks). It recommends that APRA should ban finance companies from using words that are bank-like and from offering at-call products to consumers.¹¹ A further issue is whether there should be a prospective levy on ADIs for the deposit guarantee system, something that would be likely to be passed on to consumers. The Murray Report does not support this.¹²

Another issue is how widely should initiatives which start life as consumer protection measures extend to other sectors of the economy. Australia has long-standing and vigorous statutory injunctions against engaging in unconscionable conduct. These extend to business- to-business transactions.¹³ Unfair terms in contracts prohibitions do not cover contracts with other businesses.¹⁴ The Murray Report proposes that unfair terms

9 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Aust.).

10 Commonwealth of Australia, Financial System Inquiry Interim Report ('FSI Interim Report') at xxxi, 3–62 (July 2014).

11 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 265.

12 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 82–83. Neither does it support bail-in of depositors' funds – see 71.

13 Australian Securities and Investments Commission Act 2001 (Act No. 51/2001, as amended), §§ 12CA, 12CB (Aust.).

14 Australian Securities and Investments Commission Act 2001 (Act No 51/2001, as amended), §12BF (Aust.).

prohibitions should extend to small business. This would address problems connected with loans to small businesses and business-to-business lending.¹⁵

THE CONSUMER LANDSCAPE

Australians are sophisticated consumers of financial services. Nearly all Australians have bank accounts. The reason for this is the payments system for wages and pensions. Wages and salaries are commonly paid directly into bank accounts. All pensions and social security benefits are paid into bank accounts. This means that there is limited scope for an informal economy and little room for arguments regarding the unbanked. It also means that there are strong arguments for the protection of bank deposits. Australia is a capital importing country and the availability of credit, particularly for housing is linked to macroeconomic concerns. Consumer lending is undertaken by banks and customer-owned banks, collectively authorised deposit taking institutions (ADIs). Finance companies, community groups and others also lend to consumers. There is a compulsory system of saving for retirement, called superannuation, which is enforced through the employment and tax system. All employers must contribute a mandated percentage of an employee's salary to a superannuation fund. The employee can choose which fund. Individuals cannot draw on these funds until they reach retirement age. Individuals may also set up self-managed superannuation funds. This means that collectively in the Australian system there is a large quantum of funds under management and Australia has developed considerable expertise in funds management. On retirement individuals are able to take money from a superannuation fund as a lump sum to spend or reinvest. There is a deficit in annuity products and life insurance. In addition a large proportion of Australians invest outside superannuation in equities and forms of collective investments. A large industry has grown which provides broking services for credit, particularly mortgage credit, and advice or planning for superannuation and investment.

15 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 264.

THE REGULATORY LANDSCAPE

There are intermittent but regular inquiries into the Australian financial system which canvas current challenges, and include discussion of regulation and protection for financial citizens. The recent Murray Inquiry into the Australian Financial System builds on the work of the earlier Wallis Report. The “twin peaks” structure, which has served Australia well, resulted from the Wallis inquiry. The Murray report has endorsed the overall regulatory structure and makes a number of recommendations to enhance this.

What is this structure from the point of view of consumer protection? There are two Commonwealth government agencies explicitly charged with protection of consumers. The Australian Competition and Consumer Commission (ACCC) is the successor to the Trade Practices Commission. It is responsible for laws to ensure competition and for consumer protection in all parts of the economy with the exception of financial services and consumer credit. Its chief legislation is the *Australian Competition and Consumer Act 2010* (Cth). This legislation re-enacts part of the former *Trade Practices Act 1974* (Cth). The most relevant part for consumers is the Australian Consumer Law (ACL) which is found in a Schedule to the Act. The ACL contains provisions on misleading and deceptive conduct, unconscionable conduct, unfair terms in consumer contracts, product safety and product liability. It also contains provisions which institute consumer guarantees with regard to the characteristics and qualities of goods which replace the old provisions of non-excludable implied terms in consumer contracts for the supply of goods. Consumer protection for financial services was integrated with the companies regulator, ASIC, following the regulatory changes as part of the corporations law reform process towards the end of the twentieth century. The rationale for this is the importance of specialist regulatory expertise which can also be applied in a retail client context. Since then, ASIC has also been given responsibility for margin lending against shares as security and for consumer credit laws.¹⁶

¹⁶ Corporations Act 2001 (Act No 50/2001, as amended), Part 7.8 Division 4A (Aust.).

