



**ASIC**

Australian Securities & Investments Commission

## REPORT 515

# Financial advice: Review of how large institutions oversee their advisers

March 2017

### About this report

In July 2015, ASIC commenced a project to review how effectively Australia's largest banking and financial services institutions oversee their financial advisers.

This project focused on:

- how these institutions identified and dealt with non-compliant conduct by advisers between 1 January 2009 and 30 June 2015;
- the development and implementation by the institutions of a framework for the large-scale review and remediation of customers who received non-compliant advice between 1 January 2009 and 30 June 2015; and
- a review of Australian financial services (AFS) licensees, selected from within the institutions, to test their current processes for monitoring and supervising their advisers.

This report outlines ASIC's observations and findings from this project, and provides an update on the actions of the largest advice institutions to address customer loss or detriment. The report will assist the financial advice industry as a whole to raise its standards and reduce the risk of current customers receiving non-compliant advice in the future.

### About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

**Consultation papers:** seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

**Regulatory guides:** give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

**Information sheets:** provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

**Reports:** describe ASIC compliance or relief activity or the results of a research project.

### Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

Examples in this report are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements.

## Contents

<b>Executive summary</b> .....	<b>4</b>
<b>A Background</b> .....	<b>21</b>
Purpose of this project .....	21
Scope of our review .....	22
Our approach .....	23
<b>B Phase 1: Identifying and dealing with non-compliant conduct by advisers</b> .....	<b>31</b>
What we did .....	31
What we found .....	34
Next steps .....	36
<b>C Phase 2: Customer review and remediation</b> .....	<b>37</b>
What we did .....	37
What we found .....	43
Next steps .....	48
<b>D Phase 3: Monitoring and supervision of advisers</b> .....	<b>49</b>
Background to Phase 3 .....	49
Background and reference-checking processes .....	51
Effectiveness of adviser audit process .....	56
Further observations about KRIs and data analytics.....	67
Next steps .....	68
<b>Appendix 1: Advice licensees within the scope of this project</b> .....	<b>69</b>
<b>Appendix 2: Checklist—Background checking of advisers</b> .....	<b>71</b>
<b>Appendix 3: Checklist—Reviewing personal advice as part of an adviser audit</b> .....	<b>73</b>
<b>Appendix 4: Checklist—Key risk indicators for monitoring and supervising advisers</b> .....	<b>82</b>
<b>Appendix 5: Accessible versions of figures</b> .....	<b>84</b>
<b>Key terms</b> .....	<b>86</b>
<b>Related information</b> .....	<b>90</b>

## Executive summary

- 1 This project—which forms part of ASIC’s broader Wealth Management Project—focuses on five of Australia’s largest banking and financial services institutions (institutions):
  - (a) AMP Limited (AMP);
  - (b) Australia and New Zealand Banking Group Limited (ANZ);
  - (c) Commonwealth Bank of Australia (CBA);
  - (d) National Australia Bank Limited (NAB); and
  - (e) Westpac Banking Corporation (Westpac).
  
- 2 More specifically, we considered the conduct of Australian financial services (AFS) licensees that were solely controlled or owned by the above institutions for all or part of the period between 1 January 2009 and 30 June 2015, where these licensees provided personal advice to retail clients. A list of the 35 advice licensees that fell within the scope of this project is set out in Appendix 1.
 

Note: In this report, we use the terms:

  - ‘advice licensee’ to refer to ‘AFS licensees that provide personal advice to retail clients’;
  - ‘advice’ or ‘personal advice’ to refer to ‘personal advice provided to retail clients’: see s766B(3) of the *Corporations Act 2001* (Corporations Act) for the exact definition of ‘personal advice’; and
  - ‘customer’ or ‘client’ to refer to ‘retail client’, as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations 2001.

See also the list of ‘Key terms’ in this report.
  
- 3 As set out in [ASIC’s Corporate Plan 2016–17 to 2019–20](#), ASIC’s aim in the sectors it regulates is to promote investor and consumer trust and confidence and market integrity. For the financial advice industry this can be achieved if financial advisers:
  - (a) act professionally, avoid conflicts of interest and treat customers fairly;
  - (b) deliver strategic financial advice that is aligned with customer needs and preferences; and
  - (c) ensure that customers are fully compensated when loss or detriment results from poor conduct.
  
- 4 We recognise that a key driver to realising this aim is the impact that organisational culture and collective industry norms and practices have on the behaviour and conduct of the firms that we regulate and the individuals who work within these firms.
  
- 5 We commenced this project because of information ASIC received about non-compliant advice, as well as public concerns about wider problems in

large advice firms. This included information disclosed by some of the institutions in early 2015. Similar information was provided to the Senate Economics References Committee Inquiry into the Scrutiny of Financial Advice. A range of reviews and enforcement actions by ASIC in the financial advice industry, in recent years, had also highlighted systemic concerns.

6 Before the start of this project, it was apparent that some of the institutions had identified potentially significant past advice failings which they were seeking to address through customer remediation. The institutions also notified ASIC of a number of advisers they suspected of past non-compliant conduct.

7 Since 1 July 2013, significant law reform has taken place to improve standards in the financial advice industry, including the Future of Financial Advice (FOFA) reforms and the introduction of ASIC's financial advisers register. More reforms are being introduced, including improvements to professional standards for advisers. These reforms will help to improve customer outcomes in the future. However, we also consider it important that past misconduct is effectively addressed.

8 The aims of this project were therefore:

- (a) to ensure that past non-compliant conduct by advisers was identified by the institutions, and for ASIC to determine which of these advisers should be considered for regulatory and enforcement actions;
- (b) to ensure that a framework for large-scale customer review and remediation would be developed and implemented by each of the institutions to remediate customers who received non-compliant advice between 1 January 2009 and 30 June 2015; and
- (c) to review the current monitoring and supervision processes used by advice licensees, to determine whether changes were required to ensure that, in the future, these processes would effectively identify advisers who provided non-compliant advice. We will continue to work with licensees where we see areas for improvement.

Note: See 'Key terms' for definitions of 'non-compliant conduct' and 'non-compliant advice'.

9 To improve trust and confidence in the financial advice industry, we considered it imperative that the institutions' work on addressing non-compliant advice was undertaken transparently and effectively. In addition, we wanted to ensure that insights gained from past experience were applied by the institutions. ASIC is working actively with the institutions, and other industry participants, to rectify past problems and identify areas for improvement.

- 10 This report outlines our observations and findings from the project to date. Except in relation to the development of the review and remediation frameworks, this report does not name specific institutions or licensees because the information on which it relies:
- (a) was provided by the institutions in response to our compulsory information-gathering powers which require us to maintain confidentiality; and
  - (b) may be used to seek an enforcement outcome against the institutions or, depending on the conduct, an adviser.

Note: This report does not cover separate actions and outcomes in relation to individual financial advice firms—such as ASIC’s earlier actions against CBA (see paragraphs 116–119)—and it does not cover the actions and remediation we are seeking through our work on advice fees charged where no services were provided: see [Report 499](#) *Financial advice: Fees for no service* (REP 499).

- 11 When we have public enforcement outcomes, our public reporting names the affected institutions and advisers. Further details can be found on ASIC’s website.

### **Phase 1: Identifying and dealing with non-compliant conduct by advisers**

- 12 The project was conducted in three phases. In Phase 1, we directed the institutions to identify and provide information about their advisers whose past conduct had been identified as non-compliant. The purpose of gathering this information was to:
- (a) determine how the institutions identified and dealt with non-compliant conduct by advisers; and
  - (b) allow ASIC to consider whether to take action against those advisers.

- 13 In response to our direction, the institutions identified serious compliance concerns about 149 advisers, and provided this information to ASIC by 16 December 2015. At that time, ASIC had already banned 14 of these SCC advisers and had ongoing investigation or surveillance activities in relation to a further 38 of these advisers.

Note: In this report, we use the term ‘SCC adviser’ to refer to an adviser whose conduct has given rise to serious compliance concerns. For our definition of ‘serious compliance concerns’, see paragraph 108.

- 14 Over the course of the project, 36 additional SCC advisers were brought to our attention. This resulted in a total of 185 SCC advisers to be considered for further regulatory or enforcement action. As at 31 December 2016, we had banned 26 of these SCC advisers and had ongoing investigation or surveillance activities in relation to 75 SCC advisers.

Note: For details about how we selected the SCC advisers for further regulatory or enforcement action, see paragraphs 149–159.

- 15 We reviewed the breach reports and other notifications provided to ASIC by the institutions since 1 January 2009. From the information held on our registers, and information provided to us by the institutions, it was apparent that reporting practices varied, with some of the institutions notifying ASIC more often. However, nearly half of the SCC advisers were not notified to ASIC until the licensees identified and reported their SCC advisers to us in response to our direction.
- 16 We observed that, where breach reports were lodged relating to the SCC advisers, there was often a considerable delay between the institution first becoming aware of the suspected non-compliant conduct and the breach report being lodged with ASIC.
- 17 Failure or delay in notifying us of reportable breaches, or suspected serious non-compliant conduct, may impede our ability to take appropriate enforcement or other regulatory action. Importantly, it may also result in an increased risk of customer loss or detriment as a result of advice being provided by non-compliant advisers who have been allowed to continue to work in the industry.
- 18 We accept that not every instance of adviser non-compliance will trigger the need to lodge a breach report with ASIC, and we will not take formal enforcement or other regulatory action in relation to every breach report. This is because we have limited resources and must therefore prioritise taking action on matters that will address the most significant risks and have the greatest impact. However, even if breach reports do not lead to ASIC taking action, they help us to better understand the trends and potential risks in the financial advice industry and to improve our identification of matters where we need to take action.
- 19 ASIC has clearly and publicly signalled to the financial advice industry the importance of breach reporting, and we are receiving more breach reports from advice licensees. The launch of ASIC’s financial advisers register on 31 March 2015 underlines the role that breach reporting can play in helping to address poor adviser conduct. The register assists ASIC to more readily identify where advisers whose conduct has been the subject of a breach report are now working, or whether they have left the industry.
- 20 For further information about our review of advisers whose conduct has been identified as non-compliant, including a full definition of ‘serious compliance concerns’, see Section B.

## Phase 2: Customer review and remediation

- 21 In Phase 2, we engaged with each of the institutions to oversee the development and implementation of a framework for large-scale customer review and remediation.
- 22 The purpose of this engagement was to ensure that the institutions identified and remediated—in a comprehensive, fair, timely and transparent manner—customers who had suffered loss or detriment as a result of receiving non-compliant advice between 1 January 2009 and 30 June 2015. These are large-scale, complex remediation processes, and if this purpose is to be met, the institutions need to ensure they invest adequate resources into developing their frameworks.
- 23 The institutions recognise the importance of this work, and the development of their review and remediation frameworks has been undertaken on a consultative basis. We worked with each of the institutions to ensure that the review and remediation framework they put in place would be consistent with the principles that were developed through [Consultation Paper 247](#) *Client review and remediation programs and update to record-keeping requirements* (CP 247) and are set out in our recently published guidance in [Regulatory Guide 256](#) *Client review and remediation conducted by advice licensees* (RG 256).
- 24 In particular, the completed review and remediation framework should:
- (a) provide a streamlined review and remediation process for each of the institutions;
  - (b) operate efficiently, honestly and fairly—in line with advice licensees’ obligations—by addressing the key principles set out in our guidance; and
  - (c) provide customers with confidence in the fairness of remediation outcomes.
- 25 In the past, the institutions have relied on traditional monitoring and supervision tools, such as customer complaints data or adviser audit outcomes, to identify which advisers pose a higher risk of non-compliant conduct (high-risk advisers).
- 26 More recently, as part of their review and remediation processes, the institutions have been using new technologies and data analytics to develop key risk indicators (KRIs) to assist in identifying high-risk advisers and affected customers. This will contribute to more effective monitoring and supervision.
- 27 When developing these KRIs, the institutions faced challenges because of the limitations on data collection and retention. Some of the reasons observed for these limitations included that:



- (a) older data was less reliable, unavailable or non-existent;
- (b) paper-based record keeping made information more difficult to access;
- (c) incompatible legacy systems, resulting from technology upgrades and business mergers, made data extraction difficult; and
- (d) different data-recording methods were used within the institutions and across their different licensees.

28 Nevertheless, we think that the development and use of KRIs, and enhanced records and data management, appropriate to the licensee's business, can assist in identifying high-risk advisers and affected customers.

29 As at 23 February 2017, some institutions were yet to finalise all of the documentation relating to their review and remediation framework. Phase 2 of the project is therefore ongoing. Table 3 sets out the key elements that we encouraged institutions to include in their review and remediation framework, and the progress made by each institution towards incorporating these elements.

30 To ensure that its review and remediation framework will satisfy the objective of Phase 2, each of the institutions has agreed to appoint an external expert to provide assurance on the design and operational effectiveness of its framework.

### **Compensation**

31 The compensation arising from the non-compliant conduct identified within the scope of this project—reported to ASIC as paid at 31 December 2016—was approximately \$30 million in total. This was paid across the institutions to approximately 1,347 customers who had suffered loss or detriment as a result of non-compliant conduct by 97 currently identified high-risk advisers whose conduct occurred between 1 January 2009 and 30 June 2015.

32 The compensation amount can be broken down into:

- (a) \$5,928,821 paid in response to customer complaints;
- (b) \$22,765,365 paid under previous or existing remediation processes; and
- (c) \$1,572,086 paid under the frameworks for large-scale review and remediation developed as part of this project.

Note 1: The above figures are rounded to the nearest dollar.

Note 2: We will provide ongoing updates by publicly reporting on the progress made by the institutions on remediating customers who have suffered loss or detriment as a result of receiving non-compliant advice between 1 January 2009 and 30 June 2015, until the completion of that work.

Note 3: For further details on the compensation paid by the institutions, see Table 5.

- 33 The compensation figures set out in this report do not include compensation amounts paid in relation to:
- (a) CBA's other large-scale remediation programs, as noted in:
    - (i) [Media Release \(15-083MR\)](#) *Update on licence conditions on two Commonwealth Bank financial planning businesses: ASIC releases initial report into advice compensation program* (23 April 2015);
    - (ii) [Media Release \(16-415MR\)](#) *Update on licence conditions of two CBA financial advice businesses: ASIC releases compliance report from KordaMentha Forensic* (5 December 2016); and
    - (iii) CBA's [Open Advice Review program](#); or
  - (b) fees-for-no-service issues, as noted in REP 499.

34 For further information on the review and remediation of customers, see Section C.

### Phase 3: Monitoring and supervision of advisers

35 For Phase 3, we selected 10 advice licensees (Phase 3 licensees) from the 35 advice licensees in this project. We undertook a review of two key aspects of the Phase 3 licensees' monitoring and supervision processes.

36 Our review focused on:

- (a) the adequacy of the licensees' background and reference-checking processes when appointing new advisers; and
- (b) the effectiveness of the licensees' adviser audit processes.

37 We also observed how the advice licensees have increasingly been using data analytics to develop their KRIs as part of monitoring and supervising their advisers.

#### Background and reference-checking

38 We reviewed the background and reference-checking processes used by the Phase 3 licensees. We found that all of these licensees currently undertake some form of background and reference checking when recruiting new advisers—however, these processes were inadequate and often failed to identify which advisers had a history of non-compliant conduct.

39 In particular, we were concerned about the following issues:

- (a) *Contacting referees:* We found that, in some instances, recruiting licensees sought references from former colleagues of an adviser. These former colleagues were not appropriately independent and would not have had access to the compliance records of their advice licensee. When conducting background and reference checks, it is important that the recruiting licensee contacts an appropriately qualified and

authorised person, within the former licensee, who has access to the adviser's compliance history.

- (b) *Adviser audit reports*: We found that recruiting licensees rarely received effective responses to a request for an adviser's previous audit reports. We were concerned that, when recruiting licensees did receive an audit report that flagged potential non-compliant conduct by an adviser, there were instances where those licensees failed to make further inquiries about the conduct identified.

#### *Policy for providing references*

- 40 We found that the limited effectiveness of advice licensees' background and reference-checking processes could sometimes be attributed to a former licensee's reluctance to provide relevant information to a recruiting licensee about a former adviser's compliance history. As a result, we found that some advisers were employed without this information becoming known to the recruiting licensee.
- 41 The Australian Bankers' Association (ABA)—together with its members, which include the institutions—is also concerned about the background and reference-checking processes in the financial services industry. The ABA has recently released its *Reference checking and information sharing protocol* ([ABA protocol](#)), which seeks to set out a standard for background and reference checking.
- 42 The ABA protocol is a positive initiative and helps to highlight the importance of reference checking. However, we note that the obligation to disclose information remains subject to exceptions. We will continue to liaise with the ABA on this important initiative as we wish to support effective reference checking in the financial advice industry.
- 43 We also note that the operation of the ABA protocol is limited to those AFS licensees that subscribe to it. The ABA states that current subscribers to its protocol appoint approximately 38% of the financial advisers recorded on ASIC's financial advisers register. We encourage advice licensees that are not ABA members to contact the ABA to subscribe to the protocol.
- 44 Appendix 2 sets out a checklist of issues that all advice licensees should consider when conducting background and reference checks before appointing a new adviser. In future surveillances, where we see advice licensees failing to adequately conduct or provide background and reference checks, we will seek to publicly highlight this conduct.
- 45 For further information on background and reference checking, see paragraphs 223–245.

### Effectiveness of the adviser audit process

46 Each of the Phase 3 licensees uses regularly scheduled adviser audits (referred to in this report as business-as-usual audits) as part of its broader audit process for monitoring adviser compliance with financial services laws and the licensee's business rules: see Table 8 for further details about business-as-usual adviser audits.

47 Outcomes from the adviser audits are used by the Phase 3 licensees for a number of purposes, including determining the subsequent level of monitoring and supervision required for each adviser. An adequate adviser audit process is therefore an integral part of effective monitoring and supervision. For further discussion, see paragraphs 219–221.

48 To assess the effectiveness of the adviser audit processes of the Phase 3 licensees, we selected and reviewed a total of 160 customer files (sample files). We assessed each of the sample files, together with the licensees' audit outcomes for those files, to determine whether the licensees' auditors had correctly identified whether advisers had demonstrated compliance with the best interests duty and related obligations. As part of the next steps following this project, we will be undertaking further work with the licensees in this area to assist them in improving the way they monitor and supervise their advisers.

Note: 'Best interests duty and related obligations' refers to the obligations set out in Div 2 of Pt 7.7A of the Corporation Act. See also 'Key terms'.

49 From our assessment, we found that:

- (a) the audit process was *effective* in 18% of the sample files—that is, the findings by the licensees' auditors aligned with our own file review. We observed an effective audit process only on files where no areas of non-compliance were identified by either the licensees' auditors or our advice reviewers;

Note: We did not observe an effective audit process for any of the sample files where our reviewers identified areas of non-compliance. In these cases, the licensees' auditors did not correctly identify all of the compliance concerns found by ASIC.

- (b) the audit process was *partially effective* in 57% of the sample files—that is, some areas of non-compliance were identified by the licensees' auditors, but our advice reviewers found additional areas of non-compliance; and
- (c) the audit process was *ineffective* in 25% of the sample files—that is, no areas of non-compliance were identified by the licensees' auditors, but our advice reviewers found that there were areas of non-compliance.

50 It is important to note that, where we observed non-compliance with the best interests duty and related obligations in the 160 sample files, this did not indicate a serious compliance concern requiring formal enforcement or other

regulatory action in relation to the advisers. Non-compliant advice does not necessarily indicate that financial remediation or similar action is required.

51 Our project did not draw conclusions on customer detriment. However, where we assessed that an adviser had failed to demonstrate compliance with the best interests duty and related obligations, we will meet with the advice licensee to discuss our findings.

52 Where we found the adviser audit process to be ineffective, or partially effective, we formed the view that some form of corrective action (often referred to as ‘consequence management’) should have occurred in 127 out of 131 cases. We observed that the licensees’ auditors recorded that corrective action was only required in 80 out of these 131 cases.

53 In our review, we identified a number of potential issues that may have affected the effectiveness of the business-as-usual adviser audits undertaken by the Phase 3 licensees. In particular, we were concerned about:

- (a) the adequacy of the file audit questionnaire;
- (b) amendments made to the customer file to resolve identified non-compliance following recommendations made by the auditor as part of the adviser audit; and
- (c) the adequacy of audit record keeping.

54 In Appendix 3, we provide a checklist which sets out the relevant factors for all advice licensees and compliance consultants to consider when auditing advisers to determine whether they have demonstrated compliance with the best interests duty and related obligations when providing personal advice. The checklist covers compliance with these legal obligations, as well as providing additional commentary on giving good quality advice. Each advice licensee should tailor the application of this checklist to the unique nature, scale and complexity of its advice business.

