ASIC

Australian Securities & Investments Commission

CONSULTATION PAPER 46

Licensing: Managing conflicts of interest

(with specific guidance for providers of research reports)

October 2003

Your comments

You are invited to comment on the proposals and issues for consideration in this paper, including the explanation sections. We will not treat your submission as confidential unless you specifically request that we treat the whole or part of your submission as confidential.

Comments are due by 31 January 2004 and should be sent to:

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You can also contact the ASIC Infoline on 1300 300 630 for information and assistance.

What this policy proposal is about

1 This policy proposal paper sets out:

(a) our general approach to compliance with the proposed statutory obligation to manage conflicts of interest in proposed s911A(1)(aa) (the "conflicts management obligation") **(Section A)**; and

(b) guidance for licensees generally on controlling, disclosing and avoiding conflicts of interest **(Section B)**.

It also includes some questions for licensees generally to consider (Schedule 1) and specific guidance for providers of research reports (Schedule 2).

Note 1: For definitions of "research report" and "research report provider", see Schedule 2.

Note 2: The conflicts management obligation is set out in the Exposure Draft Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 (Draft CLERP 9 Bill), published on 8 October 2003.

2 We have included more detailed guidance in Schedule 2 for research report providers taking into account domestic and international developments, including the Government's discussion paper, "Corporate disclosure: Strengthening the financial reporting framework" (CLERP 9) (September 2002) and the Draft CLERP 9 Bill. But because the guidance in Schedule 2 is based on our general approach to the conflicts management obligation, other licensees may wish to consider how it might apply to their own operations. We may provide more guidance on managing conflicts of interest for other industry areas in future, if it is needed.

Your feedback

Are there any other types of financial services or licensees where specific additional guidance should be provided? Please give reasons.

3 This paper should be read in conjunction with policy statements and guides we have previously issued on how we administer Chapter 7 of the *Corporations Act 2001* (the financial services regime), including:

(a) *Licensing: The scope of the licensing regime: Financial product advice and dealing — An ASIC guide* (November 2001, updated November 2002);

(b) Policy Statement 164 *Licensing: Organisational capacities* [PS 164]; and

(c) Policy Statement 175 *Licensing: Financial product advisers — Conduct and disclosure* [PS 175].

4 This paper does not consider the management of conflicts of interest that are wholly outside a licensee's financial services business. However, such conflicts may still be regulated by other statutory provisions and by the common law.

When will our policy commence?

5 This paper is based on the conflicts management obligation. It explains how we expect licensees to comply with the proposed obligation when it commences.

6 We do not expect the proposed conflicts management obligation to commence until 1 July 2004 at the earliest: see the Treasurer's media release 2003/87, 8 October 2003. Because the transitional provisions for the Draft CLERP 9 Bill (including the conflicts management obligation) are still being developed, the commencement date for the obligation may be even later: see the Commentary on the Draft Provisions at paragraph 24.

7 However, some existing licensee obligations also deal with conduct that is affected by conflicts of interest. This paper may assist licensees in their compliance with these existing obligations.

8 This paper is not final ASIC policy. The timing of our final policy will depend on the finalisation of the Draft CLERP 9 Bill. In finalising the policy, we are considering inserting additional material on managing conflicts of interest generally in [PS 164]. We may also publish separate guidance covering research report providers.

Contents

Important note: The proposals, explanations and examples in this paper do not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act applies to you. It is your responsibility to determine your obligations under the Corporations Act and regulations. The proposals, explanations and examples in this paper are at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

Examples in this paper are purely illustrative; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

We are issuing a policy proposal paper at this time to provide early guidance on the conflicts management obligation and to help you plan effectively. The Commentary on the Draft Provisions flagged that we might provide this guidance (at paragraph 586).

This paper is based on the legislation and regulations as at 29 October 2003. It refers to proposed amendments to the Corporations Act set out in the Draft CLERP 9 Bill. We will take into account changes to the legislation or regulations in the finalisation of this policy. In particular, we will review our proposals, if necessary, in light of the passage of the Draft CLERP 9 Bill through Parliament.

Policy proposals

In this paper, we have two sections of policy proposals. Section A discusses our "outcomes based" approach to administering the proposed licensee obligation to have adequate arrangements to manage conflicts of interest. Section B provides guidance on our expectations of how licensees can manage conflicts of interest. For each section, we set out the proposals and identify issues we would like you to comment on. When necessary, we have also included explanations of our proposals.

Special note: There may be other issues that you consider important. We are keen to hear from you on our general approach and any other issues you consider important, as well as your answers to our specific questions.

A Our approach to managing conflicts of interest

Policy proposal	Your feedback

Key outcomes

A1 Under proposed s912A(1)(aa) (the "conflicts management obligation"), licensees will be obliged to have in place adequate arrangements to manage conflicts of interest. We intend to adopt an outcomes based approach in considering whether arrangements for the management of conflicts are adequate. In our view, if arrangements are adequate they will help achieve the key outcomes of the licensing regime in policy proposal paragraph A2.

Note: The term "conflicts of interest" is used broadly in this paper and includes actual or potential conflicts as well as present or future conflicts. For a description of "conflicts of interest", see paragraph 1 of the explanation in this section.

A2 The conflicts management obligation forms part of the licensing regime, which promotes the following primary outcomes:

(a) confident and informed decision making by consumers;

(b) fairness, honesty and professionalism by those who provide financial services; and

(c) fair, orderly and transparent markets for financial products: s760A.

Policy proposal	Your feedback
Key mechanisms	
A3 In our view, the three key mechanisms that licensees generally use in managing conflicts of interest are: **(a)** controlling conflicts of interest; **(b)** disclosing conflicts of interest; and **(c)** avoiding conflicts of interest.	**A3Q1** Could these three key mechanisms be more clearly or helpfully described? Please give details. **A3Q2** Are there any other key mechanisms? Please give details.
Controlling conflicts	
A4 In controlling conflicts of interest, licensees should ensure that their financial services are provided with fairness, honesty and professionalism. The quality of their financial services should not be significantly compromised by conflicts of interest. Note 1: Licensees should consider conflicts between their interests and the interests of both particular clients and clients generally. In some situations, there may be a conflict of interest that does not involve any particular client, but that may still need to be adequately managed by the licensee. Note 2: For our proposals and guidance on how licensees might use this mechanism, see Section B.	**A4Q1** Do you agree with this approach to controlling conflicts? Please give reasons.
Disclosing conflicts	
A5 Licensees should use appropriate disclosure in their management of conflicts of interest. They should ensure that clients are sufficiently informed about any conflicts that may affect the provision of financial services to them. Note: For our proposals and guidance on how licensees might use this mechanism, see Section B. This mechanism would generally be used in conjunction with measures, processes and procedures to control conflicts of interest: see policy proposal paragraph A4.	**A5Q1** Do you agree with this approach to disclosing conflicts? Please give reasons.

Policy proposal	Your feedback
Avoiding conflicts	
A6 Some conflicts of interest have such a serious impact on a licensee or their clients that they need to be avoided. In these cases, controlling and/or disclosing such conflicts will not adequately manage the conflict. Note: For our proposals and guidance on how licensees might use this mechanism, see Section B.	**A6Q1** Do you agree with this approach to avoiding conflicts? Please give reasons.

Explanation

What are conflicts of interests?

1 For the purposes of this paper, conflicts of interest are circumstances where some or all of the client's interests are inconsistent with or divergent from some or all of the licensee's or its representatives' interests. These include all conflicts of interest, whether they are actual or potential, and present or future.

Note: For example:

(a) licensee X has an interest in encouraging client Y to invest in higher risk products that result in high commissions, which is inconsistent with client Y's personal desire to obtain a lower risk product;

(b) licensee A has an interest in maximising trading volume by their clients (including client B) so as to increase commission revenue, which is inconsistent with client B's personal objective of minimising their investment costs.

What are the relevant provisions?

2 The key legislative provision on conflicts of interest is the proposed obligation on licensees to have in place adequate arrangements to manage conflicts of interest: proposed s912A(1)(aa).

Note: The conflicts management obligation requires that licensees "have in place adequate arrangements for the management of conflicts of interest that may arise wholly, or partially, in relation to activities undertaken by the licensee or a representative of the licensee in the provision of financial services as part of the financial services business of the licensee or the representative": Schedule 10, Draft CLERP 9 Bill.

3 The conflicts management obligation will impose for the first time a direct and specific statutory obligation on licensees to have adequate arrangements to manage conflicts of interest. This paper explains how we expect licensees to comply with that obligation when it takes effect. We understand that the obligation will not commence until 1 July 2004 at the earliest.

4 Some existing licensee obligations also deal with conduct that is affected by conflicts of interest. These include prohibitions and other obligations (eg mandatory disclosures). This paper may assist licensees in their compliance with these existing obligations, which include:

(a) the licensee's obligation to operate efficiently, honestly and fairly (s912A(1)(a));

(b) the licensee's obligation to comply with financial services laws and to take reasonable steps to ensure their representatives do likewise (s912A(1)(c) and (ca));

(c) the obligation to disclose benefits and relationships in a Financial Services Guide (FSG) before providing financial services to retail clients (s941A and 941B);