The responsibilities of ASIC for protection of financial citizens are in three pieces of legislation: the *Australian Securities and Investments Commission Act 2001* (Cth), the *Corporations Act 2001* (Cth), and the *National Consumer Credit Protection Act 2009* (Cth). There is legislation relevant to consumer protection in insurance contracts and in superannuation (retirement) funds which will not be discussed.

The consumer is described differently in the three different pieces of legislation. The credit legislation uses the term consumer and describes consumer credit by reference to the purposes of the credit with a major exception of the acquisition of residential housing for investment purposes which falls within the legislation. An ongoing issue is whether credit for other investments may be for “personal domestic or household use” and entitled to protection.¹⁷ The ASIC Act legislation uses the term consumer and also modifies this by reference to the purposes for which the financial product or service is acquired.¹⁸ By contrast, the Corporations Act uses the term retail client which is defined by price and lack of “big” business use.¹⁹ These definitions appear to work reasonably well. Commentary has tended to focus on the different definitions of consumer for different purposes in the ACL.

REGULATORY STRATEGIES

The approaches to regulation involve licensing providers for participation in the market; disclosure of information about providers and products to aid the decisions of consumers; regulation of market conduct and conduct towards consumers to ensure such conduct is not misleading or deceptive or unconscionable; and product regulation.

17 Gail Pearson, *Regarding Unfair Terms in Financial Services Contracts*, 37(1) UNIVERSITY OF WESTERN AUSTRALIA LAW REVIEW 216 (2013).

18 Australian Securities and Investments Commission Act 2001 (Act No. 51/2001, as amended), § 12BC (Aust.).

19 Corporations Act 2001 (Act No 50/2001, as amended), § 761G (Aust.).

4.1. WHO CAN BE IN THE MARKET AS A PROVIDER?

The first strategy for financial citizen protection has been to ensure that those providing products and services within the market have the requisite capacity to do so and further that they provide redress if required. All providers of financial services and consumer credit must be licensed.²⁰ To maintain a licence, the licence holder must abide by certain obligations which include managing risk, ensuring the standard of their representatives, having internal dispute resolution mechanisms and being a member of an external dispute resolution scheme. ASIC does and will cancel licences. It cancelled the licence of failed debenture issuer Banksia, which a number of investors believed was a deposit taking institution.²¹ Following a review, seven licensees who failed to meet their professional indemnity insurance obligations lost their licences.²² A number of mortgage brokers have had their credit licences cancelled for failure to verify documents related to loan applications submitted to banks.²³ In 2013-2014, one hundred and three individuals or companies were banned from providing financial services or credit services.²⁴

Many financial advisers work as authorised representatives of licensees or as their employees. They are not separately licensed. The Murray Report

20 Corporations Act 2001 (Act No 50/2001, as amended), § 911A (Aust.); National Consumer Credit Protection Act (Act No. 134/2009 as amended), §§ 27, 29 (Aust.).

21 Australian Securities and Investments Commission, ASIC Cancels Banksia's AFS Licence (28 April 2014) (ASIC Media Release 14-087MR), *available at* <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-087mr-asic-cancels-banksias-afs-licence/>.

22 AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION, ASIC SURVEILLANCE RESULTS IN CANCELLATION OF SEVEN AFS LICENCES (4 August 2014) (ASIC Media Release 14-187MR), *available at* <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-187mr-asic-surveillance-results-in-cancellation-of-seven-afs-licences/>.