55 For further information on the adviser audit process, see Section D.

### **Use of data analytics in monitoring and supervision**

56 Data collection, the use of data analytics, and effective record keeping underpin all aspects of this project. In particular, they form the basis of targeted and effective KRIs to improve the monitoring and supervision of advisers and the identification of high-risk advisers.

57 From our engagement with the institutions, we observed that significant resources have been allocated to the development and improvement of data systems and data analytic tools. These changes range from the centralisation of their licensees’ data records, through to their transition from paper-based to digital record keeping.

Note: See ‘Key terms’ for the meaning of ‘data analytics’.

- 58 In this project, we observed that the development of data analytics and KRI tools is more advanced in some institutions than others, and all of the institutions are continuing to work in this area. For example, some of the institutions currently use KRIs, supported by data analytics, to identify potentially non-compliant advice—which is then further tested by reviewing a sample of the relevant customer files. This analysis is in addition to the business-as-usual adviser audits conducted by those institutions.
- 59 All of the institutions expect to use the technical capabilities and infrastructure being developed as part of their review and remediation frameworks to make continual improvements to their data analytics and KRI tools.
- 60 We expect that these changes will have a substantial positive impact on the ability of the institutions to monitor and supervise their advisers:
- (a) improved data collection will result in more data being available that can be organised into a wider range of searchable categories. This will allow for better oversight by enabling a variety of complex KRIs to be applied;
  - (b) more effective record keeping will improve the way auditors are able to access and review advisers' customer files; and
  - (c) better access to business records will allow the institutions to interact in a more timely way with their regulators, including ASIC.
- 61 These changes align with ASIC's recently amended [Class Order \[CO 14/923\]](#) *Record-keeping obligations for Australian financial services licensees when giving personal advice*. The enhanced obligation for advisers to keep appropriate records and, most importantly, to make these records available to their licensee at all times, will enable advice licensees to improve their monitoring and supervision of advisers.
- 62 In Appendix 4, we set out our checklist and guidance for consideration by all advice licensees in the financial advice industry when developing and implementing their KRIs for monitoring and supervising advisers in their retail advice businesses. We expect that using these KRIs will help licensees to identify potentially high-risk advisers and non-compliant advice.
- 63 For further information on KRIs, see paragraphs 189–197 and 285–292.

### **Observations on cultural indicators**

- 64 ASIC is concerned about culture because it is a key driver of conduct within the AFS licensees that we regulate. It is an issue that we have highlighted for the financial services industry in general, and not just for large banking and financial services institutions.

- 65 Culture is a set of shared values or assumptions. Values are what an organisation chooses to prioritise, and these shared values can shape and influence people's behaviour and attitudes towards, for example, the treatment of customers and compliance.
- 66 In this project, we considered how the culture of an institution can influence the effectiveness of its processes for monitoring and supervising its advisers. In particular, we considered a number of key indicators of culture in the institutions to determine whether the interests of customers were being prioritised. These indicators include:
- (a) the way that an institution deals with advisers whose conduct has been identified as non-compliant;
  - (b) how an institution remediates customers who have been adversely affected by receiving non-compliant advice; and
  - (c) how effectively an institution's monitoring and supervision processes identify adviser non-compliance.
- 67 Where there are systemic failures in an organisation, the culture of that organisation is very likely to have been a contributing factor. The information we gathered for this report suggests to us that cultural factors in the institutions contributed to the failures we observed.
- 68 All of the institutions publicly state that their core values include being customer focused, 'doing what is right' for customers, and acting with integrity.
- 69 Our concern is that, despite these stated values, many of the institutions we reviewed did not ensure that their internal processes consistently supported the value of 'doing what is right' for the customer. Many of the failings we identified led, or had the potential to lead, to poor outcomes for customers. For example, we observed:
- (a) *inadequate information sharing*: when advice licensees became aware of serious non-compliance by an adviser, they often failed to protect future customers by adequately notifying ASIC or the recruiting licensee;
  - (b) *inadequate background and reference-checking processes*: when recruiting advice licensees failed to make comprehensive background-checking inquiries, advisers with a poor compliance record were able to circulate undetected within the financial services industry, increasing the risk that new customers would receive non-compliant advice; and
  - (c) *inadequate audit processes*: when customers had potentially received non-compliant advice, the audit process failed to properly assess whether the adviser had demonstrated compliance with the best interests duty and other related obligations, so that affected customers were not always identified or properly remediated, where necessary, and advisers providing non-compliant advice remained undetected.



70 In the course of ASIC's broader engagement with the institutions, it is apparent that they are now more engaged with the issue of culture. We have observed an increasing use of technology to improve staff oversight and the identification of issues that may lead to, or indicate the presence of, poor culture. The institutions have also recognised that background and reference-checking processes need to be improved. While we have noticed that progress is being made, there is still room for significant ongoing cultural change to occur at all levels within the institutions.

71 We recognise that there is no single measure or action that will raise standards and improve culture across the financial advice industry. Rather, it is the combination of broad industry reforms as well as the work within advice firms that will improve consumer trust and confidence. We encourage the institutions to consider how improvements in areas such as remuneration structures, professional standards, reference checking and record keeping can be used in practical ways to improve and strengthen a customer-focused culture.

### **Regulatory reform**

72 Our project findings highlight the importance of both recent law reforms and current reform processes that are designed to address poor conduct and structural problems in the financial advice industry. Most of the reforms are phased in over a period of time, as they generally require very significant industry change. However, as a 'package', these reforms will raise standards and reduce misconduct in the industry.

73 Some of the key recent, current and future law reforms relevant to the findings in this report are set out below. Reforms that ASIC has supported include measures to address conflicts of interest in adviser remuneration, efforts to raise professional standards, and the Government's current proposals to strengthen breach reporting.

### **Recently implemented reforms**

#### *Future of Financial Advice*

74 The FOFA reforms were passed by Parliament and commenced on 1 July 2013.

75 The FOFA reforms are an important step in moving the financial advice industry away from a commission-driven distribution network to a professional services industry. These reforms were designed to improve trust and confidence in the industry by introducing the best interests duty and related obligations, a ban on conflicted forms of remuneration, fee disclosure statements and opt-in requirements for ongoing service.



76 The FOFA reforms have also extended the scope of the conduct obligations. The legislation now imposes obligations on employed advisers, and not just the advice licensee or its authorised representatives.

77 This report covers advice given both before and after FOFA. In Phase 3, we focused on testing the effectiveness of key aspects of advice licensees' monitoring and supervision processes after the FOFA reforms were implemented.

#### *Financial advisers register*

78 On 24 October 2014, the Government announced that it was delivering on its commitment to establish an enhanced, industry-wide public register of financial advisers. The financial advisers register, administered by ASIC, provides key information on all individuals who have, since 31 March 2015, provided personal advice to retail clients on relevant financial products (i.e. all financial products other than basic banking products, general insurance products or consumer credit insurance, or a combination of any of these products). The register is intended to improve transparency for consumers, allow ASIC to track and monitor financial advisers, and assist advice licensees to improve recruitment practices and manage risks.

79 We successfully launched the financial advisers register on 31 March 2015. The key information on the register includes:

- (a) the adviser's name, registration number, status and experience;
- (b) the name of each AFS licensee who authorises the adviser;
- (c) if an adviser is authorised by an authorised representative, their details;
- (d) the recent advising history of the adviser;
- (e) what product areas the adviser can provide advice on;
- (f) any bans, disqualifications or enforceable undertakings entered into by the adviser; and
- (g) the adviser's qualifications and training courses and any memberships of professional bodies.

Note: The *Corporations Amendment (Professional Standards of Financial Advisers) Act 2017* inserts additional information to be included on the financial advisers register from 1 January 2019.

80 The financial advisers register is proving to be a useful tool. As at 31 December 2016, over 25,300 advisers were recorded on the register, and more than 1.5 million searches of the register had been undertaken since it was launched. ASIC sees the financial advisers register as a positive step towards a more transparent advice industry.

81 Further reforms introduced by the Government on professional, ethical and education standards (see paragraphs 82–86) will lead to enhancements to the register.

### **Current reform proposals**

#### *Professional, ethical and education standards*

82 We have observed in this project that advisers have often failed to demonstrate compliance with the best interests duty and related obligations. Inadequate education standards for advisers may be one of the causes of this non-compliance. ASIC has long advocated for stronger education standards for advisers.

83 On 15 March 2017, the *Corporations Amendment (Professional Standards of Financial Advisers) Act 2017* commenced. The legislation seeks to raise the professional, ethical and education standards of financial advisers. We consider that the enhanced professional standards framework for financial advisers will assist in improving the quality of advice.

84 Key elements of the reforms include requirements for advisers to hold a bachelor's degree or higher, pass an exam that will provide a common benchmark across the industry, undertake continuing professional development, and subscribe to a code of ethics. The Government will also establish an independent industry-funded body, recognised in legislation, to develop the new standards.

85 There is a transitional period which means that most of the new provisions relating to professional standards have staggered commencement dates from 1 January 2019. Existing advisers will have until 1 January 2021 to pass the exam, and until 1 January 2024 to reach degree-equivalent status.

86 ASIC strongly supports these reforms.

### **Future reform**

87 In October 2016, the Government announced that it would set up the ASIC Enforcement Review Taskforce to assess the suitability of the existing regulatory tools available to ASIC to perform its functions adequately. The terms of reference allow for a thorough but targeted examination of the adequacy of ASIC's enforcement regime—including in relation to industry codes of conduct—to deter misconduct and foster consumer confidence in the financial system.

88 We strongly support the review and, in our submission to the taskforce, we have argued that the regulatory tools available to us should be strengthened.

- 89 The review will include (relevant to this project) an examination of the legislation dealing with corporations, financial services, credit, and insurance to assess the adequacy of:
- (a) the frameworks for notifying ASIC of breaches of the law;
  - (b) our powers in relation to the licensing of financial services providers and credit providers;
  - (c) our coercive powers to direct licensees to take, or refrain from taking, particular action; and
  - (d) our power, where appropriate, to ban offenders from being corporate officers following the commission of, or involvement in, serious contraventions.

*Breach reporting*

- 90 The terms of reference for the ASIC Enforcement Review provide for a review into the adequacy of the framework for notifying ASIC of breaches of the law, including:
- (a) the triggers for the obligation to notify ASIC of a breach;
  - (b) the time period in which notifications must be made; and
  - (c) whether the obligation to notify breaches should be expanded to take into account the conduct of other regulated parties. The obligation to lodge breach reports is currently confined to auditors, liquidators, and licensees.

- 91 We support a review into the breach reporting framework, and have publicly highlighted the importance of improvements to these provisions. We have highlighted deficiencies in the approach to breach reporting within this project.

*Directions power*

- 92 In this project, the development of a framework for large-scale customer review and remediation has been undertaken by each of the institutions voluntarily.
- 93 We support the taskforce's examination of providing ASIC with a power to direct AFS licensees and credit licensees, among other things, to conduct customer review and remediation, or to undergo an independent compliance review. This will allow more effective regulation of our stakeholders, and promote investor and consumer trust and confidence.

*Power to ban an individual from managing a financial services business*

- 94 In this project, we observed instances where an adviser's past conduct has given rise to serious compliance concerns and the adviser has since become a director of an AFS licensee, or of a corporate authorised representative, although they are no longer providing financial advice.

95 Our current licensing powers allow us to suspend or cancel a licence, or ban an individual from providing financial services. Our powers do not extend to banning individuals from having an integral role in managing a financial services business. We support the review into the adequacy of our power to ban an individual because this would allow ASIC to more effectively target those who set the compliance culture within a business.

### **Next steps**

96 We will continue to carry out our review of SCC advisers. We will publicly report on our regulatory outcomes arising from this review.

97 We will continue to meet with the institutions until the design and operational effectiveness of their review and remediation frameworks have been assured by their external experts.

98 We will report further as each institution's framework is finalised and implemented. Following implementation, we will continue to monitor the external expert's assurance of any customer review and remediation undertaken. We will provide updates on that further work, including the number of customers remediated and the amount of monetary compensation paid.

99 Further to our Phase 3 review, we will meet with each of the institutions to discuss their adviser audit outcomes and the findings of our file reviews, and to highlight our concerns about the licensees' background and reference-checking processes. If necessary, we will consider enforcement or other appropriate regulatory action.

## A Background

### Key points

This project forms part of ASIC's Wealth Management Project and was undertaken to review how Australia's largest banking and financial services institutions oversee their financial advisers.

The project focused on 35 advice licensees that were solely owned or controlled by AMP, ANZ, CBA, NAB or Westpac.

The project was undertaken in three phases:

- identifying and dealing with non-compliant conduct by advisers between 1 January 2009 and 30 June 2015;
- the review and remediation of customers affected by non-compliant advice received between 1 January 2009 and 30 June 2015; and
- our review of some of the key aspects of the institutions' current processes for monitoring and supervising their advisers.

### Purpose of this project

- 100 This project was undertaken as part of ASIC's Wealth Management Project. The Wealth Management Project was established in October 2014 with the aim of raising standards within the major providers of financial advice to retail customers and, in doing so, promote investor and consumer trust and confidence in the financial advice industry.
- 101 In July 2015, we commenced this review of how large institutions oversee their financial advisers, following public discussion about past non-compliant advice provided by the institutions. We focused on five of Australia's largest banking and financial services institutions, as set out in paragraph 1.
- 102 To achieve the aims of this project, as set out in paragraph 8, we focused on three key areas:
- (a) *Phase 1*—reviewing how each of the institutions identified and dealt with non-compliant conduct by advisers between 1 January 2009 and 30 June 2015, and determining which of these advisers should be considered for regulatory or enforcement action by ASIC;
  - (b) *Phase 2*—overseeing the development and implementation by each of the institutions of a framework for the large-scale review and remediation of customers affected by non-compliant advice received between 1 January 2009 and 30 June 2015; and
  - (c) *Phase 3*—conducting a review of 10 advice licensees selected from within the institutions (Phase 3 licensees) to test the current processes

used by these licensees for monitoring and supervising their advisers.  
We considered:

- (i) the adequacy of the licensees' background and reference-checking processes when appointing new advisers; and
- (ii) the effectiveness of the licensees' processes to audit the advice provided by their existing advisers.

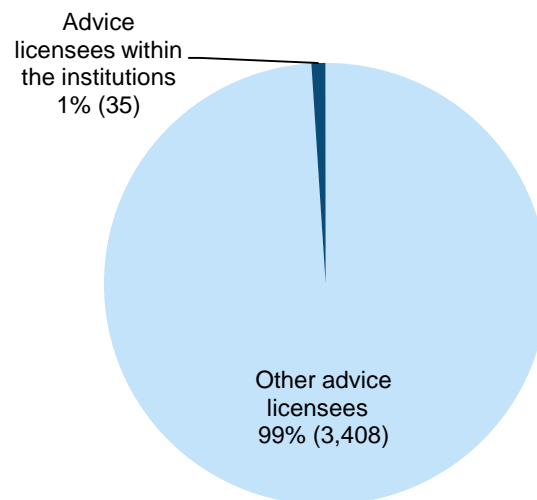
## Scope of our review

103 This project focused on the 35 advice licensees that were solely controlled or owned by the institutions for all or part of the period between 1 January 2009 and 30 June 2015.

Note: A list of these 35 advice licensees is set out in Appendix 1.

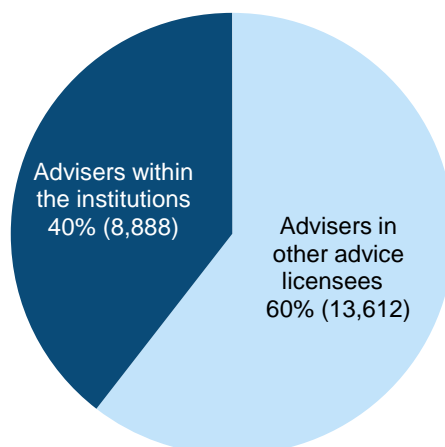
104 As shown in Figure 1 and Figure 2, when the project commenced on 1 July 2015, the 35 advice licensees in this project represented 1% of the 3,443 advice licensees authorised to provide personal advice in the Australian financial advice industry. However, at that time, these 35 advice licensees authorised around 40% (8,888) of Australia's approximate 22,500 financial advisers.

**Figure 1: Distribution of advice licensees (as at 1 July 2015)**



Note: See Table 14 in Appendix 5 for the data shown in this figure (accessible version).

Source: Institutions, ASIC

**Figure 2: Distribution of advisers (as at 1 July 2015)**

Note: See Table 15 in Appendix 5 for the data shown in this figure (accessible version).

Source: Institutions, ASIC

## Macquarie Group

105 Although Macquarie Group Limited is part of the larger Wealth Management Project, it has not been included in this project. This is because ASIC accepted an enforceable undertaking from Macquarie Equities Limited (MEL)—a subsidiary of Macquarie Group—in January 2013, the effect of which was for MEL to undertake work that was largely consistent with the aims of this project. As at December 2016, total compensation of approximately \$20.86 million (plus interest) had been paid out by MEL under the consequential remediation program.

Note: Further detail about ASIC's engagement with MEL can be found in [Media Release \(13-010MR\)](#) *ASIC accepts enforceable undertaking from Macquarie Equities Limited* (29 January 2013), [Media Release \(14-201MR\)](#) *Macquarie Equities' financial advice remediation* (15 August 2014) and [Media Release \(15-022MR\)](#) *Macquarie Equities Limited enforceable undertaking and next steps* (13 February 2015).

## Our approach

106 Each phase of this project is described below, including details about our objectives and how we went about gathering information.

### Phase 1: Identifying and dealing with non-compliant conduct by advisers

107 Using our compulsory notice powers, we directed each of the 35 licensees to identify and inform us about existing and former advisers whose conduct had given rise to compliance concerns within the relevant periods detailed below: see paragraphs 109–110.

108 We defined the following two categories of compliance concern to assist the institutions in assessing non-compliant conduct by advisers:

- (a) *Serious compliance concerns*: This is where an advice licensee believes, and has some credible information in support of the concerns identified, that an adviser—in the course of providing financial services (as defined in s766A of the Corporations Act)—may have engaged in the following:
  - (i) dishonest, illegal, deceptive, and/or fraudulent misconduct;
  - (ii) any misconduct that, if proven, would be likely to result in the instant dismissal or immediate termination of the adviser;
  - (iii) deliberate non-compliance with financial services laws; or
  - (iv) gross incompetence or gross negligence.
- (b) *Other compliance concerns*: This is where an advice licensee has reason to believe, and has some credible information in support of the concerns identified, that an adviser—in the course of providing financial services (as defined in s766A of the Corporations Act)—may have been involved in misconduct (other than a serious compliance concern), including but not limited to:
  - (i) a breach by act or omission of the licensee’s internal business rules or standards, such as where an adviser has recommended non-approved products, entered into personal agreements or arrangements with customers, demonstrated poor record keeping, or acted outside the scope of their authorisation or competence;
  - (ii) an adverse finding from audits conducted by, or for, the licensee; or
  - (iii) conduct resulting in actual or potential financial loss to customers as a result of the advice received.

109 The relevant period for identifying non-compliant conduct giving rise to ‘serious compliance concerns’ was between 1 January 2009 and 30 June 2015. This period was chosen to align with the advice licensees’ record-keeping obligations and with the scope of the institutions’ customer review and remediation work undertaken as part of Phase 2.

Note: The relevant period for identifying serious compliance concerns for two of CBA’s advice licensees—Commonwealth Financial Planning Limited (CFPL) and Financial Wisdom Limited (FWL)—differed from the other advice licensees because of previous customer review and remediation conducted by CFPL and FWL (see paragraphs 116–119). The relevant period for CFPL and FWL was between 1 July 2012 and 13 August 2015.

110 The relevant period for identifying non-compliant conduct giving rise to ‘other compliance concerns’ was between 1 July 2013 and 30 June 2015. We sought information from this period to assist in understanding the licensees’ current monitoring and supervision processes.



111 A summary and analysis of the information gathered in Phase 1 is set out in Section B.

## Phase 2: Customer review and remediation

112 In Phase 2, we asked the institutions to develop a framework for large-scale customer review and remediation to ensure that customers affected by non-compliant advice, received between 1 January 2009 and 30 June 2015, would be identified and remediated. Commencing in July 2015, we held meetings with the institutions approximately every three to four weeks throughout the project.

