

9 September 2016

Ms Leanne Damary  
Senior Lawyer,  
Investment Managers and Superannuation  
Australian Securities and Investments Commission  
Level 5, 100 Market Street  
SYDNEY NSW 2000

By email: [Leanne.damary@asic.gov.au](mailto:Leanne.damary@asic.gov.au)

Dear Ms Damary,

**AFA Submission – Risk management systems of responsible entities: Further proposals  
(Consultation Paper 263)**

The Association of Financial Advisers Limited (AFA) has served the financial advice industry for 69 years. Our objective is to achieve Great Advice for More Australians and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

The Board of the AFA is elected by the Membership and all Directors are required to be practising financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting wealth.

**Summary of the AFA's position**

The AFA welcomes the draft Regulatory Guide from ASIC. We support the clarity that this guidance will provide to Responsible Managers because this is an area that has long needed attention considering the domino effect that a failure of risk management in a managed investment can have upon the clients of financial advisers.

We have recommended a couple of measures/adjustments that AFA members consider are in the best interests of unitholders of these investments, consumers generally and will engender a culture of transparency and consideration for the end user amongst Responsible Entities.

### **Specific recommendations**

On page 6 of the Consultation Paper, ASIC proposes several measures that Responsible Entities may consider as good practice. The AFA considers that two of these should be mandatory expectations for compliance standard, being:

- at least every three years, conduct a comprehensive independent review of the appropriateness, effectiveness and adequacy of the risk management systems, and
- publicly disclose appropriate details of the responsible entity's risk management system.

The first measure is, in our view, **a necessary safeguard** to ensure that Responsible Entities' and their unitholders get the benefit of external opinion on a regular, but not onerous, basis. **Independent reviews help to mitigate against 'group think' and a lack of perspective, experience or knowledge.**

They are a standard that are required for:

- corporate financial statements,
- compliance measures,
- EDR-scheme reviews,
- the competition sector,
- ASIC approval of industry Codes of Conduct,
- Government charters and audit committees,
- the financial system (as recommended by the Murray Inquiry),
- Human Services Standards, and
- many more organisations and instruments.

The AFA considers that the benefit of independent opinions about Responsible Entity risk management systems is worth the professional cost involved (spread over three years) and does not impose an unreasonable burden for Responsible Entities – especially when you consider the cost can reasonably be accommodated by so many other aspects of our systems and institutions without objection. The AFA considers that the volume of the funds under management that Australians have entrusted to Responsible Managers deserve the protection of mandatory independent reviews.

Making the second measure mandatory would significantly increase the information available to financial advisers and assist their **Know Your Product obligations** under their best interest duty. This is an obligation that financial advisers hold primarily and ASIC says that the obligation to know the product and risks involved cannot be outsourced to model portfolio managers, investment research committees or research houses. This was highlighted particularly with the fixed interest managed fund failures, such as Basis Capital, Absolute Capital, Babcock & Brown and Allco Finance.

The AFA again considers that **the cost involved with complying with this requirement is not onerous** and should be a simple matter for a Responsible Entity who is complying with the other expectations for compliance standard given the documentation that would need to be produced to comply with those other expectations.

### **Closing remarks**

The AFA supports ASIC's initiative to better clarify how Responsible Entities are expected to comply with their risk management obligations. Unfortunately, **many consumers and advisers had to learn the hard way** (through Trio and other failures) how important risk management is in the financial services space. At least though we can reconcile those unrecoverable losses with the greater lesson this unfortunate situation has highlighted – that despite their statutory Know Your Product obligations, **financial advisers are largely information takers and consumers of those services and solutions are in an even less informed position.**

These situations really highlight the **information asymmetry in managed investment schemes** and ASIC's proposals highlight the importance of transparency for the end users. Our recommendations are not onerous or costly for Responsible Entities to implement and we consider the end benefit to outweigh any detriment or small increases to the administration costs that would be applied to the end unit values.

If you require clarification of anything in this submission, please contact us on 02 9267 4003.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Brad Fox', is positioned above the printed name and title.

**Brad Fox**  
Chief Executive Officer  
Association of Financial Advisers Ltd