ASIC
Australian Securities & Investments Commission

REGULATORY GUIDE 181

Licensing: Managing conflicts of interest

Chapter 7 — Financial services and markets

Issued 30/8/2004

From 5 July 2007, this document may be referred to as Regulatory Guide 181 (RG 181) or Policy Statement 181 (PS 181). Paragraphs in this document may be referred to by their regulatory guide number (e.g. RG 181.1) or their policy statement number (e.g. PS 181.1).

What this guide is about

RG 181.1 This policy sets out:

A our general approach to compliance with the statutory obligation to manage conflicts of interest in s912A(1)(aa) (the conflicts management obligation)

see RG 181.8–RG 181.26

B guidance for licensees generally on controlling and avoiding conflicts of interest

see RG 181.27–RG 181.48

C guidance for licensees generally on disclosing conflicts of interest

see RG 181.49–RG 181.63

It also includes some issues for licensees to consider in complying with their obligations (see the Schedule).

Note: The conflicts management obligation was enacted by the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (CLERP 9 Act).

RG 181.2 The conflicts management obligation forms part of the licensing regime, which promotes the following primary outcomes:

(a) confident and informed decision making by consumers;

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

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

RG 181.3 This guide should be read in conjunction with guides we have previously issued on how we administer Chapter 7 of the *Corporations Act 2001* (the financial services regime), including:

(a) Regulatory Guide 36 *Licensing: Financial product advice and dealing* (RG 36);

(b) Regulatory Guide 164 *Licensing: Organisational capacities* (RG 164); and

(c) Regulatory Guide 175 *Licensing: Financial product advisers—Conduct and disclosure* (RG 175).

RG 181.4 The conflicts management obligation and this guide relate to conflicts of interest that arise within a licensee's financial services business. This policy also applies to conflicts of interest that arise between something within the financial services business and something outside it. The policy does not apply to conflicts of interest that occur wholly outside a licensee's financial services business. This policy applies to services provided to both retail and wholesale clients, and to the conduct of licensees as well as their representatives.

Note: See Explanatory Memorandum to Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 at para 5.599.

RG 181.5 This policy is not a summary of all legal obligations relating to conflicts of interest. Licensees should consider other legislative requirements (such as Chapters 2D, 2E and 5C of the Corporations Act), and regulations and common law that apply to conflict of interest situations—both within and wholly outside the licensee's financial services business.

RG 181.6 We will continue to monitor and review the provision of financial services generally to determine whether the objectives of

s912A(1)(aa) could be promoted through further ASIC policy or guidance.

When will our policy commence?

RG 181.7 This policy is based on the conflicts management obligation. It explains how we expect licensees to comply with the obligation when it commences on 1 January 2005.

Important note: The contents of this guide are based on the law as at 30 August 2004. Examples in this guide are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements. This guide does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act applies to you. It is your responsibility to determine your obligations under the Corporations Act and regulations.

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A Our general approach

Our regulatory approach

RG 181.8 We will take the guidance and expectations in this policy into account in administering the law, including considering whether to take action in relation to any particular licensee. In our view, licensees whose conflicts of interest management arrangements are not consistent with the guidance and expectations in this policy are less likely to be complying with their obligations (in particular, the conflicts management obligation (see RG 181.16)) and will be exposed to a greater risk of regulatory action.

Our general expectations

RG 181.9 A licensee is responsible for ensuring that it complies, on an ongoing basis, with its obligations as a licensee (and for taking reasonable steps to ensure that its representatives comply with the financial services laws). The primary responsibility for implementing adequate conflicts management arrangements and complying with other relevant obligations (including ensuring financial services provided by the licensee or its representatives are provided efficiently, honestly and fairly) rests with the licensee.

RG 181.10 What constitute adequate conflicts management arrangements will depend on the nature, scale and complexity of the licensee's business. In many cases, a licensee may be able to comply with the law's requirements in a number of different ways.

RG 181.11 We do not think that we can, or should, provide exhaustive guidance on what licensees need to do to comply with the law. Licensees must determine, on an ongoing basis, what arrangements (i.e. measures, processes and procedures) they need to have in place to ensure they maintain adequate conflicts management arrangements.