113 We asked the institutions to consider the following elements when developing their review and remediation frameworks, to ensure that these would be structured fairly and efficiently:

- (a) all advisers who should form part of the review and remediation are properly identified;
- (b) all customers who should form part of the review and remediation are properly identified;
- (c) communication with customers is fair and transparent;
- (d) the adviser audit process, which determines whether the adviser has demonstrated compliance with the relevant financial services laws, is fair and effective;
- (e) the compensation calculation methodologies are consistent with the principles of the Financial Ombudsman Service (FOS);
- (f) a variation to the FOS terms of reference is agreed with FOS, so that customers may access FOS for claims extending back to 1 January 2009 and up to a monetary limit of \$1 million;
- (g) affected customers are reimbursed for the cost of seeking an independent opinion on the result of an advice review or compensation offer;
- (h) an external expert is engaged to provide assurance on the design and operational effectiveness of the review and remediation framework; and
- (i) ASIC has oversight of the external expert's terms of engagement and will receive a report on the completed assurance.

Note: For details about the progress that each of the institutions has made towards incorporating these elements, see Table 3.

114 These elements are consistent with RG 256, which was being developed at the same time as this project was being carried out.

Note: The principles set out in RG 256 should be considered by all advice licensees; however, these principles may be:

- scaled up or down, as appropriate for the size of review and remediation to be undertaken; or
- otherwise adapted to suit advice licensees of different sizes and with different internal structures.

115 A summary and analysis of the information gathered in Phase 2 is set out in Section C.

### **CBA's previous review and remediation**

116 The scope of Phase 2 was different for CBA licensees because of previous regulatory outcomes in relation to CFPL and FWL. ASIC accepted an enforceable undertaking from CFPL in 2011; and additional AFS licence conditions were imposed, by agreement, on CFPL and FWL during 2014.

117 The effect of the work undertaken by CFPL and FWL was similar to the large-scale review and remediation framework that we requested the institutions develop within this project, including having external expert assurance. Before this project, CBA applied the insight gained from its work with CFPL and FWL to develop a large-scale review and remediation framework for use, as needed, within other licensees in the CBA Group.

Note: Further details about ASIC's engagement with CFPL and FWL can be found in [Media Release \(11-229MR\)](#) *ASIC accepts enforceable undertaking from Commonwealth Financial Planning* (26 October 2011) and [15-083MR](#).

118 At the commencement of this project, therefore, CBA had already developed and implemented a large-scale review and remediation framework, and CFPL and FWL had undertaken work to identify and remediate customers who had experienced loss or detriment as a result of receiving non-compliant advice.

119 Our work with CBA has since focused on assessing, and receiving external expert assurance on, the adequacy of the work undertaken by CBA's other licensees (apart from CFPL and FWL) to identify high-risk advisers, and to identify and remediate potentially affected customers.

## **Phase 3: Monitoring and supervision of advisers**

### **Scope of review**

120 In Phase 3 of the project, we conducted a review of selected advice licensees (Phase 3 licensees) to test the current processes they used for monitoring and supervising their advisers.

121 We considered the extent to which the Phase 3 licensees relied on background and reference checking when recruiting new advisers, and assessed how they used the audit process to identify advisers providing non-compliant advice. We also observed how the advice licensees used data analytics to develop their KRIs as part of monitoring and supervising their advisers.

122 Our review covered the period between 1 July 2013 and 31 March 2016 so that we could review the advice licensees' current policies and procedures implemented in light of the FOFA reforms.

123 To select the Phase 3 licensees, we selected two advice licensees from each institution.

124 Advice licensees generally operate:

- (a) an employee representative model—where the advisers are predominantly employees of the licensee; or
- (b) an authorised representative model—where the advisers are predominantly self-employed and appointed as authorised representatives.

125 For each institution, we selected:

- (a) from those licensees operating an employee representative model, the licensee with the largest number of advisers; and
- (b) from those licensees operating an authorised representative model, the licensee with the largest number of advisers.

A total of 10 advice licensees were selected.

Note: For details of the 10 Phase 3 licensees, see Appendix 1.

126 We used our compulsory notice powers to obtain information and documentation from the Phase 3 licensees addressing the following key areas:

- (a) background and reference checking of advisers;
- (b) the adviser audit process; and
- (c) the use of data analytics to develop KRIs.

127 For our review of the adviser audit process, we selected four advisers from each of the 10 Phase 3 licensees—a total of 40 advisers (sample advisers); and four customer files from each sample adviser—a total of 160 customer files (sample files): see paragraphs 134–137 for more details.

128 A summary and analysis of the information gathered in Phase 3 is set out in Section D.

### **Background and reference checking**

129 We have had concerns for more than a decade about the effectiveness of background and reference-checking processes used industry wide by advice licensees when recruiting new advisers.

130 In October 2007, we announced the launch of [Standards Australia's Handbook HB 322-2007 Reference checking in the financial services industry](#) (reference-checking handbook), which was developed by ASIC and a panel of industry representatives to provide guidance on appropriate reference-checking processes. We subsequently reported in 2011 ([Report 251 Review of financial advice industry practice](#) (REP 251)) and in 2013

([Report 362](#) *Review of financial advice industry practice: Phase 2* (REP 362)) on continuing deficiencies we had observed in advice licensees' background and reference-checking processes.

- 131 To test whether the background and reference-checking processes used by the advice licensees had improved since 2013, we used our compulsory notice powers to direct the Phase 3 licensees to provide information about their current processes—including:
- (a) for background and reference checking in general:
    - (i) the information that is sought from the former licensee about the adviser; and
    - (ii) the information that is provided about an adviser when responding to a request from a recruiting licensee; and
  - (b) details about the background and reference checks undertaken when the 40 sample advisers were appointed.

### **Effectiveness of the adviser audit process**

132 An effective adviser audit process is fundamental to the success of an advice licensee's monitoring and supervision processes. For further discussion, see paragraphs 219–221.

133 To form a view on the effectiveness of the Phase 3 licensees' adviser audit processes, we independently reviewed a number of the customer files (including Statements of Advice) that had been reviewed by the licensees as part of their business-as-usual adviser audits. We compared our assessment of the customer files and advice with the findings of the licensees' adviser audits.

### *Selecting advisers*

134 We found that the Phase 3 licensees conducted a number of different types of adviser audits as part of their monitoring and supervision processes. For our review, we focused solely on the business-as-usual adviser audits that formed part of the licensees' business-as-usual supervision of advisers.

- 135 We selected four sample advisers from each of the 10 Phase 3 licensees using the following criteria:
- (a) one adviser about whom compliance concerns had been identified while working at their previous institution, and before being appointed by their current licensee;
  - (b) one adviser who had the licensee's highest number of customers in 2014–15; and
  - (c) two advisers, chosen at random, who did not have any relevant history of non-compliant conduct known to ASIC.

Note: The advisers who were selected at paragraph 135(a) had been identified by the institutions as an SCC adviser or an OCC adviser as part of this project. In this report,

we use the terms ‘SCC adviser’ or ‘OCC adviser’ to mean an adviser whose conduct has given rise to ‘serious compliance concerns’ or ‘other compliance concerns’, respectively.

#### *Selecting customer files*

- 136 Using our compulsory notice powers, we directed the Phase 3 licensees to:
- (a) provide the detailed compliance findings for each of the customer files prepared as part of the most recent business-as-usual audit for each of the sample advisers; and
  - (b) undertake an adviser audit capturing the five most recently completed Statements of Advice (or records of advice) provided by each of the sample advisers, and provide the findings to ASIC—including whether the adviser had demonstrated compliance with the best interests duty and related obligations in providing the advice to the customer.
- 137 From these findings, we selected four customer files for each sample adviser—two from the business-as-usual audit in paragraph 136(a), and two from the ASIC-directed audit in paragraph 136(b). In total, 160 customer files were selected for our independent review.

#### *Requesting customer files*

- 138 Using our compulsory notice powers, we directed the Phase 3 licensees to provide the following documentation for each of the 160 sample files:
- (a) the customer file;
  - (b) the adviser audit results and all of the working papers created by the advice licensee as a result of the adviser audit;
  - (c) any recommendations made for corrective action or consequence management, and/or customer remediation; and
  - (d) the advice licensee’s policies and procedures applicable at the time of the adviser audit.

#### *Conducting file reviews*

- 139 We conducted independent reviews of the 160 sample files, and supporting documentation (see paragraph 138), on the basis of whether advisers had demonstrated compliance with the best interests duty and related obligations when providing the advice.
- 140 We engaged an external consultant to review some of the sample files. The external consultant reviewed 90 files, and ASIC analysts reviewed the remaining 70 files.

Note: Each file review carried out by the external consultant, or by ASIC, was subject to a peer review to check for consistency of approach.

- 141 The assessments of the sample files were compared with each licensee’s adviser audits to determine whether the licensee’s auditor had correctly

identified whether advisers had demonstrated compliance with the best interests duty and related obligations.

142

The results of our findings were grouped into three categories:

- (a) If the auditor correctly identified all areas of non-compliance (if any) in a sample file, we considered the audit to be *effective*.
- (b) If the auditor identified some areas of non-compliance but our advice review found additional areas of non-compliance, we considered the audit to be *partially effective*.
- (c) If the auditor identified no areas of non-compliance but our advice review found there were areas of non-compliance, we considered the audit to be *ineffective*.

143

We also assessed the adequacy of the recommendations made by each auditor for:

- (a) consequence management of the adviser; and
- (b) remediation of the customer.

## B Phase 1: Identifying and dealing with non-compliant conduct by advisers

### Key points

We directed that each institution identify the advisers about whom they had compliance concerns. The institutions identified serious compliance concerns about 149 advisers.

As at 31 December 2016, ASIC had banned 26 SCC advisers and we had ongoing investigation or surveillance activities in relation to 75 SCC advisers.

We found that many of the SCC advisers had not previously been reported by the institutions to ASIC by a breach report or other notification.

We found that there were inadequacies in the approach taken by the institutions to the background and reference checking of advisers.

### What we did

144 Using our compulsory notice powers, we directed the institutions to identify their existing and former advisers whose conduct had been found to be non-compliant during the relevant periods: see paragraphs 107–111.

145 We asked each institution to provide information on the advisers about whom they had identified serious compliance concerns (SCC advisers) or other compliance concerns (OCC advisers).

Note: ‘Serious compliance concerns’ and ‘other compliance concerns’ are defined in paragraph 108. See also ‘Key terms’.

146 We gathered information about:

- (a) the nature and seriousness of the compliance concerns and the length of time that had passed since the suspected non-compliant conduct occurred;
- (b) how the institution identified the compliance concerns;
- (c) actions the institution took to deal with the adviser;
- (d) how the institution remediated the customers affected by the non-compliant conduct;
- (e) whether ASIC had previously been notified of the non-compliant conduct; and
- (f) whether background and reference checks on the adviser were undertaken before their appointment to the institution.

- 147 We assessed the information received to determine whether we should take regulatory or enforcement action in relation to the SCC advisers. All SCC and OCC adviser information has also been recorded on ASIC's confidential internal databases.
- 148 It should be noted that, outside of this project, we have taken—and continue to take—enforcement action against other financial advisers who have engaged in misconduct. Public reporting on these actions is available on ASIC's website.

### Serious compliance concerns

- 149 By 16 December 2015, the institutions had informed us about 149 SCC advisers. At that time, we had ongoing investigation or surveillance activities in relation to 38 of these advisers.
- 150 We assessed the information provided by the institutions to consider whether further enforcement or other regulatory action should be taken in relation to any of the remaining SCC advisers. A two-stage approach was used.

### Identification of SCC advisers for further action

- 151 In the first stage, for each of the remaining 111 SCC advisers, we considered:
- (a) whether the adviser was already subject to a banning order;
  - (b) whether the adviser was currently providing personal advice; and
  - (c) the nature and seriousness of the compliance concern and the length of time that had passed since the suspected non-compliant conduct occurred.
- 152 Table 1 sets out a summary of our findings.
- 153 ASIC does not commence an investigation into every matter that is brought to our attention. To ensure that we direct our finite resources appropriately, we consider a range of factors, including the risk to customers, when deciding whether to investigate and possibly take enforcement action: see [Information Sheet 151](#) *ASIC's approach to enforcement* (INFO 151) for more detail.

**Table 1: Number of SCC advisers not being considered for further enforcement or other regulatory action by ASIC as at 16 December 2015**

Reasons for not taking further action	Number of SCC advisers
The adviser is already subject to a banning order	14
The adviser is not currently providing personal advice	38
The nature and seriousness of the compliance concern, and the length of time that has passed since the suspected non-compliant conduct occurred, does not warrant further action	19
<b>Total number of SCC advisers not being considered for further action</b>	<b>71</b>

Source: Institutions, ASIC



154 There were 40 SCC advisers who remained within the scope of our ongoing review to determine whether enforcement or other regulatory action would be appropriate.

Note: This is in addition to the 38 advisers in relation to whom we already had an ongoing investigation or surveillance at the time of the original notification by the institutions: see paragraph 149.

155 We implemented processes to alert us if any of the 38 advisers who were not currently providing personal advice re-entered the industry. If this occurred, we would reassess whether action by ASIC was appropriate: see paragraph 157(a).

### **Review of SCC advisers**

156 In the second stage, we undertook or commenced a review in relation to the 40 SCC advisers identified in stage one as advisers to be considered for further enforcement or other regulatory action. The reviews used:

- (a) additional information provided by the institutions (requested under our compulsory notice powers);
- (b) information available from searching ASIC's internal confidential databases; and
- (c) up-to-date information sought from the adviser's current licensee.

### *Additional SCC advisers*

157 As at 31 December 2016, 43 advisers were added as SCC advisers to our review to be considered for further enforcement or other regulatory action. These advisers were drawn to our attention because:

- (a) SCC advisers, who had previously been assessed as requiring no further action, returned to the financial advice industry;
- (b) further information was received, resulting in ASIC reclassifying some OCC advisers as SCC advisers; and
- (c) new relevant information was received from an institution, resulting in the addition of new SCC advisers.

Note: As more information is received, it is possible that this figure of 83 may increase.

158 As at 31 December 2016, the total number of SCC advisers identified had increased to 185. At that time, 26 had been the subject of a banning order and we had ongoing investigation or surveillance activities in relation to 75 of these advisers.

159 As these activities progress, more advisers are likely to be subject to banning actions. We will publicly report on these outcomes.

## Other compliance concerns

160 We consider that the conduct of the advisers classified by the institutions as giving rise to ‘other compliance concerns’ was not serious enough to warrant enforcement or other regulatory action by ASIC.

161 We have also requested that the institutions notify us of any new relevant information that becomes available about OCC advisers. We will assess any additional information on a case-by-case basis. As noted in paragraph 157(b), where appropriate, these individuals may be reclassified as SCC advisers. If this occurs, we will reassess whether we should take action.

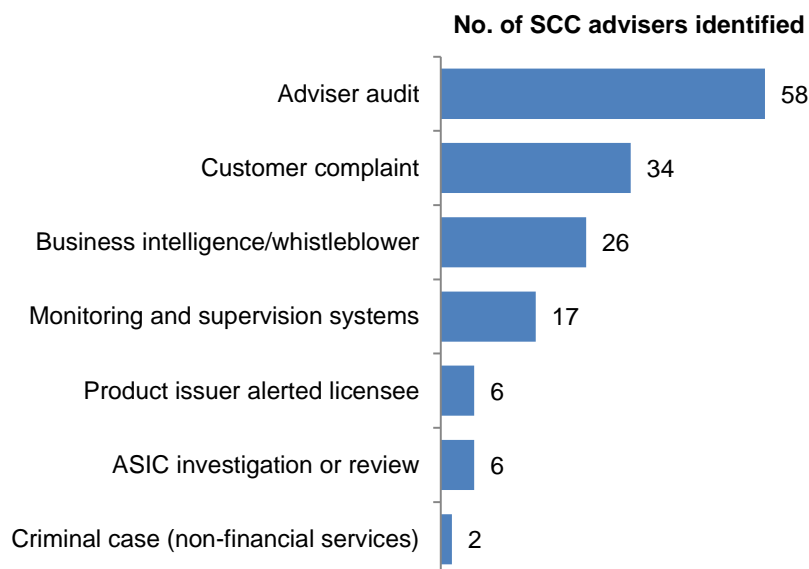
162 We have recorded the information about the OCC advisers in our internal confidential databases. If further information is received about these advisers, it will be assessed, together with our existing data, to determine whether further action is appropriate.

## What we found

### Identification of SCC advisers

163 The institutions used various methods to identify the 149 SCC advisers. As set out in Figure 3, the primary method of identification relied on information from adviser audits. This demonstrates the reliance institutions place on the adviser audit process as part of the overall monitoring and supervision of advisers. See Section D for further discussion.

**Figure 3: Methods used by the institutions to identify SCC advisers**



Note 1: The data shown in this figure has been compiled and interpreted by ASIC from the information received from the institutions.

Note 2: See Table 16 in Appendix 5 for the accessible version of this figure.

Source: Institutions, ASIC

## Notification of non-compliance to ASIC

164 We found that, until the advice licensees notified ASIC of their SCC advisers as part of this project, 73 of the 149 SCC advisers had not been the subject of a breach report or other notification to ASIC by the reporting licensees.

### Breach reporting

165 Before notifying ASIC of the 149 SCC advisers, the institutions had lodged breach reports in relation to the conduct of 42 of these advisers. However, these breach reports were often provided to us a substantial period after the institution became aware of the matters giving rise to the serious compliance concerns.

166 Breach reports are an important part of ASIC's regulatory framework and a valuable source of information. Not every instance of adviser non-compliance will trigger the need to lodge a breach report with ASIC. However, when adviser non-compliance is identified, and results in a significant breach or likely breach of the licensee's obligations, it must be reported to ASIC in a timely manner.

167 Breach reporting is time sensitive, and a breach report must be lodged with ASIC as soon as practicable, and no later than 10 business days, after the licensee becomes aware of a breach, or likely breach, that is significant: s912D of the Corporations Act and [Regulatory Guide 78 Breach reporting by AFS licensees](#) (RG 78).

168 We are aware that there is an industry-wide approach which considers that the time period for breach reporting commences only after the decision-makers delegated to decide whether a breach should be reported have determined that the breach or likely breach is *significant* to the licensee.

169 This approach has led to considerable delays in reporting to ASIC. For example, in one instance, an institution acknowledged that 179 days had passed from when it first became aware of the suspected non-compliance to formally assessing the breach as significant, and subsequently lodging a breach report with ASIC.

170 There appeared to be considerable delays in many other cases between the date the non-compliant conduct occurred and the date the breach report was lodged with ASIC. However, because many of the breach reports did not indicate when the institution first became aware of the breach, it has not been possible to accurately determine the extent of the delay.

171 While this approach may not necessarily contravene the breach reporting requirements, this lack of timeliness can affect the value of the breach report to ASIC. The delay in reporting non-compliant conduct to ASIC may also result in an increased risk of customer loss or detriment.

172 We are currently involved in the Treasury’s taskforce to review ASIC’s enforcement regime. The terms of reference for this taskforce include the adequacy of the frameworks for notifying ASIC of breaches of law: see paragraphs 90–91. As we have submitted to the taskforce, we believe that the regulatory tools available to us should be strengthened, particularly in relation to the breach reporting regime.

#### **Other notifications to ASIC**

173 In addition to the 42 SCC advisers who have been the subject of a breach report, 34 SCC advisers were notified to ASIC by the licensees in some other way—including, for example, through reports of misconduct. The remaining 73 SCC advisers were not notified to ASIC until the licensees identified and reported their SCC advisers to us in response to our direction.

174 We expect that, if an advice licensee identifies serious compliance concerns about an adviser, the advice licensee will voluntarily notify ASIC even if the obligation to lodge a breach report does not arise.

#### **Background and reference checking**

175 For some of the SCC advisers, we found that there were inadequacies in the approach taken by the institutions to background and reference checking. A detailed discussion of these findings is set out in Section D.

### **Next steps**

176 We will continue our review of the SCC advisers. As our reviews progress, more advisers are likely to be subject to banning actions or other enforcement action. We will report publicly on these outcomes.

## C Phase 2: Customer review and remediation

### Key points

We engaged with each of the institutions to oversee the development and implementation of a customer review and remediation framework. This engagement required that each institution:

- identify non-compliant advice provided by its advisers in the period between 1 January 2009 and 30 June 2015, and remediate affected customers; and
- appoint an external expert to provide assurance on the design and operational effectiveness of the framework.

We found that:

- the identification of high-risk advisers to be included in the scope of the review and remediation framework represented a significant challenge for the institutions; and
- as a result of our feedback, the institutions have improved their customer communication strategies, advice review templates, and compensation calculation methodologies.