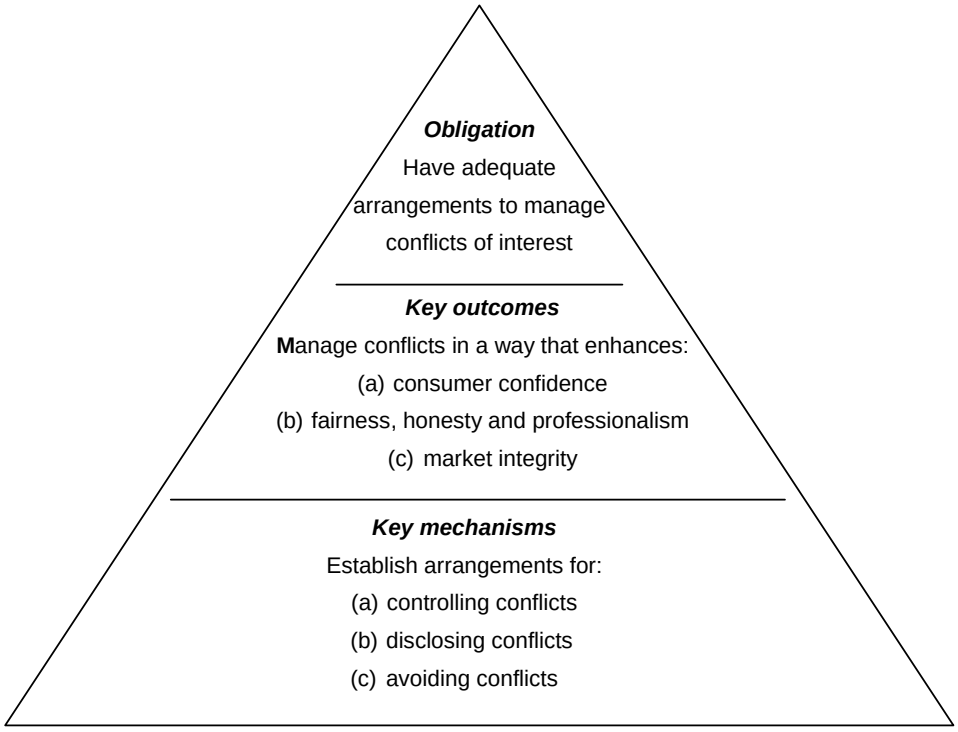
(d) the obligation to disclose benefits and relationships in a Statement of Advice (SOA) when providing personal financial product advice to retail clients (s946A);

(e) a range of prohibitions, including for misleading or deceptive conduct in the provision of financial services, dishonest conduct, unconscionable conduct and insider trading; and

(f) the duties of the responsible entity of a registered managed investment scheme, including acting in the best interests of the members of the scheme (s601FC).

Key outcomes

5 We believe that there are a number of *key outcomes* and *key mechanisms* that underpin the proposed conflicts management *obligation*. The interrelationship between these three concepts is shown in the diagram below.



6 Without adequate arrangements for managing conflicts of interest, there is a real risk that a licensee's fairness, honesty and professionalism in providing financial services to clients may be significantly compromised because:

(a) financial services may be provided that are not in the best interests of the clients (as a result of competing interests of licensees and their representatives);

(b) clients will not be in a position to make an informed decision about whether to obtain financial services from a particular provider or whether to rely on the services provided;

(c) licensees whose interests conflict with those of the client may take advantage of that client in a way that diminishes confidence in the market; and

(d) licensees may use their position to profit at the expense of particular clients or participants generally in the market.

Key mechanisms

7 We will take into account the three key outcomes of the licensing regime in policy proposal paragraph A2 when administering the conflicts management obligation. Licensees should take reasonable steps to ensure they achieve these key outcomes. This includes having appropriate mechanisms (ie measures, processes and procedures) in place to ensure that these outcomes are achieved.

8 We expect that licensees will generally use the three key mechanisms in policy proposal paragraphs A3–A6 to achieve these outcomes. This paper provides some specific proposals and guidance on the application of these mechanisms in Section B. The schedules contain additional information on:

(a) issues that we expect all licensees to consider in complying with the conflicts management obligation (see Schedule 1); and

(b) some additional matters that we expect research report providers to consider in complying with the conflicts management obligation (see Schedule 2). This might also include some useful considerations for other licensees – depending on their facts and circumstances.

Note: For more information on our approach to implementing appropriate measures, processes and procedures to achieve the regulatory outcomes of the licensing regime (including a discussion on tailoring processes to the nature, scale and complexity of the licensee's business), see Policy Statement 164 *Licensing: Organisational capacities* at [PS 164.43]–[PS 164.55].

Controlling conflicts

9 Licensees should ensure that, regardless of the presence of conflicts, their services are provided in a way that clearly demonstrates fairness, honesty and professionalism. Obviously licensees legitimately expect a return for the services they provide (eg fees). However, this needs to be done in a manner that does not involve treating the client unfairly (eg fees need to be disclosed in a transparent way). We acknowledge that, in some limited situations, the nature of the financial service being provided is such that the licensee will necessarily profit at the expense of the client they are dealing with (eg market making).

Disclosing conflicts

10 Confident and informed participation by consumers in the financial services market depends on adequate disclosure. Disclosure is a key mechanism that licensees should use in managing conflicts: see policy proposal paragraph A5. Licensees should make sufficient disclosure to their clients of any conflicts that may affect the financial services they provide.

Avoiding conflicts

11 The conflicts management obligation does not generally prohibit conflicts of interest; it requires adequate arrangements to manage conflicts. However, in some situations, the only appropriate response to a particular conflict will be to avoid it: see policy proposal paragraph A6. In assessing whether a particular conflict should be avoided, a licensee should consider both:

(a) the impact of the conflict on the consumer or licensee; and

(b) the likelihood of the conflict occurring.

12 This is part of the process of identifying, assessing and deciding upon the appropriate response to a particular conflict: see policy proposal paragraph B3. Where the impact of the conflict on the consumer or licensee is substantial or the likelihood of the conflict occurring is great, it is more likely that disclosure and internal controls will not be adequate to manage the conflict.

Note: For example:

(a) licensees should not permit their staff to offer to publish or give positive advice about a particular financial product issuer, or include their product on a recommended list, solely in return for continuing business from that issuer; and

(b) licensees should not disclose pending client orders to third parties (eg to enable those third parties to trade ahead of the client).

Industry standards, practices and codes

13 In administering the law, we often take into account whether a licensee complies with established industry practices or standards, as well as what the law explicitly requires: see [PS 164.22]–[PS 164.24].

International approaches

14 In a number of countries, as part of their general duty of care to clients, licensed advisers, their representatives, or equivalents, are obliged to manage and disclose conflicts of interest. For example, the following jurisdictions have comparable conflicts of interest management obligations:

(a) United States (common law duty, s206 of the *Investment Advisers Act* and Rule 204–3 ("Brochure Rule"));

(b) Canada (common law duty, and s40 and 223(1) of the *Securities Act*);

(c) United Kingdom (Financial Services Authority *Handbook*, Conduct of Business, Section 7.1);

(d) Hong Kong (paragraph 10.1 of the *Code of Conduct for Persons Registered with the Securities and Futures Commission*); and

(e) Singapore (s27 of the *Financial Advisers Act*).

15 The Technical Committee of the International Organization of Securities Commission published a *Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest* on 25 September 2003 (see paragraph 13 of Schedule 2). Further, a number of countries have more specific conflicts management obligations for securities analysts (eg recent rules introduced by the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE)). These are also described in Schedule 2.

B How can licensees manage conflicts of interest?

Policy proposal	Your feedback
Achieving the key outcomes	
B1 Under the conflicts management obligation, licensees will be specifically obliged to have adequate arrangements for managing conflicts of interest. Arrangements that are not consistent with the proposals in this section are unlikely to be adequate and will expose licensees to a greater risk of regulatory action.	
Retail and wholesale clients	
B2 Licensees' obligations to manage conflicts of interest will not depend on whether their clients are retail or wholesale. Therefore, the proposals in this paper do not distinguish between licensees providing services to wholesale clients and those providing services to retail clients.	**B2Q1** Should some or all of the proposals in Section B differentiate between retail and wholesale services? Please give details.
Controlling conflicts	
Ensuring arrangements are adequate	
B3 Licensees should have measures, processes and procedures to: **(a)** identify conflicts of interest; **(b)** assess and evaluate those conflicts; **(c)** decide upon and implement an appropriate response to those conflicts (which may include disclosing and/or avoiding them: see policy proposal paragraphs B10–B13); and	**B3Q1** Are there any measures, processes or procedures that we should expect most or all licensees to have in place? Please give details. **B3Q2** Are there any practical problems with the application of this proposal to particular financial services? Please give details.

Policy proposal	Your feedback
(d) ensure that, regardless of any conflicts, the quality of the financial services they provide is not significantly compromised.	
B4 Generally, we consider that the quality of *financial product advice* is significantly compromised if an adviser without the conflict of interest would be likely to have provided materially different advice in similar circumstances. Note: We do not propose, at this stage, to give specific guidance on when the provision of financial services other than advice has been significantly compromised.	**B4Q1** Are there any practical problems with this proposal? Please give details. **B4Q2** Is guidance needed for situations where the provision of services other than advice is significantly compromised? Please give details.
Ensuring arrangements are implemented and maintained	
B5 Licensees should ensure that the measures, processes and procedures they adopt are: **(a)** approved and endorsed by the owners or senior management of the licensee; **(b)** designed or tailored for the nature, scale and complexity of the licensee's business; **(c)** effectively implemented; **(d)** regularly monitored and reviewed, and updated as needed (including taking appropriate action where non-compliance is identified); and **(e)** overseen by a specific person (or persons) who takes responsibility for their implementation and monitoring.	**B5Q1** Are there other key features of effective and efficient arrangements that we should expect most or all licensees to have in place? Please give details. **B5Q2** Are there any practical problems with the application of this proposal to particular financial services? Please give details.
B6 Licensees should ensure that their internal structures and reporting lines enable them to effectively manage conflicts of interest.	**B6Q1** Are there any minimum features of effective internal structures and reporting lines we should expect most or all licensees to have in place? Please give details.

Policy proposal	Your feedback
Considering remuneration	
B7 Licensees should consider whether their remuneration practices (including non-monetary benefits) are consistent with the provision of financial services in a fair, honest and professional manner. Licensees' conflicts of interest management arrangements should ensure that remuneration practices do not result in the provision of financial services being significantly compromised.	**B7Q1** Are there any minimum features of responsible remuneration practices we should expect most or all licensees to have in place? Please give details. **B7Q2** Should we give further guidance about responsible remuneration practices? Please give suggested guidance.
B8 In many cases, disclosure is an appropriate mechanism to address conflicts of interest arising from remuneration practices. However, remuneration practices that place the interests of the licensee or its representatives in direct and significant conflict with those of the licensee's clients should be avoided (and not merely disclosed).	**B8Q1** Are there any practical problems with the application of this proposal to particular financial services? Please give details. **B8Q2** Are there any circumstances where direct and significant conflicts cannot reasonably be avoided? If so, how can licensees ensure that the interests of consumers are fully protected?
Treating clients fairly	
B9 Licensees should ensure that they and their representatives do not: **(a)** provide financial services in a manner calculated to put the interests of the licensee (or its representatives) ahead of their clients; **(b)** provide financial services in a way calculated to put the interests of one client ahead of other clients; or **(c)** use knowledge about their clients to advance their own interests without sufficient disclosure to and consent of any affected clients.	**B9Q1** Are there any practical problems with the application of this proposal to particular financial services? Please give details. **B9Q2** Are there other types of unfair treatment we should expect licensee to avoid? Please give details.