RG 181.12 We have issued this guide to help licensees and Australian financial services (AFS) licence applicants:

(a) assess the adequacy of the arrangements they currently have in place to manage conflicts of interest;

(b) if necessary, develop adequate arrangements to manage conflicts of interest; and

(c) understand what we look for when assessing whether a licensee or licence applicant has in place adequate conflicts management arrangements.

Underlying principles

RG 181.13 Adequate conflicts management arrangements help minimise the potential adverse impact of conflicts of interest on clients. Conflicts management arrangements thereby help promote consumer protection and maintain market integrity. Without adequate conflicts management arrangements, licensees whose interests conflict with those of the client are more likely to take advantage of that client in a way that may harm that client and may diminish confidence in the licensee or the market.

RG 181.14 Having adequate conflicts management arrangements should also help a licensee ensure that the quality of their financial services is not significantly compromised by conflicts of interest. The quality of a service is significantly compromised if the service is of materially lesser quality than the licensee would have been likely to provide if they were not subject to the relevant conflict of interest.

Conflicts of interest: a definition

RG 181.15 For the purposes of this policy, conflicts of interest are circumstances where some or all of the interests of people (clients) to whom a licensee (or its representative) provides financial services are inconsistent with, or diverge from, some or all of the interests of the licensee or its representatives. This includes actual, apparent and potential conflicts of interest.

Note: For example:

(a) Licensee A has an interest in encouraging client B to invest in higher risk products that result in high commissions, which is inconsistent with client B's personal desire to obtain a lower risk product.

(b) Licensee C has an interest in maximising trading volume by its clients (including client D) in order to increase its commission revenue, which is inconsistent with client D's personal objective of minimising investment costs.

(c) Licensee E is the trustee of a retail superannuation fund and has an interest in maximising the fees it earns from managing the fund (and therefore maximising the returns to its shareholders), but the beneficiaries have an interest in minimising the fees they pay as members of the fund.

The conflicts management obligation

RG 181.16 Licensees are obliged (among other things) to have adequate arrangements for the management of conflicts of interest that may arise wholly, or partially, in relation to the provision of financial services by the licensee, or a representative of the licensee, as part of the financial services business of the licensee or the representative (the 'conflicts management obligation'): s912A(1)(aa).

Note: The conflicts management obligation (s912A(1)(aa)) has effect from 1 January 2005.

Other licensee obligations

RG 181.17 Other licensee obligations also deal with or relate to conduct potentially affected by conflicts of interest, including:

(a) the obligation to do all things necessary to ensure that their financial services are provided efficiently, honestly and fairly (s912A(1)(a));

(b) the obligation to have adequate risk management systems (s912A(1)(h));

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

(d) the obligation to have adequate compliance arrangements (reg 7.6.03(g) and Pro Forma [PF 209]);

(e) the licensee's (and their authorised representatives') obligation to disclose benefits and relationships in a Financial Services Guide (FSG) before providing financial services to retail clients (s941A and 941B);

(f) the licensee's (and their authorised representatives') obligation to disclose benefits and relationships in a Statement of Advice (SOA) when providing personal financial product advice to retail clients (s946A);

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

(h) the duties of the responsible entity of a registered managed investment scheme, including duties to act in the best interests of the members of the scheme and, if there is a conflict between the

members' interests and its own interests, to give priority to the members' interests (s601FC).

Note: The Corporations Act risk-management-systems obligation does not apply to APRA-regulated bodies.

RG 181.18 The conflicts management obligation (see RG 181.16) and the obligation to operate efficiently, honesty and fairly are interconnected. A licensee is unlikely to comply with the efficiently, honestly and fairly obligation if they have inadequate conflicts management procedures. Conversely, having adequate conflicts management arrangements will help licensees comply with their other obligations, including the obligation to operate efficiently, honestly and fairly. It will also help licensees establish and maintain a reputation for integrity in the provision of financial services.