## What we did

### Developing a review and remediation framework

- 177 Each of the institutions acknowledged that, in the past, they have had difficulties in identifying all of their high-risk advisers and remediating affected customers. Each of the institutions agreed that, to address these concerns, it was appropriate to develop and implement a framework for large-scale customer review and remediation.
- 178 Our objective in Phase 2 was to ensure that the institutions identified and remediated—in a comprehensive, timely, fair and transparent manner—customers who had suffered loss or detriment as a result of receiving non-compliant advice between 1 January 2009 and 30 June 2015.
- 179 To achieve this objective, we have worked with the institutions to ensure that they each develop a review and remediation framework that would be consistent with the principles in RG 256 and, in particular, that this framework would:
- (a) provide a streamlined review and remediation process for the advice licensees within each institution;
  - (b) operate efficiently, honestly and fairly—in line with advice licensees' obligations—by addressing the key principles set out in our guidance; and
  - (c) provide customers with confidence in the fairness of remediation outcomes.

- 180 While developing their review and remediation frameworks, the institutions produced supporting documents for our consideration. These included:
- (a) methodologies for identifying the advisers who provided non-compliant advice;
  - (b) methodologies for identifying the customers affected by the non-compliant advice;
  - (c) policies and guidance on customer communications;
  - (d) advice review templates and guidance;
  - (e) compensation calculation methodologies;
  - (f) policies and guidance on the governance processes for the review and remediation; and
  - (g) the terms of engagement for an external expert to provide assurance on the framework.

Note: We advised the institutions that the advisers who should be considered for the purposes of paragraph 180(a) should not be limited to their identified SCC or OCC advisers.

181 Since July 2015, ASIC has held regular meetings with each of the institutions to oversee the development and implementation of their review and remediation framework. As part of these meetings, we provided feedback on the documents that were provided throughout the project.

182 As part of developing their review and remediation framework, we encouraged each of the institutions to:

- (a) establish a variation of the FOS terms of reference to allow customers within the scope of the remediation to lodge a claim with FOS relating to advice extending back to 1 January 2009 and up to a monetary limit of \$1 million;
- (b) offer financial assistance to all customers who wished to seek their own professional opinion about the advice licensee's remediation decision; and
- (c) appoint an external expert to provide assurance on the design and operational effectiveness of the review and remediation framework.

Note: For further details about each of the elements considered by the institutions as part of their large-scale review and remediation frameworks, see Table 3.

183 For the reasons set out in paragraphs 116–119, the approach taken by CBA has differed from the other institutions. Rather than developing a new review and remediation framework in response to this project, CBA has engaged with us to demonstrate that its existing processes, developed to address previously identified issues, satisfy ASIC's expectations.

## Key elements of review and remediation frameworks and progress made

184 As at 23 February 2017, some institutions are yet to finalise all of their framework documentation. Our work on this phase of the project is therefore ongoing. An overview of the current status of each institution's review and remediation framework is set out in Table 2.

**Table 2: Status of each institution's review and remediation framework as at 23 February 2017**

Institution	Current progress made
AMP	<p>AMP commenced implementation of its large-scale review and remediation framework in relation to its identified high-risk advisers in September 2016.</p> <p>AMP is continuing to develop KRIs to identify other high-risk advisers.</p>
ANZ	<p>ANZ implemented its large-scale review and remediation framework in July 2016. At this time, ANZ's external expert provided assurance that, at a high level, the design of this framework was appropriate. ANZ is currently reviewing 16 SCC advisers under this framework.</p> <p>Following the publication of RG 256, initial feedback received from ASIC and the findings from ANZ's pilot program, ANZ has developed a revised framework. This framework remains subject to assurance of its design effectiveness by ANZ's external expert, and approval by ASIC.</p> <p>ANZ is continuing to develop KRIs to identify any high-risk advisers not identified by its previous monitoring and supervision processes.</p>
CBA	<p>CBA has a process in place for the large-scale review and remediation of customers. This work was developed in response to business-initiated programs and other regulatory outcomes.</p> <p>Three of the advice licenses within CBA are seeking external expert assurance that the work to identify high-risk advisers and remediate affected customers is adequate: see paragraphs 116–119 for the advice licensees not included in the current work.</p> <p>CBA has advised that its large-scale review and remediation framework is being reviewed to ensure that it is consistent with the principles set out in RG 256.</p> <p>ASIC will review this work as it is completed.</p>
NAB	<p>NAB announced the commencement of a remediation program in February 2015.</p> <p>NAB implemented its revised large-scale review and remediation framework (Customer Response Initiative (CRI)), approved by ASIC, on 21 October 2015: see <a href="#">Media Release (15-306MR) National Australia Bank to implement a large-scale financial advice remediation program</a> (21 October 2015).</p> <p>At that time, the CRI focused on identifying and remediating customers of its currently identified high-risk advisers.</p> <p>NAB has developed KRIs to identify other high-risk advisers.</p>
Westpac	<p>Westpac has undertaken significant work to identify and remediate customers affected by non-compliant advice provided by its identified high-risk advisers. This work, which commenced before we engaged with Westpac as part of this project in July 2015, is ongoing.</p> <p>Westpac is seeking external expert assurance of the work that it has already undertaken, including whether previous assessments of customer remediation are consistent with ASIC's expectations in RG 256.</p> <p>As a result of this project, Westpac has developed a customer review and remediation framework, and we have provided feedback on this framework.</p> <p>Westpac has developed KRIs to identify other high-risk advisers.</p>

Source: Institutions, ASIC

- 185 In Table 3, we set out further detail about what we consider to be the key elements of a large-scale review and remediation framework, and the progress made by each institution towards incorporating these elements.
- 186 The review and remediation frameworks set out in Table 3 relate to the identification of non-compliant advice and the assessment of remediation in circumstances where the customer may not have complained about the advice, or may have had no reason to believe that they received non-compliant advice.
- 187 If a customer has made a complaint to the institution about the advice they received, we expect that this will have been dealt with by the institution in accordance with its processes for internal dispute resolution (IDR) and external dispute resolution (EDR).
- 188 Following the implementation of the large-scale review and remediation frameworks, we expect there to be a high degree of consistency in customer remediation outcomes, whether this occurs through IDR and EDR, or through large-scale customer review and remediation.



**Table 3: Key elements of the institutions' review and remediation frameworks and progress made as at 23 February 2017**

Element	AMP	ANZ	CBA	NAB	Westpac
Key risk indicators to assist in identifying high-risk advisers not identified by previous monitoring and supervision processes	Nearing finalisation	Being developed	Design and implementation finalised and currently being externally assured	Design finalised and externally assured	Nearing finalisation
Key risk indicators to assist in identifying affected customers	Design finalised and externally assured	Finalised and currently being externally assured	Design and implementation finalised and currently being externally assured	Design finalised and externally assured	Nearing finalisation
Customer communications: <ul style="list-style-type: none"> <li>• template letters;</li> <li>• call scripts; and</li> <li>• brochures</li> </ul>	Design finalised and externally assured	Nearing finalisation	Developed as part of its previous review and remediation processes  Due to be updated in response to RG 256 and then to be reviewed by ASIC	Design finalised and externally assured	Nearing finalisation
Advice review template and guidance	Design finalised and externally assured	Nearing finalisation	As above	Design finalised and externally assured	Nearing finalisation
Compensation calculation methodology	Design finalised and externally assured	Nearing finalisation	As above	Design finalised and externally assured	Nearing finalisation
Variation of FOS terms of reference to ensure customer access to: <ul style="list-style-type: none"> <li>• an increased monetary limit to \$1 million; and</li> <li>• an extended time period—back to at least 1 January 2009</li> </ul>	Agreed	Agreed	Not applicable	Agreed	Agreed (subject to formal documentation being finalised with FOS)

Element	AMP	ANZ	CBA	NAB	Westpac
Reimbursement of <i>all</i> customers wishing to seek an independent opinion about remediation	Will reimburse customers seeking independent advice from qualified professionals—up to a set maximum amount of \$5,000 plus GST	Not agreed. ANZ will indemnify vulnerable customers, or customers suffering loss as a result of adviser fraud, for their reasonable costs of obtaining independent advice about their remediation outcome. ANZ has advised us it will assess other customers on a case-by-case basis, and will provide assistance where it considers this to be appropriate. This support could take the form of costs indemnity or other assistance. ANZ will provide support in excess of \$5,000, where appropriate	Not agreed. As part of its current review and remediation framework, CBA considers on a case-by-case basis whether to contribute to the cost of the customer obtaining independent advice. CBA has advised us that it will take into account factors such as customer vulnerability and understanding (e.g. customers from non-English speaking backgrounds)  Note: These details recorded for CBA are independent of the requirements agreed with ASIC by advice licensees within the CBA Group under an enforceable undertaking or AFS licence conditions: see <a href="#">11-229MR</a> and <a href="#">15-083MR</a> .	Will reimburse customers seeking independent advice from qualified professionals—up to a set maximum amount of \$5,000 plus GST	Not agreed. Vulnerable customers who require assistance to understand and make an informed assessment about the circumstances relating to their remediation will be reimbursed by Westpac for the reasonable cost of an appropriate and independent interpreter and/or support person, determined on a case-by-case basis
Engagement of an external expert to provide assurance	Expert appointed	Expert appointed	Expert appointed	Expert appointed	Expert appointed

Note 1: Although ASIC's discussions with the institutions are finalised or nearing finalisation for many elements of the review and remediation frameworks, the design and operational effectiveness remain subject to assurance provided by an external expert.

Note 2: Once finalised, the institutions' review and remediation frameworks will be subject to continuing improvement for a number of reasons, including the insights gained from the implementation of their frameworks, feedback from the external expert, changes in technology and improvements in data analytics, feedback from both customers and ASIC, and changes in industry practices that may give rise to new areas of risk.

Source: Institutions, ASIC

## What we found

### Identifying high-risk advisers and affected customers

189 Identifying high-risk advisers and customers affected by non-compliant advice who fall within the scope of a review and remediation has been a significant challenge for the institutions.

190 In the past, KRIs commonly used to identify high-risk advisers and affected customers for remediation arose predominantly from customer complaints and adviser audit outcomes. More recently—and as part of the institutions’ work to develop their review and remediation frameworks for this project—the institutions have recognised the importance of using data analytics to develop new KRIs to improve the identification of high-risk advisers and affected customers.

Note: The development and application of data analytics within the monitoring and supervision process is discussed in Section D.

191 The use of data analytics to develop KRIs for identifying high-risk advisers and affected customers is an essential part of the institutions’ review and remediation frameworks. However, the development of KRIs using data analytics has presented challenges for the institutions because:

- (a) older data was found to be less reliable, unavailable, or non-existent;
- (b) paper-based record keeping made information more difficult to access;
- (c) incompatible legacy systems, as a result of technology upgrades and business mergers, made data extraction difficult; and
- (d) different data-recording methods were used within the institutions and across their different licensees, resulting in different naming conventions and data that were not easily comparable.

192 These difficulties have influenced the volume and quality of digital data available to the institutions for assessment. Limited digital data reduces the range of KRIs that can be applied effectively.

193 We have also observed situations in which advice licensees had difficulty in accessing copies of records that they still controlled legally, but not physically. This was generally because the adviser who had provided the advice under review had moved to a new licensee and the adviser refused or failed to provide the relevant records.

Note: ASIC has recently amended [Class Order \[CO 14/923\]](#) *Record-keeping obligations for Australian financial services licensees when giving personal advice* to require that advice licensees must have access to records for the period of time that the records are required to be kept, even if a person other than the licensee holds the records; and to make explicit that authorised representatives who are advisers must keep records, and give the records to their authorising licensee, if the licensee requests the records for the purposes of complying with financial services laws. See also Media Release ([16-362MR](#)) *ASIC clarifies record-keeping obligations for financial services licensees* (27 October 2016).

- 194 The institutions have told us that one of the challenges they face in developing effective KRIs is choosing which KRIs to apply and how to set appropriate tolerance levels at which a KRI will be triggered.
- 195 Appropriate tolerance levels seek to strike a balance between limiting ‘false positive’ results and maintaining KRI effectiveness. We observed that, to set appropriate tolerance levels, the institutions engaged with subject-matter experts and considered their own data and industry averages.
- 196 Appendix 4 sets out a list of the KRIs that we have observed from this project, which has been compiled, in part, through consultation with the institutions. Not all of the listed KRIs will be used by each institution as part of its review and remediation framework for a number of reasons, including:
- (a) because there is limited availability of data, as set out in paragraph 191; and
  - (b) because the KRI is not an effective indicator for a particular licensee’s adviser or customer population.
- 197 For each institution’s review and remediation framework, we have required that an external expert test and report on the KRIs that will be used and, in particular, to confirm that the KRIs will be reasonably effective in identifying high-risk advisers.

### **Customer communication**

- 198 In the past, we have found that advice licensees’ communication with their customers about remediation has not been clear, and this often resulted in low rates of customer engagement. To understand the current position, we have reviewed, or will review, the institutions’ proposed customer communication policies and template documents.
- 199 We encouraged each of the institutions to develop customer communication strategies that:
- (a) are transparent and clearly identify why the customer is being written to and what action, if any, the customer should take; and
  - (b) allow customers adequate time and opportunity to consider and respond to communications.
- 200 During this phase of the project, we consistently found that there was room for improvement in the quality of the communication with customers. Common improvements that we required to be made included:
- (a) being clear about the purpose of the communication—including that the customer has, or may have, received non-compliant advice;
  - (b) setting out clearly the steps the customer can take to assist the progress of their remediation assessment; and

- (c) clarifying that the institution will assess the advice the customer received, whether or not the customer chooses to be involved in the process.

201 To assist with customer engagement, some institutions have also developed a customer information brochure to be sent with the initial customer communication. We are encouraging each institution to develop this as part of their finalised customer communication documents.

202 Table 4 sets out some observations we made about poor customer communication, and why that communication was not effective.

**Table 4: Examples of poor customer communication**

Poor customer communication	Reasons why communication was poor
We informed you that we have evaluated the advice provided by Adviser A and believe your circumstances should be reviewed to ensure the advice is meeting your objectives.	The licensee does not make clear that the correspondence is only being sent because it has identified the risk that the customer may have received non-compliant advice.
Even though you have declined our offer to review the appropriateness of the advice previously provided to you, we would like to encourage you to take up the offer of a review with one of our advisers.	In addition to the reason set out in the row above, this communication does not set out the process for the review and remediation that the licensee is conducting, and presents the review of advice as a bonus that the licensee is offering to the customer.

Note: The examples in this table have been de-identified but are drawn from actual observations within this project.

Source: Institutions, ASIC

### Advice review templates and guidance

203 An effective review and remediation process relies on the institutions fairly and correctly assessing whether the customer has received non-compliant advice that caused loss or detriment to the customer. Institutions use an advice review template to assist in the assessment process and record the findings.

204 The advice review templates we have seen to date have generally been appropriately focused on compliance with the relevant financial services laws.

205 The effectiveness of the templates relies on each institution ensuring that the staff who use them are appropriately qualified and trained, and are allocated sufficient resources.

206 We expect that the institutions' external experts will select a sample of advice to test, and consequently assure and report on, the effectiveness of the advice review process.

### Compensation calculation methodologies

207 We required each institution to develop and apply guidance and policies to calculate the amount of customer loss, consistent with the compensation principles of the institution's EDR scheme—in each case the Financial Ombudsman Service (FOS).

208 In some cases, we observed different approaches between the institutions in their proposed interpretation of the FOS compensation principles and, in particular, the level of guidance provided to assess customer loss. For example, the [FOS Terms of Reference](#) provide for compensation of direct financial loss. We had some concerns that the proposed guidance to calculate customer loss sought to interpret what is meant by direct financial loss too narrowly, potentially limiting the extent of legitimate claims.

209 We also observed a tendency for guidance to be developed with reference to case studies which interpreted the FOS principles in narrow factual scenarios. We encouraged the institutions to provide additional case studies and guidance to support the application and interpretation of the FOS principles.

210 In developing their compensation calculation methodologies, where the institutions had little or no data to accurately calculate compensation (e.g. if it could not be determined what alternative investment strategy a customer would have implemented if compliant advice had been provided), we encouraged the use of a proxy interest rate, equivalent to the Reserve Bank of Australia (RBA) cash rate plus a margin of 6% per year.

Note: For an example of how an AFS licensee has applied a proxy interest rate in the absence of adequate data to calculate accurate compensation, see Example 8 in [RG 256](#).

### Compensation

211 As reported to ASIC, at 31 December 2016 a total of approximately \$30 million had been paid across the institutions to approximately 1,347 customers who had suffered loss or detriment as a result of non-compliant conduct by 97 currently identified high-risk advisers whose conduct occurred between 1 January 2009 and 30 June 2015.

Note: In this context, the compensation is not limited solely to customer loss or detriment arising out of non-compliant advice.

212 The figures set out in this report do not include the compensation amounts paid in relation to fees-for-no-service issues, as noted in [REP 499](#), or the compensation paid under CBA's other large-scale remediation programs—

totalling approximately \$80 million—as noted in [15-083MR](#), [16-415MR](#) and CBA’s [Open Advice Review Program](#).

- 213 The total compensation amount can be broken down into:
- (a) \$5,928,821 paid in response to customer complaints;
  - (b) \$22,765,365 paid under previous or existing remediation processes; and
  - (c) \$1,572,086 paid under the frameworks for large-scale review and remediation developed as part of this project.

Note: The above figures are rounded to the nearest dollar.

- 214 Table 5 sets out the compensation paid by the institutions to customers as at 31 December 2016.

**Table 5: Compensation paid to customers as at 31 December 2016**

Compensation type	AMP	ANZ	CBA	NAB	Westpac
Compensation paid under the review and remediation framework developed as part of this project	\$1,105,909 (341 customers) (8 advisers)	\$53,363 (2 customers) (1 adviser)	N/A	\$3,400 (2 customers) (2 advisers)	\$409,414 (11 customers) (4 advisers)
Compensation paid under previous or existing remediation processes	\$5,095,248 (24 customers) (4 advisers)	\$6,677,105 (182 customers) (11 advisers)	\$4,158,167 (207 customers) (10 advisers)	\$757,952 (59 customers) (2 advisers)	\$6,076,893 (221 customers) (12 advisers)
Compensation paid under complaints process	\$1,063,430 (64 customers) (14 advisers)	\$1,169,643 (116 customers) (21 advisers)	\$1,072,974 (26 customers) (11 advisers)	\$1,523,207 (56 customers) (24 advisers)	\$1,099,567 (38 customers) (14 advisers)
<b>Total compensation paid including under remediation and complaints</b>	<b>\$7,264,587</b> (429 customers) (19 advisers)	<b>\$7,900,111</b> (300 customers) (22 advisers)	<b>\$5,231,141</b> (233 customers) (16 advisers)	<b>\$2,284,559</b> (115 customers) (24 advisers)	<b>\$7,585,874</b> (270 customers) (16 advisers)

Note 1: The data in this table has been compiled and interpreted by ASIC from the information received from the institutions. It relates to the currently identified high-risk advisers whose non-compliant conduct occurred between 1 January 2009 and 30 June 2015.

Note 2: The compensation figures are rounded to the nearest dollar.

Note 3: An adviser or a customer can appear under more than one compensation type.

Note 4: As part of its pilot work under the review and remediation framework developed as part of this project, NAB focused on an adviser whose non-compliant conduct commenced before 1 January 2009. Under its CRI, NAB has paid \$3,385,154 as compensation to affected customers (as at 31 October 2015). These figures do not appear in this table.

Note 5: The figures recorded for CBA do not include compensation amounts paid under its previous large-scale remediation programs: see paragraph 211.

Source: Institutions, ASIC

## Next steps

- 215 We are continuing our discussions with the institutions about the outstanding elements of their review and remediation frameworks, including the external expert assurance of the design effectiveness of their frameworks. We will publicly report on this as each institution's review and remediation framework is implemented.
- 216 Following implementation, the external experts will periodically report to ASIC on their work to assure operational effectiveness of the review and remediation frameworks.
- 217 We will provide updates on the institutions' remediation of customers who have suffered loss or detriment as a result of receiving non-compliant advice between 1 January 2009 and 30 June 2015.



## D Phase 3: Monitoring and supervision of advisers

### Key points

We found that the advice licensees' background and reference-checking processes when appointing advisers were inadequate, and that this allowed the circulation of non-compliant advisers within the financial advice industry.

We also assessed whether the Phase 3 licensees' business-as-usual audits were effective and, in particular, whether their auditors had correctly identified whether advisers had demonstrated compliance with the best interests duty and related obligations.

From our assessment, we found that the licensees' audit processes were:

- *effective* in 18% of the sample files;
- *partially effective* in 57% of the sample files; and
- *ineffective* in 25% of the sample files.

Where we assessed that the business-as-usual adviser audit was ineffective or partially effective, we found that there were 48 cases where some form of corrective action should have been recommended by the licensee's auditor but none had been recommended.