23 AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION, ASIC Concerns About Loan Applications Result in Cancellation of Mortgage Brokers Licence (18 February 2014) (ASIC Media Release 14-030MR), *available at* <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-030mr-asic-concerns-about-loan-applications-result-in-cancellation-of-mortgage-brokers-licence/>.

24 Australian Securities and Investments Commission, Annual Report, at 5 (2013–2014).

recommended lifting competency in financial advice and also a register of financial planners.²⁵

There have been calls to establish a register and on 31 March 2015 ASIC launched the register for financial advisers which will include their qualifications, and experience and any regulatory action taken against an individual planner.²⁶ This means that consumers can make sure advisers are authorised and employers can check on individual financial planners. The shape of further regulation is unclear. The current consultation paper on standards for financial advisers suggests there will be additional mandatory educational requirements.²⁷

4.2. THE LIMITATIONS OF DISCLOSURE

A major approach²⁵ has been to adopt the efficient market hypothesis and the importance of disclosure of information to prospective acquirers of financial products or services. To this end retail clients must receive information about the company they are dealing with, the proposed product and any advice. Similarly, consumers must receive information about a proposed credit products and the proposed credit contract. There is acknowledgement in Australia about the limitations of disclosure as the most effective model to ensure protection of financial citizens. This is linked to a number of factors most particularly the insights of behavioural economics and the understanding that individuals do not make rational decisions based on due assessment of all available information.²⁸ Individuals are subject to

25 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at xix, xxv, 28.

26 AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION, AFS LICENSEES – FINANCIAL ADVISERS REGISTER (15 April 2015), *available at* <http://asic.gov.au/for-finance-professionals/afslicensees/financial-advisers-register/>.

27 Australian Government, *Lifting the Professional, Ethical and Education Standards in the Financial Services Industry – Consultation on Recommendations of the Parliamentary Joint Committee on Corporations and the Financial Services’ Inquiry into Proposals to Lift the Professional, Ethical and Educational Standards in the Financial Services Industry* (March 2015).

28 For example, Omri Ben-Shahar & Carl E Schneider, *More Than You Wanted To Know: The Failure of Mandated Disclosure* (Princeton University Press, 2014); Commonwealth of Australia, *supra* note 10, at 1.20, 3–57; Commonwealth of Australia Senate Economics References Committee, *supra* note 4, at 42.

their own biases which might include irrational over-optimism or undue risk aversion. A further debate is linked to the notion of a regulatory burden and the expense and time to industry in complying with disclosure obligations. This has led to evidence-based attempts to craft more effective disclosure that reaches an individual as early as possible in the decision-making process and which has short and intelligible information targeted at what is critical information.²⁹

Another form of information provision is comparison websites that permit a consumer to enter information. The site will then compute a result for the consumer. ASIC has provided regulatory guidance on comparison websites.³⁰

Disclosure is noted in the Murray Report. It says there should be more innovative forms of disclosure that take account of both behavioural biases and technology.³¹ This does not just envisage disclosure by industry about itself and its products. It also includes access by consumers to their own personal data. Such information could assist individual consumers to better understand their own circumstances and make better decisions.³² While there is extensive mandated disclosure, the regulator does not have power to intervene to impose requirements about product features or risk characteristics especially regarding new complex financial products. The Murray Report has advocated that ASIC should have such a power.³³

The Report refers to the “limits of the disclosure-based regulatory regime,”³⁴ again in the context of complex high-risk products. In some instances, it says, consumers will not be able to understand product features and the risk return trade-off, even with accurate disclosure. An earlier report

29 P O’Shea, SIMPLIFYING DISCLOSURE IN CONSUMER CREDIT; EMPIRICAL RESEARCH AND REDESIGN, (Ministerial Council for Consumer Affairs, Commonwealth of Australia, Canberra, 2010).

30 AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION, Regulatory Guide 234 – Advertising Financial Products and Advice Services: Good Practice Guidance (November 2012).

31 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 195.