RG 181.19 Many licensees are also bound by common law obligations that affect their management of conflicts of interest. For example, many licensees have fiduciary obligations to their clients to whom they provide advice or for whom they act in a trustee capacity. These obligations operate in addition to the statutory requirements and should be taken into account when formulating conflicts management arrangements.

Three mechanisms for managing conflicts of interest

RG 181.20 The three mechanisms that licensees would generally use to manage conflicts of interest are:

(a) *controlling* conflicts of interest;

(b) *avoiding* conflicts of interest; and

(c) *disclosing* conflicts of interest.

For guidance on controlling and avoiding conflicts of interest, see Section B. For guidance on disclosing conflicts of interest, see Section C.

RG 181.21 The conflicts management obligation is more than simply a disclosure obligation: the obligation is to have adequate arrangements in place to *manage* conflicts of interest. We expect that licensees will generally use the three mechanisms of controlling, avoiding and disclosing conflicts. Disclosure alone will often not be enough to manage a conflict of interest.

Retail versus wholesale clients

RG 181.22 A licensee's obligation to manage conflicts of interest does not depend on whether its clients are retail or wholesale. Licensees must have adequate arrangements to identify and manage *all* conflicts of interest (other that those that occur wholly outside a licensee's financial services business), whether they relate to retail clients or wholesale clients. Licensees are also obliged to operate efficiently, honestly and fairly in relation to all clients.

RG 181.23 However, we recognise that what licensees need to do to comply with the law will depend on a range of matters, including the nature of the clients to whom financial services are provided.

Compliance with industry standards, practices and codes

RG 181.24 When administering the law we may take into account compliance with industry standards or practices: see Regulatory Guide 164 *Licensing: Organisational capacities* at RG 164.22–RG 164.24.

Compliance with foreign rules and standards

RG 181.25 In a number of countries, intermediaries are obliged to manage and disclose conflicts of interest. For example, the following jurisdictions have comparable conflicts of interest management obligations:

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

(b) Canada (common law duty, and s40 and s223(1) of the *Securities Act*);

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

(d) Hong Kong (common law duty, para 10.1 of the *Code of Conduct for Persons Registered with the Securities and Futures Commission*); and

(e) Singapore (common law duty, s27 of the *Financial Advisers Act*).

RG 181.26 We recognise that some licensees will also be subject to foreign rules or standards for managing conflicts of interest. Regardless of this, each licensee must ensure compliance with the Australian conflicts management obligation. However, by complying with comparable foreign rules or standards, we anticipate that some licensees will comply with most of our policy already.

B Controlling and avoiding conflicts of interest

RG 181.27 The conflicts management obligation does not prohibit all conflicts of interest. It does *not* provide that a licensee can *never* provide financial services if a conflict of interest exists. Rather, the conflicts management obligation requires that all conflicts of interest be adequately managed. Many conflicts of interest can be managed by a combination of:

(a) internal controls (see RG 181.28–RG 181.41); and

(b) disclosures (see RG 181.49–RG 181.63).

However, some conflicts cannot be managed in this way: where conflicts cannot be adequately managed through controls and disclosure, the licensee must *avoid* the conflict or refrain from providing the affected financial service: see RG 181.42–RG 181.43.

Controlling conflicts of interest

RG 181.28 To control conflicts of interest a licensee must:

(a) identify the conflicts of interest relating to their business;

(b) assess and evaluate those conflicts; and

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

RG 181.29 Depending on the circumstances and the nature of any given conflict, it may be appropriate to:

(a) disclose the conflict of interest to the relevant client(s);

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

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

(d) initiate internal or external disciplinary action (e.g. referring the matter to a professional body or regulator) where warranted.

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

Ensuring arrangements are adequate

RG 181.30 To be adequate, conflicts management arrangements must successfully identify conflicts of interest and *control* the effects

of those conflicts on the provision of financial services so that the quality of those financial services is not significantly compromised. Licensees should monitor whether their conflict management arrangements successfully do this.

Note: The conflicts management obligation 'will require internal policies and procedures for preventing and addressing potential conflicts of interest that are robust and effective': see the Explanatory Memorandum to Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 at para 5.597.