We found that the effectiveness of the audit process was affected by:

- the inadequacy of the file audit questionnaire;
- the inadequacy of the auditor's assessment of a customer file to review whether advisers had demonstrated compliance with the best interests duty and related obligations;
- recommendations that the customer file be updated during the adviser audit process; and
- inadequacies in audit record keeping.

We observed that the institutions have been developing increasingly sophisticated KRIs to identify high-risk advisers as part of their monitoring and supervision processes.

### Background to Phase 3

218

The Corporations Act requires advice licensees to implement adequate monitoring and supervision processes to provide financial services efficiently, honestly and fairly, and to ensure their representatives provide financial services that comply with the financial services laws.

Note: For further detail on these obligations, see s912A of the Corporations Act and Section C of [Regulatory Guide 104](#) *Licensing: Meeting the general obligations* (RG 104).

- 219 In Phase 3 of the project, we reviewed the way that 10 advice licensees selected from within the institutions (Phase 3 licensees) monitor and supervise their advisers and the quality of advice provided.
- 220 Effective monitoring and supervision of advisers requires a wide-reaching framework with many elements. These elements may include the use of data analytics, effective records management, business-as-usual audits, impromptu audits, appropriate background and reference checking, pre-vetting of advice, and qualified and competent compliance staff.
- 221 For this report, we chose to focus on two elements that we consider to be integral to an effective monitoring and supervision framework:
- (a) *background and reference-checking processes*: reference checking when recruiting advisers is a longstanding area of concern for ASIC, and we have observed that advisers whose past conduct has been identified as non-compliant sometimes circulate undetected within the financial advice industry. Following our previous reporting and guidance on this issue (see paragraphs 129–131), we wanted to observe whether there have been appropriate changes to processes to address these deficiencies; and
  - (b) *the effectiveness of the adviser audit process*: in Phase 1, the institutions notified us that the adviser audit process was central to their identification of 58 of the SCC advisers: see paragraph 163. We therefore wanted to assess the licensees' current adviser audit processes to determine whether these were effective in assessing whether an adviser had demonstrated compliance with the best interests duty and related obligations when providing advice. For this report, we focused on business-as-usual audits conducted during 2016 because of:
    - (i) the availability of better quality data and records to allow for a comprehensive customer file to be produced; and

Note: Paragraph 27 sets out some of the reasons observed, as part of this project, for limitations on data collection and retention.

    - (ii) the standardisation of the way that these more recent audits are conducted as a result of updated policies reflecting the FOFA reforms.
- 222 As a result of the information evaluated in Phase 2 and Phase 3, we have made some observations about the way institutions are using data analytics, as part of their monitoring and supervision processes, to develop KRIs for identifying high-risk advisers.

## Background and reference-checking processes

223 This project is not the first time that ASIC has examined industry policies and practices in relation to the processes for background and reference checking of advisers. For further details, see paragraphs 129–131.

### What we did

224 We used our compulsory notice powers to direct the Phase 3 licensees to provide information about their background and reference-checking processes. In particular, we sought the following information:

- (a) whether recruiting licensees sought information from former licensees before appointing a new adviser, and if so, details of the information sought; and
- (b) whether the former licensees provided information to the recruiting licensees in response to requests for background or reference checks for a former adviser, and if so, the details of the information provided.

### What we found

225 Our review showed that all of the institutions were aware of Standards Australia's reference-checking handbook, and followed parts of it. However, none of the Phase 3 licensees followed every aspect of it. We observed that, most often, the deficiencies related to the extent to which the former licensees followed the handbook guidance on the provision of information to a recruiting licensee.

Note: For further details about Standards Australia's Handbook HB 322-2007, see paragraph 130.

### Factual background information

226 We found that the Phase 3 licensees generally contacted an adviser's former licensee before appointing the adviser, and that requests for factual information, such as verification of the adviser's employment, were responded to adequately.

227 While we acknowledge it is necessary to verify relevant factual information, it is also important to seek information about the adviser's compliance history from an appropriate person.

### Compliance history (including audit reports)

228 We found that the Phase 3 licensees often requested details, from the former licensee, of an adviser's compliance history together with the adviser's previous audit reports.

229 We found, however, that there was widespread failure by former licensees to respond adequately to such requests for information or to provide the relevant audit reports.

230 Even where the recruiting licensee did receive information that raised potential concerns about the adviser's past non-compliant conduct, we observed instances where the recruiting licensee failed to make appropriate further inquiries and appointed the adviser regardless.

*Who should be asked to provide information?*

231 The recruiting licensee should ensure that it obtains an adviser's compliance history from an appropriately qualified and authorised person within the former licensee.

232 We found that, in some instances, references were sought from former colleagues of an adviser. Former colleagues are often not appropriately independent and are unlikely to have had access to the advice licensee's compliance records for the adviser.

### Case study 1: Appropriateness of referee

#### Scenario

Adviser B's employment with Old Bank is terminated for serious misconduct.

Adviser B applies to be an adviser at New Bank. On their application, the adviser does not disclose that their employment had been terminated.

Adviser B provides New Bank with details of two referees. Both are former colleagues, one of whom no longer works for Old Bank. Neither has supervised Adviser B in any capacity.

Neither reference provided to New Bank discloses the genuine reason for Adviser B's departure from Old Bank.

Adviser B is appointed by New Bank.

#### Commentary

We expect that a recruiting licensee will take reasonable steps to ensure that compliance information is sought from staff members of the former licensee who are appropriately informed and authorised to provide it.

If references are provided in a personal capacity by former colleagues (rather than on behalf of the former licensee), this should be made clear to the recruiting licensee so that the need to seek further information is apparent.

Note: This case study has been de-identified but is based on an actual example observed within this project.

#### Policy for providing references

233 We found that only two of the Phase 3 licensees had a written policy about providing background and reference material in relation to their former advisers. The remaining eight licensees did not have a written policy about responding to a background and reference-checking request, although they had generally accepted practices. The findings below refer to both of these situations as 'policies'.

## Case study 2: Completing a background reference check

### Scenario

Adviser C resigns after receiving a warning letter from Old Bank raising certain compliance concerns about advice the adviser has provided.

Two weeks later, Old Bank determines, internally, that it would have terminated Adviser C's employment if they had not resigned.

Adviser C seeks employment as a financial adviser with New Bank. New Bank has a policy of conducting background and reference checks with the compliance manager of an applicant adviser's most recent AFS licensee.

New Bank contacts Old Bank to seek a compliance reference for its proposed appointment of Adviser C. Old Bank has a policy of not providing a written reference if there are known adviser compliance failings. Old Bank therefore declines to provide a written reference to New Bank. The compliance staff at Old Bank, however, offer to provide a verbal reference. New Bank does not accept this offer.

As a result, New Bank appoints Adviser C without having any knowledge of their poor compliance record.

### Commentary

We expect that licensees will take reasonable steps to conduct background and reference checks when recruiting advisers. This did not occur in this case.

Note: This case study has been de-identified but is based on an actual example observed within this project.

- 234 As set out in paragraph 229, we found that most of the Phase 3 licensees did not provide information to a recruiting licensee about an adviser's compliance history. We were told that this was because of concerns about:
- (a) a potential breach of the privacy legislation;
  - (b) a perception that a defamation action may be pursued by the adviser; and
  - (c) procedural fairness in circumstances where the adviser had resigned before investigations into their suspected non-compliant conduct had been completed, and the adviser had therefore not had an opportunity to respond.
- 235 Table 6 summarises the policies on providing information about an adviser's background for the Phase 3 licensees (grouped by institution).

**Table 6: Summary of policies for providing information about former advisers**

Institutions	Policy on responding to requests for background checks
A (employee and authorised representative model)	A will only provide the details that are specifically asked for and that the adviser has specifically consented to having released.
B (employee and authorised representative model)	B will provide background-checking information, provided that the adviser gives written consent allowing the information to be released.
C (employee representative model)	C (employee representative model) does not provide responses to background checks because of privacy and confidentiality considerations.  If the <i>adviser</i> requests the release of limited information (e.g. confirmation of employment, length of service and nature of the role), this can be provided.
C (authorised representative model)	C (authorised representative model) will provide background-checking information.
D (employee and authorised representative model)	D will generally only provide the details that are specifically requested and that the adviser has specifically consented to having released. However, if the adviser has not given their consent, D may still consider, on a case-by-case basis, whether some information can be disclosed.
E (employee and authorised representative model)	E will provide background-checking details; however, if there are any compliance issues, only a verbal response may be provided.

Note: Institutions A, B, D and E had the same policies on providing background and reference checks for both their employee representative models and the authorised representative models. Only Institution C had any material differences between the employee representative model and the authorised representative model.

Source: Institutions, ASIC

236

The policies set out in Table 6 result in limited information sharing between the former licensee and the recruiting licensee. We found that ineffective background and reference checking has resulted in non-compliant conduct by advisers not being identified to recruiting licensees. This is attributable to the practices and procedures of both the recruiting licensee and the former licensee—together with legal and procedural fairness concerns: see paragraph 234.

### Case study 3: Information sharing between licensees

#### Scenario

Adviser D has applied for a position as adviser with New Bank.

New Bank has a policy of conducting compliance reference checks with an applicant adviser's most recent licensee (although not necessarily with the compliance manager). New Bank contacts Old Bank to request a compliance reference check for Adviser D.

New Bank's request is made using the consent, direction and release forms from Appendices B and C of the reference-checking handbook (Standards Australia, HB 322-2007), appropriately signed by Adviser D. The forms direct Old Bank (and give Adviser D's consent to the extent that it is required) to share information about Adviser D's compliance history, and to release Old Bank from legal responsibility for any loss, damage or claim arising from sharing this information.

It is Old Bank's policy not to provide a response in writing if there are known compliance concerns about an adviser. Despite the direction and release, Old Bank refuses to answer the specified questions, stating that it is unable to provide the information sought, with no further explanation provided.

### **Commentary**

We expect that licensees will respond to a request for a background reference check, particularly when the adviser has consented to the disclosure.

Note: This case study has been de-identified but is based on an actual example observed within this project.

### **Improving industry standard of background and reference checking**

- 237 The ABA has recognised that there have been inadequacies in the background and reference-checking processes within the financial advice industry.
- 238 The ABA has recently released its protocol on reference checking and sharing information about an adviser's compliance, risk management and quality of advice.
- 239 We consider that the ABA protocol has the potential to address some of the failings we observed relating to background and reference checking. We will continue to liaise with the ABA on this important initiative, as we strongly support efforts to improve the background and reference checking of advisers.
- 240 The effectiveness of the protocol will be affected by:
- (a) the extent that AFS licensees subscribe (at present, the ABA reports that subscribing licensees appoint approximately 38% of the advisers recorded on ASIC's financial advisers register); and
  - (b) the exceptions, in the protocol, to the obligation to provide information, including:
    - (i) any legal obligations or considerations that prevent the sharing or disclosure of information; and
    - (ii) operational reasons (e.g. the AFS licensee does not have the required records).

- 241 In relation to the first issue, the protocol states that any AFS licensee with financial advisers operating under its licence may subscribe to the protocol, and must then adhere to its obligations. This includes licensees that are not ABA members. The ABA has published a list of all current subscribers to the protocol. We expect that this ongoing public reporting will encourage non-ABA licensees to contact the ABA to become subscribing licensees.
- 242 In relation to paragraph 240(b), because of the potentially broad nature of the protocol's exceptions, we consider that it is currently difficult to assess how effective it will be in practical terms. For example, we found in this project that the institutions often did not share their existing concerns about an adviser because they were concerned about the risk of adviser claims of defamation, misrepresentation, or breach of privacy or confidentiality. Each of these concerns may continue to fall within the exception relating to legal obligations or considerations. ASIC will continue to highlight this issue during the implementation of the protocol to understand the impact of the exceptions.
- 243 The ABA has informed ASIC that, to assess any impact the exemptions to the protocol may have, the current subscribing members have agreed to participate in a review of the protocol and its underlying processes. ABA will make enhancements to the protocol based on the outcomes of that review, which is due to take place during June 2017.
- 244 We consider that initiatives limiting the opportunity for an adviser whose past conduct has been identified as non-compliant to move undetected through the financial advice industry are fundamental in promoting customer trust and confidence in the industry and improving customer outcomes.
- 245 Appendix 2 sets out a checklist of issues for advice licensees to consider when conducting background checks on advisers. One of the key steps that we consider will improve background and reference checking is for the recruiting licensee to require an adviser to provide their consent for the release of the adviser's compliance history from the former licensee. In turn, the former licensee should rely on the adviser's consent to respond meaningfully.

## Effectiveness of adviser audit process

### What we did

#### Selecting the sample files

- 246 To test the effectiveness of the adviser audit process, we selected 160 customer files (sample files) from the Phase 3 licensees, where these files had been subject to the licensee's business-as-usual audit. The files related to advice given by 40 advisers (sample advisers).

Note: For further detail about how these 160 sample files were selected, see paragraphs 123–127 and 134–137.



- 247 To observe whether there would be a difference in outcome between files audited during the previous 12 months as part of the licensees' business-as-usual audit and files audited at our direction, we directed the licensees to audit the five most recently completed Statements of Advice (or records of advice) provided by each of the sample advisers.
- 248 We then selected four customer files for each sample adviser—half from the business-as-usual audit and the remaining half from the ASIC-directed audit.
- 249 The sample files were drawn from a range of high-rated and low-rated outcomes in the licensees' adviser audits. As a result, we expected to observe how each licensee applied its adviser audit process to different advice compliance issues, including non-compliant advice.

Note: The 160 sample files represent a very small subset of the total advice provided by the Phase 3 licensees. Our findings are therefore limited by the scope of the work we have undertaken.

### **Reviewing the sample files**

- 250 We observed a wide variety of adviser audit processes—sometimes even between licensees within the same institution. To draw conclusions about the effectiveness of each adviser audit process, we assessed the sample files to determine, in each case, whether the adviser had demonstrated compliance with the best interests duty and related obligations in giving advice.
- 251 We did this by first applying our usual file review processes. We then compared our assessment against the licensee's adviser audit outcomes for each sample file to determine whether the licensees had identified the same compliance concerns that we found during our file review process.
- 252 The sample files were:
- (a) reviewed by ASIC analysts or our external consultant; and
  - (b) subject to quality checks.
- Note: The external consultant is an independent subject matter expert engaged as an agent of ASIC. For further detail, see paragraph 140.
- 253 We reviewed the files against the obligations in the Corporations Act, including the obligations in Div 2 of Pt 7.7A; however, for the purposes of assessing the effectiveness of the licensees' adviser audit process, we treated the files as fully compliant if the adviser had demonstrated compliance with s961B, 961G and 961J.
- 254 Table 7 sets out a summary of these obligations.

**Table 7: Summary of the requirements in s961B, 961G and 961J of the Corporations Act**

Statutory provision	Summary of requirements
Best interests duty: s961B(1)	An advice provider must act in the best interests of the customer in relation to the advice they provide to the customer.
Safe harbour for complying with the best interests duty: s961B(2)	Section 961B(2) provides a 'safe harbour' that advice providers may rely on to prove they have complied with the best interests duty. If an advice provider shows they have taken the steps in s961B(2), they have met their obligation to act in the best interests of the customer.
Providing appropriate advice: s961G	Advice providers must only provide advice if it is reasonable to conclude that the advice is appropriate for the customer, assuming the best interests duty has been complied with.
Prioritising the interests of the customer: s961J	When providing customers with advice, advice providers must place the interests of the customers ahead of any interests they have or those of their related parties.

Note: An 'advice provider' is generally the adviser who provides the personal advice. This is the person to whom the obligations in Div 2 of Pt 7.7A of the Corporations Act apply: see also the key term definition of 'advice provider' in [Regulatory Guide 175 Licensing: Financial product advisers—Conduct and disclosure](#) (RG 175).

Source: ASIC

### Evaluation of the licensees' adviser audits for the sample files

- 255 The licensees' adviser audits in relation to the sample files were evaluated against ASIC's assessment of compliance, as set out in paragraph 253.
- 256 The results of our findings were grouped into three categories:
- (a) If the licensee's adviser audit correctly identified all areas of non-compliance (if any) in a sample file, we considered the audit to be *effective*.
  - (b) If the licensee's adviser audit identified some areas of non-compliance but our advice review found additional areas of non-compliance, we considered the adviser audit to be *partially effective*; and
  - (c) If the licensee's adviser audit identified no areas of non-compliance but our advice review found there were areas of non-compliance, we considered the audit to be *ineffective*.
- 257 If the licensee's adviser audit for a sample file identified non-compliance, we expected to see appropriate recommendations by the licensee's auditor to address the non-compliance by carrying out:
- (a) adviser consequence management—for example, requiring the adviser to:
    - (i) undertake additional training;
    - (ii) improve their record-keeping practices;
    - (iii) submit all draft advice to the licensee for approval before being authorised to provide the advice to a customer (pre-vet); and/or
    - (iv) undergo closer scrutiny under the licensee's monitoring and supervision systems; and

- (b) *customer remediation*, where appropriate—for example, requiring corrective disclosure, offering the customer access to a free advice appointment, rectifying errors that occurred when the advice was implemented, and/or paying monetary compensation.

## What we found

### Use of adviser audit

- 258 We found that the Phase 3 licensees used the adviser audit process to:
- (a) test adviser compliance with financial services laws and the licensee’s business rules;
  - (b) risk assess advisers for future monitoring and supervision (i.e. if the adviser audit outcome was poor, a licensee would apply an increased level of monitoring and supervision until the compliance concerns were resolved); and
  - (c) give feedback to advisers on areas needing improvement, where these were identified (often referred to as ‘coaching’).

### Frequency of adviser audit

- 259 We observed that the Phase 3 licensees conducted business-as-usual adviser audits at regular intervals. The frequency of the audits, and the number of files reviewed, depended on a number of factors. Table 8 summarises the frequency and the file selection process for business-as-usual adviser audits conducted by the Phase 3 licensees (grouped by institution).

**Table 8: Summary of business-as-usual adviser audit processes for Phase 3 licensees**

Institution	Frequency of audit	No. of files reviewed per audit	How customer files were selected for business-as-usual audit
A	Dependent on previous audit results—can occur every 3, 6 or 12 months	Minimum of 3 files	Files were selected from 4 advice categories: retirement income, personal insurance, superannuation, and investment strategies. However, where the adviser was authorised to provide advice on complex strategies, additional customer files were selected.
B	Dependent on adviser’s previous compliance rating—can occur every 3, 6 or 12 months	5 files	Files were selected from new customers (from the previous 12 months), taking into account the types of advice provided by the adviser.  The areas the audit focused on were influenced by the adviser’s profile.

Institution	Frequency of audit	No. of files reviewed per audit	How customer files were selected for business-as-usual audit
C	Dependent on the licensee and on the adviser's previous compliance rating—can occur every 3 or 12 months	2–6 files (with a minimum of 6 annually)	File selection was random and/or files were selected from areas of complex advice. File selection also depended on the adviser's compliance history and the individual licensee's processes.
D	Dependent on adviser's previous compliance rating and advice profile—can occur every 6 or 12 months	5–8 files	File selection was based primarily on the adviser's past compliance and complaints history, adviser profile, and responses to a pre-review questionnaire.
E	Dependent on adviser's previous compliance rating and advice profile—can occur every 3, 6, 9, 12 or 24 months	Minimum of 4 files	File selection was based on the use of KRIs to identify high-risk strategies (e.g. gearing, managed discretionary account products, structured products, self-managed superannuation funds (SMSFs) or limited recourse borrowing arrangements, and superannuation switching).

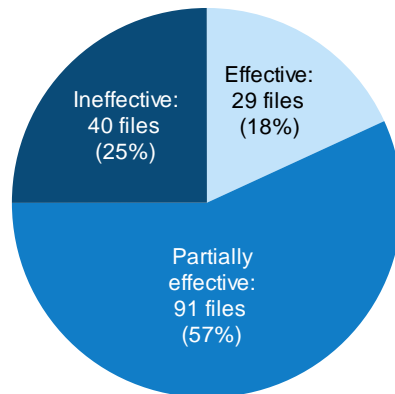
Source: Institutions, ASIC

### Differences in approach to audit

- 260 The Phase 3 licensees differed in their approach to the audit of customer files. The main differences we observed from the sample files were:
- (a) variations in the audit questionnaires and accompanying guidance about:
    - (i) whether sufficient evidence was held on the file to support making a finding;
    - (ii) the required level of compliance with financial services laws;
    - (iii) the required level of compliance with the licensee's internal policies and business rules; and
    - (iv) other legal compliance matters, such as compliance with privacy legislation; and
  - (b) different methodologies used to award audit ratings to the individual advisers based on the findings of the audit.