32 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 187.

33 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 208.

34 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 208.

on existing disclosure requirements for consumer credit contracts suggested that consumers did not easily understand complex documents, that they could grasp salient features such as interest rates if these were presented clearly and that the earlier in the process a consumer received information the more likely it would be of value to the decisions to be made about whether or not to enter into a loan.³⁵ Types of disclosure documents for financial services and credit include: the Financial Services Guide and the Credit Guide which give information about whom the consumer is dealing with; the Statement of Advice and the Product Disclosure Statement.

4.3. BEYOND DISCLOSURE TO REGULATION OF THE PRODUCT FOR THE CONSUMER

(i) Contract terms

Product regulation takes a number of different forms. One is the form that the contract may take. There is an overarching obligation the standard form contracts with consumers should not contain unfair terms.³⁶ Many financial services products are contracts so this establishes a fairness standard for the contours of such products. This was tested recently in a case which asked whether certain bank fees were unconscionable, unjust or unfair.³⁷ There are different statutory regimes with rules for each of these principles. In this decision, emphasis was laid on the distinction between unconscionability on the one hand and unjustness and unfairness on the other. The Court said that unjustness and unfairness “are of a lower moral or ethical standard than unconscionability.”³⁸ It found that the bank fees in question (including credit card fees) were neither unconscionable, unjust nor unfair. With respect to unfairness, there was no imbalance in

35 P O’Shea, *supra* note 29.

36 Australian Securities and Investments Commission Act 2001 (Act No. 51/2001, as amended), § 12BF.

37 *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50. It is not yet known whether this will be appealed to the High Court of Australia. The question of fairness was decided on state legislation which has now been repealed.

38 *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50 at [363].

the rights and obligations of the parties to the detriment of the consumer at the time of entry into the contract. The terms were disclosed, there was no trickery, the fees could be avoided by reasonable conduct on the part of the consumer through keeping within contractual limits, and the contracts were terminable at will by the consumer.³⁹

Product regulation also occurs through terms that are implied into financial services contracts. In the case of financial services contracts there are non-excludable warranties that the services are fit for the purpose and will be delivered with due care and skill.⁴⁰

(ii) Suitability

Another form of product regulation is to create requirements about the relationship between the product and the particular individual. This is the case with the requirement that a consumer credit contract product be suitable for the particular consumer.

In the credit space, regulation has moved beyond disclosure. Risk also arises outside the investment context as the risk of not being able to re-pay a loan is important to borrowers as well as to lenders. In the case of consumer loans, those who advise on or broker loans and those who provide loans must ensure that the loan is suitable for that consumer.⁴¹ The legislation prescribes steps which the “credit assistance provider” and the “credit provider” must take before recommending a loan product or before entering into a loan contract. The first involves a “preliminary assessment” and the second the assessment. In the lead-up to the legislation, credit providers argued they should be able to rely on assessment made

39 *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50 at [358].

40 Australian Securities and Investments Commission Act 2001 (Act No. 51/2001, as amended), Division 2 Subdivision E, § 12 ED.

41 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Australia), §§ 115, 116, 128 and 129; G Pearson and R Batten, *Understanding Australian Consumer Credit Law* (CCH Wolters Kluwer 2010); Jessica Tuffin, *Responsible Lending Laws: Essential Development or Overreaction?* 9(2) QUEENSLAND UNIVERSITY OF TECHNOLOGY LAW JOURNAL 280, (2009).

by brokers. However, the argument that as credit providers were the ones extending credit, they should make their own assessment rather than risk relying on a suitability assessment, which might or might not be properly conducted, prevailed. A preliminary assessment is valid only for ninety days before the consumer enters the credit contract or increases the credit limit.⁴² The suitability assessment requires the person making the assessment to do three things: make reasonable enquiries about the requirements and objectives of the consumer; make reasonable enquiries about the financial situation of the consumer, and take reasonable steps to verify the consumer's financial position.⁴³ The test of suitability is whether the consumer will be able to repay the loan without substantial hardship and whether the loan will meet the objectives and requirements of the consumer.⁴⁴