Policy proposal	Your feedback
Disclosing conflicts	
Timely, prominent, specific and meaningful	
B10 Licensees should ensure that they provide clients with sufficient disclosure about conflicts of interest. Disclosure should: **(a)** be timely, prominent and specific; **(b)** occur before or when the financial service is provided and refer to that specific service; and **(c)** contain enough detail for the client to understand the potential impact of the conflict on the financial service.	**B10Q1** Are there any practical problems with the application of this proposal to particular financial services? Please give details. **B10Q2** Are there any other minimum features of effective disclosure we should expect of most or all licensees? Please give details. **B10Q3** Should these disclosure expectations be set out in a licence condition? Why or why not?
Specific disclosure	
Financial product advice	
B11 When providing financial product advice, disclosures on the following matters will generally be appropriate: **(a)** the extent to which (if at all) the licensee has a legal or beneficial interest in the financial products that are the subject of the financial product advice; **(b)** the extent to which (if at all) the licensee is related to or associated with the issuer of the financial products that are the subject of the financial product advice; and **(c)** the extent to which (if at all) the licensee is likely to receive (financial or other) benefits from the advice or how it is followed.	**B11Q1** Is disclosure of any of these matters not appropriate? Please give reasons. **B11Q2** Are there any other matters that we should expect most or all licensees to disclose? Please give reasons. **B11Q3** Should these disclosure expectations be set out in a licence condition? Why or why not?

Policy proposal	Your feedback
Note 1: This list is not an exhaustive list of all relevant matters. What is appropriate conflicts of interest disclosure will depend upon all of the circumstances. Note 2: Similar disclosures are already required before financial product advice is given to retail clients (in a Financial Services Guide) and when personal financial product advice is given to retail clients (in a Statement of Advice): see Policy Statement 175 Licensing: *Financial product advisers — Conduct and disclosure* [PS 175].	
### Other financial services	
B12 At this stage, we do not propose specific guidance about conflicts of interest disclosures for other financial services. What is appropriate disclosure will depend on all of the facts and circumstances.	**B12Q1** Should guidance on conflicts disclosure be given for financial services other than financial product advice? Please give details.
## Avoiding conflicts	
B13 Some conflicts of interest cannot be adequately addressed by controls and/or disclosure. In some cases, the continuing presence of a conflict (even where disclosed) will be incompatible with the fair, honest and professional provision of the affected services. If so, licensees should either: **(a)** decline to provide the affected financial service; or **(b)** ensure that the conflict is avoided entirely.	**B13Q1** Are there any minimum expectations we should have of most or all licensees about avoiding conflicts? Please give details.
## Record keeping	
B14 Licensees should document their arrangements for managing conflicts of interest. We are considering imposing a licence condition requiring licensees to do this. This documentation may be kept electronically.	**B14Q1** In what circumstances (if any) is a licence condition not appropriate? How would effective compliance processes be maintained in these circumstances?

Policy proposal

B15 We also are considering imposing a licence condition requiring licensees to keep records of their compliance with their conflicts of interest management arrangements for at least seven years. This would include records of:

(a) actions taken about particular conflicts;

(b) breaches of the licensee's conflicts management arrangements;

Note: For example, licensee should keep a copy of its breach register on conflicts of interest matters.

(c) reports given to the licensee's owners or senior management about conflicts matters; and

(d) conflicts disclosures given to clients or the public as a whole.

Note: For example, a licensee should keep copies of written conflicts disclosures given to individual clients or otherwise made available (eg on a website).

These records and documents may be kept electronically.

Your feedback

B15Q1 In what circumstances (if any) is seven years not appropriate? What would be a more appropriate period and why?

B15Q2 In what circumstances (if any) is a licence condition not appropriate? How would efficient dispute resolution and compliance processes be maintained in these circumstances?

B15Q3 In what circumstances are keeping records of verbal conflicts disclosure not reasonably practicable? Please give details.

Explanation

Achieving the key outcomes

1 Licensees will need to control, disclose and avoid conflicts to consistently comply with the conflicts management obligation. This paper describes our broad expectations on compliance with that obligation. We do not think that we can, or should, provide exhaustive guidance on how licensees should comply. However, Schedule 1 sets out a number of practical issues that licensees should consider in complying with the conflicts of interest management obligation. We will take these into account in our administration of the licensing regime.

2 Under the law, licensees are responsible for ensuring that they comply on an ongoing basis with their obligations (and for ensuring that their representatives comply). Licensees have to determine on an ongoing basis what mechanisms (measures, processes and procedures) they need to have in place to ensure they maintain adequate conflicts of interest management arrangements.

3 Conflicts of interest affect both retail and wholesale clients. It is important that conflicts are controlled, disclosed and (as necessary) avoided in dealings with wholesale clients. This is consistent with the focus in Chapter 7 of the Corporations Act on matters beyond consumer protection: see policy proposal paragraph A2.

4 This section provides guidance on the management of conflicts of interest using the three key mechanisms of controlling, disclosing and avoiding conflicts. The table below provides an overview.

1 Controlling conflicts	2 Disclosing conflicts	3 Avoiding conflicts
• Ensure arrangements are implemented and maintained • Identify and assess conflicts • Make decisions about and respond to conflicts • Consider benefits and remuneration • Treat clients fairly • Ensure the quality of services are not significantly compromised	• Ensure disclosure is timely, prominent, specific and meaningful • Give disclosure in writing or verbally • Disclosure obligation applies to both retail and wholesale clients	• Avoid those conflicts that cannot be adequately addressed by controlling or disclosing conflicts of interest

Controlling conflicts

Ensuring arrangements are adequate

5 The conflicts management obligation will apply to all licensees and all conflicts of interest relevant to the licensee's financial services business (other than conflicts of interest that are wholly outside the financial services business of the licensee).

6 The obligation requires "adequate" conflicts management arrangements, that is "it will require internal policies and procedures for preventing and addressing potential conflicts of interests that are robust and effective": Commentary on the Draft Provisions at paragraph 585. We do not consider that arrangements are adequate unless they enable the licensee to consistently and effectively manage conflicts of interest. Where there are systematic breaches, we will generally assume that conflicts management arrangements are inadequate.

7 Conflicts management arrangements need to be documented in some way. Because the nature, scale and complexity of licensees' businesses will vary, the measures, processes and procedures they need to adopt will vary according to their business.

Note 1: For more information on our approach to how the Corporations Act applies to a wide variety of licensees, see Policy Statement 164 Licensing: Organisational capacities at [PS 164.11]–[PS 164.18].

Note 2: We are considering imposing a licence condition requiring documentation of conflicts management arrangements: see policy proposal paragraph B14.

8 Licensees should have monitoring and reporting procedures in place so that conflicts can be identified, assessed, monitored, and any breaches can be reported and acted upon. Licensees should record action taken on breaches. Arrangements that are not monitored and enforced are unlikely to be adequate.

Note 1: For example, arrangements could include measures such as:

(a) meetings with affected staff or clients;

(b) periodic reviews of business operations by an internal or external auditor or other person independent from the business unit; and

(c) periodic reviews of client files and records of services provided.

Note 2: We are considering imposing a licence condition requiring record keeping about conflicts of interest: see policy proposal paragraph B15.

9 Licensees should ensure that the fairness, honesty and professionalism of the financial services they provide are not significantly compromised

by conflicts of interest. To do this, they should ensure that the services they provide are not of significantly lower quality than those that could be reasonably expected from a person unaffected by the relevant conflict.

Note: An example of significant reduction in service quality is where adviser A stands to materially gain from client B purchasing a financial product and adviser A recommends the purchase, whereas a reasonable adviser not affected by the same conflict would not have done so.

Ensuring arrangements are implemented and maintained

10 Merely having or possessing conflicts management arrangements is insufficient. To be adequate, the arrangements must be implemented, maintained and followed.

Note 1: Licensees should consider how their conflicts management arrangements are communicated to their key stakeholders. Licensees may wish to make their conflicts management arrangements publicly available.

Note 2: "A stockbroker employing brokers cannot supervise each dealing they make as they make it. It can, however, set down policies … Policies, however, are worthless without systems and people in place to enforce those policies by checking from time to time that they are being applied." *Rahmat Ali v Hartley Poynton Ltd* [2002] VSC 113 per Smith J at paragraph 365.

11 It is important that a licensee's conflicts management arrangements are designed with their particular circumstances in mind. We encourage licensees to ensure that their conflicts management arrangements are tailored to their particular circumstances.

12 Primary responsibility for ensuring compliance with the licensee obligations rests with the senior management or owners of a licensee. These officers should satisfy themselves that the conflicts management arrangements are adequate. A licensee's conflicts management arrangements should be approved by its senior management (eg owners or governing body).

Note: For more information on our approach to internal compliance structures and responsibilities, see [PS 164.51]–[PS 164.53].

Effective implementation

13 It is important that internal structures and reporting lines support a licensee's management of conflicts of interest. Licensees should consider how their organisational structure, physical layout and reporting processes affect managing their conflicts.

Note: For example, licensees should consider whether it is appropriate to have:

(a) advisory staff reporting to marketing staff;

(b) "stand-alone advice" units within the organisation in the same physical location as sales or investment management staff; or

(c) compliance or internal audit staff reporting to a business unit.

14 A licensee's monitoring and supervision procedures need to take into account conflicts of interest management issues. This includes:

(a) identifying and assessing conflicts of interest between the licensee and clients;

(b) identifying and assessing conflicts of interest between representatives of the licensee and clients; and

(c) ensuring that appropriate action is taken if conflicts are identified.