### Adviser audit outcomes

- 261 Our evaluation of the Phase 3 licensees' adviser audit processes showed that there were deficiencies in the effectiveness of these processes. Figure 4 shows the relative distribution of the effectiveness of the audit process for the sample files. For further details of how our evaluation was carried out, see paragraphs 250–256 and Figure 5.

**Figure 4: Effectiveness of adviser audit process for sample files**

Note: See Table 17 in Appendix 5 for the data shown in this figure (accessible version).

Source: Institutions, ASIC

262 From our assessment, we found that:

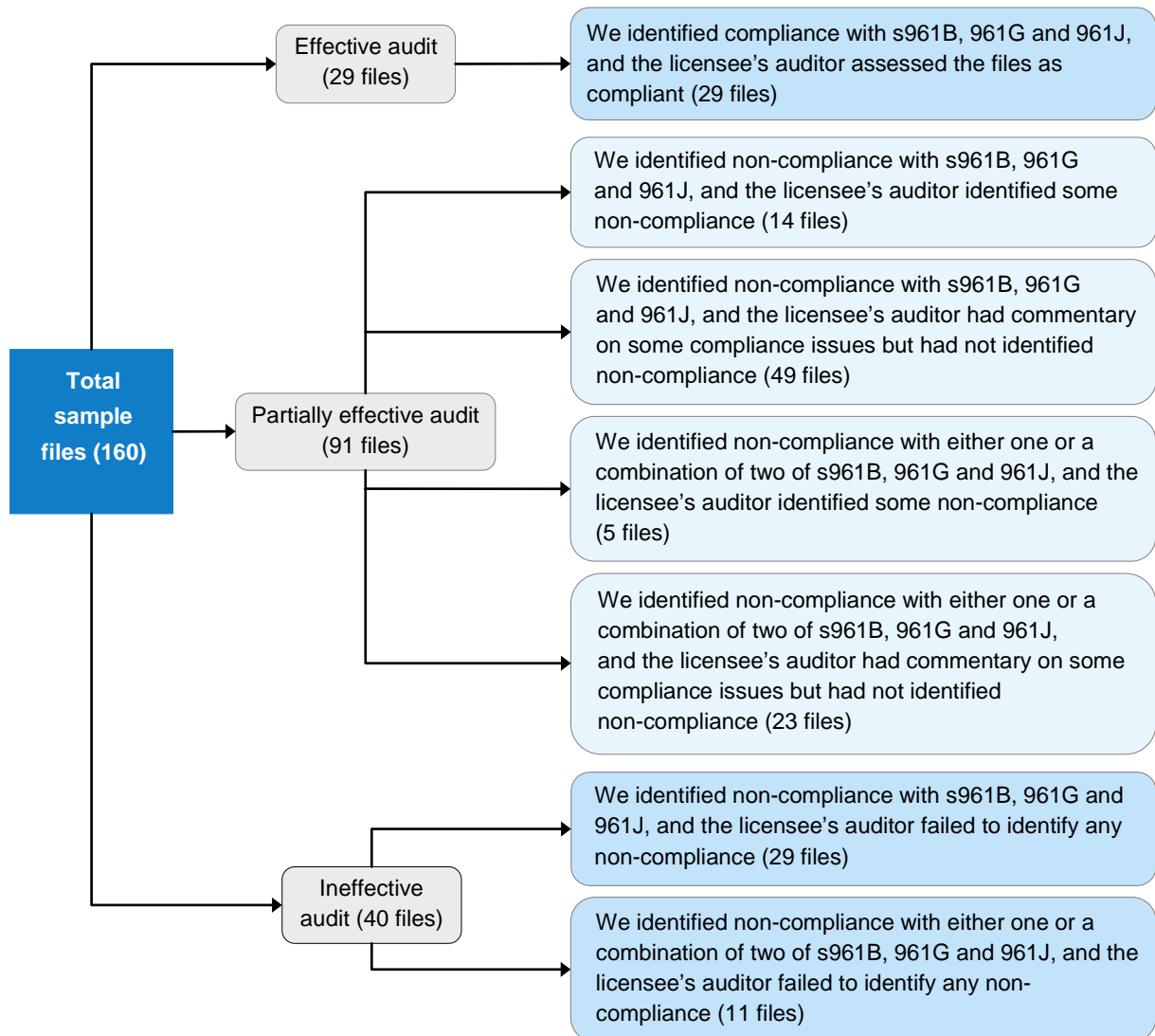
- (a) the audit process was *effective* in 18% of the sample files—that is, the findings by the licensees’ auditors aligned with our own file review. We observed an effective audit process only on files where no areas of non-compliance were identified by either the licensees’ auditors or our advice reviewers;

Note: We did not observe an effective audit process for any of the sample files where our reviewers found compliance concerns. In these cases, the licensees did not correctly identify all of the compliance concerns found.

- (b) the audit process was *partially effective* in 57% of the sample files—that is, some areas of non-compliance were identified by the licensees’ auditors, but our advice reviewers found additional areas of non-compliance; and
- (c) the audit process was *ineffective* in 25% of the sample files—that is, no areas of non-compliance were identified by the licensees’ auditors, but our advice reviewers found that there were some areas of non-compliance.

263 Figure 5 sets out a summary of the findings from our evaluation of how effective the licensees’ adviser audits were in identifying adviser compliance with the best interests duty and other statutory obligations.

**Figure 5: Our assessment of the adviser audit process for sample files**



Note 1: Table 7 sets out a summary of s961B, 961G and 961J.

Note 2: See Table 18 in Appendix 5 for the data shown in this figure (accessible version).

Source: Institutions, ASIC

*Incidental findings to the adviser audit process*

264 To assess the effectiveness of the adviser audit process, it was necessary to review the underlying customer files. The basis on which we assessed the advice is set out in paragraphs 246–254.

265 Our file review process was carried out by reviewing the entire customer file. Consistent with record-keeping obligations, we expect all the relevant information to be contained in the file. When assessing compliance, we expect to see positive evidence that shows:

- (a) why or how the advice was in the customer’s best interests;

- (b) that the advice is likely to satisfy the customer’s relevant circumstances and is likely to be appropriate for the customer; and
- (c) how the customer’s interests have been prioritised over those of the adviser or related parties.

266 We expected that some of the advice reviewed would be non-compliant because our sampling exercise included selecting files for which the licensees’ auditors had identified adviser compliance failings.

267 Our findings revealed that, in a significant number of the sample files, the adviser failed to demonstrate compliance with the best interests duty and related obligations. However, in these cases, we found that:

- (a) none of the adviser non-compliance fell within the definition of a ‘serious compliance concern’;
- (b) some of the adviser non-compliance did fall within the definition of ‘other compliance concerns’; and
- (c) regardless of how the adviser was selected—that is, whether the adviser had demonstrated past compliance concerns or whether they were selected randomly—there was no observable variance in either the rate of occurrence, or type, of the non-compliance.

268 Our proposed next steps in relation to these findings are set out at paragraph 293.

### **Factors affecting the adviser audit process**

269 As part of the Phase 3 review, we identified a number of deficiencies that affected the quality of the adviser audits undertaken by the Phase 3 licensees. We found that:

- (a) the adviser audit questionnaire often did not directly align with the best interests duty and related obligations;
- (b) the licensees’ auditors often failed to identify adviser non-compliance with the best interests duty and related obligations;
- (c) recommendations were made to amend customer files during the adviser audit process; and
- (d) audit record keeping was often inadequate.

#### *Inadequacy of the file audit questionnaire*

270 We observed deficiencies in the file audit questionnaires used by the Phase 3 licensees in the audit process. We found that the questionnaire often did not directly align with the best interests duty and related obligations, making it more difficult for the licensees’ auditors to assess compliance. For example:

- (a) the majority of the licensees’ questionnaires did not directly provide for the assessment of the appropriateness of advice under s961G; and

- (b) in some cases, the questionnaire addressed whether there was disclosure of conflicts of interest, but did not adequately address whether the customer's interests had been prioritised in line with s961J.

271 We expect the audit questionnaire to align with the best interests duty and related obligations. An effective adviser audit also requires auditors to use their professional judgement in recording why an adviser passes or fails each step. Appendix 3 sets out some template questions on the matters we would expect an audit questionnaire to include.

*Failure of auditor to identify non-compliance*

272 We observed that the auditor often failed to identify advisers who had not:

- (a) demonstrated compliance with the best interests duty (or satisfied the safe harbour steps), including;
  - (i) identifying the scope of the advice;
  - (ii) identifying the customer's relevant circumstances; and
  - (iii) investigating and considering the customer's existing financial products—including a 'like-for-like' comparison of the fees and features of existing and new products;
- (b) provided advice that was appropriate for the customer; and
- (c) prioritised the customer's interests over those of the adviser or related parties.

273 We also observed that auditors commonly assessed advisers as demonstrating compliance with the best interests duty and related obligations, despite the customer file containing incomplete documentation.

274 The failure of auditors to identify non-compliant advice may be a competence issue which extends beyond the inadequacy (in some cases) of the file audit questionnaire. However, this seems unlikely to be the only reason. This is because we found that:

- (a) when non-compliant advice was identified by ASIC in business-as-usual audits, the licensee's auditor failed, in 37% of cases, to identify any of the non-compliance that we observed. This improved in the ASIC-directed audits, with the auditor failing to identify any of the compliance issues that we observed in 23% of cases; and
- (b) when non-compliant advice was identified by ASIC in business-as-usual audits, and assessed as requiring a remediation response, the licensee's auditor recommended consequence management or customer remediation in 58% of cases. This increased to 67% of cases in the ASIC-directed audits.

Note: See paragraph 247 for more information about the ASIC-directed audits.



275 Other causes that may explain the failure of auditors to identify non-compliant advice include the level of resourcing available to conduct the adviser audits, and the adequacy of auditor training.

*Amending customer files during the audit process*

276 We found that, where deficiencies in the file documentation were identified within the adviser audit process, the auditor would sometimes recommend that the adviser amend the customer file to make it compliant. In our view, this practice is undesirable because it is inconsistent with the obligation for the adviser to maintain records to demonstrate that they have complied with the best interests duty and related obligations.

277 File notes should be made at the same time as the events that they record. In some cases, we observed a time delay of up to 12 months between the advice being provided to the customer and the recommendation from the auditor to update the file. Often, amendments to the customer file were made without any customer engagement.

278 Where record-keeping deficiencies are identified—and, in particular, where these relate to instructions provided by, or information given to, the customer—any amendments to the customer file should occur in consultation with the customer. Table 9 sets out some of the file amendment recommendations that we observed.

Note: In appropriate cases, we will take action when customer records have been altered: see [Media Release \(16-239MR\) ASIC bans North Queensland financial adviser](#) (26 July 2016).

**Table 9: Observed recommendations made to amend customer files during the audit process**

	Customer File A	Customer File B
<b>Observed audit findings</b>	The SOA referred to the customer’s existing superannuation fund but there was no demonstration of a like-for-like comparison with the recommended superannuation product, including the difference in premium payable and any benefits lost or gained.	The adviser failed to properly record meetings with the customer, including establishing the customer’s individual circumstances and goals, and how advice would assist the customer.
<b>Remedial action recommended by auditor</b>	<p>The auditor recommended that:</p> <ul style="list-style-type: none"> <li>the adviser should research the maximum benefit and premium of the former product through the superannuation fund website and PDS;</li> <li>the research should identify the limit of suitable cover within the former product;</li> <li>the file should be updated to show the new like-for-like research; and</li> <li>copies of relevant documents and file notes of discussions should be retained.</li> </ul>	<p>The auditor recommended that the adviser should prepare file notes, using the current date, to record the adviser’s recollection of:</p> <ul style="list-style-type: none"> <li>discussions with the customer, including the customer’s circumstances, goals and reasons for seeking personal insurance advice; and</li> <li>explanations about why specific features, benefits and sum amounts were agreed on.</li> </ul>

	Customer File A	Customer File B
<b>Course of action ASIC would expect</b>	<p>We expect that this non-compliance would be recorded on the audit record and affect the audit rating.</p> <p>To remediate the situation, we agree that research should be undertaken.</p> <p>After the necessary research has been completed, we expect that (when appropriate):</p> <ul style="list-style-type: none"> <li>• corrective disclosure should be made to the customer;</li> <li>• a determination should be made about whether the existing advice has complied with the best interests duty and related obligations, and if not, the affected customer should receive further remediation;</li> <li>• the licensee should monitor that the adviser has undertaken these steps appropriately;</li> <li>• a determination should be made about what, if any, adviser consequence management is required; and</li> <li>• the licensee should ensure that any systemic issues identified by the auditor, if relevant, are captured as part of the audit process.</li> </ul>	<p>We expect that this non-compliance would be recorded on the audit record and affect the audit rating.</p> <p>To remediate the situation, we agree that appropriate records should be created using the current date.</p> <p>When creating such a record, we expect that:</p> <ul style="list-style-type: none"> <li>• the customer should be consulted to verify the accuracy of the adviser's recollection;</li> <li>• where there is disagreement about what was discussed, the customer's recollection of events should be favoured;</li> <li>• if the customer provides alternative facts, a determination should be made about whether the existing advice complies with the best interests duty and related obligations, and whether an affected customer should be remediated;</li> <li>• the licensee should monitor that the adviser has undertaken these steps appropriately;</li> <li>• a determination should be made about what, if any, adviser consequence management is required; and</li> <li>• the licensee should ensure that any systemic issues identified by the auditor, if relevant, are captured as part of the audit process.</li> </ul>

Source: Institutions, ASIC

### *Inadequacy of audit record keeping*

- 279 As part of our review, we asked the institutions whether they retained a full copy of the customer file at the time it was audited (point-in-time copy).
- 280 We consider retaining a point-in-time copy of the customer file to be an important part of an advice licensee's audit process because the file forms the source documentation for any subsequent audit of the licensee's control testing environment. If a point-in-time copy of the customer file is not retained, we consider that the licensee's ability to test the effectiveness of the adviser audit process itself is likely to be impeded.
- 281 We found that eight of the 10 Phase 3 licensees did not have a practice of retaining a point-in-time copy of the customer file that was subject to an audit. One explanation offered was that retaining point-in-time copies of customer files would be too costly and time consuming.

Note: The ability to test the adequacy of risk management processes, including the adviser audit, forms part of the 'three lines of defence' risk management model which all of the institutions told us they used. The 'three lines of defence' model is discussed in [Report 298](#) *Adequacy of risk management systems of responsible entities* (REP 298).

### Recommendations to address non-compliance

- 282 We observed that, in some instances, where non-compliant advice was identified by the auditor, the Phase 3 licensees have undertaken:
- (a) *adviser consequence management*—for example:
    - (i) requiring the adviser to undertake additional training and improve their record-keeping practices;
    - (ii) returning the adviser to pre-vet status; and/or
    - (iii) placing the adviser under closer scrutiny within the licensee’s monitoring and supervision systems by requiring more frequent adviser audits in the future; and
  - (b) *customer remediation*, where appropriate—for example, requiring corrective disclosure, offering the customer access to a free advice appointment, rectifying errors that occurred when the advice was implemented, and/or paying monetary compensation.

283 The recommendations made for adviser consequence management or customer remediation were often inadequate to address the compliance issues that we identified. Of the 131 audit outcomes that we assessed as being ineffective or partially effective, we found that there were 48 cases where corrective action should have been recommended by the licensee’s auditor but none had been recommended. We have set out in paragraph 293 what we will do to address these issues with the licensees.

284 We also observed that, for a significant number of the sample files where we assessed the advice as non-compliant, the licensee’s auditor made no recommendations for consequence management of the adviser or customer remediation. This occurred in two ways:

- (a) the licensee’s auditor did not identify non-compliance and therefore no recommendations were made for adviser consequence management or customer remediation; or
- (b) the licensee’s auditor identified non-compliance but made no recommendation for adviser consequence management or customer remediation.

## Further observations about KRIs and data analytics

### What we did

285 We used our compulsory notice powers to direct the institutions to provide information about the use of data analytics within their monitoring and supervision processes.

286 As part of Phase 2, we also received information from the institutions about the development of data analytics and the use of KRIs to identify high-risk advisers for the purposes of remediation.

## What we found

- 287 We believe that the use of data analytics to develop KRIs is a useful and efficient method to improve the identification of high-risk advisers and non-compliant advice.
- 288 We found that the main KRIs used by the institutions, as part of their monitoring and supervision processes, included:
- (a) the use of adviser audit ratings as a measure of the risk the advisers expose their licensee to—the ratings are then used to assess whether more frequent audits need to be undertaken;
  - (b) the occurrence of potentially systemic issues identified by the adviser audit process—so that institutions can review similar customer files to determine whether the non-compliance is widespread and customer remediation is necessary; and
  - (c) the frequency and monetary value of customer complaints.
- 289 We observed the increasing trend to use data analytics in the development of KRIs for identifying high-risk advisers, although it was apparent that some of the institutions had more advanced processes than others for using data analytics to monitor their advisers.
- 290 We asked the institutions to ensure that the development of data analytics to identify high-risk advisers within their remediation work would also form the basis of the continuing development of their KRIs for monitoring and supervision.
- 291 ASIC has worked with the institutions to establish a number of KRIs as part of their monitoring and supervision processes. In Appendix 4, we include a list of possible KRIs for advice licensees to consider when developing and implementing their KRIs to identify potentially high-risk advisers and non-compliant advice.
- 292 We expect that KRIs developed using data analytics will be subject to continuous review and improvement as new industry and product risks emerge.

## Next steps

- 293 We will meet with each of the institutions to discuss the findings of our customer file reviews, and our concerns about the institutions' adviser audit processes. We will consider enforcement or other appropriate regulatory action against the Phase 3 licensees, and will make a public statement where we take enforcement action.

## Appendix 1: Advice licensees within the scope of this project

294 Table 10 sets out a list of the advice licensees that were part of this project. These licensees were solely owned or controlled by the institutions for all or part of the period between 1 January 2009 and 30 June 2015.

Note 1: This list includes only licensees that provided personal advice during the relevant period for this project.

Note 2: The 10 licensees that we also selected as our Phase 3 licensees are identified in the table: see also paragraph 35.

**Table 10: Advice licensees we reviewed in this project**

Institution	Licensee
AMP	AMP Direct Pty Ltd
	AMP Financial Planning Pty Limited (also a Phase 3 licensee)
	Charter Financial Planning Limited
	Forsythes Financial Services Pty Ltd
	Genesys Wealth Advisers Limited
	Hillross Financial Services Limited
	IPAC Securities Limited (also a Phase 3 licensee)
	King Financial Services Pty Ltd
	PPS Lifestyle Solutions Pty Ltd
	Prosperitus Pty Ltd
	Quadrant Securities Pty Ltd
	SMSF Advice Pty Limited
	Strategic Planning Partners Pty Ltd
	TFS Financial Planning Pty Ltd
Total Super Solutions Pty Ltd	
Tynan Mackenzie Pty Ltd	
ANZ	Australia and New Zealand Banking Group Limited (also a Phase 3 licensee)
	Financial Services Partners Pty Limited
	Millennium 3 Financial Services Pty Ltd (also a Phase 3 licensee)
	RI Advice Group Pty Ltd

Institution	Licensee
CBA	Commonwealth Financial Planning Limited (also a Phase 3 licensee) Financial Wisdom Limited BW Financial Advice Limited Count Financial Limited (also a Phase 3 licensee) Commonwealth Private Limited Commonwealth Securities Limited
NAB	GWM Adviser Services Limited (also a Phase 3 licensee) Apogee Financial Planning Limited Godfrey Pembroke Limited Meritum Financial Group Pty Ltd JB Were Limited National Australia Bank Limited (also a Phase 3 licensee)
Westpac	Westpac Banking Corporation (also a Phase 3 licensee) Securitor Financial Group Ltd (also a Phase 3 licensee) Magnitude Group Pty Ltd

## Appendix 2: Checklist—Background checking of advisers

295 Table 11 sets out a checklist of issues for advice licensees to consider when conducting background checks on advisers.