RG 181.31 Licensees should have monitoring procedures in place to ensure that any non-compliance with the licensee's conflicts management arrangements are identified and appropriately acted upon. Licensees should record action taken on breaches. Arrangements that are not monitored and enforced are unlikely to be adequate.

Note: For example, systemic instances of non-compliance with a licensee's conflicts management arrangements will tend to suggest that the arrangements themselves are inadequate.

RG 181.32 It is important that a licensee's conflicts management arrangements are designed with their own particular circumstances in mind. We encourage licensees to ensure that their conflicts management arrangements are designed or tailored according to the nature, scale and complexity of their business.

Note: Arrangements could include measures such as:

(a) meetings with affected staff or clients;

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

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

This is not an exhaustive list of all possible measures, processes or procedures. What constitutes appropriate arrangements will depend on the particular circumstances of the licensee.

RG 181.33 For conflicts management arrangements to be adequate, they need to be documented, with compliance-monitoring records also kept: see RG 181.44–RG 181.48 on documentation and record keeping.

Ensuring arrangements are implemented and maintained

RG 181.34 Merely having or possessing conflicts management arrangements is insufficient. To be adequate, the arrangements must be implemented and maintained. Generally this means that licensees

should ensure that the arrangements (i.e. measures, processes and procedures) they adopt to control conflicts of interest are:

(a) approved and endorsed by the senior management of the licensee;

(b) designed or tailored according to the nature, scale and complexity of the licensee's business;

(c) effectively implemented (and accompanied by effective compliance monitoring designed to ensure that the conflicts management arrangements are actually followed and appropriate action is taken where non-compliance is identified);

(d) regularly reviewed (internally or by a third party such as an auditor, as appropriate) and, where necessary, updated to ensure that the arrangements are adequate to identify, assess, and evaluate and successfully control conflicts of interest; and

(e) overseen by a specific person or persons who take responsibility for their implementation, reviewing and updating.

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

Internal structures

RG 181.35 Licensees should ensure that their internal structures and reporting lines enable them to effectively manage conflicts of interest. It is important that internal structures and reporting lines support a licensee's management of conflicts of interest. Licensees should consider how their organisational structure, physical layout and reporting processes affect their conflicts management.

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

(a) to have advisory staff reporting to marketing staff;

(b) for 'stand-alone' advice units within the organisation to be in the same physical location as sales or investment management staff; and

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

RG 181.36 Robust information barriers may help a licensee manage their conflicts of interest. They may allow a licensee to insulate one group of staff from the information or other circumstances that give rise to a particular conflict, so that the group is not affected by that conflict. To be effective, such barriers must

actually prevent information being passed to the relevant group of staff.

RG 181.37 A licensee's monitoring and supervision procedures need to take conflicts of interest management issues into account. The people who decide what is an appropriate action to take where a conflict of interest arises should not be significantly affected by the conflict themselves.

Remuneration

RG 181.38 Licensees need to consider their remuneration practices (including non-monetary benefits) as part of ensuring that they operate efficiently, honestly and fairly, and have in place adequate conflicts management arrangements.

Note 1: For example:

(a) if a product provider pays a higher rate of commission to a financial adviser for achieving certain volumes of sales, we would expect disclosure to be part of how the licensee manages that conflict;

(b) licensees should avoid remuneration structures where advisers are paid exclusively by commission (e.g. no salary or other remuneration is paid); and

(c) trustees taking fees based on funds under management should consider how to ensure they address any tendency to act other than in the best interests of their clients (beneficiaries).

Note 2: See also 'Preferential remuneration project', ASIC report, April 2004, and 'Disclosure of soft dollar benefits', ASIC report, June 2004.

RG 181.39 In some cases, disclosure to clients is an adequate mechanism for controlling conflicts of interest arising from remuneration practices. Part 7.7 of the Act generally approaches remuneration issues from a disclosure perspective (i.e. remuneration must be fully disclosed). However, licensees should consider whether any particular benefits, compensation or remuneration practices are inconsistent with the requirement to have adequate arrangements in place to manage conflicts of interest or with the requirement for the efficient, honest and fair provision of financial services. For example, those remuneration practices that place the interests of the licensee or its representatives in direct and significant conflict with those of the licensee's clients should be avoided (and not merely disclosed).