15 Depending on the circumstances and the nature of the conflict, it may be appropriate to:

(a) fully disclose the conflict to the relevant client(s) and obtain their informed consent;

(b) allocate another representative to service the particular client;

(c) decline to provide services to the particular client; or

(d) initiate internal or external disciplinary action (eg referring the matter to a professional body or regulator) where a representative has behaved inappropriately.

Note: This is not an exhaustive list. What is an appropriate response to a given conflict of interest will always depend on the facts and circumstances.

16 The person who is deciding what is an appropriate action to take on a conflict of interest should not be significantly affected by the conflict themselves.

17 A licensee must monitor and supervise the activities of representatives to ensure they are complying with the financial services laws: see s912A(1)(ca) and [PS 164.19]–[PS 164.21].

Considering remuneration

18 Chapter 7 of the Corporations Act generally approaches remuneration issues from a disclosure perspective (ie remuneration practices must be fully disclosed). The law does not prohibit all conflicts; rather, in many cases, it envisages conflicts will be present and will be disclosed to clients. However, licensees should also consider whether any particular benefits, compensation or remuneration practices are inconsistent with

the provision of financial services in a fair, honest and professional manner.

Note 1: The need for robust conflicts management arrangements is likely to be higher where a licensee relies heavily on commission-based remuneration.

Note 2: When providing personal advice to retail clients, advisers are specifically obliged to ensure their advice is appropriate (regardless of remuneration or other issues): see Section D of [PS 175].

Treating clients fairly

19 The principles in policy proposal paragraph B9 relate to the behaviour of both licensees and their representatives. Licensees are responsible for their own conduct and that of their representatives. The conflicts management arrangements of a licensee need to take this into account.

20 Licensees are generally in a position of trust with their clients and should not take advantage of this. As far as possible, licensees (and their representatives) should avoid placing themselves in a position where there is a material conflict between their own interests and those of their clients. This is to minimise the risk that the licensee will be tempted to prefer their own interests to those of their clients.

21 Licensees need to manage conflicts between the interests of various clients (existing or potential clients) as well as conflicts between the licensee's own interests and those of their clients. Generally, they should not provide financial services in a manner calculated to advance one client's interests unfairly ahead of other clients' interests.

Disclosing conflicts

22 Disclosure is a key mechanism that licensees should use in managing conflicts: see policy proposal paragraph A5. Together with internal controls, disclosure will often be adequate to manage a conflict of interest.

23 Having adequate arrangements in place to manage conflicts of interest "will include ensuring that there is adequate disclosure of conflicts to investors, who can then consider their impact before making investment decisions": Commentary on the Draft Provisions at paragraph 585. In our view, licensees will need to disclose conflicts of interest to consistently comply with the conflicts management obligation.

Timely, prominent, specific and meaningful

24 Conflicts of interest disclosure should be timely, prominent, specific and meaningful. In our view, "boilerplate" disclosure is unlikely to satisfy the conflicts management obligation. In order to be effective,

conflicts of interest disclosure should refer to the specific service to which it relates and should be specific enough for the client to understand the potential impact of the conflict of interest on the service. Disclosures may be given in writing or verbally.

Specific disclosure

Financial product advice

25 Specific conflicts of interest disclosures should be given when financial product advice is provided. Such disclosures should be given before or at the time the service is provided, and may be given in writing or verbally. Licensees should provide the disclosure in the same form as the advice (eg written disclosures where the relevant advice is in writing).

Note: This paper does not consider in any detail the conflicts of interest disclosures that must be given under the law when personal financial product advice is provided to retail clients. For our guidance and expectations on conflicts of interest disclosures to retail clients in an FSG or SOA, see Sections B and D of [PS 175] respectively.

26 The content of disclosures concerning the provision of advice will vary depending on the circumstances. However, it is generally accepted that there is a conflict of interest where a licensee (or representative):

(a) has an interest in the subject matter of their advice;

(b) is related to or associated with the issuer of the financial product that is the subject of their advice; or

(c) is likely to receive benefits or remuneration in relation to the advice or how it is followed.

While these conflicts of interest will not necessarily cause the advice to be significantly compromised, they should be brought to the client's attention. The client can then decide whether the conflicts of interest are significant and to what extent they will rely on the advice.

Note: For example:

(a) a product issuer, in giving advice about its own product, should identify itself as both the adviser and product issuer; and

(b) a licensee in a group that is owned by a product issuer, in giving advice about the product issued by that product issuer, should disclose this relationship when giving the advice.

Other financial services

27 We are not currently proposing specific guidance or expectations regarding disclosure of conflicts for financial services other than financial product advice. Although policy proposal paragraph B11 may provide useful guidance, we believe that licensees are in the best position to

determine how they disclose conflicts of interest for these services. These disclosures may be given in writing or verbally.

Note: For example, we would generally expect market makers to disclose their status as a market maker to other persons with whom they transact.

Avoiding conflicts

28 Licensees may need to avoid certain conflicts of interest between their interests and the interests of their clients to ensure that the quality of their financial services is not significantly compromised by the conflicts: see policy proposal paragraph A4. The fact that managing conflicts will at times involve avoiding conflicts has been generally accepted in most jurisdictions.

Note 1: For example, where an adviser is significantly affected by conflicts of interest for particular financial product advice, the adviser may need to decline to provide the advice.

Note 2: For example, licensees should not disclose pending client orders to third parties (eg to enable those third parties to trade ahead of the client). The most obvious way of avoiding this conflict is to ensure that information about pending client orders is not communicated to third parties.

Record keeping

29 We expect that licensees will document their arrangements for the management of conflicts of interest. Licensees should also keep records of steps taken to manage conflicts and breach notifications. It is highly unlikely that a licensee could comply with the conflicts management obligation without documenting their conflicts management arrangements and keeping these records. Documentation allows a licensee to demonstrate (either to ASIC or others) that they know whether or not they are complying with the licensee obligations (eg the conflicts management obligation).

30 We are considering imposing a licence condition requiring licensees to ensure that these documents and records are kept for at least seven years. We recognise that other legislation, standards or good practice may necessitate longer record-keeping periods in some cases.

31 Each licensee will need to consider how best to keep these documents and records. Documents and records may be kept electronically.

32 Licensees should consider what records of verbal disclosures should be kept to assist them in reviewing compliance with their conflicts obligations. They should consider how they will demonstrate their compliance with these obligations in the event of a review (either by the licensee, its auditor or ASIC). For example, they may wish to keep copies of verbal disclosure “scripts” used by their representatives.

Schedule 1: Licensees generally — Issues to consider

In the final policy following this paper, we propose to include a list of issues that we suggest licensees consider in complying with the conflicts management obligation. The table below is a sample of a possible list of issues.

We encourage licensees to consider this list in managing conflicts of interest. It is not suggested that all the matters in this table are relevant to every particular licensee or that they are exhaustive. Licensees should determine which matters are relevant to their business. These are the types of matters that we propose to consider in assessing Australian financial services (AFS) licence applications and when carrying out surveillance. We will review them in light of our experience in administering the Corporations Act.

Your feedback

Q1.1 Are there any issues set out in this schedule that are not appropriate for us to expect some or all licensees to consider? Please give details.

Q1.2 Are there any important issues missing from this schedule that we should expect some or all licensees to consider in complying with s912A(1)(aa)? Please give details.

Mechanism	Issues to consider
Controlling conflicts	• What are your procedures for identifying conflicts of interest? • How well do your conflicts management arrangements enable you to identify and assess conflicts? • How well do your conflicts management arrangements enable you to decide how to respond to or deal with particular conflicts? • Are your conflicts management arrangements documented (eg do you have a written conflicts management policy)? • When were your conflicts management arrangements last updated? • When were your conflicts management arrangements last reviewed internally or by a third party (eg an auditor)? • What structural arrangements do you have in place to manage conflicts of interest? • How does your organisation's structure support your management of conflicts of interest? • What information barriers do you have within your organisation to manage conflicts of interest? • How do your conflicts management arrangements ensure that conflicts do not significantly reduce the integrity or quality of the services you provide? How do you test their effectiveness in achieving this? • How do your conflicts management arrangements ensure that your clients are not treated unfairly? How do you test their effectiveness in achieving this? • How were your conflicts management arrangements formulated and approved? Were they approved by your owners, board or governing body (or a delegated body)? If not, why not? • How are your conflicts management arrangements communicated to staff and other stakeholders (including clients, customers, and the public)? • Is a nominated person (or persons) responsible for your compliance with these arrangements? Who do they report to? • How are breaches of your conflicts management arrangements dealt with? How are they recorded and reported to your governing body? • What impact do your remuneration and benefits practices have on your management of conflicts? • How do you ensure your remuneration and benefits practices do not result in the integrity and quality of the services you provide being significantly compromised?

Mechanism	Issues to consider
	• How do your dealing or trading practices affect your management of conflicts? • How do you ensure that your dealing or trading practices do not significantly compromise the quality of services you provide?
Disclosing conflicts	• What are your procedures for disclosing conflicts of interest to affected clients? • How do your conflicts management arrangements ensure that your clients receive sufficient and specific disclosure about conflicts? • How do you ensure these procedures are followed consistently and at all times? • How do you ensure that disclosures of conflicts are timely, prominent, specific and meaningful? • What disclosures do you give for personal financial product advice? • What disclosures do you give for general financial product advice? • What disclosures do you give for other financial services? • Do your disclosures vary between wholesale and retail clients? How?
Avoiding conflicts	• What are your procedures for assessing the seriousness of a conflict of interest? • How do you ensure that more serious conflicts are referred to owners or managers? • In what circumstances do you avoid conflicts of interest (as opposed to dealing with them via disclosure or other internal controls)? How are these decisions made and recorded?

Schedule 2: Research report providers — Issues to consider

Note: While not all of this schedule will be relevant to other licensees, they may wish to consider how this guidance may apply, with appropriate modifications, to their own operations.

1 The policy proposals in Sections A and B of this paper focused on broad principles and guidance for licensees generally in managing conflicts of interest, and set out expectations that licensees should meet to ensure that they comply with the conflicts management obligation (proposed s912A(1)(aa)). This schedule builds on those expectations and sets out additional guidance and expectations for research report providers on:

(a) our general approach to conflicts management (see paragraphs 4–18);

(b) controlling and avoiding conflicts (see paragraphs 19–42); and

(c) disclosing conflicts (see paragraphs 43–52).