**Table 11: Issues for advice licensees to consider when conducting background checks on advisers**

Issue	Considerations
Regulatory status and history	<p>Licensees should check whether the adviser is listed on:</p> <ul style="list-style-type: none"> <li>• ASIC’s financial advisers register;</li> <li>• ASIC’s banned and disqualified register, or enforceable undertakings register;</li> <li>• the professional registers on ASIC Connect; and</li> <li>• the Australian Prudential Regulation Authority’s (APRA) disqualification register.</li> </ul> <p>Note: Advisers who were banned or disqualified, or who entered into an enforceable undertaking, before 31 March 2015—and who have not re-entered the advice industry—will appear on our banned and disqualified register or enforceable undertakings register, but will not be listed on ASIC’s financial advisers register.</p>
Other background checks	<p>Licensees should carry out the following checks:</p> <ul style="list-style-type: none"> <li>• criminal history (in Australia or overseas if the adviser has been resident overseas);</li> <li>• bankruptcy;</li> <li>• directorship and significant shareholdings history (for companies in external administration);</li> <li>• 100 point identification; and</li> <li>• Anti-Money Laundering, Counter Terrorism Financing Rules and Global Official List (Sanctions).</li> </ul> <p>Note: See page 12 of <a href="#">Standards Australia’s Handbook HB 322-2007</a> (PDF 1 MB).</p>
Disclosure, verification and consent from the adviser	<p>The appointment application form should request:</p> <ul style="list-style-type: none"> <li>• a copy of the adviser’s curriculum vitae, showing their qualifications, professional memberships and work history;</li> <li>• information about the adviser’s compliance history;</li> </ul> <p>Note: See Appendix D of <a href="#">Standards Australia’s Handbook HB 322-2007</a> (PDF 1 MB).</p> <ul style="list-style-type: none"> <li>• information about complaints made against the adviser;</li> <li>• information about the adviser’s conflicts of interest;</li> <li>• information about any high-risk positions the adviser has held (including appointment by a customer as an attorney under power of attorney, an executor of estate, a trustee, a guarantor or an authorised signatory on a customer account);</li> <li>• information about any related businesses the adviser carries on (e.g. providing credit, accounting or real estate services);</li> <li>• a list of the adviser’s directorships and significant shareholdings (past and current);</li> <li>• a character questionnaire;</li> <li>• confirmation about whether the adviser has been known by any other name (e.g. alias or by marriage);</li> <li>• acknowledgments and declarations of the truth and accuracy of the information provided; and</li> <li>• the adviser’s consent for background checks to be conducted, and direction to the adviser’s recent former licensees requiring them to provide the necessary information to the recruiting licensee.</li> </ul> <p>Note: See Appendices B and C of <a href="#">Standards Australia’s Handbook HB 322-2007</a> (PDF 1 MB).</p>

Issue	Considerations
Compliance history	<p>Licensees should request:</p> <ul style="list-style-type: none"> <li>• the findings of the adviser's most recent audit reports; and</li> <li>• references from designated compliance managers—or an appropriately qualified and authorised person within the adviser's recent former licensees—who can provide objective, relevant and factual compliance information about the adviser.</li> </ul> <p style="text-align: right;">Note: See Part B and Appendix C of <a href="#">Standards Australia's Handbook HB 322-2007</a> (PDF 1 MB).</p>
Qualifications and training	<p>Licensees should verify whether the adviser:</p> <ul style="list-style-type: none"> <li>• has appropriate qualifications; and</li> </ul> <p style="text-align: right;">Note: The minimum level of training and competence required to provide personal advice is set out in <a href="#">Regulatory Guide 146 Training of financial product advisers</a> (RG 146) and, in some cases, more specialised training may be required by licensees. The <i>Corporations Amendment (Professional Standards of Financial Advisers) Act 2017</i> commenced on 15 March 2017. This seeks to raise the professional, ethical and education standards of financial advisers. There is a transitional period which means that most of the new provisions relating to professional standards have staggered commencement dates from 1 January 2019.</p> <ul style="list-style-type: none"> <li>• has undertaken appropriate continuing professional development.</li> </ul>
Online media	<p>Licensees should carry out a general internet search—for example, by reviewing the adviser's website(s) and any mention of them in published media, social media and on professional networking sites.</p>
Assessment of information	<p>The officer responsible for auditing should assess the adviser's recent audit reports.</p> <p>The officer responsible for training should assess the adviser's qualifications and training.</p> <p>An appropriate compliance officer should carry out an overall assessment of all the collated information, including responses and feedback from specialist teams and any outsourced checking or verification service providers.</p> <p>Issues or concerns should be escalated to appropriate designated decision makers (e.g. a compliance committee or compliance manager).</p>
Process management	<p>Senior management should commit to an effective process of conducting and responding to background checks.</p> <p>Licensees should:</p> <ul style="list-style-type: none"> <li>• have in place written policies and procedures on conducting and responding to background checks;</li> <li>• use an appointment form and checklist; and</li> <li>• retain an organised and accessible record of checks conducted, information and documents received, and assessments undertaken.</li> </ul> <p>The extent of process management will vary depending on the nature, size and complexity of the licensee.</p>



## Appendix 3: Checklist—Reviewing personal advice as part of an adviser audit

- 296 Table 12 sets out a checklist of issues that all advice licensees and compliance consultants should consider when reviewing personal advice as part of an adviser audit to determine whether the adviser has demonstrated compliance with the best interests duty and related obligations.
- 297 The checklist covers the existing obligations in the Corporations Act, as well as additional considerations for giving good quality advice. It is based on our guidance in [Regulatory Guide 175](#) *Licensing: Financial product advisers—Conduct and disclosure* (RG 175) and [Regulatory Guide 244](#) *Giving information, general advice and scaled advice* (RG 244).
- 298 This is not a complete checklist of issues to consider when reviewing personal advice. A licensee may want, or need, to include additional questions and considerations, or tailor these matters according to the nature of its particular advice business. A licensee will also need to assess, in its audit process, an adviser’s compliance with other legal obligations, in addition to the best interests duty and related obligations.

### Other resources

- 299 In addition to the checklist in Table 12, ASIC has extensive regulatory guides and information for advice licensees to refer to when reviewing customer files and advice:
- (a) [Information Sheet 182](#) *Super switching advice—Complying with your obligations* (INFO 182);
  - (b) [Information Sheet 205](#) *Advice on self-managed superannuation funds: Disclosure of risks* (INFO 205);
  - (c) [Information Sheet 206](#) *Advice on self-managed superannuation funds: Disclosure of costs* (INFO 206);
  - (d) [Regulatory Guide 90](#) *Example Statement of Advice: Scaled advice for a new client* (RG 90);
  - (e) [Regulatory Guide 175](#) *Licensing: Financial product advisers—Conduct and disclosure* (RG 175);
  - (f) [Regulatory Guide 244](#) *Giving information, general advice and scaled advice* (RG 244);
  - (g) [Report 337](#) *SMSFs: Improving the quality of advice given to investors* (REP 337)—in particular, Section C; and
  - (h) [Report 413](#) *Review of retail life insurance advice*—in particular, Section D and the appendix ‘Life insurance advice checklist’ (REP 413).

**Table 12: Issues to consider when reviewing personal advice as part of an adviser audit**

Key issue	Audit questions	Considerations
Acting in the best interests of the customer: s961B(1)	<p>Has the adviser acted in the best interests of the customer?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Advisers must act in the best interests of their customers. As a result, a reasonable adviser would believe that the customer is likely to be in a better position if they follow the advice, than at the time the advice is provided. See RG 175.224–RG 175.231, including Examples 1–6, for further information.</p> <p>Advice provided by an adviser who has complied with the best interests duty is likely to leave the customer in a better position if they follow the advice. ‘Better position’ depends on the circumstances and includes:</p> <ul style="list-style-type: none"> <li>• the position the customer would be in if they did not follow the advice;</li> <li>• the facts at the time the advice is provided;</li> <li>• the subject matter of the advice sought by the customer (both explicit and implicit)—that is, whether the scope of the advice is consistent with the customer’s relevant circumstances and the subject matter of the advice sought (and why/why not);</li> <li>• whether the advice balances the need for strategic advice and/or financial product advice;</li> <li>• where relevant, the product features that the customer particularly values—provided that the customer understands the cost of, and is prepared to pay for, those features; and</li> <li>• whether the benefits the customer receives as a result of the advice are more than trivial (and why/why not).</li> </ul> <p>If an advice model produces a ‘one-size-fits-all’ outcome (i.e. the processes do not allow each customer’s relevant circumstances to be taken into account, or result in advice that does not reflect the customer’s relevant circumstances), it will be difficult to demonstrate that the best interests duty is being complied with.</p> <p>When assessing whether the best interests duty has been complied with, advice reviewers should assess:</p> <ul style="list-style-type: none"> <li>• which aspects of the advice were in the customer’s best interests;</li> <li>• which aspects of the advice were not in the customer’s best interests;</li> <li>• whether a reasonable adviser assessing the advice, at the time it was given, would believe that the customer would be likely to be in a better position if the customer followed the advice;</li> <li>• whether the advice took into account and reflected the customer’s relevant circumstances;</li> <li>• whether the scope of advice was consistent with the customer’s relevant circumstances and the subject matter of the advice sought; and</li> <li>• whether the advice balanced the need for strategic advice and/or financial product advice.</li> </ul> <p>Deficient switching advice (see below) may lead to the customer file and advice failing s961B(1).</p>

Key issue	Audit questions	Considerations
<p>Identifying the customer's objectives: s961B(2)(a)</p> <p>Note: This is a safe harbour step.</p>	<p>Did the adviser identify the objectives of the customer that were disclosed to the adviser by the customer through instructions?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Personal advice should ensure that a customer's objectives are specific, measurable and prioritised: see RG 175.218(c). These objectives may include, but are not limited to:</p> <ul style="list-style-type: none"> <li>• cash flow management and budgeting;</li> <li>• debt reduction or repayment;</li> <li>• building savings and wealth;</li> <li>• superannuation advice;</li> <li>• planning for retirement;</li> <li>• personal insurance advice; and</li> <li>• investment of a lump sum.</li> </ul> <p>The reasons or objectives that prompted the customer to seek advice should be clear and recorded in the customer's own words. Both the customer file and Statement of Advice (SOA) should clearly explain why the customer is seeking advice and the outcomes the customer wants to achieve.</p> <p>If a customer file and SOA are based on pre-determined or leading instructions, and questions from a 'fact find', this does not allow each customer's relevant circumstances to be taken into account and is likely to result in advice that does not reflect the customer's relevant circumstances.</p>
<p>Identifying the customer's financial situation and needs: s961B(2)(a)</p> <p>Note: This is a safe harbour step.</p>	<p>Did the adviser identify the financial situation and needs of the customer that were disclosed to the adviser by the customer through instructions?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>The adviser should identify, discuss and document all relevant aspects of the customer's financial situation and needs, such as:</p> <ul style="list-style-type: none"> <li>• their financial position (i.e. income, expenses, assets and liabilities);</li> <li>• their personal circumstances (i.e. age, relationship status and family situation);</li> <li>• their health status;</li> <li>• any foreseen changes to their personal or financial position (i.e. inheritance, home renovations, divorce, new baby, sale of business, retirement, redundancy, job or career changes);</li> <li>• any existing insurance arrangements (including insurance held within their superannuation fund); and</li> <li>• their insurance needs and the relative priority of those needs.</li> </ul> <p>The customer's financial situation and needs should be recorded in the customer file (e.g. in a fact find or file note summarising the conversation) and summarised concisely in the SOA to the extent that this information provides the basis of the advice given. Some of this information will merely provide context and background to the advice and does not need to be in the SOA.</p>

Key issue	Audit questions	Considerations
<p>Identifying the subject matter and scope of the advice sought by the customer: s961B(2)(b)(i)</p> <p>Note: This is a safe harbour step.</p>	<p>Did the adviser identify the subject matter of the advice sought by the customer and, where relevant, change the scope of the advice accordingly?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>A customer file and SOA should together demonstrate:</p> <ul style="list-style-type: none"> <li>• why the customer is seeking advice;</li> <li>• the subject matter and scope of the advice being provided; and</li> <li>• why the subject matter and scope are suitable for the customer and consistent with the customer's objectives, financial situation and needs.</li> </ul> <p>A customer file should also demonstrate that the subject matter of the advice sought was identified through a two-way process between the customer and the adviser.</p> <p>The scope of advice must not be reduced by the adviser to exclude critical issues that are relevant to the subject matter of the advice sought.</p> <p>Where the customer seeks to limit the scope of the advice, the adviser should decline to provide the advice if their ability to act in the customer's best interests is affected by the customer's instructions.</p> <p>Where the subject matter of the advice is limited in scope at the request of the customer, the adviser should carefully record this in the customer file, including the customer's reasons for the request. This should also be detailed in the SOA.</p>
<p>Identifying the customer's relevant circumstances: s961B(2)(b)(ii)</p> <p>Note: This is a safe harbour step.</p>	<p>Depending on why the customer is seeking advice, the adviser should exercise their judgement in identifying the customer's relevant circumstances, based on the information disclosed. Has this occurred?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>As part of identifying the customer's circumstances that are reasonably considered relevant to the subject matter of the advice sought, an adviser may need to make inquiries that are additional to those they would normally make. This is particularly important if the advice is relatively complex or if it is reasonably apparent that the customer has a low level of financial literacy.</p> <p>If the subject matter of the advice is revised as part of this process, this should be clear in the customer file and in the SOA, including why the revised subject matter is suitable and in the customer's best interests.</p> <p>The customer's relevant circumstances would normally encompass any matter that the customer indicates is important.</p>

Key issue	Audit questions	Considerations
<p>Making inquiries where information is incomplete or inaccurate: s961B(2)(c)</p> <p>Note: This is a safe harbour step.</p>	<p>If it was reasonably apparent that information about the customer's relevant circumstances was incomplete or inaccurate, did the adviser make reasonable inquiries to obtain complete and accurate information?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Where there is incomplete or inaccurate information (including inconsistent information) about the customer's relevant circumstances, the adviser should clearly demonstrate what steps they took to obtain or clarify information.</p> <p>Advisers should use their knowledge, skill and judgement to identify incomplete or inaccurate information that is required to provide the advice sought by the customer on that subject matter.</p> <p>In some cases, where the information is incomplete or inaccurate, the adviser should consider whether they should decline to provide advice.</p>
<p>Assessing the adviser's expertise: s961B(2)(d)</p> <p>Note: This is a safe harbour step.</p>	<p>Does the adviser have the expertise required to provide the advice sought by the customer on that subject matter?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Advice reviewers should make an objective assessment about the competence and experience of the adviser. This includes consideration of the adviser's authorisations, education, experience and memberships as recorded on ASIC's financial advisers register.</p> <p>If the adviser is not trained or authorised to provide the advice sought by the customer on that subject matter, they should decline to provide the advice.</p>

Key issue	Audit questions	Considerations
<p>Recommending a financial product: s961B(2)(e)</p> <p>Note: This is a safe harbour step.</p>	<p>Where a financial product is recommended, did the adviser conduct a reasonable investigation and assessment of the financial products that might meet the objectives and needs of the customer that would reasonably be considered as relevant to the advice on that subject matter?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Before recommending that a customer acquire a financial product, we expect advisers to formulate the strategy that they are basing their advice on. In some cases, it is unlikely that a product recommendation would be in the customer's best interests, given the subject matter of the advice sought. For example:</p> <ul style="list-style-type: none"> <li>• a customer experiencing financial difficulty may need advice on how to manage their cash flow and reduce debt. If the customer is unwilling or unable to pay for this advice, consideration should be given to referring the customer to a financial counsellor; or</li> <li>• a customer whose existing superannuation and insurance products meet their needs and objectives may need advice to make no changes and continue what they are already doing.</li> </ul> <p>An adviser should consider the customer's existing financial products and whether the customer's needs and objectives can be met by retaining (or modifying) their existing financial products.</p> <p>An adviser must conduct a reasonable investigation into products that will meet the customer's needs and objectives. The level of inquiries will vary according to the complexity of the advice, including the financial products and strategies recommended. Complex financial products and strategies necessitate more extensive inquiries.</p> <p>Advisers can refer to investigations conducted by their AFS licensee or various service providers (e.g. research houses) to assist their own inquiries. However, product research does not take into account the customer's unique personal circumstances, objectives, and needs. The adviser is ultimately responsible for ensuring that the product is suitable for the customer, given their relevant circumstances.</p> <p>Note: Not all research is the same. For further information, see <a href="#">Regulatory Guide 79</a> <i>Research report providers: Improving the quality of investment research</i> (RG 79).</p> <p>In summary, a customer file should demonstrate:</p> <ul style="list-style-type: none"> <li>• whether it was reasonable to recommend a financial product, taking into account the reasons why the customer sought advice;</li> <li>• consideration of strategic advice that may form the basis of the financial product recommendations;</li> <li>• consideration and investigation of financial products, taking into account: <ul style="list-style-type: none"> <li>– the customer's existing financial products;</li> <li>– financial products that might meet the customer's needs and objectives (including the recommended financial products);</li> <li>– a clear rationale about why the recommended financial products meet the customer's needs and objectives when compared with other products considered (including the customer's existing products); and</li> <li>– any research used by the adviser.</li> </ul> </li> </ul>

Key issue	Audit questions	Considerations
<p>Making a recommendation to replace a financial product: s961B(2)(e)</p> <p>Note: This is a safe harbour step.</p>	<p>Where an adviser recommends that a financial product is replaced, did the adviser conduct a reasonable investigation and assessment of the financial products that might meet the objectives and needs of the customer that would reasonably be considered relevant to the advice on that subject matter?</p> <p>Why/Why not?</p> <p>Did the adviser consider and investigate the customer's existing products?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Advice that recommends replacing one financial product with another (switching advice) must be in the customer's best interests. Advisers should carefully consider important risks to the customer.</p> <p>This is particularly important where an adviser recommends a switch of superannuation and/or insurance products, because this can have significant risks of lost benefits for a customer. In addition, a superannuation fund often contains insurance cover that should always be considered and investigated when providing switching advice.</p> <p>Once an adviser has established it is reasonable to recommend a financial product, before recommending a replacement product, the adviser must consider and investigate:</p> <ul style="list-style-type: none"> <li>• the customer's existing products;</li> <li>• the new financial products that the customer could potentially acquire or invest in; and</li> <li>• the new recommended products.</li> </ul> <p>Switching advice should:</p> <ul style="list-style-type: none"> <li>• be clear, concise and effective;</li> <li>• be easily understandable and enable the customer to make an informed decision; and</li> <li>• compare 'like-for-like' fees and features of existing and new products.</li> </ul> <p>When giving switching advice, an adviser must consider the advantages and disadvantages, including the costs and risks, of both the existing and new products. This obligation also applies if an adviser recommends that the customer redirects their superannuation contributions into a new superannuation fund, including an SMSF, or other product.</p> <p>Advice may leave the customer in a better position if there are overall cost savings for the customer that override the loss of any benefits. The overall cost savings must take into account all the circumstances, including the cost of the replacement product and the adviser's fees.</p> <p>Switching advice will generally not be in the customer's best interest if the adviser knows (or should have known) that:</p> <ul style="list-style-type: none"> <li>• the overall benefits likely to result from the replacement product would be lower than under the existing product, unless outweighed by overall cost savings; or</li> <li>• the cost of the replacement product is higher than the existing product, unless the replacement product better satisfies the customer's needs.</li> </ul> <p>Deficient switching advice may lead to the adviser failing the obligation to act in the customer's best interests (s961B(1)), satisfy the safe harbour step in s961B(2)(e), or provide appropriate advice (s961G).</p>

Key issue	Audit questions	Considerations
<p>All judgements are based on the customer's relevant circumstances: s961B(2)(f)</p> <p>Note: This is a safe harbour step.</p>	<p>Has the adviser based all judgements made, in advising the customer, on the customer's relevant circumstances?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>An adviser must base all judgements made, in advising the customer, on the customer's relevant circumstances. This includes:</p> <ul style="list-style-type: none"> <li>• whether the scope of advice is suitable;</li> <li>• the extent of inquiries made into the customer's relevant circumstances (i.e. whether the adviser has identified and inquired about all of the customer's relevant circumstances);</li> <li>• the strategies and financial products investigated and assessed, including existing products;</li> <li>• the strategies and financial products recommended, including why the recommended strategies and products meet the customer's relevant circumstances, and are suitable and in the customer's best interests;</li> <li>• where relevant, how the customer should acquire financial products—for example: <ul style="list-style-type: none"> <li>– whether personal insurance should be held through the customer's superannuation benefits (and why/why not); and</li> <li>– whether the customer's superannuation should be in an SMSF, industry fund or retail investor directed portfolio service (IDPS) platform (and why/why not); and</li> </ul> </li> <li>• whether complying with the best interests duty means that the advice required is not product specific.</li> </ul> <p>We consider that, to satisfy s961B(2)(f), a reasonable adviser would believe the customer is likely to be in a better position if the customer follows the advice.</p> <p>In some cases, complying with the best interests duty will require an adviser to give the customer advice that is not product specific and does not result in replacing a financial product or acquiring a new financial product (e.g. a customer seeking to understand when they are able to retire).</p>
<p>Other reasonable steps: s961B(2)(g)</p> <p>Note: This is a safe harbour step.</p>	<p>Has the adviser taken any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interests of the customer, given the customer's relevant circumstances?</p> <p>Why/Why not?</p> <p>Did the file pass or fail this step?</p>	<p>Advisers <i>may</i> need to undertake further steps, if they have not already done so—for example:</p> <ul style="list-style-type: none"> <li>• explain clearly to the customer the advice that is, and is not, being provided (see Section E of <a href="#">RG 244</a>);</li> <li>• when recommending financial products, provide strategic recommendations that benefit the customer; and</li> <li>• offer to provide advice (or refer the customer to someone who can provide advice) on any other key issues identified by the adviser.</li> </ul> <p>Advisers must use their judgement in considering whether there are any other steps that need to be taken to ensure they comply with the best interests duty.</p> <p><i>Example:</i> A customer seeks advice on obtaining life insurance only to cover new debt. In the course of providing this advice, the adviser determines that the customer is the single income earner for the customer's family and has no income protection cover. In this case, the adviser should bring this issue to the attention of the customer and offer to provide advice on this issue to the customer.</p>