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

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

Treating clients fairly

RG 181.40 Licensees must ensure that they treat their clients fairly. In considering their obligations, we would generally expect licensees to consider the following questions:

(a) Are they providing financial services in a manner that unfairly puts the interests of the licensee (or its representatives) ahead of their clients?

(b) Are they providing financial services in a way that unfairly puts the interests of one client ahead of the interests of other clients?

(c) Are they using knowledge about their clients in a way that is likely to advance their own interests without sufficient disclosure to affected clients?

Note: Licensees legitimately expect a return for the services they provide (e.g. fees). Obtaining that return needs to be done in a manner that does not involve treating the client unfairly (e.g. fees must be disclosed in a transparent way). We acknowledge that in some situations the nature of the financial service being provided is such that the licensee will necessarily profit at the expense of the client they are dealing with (e.g. market making).

RG 181.41 Licensees need to manage conflicts between the interests of various clients (existing or potential clients) as well as conflicts between the licensee's own interests and those of their clients. Generally, they should not provide financial services in a manner calculated to advance one client's interests unfairly ahead of other clients' interests.

Note: For example, licensees should avoid situations where they unfairly favour one client or group of clients over another client or clients. This includes avoiding the scenario known as late trading where a client is permitted to trade in interests in a managed fund after the relevant trading period has closed (and in some cases after prices have been set).

Avoiding conflicts of interest

RG 181.42 Some conflicts of interest have such a serious potential impact on a licensee or its clients that the only way to adequately manage those conflicts will be to avoid them. In such cases merely disclosing them and imposing internal controls will be inadequate. A licensee's conflicts management arrangements must enable the licensee and its representatives to identify those conflicts of interest that must be avoided.

Note: For example:

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

(b) licensees should not disclose pending client orders to third parties associated with the licensee (which would enable those third parties to trade ahead of the client). The most obvious way of avoiding this conflict is to ensure that information about pending client orders is not communicated to third parties;

(c) licensees who are fund managers should not permit 'late trading' by some of their clients (e.g. allowing clients to buy and sell interests in their funds at a particular day's price based on information that comes to light only after general trading in that fund for that day has closed); and

(d) where an adviser is significantly affected by conflicts of interest for particular financial product advice, the adviser may need to decline to provide the advice.

RG 181.43 Licensees are responsible for their own conduct and that of their representatives. The conflicts management arrangements of a licensee need to take this into account. As far as possible, licensees (and their representatives) should avoid placing themselves in a position where there is a material conflict between their own interests and those of their clients. This is to minimise the risk that the licensee will be tempted to unfairly prefer their own interests to those of their clients.

Note: Many licensees are also bound by fiduciary obligations in their dealings with clients.

Documentation and record keeping

RG 181.44 For conflicts management arrangements to be adequate, they need to be documented. This generally involves having a written conflicts management policy (which may form part of the licensee's compliance procedures or manual).

RG 181.45 We expect that licensees will keep records showing what they have actually done to monitor compliance with their conflicts management arrangements. Conflicts management arrangements are unlikely to be adequate if they do not ensure that compliance-monitoring records are kept.

RG 181.46 We expect that licensees will keep, for at least seven years, records of:

(a) conflicts identified and action taken;

(b) any reports given to the licensee's owners or senior management about conflicts of interest matters; and

(c) copies of written conflicts of interest disclosures given to clients or the public as a whole.

Note 1: For example, a licensee should keep copies of written conflicts disclosures given to individual clients or otherwise made available (e.g. on a website). If similar disclosures are used repeatedly, we would expect a representative sample of conflicts disclosures to be kept. A licensee may already be required to keep records on conflicts disclosure in FSGs and SOAs under its licence conditions.

Note 2: Licensees should consider what records of oral disclosures should be kept to help them in monitoring their compliance with their conflicts management obligations. Licensees should consider how they will demonstrate their compliance with these obligations in the event of a review (by the licensee, its auditor or ASIC). For example, they may wish to keep copies of oral disclosure 'scripts' used by their representatives.