2 This schedule focuses on research report providers, being licensees who provide research reports. We expect licensees to implement the measures in this schedule, including by referring any of their staff that are involved in the provision of research reports (research staff) to this schedule.

Note: "Research report provider" and "research report" is defined in paragraph 4 below.

3 Our views on conflicts of interest management by research report providers are more advanced than our views in some other areas. This is a result of significant recent developments, including:

(a) the Government's Corporate Law Economic Reform Program (CLERP) Paper No 9 Discussion Paper "Corporate disclosure: Strengthening the financial reporting framework" (CLERP 9) and the Exposure Draft Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 (Draft CLERP 9 Bill);

(b) "Research analyst independence", ASIC surveillance report, 22 August 2003;

(c) the Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest Principles published by the

Technical Committee of the International Organization of Securities Commissions on 25 September 2003; and

(d) the Australian Stock Exchange's draft Guidance Note "Independence of research, disclosure of conflicts of interest and dealing before research recommendations" ("ASX draft Guidance Note");

(e) the Securities Institute of Australia and the Securities and Derivatives Industry Association "Best practice guidelines for research integrity" ("SIA/SDIA Guidelines");

(f) a number of US Congressional hearings, the introduction of the Sarbanes-Oxley, and a number of high profile prosecutions/ settlements involving major US investment banking firms (including New York Attorney-General Eliot Spitzer's campaign); and

(g) a number of initiatives by international regulators and industry representatives (including US Securities and Exchange Commission's Regulation AC, the recent New York Stock Exchange and National Association of Securities Dealers rules governing analysts, the European Union's revision of the Investment Services and Market Abuse Directives, the Committee of European Securities Regulator's advice to the European Commission regarding implementing measures on publication of research reports, the UK Financial Services Authority' Consultation Paper *Conflicts of Interest: Investment Research and Issues of Securities* (CP 171), the Hong Kong Securities and Futures Commission's survey on investment research activities and various industry best practice recommendations and standards).

Your feedback

We have included a number of questions for your feedback in this schedule. We are also interested in general feedback on this schedule, including whether it would be helpful to set out the guidance and expectations in the schedule in a stand-alone document (eg a "guide" on conflicts of interest management for research report providers).

Contents

A Our general approach

What is a research report?

4 For the purposes of this schedule, a research report is general advice about a financial product with an investment component that is not prepared for any particular client. This definition applies regardless of whether the report is provided to retail or wholesale clients. We will not treat general advice provided by an issuer about its own financial products as a research report. Licensees who carry on a business of preparing and providing research reports are referred to in this paper as "research report providers".

Note: For example, a report provided by a securities analyst, research house or credit rating agency would generally be a research report. A letter containing general advice provided to a specific named client would not be a research report.

5 Personal advice and reports that do not involve financial product advice are excluded from the definition of research report used in this schedule.

Note: A specific statutory regime dealing with disclosure of conflicts of interest applies to personal advice: see Part 7.7, Division 3 and Policy Statement 175 *Licensing: Financial product advisers — Conduct and disclosure* [PS 175]. Reports that do not involve financial product advice are beyond the scope of most of Chapter 7 and therefore are not included in the definition of research report for the purposes of this policy proposal paper.

6 Our focus is on the output (the research report) and not the identity of the provider. Whether the provider is someone generally known as a securities or research analyst is immaterial for the purposes of this definition. What is important is whether the relevant person provides research reports. Consistent with this focus, the guidance in this schedule applies to research reports provided to retail clients, wholesale clients, or both.

7 Generally, the guidance in this schedule is directed towards research report providers carrying on a financial services business in Australia: s911D. This includes foreign research report providers who provide research reports to Australian clients. It does not include foreign research report providers who provide research reports to their related Australian companies only. However, if the Australian related company provides those research reports to Australian clients, the guidance in this schedule would be relevant to that service (ie the service provided to the Australian client).

Note: See also paragraphs 13–18 on international standards. We note that different definitions of research are adopted in the NYSE/NASD rules, SEC Regulation AC and the proposed UK rules (CP 171, Annex 7).

Your feedback

Q2.1 Should the definition of research report be limited to:

(a) financial products with an investment component (as compared to all financial products)?

(b) broadly disseminated general advice (as compared to all general advice)?

(c) reports containing detailed analysis and research (as compared to all reports)?

(d) reports provided to retail clients only (as compared to all clients)?

(e) reports containing recommendations, ratings or valuations (as compared to all reports)?

Please give reasons for your answers to each part of this question.

Compliance

8 Under the law, a licensee is responsible for ensuring it complies on an ongoing basis with its obligations as a licensee (and for ensuring its representatives comply). Therefore licensees have to determine on an ongoing basis what mechanisms (measures, processes and procedures) they need to have in place to ensure they maintain adequate arrangements and satisfy the general outcomes intended by the licensee obligations.

9 In this schedule, we describe various issues that we believe research report providers should address in their conflicts management arrangements. Research report providers should take these issues into account in the design, implementation and maintenance of their conflicts management arrangements.

10 We propose to take this schedule into account in administering the conflicts management obligation and in considering whether to take action in relation to any particular licensee. In our view, licensees whose conflicts management arrangements are not consistent with the guidance and expectations in this schedule are unlikely to be complying with the conflicts management obligation and will be exposed to a greater risk of regulatory action.

Your feedback

Q2.2 Do you agree with this approach? Please give details.

Q2.3 Are there any practical problems with the proposed approach? Please give details.

Interaction with other standards and guidance

Australian

11 We acknowledge the work done by:

(a) the Securities Institute of Australia (SIA) and the Securities and Derivatives Industry Association (SDIA) in developing "Best practice guidelines for research integrity" (November 2001); and

(b) the Australian Stock Exchange Ltd (ASX) in developing a draft Guidance Note "Independence of research, disclosure of conflicts of interest and dealing before research recommendations" (February 2003). We understand that the ASX is considering finalisation of any guidance in the context of the Draft CLERP 9 Bill and this policy proposal paper.

We believe our guidance and expectations are generally consistent with the standards and draft guidance previously published by these organisations.

Note: See also ASIC surveillance report "Research analyst independence" at paragraphs 1.10 and 6.8.

12 We acknowledge that on some topics this schedule is more detailed or extensive than existing industry standards and guidance, and on some other topics existing industry standards and guidance may be more detailed or extensive. We expect that research report providers will take into account both this schedule, and existing industry standards and guidance.

IOSCO

13 The International Organization of Securities Commissions published a "Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest" on 25 September 2003. We have taken these principles into account in developing this schedule. We believe that this schedule and the principles are consistent. The principles in the IOSCO statement are:

(a) mechanisms should exist so that sell-side analysts' trading activities or financial interests do not prejudice their research and recommendations (principle 1);

(b) mechanisms should exist so that analysts' research and recommendations are not prejudiced by the trading activities or financial interests of the firms that employ them (principle 2.1);

(c) mechanisms should exist so that analysts' research and recommendations are not prejudiced by the business relationships of the firms that employ them (principle 2.2);

(d) reporting lines for sell-side analysts and their compensation arrangements should be structured to eliminate or severely limit actual and potential conflicts of interest (principle 3);

(e) firms that employ sell-side analysts should establish written internal procedures or controls to identify and eliminate, manage or disclose actual and potential analyst conflicts of interest (principle 4);

(f) the undue influence of issuers, institutional investors and other outside parties upon sell-side analysts should be eliminated or managed (principle 5);

(g) disclosures of actual and potential conflicts of interest should be complete, timely, clear, concise, specific and prominent (principle 6);

(h) sell-side analysts should be held to high integrity standards (principle 7); and

(i) investor education should play an important role in managing sell-side analyst conflicts of interest (principle 8).

Note: Some of these principles are addressed elsewhere in this jurisdiction. For example, analyst training is addressed in Policy Statement 146 *Licensing: Training of financial product advisers* [PS 146] and Policy Statement 164 *Licensing: Organisational capacities* [PS 164].

Other international

14 In preparing this schedule, we have considered equivalent requirements on the independence of analysts, the integrity of research reports in overseas jurisdictions and conflicts management. We believe that this schedule is generally consistent with other international standards and requirements for research report providers. We recognise that some research report providers will also be subject to foreign rules or standards for managing conflicts of interest. Each licensee will need to ensure compliance with the conflicts management obligation. However, by complying with those foreign rules or standards we expect that some licensees will be complying with most of this schedule already.

15 The UK Financial Services Authority's Consultation Paper "Conflicts of interest: Investment research and issues of securities" (CP 171) proposes a set of rule changes to the Conduct of Business Handbook. A proposed new Section 7.16 on investment research would set out guidance to relevant entities on internal management arrangements designed to avoid and manage conflicts of interest.

16 The European Union amendments to the Investment Services Directive (ISD) explicitly recognise financial analysis and research as ancillary services, where undertaken in conjunction with core investment services, thereby subjecting these services to the provisions regarding conflicts of interest and conduct of business. In addition, the Market Abuse Directive (MAD) includes a conflicts disclosure obligation that reinforces the fair presentation of research. The Committee of European Securities Regulators has also provided advice to the European Union on implementing measures relating to publication of research reports.

17 The US Securities and Exchange Commission's Regulation Analyst Certification ("Regulation AC") requires a statement by the research analyst (or analysts) certifying that the views expressed in the research report accurately reflect their personal views and that other possible influences on the integrity of the research have been managed. We have also taken into account the new conflicts management rules introduced by the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE), Rule 2711 and Rules 351, 472, respectively.

18 We are also aware of other regulatory work currently underway by, for example, the Hong Kong Securities and Futures Commission's survey of investment research activities and the "Fair Dealing" concept paper by the Ontario Securities Commission.

Your feedback

Q2.4 Are our expectations of compliance with this schedule inappropriate? Please give details.

Q2.5 Do you agree with our views about consistency with domestic and international standards? Please give details.

Q2.6 Are there any practical problems with our proposed approach to compliance with international standards? Please give details.