In a recent decision, the Federal Court said that if the statement of the purpose of the loan is "too general" this is not sufficient to meet the obligation to make enquiries about the consumer's requirements and objectives.⁴⁵ Examples of purposes that were too general included "wedding"; "travel"; "cash shortfall". A purpose of "doctor, insulin" was treated as reasonably specific.⁴⁶ The court also said that assessing whether a consumer had "a real chance" of repaying required, at a minimum, information about current income and living expenses and further information "will be a matter of degree in each particular case."⁴⁷

The regime for margin lending on securities also requires lenders to assess whether a margin loan facility is suitable for the client.⁴⁸ Like

42 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Aust.), § 115.

43 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Aust.), §§ 117, 130.

44 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Aust.), §§ 118, 131(2).

45 *Australian Securities and Investments Commission v Cash Store Pty Ltd (in liquidation)* [2014] FCA 926 at [36].

46 *Australian Securities and Investments Commission v Cash Store Pty Ltd (in liquidation)* [2014] FCA 926 at [38].

47 *Australian Securities and Investments Commission v Cash Store Pty Ltd (in liquidation)* [2014] FCA 926 at [42].

48 Corporations Act 2001 (Act No 50/2001, as amended), § 985E.

consumer credit, this requires an assessment of whether the client has the capacity to pay without substantial hardship if the facility goes into a margin call.⁴⁹ There have been no decisions on this provision.

There are further requirements that circumscribe particular consumer credit products such as reverse mortgages which have additional suitability requirements⁵⁰ and payday or small amount loans which have a cap on costs, a mandatory warning statement, additional requirements for assessing the potential debtors financial situation and unsuitability presumptions.⁵¹ Problems have been identified with on line small amount lending.⁵²

FINANCIAL ADVICE

Financial advice became the subject of particular controversy in Australia through 2014. There were attempts to alter the Future of Financial Advice legislation which had been put in place just two years earlier and Parliamentary enquiries which revealed the extent of unscrupulous and illegal behaviour in large financial institutions prior to the introduction of these reforms.⁵³ It is common for consumers to deal through an intermediary rather than directly with a product or service provider. This will be a mortgage broker or “credit assistant” in the case of home loan credit and a financial planner or adviser for investment. Advisers owe a fiduciary duty to clients.⁵⁴

49 Corporations Act 2001 (Act No 50/2001, as amended), § 985H.

50 National Consumer Credit Protection Act (Act No. 134/2009 as amended) (Aust.), §§ 133DA–133DE.

51 See Australian Securities and Investments Commission, Report 426 – Payday Lenders and the New Small Amount Provisions (March 2015).

52 S Long and M Christodoulou, *Payday Lender Good2Go Loans Under ASIC Microscope Accused of Lending to Drug Addicts, Gamblers*, ABC Four Corners, [http://www.abc.net.au/news/2015-03-30/good2go-loans-investigated-by-asic/6357166\(30/03/2015 1:36:48 PM\)](http://www.abc.net.au/news/2015-03-30/good2go-loans-investigated-by-asic/6357166(30/03/2015 1:36:48 PM)).

53 Senate Economics Legislation Committee, Corporations Amendment (Streamlining Future of Financial Advice) Bill 2014 (June 2014); Senate Economics Legislation Committee, Corporations Amendment (Streamlining Future of Financial Advice) Bill 2014 (September 2014); The Senate Economics References Committee, *Performance of the Australian Securities and Investments Commission* June 2014.

54 *Daly v The Sydney Stock Exchange* (1986) 160 CLR 371; *Wingecarribee Shire Council v Lehmann Brothers Australia Ltd (in Liq)* [2012] FCA 1028; *Bathurst Regional Council v Local Government Financial Services* (No 5) [2012] FCA 1200.