RG 181.47 Each licensee will need to consider how best to keep these documents and records (e.g. it may be appropriate to keep records in the form of a register). Documents and records may be kept electronically.

RG 181.48 The keeping of documents and records assists the licensee to demonstrate, to ASIC and itself, that it knows whether or not it is complying with the financial services laws: for more information, see RG 164.48.

C Disclosing conflicts of interest

RG 181.49 Licensees should make appropriate disclosures to clients as part of their arrangements to manage conflicts of interest. While disclosure alone will often not be enough, disclosure is an integral part of managing conflicts of interest. Licensees should ensure that clients are adequately informed about any conflicts of interest that may affect the provision of financial services to them.

RG 181.50 Adequate disclosure means providing enough detail in a clear, concise and effective form to allow clients to make an informed decision about how the conflict may affect the service being provided to them. We expect disclosure by licensees to focus on material conflicts.

RG 181.51 Disclosure helps clients to assess the service they are being offered in light of the licensee's own interests and to decide on the extent (if any) to which they will rely on the service. Having adequate arrangements in place to manage conflicts of interest 'will include ensuring that there is adequate disclosure of conflicts to investors, who can then consider their impact before making investment decisions': see the Explanatory Memorandum to Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003 at para 5.597.

Timely, prominent, specific and meaningful disclosure

RG 181.52 Disclosure about conflicts of interest should:

(a) be timely, prominent, specific and meaningful to the client;

(b) occur before or when the financial service is provided, but in any case at a time that allows the client a reasonable time to assess its effect; and

(c) refer to the specific service to which the conflict relates.

RG 181.53 In our view, the use of generic ('boilerplate') disclosures is unlikely to satisfy the conflicts management obligation. In order to be effective, conflicts of interest disclosure should refer to the specific service to which it relates, and should be specific and clear enough for the client to understand the conflict and its potential impact on the service they are being offered. Disclosures may generally be given in writing or orally.

Disclosures for financial product advice

RG 181.54 At or about the time of providing financial product advice, disclosures on the following matters will generally be appropriate:

(a) the extent (if any) to which the licensee (or any associated person) has a legal or beneficial interest in the financial products that are the subject of the financial product advice;

(b) the extent (if any) to which the licensee (or any associated person) is related to or associated with the issuer or provider of the financial products that are the subject of the financial product advice; and

(c) the extent (if any) to which the licensee (or any associated person) is likely to receive financial or other benefits depending on whether the advice is followed.

Licensees should provide the disclosure in the same form as the advice (e.g. written disclosures where the relevant advice is in writing).

Note: 'Associated person' is defined in the 'Key terms'.

RG 181.55 The content of disclosures concerning the provision of advice will vary depending on the circumstances. While the conflict of interest will not necessarily cause the advice to be significantly compromised, it should nonetheless be brought to the client's attention. The client can then decide whether the conflict of interest is significant and to what extent they will rely on the advice.

Note: For example:

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

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

RG 181.56 Similar disclosures are already required before financial product advice is given to retail clients (in an FSG) and when personal financial product advice is given to retail clients (in an SOA): see RG 175. In many cases the disclosures suggested in this policy will already have been provided in an SOA or FSG.

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

Disclosures for other financial services

RG 181.57 What conflicts of interest disclosures are needed for other financial services will depend on all of the facts and circumstances, including (among other things) whether the client is retail or wholesale. Although RG 181.54 may provide useful guidance, we believe that licensees are in the best position to determine how they disclose conflicts of interest for these services. These disclosures may generally be given in writing or orally.

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

Retail versus wholesale clients

RG 181.58 As set out in RG 181.22, the conflicts management obligation applies equally to services provided to retail and wholesale clients. What constitutes appropriate disclosure to a client (whether retail or wholesale) will depend on all of the facts and circumstances. We recognise that, in some cases, the disclosure a licensee needs to give to a wholesale client to comply with the law will be less detailed than is required for a retail client. The following factors should be considered in assessing the disclosure that should be provided to a client:

(a) the level of financial sophistication of the client;

(b) the extent to which third persons are likely to rely, directly or indirectly, on the service (e.g. where advice is given to a wholesale client in circumstances where it is likely to be passed on to retail clients);

(c) how much the client already actually knows about the specific conflict; and

(d) the complexity of the service.