B Controlling and avoiding conflicts

19 Research report providers should maintain specific policies and practices for managing conflicts of interest. Australian and overseas research has shown that there is considerable potential for conflicts of interest in the production of research reports.

Note 1: See ASIC surveillance report "Research analyst independence" at paragraphs 1.9, 5.3 and 6.1–6.8.

Note 2: In July 2002, the Financial Services Authority (FSA) published a discussion paper "Investment research: Conflicts and other issues" (DP 15). The paper contained some findings of analysis of recommendations made by research analysts within investment banking firms. They found that the proportion of "buy" recommendations made by firms acting as corporate brokers/adviser to the subject company (FTSE 100 companies) is, at 80%, almost twice as high as the proportion of "buys" where the analyst does not work for the corporate broker (page 3).

20 Research report providers should take reasonable steps to ensure that conflicts of interest:

(a) do not significantly compromise the quality of their advice (in the research reports);

(b) do not result in inappropriate behaviour towards particular clients or the market generally; and

(c) are fully disclosed.

In our view, some conflicts of interest carry such a high risk of interfering with these key outcomes that they should be avoided entirely. Other conflicts, however, can be addressed by adequate controls and appropriate disclosure. These are the three key mechanisms we expect licensees generally to use to manage conflicts of interest: see policy proposal paragraph A3.

21 Research report providers, together with all other licensees, should have measures, processes and procedures to:

(a) identify conflicts of interest;

(b) assess and evaluate those conflicts;

(c) decide upon and implement an appropriate response to those conflicts; and

(d) ensure that, regardless of any conflicts, the quality of the financial services they provide are not significantly compromised: see policy proposal paragraph B3.

22 Research report providers should encourage a culture of integrity and ethical conduct among their staff, including attitudes to conflicts of interest. However, this is no substitute for implementing, maintaining and monitoring robust policies and procedures. It will generally be inadequate to entirely rely on staff integrity to address conflicts; research report providers must have tangible conflicts management arrangements in place.

Note: See ASIC surveillance report "Research analyst independence" at paragraph 6.4.

23 In administering the law, we will have regard to the nature, scale and complexity of a licensee's business.

Note: For our general approach to taking into account the nature, scale and complexity of a licensee's business, see [PS 164.17]–[PS 164.18].

Structure and general practices

24 Research report providers should maintain specific policies and practices for the management of conflicts of interest, and make these available to all staff. These policies and practices should be documented. However, it is not adequate merely to have documented practices and policies; these practices and policies need to be implemented, maintained and enforced.

Note 1: We expect that conflicts management policies will include specific reference to supervision, monitoring, review, audit and discipline matters. When reviewing compliance with the conflicts management obligation, we will consider whether there is evidence that the research report provider has active and effective conflicts management arrangements. See also Guideline 9 in the SIA/SDIA Guidelines. Research report providers should also consider how their conflicts management arrangements are communicated to their key stakeholders (eg by making them publicly available).

Note 2: Policy proposal paragraph B14 discusses a possible licence condition requiring that conflicts management arrangements be documented.

25 Generally, research report providers should maintain an organisational unit separate to the business units (eg within the compliance area) that is responsible for ensuring that conflicts management arrangements are implemented, monitored, reviewed and updated.

Note: It is important that the unit responsible for monitoring the research report providers' compliance with its conflicts management obligations is separate from the business units where the potential conflicts are likely to arise. In smaller firms, it may be an individual person rather than an organisational unit who is responsible for conflicts of interest management. However, they still need to be able to ensure that their research reports are provided in a fair, honest and professional manner.

26 Research report providers should have a communications policy that outlines appropriate and inappropriate communications practices within the organisation and with external parties.

Note: Research report providers need to pay particular attention to communications between their research staff and other staff within the organisation, and between their research staff and external organisations (particularly product issuers). The communications policy should be made clear to all staff (both research staff and others). This includes, but is not limited to, information barriers.

27 Where research report providers or their research staff provide non-research services to a product issuer, there is a potential conflict of interest. Research report providers should ensure that this conflict does not result in the quality of their research reports being significantly compromised. Possible solutions include:

(a) ensuring that research on a product issuer is not published while non-research services are being provided to the product issuer, and for a short period afterwards (ie a "quiet period");

(b) fully disclosing in relevant research reports the nature of any non-research services provided to a product issuer.

What is an appropriate solution will depend on the circumstances, the nature of the non-research services being provided, and the significance of the particular research staff member's role in providing the non-research services.

Note 1: Examples of non-research services include:

(a) underwriting a public offering;

(b) advice about the prospects for a potential public offering (including likely reception in the financial market);

(c) assistance in marketing and promoting a public offering (including participation in "roadshows" and "conference calls"); and

(d) advice on structuring and developing new financial products.

Note 2: The FSA proposes a quiet period of thirty days after an initial public offering and five days after a secondary offering: see paragraphs 4.13–4.19 of the FSA's Consultation Paper "Conflicts of interest: Investment research and issues of securities" (CP 171).

28 Robust information barriers may mean the staff preparing and authorising a research report are unaffected by the research report provider (or its other staff) providing non-research services to a product issuer. Such barriers must prevent information going to research staff if it might create a conflict of interest for them. If this is the case, a research report may be published despite non-research services being provided to the issuer. Whether the non-research services have, or are likely to have,

an impact on the preparation of research will depend upon all of the facts and circumstances.

Note: See ASIC surveillance report "Research analyst independence" at paragraphs 5.39-5.42.

29 Where research staff are also involved in receiving and executing client orders, there is the risk that they will be more inclined than an independent person to produce a research report that will stimulate increased trading activity. Research report providers should consider whether to prevent staff that prepare research reports from taking or executing client orders.

Note: See also paragraph 1.6 of the ASX draft Guidance Note.

Your feedback

Q2.7 Are there any practical problems with this guidance on structure and general practices? Please give details.

Q2.8 Are there any additional practical problems with this guidance on structure and general practices for smaller firms? Please give details and suggestions of any alternate expectations you believe we should have for smaller firms.

Q2.9 Should this guidance on structure and general practices be mandated by a licence condition? Please give reasons.

Q2.10 Should research report providers ensure that they do not publish research on issuers to whom they or their staff provide non-research services? During what period of time? Please give reasons.

Q2.11 Are there any non-research services that have such a minor impact on research that disclosure and/or information barriers are adequate responses? Please give details.

Q2.12 Should all research report providers be expected to ensure that their research staff do not accept or deal with client trading orders? Please give reasons.

Monitoring and supervision

30 Generally we will expect research report providers to ensure that staff preparing research reports are structurally and physically separated from and not supervised by staff performing an investment banking, corporate advisory or dealing function. The appropriate monitoring and supervision practices for a research report provider will depend on the nature, scale and complexity of its business.

Note: For example, where staff who prepare research reports are supervised by or report to other staff who perform an investment banking, corporate advisory or dealing function, there is a risk that the research staff will be more inclined to produce research that generates additional trading volume or is favourable to particular corporate clients. We acknowledge that smaller firms may have less capacity to fully separate research and other staff, and may need to consider other measures (eg information barriers) to ensure their research reports are provided in a fair, honest and professional manner.

31 Research report providers should ensure that research reports are reviewed and approved before publication by an experienced and independent supervisor or by a group of peers (eg review committee) to maintain the quality and integrity of reports. Reports should not be reviewed or approved by staff from another business area (eg investment banking, corporate advisory or dealing function), other than a restricted review for factual accuracy purposes. A written record should be kept of the review and approval of each research report.

Note: See paragraphs 1.1–1.2 of the ASX draft Guidance Note.

Your feedback

Q2.13 Are there any practical problems with this guidance on monitoring and supervision? Please give details.

Q2.14 Are there any additional practical problems with this guidance on monitoring and supervision for smaller firms? Please give details and suggestions of any alternate expectations you believe we should have for smaller firms.

Q2.15 Should this guidance on monitoring and supervision be mandated by a licence condition? Please give reasons.

Benefits and remuneration

32 Research report providers should ensure that decisions about the remuneration of staff preparing research reports are:

(a) made by persons not directly connected with another business unit (eg investment banking, corporate advisory, dealing and asset management units);

(b) not contingent on the introduction of new clients or retention of existing clients for the investment banking, corporate advisory or dealing units by those staff;

(c) not contingent on the volume of dealing transactions in financial products relating to research that those staff prepare; and

(d) not contingent on any particular investment banking or corporate advisory transaction, or asset management fee.

Note: Where the remuneration and other benefits of staff preparing research reports are based on, for example, introduction of new clients or retention of existing clients for the investment banking or corporate advisory units, there is a potential conflict of interest. For example, research staff may be more inclined to produce research that generates additional trading volume or is favourable to particular corporate clients. See also Guideline 6 in the SIA/SDIA Guidelines.

Your feedback

Q2.16 Are there any practical problems with this guidance on benefits and remuneration? Please give details.

Q2.17 Should this guidance on monitoring and supervision be mandated by a licence condition? Please give reasons.

Trading restrictions

33 Some types of conduct are so inconsistent with proper management of conflicts of interest that they should be avoided completely. Where research report providers provide research about products that they or their staff hold a material interest in, there is a potential conflict of interest. Research report providers should ensure that this conflict does not result in the quality of their research reports being significantly compromised. Possible solutions include:

(a) ensuring that the research report provider does not publish research on financial products that it has a material interest in;

(b) prohibiting research staff from holding or trading in financial products that they prepare or provide research on;

(c) ensuring that any holding or trading of financial products by the firm or research staff is fully disclosed in the relevant research reports (see paragraphs 43–52).

We expect that research report providers will adopt a combination of these approaches. What is an appropriate solution will depend on the circumstances. Some of these potential solutions are described in more detail in paragraphs 34–37.

Note 1: For example, a research report provider may prohibit research staff from trading in securities (or derivatives of that security) that they cover, or any securities in that industry sector (eg following the S&P/ASX GICS sector indices).

Note 2: Trading restrictions should take into account both direct and indirect interests (eg a person may have an indirect interest due to derivatives they hold, or the assets of a discretionary account that they manage).