New legislation to regulate giving advice and receiving commissions was introduced in 2012 following managed investment scheme collapses and large losses to consumers (who may not have perceived the risk) persuaded into high risk investments for the benefit of high commissions for advisers. This provided a standard of “appropriate” advice that could be met by, in turn, meeting a “best interests” of the client duty.⁵⁵ It also set out an obligation to give priority to the interests of the client.⁵⁶ The legislation sets out seven steps which an adviser should complete in order to demonstrate having acted in the best interests of the client.⁵⁷ These are identifying the client’s objectives, financial situation and needs; the subject matter of the advice and the clients’ circumstances relevant to the advice; obtaining additional information if necessary; assessing the adviser’s own expertise in relation to the advice sought; considering if advice should be given; investigating financial products that might meet the objectives and needs of the client; and finally taking any other necessary step.⁵⁸ The Murray Report recommended that the standards of financial advice should be improved.

Although the Murray Report stopped short of recommending an individual suitability test for financial products, it did say that product design and accountability of product issuers and distributors should be improved and recommended that ASIC should have a strengthened product intervention power.⁵⁹ It has also recommended a principles-based regulatory obligation for industry to develop standards tailored to product classes.⁶⁰

The 2012 legislation also established a ban on accepting and paying conflicted remuneration.⁶¹ Well-established advice firms are often vertically integrated as the subsidiaries of financial institution conglomerates headed

55 Corporations Act 2001 (Act No 50/2001, as amended), § 961G.

56 Corporations Act 2001 (Act No 50/2001, as amended), § 961J.

57 Corporations Act 2001 (Act No 50/2001, as amended), § 961B.

58 Corporations Act 2001 (Act No 50/2001, as amended), § 961B(2). There have been attempts to repeal this final step.

59 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at xix, 195.

60 COMMONWEALTH OF AUSTRALIA, *supra* note 1, 204.

61 Corporations Act 2001 (Act No 50/2001, as amended), §§ 963E, 963F.

by the large banks. The legislation does not ban commissions per se but it defines conflicted remuneration as payments or benefits that could reasonably be expected to influence advice.⁶² One of the exemptions has been commissions for the sale of life insurance which may be greater than the policy in initial years. The Murray Report said firm culture should be focused on the interests of consumers and conflicts of interest addressed.⁶³ There has been a high degree of churn as unscrupulous brokers persuade consumers to leave old policies and take out new policies for the sake of commissions.⁶⁴ This is currently being reviewed.⁶⁵ The recommendation to reform adviser remuneration would limit commissions to 50% of the premium and an advice payment limited to only once every five years.⁶⁶

CONCLUSIONS

Like a number of jurisdictions, Australia is moving from relying on licensing, conduct and disclosure obligations towards ensuring there is a better fit between the needs of consumers and the financial products they acquire. This multi-pronged approach removed incentives for mis-selling as with bans on conflicted remuneration and limitations on insurance commissions. It also introduced obligations towards safer and suitable products, seen most clearly in consumer credit. In investment, this is an ongoing policy debate. The latest round of proposals builds on earlier principles and laws. The Australian public knows that returns in the financial services market cannot be guaranteed and is keen to see the eradication of malign practices and products. Hearings in the current Senate enquiry⁶⁷ reflect the widespread desire of financial citizens in Australia to ensure that financial markets and those within them act fairly.

62 Corporations Act 2001 (Act No 50/2001, as amended), § 963A.

63 COMMONWEALTH OF AUSTRALIA, *supra* note 1, at 95.

64 Australian Securities and Investments Commission, Report 413 – Review of Retail Life Insurance Advice (October 2014).

65 J Trowbridge, Review of Retail Life Insurance Final Report (March 2015)

66 J Trowbridge, Review of Retail Life Insurance Final Report (March 2015), 24f.

67 COMMONWEALTH OF AUSTRALIA Senate Economics References Committee, Scrutiny of Financial Advice (Public Hearing April 21 2015, to Report February 2016).