Note: This is not an exhaustive list of all relevant matters. What is appropriate conflicts of interest disclosure will depend upon the circumstances.

RG 181.59 Licensees should remember that disclosing conflicts not only allows clients to make an informed choice. It also allows the licensee to recognise and record the existence and nature of conflicts within their business, and promotes honesty and fairness in their provision of financial services. A client's circumstances are only one of many factors that ought to be considered when disclosing conflicts.

Other disclosure issues

RG 181.60 We recognise there are some situations where disclosing a particular conflict will be inappropriate. There may be situations in which conflicts of interest arise that are confidential, and even amount to 'inside information' under the insider trading provisions: s1042A. In such situations licensees will need to assess whether any disclosures can be given and whether the conflict can be adequately managed through other mechanisms. It may be that the conflict needs to be avoided by, for example, declining to provide the affected service.

> Note: An example is a situation in which an adviser is prevented from making adequate conflict of interest disclosure because the information to be disclosed is commercially sensitive or is protected by confidentiality agreements. Such situations are difficult to manage adequately and it may be that the adviser will need to avoid providing the advice altogether.

RG 181.61 Licensees should clearly disclose enough detail to allow clients to make informed decisions about how the conflict may affect the service being provided to them. Excessive disclosure is likely to confuse clients and reduce the effectiveness of the disclosure. Detailed and exhaustive disclosure about conflicts of interest should not be used to obscure conflicts. Generally, we expect disclosure by licensees to focus on material conflicts.

RG 181.62 Robust information barriers may mean the relevant group of people providing a particular service (e.g. an adviser, their colleagues and supervisors) are unaware of some of the matters in RG 181.54: see RG 181.36. Where the relevant people do not have actual or constructive knowledge about a given matter owing to the operation of effective information barriers, the conflicts management obligation will not necessarily require them to make disclosures about the matter. Whether any particular matter does not need to be disclosed will depend on the facts and circumstances.

RG 181.63 Documentation and record keeping is dealt with in Section B: see RG 181.44–RG 181.48.

Schedule: Issues for licensees to consider

RG 181.64 We encourage licensees to consider this list of issues in managing conflicts of interest. It is not suggested that all the issues are relevant to every particular licensee, or that they are exhaustive. Licensees should determine which issues are relevant to their business. These are the types of issues that we will consider in assessing Australian financial services (AFS) licence applications and when carrying out surveillance. We will review this list in light of our experience in administering the Corporations Act.

Table 1 Issues to consider in complying with the conflicts management obligations

Mechanism	Issues to consider
Controlling and avoiding conflicts	• What are your procedures for identifying conflicts of interest? • What are your procedures for assessing and evaluating conflicts of interest? • How do your conflicts management arrangements enable you to decide how to respond to or deal with particular conflicts? • Do you have a written conflicts management policy? • When were your conflicts management arrangements last reviewed internally or by a third party (e.g. an auditor)? • When were your conflicts management arrangements last updated? • What structural arrangements do you have in place to manage conflicts of interest? • How does your organisation's structure support your management of conflicts of interest? • What information barriers do you have within your organisation? How do they help you manage conflicts of interest? • How do your conflicts management arrangements ensure that conflicts do not affect your compliance with your licensee obligations under s912A? How do you test their effectiveness in achieving this? • How do your conflicts management arrangements ensure that your clients are not treated unfairly? How do you test their effectiveness in achieving this? • How do your conflicts management arrangements ensure that any personal advice you give is appropriate? How do you test their effectiveness in achieving this? • How were your conflicts management arrangements formulated and approved? Were they approved by your owners, board or governing body (or a delegated body)? • How are your conflicts management arrangements communicated to staff and other stakeholders (e.g. clients, customers and the public)?