Key issue	Audit questions	Considerations
Providing appropriate personal advice: s961G	<p>Would it be reasonable to conclude that the advice is appropriate to the customer?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>A customer file and SOA should together demonstrate that the customer is likely to be in a better position if they follow the advice.</p> <p>When assessing whether the duty to provide appropriate advice has been complied with, advice reviewers should consider the following:</p> <ul style="list-style-type: none"> <li>• What were the customer's objectives?</li> <li>• Was each objective satisfied by the advice? Why/why not?</li> <li>• Which aspects of the advice were appropriate?</li> <li>• Which aspects of the advice were not appropriate?</li> <li>• Was the customer likely to be in a better position if they followed the advice (see RG 175.224–RG 175.231)?</li> </ul> <p>Deficient switching advice may lead to the adviser failing s961G.</p>
Resulting advice based on incomplete or inaccurate information: s961H	<p>Was the information about the customer's relevant circumstances, on which the advice was based, incomplete or inaccurate?</p> <p>If yes, was the customer given a warning that the advice was based on incomplete or inaccurate information?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Advisers must make reasonable inquiries to obtain complete and accurate information about the customer's relevant circumstances. Personal advice may be provided if an adviser makes reasonable inquiries into the customer's relevant circumstances, even if the customer has not, in fact, provided all the information that the adviser has sought.</p> <p>If it is reasonably apparent, after reasonable inquiries have been made, that information about the customer's relevant circumstances, on which the advice is based, is incomplete or inaccurate, an adviser must warn the customer that:</p> <ul style="list-style-type: none"> <li>• the advice is, or may be, based on incomplete or inaccurate information relating to the customer's relevant circumstances; and</li> <li>• because of this, the customer should consider the appropriateness of the advice, taking into account their relevant circumstances, before acting on the advice.</li> </ul>
Prioritising the customer's interests: s961J	<p>Where there is a known, or reasonably apparent, conflict between the interests of the adviser and the customer, did the adviser prioritise the interests of the customer when giving the advice?</p> <p>Why/Why not?</p> <p>Did the customer file pass or fail this step?</p>	<p>Does the advice, product and/or service create additional revenue or some other form of benefit for the adviser, their advice licensee or another related party?</p> <ul style="list-style-type: none"> <li>• If yes, can additional benefits for the customer be demonstrated?</li> <li>• If yes, what are these additional benefits and how do they prioritise the interests of the customer?</li> <li>• Would a reasonable adviser without a conflict of interest have provided this advice? Why/why not?</li> </ul> <p>This information should be clear in the customer file. Any potential or actual conflicts of interest should be clearly set out in the SOA.</p> <p>Where appropriate, advisers should recommend solutions relevant to the customer's situation that are not product specific (e.g. advice on debt reduction, estate planning, and Centrelink benefits).</p>

Source: ASIC

## Appendix 4: Checklist—Key risk indicators for monitoring and supervising advisers

- 300 Table 13 sets out some key risk indicators (KRIs) that we have observed from this project. Advice licensees can consider using these, as appropriate, for monitoring and supervising advisers in their retail advice businesses. Each licensee should tailor the application of this checklist to the unique nature, scale and complexity of its business. We expect that using these KRIs will help licensees to identify potentially high-risk advisers and non-compliant advice.
- 301 Before adopting these KRIs, advice licensees should consider:
- (a) *identifying the available data*—for example, data may be available from the software and systems used for compliance, revenue and remuneration, financial products, and financial planning;
  - (b) *determining which data sources will provide reliable data*—when appropriate, this will involve testing. Characteristics of reliable data include consistency and scalability;
  - (c) *choosing appropriate KRIs* for the nature, scale and complexity of the licensee’s particular advice business;
  - (d) *ensuring appropriate testing is undertaken* when setting thresholds for the KRIs, to minimise the incidence of ‘false positive results’, while still ensuring the KRI is effective. Consideration should be given to:
    - (i) the nature, scale and complexity of the advice business;
    - (ii) engagement with senior staff and subject matter experts to set and approve risk thresholds; and
    - (iii) research into industry tolerances and risk thresholds; and
  - (e) *monitoring and testing KRIs* and relevant thresholds on a regular basis to ensure they remain effective and achieve their stated purpose.

**Table 13: KRIs for advice licensees to consider when monitoring and supervising advisers**

Indicator category	Key risk indicators
Product or advice type	<p>High ratio of records of advice to Statements of Advice provided to customers</p> <p>High level of ‘execution only’ services or evident lack of advice documents</p> <p>Variations, spikes and changes in remuneration or revenue of advisers. This may be assessed on a product basis or on an adviser basis</p> <p>High level of insurance commission clawbacks and lapse rates</p> <p>High level of product replacement</p> <p>High level of funds withdrawal from financial products or platforms</p> <p>High level of higher-risk or complex strategies and/or products (e.g. gearing, direct share advice, structured products and SMSFs)</p> <p>Recommendation of similar advice strategies to all customers (i.e. a ‘one-size-fits-all’ advice or business model)</p> <p>Trend of recommending insurance premium payments to be paid from superannuation when cash flow is raised as a concern by customers</p>

Indicator category	Key risk indicators
Adviser profile	<p>Adverse complaints history in terms of both the number and value of complaints</p> <p>Adverse adviser audit outcomes</p> <p>High level of recorded incidents, issues and events, and breaches</p> <p>Note: The institutions use a variety of terms, similar to and including those in the product or advice category above, to describe and record matters of adviser non-compliance. These matters may result in a breach report to ASIC.</p> <p>Poor training history (e.g. training not completed by due dates or failure rates)</p> <p>Identified personal or behavioural concerns (e.g. gambling habits, financial stress or acute health concerns)</p> <p>Identified conflicts of interest</p> <p>Customer signature irregularities</p> <p>Customer file integrity issues (e.g. unexplained additions, omissions or variations to a customer file)</p> <p>Advisers working in the same office as an identified high-risk adviser</p>
Customer profile	<p>High percentage of advice to elderly or vulnerable customers</p> <p>High percentage of customers in retirement who hold gearing products that may be unsuitable for their circumstances (e.g. customers approaching or in retirement, vulnerable customers, or customers with insufficient cash flow)</p> <p>High percentage of customers approaching retirement, or in retirement, who have an aggressive or assertive risk profile</p> <p>Adviser charging excessive fees relative to the amount being invested by the customer</p> <p>Adverse customer survey results</p>
Other	<p>Adverse results of an ASIC surveillance</p> <p>Adverse results revealed by searching the ASIC registers</p> <p>Any judgements against the adviser, or tribunal or banning decisions</p> <p>Negative or concerning feedback from the business, para-planners and compliance teams</p> <p>Whistleblowing reports</p> <p>Industry-wide risks</p>

## Appendix 5: Accessible versions of figures

302 This appendix is for people with visual or other impairments. It provides the underlying data for any figures included in this report.

**Table 14: Distribution of advice licensees as at 1 July 2015**

Category of advice licensee	Percentage of all advice licensees in industry	Number of advice licensees out of industry total of 3,443
Advice licensees within the institutions	1%	35
Other advice licensees	99%	3,408

Note: This is the data contained in Figure 1.

**Table 15: Distribution of advisers as at 1 July 2015**

Category of advisers	Percentage of all financial advisers in industry	Number of financial advisers out of industry total of 22,500
Advisers within the institutions	40%	8,888
Advisers in other advice licensees	60%	13,612

Note: This is the data contained in Figure 2.

**Table 16: Methods used by the institutions to identify SCC advisers**

Method used to identify SCC advisers	Number of SCC advisers identified
Adviser audit	58
Customer complaint	34
Business intelligence or whistleblower	26
Monitoring and supervision systems	17
Product issuer alerted licensee	6
ASIC investigation or review	6
Criminal case (non-financial services)	2

Note: This is the data contained in Figure 3.

**Table 17: Effectiveness of adviser audit process for sample files**

Outcomes of adviser audit	Number of files	Percentage of total files reviewed
Effective audit process	29	18%
Partially effective audit process	91	57%
Ineffective audit process	40	25%
Total files	160	100%

Note: This is the data contained in Figure 4.

**Table 18: Adviser audit outcomes for sample files**

Type of audit outcome	Breakdown of findings	Number of sample files
Effective audit	We identified compliance with s961B, 961G and 961J, and the licensee's auditor assessed the files as compliant	29
Partially effective audit	We identified non-compliance with s961B, 961G and 961J, and the licensee's auditor identified some non-compliance	14
Partially effective audit	We identified non-compliance with s961B, 961G and 961J, and the licensee's auditor had commentary on some compliance issues but had not identified non-compliance	49
Partially effective audit	We identified non-compliance with either one or a combination of two of s961B, 961G and 961J, and the licensee's auditor identified some non-compliance	5
Partially effective audit	We identified non-compliance with either one or a combination of two of s961B, 961G and 961J, and the licensee's auditor had commentary on some compliance issues but had not identified non-compliance	23
Ineffective audit	We identified non-compliance with s961B, 961G and 961J, and the licensee's auditor failed to identify any non-compliance	29
Ineffective audit	We identified non-compliance with either one or a combination of two of s961B, 961G and 961J, and the licensee's auditor failed to identify any non-compliance	11
Total files	Not applicable	160

Note: This is the data contained in Figure 5.

## Key terms

Term	Meaning in this document
ABA	Australian Bankers' Association
ABA protocol	<i>Reference checking and information sharing protocol</i> , issued by the Australian Bankers' Association
advice	Personal advice given to retail clients
advice licensee	An AFS licensee that provides personal advice to retail clients
adviser	A natural person providing personal advice to retail clients on behalf of an AFS licensee who is either: <ul style="list-style-type: none"> <li>• an authorised representative of an AFS licensee; or</li> <li>• an employee representative of an AFS licensee</li> </ul> <p>Note: This is the person to whom the obligations in Div 2 of Pt 7.7A of the Corporations Act apply: see key term definition of 'advice provider' in RG 175.</p>
AFS licence	An Australian financial services licence under s913B of the Corporations Act that authorises a person who carries on a financial services business to provide financial services <p>Note: This is a definition contained in s761A.</p>
AFS licensee	A person who holds an AFS licence under s913B of the Corporations Act <p>Note: This is a definition contained in s761A.</p>
AMP	AMP Limited
ANZ	Australia and New Zealand Banking Group Limited
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
authorised representative	A person authorised by an AFS licensee, in accordance with s916A or 916B of the Corporations Act, to provide a financial service or services on behalf of the licensee <p>Note: This is a definition contained in s761A.</p>
authorised representative model	Business model used by an advice licensee where the licensee's advisers are predominantly self-employed and appointed as authorised representatives of the licensee
best interests duty	The duty to act in the best interests of the client when giving personal advice to a client as set out in s961B(1) of the Corporations Act
best interests duty and related obligations	The obligations in Div 2 of Pt 7.7A of the Corporations Act

Term	Meaning in this document
business-as-usual audits	Regularly scheduled adviser audits conducted by the Phase 3 licensees as part of their broader audit processes for monitoring adviser compliance with financial services laws and the licensee's business rules  Note: See Table 8 for further details about this type of audit.
CBA	Commonwealth Bank of Australia
CFPL	Commonwealth Financial Planning Limited
Corporations Act	<i>Corporations Act 2001</i> , including regulations made for the purposes of that Act
CPL	Commonwealth Private Limited
customer (or client)	Retail client
customer's relevant circumstances	The objectives, financial situation and needs of a customer that would reasonably be considered relevant to the subject matter of advice sought by the customer
data analytics	The analysis of raw data to identify key trends using automated computer processes and statistics
employee representative	A person employed by an AFS licensee, or by a representative of the licensee, to provide a financial service or services on behalf of the licensee
employee representative model	Business model used by an advice licensee where the licensee's advisers are predominantly employees of the licensee
financial advice	Financial product advice
financial adviser	See 'adviser'
financial product	Generally a facility through which, or through the acquisition of which, a person does one or more of the following: <ul style="list-style-type: none"> <li>• makes a financial investment (see s763B);</li> <li>• manages financial risk (see s763C);</li> <li>• makes non-cash payments (see s763D)</li> </ul> Note: See Div 3 of Pt 7.1 of the Corporations Act for the exact definition.
financial product advice	A recommendation or a statement of opinion, or a report of either of these things, that: <ul style="list-style-type: none"> <li>• is intended to influence a person or persons in making a decision about a particular financial product or class of financial product, or an interest in a particular financial product or class of financial product; or</li> <li>• could reasonably be regarded as being intended to have such an influence.</li> </ul> This does not include anything in an exempt document  Note: This is a definition contained in s766B of the Corporations Act.

Term	Meaning in this document
financial service	Has the meaning given in s766A of the Corporations Act
FOFA	Future of Financial Advice
GST	Goods and services tax
high-risk adviser	An adviser who poses a higher risk of non-compliant conduct
institutions	Five of Australia's largest banking and financial services institutions, including AMP, ANZ, CBA, NAB and Westpac
key risk indicators (KRIs)	A set of factors that can indicate whether an adviser may be a high-risk adviser
Macquarie Group (or Macquarie)	Macquarie Group Limited
NAB	National Australia Bank Limited
non-compliant advice	<p>Personal advice provided to a retail client by an adviser who has not demonstrated compliance with the relevant provisions of Ch 7 of the Corporations Act, including the best interests duty and related obligations, in providing the advice</p> <p>Note: Further guidance on these provisions is set out in RG 175.</p>
non-compliant (financial) adviser	An adviser whose conduct has been identified as non-compliant
non-compliant conduct (or non-compliance)	<p>Conduct of an adviser that fails to comply with the obligations imposed by:</p> <ul style="list-style-type: none"> <li>• relevant Commonwealth, state or territory legislation;</li> <li>• the requirements of regulatory bodies; or</li> <li>• a licensee's internal business rules or standards.</li> </ul> <p>Non-compliant conduct may include providing non-compliant advice. In Phase 1, non-compliant conduct refers to serious compliance concerns or other compliance concerns</p>
OCC adviser	An adviser whose conduct has given rise to other compliance concerns
other compliance concerns	<p>Where an advice licensee has reason to believe, and has some credible information in support of the concerns identified, that an adviser—in the course of providing financial services (as defined in s766A of the Corporations Act)—may have been involved in misconduct (other than a serious compliance concern), including but not limited to:</p> <ul style="list-style-type: none"> <li>• a breach by act or omission of the licensee's internal business rules or standards, such as where an adviser has recommended non-approved products, entered into personal agreements or arrangements with customers, demonstrated poor record keeping, or acted outside the scope of their authorisation or competence;</li> <li>• an adverse finding from audits conducted by, or for, the licensee; or</li> <li>• conduct resulting in actual or potential financial loss to customers as a result of the advice received</li> </ul>



Term	Meaning in this document
personal advice	<p>Financial product advice that is given or directed to a person who is a retail client in circumstances where the provider of the advice has considered one or more of the person's objectives, financial situation and needs, or a reasonable person might expect the provider to have done so</p> <p>Note: See s766B(3) of the Corporations Act for the exact definition.</p>
Phase 3 licensees	The 10 advice licensees that were selected for Phase 3 of this project: see paragraph 125
retail client	A client as defined in s761G of the Corporations Act and Div 2 of Pt 7.1 of the Corporations Regulations 2001
RG 256 (for example)	An ASIC Regulatory Guide (in this example numbered 256)
s912A (for example)	A section of the Corporations Act (in this example numbered 912A)
sample advisers	The 40 advisers that we selected from the Phase 3 licensees
sample files	The 160 customer files that we selected from the files that had been reviewed by the Phase 3 licensees—either as part of their business-as-usual adviser audit, or as part of an ASIC-directed audit—for each of the sample advisers: see paragraph 137
SCC adviser	An adviser whose conduct has given rise to serious compliance concerns
serious compliance concerns	<p>Where an advice licensee believes, and has some credible information in support of the concerns identified, that an adviser—in the course of providing financial services (as defined in s766A of the Corporations Act)—may have engaged in the following:</p> <ul style="list-style-type: none"> <li>• dishonest, illegal, deceptive, and/or fraudulent misconduct;</li> <li>• any misconduct that, if proven, would be likely to result in the instant dismissal or immediate termination of the adviser;</li> <li>• deliberate non-compliance with financial services laws; or</li> <li>• gross incompetence or gross negligence.</li> </ul>
SMSF	Self-managed superannuation fund
SOA	Statement of Advice
switching advice	Advice that recommends that a customer replaces one financial product with another
Westpac	Westpac Banking Corporation

## Related information

### Headnotes

advice licensee, advice review checklist, adviser audit process, AFS licensee, background and reference checking, banking and financial services institutions, best interests duty, breach reporting, client compensation, customer files, customer review and remediation, data analytics, external expert assurance, financial advisers, key risk indicators, KRIs, monitoring and supervision processes, non-compliance, non-compliant advice, other compliance concerns, serious compliance concerns

### Instruments

[\[CO 14/923\]](#) *Record-keeping obligations for Australian financial services licensees when giving personal advice*

### Regulatory guides

[RG 78](#) *Breach reporting by AFS licensees*

[RG 79](#) *Research report providers: Improving the quality of investment research*

[RG 90](#) *Example Statement of Advice: Scaled advice for a new client*

[RG 104](#) *Licensing: Meeting the general obligations*

[RG 146](#) *Licensing: Training of financial product advisers*

[RG 175](#) *Licensing: Financial product advisers—conduct and disclosure*

[RG 244](#) *Giving information, general advice and scaled advice*

[RG 256](#) *Client review and remediation conducted by advice licensees*

### Information sheets

[INFO 151](#) *ASIC's approach to enforcement*

[INFO 182](#) *Super switching advice—Complying with your obligations*

[INFO 205](#) *Advice on self-managed superannuation funds: Disclosure of risks*

[INFO 206](#) *Advice on self-managed superannuation funds: Disclosure of costs*

## Legislation

Corporations Act, Div 2 of Pt 7.7A; s761A, 761G, 763B, 763C, 763D, 766A, 766B(3), 912A, 912D, 913B, 916A, 916B, 922C, 961B, 961G, 961H, 961J

Corporations Regulations, Div 2 of Pt 7.1

*Corporations Amendment (Professional Standards of Financial Advisers) Act 2017*

## Consultation papers and reports

[CP 247](#) *Client review and remediation programs and update to record-keeping requirements*

[REP 251](#) *Review of financial advice industry practice*

[REP 298](#) *Adequacy of risk management systems of responsible entities*

[REP 337](#) *SMSFs: Improving the quality of advice given to investors*

[REP 362](#) *Review of financial advice industry practice: Phase 2*

[REP 413](#) *Review of retail life insurance advice*

[REP 499](#) *Financial advice: Fees for no service*

## Media and other releases

[11-229MR](#) *ASIC accepts enforceable undertaking from Commonwealth Financial Planning*

[13-010MR](#) *ASIC accepts enforceable undertaking from Macquarie Equities Limited*

[14-201MR](#) *Macquarie Equities' financial advice remediation*

[15-022MR](#) *Macquarie Equities Limited enforceable undertaking and next steps*

[15-083MR](#) *Update on licence conditions on two Commonwealth Bank financial planning businesses: ASIC releases initial report into advice compensation program*

[15-306MR](#) *National Australia Bank to implement a large-scale financial advice remediation program*

[16-239MR](#) *ASIC bans North Queensland financial adviser*

[16-362MR](#) *ASIC clarifies record-keeping obligations for financial services licensees*

[16-415MR](#) *Update on licence conditions of two CBA financial advice businesses: ASIC releases compliance report from KordaMentha Forensic*

## **Other publications**

[ASIC's Corporate Plan 2016–17 to 2019–20](#)

[Australian Bankers' Association, Reference checking and information sharing protocol](#) (ABA protocol)

[Commonwealth Bank, Open Advice Review program](#)

[Financial Ombudsman Service, Terms of reference](#)

[Standards Australia's Handbook HB 322-2007, Reference checking in the financial services industry](#) (reference-checking handbook)