34 Research report providers should not trade in a financial product in advance of (or shortly after) their publication of a research report about that product (ie a quiet period). Research report providers will need to assess what is a reasonable period before and after the publication of research for trading to be restricted. Quiet periods may also need to cover:

(a) discretionary trading on accounts managed by the research report providers (as well as dealings on the research report providers' own account); and

(b) dealings in derivatives of financial products that are the subject of research reports, or in other financial products closely related to the products that are the subject of the research report (eg a related company or close competitor of the product issuer).

Note: Where research report providers are aware of research reports to be published shortly, there is a risk that they will be tempted to take advantage of this knowledge and deal in the financial product that is the subject of the report before it is published. The ASX draft guidance note discussed a quiet period of thirty days before publication of a research report and five days after publication of a research report: paragraph 3.6 in the ASX draft Guidance Note.

35 Research report providers should also take reasonable steps to ensure that any staff relevantly involved in preparing the research report do not trade in advance of (or shortly after) the research report provider publishing a report about that financial product.

Note: Not all staff will have actual or constructive knowledge of a pending research report or of its content. We expect that research report providers will structure their policies and practices so that the trading restrictions apply at least to staff who are likely to know of pending research reports and their contents (eg staff preparing or approving reports). Research report providers may also want to consider measures to limit the number of persons to whom information about pending research reports is communicated.

36 Research report providers should take reasonable steps to ensure that their staff do not circumvent these trading restrictions by encouraging or arranging for other persons (eg the representative's immediate family) to deal during the quiet periods. For example, research report providers should monitor and record the trading activities of their staff (not limited to research staff). Research report providers should also consider requiring staff to obtain express permission before some or all trades in financial products covered by the research report provider.

37 To the extent that the research report itself is or involves "inside information" (as opposed to the information on which it based), trading before or shortly after its publication is likely to amount to insider trading: s1043A(1). Non-public information about the timing of and recommendations contained in future research reports may amount to inside information: s1042A. This is especially so where the report is based on information which is itself not generally available.

Note: See also paragraph 3.1 in the ASX draft Guidance Note, Guideline 5 in the SIA/SDIA Guidelines, and the Companies and Securities Advisory Committee "Insider Trading Discussion Paper" at paragraph 2.78.

38 Research report providers should also ensure that they (and staff relevantly involved in preparing the research report) do not trade inconsistently with a recommendation in one of their current research reports.

Note: Where research report providers and their staff are free to deal on their own behalf in a manner that is inconsistent with current research reports there is the risk that, for example, they will be tempted to publish research that encourages clients to acquire particular securities that they also hold (which may have the effect of increasing the market price for those securities) and then dispose of those securities at the higher price. We acknowledge that in some circumstances dealings that are not consistent with current research are acceptable (eg where the research report provider for legitimate commercial reasons needs to urgently realise its investments in a particular financial product). We expect that research report providers will have strict approval procedures for any proposed trading inconsistent with current research. See also paragraph 3.2 in the ASX draft Guidance Note, and Guideline 5 in the SIA/SDIA Guidelines.

Your feedback

Q2.18 Are there any practical problems with this guidance on trading restrictions? Please give details.

Q2.19 Should research report providers impose a general prohibition on research about financial products:

(a) held or traded by the member of staff preparing the research; or

(b) held or traded by the firm generally?

Please give reasons.

Q2.20 What is an appropriate period before and after the publication of a research report for trading to be restricted: see paragraph 34? Please give details.

Q2.21 Should this guidance on trading restrictions be mandated by a licence condition? Please give reasons.

Other steps to prevent inappropriate conduct

39 Research report providers should ensure that research reports are based on objective, verifiable facts and analysis, and not on special interests of the research report provider, product issuer or other persons. Research reports that are not based on reasonable grounds may be misleading or deceptive within the meaning of the Corporations Act: s1041H. Cases decided under the analogous ASIC Act and Trade Practices Act provisions have held that a statement of opinion by a person in their professional capacity involves an implied assertion that the opinion has a reasonable basis, is the result of the exercise of due care and skill, and is able to be relied upon.

Note: See s52 of the Trade Practices Act; *MGIGA (1992) Ltd v Kenny & Good Pty Ltd* (1996) 70 FCR 236; *RAIA Insurance Brokers Ltd v FAI General Insurance Co Ltd* (1993) 41 FCR 164; *Chiarabaglio v Westpac Banking Corporation* (1989) ATPR 40–971. See also paragraph 1.5 of the ASX draft Guidance Note.

40 To reduce the risk that research reports are not based on reasonable grounds, research report providers should ensure that each report reflects the views of its author or the relevant responsible officer who approves its publication.

Note: A research report that contains an opinion or recommendation that is not in fact held by its author or the relevant responsible officer may be misleading for the purposes of the Corporations Act: s1041H. See also paragraph 2.6 in the ASX draft Guidance Note, Regulation AC (Analyst Certification) of the US SEC and paragraphs 4.30–4.31 of the FSA's Consultation Paper "Conflicts of interest: Investment research and issues of securities" (CP 171).

41 Research report providers should ensure that favourable research or ratings are not offered, or changes to research or ratings threatened, as an inducement to secure the business of a corporate client or receive other benefits.

Note 1: For example, a research report provider should not offer to publish favourable research to solicit or retain investment banking business from a product issuer.

Note 2: It is important that product issuers and research report providers take reasonable steps to ensure that:

(a) selective disclosure is avoided; and

(b) "black-banning" or other refusals to co-operate are not threatened or used against staff that prepare research reports that are critical of or otherwise not positive about a product issuer.

42 Research report providers should also ensure that:

(a) research reports are not used to deliberately increase trading volume and revenue; and

Note: Where research report providers are able to use research reports as a way of deliberately increasing trading volume, there is a risk that, for example, they might be tempted to make a disproportionate number of "buy" and "sell" recommendations to increase trading volume.

(b) research reports or information about their contents are not communicated outside the research report provider before they publish the report in the normal course of business.

Note 1: Otherwise, staff could circumvent the trading restrictions, for example, by simply communicating some or all of the content of a research report to a third party. This may also amount to insider trading: see paragraph 37.

Note 2: This does not mean that checking the factual accuracy of parts of a research report with a product issuer cannot take place before publication. We expect that this would be done in a carefully controlled way (eg without communicating the recommendations or opinions also contained in the report).

Your feedback

Q2.22 Are there any practical problems with this guidance on other steps to prevent inappropriate conduct? Please give details.

Q2.23 Should this guidance on other steps to prevent inappropriate conduct be mandatory? If so, how?

C Disclosing conflicts

Specific disclosure

43 Research reports are, by their nature, likely to be relied upon by retail and wholesale clients as a source of useful information for making decisions about investments in financial products. Users of research reports should be given sufficient information about conflicts of interest relating to the report so that they are able to form a realistic view about the report and whether to rely on it. Specific, prominent and meaningful disclosures about conflicts are needed either in or with each research report.

Note: Research report providers should also consider what other steps they may take. In many cases, disclosure alone will not be an adequate response to a conflict of interest.

44 Research report providers should disclose in or with each research report the extent to which they (or any associated persons) have or are likely in the future to have an interest in financial products that are the subject of the report. It is important that conflicts of interest disclosures are specific and clear. It would be inadequate simply to make a generic statement that the research report provider may from time to time have interests in those financial products the subject of research.

Note: For example, the disclosures should cover:

(a) beneficial interests in and derivatives relating to the financial product and products issued by a related company or close competitor of the product issuer;

(b) likely allocations as part of a public offering; and

(c) significant interests that the research report provider (or its staff) may have in the product issuer (eg a substantial loan to or from the product issuer).

See also paragraphs 2.2 and 2.3 in the ASX draft Guidance Note and Guideline 4 in the SIA/SDIA Guidelines.

45 Research report providers should disclose the extent to which they (or any associated persons) are likely to receive any benefits from the report.

Note: For example, the disclosures should cover:

(a) if the research analyst principally responsible for the preparation of the report received any benefit or inducement (including compensation based on investment banking or equity dealing revenues); and

(b) if the research report provider (or its staff) received compensation from the subject of the report within the last twelve months, or if the research report provider (or its staff) expects to receive or intends to seek compensation for investment banking services in the next three months.

See also paragraph 2.4 in the ASX draft Guidance Note and Guideline 4 in the SIA/SDIA Guidelines.

46 Where any of the following apply, they should be disclosed in or with the research report:

(a) that the research report provider (or an associated person) provides underwriting, managerial, consultancy or market-making services to the product issuer;

(b) that the product issuer is otherwise a corporate client of the research report provider; or

(c) that the product issuer is related to or otherwise associated with the research report provider.

Note: For example, the disclosures should cover the following relationships (if present) between the research report provider (or its associates) and a product issuer (or its associates):

(a) underwriting or sub-underwriting;

(b) making a market in the relevant financial product;

(c) acting as broker or sponsor in an issue of securities;

(d) holding a senior position (including as a director) in the issuer;

(e) providing expert opinions; and

(f) investment banking, corporate advisory and dealing services.

See also paragraph 2.1 in the ASX draft Guidance Note and Guideline 4 in the SIA/SDIA Guidelines.

47 The research report (or accompanying disclosures) should state the extent to which the person who prepared the research report was provided with any assistance by the product issuer.

Note 1: For example, the disclosures should refer to any assistance provided via site visits or other means.

Note 2: It is important that product issuers and research report providers take reasonable steps to ensure that selective disclosure is avoided. See "Heard it on the grapevine…", Draft ASIC guidance and discussion paper – Disclosure of information to investors and compliance with continuous disclosure and insider trading provisions, November 1999.

48 The research report (or accompanying disclosures) should state:

(a) the period during which the research is current;

(b) the reasons for the opinions and recommendations (eg ratings or valuations) contained within the research report; and

Note: Research report providers should keep documents and records setting out why particular opinions were held and why recommendations were made in a research report.

(c) a statement as to who wrote and who approved the report.

We believe that readers will reasonably require disclosure about each of these matters in forming a realistic view about the research report and whether to rely on it.

49 Robust information barriers may mean the staff preparing and authorising a research report are unaware of some of the matters in paragraphs 43–48. Such barriers must prevent information going to research staff if it might create a conflict of interest for them. For example, they may be unaware of some confidential non-research services being provided to a product issuer by another department. If that is the case for a particular non-research service being provided, the research report could omit the matters relating to that service. Whether any particular matter does not need to be disclosed in a research report will, of course, depend on the facts and circumstances.