Mechanism	Issues to consider
Controlling and avoiding conflicts (cont.)	• Are nominated persons responsible for the implementation, reviewing and updating of your conflicts management arrangements? Who do they report to? • What procedures do you have to identify instances of non-compliance with your conflicts management arrangements? How is non-compliance dealt with? How is non-compliance recorded and reported to your governing body? • What impact do your remuneration and benefits practices have on your management of conflicts? • How do you ensure your remuneration and benefits practices do not result in the integrity and quality of the services you provide being significantly compromised? • How do your dealing or trading practices affect your management of conflicts? • How do you assess the impact of conflicts of interest on the quality of the services you provide? What processes do you have (if any) to ensure that the quality of your services is not significantly compromised by the presence of conflicts of interest? • What are your procedures for assessing the seriousness of a conflict of interest? • How do you ensure that more serious conflicts are referred to your owners or managers? • In what circumstances do you avoid conflicts of interest (as opposed to dealing with them through disclosure or internal controls)? How are these decisions made and recorded?
Disclosing conflicts	• What are your procedures for disclosing conflicts of interest to affected clients? • How do your conflicts management arrangements ensure that your clients receive adequate and specific disclosure about conflicts? • How do you ensure these procedures are followed consistently and at all times? • What disclosures do you give for general financial product advice? • What disclosures do you give for other financial services? • Do your disclosures vary between wholesale and retail clients? How? • How do you deal with conflicts of a confidential nature (i.e. those where disclosure may not always be an available remedy)? • How do you ensure that disclosures of conflicts are timely, prominent, specific and meaningful? • What disclosures do you give for personal financial product advice?

Key terms

RG 181.65 In this guide, unless a contrary intention appears, terms have the following meaning.

ASIC The Australian Securities and Investments Commission.

ASIC Act The *Australian Securities and Investments Commission Act* 2001.

associated person An associate (within the meaning of Div 2 of Pt 1.2 of the Corporations Act) of the relevant person.

CLERP 9 Act The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004*.

conflicts of interest See the definition in RG 181.15 in Section A.

conflicts management obligation Section 912A(1)(aa), as set out in Schedule 10 of the CLERP 9 Act.

Corporations Act The *Corporations Act 2001*, including regulations made for the purposes of that Act.

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

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

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

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

Note: This is a definition contained in s763A.

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

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

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

but does not include anything in an exempt document.

Note: This is a definition contained in s766B.

licensee or **financial services licensee** A person who holds an Australian financial services (AFS) licence.

Note: This is a definition contained in s761A.

personal advice Financial product advice that is given or directed to a person (including by electronic means) in circumstances where:

(a) the provider of the advice has considered one or more of the person's objectives, financial situation and needs; or

(b) a reasonable person might expect the provider to have considered one or more of those matters.

Note: This is a definition contained in s766B(3)

RG 136 (for example) A regulatory guide (in this example numbered 136).

representative A representative of a financial services licensee means:

(a) an authorised representative of the licensee;

(b) an employee or director of the licensee;

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

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

Note: This is a definition contained in s910A.

retail client Has the meaning set out in s761G.

s782 (for example) A section of the Corporations Act (in this example numbered 782).

Related information

RG 181.66

Headnotes

Conflict of interest, internal controls, information barriers, conflicts management, disclosure, avoiding, significantly compromised

Regulatory guides

RG 36 *Licensing: Financial product advice and dealing*

RG 164 *Licensing: Organisational capacities*

RG 175 *Licensing: Financial product advisers—Conduct and disclosure*

Legislation

Corporations Act 2001, s601FC, 760A, 912A(1)(aa), 912A(1), 912A(1)(a), 912A(1)(c), 912A(1)(ca), 941A, 941B, 946A.

Cases

Rahmat Ali v Hartley Poynton Ltd [2002] VSC 113

Consultation papers and reports

CP 46 *Licensing: Managing conflicts of interest*

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

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

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

REP 24 R*esearch analyst independence*

REP 29 *Preferential remuneration project*

REP 30 *Disclosure of soft dollar benefits*

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Treasurer's media release 2003/87, 8 October 2003

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