Note: See ASIC surveillance report "Research analyst independence" at paragraphs 5.39–5.42.

Your feedback

Q2.24 Are there any practical problems with this guidance on specific disclosure? Please give details.

Q2.25 Should this guidance on specific disclosure be mandated through a licence condition? Why or why not?

Q2.26 Is there a level below which interests, benefits and associations need not be disclosed (eg a materiality threshold)? If so, what is the threshold and why?

Q2.27 What disclosures or other measures are appropriate should be expected in relation to confidential and sensitive services provided to a product issuer (eg takeover advice)? Please give details.

Q2.28 To what extent does the presence of robust information barriers limit the conflicts disclosure needed in a research report? Please give reasons.

Other disclosure issues

50 Other matters that a reasonable person might take into account in assessing the impact of conflicts on a research report and whether to rely on it should also be disclosed. This information could be provided in a number of ways, including in or with research reports, in a separate document and on the research report provider's public website. We suggest research report providers should consider making publicly available (whether or not in research reports):

(a) the status of current research reports;

Note: For example, research report providers should make available information about when the research recommendations (eg ratings or valuations) in each research report were made and last reviewed.

(b) which financial products they provide research on from time to time;

Note: Where the research report provider begins or ceases to cover a financial product, they should make this known publicly and where practicable provide reasons.

(c) the proportion of each type of recommendation they make that has been given to product issuers who are corporate clients (compared to other product issuers); and

Note: For example, the research report provider could state what proportion of product issuers who are corporate clients have received a "buy" recommendation compared to the proportion of product issuers who are not corporate clients over a period of twelve months.

(d) information about the relative performance of their research recommendations in the market.

Note: For example, the research report provider could state what proportion of shares that they gave a "buy" recommendation to increased in value relative to the market index over a period of twelve months. Research report providers will need to consider how best to present the information, what to base the comparison on, how to represent changes in recommendations, and when this information is updated and made available.

51 Where research is provided in a public forum or reported in the media, research report providers should take reasonable steps to ensure that users have access to the full research report (including conflicts of interest disclosures).

Note: For example, research report providers should take reasonable steps to ensure that:

(a) research reports are disseminated together with conflicts of interest disclosure (or made available by reference); and

(b) when research is provided or reported on in public appearances or through third parties (eg in the media), the relevant conflict of interest disclosures are also provided (or made available by reference).

52 To improve the effectiveness of conflict of interest disclosures and appropriate use of research reports, research report providers should take reasonable steps to ensure that their research recommendations are clear, unambiguous and transparent.

Note: This is particularly so for the main recommendation or opinion given in the report (if any). For example, research report providers should ensure that research reports provide an explanation of terminology, rating systems and valuation methods used in the report.

Your feedback

Q2.29 Are there any practical problems with this guidance on other disclosure issues? Please give details.

Q2.30 Should this guidance on other disclosure issues be mandatory? If so, how?

Regulatory and financial impact

We have considered the likely regulatory and financial impact of the policy proposals in this paper. Based on the information that we currently have, we believe that our proposals strike an appropriate balance between facilitating financial services activity and investor protection. To ensure that we have achieved an appropriate balance, we are also developing a Regulatory and Financial Impact Statement (RIS).

The RIS will address the following seven key elements:

1 Issue/problem

This will discuss the nature and magnitude of the problem.

2 Objective(s)/analysis of the problem

The objective(s), or the outcome sought for the identified issue/problem, will be addressed.

3 Options/solutions

This will identify all the alternative options that could achieve the objective(s) stated above for dealing with the issue being considered (eg no specific action; ASIC policy proposal; media release; information statement; self-regulation/quasi-regulation; codes of conduct; and co-regulation, compliance and enforcement strategies).

4 Impact analysis (costs and benefits) of each option

Impact analysis will include:

(a) analysis of the benefits and costs of the options, including any restriction on competition for different persons affected;

(b) identification of persons or bodies affected by the problem; and those who will be affected by the solutions or options identified (ie applicant/proponent of issue; other interested parties, consumers, business and government);

(c) a consideration of how each of the proposed options will affect the existing Act, regulations or policies;

(d) identification and categorisation of the expected impacts of the proposed options as likely benefits or likely costs against each of the people/bodies identified as likely to be affected;

We will try to quantify these effects where possible (eg will there be any restriction on competition as a result of the proposed regulation?).

Costs to businesses affected by a regulatory initiative might include: administrative costs; complying with new regulatory standards; licence fees; delays; and so on.

Costs to consumers affected could also include higher prices for goods and services; reduced utility of goods and services; delays and more difficult or expensive options for seeking redress.

(e) benefits of the options will also be identified (even where they are not quantifiable); and

(f) the data sources used and assumptions made in making these assessments will be identified.

5 Consultation

The consultation undertaken in the policy process will be detailed.

6 Conclusions and recommended option

The preferred option(s) will be given, and reasons why.

7 Implementation and review

This will discuss how the proposed option will be administered, implemented or enforced (eg instrument of relief, policy statement, practice note, no action letter).

Your feedback

In order for us to fully assess the financial and regulatory impact of our proposals, we invite you to consider possible options that would achieve our objectives, comment on the impact that these policy proposals might have, and, in particular, give consideration to the costs and benefits of these proposals. Where possible, we are seeking both quantitative and qualitative data.

Any comments that we receive will be taken into account when preparing our final RIS.

Development of policy proposal

We have developed this policy proposal paper by considering:

(a) the intention of the *Financial Services Reform Bill* 2001 as indicated in the first and second CLERP 6 papers, Explanatory Memorandum to the Bill and the Second Reading Speech in the House of Representatives on the introduction of the Bill into Federal Parliament;

(b) the Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest Principles published by the Technical Committee of the International Organization of Securities Commission on 25 September 2003;

(c) relevant comparisons with current legislative requirements for the regulation of financial services activity under the law;

(d) relevant comparisons with current legislative requirements for the regulation of financial services activity in similar overseas jurisdictions (in particular, the United States, United Kingdom, Canada, Hong Kong, and Singapore);

(e) existing ASIC policies and practices relevant to the regulation of financial services activity under the law;

(f) the Government's Corporate Law Economic Reform Program (CLERP) Paper No 9 "Corporate Disclosure: Strengthening the Financial Reporting Framework";

(g) the Exposure Draft Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003; and

(h) ASIC's surveillance report "Research analyst independence".

.

Key terms

In this policy proposal:

"ASIC" means the Australian Securities and Investments Commission

"ASIC Act" means the *Australian Securities and Investments Commission Act 2001*

"associated person" means an associate (within the meaning of Division 2 of Part 1.2 of the Corporations Act) of the relevant second person

"CLERP 9 discussion paper" means the government's Corporate Law Economic Reform Program (CLERP) Paper No 9 "Corporate disclosure: Strengthening the financial reporting framework"

"Corporations Act" means the *Corporations Act 2001* and includes regulations made for the purposes of that Act

"conflicts of interest" include all conflicts of interest, whether they are actual or potential, and present or future

Note: This is described in more detail in paragraph 1 of the explanation following Section A.

"conflicts management obligation" means proposed section 912A(1)(aa) as set out in Schedule 10 of the Draft CLERP 9 Bill

"Draft CLERP 9 Bill" means the Exposure Draft Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003

"financial product" means a facility through which, or through the acquisition of which, a person does one or more of the following:

(a) makes a financial investment (see s763B);

(b) manages financial risk (see s763C); and/or

(c) makes non-cash payments (see s763D)

Note: This is a definition contained in s763A.

"financial product advice" means a recommendation, a statement of opinion or an interpretation of information, or a report of any of those things, that:

(a) is intended to influence a person or persons in making a decision about a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or

(b) could reasonably be regarded as being intended to have such an influence;

but does not include anything in an exempt document

Note: This is a definition contained in s766B.

"general advice" means financial product advice that is not personal advice

Note: This is a definition contained in s766B.

"licensee" or "financial services licensee" means a person who holds an Australian financial services (AFS) licence

Note: This is a definition contained in s761A.

"personal advice" has the meaning set out in s766B(3)

"PS 136" (for example) means an ASIC policy statement (in this example numbered 136)

"representative" of a financial services licensee means:

(a) an authorised representative of the licensee;

(b) an employee or director of the licensee;

(c) an employee or director of a related body corporate of the licensee; or

(d) any other person acting on behalf of the licensee

Note: This is a definition contained in s910A.

"research report" means general advice about a financial product with an investment component that is not prepared for any particular client.

Note: This is a definition contained in Schedule 2 of this policy proposal paper.

"research report provider" means licensees who carry on a business of preparing and providing research reports

"retail client" has the meaning set out in s761G

"s782" (for example) means a section of the Corporations Act (in this example numbered 782)

What will happen next?

Stage 1

29 October 2003	ASIC policy proposal paper released

Stage 2

31 January 2004	Comments due on the policy proposal
February 2004 – April 2004	Drafting of policy statement

Stage 3

May 2004	Final policy statement released

Your comments

You are invited to comment on the proposals and issues for consideration in this paper. All submissions will be treated as public documents unless you specifically request that we treat the whole or part of your submission as confidential.

Comments are due by 31 January 2004 and should be sent to:

Liz Roberts
Regulatory Policy Branch
Australian Securities & Investments Commission
GPO Box 9827
Sydney NSW 2001
email: policy.submissions@asic.gov.au

You can also contact the ASIC Infoline on 1300 300 630 for information and assistance.

Related papers

Corporate disclosure: Strengthening the financial reporting framework, Corporate Law Economic Reform Program, Proposals for Reform: Paper No 9, Commonwealth Treasury, 2002

Exposure Draft Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003

Commentary on the Draft Provisions (CLERP (Audit Reform and Corporate Disclosure) Bill)

"Research analyst independence", ASIC surveillance report, 22 August 2003

Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest Principles, International Organization of Securities Commission's Securities Analyst Task Force, 25 September 2003

Policy Statement 164 *Licensing: Organisational capacities* [PS 164]

Policy Statement 175 *Licensing: Financial product advisers – Conduct and disclosure* [PS 175]

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